

**INSURANCE MEDIATION AND  
MORTGAGE MEDIATION, LENDING AND ADMINISTRATION  
(PRUDENTIAL PROVISIONS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (the "Act"):
- (1) section 59 (Approval for particular arrangements);
  - (2) section 138 (General rule-making power);
  - (3) section 139 (Miscellaneous ancillary matters);
  - (4) section 149 (Evidential provisions);
  - (5) section 156 (General supplementary powers);
  - (6) section 157(1) (Guidance);
  - (7) section 214 (General); and
  - (8) section 341 (Access to books etc.).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

[commencement provisions on the next page]

## Commencement

C. This instrument (except Annex I) comes into force as indicated in this table.

<b>Annex</b>	<b>Date</b>
A. COND	1 February 2004
B. PRU	31 October 2004 (in part) and 14 January 2005 (in part) (see note 1)
C. CASS	14 January 2005
D. AUTH	31 October 2004 (in part) and 14 January 2005 (in part) (see notes 1 and 2)
E. AUTH	1 February 2004
F. SUP	31 October 2004 (in part) and 14 January 2005 (in part) (see notes 1 and 2)
G. Glossary	as for the provision in which a term is used
H. Miscellaneous	31 October 2004 (in part) and 14 January 2005 (in part) (see note 1)
<b>Note 1</b> To the extent that a provision relates to: (1) the regulated activities of: (a) arranging (bringing about) regulated mortgage contracts (article 25A(1) of the Regulated Activities Order); (b) making arrangements with a view to regulated mortgage contracts (article 25A(2) of that Order); (c) advising on regulated mortgage contracts (article 53A of that Order); (d) administering a regulated mortgage contract (article 61(2) of that Order); (e) entering into a regulated mortgage contract (article 62(1) of that Order); and (f) agreeing to carry on a regulated activity in (a) to (e); and (2) any regulated activity in relation to a long-term care insurance contract; it comes into force on 31 October 2004. Otherwise, it comes into force on 14 January 2005. <b>Note 2</b> To the extent that a provision in AUTH 5, SUP 13 and SUP 14 relate to passporting rights under the Insurance Mediation Directive, it comes into force on 14 January 2005.	

### **Commencement and expiry of Annex I**

- D. Part 1 of Annex I comes into force on 31 October 2004 and ceases to have effect on 14 January 2005.
- E. Part 2 of Annex I comes into force on 1 February 2004 and ceases to have effect on 14 January 2005.

### **Amendments to the Handbook**

- F. (1) COND is amended in accordance with Annex A to this instrument.
- (2) PRU is made by inserting the provisions in Annex B to this instrument.
- (3) CASS is made by inserting the provisions in Annex C to this instrument.
- (4) AUTH is amended in accordance with Annex D to this instrument (AUTH 2, AUTH 5, AUTH 7 and AUTH App 1).
- (5) AUTH is further amended in accordance with Annex E to this instrument (AUTH App 5, the perimeter guidance).
- (6) SUP is amended in accordance with Annex F to this instrument.
- (7) The Glossary is amended in accordance with Annex G to this instrument.
- (8) PRIN, SYSC, CASS, ENF, and COMP are amended in accordance with Annex H to this instrument.
- (9) PRU and AUTH are amended in accordance with Annex I to this instrument.

### **Citation**

- G. This instrument may be cited as the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004.

By order of the Board  
15 January 2004

Amended by Addendum  
8 December 2004

## Annex A

### Amendments to the Threshold Conditions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.2.1 Table: Paragraph 2, Schedule 6 to the Act.

- (1) Subject to sub-paragraph (3), ~~If~~ if the person concerned is a body corporate constituted under the law of any part of the United Kingdom –
  - (a) its head office, and
  - (b) if it has a registered office, that office,must be in the United Kingdom.
- (2) If the person concerned has its head office in the United Kingdom but is not a body corporate, it must carry on business in the United Kingdom.
- (3) If the regulated activity concerned is an insurance mediation activity, sub-paragraph (1) does not apply.
- (4) If the regulated activity concerned is an insurance mediation activity, the person concerned –
  - (a) if he is a body corporate constituted under the law of any part of the United Kingdom, must have its registered office, or if it has no registered office, its head office, in the United Kingdom;
  - (b) if he is a natural person, is to be treated for the purposes of sub-paragraph (2), as having his head office in the United Kingdom if his residence is situated there.
- (5) “Insurance mediation activity” means any of the following activities –
  - (a) dealing in rights under a contract of insurance as agent;
  - (b) arranging deals in rights under a contract of insurance;
  - (c) assisting in the administration and performance of a contract of insurance;
  - (d) advising on buying or selling rights under a contract of insurance;
  - (e) agreeing to do any of the activities specified in sub-paragraph (a) to (d).
- (6) Paragraph (5) must be read with –
  - (a) section 22;
  - (b) any relevant order under that section; and
  - (c) Schedule 2.

2.2.2 G *Threshold condition 2 (1) and (2)* (Location of offices), implements the requirements of article 6 of the *Post BCCI Directive* and *threshold condition 2(3) and (4)* implements article 2.9 of the *Insurance Mediation Directive*, although the *Act* extends ~~this condition~~ *threshold condition 2* to *firms* which are outside the scope of the *Single Market Directives* and the *UCITS Directive*.

2.2.3 G Neither the *Post BCCI Directive*, the *Insurance Mediation Directive* nor the *Act* define what is meant by a *firm's* 'head office'. This is not necessarily the *firm's* place of incorporation or the place where its business is wholly or mainly carried on. Although the *FSA* will judge each application on a case-by-case basis, the key issue in identifying the head office of a *firm* is the location of its central management and control, that is, the location of:

...

...

2.5.7 G In determining whether a *firm* will satisfy and continue to satisfy *threshold condition 5* in respect of having competent and prudent management and exercising due skill, care and diligence, relevant matters, as referred to in *COND 2.5.4G(2)*, may include, but are not limited to whether:

...

(10) the *firm* has in place the appropriate *money laundering* prevention systems and training, including identification, record-keeping and internal reporting procedures (see *ML*); ~~and~~

(11) where appropriate, the *firm* has appointed auditors and actuaries, who have sufficient experience in the areas of business to be conducted (see *SUP 3.4* (Auditors' qualifications) and *SUP 4.3.8G* to *SUP 4.3.13G* (Appointed actuary's qualifications)); and

(12) in the case of an *insurance intermediary*:

(a) a reasonable proportion of the *persons* within its management structure who are responsible for the *insurance mediation activity*; and

(b) all other *persons* directly involved in its *insurance mediation activity*;

demonstrate the knowledge and ability necessary for the performance of their duties; and

(c) all the *persons* in its management structure and any staff

directly involved in *insurance mediation activity* are of good  
repute (see *PRU 9.1.8 (Knowledge, ability and good repute)*).

## Annex B

### Integrated Prudential sourcebook

The following text is made.

In this Annex, all the text is new and is not underlined.

Transitional provisions

1 Table

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1	<i>PRU 9.2.7R</i>		<p><i>PRU 9.2.7R</i> (Requirement to hold professional indemnity insurance) does not apply in respect of acts or omissions occurring before:</p> <p>(1) 31 October 2004 (in relation to <i>mortgage mediation activity</i>); and</p> <p>(2) 14 January 2005 (in relation to <i>insurance mediation activity</i>).</p>	From 31 October 2004	31 October 2004
2	<i>PRU 9.3.53R</i> and <i>PRU 9.3.57R(3)</i>		A <i>firm</i> is not required to include goodwill in its intangible assets until 14 January 2008.	From 31 October 2004 until 14 January 2008	31 October 2004

## 9.1 Responsibility for insurance mediation activity

### Application

- 9.1.1 R This section applies to a *firm* with *Part IV permission* to carry on *insurance mediation activity*.

### Purpose

- 9.1.2 G The main purpose of *PRU 9.1.3R*, *9.1.8R* and *9.1.10R* is to implement in part the provisions of the *Insurance Mediation Directive* as these apply to *firms* regulated by the *FSA*.

### Responsibility for insurance mediation activity

- 9.1.3 R An *insurance intermediary*, other than a *sole trader*, must allocate the responsibility for the *firm's insurance mediation activity* to a *director* or *senior manager*.

- 9.1.4 R The *firm* may allocate the responsibility for its *insurance mediation activity* under *PRU 9.1.3R* to an *approved person* (or *persons*) performing:

- (1) a *governing function*; or
- (2) the *apportionment and oversight function*; or
- (3) the *significant management (other business operations) function*.

- 9.1.5 G (1) Typically an *insurance intermediary* will appoint a *person* performing a *governing function* to direct its *insurance mediation activity*. Where this responsibility is allocated to a *person* performing another function, the *person* performing the *apportionment and oversight function* with responsibility for the apportionment of responsibilities under *SYSC 2.1.1R* must ensure that the *firm's insurance mediation activity* under *PRU 9.1.3R* is appropriately allocated.

- (2) The descriptions of *significant influence functions*, other than the *required functions*, do not extend to activities carried on by an *insurance intermediary* with *permission* only to carry on *insurance mediation activity* and whose principal purpose is to carry on activities other than *regulated activities* (see *SUP 10.1.21R*). In this case, the *firm* may allocate the responsibility for the *firm's insurance mediation activity* under *PRU 9.1.3R* to one or more of the *persons* performing the *apportionment and oversight function* who will be required to be an *approved person*.



- (3) In the case of a *sole trader*, the *sole trader* will be responsible for the *firm's insurance mediation activity*.
- 9.1.6 G Where a *firm* has appointed an *appointed representative* to carry on *insurance mediation activity* on its behalf, the *person* responsible for the *firm's insurance mediation activity* will also be responsible for the *insurance mediation activity* carried on by an *appointed representative*.
- 9.1.7 G The *FSA* will specify in the *FSA Register* the name of the *persons* to whom the responsibility for the *firm's insurance mediation activity* has been allocated under *PRU 9.1.3R* by inserting after the relevant *controlled function* the words “(insurance mediation)”.
- Knowledge, ability and good repute
- 9.1.8 R An *insurance intermediary* must establish on reasonable grounds that:
- (1) a reasonable proportion of the *persons* within its management structure who are responsible for *insurance mediation activity*; and
- (2) all other *persons* directly involved in its *insurance mediation activity*;
- demonstrate the knowledge and ability necessary for the performance of their duties; and
- (3) all the *persons* in its management structure and any staff directly involved in *insurance mediation activity* are of good repute.
- 9.1.9 G In determining a *person's* knowledge and ability under *PRU 9.1.8R(1)* and (2), the *firm* should have regard to matters including, but not limited to, whether the *person*:
- (1) has demonstrated by experience and training to be able, or that he will be able, to perform his duties related to the *firm's insurance mediation activity*; and
- (2) satisfies the relevant requirements of the *FSA's* Training and Competence sourcebook (*TC*).
- 9.1.10 R In considering a *person's* repute under *PRU 9.1.8R(3)*, the *firm* must ensure that the *person*:
- (1) has not been convicted of any serious criminal offences linked to crimes against property or other crimes related to financial activities (other than spent convictions under the Rehabilitation of Offenders Act 1974 or any other national equivalent); and

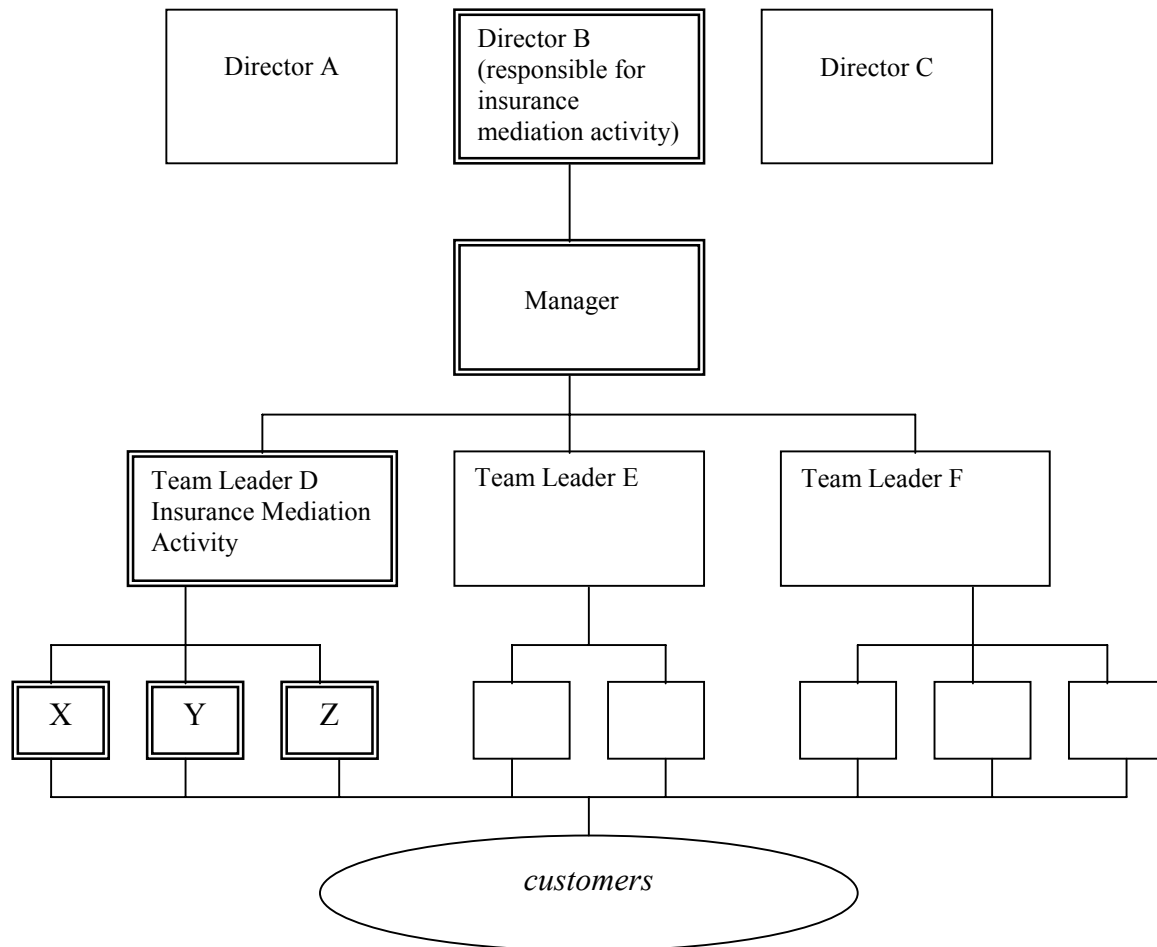
(2) has not been adjudged bankrupt (unless the bankruptcy has been discharged);

under the law of any part of the *United Kingdom* or under the law of a country or territory outside the *United Kingdom*.

- 9.1.11 G For the purposes of *PRU* 9.1.10R(1), the *firm* should give particular consideration to offences of dishonesty, fraud, financial crime or other offences under legislation relating to banking and financial services, companies, insurance and consumer protection.
- 9.1.12 G *Firms* are reminded that *Principle 3* requires *firms* to take reasonable care to organise and control their affairs responsibly and effectively. *Principle 3* is amplified in *SYSC* 3.1.1R which requires *firms* to take reasonable care to establish and maintain such systems and controls as are appropriate to its business. A *firm's* systems and controls should enable it to satisfy itself of the suitability of anyone who acts for it (*SYSC* 3.2.13G). This includes the assessment of an individual's honesty and competence. In addition, *TC* lists some general, high level commitments to training and competence which every *firm* should make and fulfil.
- 9.1.13 G *PRU* 9 Ann 1G gives an example of how the *FSA* would expect *firms* to comply with the requirements in *PRU* 9.1.3R, 9.1.4R, 9.1.8R and 9.1.10R.

PRU 9 Ann 1G:

Example of the application of *PRU 9.1.3R, 9.1.4R, 9.1.8R and 9.1.10R*



1. The *FSA* expects the *firm* to allocate to Director B the responsibility for its *insurance mediation activity* (*PRU 9.1.3R and 9.1.4R*). Director B needs to be an *approved person* (the knowledge and ability requirements in *PRU 9.1.8R(1)* and the good repute requirement in *9.1.8R(3)* will be met through the fit and proper test for *approved persons* in *FIT*).
2. The *firm* must ensure that the Manager and Team Leader D are of good repute (*PRU 9.1.8R(3)*).
3. The *firm* must ensure that either the Manager or Team Leader D (or both) demonstrate the knowledge and ability necessary for the performance of their duties (*PRU 9.1.8R(1)*).
4. The *firm* must ensure that X, Y and Z demonstrate the knowledge and ability necessary for the performance of their duties and are of good repute (*PRU 9.1.8R(2)* and (3) and *PRU 9.1.10R*).

Note that the *firm* may be subject to other *FSA* requirements which are not illustrated in this diagram.

## 9.2 Professional indemnity insurance requirements for insurance and mortgage mediation activities

### Application

- 9.2.1 R (1) This section applies to a *firm* with *Part IV permission* to carry on any of the activities in (2) unless (3), (4), (5) or (6) applies.
- (2) The activities are:
- (a) *insurance mediation activity*;
  - (b) *mortgage mediation activity*.
- (3) (a) In relation to *insurance mediation activity*, this section does not apply to a *firm* if another *authorised person* which has net tangible assets of more than £10 million provides a comparable guarantee.
- (b) If the *firm* is a member of a *group* in which there is an *authorised person* with net tangible assets of more than £10 million, the comparable guarantee must be from that *person*.
- (c) A ‘comparable guarantee’ means a written agreement on terms at least equal to those in *PRU 9.2.10R* to finance the claims that might arise as a result of a breach by the *firm* of its duties under the *regulatory system* or civil law.
- (4) In relation to *mortgage mediation activity*, this section does not apply to a *firm* if:
- (a) it has net tangible assets of more than £1 million; or
  - (b) the comparable guarantee provisions of (3) apply (as if the *firm* was carrying on *insurance mediation activity*) but substituting £1 million for £10 million in (a) and (b).
- (5) In relation to all the activities in (2), this section does not apply to:
- (a) an *insurer*; or
  - (b) a *managing agent*; or

- (c) a *firm* to which *IPRU(INV)* 13.1.4(1)R (Financial resource requirements for personal investment firms: requirement to hold professional indemnity insurance) applies.
  - (6) In relation to *mortgage mediation activity*, this section does not apply to an *authorised professional firm*:
    - (a) which is subject to *IPRU(INV)* 2.3.1 R (Professional indemnity insurance requirements for authorised professional firms); and
    - (b) whose *mortgage mediation activity* is incidental to its main business.
- 9.2.2 G The definition of *insurance mediation activity* is any of several activities ‘in relation to a *contract of insurance*’ which includes a contract of reinsurance. This section, therefore, applies to a reinsurance intermediary in the same way as it applies to any other *insurance intermediary*.
- Purpose
- 9.2.3 G The purposes of this section are to:
- (1) implement article 4.3 of the *Insurance Mediation Directive* in so far as it requires *insurance intermediaries* to hold professional indemnity insurance, or some other comparable guarantee, against any liability that might arise from professional negligence; and
  - (2) meet the *regulatory objectives* of consumer protection and maintaining market confidence by ensuring that *firms* have adequate resources to protect themselves, and their *customers*, against losses arising from breaches in its duties under the *regulatory system* or civil law.
- 9.2.4 G Any breach in the duty of a *firm* or of its agents under the *regulatory system* or civil law can give rise to claims being made against the *firm*. Professional indemnity insurance has an important role to play in helping to finance such claims. In so doing, this section amplifies *threshold condition 4* (Adequate resources). This *threshold condition* provides that a *firm* must have, on a continuing basis, resources that are, in the opinion of the *FSA*, adequate in relation to the *regulated activities* that the *firm* carries on.
- 9.2.5 G Under *Principles 3* and *4* a *firm* is required to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems and to maintain adequate financial resources. Under *Principle 9* a *firm* is obliged to take reasonable care to ensure the

suitability of its *advice on investments* and discretionary decisions for any *customer* who is entitled to rely upon its judgement.

- 9.2.6 G Although financial resources and appropriate systems and controls can generally mitigate operational risk, professional indemnity insurance has a role in mitigating the risks a *firm* faces in its day to day operations, including those arising from not meeting the legally required standard of care when *advising on investments*. The purpose of this section is to ensure that a *firm* has in place the type, and level, of professional indemnity insurance necessary to mitigate these risks.

Requirement to hold professional indemnity insurance

- 9.2.7 R A *firm* must take out and maintain professional indemnity insurance that is at least equal to the requirements of *PRU 9.2.10R* from:

(1) an *insurance undertaking* authorised to transact professional indemnity insurance in the *EEA*; or

(2) a *person* of equivalent status in:

(i) a *Zone A country*; or

(ii) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.

- 9.2.8 G A *firm* whose *Part IV permission* covers more than one *regulated activity* within the scope of this section will need to comply with the professional indemnity insurance requirements for each of these activities. However, this does not necessarily mean that the *firm* should purchase two or more separate *contracts of insurance*. It could, for example, purchase one contract that covers all of its activities, but which contains separate *limits of indemnity* and excesses for each individual activity.

- 9.2.9 G A non-*EEA firm* (such as a captive insurance company outside the *EEA*) will be able to provide professional indemnity insurance only if it is authorised to do so in one of the countries or territories referred to in *PRU 9.2.7R(2)*. The purpose of this provision is to balance the level of protection required for the *policyholder* against a reasonable level of flexibility for the *firm*.

Terms to be incorporated in the insurance

- 9.2.10 R In relation to the activities referred to in *PRU 9.2.1R(2)*, the contract of professional indemnity insurance must incorporate terms which make provision for:

- (1) cover in respect of claims for which a *firm* may be liable as a result of the conduct of itself, its *employees* and its *appointed representatives* (acting within the scope of their appointment);
- (2) the minimum *limits of indemnity* as set out in *PRU 9.2.13R* (in relation to *insurance mediation activity*) and *PRU 9.2.15R* (in relation to *mortgage mediation activity*);
- (3) an excess as set out in *PRU 9.2.17R* to *PRU 9.2.22R*;
- (4) appropriate cover in respect of legal defence costs;
- (5) continuous cover in respect of claims arising from work carried out from the date on which the *firm* was given *Part IV permission* in relation to any of the activities referred to in (2); and
- (6) cover in respect of *Ombudsman* awards made against the *firm*.

9.2.11 G In relation to *PRU 9.2.10R(1)*, a *firm* should be aware that it is responsible for the conduct of all of its *employees*. The *firm's employees* include, but are not limited to, its *partners*, *directors*, individuals that are self-employed or operating under a contract hire agreement and any other individual that is employed in connection with its business.

9.2.12 G In relation to *PRU 9.2.10R(1)*, a *firm* should be aware that it is responsible for the conduct of all of its *appointed representatives*.

Minimum limits of indemnity: insurance mediation activity

9.2.13 R In relation to *insurance mediation activity*, the minimum *limits of indemnity* referred to in *PRU 9.2.10R(2)* are:

- (1) for a single claim, €1 million; and
- (2) in aggregate, €1.5 million or, if higher, 10% of annual income (see *PRU 9.3.42R*) up to £30 million.

9.2.14 R If a *policy* is denominated in any currency other than euros, a *firm* must take reasonable steps to ensure that the *limits of indemnity* are, when the *policy* is effected and at *renewal*, at least equivalent to those required in *PRU 9.2.13R*.

Minimum limits of indemnity: mortgage mediation activity

9.2.15 R In relation to *mortgage mediation activity*, the minimum *limit of indemnity* referred to in *PRU 9.2.10R(2)* is the higher of 10% of annual income (see *PRU 9.3.42R*) up to £1 million, and:

(1) for a single claim, £100,000; or

(2) in aggregate, £500,000.

#### Excess

9.2.16 R In this section, "*client assets*" includes a *document* only if it has value, or is capable of having value, in itself (such as a bearer instrument).

9.2.17 R For a *firm* which does not hold *client money* or other *client assets*, the excess referred to in *PRU 9.2.10R(3)* is not more than the higher of:

(1) £2,500; and

(2) 1.5% of annual income (see *PRU 9.3.42R*).

9.2.18 R For a *firm* which holds *client money* or other *client assets*, the excess referred to in *PRU 9.2.10R(3)* is not more than the higher of:

(1) £5,000; and

(2) 3% of annual income (see *PRU 9.3.42R*).

#### Policies covering more than one firm

9.2.19 R If a *policy* provides cover to more than one *firm*, then in relation to *PRU 9.2.13R*, *PRU 9.2.14R* and *PRU 9.2.15R*:

(1) the *limits of indemnity* must be calculated on the combined annual income (see *PRU 9.3.42R*) of all the *firms* named in the *policy*; and

(2) each *firm* named in the *policy* must have the benefit of the minimum *limits of indemnity* as required in *PRU 9.2.13R* or *PRU 9.2.15R*.

#### Additional capital

9.2.20 R If a *firm* seeks to have an excess which is higher than the limits in *PRU 9.2.17R* (for a *firm* not holding *client money* or other *client assets*) or *PRU 9.2.18R* (for a *firm* holding *client money* or other *client assets*), it must hold additional capital as calculated in *PRU 9.2.21R* or *PRU 9.2.22R* (as appropriate).



9.2.21 R Table: Calculation of additional capital for firm not holding client money or other client assets (£000's)

Income		Excess obtained up to and including:												
		2.5	5	10	15	20	25	30	40	50	75	100	150	200+
More than	Up to													
0	100	0	5	9	12	14	17	19	23	26	33	39	50	59
100	200	0	7	12	16	19	22	25	30	34	43	51	64	75
200	300	0	7	12	16	20	24	27	32	37	47	56	71	84
300	400	0	0	12	16	21	24	28	34	39	50	60	77	91
400	500	0	0	11	16	21	24	28	34	40	53	63	81	96
500	600	0	0	10	16	20	24	28	35	41	54	65	84	100
600	700	0	0	0	15	20	24	28	35	41	55	67	87	104
700	800	0	0	0	14	19	24	28	35	42	56	68	89	107
800	900	0	0	0	13	18	23	27	35	42	56	69	91	109
900	1,000	0	0	0	0	17	22	27	34	41	57	70	92	111
1,000	1,500	0	0	0	0	0	21	26	34	41	57	71	97	118
1,500	2,000	0	0	0	0	0	0	0	30	38	56	71	98	121
2,000	2,500	0	0	0	0	0	0	0	24	33	53	69	99	126
2,500	3,000	0	0	0	0	0	0	0	0	28	50	68	101	130
3,000	3,500	0	0	0	0	0	0	0	0	0	47	67	101	132
3,500	4,000	0	0	0	0	0	0	0	0	0	43	65	101	133
4,000	4,500	0	0	0	0	0	0	0	0	0	39	62	101	134
4,500	5,000	0	0	0	0	0	0	0	0	0	0	58	99	134
5,000	6,000	0	0	0	0	0	0	0	0	0	0	54	97	133
6,000	7,000	0	0	0	0	0	0	0	0	0	0	0	91	131
7,000	8,000	0	0	0	0	0	0	0	0	0	0	0	84	126
8,000	9,000	0	0	0	0	0	0	0	0	0	0	0	75	120
9,000	10,000	0	0	0	0	0	0	0	0	0	0	0	0	113
10,000	100,000	0	0	0	0	0	0	0	0	0	0	0	0	0
100,000	n/a	0	0	0	0	0	0	0	0	0	0	0	0	0

9.2.22 R Table: Calculation of additional capital for firm holding client money or other client assets (£000's)

Income		Excess obtained up to and including:											
		5	10	15	20	25	30	40	50	75	100	150	200+
More than	Up to												
0	100	0	4	7	9	12	14	18	21	28	34	45	54
100	200	0	7	11	14	17	20	25	29	38	46	59	70
200	300	0	7	11	14	17	20	25	30	40	49	64	77
300	400	0	0	9	13	16	19	25	30	40	50	67	81
400	500	0	0	0	11	14	18	24	29	40	51	68	83
500	600	0	0	0	8	12	15	22	28	40	51	69	85
600	700	0	0	0	0	9	13	20	26	39	50	69	86
700	800	0	0	0	0	6	10	17	24	38	49	69	87
800	900	0	0	0	0	0	7	15	22	36	48	69	87
900	1,000	0	0	0	0	0	0	12	19	34	47	68	87
1,000	1,500	0	0	0	0	0	0	0	16	32	45	67	86
1,500	2,000	0	0	0	0	0	0	0	0	18	34	59	81
2,000	2,500	0	0	0	0	0	0	0	0	0	19	48	71
2,500	3,000	0	0	0	0	0	0	0	0	0	6	37	64
3,000	3,500	0	0	0	0	0	0	0	0	0	0	26	55
3,500	4,000	0	0	0	0	0	0	0	0	0	0	14	45
4,000	4,500	0	0	0	0	0	0	0	0	0	0	1	33
4,500	5,000	0	0	0	0	0	0	0	0	0	0	0	21
5,000	6,000	0	0	0	0	0	0	0	0	0	0	0	8
6,000	7,000	0	0	0	0	0	0	0	0	0	0	0	0
7,000	8,000	0	0	0	0	0	0	0	0	0	0	0	0
8,000	9,000	0	0	0	0	0	0	0	0	0	0	0	0
9,000	10,000	0	0	0	0	0	0	0	0	0	0	0	0
10,000	100,000	0	0	0	0	0	0	0	0	0	0	0	0
100,000	n/a	0	0	0	0	0	0	0	0	0	0	0	0

9.2.23 G *PRU 9.3.52R* sets out the items which are eligible to contribute to the capital resources of a *firm* for the purposes of *PRU 9.2.20R*.

### 9.3 Capital resources for insurance and mortgage mediation activity and mortgage lending and administration

#### Application

- 9.3.1 R (1) This section applies to a *firm* with *Part IV permission* to carry on any of the activities in (2) unless any of *PRU 9.3.4R* to *PRU 9.3.11R* applies.
- (2) The activities are:
- (a) *insurance mediation activity*;
  - (b) *mortgage mediation activity*;
  - (c) *entering into a regulated mortgage contract* (that is, *mortgage lending*);
  - (d) *administering a regulated mortgage contract* (that is, *mortgage administration*).

9.3.2 G As this section applies only to a *firm* with *Part IV permission*, it does not apply to an *incoming EEA firm* (unless it has a *top-up permission*). An *incoming EEA firm* includes a *firm* which is passporting into the *United Kingdom* under the *IMD* (see *AUTH 5.4.2AG*, in relation to *branches*, and *AUTH 5.5.3G*, in relation to *cross border services*).

9.3.3 G The definition of *insurance mediation activity* refers to several activities ‘in relation to a *contract of insurance*’ which includes a contract of reinsurance. This section, therefore, applies to a reinsurance intermediary in the same way as it applies to any other *insurance intermediary*.

Application: banks, building societies, insurers and friendly societies

- 9.3.4 R This section does not apply to:
- (1) a *bank*; or
  - (2) a *building society*; or
  - (3) a solo consolidated *subsidiary* of a *bank* or a *building society*; or
  - (4) an *insurer*; or
  - (5) a *friendly society*.

- 9.3.5 G The capital resources of *firms* within *PRU* 9.3.4R are calculated in accordance with the appropriate *IPRU*.
- Application: firms carrying on designated investment business only
- 9.3.6 R This section does not apply to a *firm* whose *Part IV permission* is limited to *regulated activities* which are *designated investment business*.
- 9.3.7 G A *firm* which carries on *designated investment business*, and no other *regulated activity*, may disregard this section. For example, a *firm* with *permission* limited to *dealing in investments as agent* in relation to *securities* is only carrying on *designated investment business* and *IPRU(INV)* will apply. However, if its *permission* is varied to enable it to arrange motor insurance as well, this activity is not *designated investment business* so the *firm* will be subject to the higher of the requirements in this section and *IPRU(INV)* (see *PRU* 9.3.24R).
- Application: credit unions
- 9.3.8 R This section does not apply to:
- (1) a ‘small *credit union*’, that is one with:
    - (a) assets of £5 million or less; and
    - (b) a total number of members of 5,000 or less (see *CRED* 8.3.14R); or
  - (2) a *credit union* whose *Part IV permission* includes *mortgage lending* or *mortgage administration* (or both) and no other activities in *PRU* 9.3.1R(2).
- 9.3.9 G For *credit unions* to which this section applies, the capital requirements will be the higher of the requirements in this section and in *CRED* (see *PRU* 9.3.25R).
- Application: professional firms
- 9.3.10 R (1) This section does not apply to an *authorised professional firm*:
- (a) whose main business is the practice of its profession; and
  - (b) whose *regulated activities* in *PRU* 9.3.1R(2) are incidental to its main business.
- (2) A *firm's* main business is the practice of its profession if the proportion of income it derives from professional fees is, during its

annual accounting period, at least 50% of the *firm's* total income (a temporary variation of not more than 5% may be disregarded for this purpose).

- (3) Professional fees are fees, commissions and other receipts receivable in respect of legal, accountancy or actuarial services provided to clients but excluding any items receivable in respect of *regulated activities*.

Application: Lloyd's managing agents

9.3.11 R This section does not apply to a *managing agent*.

9.3.12 G The reason for excluding *managing agents* from the provisions of this section is twofold: first, a *member* will have accepted full responsibility for those activities under the *Society's managing agent* agreement. Secondly, the *member* is itself subject to capital requirements which are equivalent to those applying to an *insurer* (to which this section is also disappplied – see *PRU 9.3.4R(4)*).

Application: social housing firms

9.3.13 G There are special provisions for a *social housing firm* when it is carrying on *mortgage lending* or *mortgage administration* (see *PRU 9.3.26R*).

Purpose

9.3.14 G This section amplifies *threshold condition 4* (Adequate resources) by providing that a *firm* must meet, on a continuing basis, a basic solvency requirement (*PRU 9.3.20R*) and a minimum capital resources requirement (*PRU 9.3.21R*). This section also amplifies *Principle 4* which requires a *firm* to maintain adequate financial resources by setting out capital requirements for a *firm* according to the *regulated activity* or *activities* it carries on.

9.3.15 G Capital has an important role to play in protecting consumers and complements the roles played by professional indemnity insurance (see *PRU 9.2* (Professional indemnity insurance)) and *client money* protection (see the *client money rules* including, in particular, those in *CASS 5* (Client money and mandates: insurance mediation activity)). Capital provides a form of protection for situations not covered by a *firm's* professional indemnity insurance and it provides the funds for the *firm's* PII excess, which it has to pay out of its own finances. The relationship between the *firm's* capital and its excess is set out in *PRU 9.2.17R*.

9.3.16 G More generally, having adequate capital gives the *firm* a degree of resilience and some indication to consumers of creditworthiness,

substance and the commitment of its owners. It reduces the possibility of a shortfall of funds and provides a cushion against disruption if the *firm* ceases to trade.

- 9.3.17 G There is a greater risk to consumers, and a greater adverse impact on market confidence, if a *firm* holding *client money* or other *client* assets fails. For this reason, the capital resources *rules* in this section clearly distinguish between *firms* holding *client* assets and those that do not.

Purpose: social housing firms

- 9.3.18 G *Social housing firms* undertake small amounts of mortgage business even though their main business consists of activities other than *regulated activities*. Their *mortgage lending* is only done as an adjunct to their primary purpose (usually the provision of housing) and is substantially different in character to that done by commercial lenders. Furthermore, they are *subsidiaries* of local authorities or registered social landlords which are already subject to separate regulation. The *FSA* does not consider that it would be proportionate to the risks involved with such business to impose significant capital requirements for these *firms*. *PRU* 9.3.26R therefore simply provides that, where their *Part IV permission* is limited to *mortgage lending* and *mortgage administration*, their net tangible assets must be greater than zero.

- 9.3.19 G A registered social landlord is a non-profit organisation which provides and manages homes for rent and sale for people who might not otherwise be able to rent or buy on the open market. It can be a housing association, a housing society or a non-profit making housing company. The Housing Corporation, which was set up by Parliament in 1964, funds homes built by registered social landlords from money received from central government.

Capital resources: general rules

- 9.3.20 R A *firm* must at all times ensure that it is able to meet its liabilities as they fall due.

- 9.3.21 R A *firm* must at all times maintain capital resources equal to or in excess of its relevant capital resources requirement.

Capital resources: UK GAAP

- 9.3.22 R A *firm* must recognise an asset or liability, and measure its amount, in accordance with the relevant *UK* generally accepted accounting principles unless a *rule* requires otherwise.

Capital resources: client assets

- 9.3.23 R In this section, "*client assets*" includes a *document* only if it has value, or is capable of having value, in itself (such as a bearer instrument).

Capital resources requirement: firms carrying on regulated activities including designated investment business

- 9.3.24 R The capital resources requirement for a *firm* carrying on *regulated activities*, including *designated investment business*, is the higher of:

- (1) the requirement which is applied by this section according to the activity or activities of the *firm* (treating the relevant *rules* as applying to the *firm* by disregarding its *designated investment business*); and
- (2) the financial resource requirement which is applied by *IPRU(INV)*.

Capital resources requirement: credit unions

- 9.3.25 R The capital resources requirement for a *credit union* to which this section applies (see *PRU 9.3.8R*) is the higher of:

- (1) the requirement which is applied by *PRU 9.3.30R* (Capital resources requirement: mediation activity only) treating that *rule* as applying to the *credit union* by disregarding activities which are not *insurance mediation activity* or *mortgage mediation activity*; and
- (2) the amount which is applied by *CRED 8* (Capital requirements).

Capital resources requirement: social housing firms

- 9.3.26 R The capital resources requirement for a *social housing firm* whose *Part IV permission* is limited to carrying on the *regulated activities* of:

- (1) *mortgage lending*; or
- (2) *mortgage administration* (or both);

is that the *firm's* net tangible assets must be greater than zero.

- 9.3.27 G If a *social housing firm* is carrying on *mortgage lending* or *mortgage administration* (and no other *regulated activity*), its net tangible assets must be greater than zero. However, if it carries on *insurance mediation activity*, or *mortgage mediation activity*, there is no special provision and *PRU 9.3.24R* or *PRU 9.3.30R* applies to it as appropriate.

Capital resources requirement: application according to regulated activities

9.3.28 R Unless any of *PRU 9.3.24R* to *PRU 9.3.26R* applies (*firms* carrying on *designated investment business*, *credit unions* and *social housing firms*), the table in *PRU 9.3.29R* specifies the provisions for calculating the capital resources requirement for a *firm* according to the *regulated activity* or *activities* it carries on.

9.3.29 R Table: Application of capital resources requirements

	Regulated activities	Provisions
1.	(a) <i>insurance mediation activity</i> ; or (b) <i>mortgage mediation activity</i> (or both); and no other <i>regulated activity</i> .	<i>PRU 9.3.30R</i>
2.	(a) <i>mortgage lending</i> ; or (b) <i>mortgage lending</i> and <i>mortgage administration</i> ; and no other <i>regulated activity</i> .	<i>PRU 9.3.31R</i> to <i>PRU 9.3.36E</i>
3.	<i>mortgage administration</i> ; and no other <i>regulated activity</i> .	<i>PRU 9.3.37R</i> to <i>PRU 9.3.38R</i>
4.	<i>insurance mediation activity</i> ; and (a) <i>mortgage lending</i> ; or (b) <i>mortgage administration</i> (or both).	<i>PRU 9.3.39R</i>
5.	<i>mortgage mediation activity</i> ; and (a) <i>mortgage lending</i> , or (b) <i>mortgage administration</i> (or both).	<i>PRU 9.3.40R</i>
6.	Any combination of <i>regulated activities</i> not within rows 1 to 5.	<i>PRU 9.3.41R</i>

Capital resources requirement: mediation activity only

9.3.30 R (1) If a *firm* (carrying on the activities in row 1 of the table in *PRU 9.3.29R*) does not hold *client money* or other *client* assets in relation to its *insurance mediation activity* or *mortgage mediation activity*, its capital resources requirement is the higher of:

(a) £5,000; and

(b) 2.5% of the annual income (see *PRU 9.3.42R*) from its *insurance mediation activity* or *mortgage mediation activity* (or both).



- (2) If a *firm* (carrying on the activities in row 1 of the table in *PRU 9.3.29R*) holds *client money* or other *client* assets in relation to its *insurance mediation activity* or *mortgage mediation activity*, its capital resources requirement is the higher of:
- (a) £10,000; and
  - (b) 5% of the annual income (see *PRU 9.3.42R*) from its *insurance mediation activity* or *mortgage mediation activity* (or both).

Capital resources requirement: mortgage lending and administration (but not mortgage administration only)

- 9.3.31 R (1) The capital resources requirement of a *firm* (carrying on the activities in row 2 of the table at *PRU 9.3.29R*) is the higher of:
- (a) £100,000; and
  - (b) 1% of:
    - (i) its total assets plus total undrawn commitments; less:
    - (ii) loans excluded by *PRU 9.3.33R* plus intangible assets (see Note 1 in the table in *PRU 9.3.53R*).
- (2) Undrawn commitments in (1)(b)(i) means the total of those amounts which a borrower has the right to draw down from the *firm* but which have not yet been drawn down, excluding those under an agreement:
- (a) which has an original maturity of up to one year; or
  - (b) which can be unconditionally cancelled at any time by the lender.

9.3.32 G When considering what is an undrawn commitment, the *FSA* takes into account an amount which a borrower has the right to draw down, but which has not yet been drawn down, whether the commitment is revocable or irrevocable, conditional or unconditional.

9.3.33 R When calculating total assets for the purposes of *PRU 9.3.31R*, the *firm* may exclude a loan which has been transferred to a third party only if it meets the following conditions:

- (1) the loan must have been transferred in a legally effective manner by one of the following means:
    - (a) novation; or
    - (b) legal or equitable assignment; or
    - (c) sub-participation; or
    - (d) declaration of trust; and
  - (2) the lender:
    - (a) retains no material economic interest in the loan; and
    - (b) has no material exposure to losses arising from it.
- 9.3.34 E (1) When seeking to rely on the condition in *PRU 9.3.33R(2)*, a *firm* should ensure that the loan qualifies for the ‘linked presentation’ accounting treatment under Financial Reporting Standard 5 (Reporting the substance of transactions) issued in April 1994, and amended in December 1994 and September 1998 (if applicable to the *firm*).
- (2) Compliance with (1) may be relied upon as tending to establish compliance with *PRU 9.3.33R(2)*.
- 9.3.35 G *PRU 9.3.34E* is aimed at those *firms* which report according to FRS 5. Other *firms* which report under other standards, including International Accounting Standards, need not adopt FRS 5 in order to meet the condition in *PRU 9.3.33R(2)*.
- 9.3.36 E (1) When seeking to rely on the condition in *PRU 9.3.33R(2)*, a *firm* should not provide material credit enhancement in respect of the loan unless it deducts the amount of the credit enhancement from its capital resources before meeting its capital resources requirement.
- (2) Credit enhancement includes:
  - (a) any holding of subordinated loans or notes in a transferee that is a special purpose vehicle; or
  - (b) over collateralisation by transferring loans to a larger aggregate value than the *securities* to be issued; or

- (c) any other arrangement with the transferee to cover a part of any subsequent losses arising from the transferred loan.
- (3) Contravention of (1) may be relied upon as tending to establish contravention of *PRU 9.3.33R*(2).

Capital resources requirement: mortgage administration only

9.3.37 R The capital resources requirement of a *firm* (carrying on the activities in row 3 of the table in *PRU 9.3.29R*), which has all or part of the *regulated mortgage contracts* that it administers on its balance sheet, is the amount which is applied to a *firm* by *PRU 9.3.31R*.

9.3.38 R The capital resources requirement of a *firm* (carrying on the activities in row 3 of the table in *PRU 9.3.29R*), which has all the *regulated mortgage contracts* that it administers off its balance sheet, is the higher of:

- (1) £100,000; and
- (2) 10% of its annual income (see *PRU 9.3.42R* and *PRU 9.3.48R*).

Capital resources requirement: insurance mediation activity and mortgage lending or mortgage administration

9.3.39 R The capital resources requirement for a *firm* (carrying on the activities in row 4 of the table in *PRU 9.3.29R*) is the sum of the requirements which are applied to the *firm* by:

- (1) *PRU 9.3.30R*; and
- (2) (a) *PRU 9.3.31R*; or  
(b) if, in addition to its *insurance mediation activity*, the *firm* carries on only *mortgage administration* and has all the assets that it administers off balance sheet, *PRU 9.3.38R*.

Capital resources requirement: mortgage mediation activity and mortgage lending or mortgage administration

- 9.3.40 R (1) If a *firm* (carrying on the activities in row 5 of the table in *PRU 9.3.29R*) does not hold *client money* or other *client* assets in relation to its *mortgage mediation activity*, the capital requirement is the amount applied to a *firm*, according to the activities carried on by the *firm*, by:
- (a) *PRU 9.3.31R*; or

- (b) if, in addition to its *mortgage mediation activity*, the *firm* carries on only *mortgage administration* and has all the assets that it administers off balance sheet, *PRU 9.3.38R*.
- (2) If a *firm* (carrying on the activities in row 5 of the table in *PRU 9.3.29R*) holds *client money* or other *client* assets in relation to its *mortgage mediation activity*, the capital resources requirement is:
- (a) the amount calculated under (1); plus
  - (b) the amount which is applied to a *firm* by *PRU 9.3.30R(2)*.

Capital resources requirement: other combinations of activities

- 9.3.41 R The capital resources requirement for a *firm* (carrying on the activities in row 6 of the table in *PRU 9.3.29R*) is the amount which is applied to a *firm* by *PRU 9.3.39R*.

Annual income

- 9.3.42 R *PRU 9.3.43R* to *PRU 9.3.50R* contain provisions relating to the calculation of annual income for the purposes of:
- (1) *PRU 9.2.13R(2)*, *PRU 9.2.15R*, *PRU 9.2.17R(2)* and *PRU 9.2.18R(2)* (all concerning the *limits of indemnity* for professional indemnity insurance); and
  - (2) *PRU 9.3.30R(1)(b)* and (2)(b), and *PRU 9.3.38R(2)*.

- 9.3.43 R ‘Annual income’ is the annual income given in the *firm*’s most recent annual financial statement from the relevant *regulated activity* or *activities*.

- 9.3.44 R For a *firm* which carries on *insurance mediation activity* or *mortgage mediation activity*, annual income in *PRU 9.3.43R* is the amount of all brokerage, fees, *commissions* and other related income (for example, administration charges, overrides, profit shares) due to the *firm* in respect of or in relation to those activities.

- 9.3.45 G The purpose of *PRU 9.3.44R* is to ensure that the capital resources requirement is calculated on the basis only of brokerage and other amounts earned by a *firm* which are its own income.

- 9.3.46 R If a *firm* is a *principal*, its annual income includes amounts due to its *appointed representative* in respect of activities for which the *firm* has accepted responsibility.

9.3.47 G If a *firm* is a *network*, it should include the relevant income due to all of its *appointed representatives* in its annual income.

Annual income for mortgage administration

9.3.48 R For the purposes of *PRU* 9.3.38R(2) (Mortgage administration only) annual income is the sum of:

(1) revenue (that is, *commissions*, fees, net interest income, dividends, royalties and rent); and

(2) gains;

arising in the course of the ordinary activities of the *firm*, less profit:

(a) on the sale or termination of an operation;

(b) arising from a fundamental reorganisation or restructuring having a material effect on the nature and focus of the *firm's* operation; and

(c) on the disposal of fixed assets, including *investments* held in a long-term portfolio.

Annual income: periods of less than 12 months

9.3.49 R If the *firm's* most recent annual financial statement does not cover a 12 *month* period, the annual income is taken to be the amount in the statement converted, proportionally, to a 12 *month* period.

Annual income: no financial statement

9.3.50 R If the *firm* does not have an annual financial statement, the annual income is to be taken from the forecast or other appropriate accounts which the *firm* has submitted to the *FSA*.

The calculation of a firm's capital resources

9.3.51 R (1) A *firm* must calculate its capital resources only from the items in *PRU* 9.3.52R from which it must deduct the items in *PRU* 9.3.53R.

(2) If the *firm* is subject to *IPRU(INV)* or *CRED*, the capital resources are the higher of:

(a) the amount calculated under (1); and

(b) the financial resources calculated under *IPRU(INV)* or the capital calculated under *CRED* 8 (Capital requirements).

9.3.52 R Table: Items which are eligible to contribute to the capital resources of a firm

	Item	Additional explanation
1.	Share capital	This must be fully paid and may include: (1) ordinary <i>share</i> capital; or (2) preference <i>share</i> capital (excluding preference <i>shares</i> redeemable by shareholders within two years).
2.	Capital other than <i>share</i> capital (for example, the capital of a <i>sole trader</i> , <i>partnership</i> or <i>limited liability partnership</i> )	The capital of a <i>sole trader</i> is the net balance on the <i>firm's</i> capital account and current account. The capital of a <i>partnership</i> is the capital made up of the <i>partners'</i> : (1) capital account, that is the account: (a) into which capital contributed by the <i>partners</i> is paid; and (b) from which, under the terms of the <i>partnership</i> agreement, an amount representing capital may be withdrawn by a <i>partner</i> only if: (i) he ceases to be a <i>partner</i> and an equal amount is transferred to another such account by his former <i>partners</i> or any <i>person</i> replacing him as their <i>partner</i> ; or (ii) the <i>partnership</i> is otherwise dissolved or wound up; and (2) current accounts according to the most recent financial statement.
3.	Audited reserves	These are the audited accumulated profits retained by the <i>firm</i> (after deduction of tax, dividends and proprietors' or <i>partners'</i> drawings) and other reserves created by appropriations of share premiums and similar realised appropriations. Reserves also include gifts of capital, for example, from a <i>parent undertaking</i> .
4.	Interim net profits	If a <i>firm</i> seeks to include interim net profits in the calculation of its capital resources, the profits have to be verified by the <i>firm's</i> external auditor, net of tax, anticipated dividends or proprietors' drawings and other appropriations.

5.	Revaluation reserves	
6.	General provisions	These are provisions that a <i>firm</i> carrying on <i>mortgage lending</i> or <i>mortgage administration</i> holds against potential losses that have not yet been identified but which experience indicates are present in the <i>firm's</i> portfolio of assets. Such provisions must be freely available to meet these unidentified losses wherever they arise. General provisions must be verified by external auditors and disclosed in the <i>firm's</i> annual report and accounts.
7.	Subordinated loans	Subordinated loans must be included in capital on the basis of the provisions in <i>PRU 9.3.56R</i> and <i>PRU 9.3.57R</i> .

9.3.53 R Table: Items which must be deducted from capital resources

1	<i>Investments</i> in own shares
2	Intangible assets (Note 1)
3	Interim net losses (Note 2)
4	Excess of drawings over profits for a <i>sole trader</i> or a <i>partnership</i> (Note 2)
Notes	
1.	Intangible assets are the full balance sheet value of goodwill (but not until 14 January 2008 - see transitional provision 2), capitalised development costs, brand names, trademarks and similar rights and licences.
2.	The interim net losses in row 3, and the excess of drawings in row 4, are in relation to the period following the date as at which the capital resources are being computed.

Personal assets

9.3.54 R In relation to a *sole trader's firm* or a *firm* which is a *partnership*, the *sole trader* or a *partner* in the *firm* may use personal assets to meet the requirements of *PRU 9.3.20R* or *PRU 9.3.21R*, or both, to the extent necessary to make up any shortfall in meeting those requirements, unless:

- (1) those assets are needed to meet other liabilities arising from:
  - (a) personal activities; or
  - (b) another business activity not regulated by the *FSA*; or
- (2) the *firm* holds *client money* or other *client* assets.

9.3.55 G The purpose of *PRU 9.3.54R* is to enable a *sole trader* or a *partner* to use any personal assets, including property, to meet the capital requirements of this section, but only to the extent necessary to make up a shortfall. The requirements are the solvency requirement (*PRU 9.3.20R*) and the capital resources requirement (*PRU 9.3.21R*).

#### Subordinated loans

9.3.56 R In row 7 in the table at *PRU 9.3.52R*, subordinated debt must not form part of the capital resources of the *firm* unless it meets the following conditions:

- (1) (for a *firm* which carries on *insurance mediation activity* or *mortgage mediation activity* (or both) but not *mortgage lending* or *mortgage administration*) it has an original maturity of:
  - (a) at least two years; or
  - (b) it is subject to two years' notice of repayment;
- (2) (for all other *firms*) it has an original maturity of:
  - (a) at least five years; or
  - (b) it is subject to five years' notice of repayment;
- (3) the claims of the subordinated creditors must rank behind those of all unsubordinated creditors;
- (4) the only events of default must be non-payment of any interest or principal under the debt agreement or the winding up of the *firm*;
- (5) the remedies available to the subordinated creditor in the event of non-payment or other default in respect of the subordinated debt must be limited to petitioning for the winding up of the *firm* or proving the debt and claiming in the liquidation of the *firm*;
- (6) the subordinated debt must not become due and payable before its stated final maturity date except on an event of default complying with (4);
- (7) the agreement and the debt are governed by the law of England and Wales, or of Scotland or of Northern Ireland;
- (8) to the fullest extent permitted under the rules of the relevant jurisdiction, creditors must waive their right to set off amounts



they owe the *firm* against subordinated amounts owed to them by the *firm*;

- (9) the terms of the subordinated debt must be set out in a written agreement or instrument that contains terms that provide for the conditions set out in (1) to (8); and
- (10) the debt must be unsecured and fully paid up.

9.3.57 R (1) This *rule* applies to a *firm* which:

- (a) carries on:
  - (i) *insurance mediation activity*; or
  - (ii) *mortgage mediation activity* (or both); and
- (b) in relation to those activities, holds *client money* or other *client assets*;

but is not carrying on *mortgage lending* or *mortgage administration*.

(2) In calculating its capital resources under *PRU* 9.3.51R(1), the *firm* must exclude any amount by which the aggregate amount of its subordinated loans and its redeemable preference *shares* exceeds the amount calculated under (3).

(3) The calculation for (2) is:

four times (a – b – c);

where:

- a = items 1 to 5 in the Table at *PRU* 9.3.52R;
- b = the *firm's* redeemable preference *shares*; and
- c = the amount of its intangible assets (but not goodwill until 14 January 2008 - see transitional provision 2).

9.3.58 G If a *firm* wishes to see an example of a subordinated loan agreement which would meet the conditions in *PRU* 9.3.56R, it should refer to the *FSA* website ([www.fsa.gov.uk](http://www.fsa.gov.uk)).

## 9.4 Insurance undertakings and mortgage lenders using insurance or mortgage mediation services

### Application

9.4.1 R This section applies to a *firm* with a *Part IV permission* to carry on:

- (1) *insurance business*; or
- (2) *mortgage lending*;

and which uses, or proposes to use, the services of another person consisting of:

- (a) *insurance mediation*; or
- (b) *insurance mediation activity*; or
- (c) *mortgage mediation activity*.

### Purpose

9.4.2 G The purpose of *PRU 9.4* is to implement article 3.6 of the *Insurance Mediation Directive* in relation to *insurance undertakings*. The provisions of this section have been extended to *mortgage lenders* in relation to *insurance mediation activity*, and to *insurance undertakings* and *mortgage lenders* in relation to *mortgage mediation activity*, to ensure that *firms* using these services are treated in the same way and to ensure that *clients* have the same protection. To avoid the loss of protection where an intermediary itself uses the services of an *unauthorised person*, *PRU 9.4.4R* has the effect of ensuring that each person in the chain of those providing services is authorised.

9.4.3 G *PRU 9.4* supports the more general duties in *Principles 2* and *3*, and *SYSC 3.1.1R*.

### Use of intermediaries

9.4.4 R A *firm* must not use, or propose to use, the services of another person consisting of:

- (1) *insurance mediation*; or
- (2) *insurance mediation activity*; or
- (3) *mortgage mediation activity*;

unless the conditions in *PRU 9.4.5R* and *PRU 9.4.7R* are satisfied.

- 9.4.5 R The first condition in *PRU 9.4.4R* is that the person, in relation to the activity:
- (1) has *permission*; or
  - (2) is an *exempt person*; or
  - (3) is an *exempt professional firm*; or
  - (4) is registered in another *EEA State* for the purposes of the *IMD*; or
  - (5) in relation to *insurance mediation activity*, is not carrying this activity on in the *EEA*; or
  - (6) in relation to *mortgage mediation activity*, is not carrying this activity on in the *United Kingdom*.
- 9.4.6 E (1) A *firm* should:
- (a) before using the services of the intermediary, check:
    - (i) the *FSA Register*; or
    - (ii) in relation to *insurance mediation* carried on by an *EEA firm*, the register of its *Home State regulator*;
 for the status of the person; and
  - (b) use the services of that person only if the relevant register indicates that the person is registered for that purpose.
- (2) (a) Compliance with (1)(a)(i) and (b) may be relied on as tending to establish compliance with:
- (i) *PRU 9.4.5R(1)*; or
  - (ii) in relation to *insurance mediation activity*, also *PRU 9.4.5R(2)* and (3).
- (b) Compliance with (1)(a)(ii) and (b) may be relied on as tending to establish compliance with *PRU 9.4.5R(4)*.
- 9.4.7 R The second condition in *PRU 9.4.4R* is that the *firm* takes all reasonable steps to ensure that the person in *PRU 9.4.5R* in relation to the activity, is not, directly or indirectly, carrying out the activity as a consequence of the activities of another person which contravene section 19 of the *Act* (The general prohibition).
- 9.4.8 R In order to comply with *PRU 9.4.7R*, a *firm* may rely on a confirmation provided by the other person in writing if:

- (1) the confirmation is provided by a person within *PRU 9.4.5R*;
- (2) the *firm* checked that this is the case; and
- (3) the *firm* is not aware that the confirmation is inaccurate and has no grounds for reasonably being aware that the confirmation is inaccurate.

9.4.9 G The *FSA Register* can be accessed through the *FSA* website under the link [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register).

## Annex C

### Amendments to the Client Assets sourcebook

In the following table only, underlining indicates new text.

#### CASS Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...	...	...	...	...	...
<u>3</u>	<u>CASS 5.1 to CASS 5.6</u>	<u>R</u>	<u>In CASS 5.1 to CASS 5.6 an <i>insurance undertaking</i> (when acting as such) with whom a <i>firm</i> conducts <i>insurance mediation activity</i> may be treated by the <i>firm</i> as its <i>client</i>.</u>	<u>14 January 2005 for 12 months</u>	<u>14 January 2005</u>
<u>4</u>	<u>CASS 5.1 to CASS 5.6</u>	<u>R</u>	<u>Money held by a <i>firm</i> in accordance with an agreement made under CASS 5.2.3R may be kept in a <i>client bank account</i>.</u>	<u>14 January 2005 for 12 months</u>	<u>14 January 2005</u>
...	...	...	...	...	...

In the remainder of this Annex, all the text is new and is not underlined, except for new text inserted in schedules 1 and 2 to CASS which is underlined.

Insert the following new chapter as Chapter 5.

#### Client money and mandates: insurance mediation activity

##### 5.1 Application

- 5.1.1 R (1) *CASS 5.1 to 5.6 apply, subject to (2), (3) and CASS 5.1.3R to 5.1.6R, to a firm that receives or holds money in the course of or in connection with its insurance mediation activity.*
- (2) *CASS 5.1 to 5.6 do not, subject to (3), apply:*
- (a) *to a firm to the extent that it acts in accordance with CASS 4; or*
  - (b) *to a firm in carrying on an insurance mediation activity which is in respect of a reinsurance contract; or*
  - (c) *to an insurance undertaking in respect of its permitted activities; or*

- (d) to a *managing agent* when acting as such; or
- (e) with respect to *money* held by a *firm* which:
  - (i) is an *approved bank*; and
  - (ii) has requisite capital under article 4(4)(b) of the *IMD*;

but only when held by the *firm* in an account with itself, in which case the *firm* must notify the *client* (whether through a *client* agreement, *terms of business*, or otherwise in writing) that:

- (iii) *money* held for that *client* in an account with the *approved bank* will be held by the *firm* as banker and not as trustee (or in Scotland as agent); and
  - (iv) as a result, the *money* will not be held in accordance with *CASS 5.1* to *CASS 5.6*.
- (3) A *firm* may elect to comply with:
- (a) *CASS 5.1* to *CASS 5.6* in respect of *client money* which it receives in the course of carrying on *insurance mediation activity* in respect of *reinsurance contracts*; and
  - (b) *CASS 5.1*, *CASS 5.2* and *CASS 5.4* to *CASS 5.6* in respect of *money* which it receives in the course of carrying on an activity which would be *insurance mediation activity*, and which *money* would be *client money*, but for article 72D of the *Regulated Activities Order* (Large risks contracts where risk situated outside the EEA);

but the election must be in respect of all the *firm's* business which consists of that activity.

- (4) A *firm* must keep a record of any election in (3).

5.1.2 G A *firm* that is an *approved bank*, and relies on the exemption under *CASS 5.1.1 R(2)(e)*, should be able to account to all of its *clients* for amounts held on their behalf at all times. A bank account opened with the *firm* that is in the name of the *client* would generally be sufficient. When *money* from *clients* deposited with the *firm* is held in a pooled account, this account should be clearly identified as an account for *clients*. The *firm* should also be able to demonstrate that an amount owed to a specific *client* that is held within the pool can be reconciled with a record showing that individual's *client* balance and is, therefore, identifiable at any time.

- 5.1.3 R An *authorised professional firm* regulated by The Law Society (of England and Wales), The Law Society of Scotland or The Law Society of Northern Ireland must comply with the rules of its *designated professional body* as specified in CASS 5.1.4R, in force on 14 January 2005, and if it does so, it will be deemed to comply with CASS 5.2 to 5.6.
- 5.1.4 R For the purposes of CASS 5.1.3R the relevant rules are:
- (1) If regulated by the Law Society (of England and Wales);
    - (a) the Solicitors' Accounts Rules 1998; or
    - (b) where applicable, the Solicitors Overseas Practice Rules 1990;
  - (2) if regulated by the Law Society of Scotland, the Solicitors' (Scotland) Accounts, Accounts Certificate, Professional Practice and Guarantee Fund Rules 2001;
  - (3) if regulated by the Law Society of Northern Ireland, the Solicitors' Accounts Regulations 1998.
- 5.1.5 R Money is not *client money* when:
- (1) it becomes properly due and payable to the *firm*:
    - (a) for its own account; or
    - (b) in its capacity as agent of an *insurance undertaking* where the *firm* acts in accordance with CASS 5.2; or
  - (2) it is otherwise received by the *firm* pursuant to an arrangement made between an *insurance undertaking* and another *person* (other than a *firm*) by which that other *person* has authority to underwrite risks, settle claims or handle refunds of *premiums* on behalf of that *insurance undertaking* outside the *United Kingdom* and where the *money* relates to that business.
- 5.1.6 R In CASS 5.1 to 5.6 an *insurance undertaking* (when acting as such) with whom a *firm* conducts *insurance mediation activity* is not to be treated as a *client* of the *firm*.

Purpose

- 5.1.7 G (1) *Principle 10* (Clients' assets) requires a *firm* to arrange adequate protection for *clients'* assets when the *firm* is responsible for them. An essential part of that protection is the proper accounting and handling of *client money*. The *rules* in *CASS 5.1* to *5.6* also give effect to the requirement in article 4.4 of the *IMD* that all necessary measures should be taken to protect *clients* against the inability of an *insurance intermediary* to transfer *premiums* to an *insurance undertaking* or to transfer the proceeds of a claim or *premium* refund to the insured.
- (2) There are two particular approaches which *firms* can adopt which reflect options given in article 4.4. The first is to provide by law or contract for a transfer of risk from the *insurance intermediary* to the *insurance undertaking* (*CASS 5.2*). The second is that *clients'* *money* is strictly segregated by being transferred to *client accounts* that cannot be used to reimburse other creditors in the event of the *firm's* insolvency (*CASS 5.3* and *5.4* provide different means of achieving such segregation).
- 5.1.8 G *Firms* which carry on *designated investment business* which may, for example, involve them handling *client money* in respect of life assurance business should refer to *CASS 4* which includes provisions enabling *firms* to elect to comply solely with *CASS 4* or with *CASS 5* in respect of that business.
- 5.1.9 G *Firms* are reminded that *SUP 3* contains provisions which are relevant to the preparation and delivery of reports by auditors.
- 5.2 Holding money as agent of insurance undertaking
- Introduction
- 5.2.1 G *Money* is not *client money* when a *firm* holds *money* as agent for an *insurance undertaking* to which *premiums* are, or will become, payable or from whom claims *money* or *premium* refunds are received for onward payment to the *firm's* *client*. This is because for the purposes of *CASS 5.1* to *5.6* an *insurance undertaking* with whom a *firm* transacts *insurance mediation activity* is not treated as a *client* of the *firm*. Where a *firm* acts as the agent of an *insurance undertaking* (for the purpose of receiving *premiums*, claims *money* and *premium* refunds) the *firm's* *clients* will be adequately protected because *premiums* will be treated as being received by the *insurance undertaking* when they are received by the agent and claims *money* and *premium* refunds will only be treated as received by the *client* when they are actually paid over.



- 5.2.2 G (1) Agency agreements between *insurance intermediaries* and *insurance undertakings* may be of a general kind and facilitate the introduction of business to the *insurance undertaking*. Alternatively, an agency agreement may confer on the *intermediary* contractual authority to commit the *insurance undertaking* to risk or authority to settle claims or handle *premium* refunds (often referred to as "binding authorities"). *CASS 5.2.3 R* requires that binding authorities of this kind must provide that the *intermediary* is to act as the agent of the *insurance undertaking* for the purpose of receiving and holding *premiums* (if the *intermediary* has authority to commit the *insurance undertaking* to risk), claims *monies* (if the *intermediary* has authority to settle claims on behalf of the *insurance undertaking*) and *premium* refunds (if the *intermediary* has authority to make refunds of *premiums* on behalf of the *insurance undertaking*). Accordingly such *money* is not *client money* for the purpose of *CASS 5*.
- (2) Other introductory agency agreements may also, depending on their precise terms, satisfy some or all of the requirements of the type of written agreement which will result in a transfer of risk for the purposes of *CASS 5.2*. It is desirable that an *intermediary* should, before informing its *clients* (in accordance with *CASS 5.2.3 R (3)*) that it will receive *money* as agent of an *insurance undertaking*, agree the terms of that notification with the relevant *insurance undertakings*.

Requirement for written agreement before acting as agent of insurance undertaking

- 5.2.3 R (1) A *firm* must not agree to:
- (a) *deal in investments as agent* for an *insurance undertaking* in connection with *insurance mediation activity*; or
  - (b) act as agent for an *insurance undertaking* for the purpose of settling claims or handling *premium* refunds; or
  - (c) otherwise receive *money* as agent of an *insurance undertaking*;
- unless:
- (d) it has entered into a written agreement with the *insurance undertaking* to that effect; and
  - (e) it is satisfied on reasonable grounds that the terms of the policies issued by the *insurance undertaking* to the *firm's clients* are likely to be compatible with such an agreement; and
  - (f) (i) (in the case of (a)) the agreement required by (d) expressly provides for the *firm* to act as agent of the *insurance undertaking* for the purpose of receiving *premiums* from the *firm's clients*; and

- (ii) (in the case of (b)) the agreement required by (d) expressly provides for the *firm* to act as agent of the *insurance undertaking* for the purpose of receiving and holding claims *money* (or, as the case may be, *premium* refunds) prior to transmission to the client making the *claim* (or, as the case may be, entitled to the *premium refund*) in question.
- (2) A *firm* must retain a copy of any agreement it enters pursuant to (1) for a period of at least six years from the date on which it is terminated.
- (3) Where a *firm* holds, or is to hold, *money* as agent for an *insurance undertaking* it must ensure that it informs those of its *clients* whose transactions may be affected by the arrangement (whether in its *terms of business*, *client agreements* or otherwise in writing) that it will hold their *money* as agent of the *insurance undertaking* and if necessary the extent of such agency and whether it includes all items of *client money* or is restricted, for example, to the receipt of *premiums*.
- (4) A *firm* may (subject to the consent of the *insurance undertaking* concerned) include in an agreement in (1) provision for *client money* received by an *appointed representative* to be held by the *representative* as agent for the *insurance undertaking* (in which event it must ensure that the *representative* provides the information to *clients* required by (3)).
- 5.2.4 G *Firms* are reminded that CASS 5.1.5R(1)(b) provides that *money* held in accordance with an agreement made under CASS 5.2.3R is not *client money* and, in accordance with the *rules* in CASS 5.5, that *money* must not be kept in a *client bank account*.
- 5.2.5 G A *firm* which provides for the protection of a *client* under CASS 5.2 is relieved of the obligation to provide protection for that *client* under CASS 5.3 or CASS 5.4 to the extent of the items of the *money* protected by the agency agreement.
- 5.2.6 G A *firm* may in accordance with CASS 5.2.3R (4), arrange for an *insurance undertaking* to accept responsibility for the *money* held by its *appointed representatives* in which event CASS 5.5.18R to CASS 5.5.25G will not apply.
- 5.2.7 G A *firm* may operate on the basis of an agency agreement as provided for by CASS 5.2.3R for some of its *clients* and with protection provided by a *client money* trust in accordance with CASS 5.3 or 5.4 for other *clients*. A *firm* may also operate on either basis for the same *client* but in relation to different transactions. A *firm* which does so should be satisfied that its administrative systems and controls are adequate and, in accordance with CASS 5.2.4G, should ensure that *money* held for both types of *client* and business is kept separate.
- 5.3 Statutory trust

- 5.3.1 G Section 139(1) of the *Act* (Miscellaneous ancillary matters) provides that *rules* may make provision which result in *client money* being held by a *firm* on trust (England and Wales and Northern Ireland) or as agent (Scotland only). *CASS 5.3.2R* creates a fiduciary relationship between the *firm* and its *client* under which *client money* is in the legal ownership of the *firm* but remains in the beneficial ownership of the *client*. In the event of failure of the *firm*, costs relating to the distribution of *client money* may have to be borne by the trust.
- 5.3.2 R A *firm* (other than a *firm* acting in accordance with *CASS 5.4*) receives and holds *client money* as trustee (or in Scotland as agent) on the following terms:
- (1) for the purposes of and on the terms of *CASS 5.3*, *CASS 5.5* and the *client money (insurance) distribution rules*;
  - (2) subject to (3), for the *clients* for whom that *money* is held, according to their respective interests in it;
  - (3) on *failure* of the *firm*, for the payment of the costs properly attributable to the distribution of the *client money* in accordance with (2); and
  - (4) after all valid claims and costs under (2) and (3) have been met, for the *firm* itself.
- 5.3.3 G (1) A *firm* which holds *client money* can discharge its obligation to ensure adequate protection for its *clients* in respect of such *money* by complying with *CASS 5.3* which provides for such *money* to be held by the *firm* on the terms of a trust imposed by the *rules*.
- (2) The trust imposed by *CASS 5.3* is limited to a trust in respect of *client money* which a *firm* receives and holds. The consequential and supplementary requirements in *CASS 5.5* are designed to secure the proper segregation and maintenance of adequate *client money* balances. In particular, *CASS 5.5* does not permit a *firm* to use *client money* balances to provide credit for *clients* (or potential *clients*) such that, for example, their *premium* obligations may be met in advance of the *premium* being remitted to the *firm*. A *firm* wishing to provide credit for *clients* may however do so out of its own funds.

## 5.4 Non-statutory client money trust

### Introduction

- 5.4.1 G (1) *CASS 5.4* permits a *firm*, which has adequate resources, systems and controls, to declare a trust on terms which expressly authorise it, in its capacity as trustee, to make advances of credit to the *firm's clients*. The *client money* trust required by *CASS 5.4* extends to such debt obligations which will arise if the *firm*, as trustee, makes credit advances, to enable a client's *premium* obligations to be met before the *premium* is remitted to the *firm* and similarly if it allows claims and *premium* refunds to be paid to the *client* before receiving remittance of those *monies* from the *insurance undertaking*.
- (2) *CASS 5.4* does not permit a *firm* to make advances of credit to itself out of the *client money* trust. Accordingly, *CASS 5.4* does not permit a *firm* to withdraw *commission* from the *client money* trust before it has received the *premium* from the *client* in relation to the *non-investment insurance contract* which generated the *commission*.

Voluntary nature of this section

5.4.2 R A *firm* may elect to comply with the requirements in this section, and may do so for some of its business whilst complying with *CASS 5.3* for other parts.

5.4.3 R A *firm* is not subject to *CASS 5.3* when and to the extent that it acts in accordance with this section.

Conditions for using the non-statutory client money trust

- 5.4.4 R A *firm* may not handle *client money* in accordance with the *rules* in this section unless each of the following conditions is satisfied:
- (1) the *firm* must have and maintain systems and controls which are adequate to ensure that the *firm* is able to monitor and manage its *client money* transactions and any credit risk arising from the operation of the trust arrangement and, if in accordance with *CASS 5.4.2R* a *firm* complies with both the *rules* in *CASS 5.3* and *CASS 5.4*, such systems and controls must extend to both arrangements;
  - (2) the *firm* must obtain, and keep current, written confirmation from its auditor that it has in place systems and controls which are adequate to meet the requirements in (1);
  - (3) the *firm* must designate a *manager* with responsibility for overseeing the *firm's* day to day compliance with the systems and controls in (1) and the *rules* in this section;
  - (4) the *firm* (if, under the terms of the non-statutory trust, it is to handle *client money* for *retail customers*) must have and at all times maintain capital resources of not less than £50,000 calculated in accordance with *PRU 9.3.51R*; and

- (5) in relation to each of the *clients* for whom the *firm* holds *money* in accordance with *CASS 5.4*, the *firm* must take reasonable steps to ensure that its *terms of business* or other *client agreements* adequately explain, and obtain the *client's* informed consent to, the *firm* holding the *client's money* in accordance with *CASS 5.4*.
- 5.4.5 G The amount of a *firm's* capital resources maintained for the purposes of *PRU 9.3.30R* will also satisfy (in whole or in part) the requirement in *CASS 5.4.4R (4)*.
- Client money to be received under the non-statutory client money trust
- 5.4.6 R A *firm* must not receive or hold any *client money* unless it does so as trustee (or, in Scotland, as agent) and has properly executed a deed (or equivalent formal document) to that effect.
- Contents of trust deed
- 5.4.7 R The deed referred to in *CASS 5.4.6R* must provide that the *money* (and, if appropriate, *designated investments*) are held:
- (1) for the purposes of and on the terms of:
    - (a) *CASS 5.4*;
    - (b) the applicable provisions of *CASS 5.5*; and
    - (c) the *client money (insurance) distribution rules*.
  - (2) subject to (3), for the *clients* for whom that *money* is held, according to their respective interests in it;
  - (3) on *failure* of the *firm*, for the payment of the costs properly attributable to the distribution of the *client money* in accordance with (2); and
  - (4) after all valid claims and costs under (2) and (3) have been met, for the *firm* itself.
- 5.4.8 R The deed (or equivalent formal document) referred to in *CASS 5.4.6R* may provide that:
- (1) the *firm*, acting as trustee (or, in Scotland, as agent), has power to make advances or give credit to *clients* or *insurance undertakings* from *client money*, provided that it also provides that any debt or other obligation of a *client* or resulting obligation of an *insurance undertaking*, in relation to an advance or credit, is held on the same terms as *CASS 5.4.7R*;
  - (2) the benefit of a letter of credit or unconditional guarantee provided by an *approved bank* on behalf of a *firm* to satisfy any shortfall in the *firm's client money* resource (as calculated under *CASS 5.5.65R*) when compared with the *firm's client money* requirement (as calculated under *CASS 5.6.66R* or as appropriate *CASS 5.5.68R*), is held on the same terms as *CASS 5.4.7R*.

## 5.5 Segregation and the operation of client money accounts

### Application

- 5.5.1 R Unless otherwise stated each of the provisions in *CASS 5.5* applies to *firms* which are acting in accordance with *CASS 5.3* (Statutory trust) or 5.4 (Non-statutory trust).
- 5.5.2 G One purpose of *CASS 5.5* is to ensure that, unless otherwise permitted, *client money* is kept separate from the *firm's own money*. Segregation, in the event of a *firm's* failure, is important for the effective operation of the trust that is created to protect *client money*. The aim is to clarify the difference between *client money* and general creditors' entitlements in the event of the *failure* of the *firm*.
- Requirement to segregate
- 5.5.3 R A *firm* must, except to the extent permitted by *CASS 5.5*, hold *client money* separate from the *firm's money*.

Money due to a client from a firm

- 5.5.4 R If a *firm* is liable to pay *money* to a *client*, it must as soon as possible, and no later than one *business day* after the *money* is due and payable:
- (1) pay it into a *client bank account*, in accordance with CASS 5.5.5R;  
or
  - (2) pay it to, or to the order of, the *client*.

Segregation

- 5.5.5 R A *firm* must segregate *client money* by either:
- (1) paying it as soon as is practicable into a *client bank account*; or
  - (2) paying it out in accordance with CASS 5.5.80R.
- 5.5.6 G The *FSA* expects that in most circumstances it will be practicable for a *firm* to pay *client money* into a *client bank account* by not later than the next *business day* after receipt.
- 5.5.7 G Where an insurance transaction involves more than one *firm* acting in a chain such that for example *money* is transferred from a “producing” broker who has received *client money* from a *retail customer* to an intermediate broker and thereafter to an *insurance undertaking*, each broker *firm* will owe obligations to its immediate *client* to segregate *client money* which it receives (in this example the producing broker in relation to the *retail customer* and the intermediate broker in relation to the producing broker). A *firm* which allows a third party broker to hold or control *client money* will not thereby be relieved of its fiduciary obligations (see CASS 5.5.34R).
- 5.5.8 R A *firm* may segregate *client money* in a different currency from that of receipt. If it does so, the *firm* must ensure that the amount held is adjusted at intervals of not more than twenty five *business days* to an amount at least equal to the original currency amount (or the currency in which the *firm* has its liability to its *clients*, if different), translated at the previous day's closing spot exchange rate.
- 5.5.9 R A *firm* must not hold *money* other than *client money* in a *client bank account* unless it is:
- (1) a minimum sum required to open the account, or to keep it open; or
  - (2) *money* temporarily in the account in accordance with CASS 5.5.16R (Withdrawal of commission and mixed remittance); or
  - (3) interest credited to the account which exceeds the amount due to *clients* as interest and has not yet been withdrawn by the *firm*.

- 5.5.10 R If it is prudent to do so to ensure that *client money* is protected (and provided that doing so would otherwise be in accordance with CASS 5.5.63R(2)(b)), a *firm* may pay into, or maintain in, a *client bank account money* of its own, and that *money* will then become *client money* for the purposes of CASS 5 and the *client money (insurance) distribution rules*.
- 5.5.11 R A *firm*, when acting in accordance with CASS 5.3 (statutory trust), must ensure that the total amount of *client money* held for each *client* in any of the *firm's client money bank accounts* is positive and that no payment is made from any such account for the benefit of a *client* unless the *client* has provided the *firm* with cleared funds to enable the payment to be made.
- 5.5.12 R If *client money* is received by the *firm* in the form of an automated transfer, the *firm* must take reasonable steps to ensure that:
- (1) the *money* is received directly into a *client bank account*; and
  - (2) if *money* is received directly into the *firm's* own account, the *money* is transferred into a *client bank account* no later than the next *business day* after receipt.
- 5.5.13 G A *firm* can hold *client money* in either a *general client bank account* (CASS 5.5.38R) or a *designated client bank account* (CASS 5.5.39R). A *firm* holds all *client money* in *general client bank accounts* for its *clients* as part of a common pool of *money* so those particular *clients* do not have a claim against a specific sum in a specific account; they only have a claim to the *client money* in general. A *firm* holds *client money* in *designated client bank accounts* for those *clients* who requested that their *client money* be part of a specific pool of *money*, so those particular *clients* do have a claim against a specific sum in a specific account; they do not have a claim to the *client money* in general unless a *primary pooling event* occurs. If the *firm* becomes insolvent, and there is (for whatever reason) a *shortfall* in *money* held for a *client* compared with that *client's* entitlements, the available funds will be distributed in accordance with the *client money (insurance) distribution rules*.

#### Non-statutory trust - segregation of designated investments

- 5.5.14 R (1) A *firm* which handles *client money* in accordance with the *rules* for a non-statutory trust in CASS 5.4 may, to the extent it considers appropriate, but subject to (2), satisfy the requirement to segregate *client money* by segregating or arranging for the segregation of *designated investments* with a value at least equivalent to such *money* as would otherwise have been segregated into a *client bank account*.
- (2) A *firm* may not segregate *designated investments* unless it:



- (a) takes reasonable steps to ensure that any *retail customers* whose *client money* interests may be protected by such segregation are aware that the *firm* may operate such an arrangement and have (whether through its *terms of business*, *client agreements* or otherwise in writing) an adequate opportunity to give their informed consent;
- (b) ensures that the terms on which it will segregate *designated investments* include provision for it to take responsibility for meeting any *shortfall* in its *client money* resource which is attributable to falls in the market value of a segregated *investment*;
- (c) provides in the deed referred to in *CASS 5.4.6R* for *designated investments* which it segregates to be held by it on the terms of the non-statutory trust; and
- (d) takes reasonable steps to ensure that the segregation is at all times in conformity with the range of permitted *investments*, general principles and conditions in *CASS 5*, Annex 1R.

5.5.15 G A *firm* which takes advantage of *CASS 5.5.14R* will need to consider whether its *permission* should include the *permitted activity* of *managing investments*. If the *firm* is granted a power to manage with discretion the funds over which it is appointed as trustee under the trust deed required by *CASS 5.4* then it will be likely to need a *permission to manage investments*. It is unlikely to need such a permission however if it is merely granted a power to invest but the deed stipulates that the funds may only be managed with discretion by another *firm* (which has the necessary *permission*). Such an arrangement would not preclude the *firm* holding *client money* as trustee from appointing another *firm* (or *firms*) as manager and setting an appropriate strategy and overall asset allocation, subject to the limits set out in *CASS 5*, Annex 1R. A *firm* may also need to consider whether it needs a *permission* to operate a *collective investment scheme* if any of its *clients* are to participate in the income or gains arising from the acquisition or disposal of *designated investments*.

#### Withdrawal of commission and mixed remittance

5.5.16 R (1) A *firm* may draw down *commission* from the *client bank account* if:

- (a) it has received the *premium* from the *client*; and
- (b) this is consistent with the terms of business of the *insurance undertaking* to whom the *premium* is payable;

and the *firm* may draw down *commission* before payment of the *premium* to the *insurance undertaking*, provided that the conditions in (a) and (b) are satisfied.

(2) If a *firm* receives a *mixed remittance* (that is part *client money* and part other *money*), it must:

- (a) pay the full sum into a *client bank account* in accordance with CASS 5.5.5R; and
- (b) pay the *money* that is not *client money* out of the *client bank account* as soon as reasonably practicable and in any event by not later than twenty-five *business days* after the day on which the remittance is cleared.

- 5.5.17 G
- (1) The procedure required by CASS 5.5.16R will apply where *money* becomes due to the *firm* in respect of *fees* due from *clients* (whether to the *firm* or other professionals) and amounts in respect of *commission* which becomes due to the *firm* from an *insurance undertaking*.
  - (2) *Firms* are reminded that *money* received in accordance with CASS 5.2 must not be kept in a *client bank account*. *Client money* received from a third party *premium* finance provider should however be segregated into a *client bank account*.
  - (3) Where a *client* makes payments of *premium* to a *firm* in instalments, CASS 5.5.16R applies in relation to each instalment.

Appointed representatives, field representatives and other agents

- 5.5.18 R
- (1) A *firm* must in relation to each of its *appointed representatives, field representatives* and other agents comply with CASS 5.5.19R to CASS 5.5.21R (Immediate segregation) or with CASS 5.5.23R (Periodic segregation and reconciliation).
  - (2) A *firm* must in relation to each *representative* or other agent keep a record of whether it is complying with CASS 5.5.19R to CASS 5.5.21R or with CASS 5.5.23R.
  - (3) A *firm* is, but without affecting the application of CASS 5.5.19R to CASS 5.5.23R, to be treated as the recipient of *client money* which is received by any of its *appointed representatives, field representatives* or other agents.

Immediate segregation

- 5.5.19 R
- A *firm* must establish and maintain procedures to ensure that *client money* received by its *appointed representatives, field representatives* or other agents of the *firm* is:
- (1) paid into a *client bank account* of the *firm* in accordance with CASS 5.5.5R; or
  - (2) forwarded to the *firm*, or in the case of a *field representative* forwarded to a specified business address of the *firm*, so as to ensure that the *money* arrives at the specified business address by the close of the third *business day*.

- 5.5.20 G For the purposes of CASS 5.5.19R, the *client money* received on *business day* one should be forwarded to the *firm* or specified business address of the *firm* no later than the next *business day* after receipt (*business day* two) in order for it to reach that *firm* or specified business address by the close of the third *business day*. Procedures requiring the *client money* to be sent to the *firm* or the specified business address of the *firm* by first class post no later than the next *business day* after receipt would meet the requirements of CASS 5.5.19R.
- 5.5.21 R If *client money* is received in accordance with CASS 5.5.19R, the *firm* must ensure that its *appointed representatives, field representatives* or other agents keep *client money* (whether in the form of *premiums, claims money* or *premium* refunds) separately identifiable from any other *money* (including that of the *firm*) until the *client money* is paid into a *client bank account* or sent to the *firm*.
- 5.5.22 G A *firm* which acts in accordance with CASS 5.5.19R to CASS 5.5.21R need not comply with CASS 5.5.23R.

#### Periodic segregation and reconciliation

- 5.5.23 R
- (1) A *firm* must, on a regular basis, and at reasonable intervals, ensure that it holds in its *client bank account* an amount which (in addition to any other amount which it is required by these *rules* to hold) is not less than the amount which it reasonably estimates to be the aggregate of the amounts held at any time by its *appointed representatives, field representatives* and other agents.
  - (2) A *firm* must, not later than ten *business days* following the expiry of each period in (1):
    - (a) carry out, in relation to each such *representative* or agent, a reconciliation of the amount paid by the *firm* into its *client bank account* with the amount of *client money* actually received and held by the *representative* or other agent; and
    - (b) make a corresponding payment into, or withdrawal from, the account.

- 5.5.24 G (1) *CASS 5.5.23R* allows a *firm* with *appointed representatives*, *field representatives* and other agents to avoid the need for the *representative* to forward *client money* on a daily basis but instead requires a *firm* to segregate into its *client money bank account* amounts which it reasonably estimates to be sufficient to cover the amount of *client money* which the *firm* expects its *representatives* or agents to receive and hold over a given period. At the expiry of each such period, the *firm* must obtain information about the actual amount of *client money* received and held by its *representatives* so that it can reconcile the amount of *client money* it has segregated with the amounts actually received and held by its *representatives* and agents. The frequency at which this reconciliation is to be performed is not prescribed but it must be at regular and reasonable intervals having regard to the nature and frequency of the *insurance business* carried on by its *representatives* and agents. For example a period of six *months* might be appropriate for a *representative* which conducts business involving the receipt of *premiums* only infrequently whilst for other *representatives* a periodic reconciliation at *monthly* intervals (or less) may be appropriate.
- (2) Where a *firm* operates on the basis of *CASS 5.5.23R*, the *money* which is segregated into its *client bank account* is *client money* and will be available to meet any obligations owed to the *clients* of its *representatives* who for this purpose are treated as the *firm's clients*.
- 5.5.25 G A *firm* which acts in accordance with *CASS 5.5.23R* need not comply with *CASS 5.5.19R* to *CASS 5.5.21R*.
- Client entitlements
- 5.5.26 R A *firm* must take reasonable steps to ensure that it is notified promptly of any receipt of *client money* in the form of *client* entitlements.
- 5.5.27 G The 'entitlements' mentioned in *CASS 5.5.26R* refer to any kind of miscellaneous payment which the *firm* receives on behalf of a *client* and which are due to be paid to the *client*.
- 5.5.28 R When a *firm* receives a *client* entitlement on behalf of a *client*, it must pay any part of it which is *client money*:
- (1) for *client* entitlements received in the *United Kingdom*, into a *client bank account* in accordance with *CASS 5.5.5R*; or
- (2) for *client* entitlements received outside the *United Kingdom*, into any bank account operated by the *firm*, provided that such *client money* is:
- (a) paid to, or in accordance with, the instructions of the *client* concerned; or
- (b) paid into a *client bank account* in accordance with *CASS 5.5.5R* (1), as soon as possible but no later than five *business days* after the *firm* is notified of its receipt.

5.5.29 R A *firm* must take reasonable steps to ensure that a *client* entitlement which is *client money* is allocated within a reasonable period of time after notification of receipt.

#### Interest and investment returns

5.5.30 R (1) In relation to *retail customers*, a *firm* must, subject to (2), take reasonable steps to ensure that its *terms of business* or other *client agreements* adequately explain, and where necessary obtain a *client's* informed consent to, the treatment of interest and, if applicable, investment returns, derived from its holding of *client money* and any segregated *designated investments*.

(2) In respect of interest earned on *client bank accounts*, (1) does not apply if a *firm* has reasonable ground to be satisfied that in relation to *insurance mediation activities* carried on with or for a *retail customer* the amount of interest earned will be not more than £20 per transaction.

5.5.31 G If no interest is payable to a *retail customer*, that fact should be separately identified in the *firm's client agreement* or *terms of business*.

5.5.32 G If a *firm* outlines its *policy* on its payment of interest, it need not necessarily disclose the actual rates prevailing at any particular time; the *firm* should disclose the terms, for example, LIBOR plus or minus 'x' percentage points.

#### Transfer of client money to a third party

5.5.33 G CASS 5.5.34R sets out the requirements a *firm* must comply with when it transfers *client money* to another *person* without discharging its fiduciary duty owed to that *client*. Such circumstances arise when, for example, a *firm* passes *client money* to another broker for the purposes of the *client's* transaction being effected. A *firm* can only discharge itself from its fiduciary duty by acting in accordance with, and in the circumstances permitted by, CASS 5.5.80R.

5.5.34 R A *firm* may allow another *person*, such as another broker to hold or control *client money*, but only if:

- (1) the *firm* transfers the *client money* for the purpose of a transaction for a *client* through or with that *person*; and
- (2) in the case of a *retail customer*, that *customer* has been notified (whether through a *client agreement*, *terms of business*, or otherwise in writing) that the *client money* may be transferred to another *person*.

5.5.35 G In relation to the notification required by CASS 5.5.34R (2), there is no need for a *firm* to make a separate disclosure in relation to each transfer made.

- 5.5.36 G A *firm* should not hold excess *client money* with another broker. It should be held in a *client bank account*.

Client bank accounts

- 5.5.37 G The *FSA* generally requires a *firm* to place *client money* in a *client bank account* with an *approved bank*. However, a *firm* which is an *approved bank* must not (subject to *CASS 5.1.1R(2)(e)*) hold *client money* in an account with itself.
- 5.5.38 R (1) A *firm* must ensure that *client money* is held in a *client bank account* at one or more *approved banks*.
- (2) If the *firm* is a bank, it must not hold *client money* in an account with itself.
- 5.5.39 R A *firm* may open one or more *client bank accounts* in the form of a *designated client bank account*. Characteristics of these accounts are that:
- (1) the account holds *money* of one or more *clients*;
- (2) the account includes in its title the word 'designated';
- (3) the *clients* whose *money* is in the account have each consented in writing to the use of the bank with which the *client money* is to be held; and
- (4) in the event of the *failure* of that bank, the account is not pooled with any other type of account unless a *primary pooling event* occurs.
- 5.5.40 G (1) A *firm* may operate as many *client accounts* as it wishes.
- (2) A *firm* is not obliged to offer its *clients* the facility of a *designated client bank account*.
- (3) Where a *firm* holds *money* in a *designated client bank account*, the effect upon either:
- (a) the *failure* of a bank where any other *client bank account* is held; or
- (b) the *failure* of a third party to whom *money* has been transferred out of any other *client bank account* in accordance with *CASS 5.5.34R*;
- (each of which is a *secondary pooling event*) is that *money* held in the *designated client bank account* is not pooled with *money* held in any other account. Accordingly *clients* whose *money* is held in a *designated client bank account* will not share in any *shortfall* resulting from a *failure* of the type described in (a) or (b).

- (4) Where a *firm* holds *client money* in a *designated client bank account*, the effect upon the failure of the *firm* (which is a *primary pooling event*) is that *money* held in the *designated client bank account* is pooled with *money* in every other *client bank account* of the *firm*. Accordingly, *clients* whose *money* is held in a *designated client bank account* will share in any *shortfall* resulting from a *failure* of the *firm*.

5.5.41 R A *firm* may hold *client money* with a bank that is not an *approved bank* if all the following conditions are met:

- (1) the *client money* relates to one or more insurance transactions which are subject to the law or market practice of a jurisdiction outside the *United Kingdom*;
- (2) because of the applicable law or market practice of that overseas jurisdiction, it is not possible to hold the *client money* in a *client bank account* with an *approved bank*;
- (3) the *firm* holds the *money* with such a bank for no longer than is necessary to effect the transactions;
- (4) the *firm* notifies each relevant *client* and has, in relation to a *retail customer*, a *client agreement* or *terms of business* which adequately explain that:
  - (a) the *client money* will not be held with an *approved bank*;
  - (b) in such circumstances, the legal and regulatory regime applying to the bank with which the *client money* is held will be different from that of the *United Kingdom* and, in the event of a *failure* of the bank, the *client money* may be treated differently from the treatment which would apply if the *client money* were held by an *approved bank* in the *United Kingdom*; and
  - (c) if it is the case, the particular 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*, notwithstanding the *firm's* request to the bank as required by CASS 5.5.49R; and
- (5) the *client money* is held in a designated bank account.

A firm's selection of a bank

- 5.5.42 G A *firm* owes a duty of care to a *client* when it decides where to place *client money*. The review required by CASS 5.5.43R is intended to ensure that the risks inherent in placing *client money* with a bank are minimised or appropriately diversified by requiring a *firm* to consider carefully the bank or banks with which it chooses to place *client money*. For example, a *firm* which is likely only to hold relatively modest amounts of *client money* will be likely to be able to satisfy this requirement if it selects an *authorised* UK clearing bank.
- 5.5.43 R Before a *firm* opens a *client bank account* and as often as is appropriate on a continuing basis (and no less than once in each financial year), it must take reasonable steps to establish that the bank is appropriate for that purpose.
- 5.5.44 G A *firm* should consider diversifying placements of *client money* with more than one bank where the amounts are, for example, of sufficient size to warrant such diversification.
- 5.5.45 G When considering where to place *client money* and to determine the frequency of the appropriateness test under CASS 5.5.43R, a *firm* should consider taking into account, together with any other relevant matters:
- (1) the capital of the bank;
  - (2) the amount of *client money* placed, as a proportion of the bank's capital and *deposits*;
  - (3) the credit rating of the bank (if available); and
  - (4) 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*.
- 5.5.46 G A *firm* will be expected to perform due diligence when opening a *client bank account* with a bank that is authorised by an *EEA regulator*. Any continuing assessment of that bank may be restricted to verification that it remains authorised by an *EEA regulator*.

Group banks

- 5.5.47 R Subject to CASS 5.5.41R, a *firm* that holds or intends to hold *client money* with a bank which is in the same *group* as the *firm* must:
- (1) undertake a continuous review in relation to that bank which is at least as rigorous as the review of any bank which is not in the same *group*, in order to ensure that the decision to use a *group* bank is appropriate for the *client*;



- (2) disclose in writing to its *client* at the outset of the *client* relationship (whether by way of a *client agreement*, *terms of business* or otherwise in writing) or, if later, not less than 20 *business days* before it begins to hold *client money* of that *client* with that bank:
- (a) that it is holding or intends to hold *client money* with a bank in the same *group*;
  - (b) the identity of the bank concerned; and
  - (c) that the *client* may choose not to have his *money* placed with such a bank.
- 5.5.48 R If a *client* has notified a *firm* in writing that he does not wish his *money* to be held with a bank in the same *group* as the *firm*, the *firm* must either:
- (1) place that *client money* in a *client bank account* with another bank in accordance with CASS 5.5.38R; or
  - (2) return that *client money* to, or pay it to the order of, the *client*.
- Notification and acknowledgement of trust (banks)
- 5.5.49 R When a *firm* opens a *client bank account*, the *firm* must give or have given written notice to the bank requesting the bank to acknowledge to it in writing:
- (1) that all *money* standing to the credit of the account is held by the *firm* as trustee (or if relevant in Scotland, as agent) 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
  - (2) that the title of the account sufficiently distinguishes that account from any account containing *money* that belongs to the *firm*, and is in the form requested by the *firm*.
- 5.5.50 R In the case of a *client bank account* in the *United Kingdom*, if the bank does not provide the acknowledgement referred to in CASS 5.5.49R within 20 *business days* after the *firm* dispatched the notice, the *firm* must withdraw all *money* standing to the credit of the account and deposit it in a *client bank account* with another bank as soon as possible.
- 5.5.51 R In the case of a *client bank account* outside the *United Kingdom*, if the bank does not provide the acknowledgement referred to in CASS 5.5.49R within 20 *business days* after the *firm* dispatched the notice, the *firm* must notify the *client* of this fact as set out in CASS 5.5.53R.
- 5.5.52 G *Firms* are reminded of the provisions of CASS 5.5.41R (4), which sets out the notification and consents required when using a bank that is not an *approved bank*.

Notification to clients: use of an approved bank outside the United Kingdom

- 5.5.53 R A *firm* must not hold, for a *retail customer*, *client money* in a *client bank account* outside the *United Kingdom*, unless the *firm* has previously disclosed to the *retail customer* (whether in its *terms of business*, *client agreement* or otherwise in writing):
- (1) that his *money* may be deposited in a *client bank account* outside the *United Kingdom* but that the *client* may notify the *firm* that he does not wish his *money* to be held in a particular jurisdiction;
  - (2) that in such circumstances, the legal and regulatory regime applying to the *approved bank* will be different from that of the *United Kingdom* and, in the event of a *failure* of the bank, his *money* may be treated in a different manner from that which would apply if the *client money* were held by a bank in the *United Kingdom*; and
  - (3) if it is the case, that a particular 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*, notwithstanding the *firm's* request to the bank as required by CASS 5.5.49R.

5.5.54 G There is no need for a *firm* to make a separate disclosure under CASS 5.5.53R (1) and (2) in relation to each jurisdiction.

5.5.55 G *Firms* are reminded of the provisions of CASS 5.5.41R (4), which sets out the notification and consents required when using a bank that is not an *approved bank*.

5.5.56 R If a *client* has notified a *firm* in writing before entering into a transaction that *client money* is not to be held in a particular jurisdiction, the *firm* must either:

- (1) hold the *client money* in a *client bank account* in a jurisdiction to which the *client* has not objected; or
- (2) return the *client money* to, or to the order of, the *client*.

5.5.57 G *Firms* are reminded of the provisions of CASS 5.5.41R (4), which sets out the notification and consents required when using a bank that is not an *approved bank*.

Notification to retail customers: use of broker or settlement agent outside the United Kingdom

5.5.58 R A *firm* must not undertake any transaction for a *retail customer* that involves *client money* being passed to another broker or *settlement agent* located in a jurisdiction outside the *United Kingdom*, unless the *firm* has previously disclosed to the *retail customer* (whether in its *terms of business*, *client agreement* or otherwise in writing):

- (1) that his *client money* may be passed to a *person* outside the *United Kingdom* but the *client* may notify the *firm* that he does not wish his *money* to be passed to a *person* in a particular jurisdiction; and
- (2) that, in such circumstances, the legal and regulatory regime applying to the broker or *settlement agent* will be different from that of the *United Kingdom* and, in the event of a *failure* of the broker or *settlement agent*, this *money* may be treated in a different manner from that which would apply if the *money* were held by a broker or *settlement agent* in the *United Kingdom*.

5.5.59 G There is no need for a *firm* to make a separate disclosure under CASS 5.5.58R in relation to each jurisdiction.

5.5.60 R If a *client* has notified a *firm* before entering into a transaction that he does not wish his *money* to be passed to another broker or *settlement agent* located in a particular jurisdiction, the *firm* must either:

- (1) hold the *client money* in a *client bank account* in the *United Kingdom* or a jurisdiction to which the *client* has not objected and pay its own *money* to the *firm's* own account with the broker, agent or counterparty; or
- (2) return the *money* to, or to the order of, the *client*.

Notification to the FSA: failure of a bank, broker or settlement agent

5.5.61 R On the *failure* of a third party with which *client money* is held, a *firm* must notify the *FSA*:

- (1) as soon as it becomes aware, of the *failure* of any bank, other broker or *settlement agent* or other entity with which it has placed, or to which it has passed, *client money*; and
- (2) as soon as reasonably practical, whether it intends to make good any *shortfall* that has arisen or may arise and of the amounts involved.

Client money calculation

5.5.62 G The purpose of the *client money* calculation is to act as a check that the amount of *client money* (and where appropriate the value of segregated *designated investments*) that is segregated at banks (and where appropriate third parties) is sufficient to meet the *firm's* obligations to its *clients*. For this purpose two, alternative, calculation methods are permitted, but a *firm* must use the same calculation method in relation to both CASS 5.3 and CASS 5.4. The first requires a *firm* to calculate its *client money* requirement by reference to individual *client money* balances. The second permits a *firm* to carry out the calculation on the basis of information in its business ledgers. In either case, the *firm* must carry out the calculation at least every 25 *business days*.

- 5.5.63 R A *firm* must, as often as is necessary to ensure the accuracy of its records and at least at intervals of not more than 25 *business days*:
- (1) check whether its *client money* resource, as determined by CASS 5.5.65R on the previous *business day*, was at least equal to the *client money* requirement, as defined in CASS 5.5.66R or CASS 5.5.68R, as at the close of business on that day; and
  - (2) ensure that:
    - (a) any *shortfall* is paid into a *client bank account* by the close of business on the day the calculation is performed; or
    - (b) any excess is withdrawn within the same time period unless CASS 5.5.9R or CASS 5.5.10R applies to the extent that the *firm* is satisfied on reasonable grounds that it is prudent to maintain a positive margin to ensure the test in (1) is satisfied having regard to any unreconciled items in its business ledgers as at the date on which the calculations are performed; and
  - (3) ensure that it includes in any calculation of its *client money* requirement (whether calculated in accordance with CASS 5.5.66R or CASS 5.5.68R) any amounts attributable to *client money* received by its *appointed representatives*, *field representatives* or other agents and which, as at the date of calculation, it is required to segregate in accordance with CASS 5.5.19R.

- 5.5.64 R A *firm* must keep a record of whether it calculates its *client money* requirement in accordance with CASS 5.5.66R or CASS 5.5.68R and may only use one method during each annual accounting period (which method must be the same in relation to both CASS 5.3 and CASS 5.4).

#### Client money resource

- 5.5.65 R The *client money* resource, for the purposes of CASS 5.5.63R, is:
- (1) the aggregate of the balances on the *firm's client money bank accounts*, as at the close of business on the previous *business day* and, if held in accordance with CASS 5.4, *designated investments* (valued on a prudent and consistent basis) together with *client money* held by a third party in accordance with CASS 5.5.34R;
  - (2) to the extent that *client money* is held in accordance with CASS 5.3 (statutory trust), insurance debtors (which in this case cannot include pre-funded items); and
  - (3) to the extent that *client money* is held in accordance with CASS 5.4 (non-statutory trust):

- (a) all insurance debtors (including pre-funded items whether in respect of advance *premiums*, claims, *premium* refunds or otherwise) shown in the *firm's* business ledgers as amounts due from *clients*, *insurance undertakings* and other *persons*, such debts valued on a prudent and consistent basis to the extent required to meet any shortfall of the *client money* resource compared with the *firm's client money* requirement; and
- (b) the amount of any letter of credit or unconditional guarantee provided by an *approved bank* and held on the terms of the trust (or, in Scotland, agency), limited to:
  - (i) the maximum sum payable by the *approved bank* under the letter of credit or guarantee; or
  - (ii) if less, the amount which would, apart from the benefit of the letter of credit or guarantee, be the *shortfall* of the *client money* resource compared with the *client money* requirement under CASS 5.5.66R or CASS 5.5.68R.

Client money (client balance) requirement

5.5.66 R A *firm's client money* (*client balance*) requirement is the sum of, for all *clients*, the individual *client* balances calculated in accordance with CASS 5.5.67R but excluding any individual balances which are negative (that is, uncleared *client* funds).

5.5.67 R The individual *client* balance for each *client* must be calculated as follows:

- (1) the amount paid by a *client* to the *firm* (to include all *premiums*); plus
- (2) the amount due to the *client* (to include all claims and *premium* refunds); plus
- (3) the amount of any interest or investment returns due to the *client*;
- (4) less the amount paid to *insurance undertakings* for the benefit of the *client* (to include all *premiums*);
- (5) less the amount paid by the *firm* to the *client* (to include all claims and *premium* refunds);

and where the individual *client* balance is found by the sum ((1) + (2) + (3)) – ((4) + (5)).

Client money (accruals) requirement

5.5.68 R A *firm's client money* (accruals) requirement is the sum of the following:

- (1) all insurance creditors shown in the *firm's* business ledgers as amounts due to *insurance undertakings*, *clients* and other *persons*; plus

- (2) unearned brokerage being the amount of brokerage shown as accrued (but not shown as earned and payable) as at the date of the calculation (a prudent estimate must be used if the *firm* is unable to produce an exact figure at the date of the calculation).

5.5.69 R A *firm* which calculates its *client money* requirement on the preceding basis must in addition and within a reasonable period be able to match its *client money* resource to its requirement by reference to individual *clients* (with such matching being achieved for the majority of its *clients* and transactions).

Reconciliation of client money: frequency of reconciliation

5.5.70 R A *firm* must perform a reconciliation of the *client money* balances which it holds, or if appropriate perform the *client money* (accruals) calculation, as frequently as is necessary to ensure the accuracy of its record of *money* so held, and no less than once in every 25 *business days*.

5.5.71 G In determining whether the minimum acceptable frequency is sufficient, a *firm* should consider the risks to which the business is exposed, such as the volume of business, and where and with whom the *client money* is held.

5.5.72 R A *firm* must complete the reconciliation of *client money* within ten *business days* of the date on which the *client money* resource and *client money* requirement were determined.

Verification of banking records

5.5.73 R A *firm* must for the purpose of the calculations required by CASS 5.5.63R compare 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 bank with which that account is held.

Verification discrepancies

5.5.74 R When any discrepancy arises as a result of the verification carried out under CASS 5.5.73R, the *firm* must identify the reason for the discrepancy and correct it as soon as possible, unless the discrepancy arises solely as a result of timing differences between the accounting systems of the party providing the statement or confirmation and those of the *firm*.

5.5.75 R While a *firm* is unable to resolve a difference arising from a reconciliation, and one record or a set of records examined by the *firm* during its reconciliation indicates that there is a need to have a greater amount of *client money* than is in fact the case, the *firm* must assume, until the matter is finally resolved, that the record or set of records is accurate and pay its own *money* into a relevant account.

Failure to perform calculations

- 5.5.76 R A *firm's* must notify the *FSA* immediately if it is unable to, or does not, perform the calculation required by *CASS 5.5.63R*.
- 5.5.77 R A *firm* must notify the *FSA* immediately it becomes aware that it may not be able to make good any *shortfall* identified by *CASS 5.5.63R* by the close of business on the day the calculation is performed.
- 5.5.78 R A *firm* must notify the *FSA* as soon as possible if it is unable to comply with any of the requirements of *CASS 5.5.70R*, *CASS 5.5.72R*, *CASS 5.5.73R*, *CASS 5.5.74R* and *CASS 5.5.75R*.

Discharge of fiduciary duty

- 5.5.79 G The purpose of *CASS 5.5.80R* to *CASS 5.5.83R* is to set out those situations in which a *firm* will have fulfilled its contractual and fiduciary obligations in relation to any *client money* held for or on behalf of its *client*, in relation to the *firm's* ability to require repayment of that *money*.
- 5.5.80 R *Money* ceases to be *client money* if it is paid:
- (1) to the *client*, or a duly authorised representative of the *client*; or
  - (2) to a third party on the instruction of or with the specific consent of the *client*, but not if it is transferred to a third party in the course of effecting a transaction, in accordance with *CASS 5.5.34R*; or
  - (3) into a bank account of the *client* (not being an account which is also in the name of the *firm*); or
  - (4) to the *firm* itself, when it is due and payable to the *firm* in accordance with *CASS 5.1.5R* (1); or
  - (5) to the *firm* itself, when it is an excess in the *client bank account* as set out in *CASS 5.5.63R* (2)(b).
- 5.5.81 G
- (1) A *firm* which pays professional fees (for example to a loss adjuster or valuer) on behalf of a *client* may do so in accordance with *CASS 5.5.80R* (2) where this is done on the instruction of or with the consent of the *client*.
  - (2) When a *firm* wishes to transfer *client money* balances to a third party in the course of transferring its business to another *firm*, it should do so in compliance with *CASS 5.5.80R* and a transferee *firm* will come under an obligation to treat any *client money* so transferred in accordance with these *rules*.
  - (3) *Firms* are reminded of their obligation, when transferring *money* to third parties in accordance with *CASS 5.5.34R*, to use appropriate skill, care and judgment in their selection of third parties in order to ensure adequate protection of *client money*.

- (4) *Firms* are reminded that, in order to calculate their *client money* resource in accordance with *CASS 5.5.63R* to *CASS 5.5.65R*, they will need to have systems in place to produce an accurate accounting record showing how much *client money* is being held by third parties at any point in time. For the purposes of *CASS 5.5.63R* to *CASS 5.5.65R*, however, a *firm* must assume that *monies* remain at an intermediate broker awaiting completion of the transaction unless it has received confirmation that the transaction has been completed.

- 5.5.82 R When a *firm* draws a cheque or other payable order to discharge its fiduciary duty under *CASS 5.5.80R*, it must continue to treat the sum concerned as *client money* until the cheque or order is presented and paid by the bank.
- 5.5.83 R For the purposes of *CASS 5.1.5R*, if a *firm* makes a payment to, or on the instructions of, a *client*, from an account other than a *client bank account*, until that payment has cleared, no equivalent sum will become due and payable to the *firm* or may be withdrawn from a *client bank account* by way of reimbursement.

#### Records

- 5.5.84 R A *firm* must ensure that proper records, sufficient to show and explain the *firm's* transactions and commitments in respect of its *client money*, are made and retained for a period of three years after they were made.

#### 5.6 Client money distribution

##### Application

- 5.6.1 R (1) *CASS 5.6* (the *client money (insurance) distribution rules*) applies to a *firm* that in holding *client money* is subject to *CASS 5.3* (statutory trust) or *CASS 5.4* (Non-statutory trust) when a *primary pooling event* or a *secondary pooling event* occurs.
- (2) In the event of there being any discrepancy between the terms of the trust as required by *CASS 5.4.7R* (1) (c) and the provisions of *CASS 5.6*, the latter shall apply.
- 5.6.2 G (1) The *client money (insurance) distribution rules* have force and effect on any *firm* that holds *client money* in accordance with *CASS 5.3* or *CASS 5.4*. Therefore, they may apply to a *UK branch* of a non-EEA *firm*. In this case, the *UK branch* of the *firm* may be treated as if the *branch* itself is a free-standing entity subject to the *client money (insurance) distribution rules*.
- (2) *Firms* that act in accordance with *CASS 5.4* (Non-statutory trust) are reminded that the *client money (insurance) distribution rules* should be given effect in the terms of trust required by *CASS 5.4*.

##### Purpose



- 5.6.3 G The *client money (insurance) distribution rules* seek to facilitate the timely return of *client money* to a *client* in the event of the *failure* of a *firm* or third party at which the *firm* holds *client money*.
- Failure of the authorised firm: primary pooling event
- 5.6.4 G A *primary pooling event* triggers a notional pooling of all the *client money*, in every type of *client money* account, and the obligation to distribute it.
- 5.6.5 R A *primary pooling event* occurs:
- (1) on the *failure* of the *firm*; or
  - (2) on the vesting of assets in a trustee in accordance with an 'assets requirement' imposed under section 48(1)(b) of the *Act*; or
  - (3) on the coming into force of a *requirement* for all *client money* held by the *firm*; or
  - (4) when the *firm* notifies, or is in breach of its duty to notify, the *FSA*, in accordance with *CASS 5.5.78R*, that it is unable correctly to identify and allocate in its records all valid claims arising as a result of a *secondary pooling event*.
- 5.6.6 R *CASS 5.6.5R* (4) does not apply so long as:
- (1) the *firm* is taking steps, in consultation with the *FSA*, to establish those records; and
  - (2) there are reasonable grounds to conclude that the records will be capable of rectification within a reasonable period.
- Pooling and distribution
- 5.6.7 R If a *primary pooling event* occurs:
- (1) *client money* held in each *client money* account of the *firm* is treated as pooled;
  - (2) the *firm* must distribute that *client money* in accordance with *CASS 5.3.2R* or, as appropriate, *CASS 5.4.7R*, so that each *client* receives a sum which is rateable to the *client money* entitlement calculated in accordance with *CASS 5.5.66R*; and
  - (3) the *firm* must, as trustee, call in and make demand in respect of any debt due to the *firm* as trustee, and must liquidate any *designated investment*, and any letter of credit or guarantee upon which it relies for meeting any *shortfall* in its *client money* resource and the proceeds shall be pooled together with other *client money* as in (1) and distributed in accordance with (2).

- 5.6.8 G A *client's* main claim is for the return of *client money* held in a *client bank account*. A *client* may claim for any *shortfall* against *money* held in a *firm's* own account. For that claim, the *client* will be an unsecured creditor of the *firm*.
- Client money received after the failure of the firm
- 5.6.9 R *Client money* received by the *firm* (including in its capacity as trustee under CASS 5.4 (Non-statutory trust)) after a *primary pooling event* must not be pooled with *client money* held in any *client money* account operated by the *firm* at the time of the *primary pooling event*. It must be placed in a *client bank account* that has been opened after that event and must be handled in accordance with the *client money rules*, and returned to the relevant *client* without delay, except to the extent that:
- (1) it is *client money* relating to a transaction that has not completed at the time of the *primary pooling event*; or
  - (2) it is *money* relating to a *client*, for whom the *client money* entitlement, calculated in accordance with CASS 5.5.66R, shows that *money* is due from the *client* to the *firm* including in its capacity as trustee under CASS 5.4 (Non-statutory trust) at the time of the *primary pooling event*.
- 5.6.10 G *Client money* received after the *primary pooling event* relating to an incomplete transaction should be used to complete that transaction.
- 5.6.11 R If a *firm* receives a *mixed remittance* after a *primary pooling event*, it must:
- (1) pay the full sum into the separate *client bank account* opened in accordance with CASS 5.6.9R; and
  - (2) pay the *money* that is not *client money* out of that *client bank account* into the *firm's* own bank account within one *business day* of the *day* on which the remittance is cleared.
- 5.6.12 G Whenever possible the *firm* should seek to split a *mixed remittance* before the relevant accounts are credited.
- Failure of a bank, other broker or settlement agent: secondary pooling events
- 5.6.13 R If both a *primary pooling event* and a *secondary pooling event* occur, the provisions of this section relating to a *primary pooling event* apply.
- 5.6.14 R A *secondary pooling event* occurs on the *failure* of a third party to which *client money* held by the *firm* has been transferred under CASS 5.5.34R.

5.6.15 R CASS 5.6.20R to CASS 5.6.31R do not apply if, on the *failure* of the third party, the *firm* repays to its *clients* or pays into a *client bank account*, at an unaffected bank, an amount equal to the amount of *client money* which would have been held if a *shortfall* had not occurred at that third party.

5.6.16 G When *client money* is transferred to a third party, a *firm* continues to owe a fiduciary duty to the *client*. However, consistent with a fiduciary's responsibility (whether as agent or trustee) for third parties under general law, a *firm* will not be held responsible for a *shortfall* in *client money* caused by a third party *failure* if it has complied with those duties.

5.6.17 G To comply with its duties, the *firm* should show proper care:

- (1) in the selection of a third party; and
- (2) when monitoring the performance of the third party.

In the case of *client money* transferred to a bank, by demonstrating compliance with CASS 5.5.43R, a *firm* should be able to demonstrate that it has taken reasonable steps to comply with its duties.

Failure of a bank

5.6.18 G When a bank *fails* and the *firm* decides not to make good the *shortfall* in the amount of *client money* held at that bank, a *secondary pooling event* will occur in accordance with CASS 5.6.20R. The *firm* would be expected to reflect the *shortfall* that arises at the *firm's* bank in the periodic *client money* calculation by reducing the *client money* resource and *client money* requirement accordingly.

5.6.19 G The *client money (insurance) distribution rules* seek to ensure that *clients* who have previously specified that they are not willing to accept the risk of the bank that has *failed*, and who therefore requested that their *client money* be placed in a *designated client bank account* as a different bank, should not suffer the loss of the bank that has *failed*.

Failure of a bank: pooling

5.6.20 R If a *secondary pooling event* occurs as a result of the *failure* of a bank where one or more *general client bank accounts* are held, then:

- (1) in relation to every *general client bank account* of the *firm*, the provisions of CASS 5.6.22R and CASS 5.6.26R to CASS 5.6.28G will apply;
- (2) in relation to every *designated client bank account* held by the *firm* with the *failed* bank, the provisions of CASS 5.6.24R and CASS 5.6.26R to CASS 5.6.28G will apply; and
- (3) any *money* held at a bank, other than the bank that has *failed*, in *designated client bank accounts* is not pooled with any other *client money*.

- 5.6.21 R If a *secondary pooling event* occurs as a result of the *failure* of a bank where one or more *designated client bank accounts* are held then in relation to every *designated client bank account* held by the *firm* with the *failed* bank, the provisions of CASS 5.6.24R and CASS 5.6.26R to CASS 5.6.28G will apply.
- 5.6.22 R Money held in each *general client bank account* of the *firm* must be treated as pooled and:
- (1) any *shortfall* in *client money* held, or which should have been held, in *general client bank accounts*, that has arisen as a result of the *failure* of the bank, must be borne by all the *clients* whose *client money* is held in a *general client bank account* of the *firm*, rateably in accordance with their entitlements;
  - (2) a new *client money* entitlement must be calculated for each *client* by the *firm*, to reflect the requirements in (1), and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
  - (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* bank until the *client* is repaid; and
  - (4) the *firm* must use the new *client* entitlements, calculated in accordance with (2), when performing the *client money* calculation in accordance with CASS 5.5.63R to CASS 5.5.75R.
- 5.6.23 G The term 'which should have been held' is a reference to the *failed* bank's failure (and elsewhere, as appropriate, is a reference to the other *failed* third party's failure) to hold the *client money* at the time of the pooling event.
- 5.6.24 R For each *client* with a *designated client bank account* held at the *failed* bank:
- (1) any *shortfall* in *client money* held, or which should have been held, in *designated client bank accounts* that has arisen as a result of the *failure*, must be borne by all the *clients* whose *client money* is held in a *designated client bank account* of the *firm* at the *failed* bank, rateably in accordance with their entitlements;
  - (2) a new *client money* entitlement must be calculated for each of the relevant *clients* by the *firm*, and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
  - (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* bank until the *client* is repaid; and
  - (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), when performing the periodic *client money* calculation, in accordance with CASS 5.5.63R to CASS 5.5.75R.
- 5.6.25 R A *client* whose *money* was held, or which should have been held, in a *designated client bank account* with a bank that has *failed* is not entitled to claim in respect of that *money* against any other *client bank account* or *client transaction account* of the *firm*.

Client money received after the failure of a bank

- 5.6.26 R *Client money* received by the *firm* after the *failure* of a bank, that would otherwise have been paid into a *client bank account* at that bank:
- (1) must not be transferred to the *failed* bank unless specifically instructed by the *client* in order to settle an obligation of that *client* to the *failed* bank; and
  - (2) must be, subject to (1), placed in a separate *client bank account* that has been opened after the *secondary pooling event* and either:
    - (a) on the written instruction of the *client*, transferred to a bank other than the one that has *failed*; or
    - (b) returned to the *client* as soon as possible.
- 5.6.27 R If a *firm* receives a *mixed remittance* after the *secondary pooling event* which consists of *client money* that would have been paid into a *general client bank account*, a *designated client bank account* or a *designated client fund account* maintained at the bank that has *failed*, it must:
- (1) pay the full sum into a *client bank account* other than one operated at the bank that has *failed*; and
  - (2) pay the *money* that is not *client money* out of that *client bank account* within one *business day* of the day on which the remittance is cleared.
- 5.6.28 G Whenever possible the *firm* should seek to split a *mixed remittance* before the relevant accounts are credited.
- Failure of an intermediate broker or settlement agent: pooling
- 5.6.29 R If a *secondary pooling event* occurs as a result of the *failure* of another broker or *settlement agent* to whom the *firm* has transferred *client's money* then, in relation to every *general client bank account* of the *firm*, the provisions of CASS 5.6.26R to CASS 5.6.28G and CASS 5.6.30R will apply.
- 5.6.30 R *Money* held in each *general client bank account* of the *firm* must be treated as pooled and:
- (1) any *shortfall* in *client money* held, or which should have been held, in *general client bank accounts*, that has arisen as a result of the *failure*, must be borne by all the *clients* whose *client money* is held in a *general client bank account* of the *firm*, rateably in accordance with their entitlements;
  - (2) a new *client money* entitlement must be calculated for each *client* by the *firm*, to reflect the requirements of (1), and the *firm's* records must be amended to reflect the reduced *client money* entitlement;

- (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* intermediate broker or *settlement agent* until the *client* is repaid; and
- (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), when performing the periodic *client money* calculation, in accordance with CASS 5.5.63R to CASS 5.5.75R.

Client money received after the failure of a broker or settlement agent

- 5.6.31 R *Client money* received by the *firm* after the *failure* of another broker or *settlement agent*, to whom the *firm* has transferred *client money* that would otherwise have been paid into a *client bank account* at that broker or *settlement agent*:
- (1) must not be transferred to the *failed* third party unless specifically instructed by the *client* in order to settle an obligation of that *client* to the *failed* broker or *settlement agent*; and
  - (2) must be, subject to (1), placed in a separate *client bank account* that has been opened after the *secondary pooling event* and either:
    - (a) on the written instruction of the *client*, transferred to a third party other than the one that has *failed*; or
    - (b) returned to the *client* as soon as possible.

Notification on the failure of a bank, other broker or settlement agent

- 5.6.32 R The provisions of CASS 5.5.61R apply.

5.7 Mandates

Application

- 5.7.1 R This section applies to a *firm* (including in its capacity as trustee under CASS 5.4) in respect of any written authority from a *client* under which the *firm* may control a *client's assets* or liabilities in the course of, or in connection with, the *firm's insurance mediation activity*.
- 5.7.2 R CASS 5.7 does not apply to a *firm* when:
- (1) it is carrying on an *insurance mediation activity* which is in respect of a *reinsurance contract*; or
  - (2) it acts in accordance with CASS 4.
- 5.7.3 G Mandates or similar authorities for the purpose of CASS 5.7.1 R include a *firm's* authority over a *client's* bank or *building society* account including direct debits in favour of the *firm*, and a *firm* holding a *client's* credit card details.

5.7.4 G *Firms* are reminded that the *mandate rules* do not apply to an *incoming EEA firm* with respect to its *passport activities*. The application of the *mandate rules* is also dependent on the location from which the activity is undertaken.

Purpose

5.7.5 G The *mandate rules* apply to those *firms* that control, rather than hold, *clients'* assets or are able to create liabilities in the name of a *client*. These *rules* seek to ensure that *firms* establish and maintain records and *internal controls* to prevent the misuse of the authority granted by the *client*.

General

5.7.6 R A *firm* that holds authorities of the sort referred to in CASS 5.7.1R must establish and maintain adequate records and *internal controls* in respect of its use of the mandates, which must include:

- (1) an up-to date list of the authorities and any conditions placed by the *client* or the *firm's* management on the use of them;
- (2) a record of all transactions entered into using the authority and *internal controls* to ensure that they are within the scope of authority of the *person* and the *firm* entering into the transaction;
- (3) the details of the procedures and authorities for the giving and receiving of instructions under the authority; and
- (4) where the *firm* holds a passbook or similar *documents* belonging to the *client*, *internal controls*, for the safeguarding (including against loss, unauthorised destruction, theft, fraud or misuse) of any passbook or similar *document* belonging to the *client* held by the *firm*.

Safe keeping of client's documents and other assets

Application

- 5.8.1 R
- (1) CASS 5.8 applies to a *firm* (including in its capacity as trustee under CASS 5.4) which in the course of *insurance mediation activity* takes into its possession for safekeeping any *client title documents* (other than *documents* of no value) or other tangible assets belonging to *clients*.
  - (2) CASS 5.8 does not apply to a *firm* when:
    - (a) carrying on an *insurance mediation activity* which is in respect of a *reinsurance contract*; or
    - (b) acting in accordance with CASS 2 (Custody rules).

Purpose

- 5.8.2 G The *rules* in this section amplify the obligation in *Principle 10* which requires a *firm* to arrange adequate protection for *client's* assets. *Firms* carrying on *insurance mediation activities* may hold, on a temporary or longer basis, *client title documents* such as *policy documents* (other than *policy documents* of no value) and also items of physical property if, for example, a *firm* arranges for a valuation. The *rules* are intended to ensure that *firms* make adequate arrangements for the safe keeping of such property.

Requirement

- 5.8.3 R (1) A *firm* which has in its possession or control *documents* evidencing a *client's* title to a *contract of insurance* or other similar *documents* (other than *documents* of no value) or which takes into its possession or control tangible assets belonging to a *client*, must take reasonable steps to ensure that any such *documents* or items of property:
- (a) are kept safe until they are delivered to the *client*;
  - (b) are not delivered or given to any other *person* except in accordance with instructions given by the *client*; and that a record is kept as to the identity of any such *documents* or items of property and the dates on which they were received by the *firm* and delivered to the *client* or other *person*.
- (2) A *firm* must retain the record required in (1) for a period of three years after the document or property concerned is delivered to the *client* or other *person*.

CASS 5

Annex 1R

This Annex belongs to CASS 5.5.14R.

1. The general principles which must be followed when *client money* segregation includes *designated investments*:
- (a) there must be a suitable spread of *investments*;
  - (b) *investments* must be made in accordance with an appropriate liquidity strategy;
  - (c) the *investments* must be in accordance with an appropriate credit risk policy;
  - (d) any foreign exchange risks must be prudently managed.



2. Table of permitted designated investments for the purpose of CASS 5.5.14R (1).

Investment type	Qualification
1. Negotiable <i>debt security</i> (including a certificate of deposit)	(a) Remaining term to maturity of 5 years or less; and (b) The issuer or <i>investment</i> must have a short-term credit rating of A1 by Standard and Poor's, or P1 by Moody's Investor Services, or F1 by Fitch if the instrument has a remaining term to maturity of 366 days or less; or a minimum long term credit rating of AA- by Standards and Poor's, or Aa3 by Moody's Investor Services or AA- by Fitch if the instrument has a term to maturity of more than 366 days.
2. A <i>repo</i> in relation to negotiable <i>debt security</i>	As for 1 above and where the credit rating of the counterparty also meets the criteria in 1.
3. Bond funds	(a) An <i>authorised fund</i> or a <i>recognised scheme</i> or an investment company which is registered by the Securities and Exchanges Commission of the United States of America under the Investment Company Act 1940; (b) A minimum credit rating and risk rating of Aaf and S2 respectively by Standard and Poor's or Aa and MR2 respectively by Moody's Investor Services or AA and V2 respectively by Fitch.
4. Money market fund	(a) An <i>authorised fund</i> or a <i>recognised scheme</i> ; (b) A minimum credit and risk rating of Aaa and MR1+ respectively by Moody's Investor Services or AAAm by Standard and Poor's or AAA and V1+ respectively by Fitch.
5. <i>Derivatives</i>	Only for the purpose of prudently managing foreign currency risks.

3. The general conditions which must be satisfied in the segregation of *designated investments* are:

- (a) any redemption of an *investment* must be by payment into the *firm's client money bank account*;
- (b) where the credit or risk rating of a *designated investment* falls below the minimum set out in the Table, the *firm* must dispose of the *investment* as soon as possible and in any even not later than 20 *business days* following the downgrade;
- (c) where any *investment* or issuer has more than one rating, the lowest shall apply.

...

Schedule 1  
Record keeping requirements

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...

3 Table

Handbook Reference	Subject of Record	Contents of Record	When record must be made	Retention period
<u>CASS 4.5.5R</u>	...	...	...	
<u>CASS 5.1.1R(4)</u>	<u>Record of election of compliance with CASS 5.1 to 5.6 provisions</u>	<u>Record of compliance with CASS 5.1 to 5.6 provisions on client money</u>	<u>Not specified</u>	<u>Not specified</u>
<u>CASS 5.2.3R(2)</u>	<u>Holding client money as agent</u>	<u>The terms of the agreement</u>	<u>Not specified</u>	<u>Six years</u>
<u>CASS 5.4.4R(2)</u>	<u>Adequacy of systems and controls</u>	<u>Written confirmation of adequate systems and controls from its auditor</u>	<u>Not specified</u>	<u>Not specified</u>
<u>CASS 5.5.64R</u>	<u>Client money calculation</u>	<u>Whether the firm calculates its client money requirements according to CASS 5.5.67R or CASS 5.5.68R</u>	<u>Not specified</u>	<u>Not specified</u>
<u>CASS 5.5.84R</u>	<u>Transactions and commitments for client money</u>	<u>Explanation of the firm's transactions and commitments for client money.</u>	<u>Not specified</u>	<u>Three years</u>
<u>CASS 5.7.6R</u>	<u>Mandates</u>	<u>Records of adequate</u>	<u>Not specified</u>	<u>Not specified</u>

		<u>internal controls for mandates</u>		
<u>CASS 5.8.3R(1)</u>	<u>Client's title to a contract of insurance</u>	<u>Identity of such documents and/or property and dates received and delivered to client</u>	<u>Not specified</u>	<u>Three years</u>

...

Schedule 2  
Notification requirements

G

...

3 Table

Handbook Reference	Matter to be Notified	Contents of Notification	Trigger event	Time allowed
<u>CASS 4.4.33R</u>	...	...	...	
<u>CASS 5.5.61R</u>	<u>Failure of bank, broker or settlement agent</u>	<u>Full details including whether it intends to make good any shortfall that may have arisen in the amounts involved</u>	<u>As soon as the firm becomes aware</u>	<u>Immediately</u>
<u>CASS 5.5.76R</u>	<u>Inability to perform the calculation required by CASS 5.5.63R</u>	<u>Inability to perform the calculation</u>	<u>Inability to perform the calculation</u>	<u>Immediately</u>
<u>CASS 5.5.77R</u>	<u>Inability to make good any shortfall identified by CASS 5.5.63R</u>	<u>Inability to make good any shortfall in client money</u>	<u>Inability to make good any shortfall</u>	<u>Immediately</u>
<u>CASS 5.5.78</u>	<u>Inability to comply with</u>	<u>Inability to comply with</u>	<u>Inability to comply with</u>	<u>As soon as reasonably</u>

Handbook Reference	Matter to be Notified	Contents of Notification	Trigger event	Time allowed
	<u>the requirements in CASS 5.5.70R;</u> <u>CASS 5.5.72R;</u> <u>CASS 5.5.73R;</u> <u>CASS 5.5.74R;</u> <u>CASS 5.5.75R</u>	<u>the requirements of the rules listed</u>	<u>the requirements of the rules listed</u>	<u>practical</u>

## Annex D

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

2.3.2 G There is power in the *Act* for the Treasury to change the meaning of the business element by including or excluding certain things. They have exercised this power (see the Financial Services and Markets Act 2000 (Carrying on Regulated Activities by Way of Business) Order 2001 SI No 1177 and the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003 SI No 1476). The result is that the business element differs depending on the activity in question.

...

(2) ~~Except for the trustees of *occupational pension schemes* (for which special provision is made (see *AUTH 2.3.2(3)G*)), as stated in *AUTH 2.3.2 G(2A)* and (3), the business element is not to be regarded as satisfied for any of the *regulated activities* carried on in relation to *securities* or *contractually based investments* (or for those *regulated activities* carried on in relation to 'any property') unless a *person* carries on the business of engaging in one or more of the activities. This also applies to the *regulated activities of arranging in relation to a regulated mortgage contract and advising on regulated mortgage contracts*. This is a narrower test than that of carrying on *regulated activities* by way of business (as required by section 22 of the *Act*), as it requires the *regulated activities* to represent the carrying on of a business in their own right.~~

(2A) A *person* who carries on an *insurance mediation activity* will not be regarded as doing so by way of business unless he takes up or pursues that activity for remuneration. *AUTH 2.3.3G* gives *guidance* on the factors that are relevant to the meaning of 'by way of business' in section 22 of the *Act*. *AUTH App 5.4* (The business test) gives further *guidance* on the business element as applied to *insurance mediation activities*.

...

(4) The business element for all other *regulated activities* is that the activities are carried on by way of business. This applies to the activities of *effecting or carrying out contracts of insurance*, certain activities relating to the Lloyd's market, ~~entering as provider into a funeral plan contract~~ entering as provider into a funeral plan contract and ~~activities relating to entering into or administering regulated mortgage contracts~~ regulated mortgage contracts (see *AUTH 2.7.20G*).

...

...

Modification of certain exclusions as a result of Investment Services and Insurance Mediation Directives

- 2.5.3 G The application of certain of the exclusions considered in *AUTH 2.8 (Exclusions applicable to certain regulated activities)* and *AUTH 2.9 (Regulated activities: exclusions applicable to certain circumstances)* is modified in relation to *persons* who are subject to the *Investment Services Directive* or the *Insurance Mediation Directive*. The reasons for this and the consequences of it are explained in *AUTH 2.5.4G*, as respects the *Investment Services Directive*, and *AUTH App 5 (Insurance mediation activities)*, as respects the *Insurance Mediation Directive*.

Investment services

- 2.5.4 G ...

Insurance mediation or reinsurance mediation

- 2.5.6 G The *Insurance Mediation Directive* has in part been implemented through various amendments to the *Regulated Activities Order*. These include article 4(4A) (Specified activities: general) which precludes a *person* who, for remuneration, takes up or pursues *insurance mediation or reinsurance mediation* in relation to a risk or commitment situated in an *EEA State* from making use of certain exclusions. In other cases, some of the exclusions provided in relation to particular *regulated activities* are unavailable where the activity involves a *contract of insurance*. This is explained in more detail in *AUTH App 5 (Insurance mediation activities)*.

...

- 2.6.7 G The *Regulated Activities Order* uses a two further terms in relation to ~~*long-term contracts of insurance contracts*~~ in order to identify those contracts under which rights are treated as *contractually based investments*.

(1) ~~These contracts are described as~~ The first term is ‘qualifying contracts of insurance’ (referred to as *life policies* in the *Handbook*). ~~in order to~~ This identifies those *long-term insurance contracts* under which rights are treated as *contractually based investments*. ~~These contracts are described as ‘qualifying contracts of insurance’ (referred to as *life policies* in the *Handbook*).~~ This term does not cover *long-term insurance contracts* which are contracts of reinsurance or, if specified conditions are met, contracts under which benefits are payable only on death or incapacity.

(2) The second term is ‘*relevant investments*’. This term applies to:

- (a) contractually based investments, which includes rights under life policies, and rights to or interests in such investments under article 89 of the Regulated Activities Order (Rights to or interests in investments); and
- (b) rights under contracts of insurance other than life policies (but not rights to or interests in such rights).

This term is used in connection with the treatment, under various parts of the Regulated Activities Order, of persons carrying on insurance mediation activities (see AUTH App 5 (Insurance mediation activities) for further guidance on such activities).

...

2.7.4 G In addition, certain other activities carried on in relation to rights under certain long-term contracts of insurance are regulated activities (see AUTH 2.7.5G to AUTH 2.7.10G, AUTH 2.7.15G and AUTH 2.7.16G). This is because such rights are classified as contractually based investments. These are where the activity is carried on in relation to:

- (1) life policies, where the regulated activities concerned are:
  - (a) dealing in investments as principal (see AUTH 2.7.5G);
  - (b) managing investments (see AUTH 2.7.8G);
  - (b) safeguarding and administering investments (see AUTH 2.7.9G); and
  - (c) agreeing to carry on any of those activities (see AUTH 2.7.21G); and
- (2) rights under any contract of insurance, where the regulated activities concerned are:
  - (a) dealing in investments as agent (see AUTH 2.7.5G);
  - (b) arranging (bringing about) deals in investments and making arrangements with a view to transactions in investments (see AUTH 2.7.7G);
  - (c) assisting in the administration and performance of a contract of insurance (see AUTH 2.7.7G);
  - (d) advising on investments (see AUTH 2.7.15G); and
  - (e) agreeing to carry on any of those activities (see AUTH 2.7.21G).

AUTH APP 5 (Insurance mediation activities) has more guidance on these regulated activities where they are insurance mediation activities.

...

2.7.6 G Both the activities of *dealing in investments as principal* and *dealing in investments as agent* are defined in terms of ‘*buying, selling, subscribing for or underwriting*’ certain investments. These *investments* are:

- (1) for dealing in investments as principal, securities or contractually based investments (except rights under a funeral plan contract);  
and
- (2) for dealing in investments as agent, securities and relevant investments (except rights under a funeral plan contract).

2.7.6A G Because of the different nature of the *specified investments* ...

Arranging deals in investments and arranging regulated mortgage activities

2.7.7 G ~~[deleted]Arranging applies to arrangements that relate to securities, contractually based investments and the underwriting capacity of a Lloyd’s syndicate capacity or membership of a Lloyd’s syndicate. Arrangements relating to rights to or interests in any of these specified investments are also caught. Arranging is made up of two distinct regulated activities. Both are aimed at the person who agrees with another person that he will procure a third person to buy, sell, subscribe for or underwrite the relevant specified investments.~~

- (1) ~~The first activity is “making arrangements for another person to buy, sell, subscribe for or underwrite a particular investment”. This activity is referred to in the Handbook as arranging (bringing about) deals in investments. It is aimed at arrangements that would have the direct effect that a transaction is concluded (that is, arrangements that bring it about).~~
- (2) ~~The second activity is “making arrangements with a view to a person who participates in the arrangements buying, selling, subscribing for or underwriting investments”. This activity is referred to in the Handbook as making arrangements with a view to transactions in investments. It is aimed at cases where it may be said that the transaction is “brought about” directly by the parties to it but where this happens in a context set up by a third party specifically with a view to the conclusion by others of transactions through the use of that third party’s facilities. This will catch the activities of persons such as exchanges, clearing houses and service companies (for example, persons who provide communication facilities for the routing of orders or the negotiation of transactions). A person may be carrying on this regulated activity even if he is only providing part of the facilities necessary before a transaction is brought about.~~



2.7.7A G ~~The Treasury has announced that it intends to bring within the scope of *regulated activities* the arranging of deals in *regulated mortgage contracts*. It has also announced that it intends to regulate the activities of insurance intermediaries. (The activity of arranging deals in *contracts of insurance* that are *contractually based investments* is already a *regulated activity* under article 25 of the *Regulated Activities Order*). These changes re expected to take effect in 2004. There are four arranging activities that are *regulated activities* under the *Regulated Activities Order*. These are:~~

- (1) *arranging (bringing about) deals in investments which are securities, relevant investments or the underwriting capacity of a Lloyd's syndicate or membership of a Lloyd's syndicate (article 25(1));*
- (2) *making arrangements with a view to transactions in investments which are securities, relevant investments or the underwriting capacity of a Lloyd's syndicate or membership of a Lloyd's syndicate (article 25(2));*
- (3) *arranging (bringing about) regulated mortgage contracts, which includes arranging for another person to vary the terms of a regulated mortgage contract entered into before 31 October 2004 (article 25A(1)); and*
- (4) *making arrangements with a view to regulated mortgage contracts (article 25A(2)).*

2.7.7B G The activity of *arranging (bringing about) deals in investments* is aimed at *arrangements* that would have the direct effect that a particular *transaction* is concluded (that is, *arrangements* that bring it about). The activity of *making arrangements with a view to transactions in investments* is aimed at cases where it may be said that the *transaction* is “brought about” directly by the parties. This is where this happens in a context set up by a third party specifically with a view to the conclusion by others of *transactions* through the use of that third party's *facilities*. This will catch the activities of *persons* such as exchanges, *clearing houses* and *service companies* (for example, *persons* who provide communication facilities for the routing of orders or the negotiation of *transactions*). A *person* may be carrying on this *regulated activity* even if he is only providing part of the *facilities* necessary before a *transaction* is brought about.

2.7.7C G Further guidance on the arranging activities as they relate to regulated mortgage contracts and contracts of insurance is in AUTH App 4.5 (Arranging regulated mortgage contracts) and AUTH App 5.6 (The regulated activities: arranging deals in, and making arrangements with a view to transactions in, contracts of insurance) respectively.

Assisting in the administration and performance of a contract of insurance

2.7.8A G The activity of assisting in the administration and performance of a contract of insurance is a regulated activity that is identified in the Insurance Mediation Directive. Further guidance on this activity is in AUTH App 5.7 (The regulated activities: assisting in the administration and performance of a contract of insurance)

...

2.7.15 G The regulated activity activity of advising on investments falls to be regulated only if it under article 53 of the *Regulated Activities Order* applies to advice on securities or contractually based investments – relevant investments. It does not, for example, include giving advice about deposits, rights under a general insurance contract or rights under a regulated mortgage contract or about things that are not specified investments for the purposes of the *Regulated Activities Order* (such as interests under the trusts of an *occupational pension scheme*). Giving advice on certain other specified investments is, however, regulated under other parts of the Regulated Activities Order (see AUTH 2.7.16AG and AUTH 2.7.17G(2)). Giving a person generic advice ...

2.7.16 G The advice must also be given to someone who holds specified investments or is a prospective investor (including trustees, nominees or discretionary fund managers). This requirement excludes advice given to a person who receives it in another capacity. An example of this might be a tax professional to whom advice is given to inform the practice of his profession or advice given to an employer for the purposes of setting up a group personal pension scheme. Further guidance on the meaning of advising on investments is in AUTH App 1.24 (Advising on investments).

2.7.16A G ~~[deleted] The Treasury has announced that it intends to bring within the scope of regulated activities advising a borrower on the merits of his entering into or varying the terms of a regulated mortgage contract. It has also announced that it intends to regulate the sale of insurance by insurance intermediaries. (Advising on contracts of insurance that are contractually based investments is already a regulated activity under article 53 of the Regulated Activities Order). These changes are expected to take effect in 2004.~~

Advising on regulated mortgages contracts

2.7.16B G Under article 53A of the Regulated Activities Order, giving advice to a person in his capacity as borrower or potential borrower is a regulated activity if it is advice on the merits of the person:

- (1) entering into a particular *regulated mortgage contract*; or
- (2) varying the terms of a *regulated mortgage contract*.

Advice on varying terms as referred to in (2) comes within article 53A only where the borrower entered into the *regulated mortgage contract* on or after 31 October 2004 and the variation varies the borrower's obligations under the contract. Further *guidance* on the scope of the *regulated activity* under article 53A is in *AUTH* App 4.6 (Advising on regulated mortgage contracts).

...

Activities in respect of Entering into and administering a regulated mortgage contracts

2.7.20 G ~~Entering into *Entering into* as lender, and administering a regulated mortgage contract- *administering, a regulated mortgage contract* will become are regulated activities under article 61 of the *Regulated Activities Order* (Regulated mortgage contracts) from a future date. The Treasury has announced that it expects this date to be in 2004. *Guidance* on these *regulated activities* is in *AUTH* App 4.7 (Entering into a regulated mortgage contract) and *AUTH* App 4.8 (Administering a regulated mortgage contract). These activities have not been included in Table 1 of *AUTH* 2 Ann 2G.~~

...

2.8.4 G

...

2.8.4A G *Persons* who enter as principal into transactions involving rights under a *contract of insurance* of any kind will need to consider whether they may, as a result, be carrying on the *regulated activity* of:

- (1) *arranging (bringing about) deals in investments*; or
- (2) *making arrangements with a view to transactions in investments*; or
- (3) agreeing to do (1) or (2).

2.8.4B G The possibility referred to in *AUTH* 2.8.4A G will only arise where it is not the case that the *person* who enters into the transaction as principal either:

- (1) is the only *policyholder*; or
- (2) as a result of the transaction, would become the only *policyholder*.

2.8.5 G The *regulated activity* of *dealing in investments as agent* applies to specified transactions relating to any *security* or to any ~~*contractually based investment*~~ *relevant investment* (apart from rights under *funeral plan contracts* or rights to or interests in such contracts). In addition, the activity is cut back by exclusions as follows.

(1) An exclusion applies to certain transactions entered into by an agent who is not an *authorised person* which depend on him dealing with (or through) an *authorised person*. It does not apply if the transaction relates to a *contract of insurance*. There are certain conditions which must be satisfied for the exclusion ...

...

(3) In addition, exclusions apply in specified circumstances (outlined in *AUTH 2.9 (Regulated activities: exclusions available in certain circumstances)*) where a *person* enters as agent into a transaction:

- (a) in connection with the carrying on of a profession or of a business not otherwise consisting of *regulated activities* (see *AUTH 2.9.5G*);
- (b) in connection with the sale of goods or supply of services (see *AUTH 2.9.7G*);
- (c) that takes place between members of a *group* or *joint enterprise* (see *AUTH 2.9.9G*);
- (d) in connection with the sale of a *body corporate* (see *AUTH 2.9.11G*);
- (e) in connection with an employee share scheme (see *AUTH 2.9.13G*);
- (f) as an *overseas person* (see *AUTH 2.9.15G*);
- (g) as an *incoming ECA provider* (see *AUTH 2.9.18G*);
- (h) as a provider of non-motor goods or travel services where the transaction involves a *general insurance contract* that satisfies certain conditions (see *AUTH 2.9.19G*);
- (i) that involves a *contract of insurance* covering large risks situated outside the *EEA* (see *AUTH 2.9.19G*).

More detailed guidance on the exclusions that relate to *contracts of insurance* is in *AUTH App 5 (Insurance mediation activities)*.

#### Arranging deals in investments and arranging regulated mortgage contracts

2.8.6 G The exclusions in relation to the *regulated activities* of arranging are of particular relevance in the context of raising corporate finance. Many of the exclusions outlined below relate to both the elements of the activity; that is, *arranging (bringing about) deals in investments* (under article 25(1) of the *Regulated Activities Order*) and *making arrangements with a view to transactions in investments* (under article 25(2) of the *Regulated Activities Order*). But several exclusions relate only to one of those activities.

- (1) Under article 26, a~~Arrangements~~ that do not or would not bring about the ~~investment~~ transaction to which they relate are excluded from article 25(1) and article 25A(1) only. A *person* will .....
- (2) Under article 27, sSimply providing the means by which parties to a transaction (or possible transaction) are able to communicate with each other are excluded from article 25(2) and article 25A(2) only. This will ensure .....
- (3) Under article 28, a~~Arranging~~ investment transactions to which the *arranger* is to be a party ..... arranging *deals* for another as regards any particular transaction. But where the transaction involves a *contract of insurance*, article 28 will not apply if the *person making the arrangements*:
  - (a) is the only *policyholder*; or
  - (b) as a result of the transaction, would become the only *policyholder*.

Under article 28A, a *person* is excluded from article 25A(1) and (2) if he is to enter into the contract to which the arrangements relate. The article also excludes from article 25A(1) a *person* who arranges a variation to a contract to which he is or is to become a party.

- (4) Under article 29, an ~~An unauthorised~~ *unauthorised person* who arranges investment transactions, with a view to a transaction between a third party and an *authorised person*, is excluded from article 25(1) and (2) and article 25A(1) and (2) if... unauthorised *unauthorised person* making the arrangements. The exclusion does not apply where the *investment* is a *contract of insurance*.
- (5) Under article 29A, an *unauthorised person* is excluded from the regulated activity of arranging for another *person* to vary the terms of a *regulated mortgage contract* entered into after 31 October 2004 (article 25A(1)(b)). This is if the arranging is the result of:
  - (1) anything done in the course of the administration of a *regulated mortgage contract* by an *authorised person* under article 62(a); or
  - (2) anything done by the *person making the arrangements* in connection with the administration of a *regulated mortgage contract* under article 62(b).

- (5) (6) Under article 30, a~~A~~rranging investment transactions in connection with lending on the security of ~~insurance policies~~ contracts of insurance is excluded, ~~in specified circumstances,~~ from article 25(1) and (2) but only where a person is not carrying on insurance mediation or reinsurance mediation.
- (6) (7) Under article 31, m~~M~~aking arrangements for finance (in whatever form) to be supplied .....
- (7) (8) Under article 32, a~~A~~rrangements the only purpose of which is .....
- (8) (9) Under article 33, m~~M~~aking arrangements under which *clients* will be introduced to third parties who will provide independent services (consisting of *advice* or the exercise of discretion in relation to certain investments) is excluded from article 25(2) and article 25(2A) only. The *person* to whom the introduction is made must be of a specified standing (including that of an *authorised person*). The exclusion does not apply where the arrangements relate to a contract of insurance.
- (10) Under article 33A, making arrangements for introducing persons to:
- (1) an authorised person who has permission to carry on certain regulated activities concerned with regulated mortgage contracts; or
- (2) an appointed representative who is able to carry on any of those activities without breaching the general prohibition; or
- (3) an overseas person who carries on any of those activities;
- is excluded from article 25A(2) subject to certain conditions related to the holding of client money and the disclosure of certain information.
- (9) (11) Under article 34, a~~A~~ company is not carrying on .....
- (10) (12) Under article 35, a~~A~~ body carrying out international securities business .....
- (11) (13) The following exclusions from both article 25(1) and (2) (outlined in *AUTH 2.9*) apply in specified circumstances where a *person* makes arrangements:
- (a) while acting as ~~trustee~~ trustee or personal representative (see *AUTH 2.9.3G*);

- (b) in connection with the carrying on of a profession or of a business not otherwise consisting of *regulated activities* (see *AUTH 2.9.5G*);
- (c) in connection with the sale of goods or supply of services (see *AUTH 2.9.7G*);
- (d) in connection with certain transactions by a *group* member or by a participator in a *joint enterprise* (see *AUTH 2.9.9G*);
- (e) in connection with the sale of a *body corporate* (see *AUTH 2.9.11G*);
- (f) in connection with an employee share scheme (see *AUTH 2.9.13G*);
- (g) as an *overseas person* (see *AUTH 2.9.15G*);
- (h) as an *incoming ECA provider* (see *AUTH 2.9.18G*);
- (i) as a provider of non-motor goods or services related to travel (see *AUTH 2.9.19G*);
- (j) involving the provision, on an incidental basis, of information to policyholders or potential policyholders about contracts of insurance (see *AUTH 2.9.19G*);
- (l) that involve a contract of insurance covering large risks situated outside the EEA (see *AUTH 2.9.19G*).

More detailed guidance on the exclusions that relate to contracts of insurance is in *AUTH App 5 (Insurance mediation activities)*.

2.8.7 G ...  
 The activities of *persons* appointed under a power of attorney are excluded, under article 38 of the *Regulated Activities Order*, from the *regulated activity of managing investments*, if specified conditions are satisfied. The exclusion only applies where a *person* is not carrying on *insurance mediation or reinsurance mediation*.

Assisting in the administration and performance of a contract of insurance

2.8.7A G *Assisting in the administration and performance of a contract of insurance is excluded under article 39B where it is carried on by a *person* acting in the capacity of:*

- (1) an expert appraiser; or
- (2) a loss adjuster acting for a relevant insurer; or
- (3) a claims manager acting for a relevant insurer.

The term 'relevant insurer' is defined in article 39B(2).

2.8.7B G The following exclusions from assisting in the administration and performance of a contract of insurance also apply to a person in specified circumstances:

- (1) while acting as trustee or personal representative (see AUTH 2.9.3G); or
- (2) in connection with the carrying on of a profession or of a business not otherwise consisting of regulated activities (see AUTH 2.9.5G); or
- (3) as an incoming ECA provider (see AUTH 2.9.18G); or
- (4) as a provider of non-motor goods or services related to travel (see AUTH 2.9.19G); or
- (5) that involve the provision, on an incidental basis, of information to policyholders or potential policyholders about contracts of insurance (see AUTH 2.9.19G(2)); or
- (6) that involve a contract of insurance covering large risks situated outside the EEA (see AUTH 2.9.19G).

...  
2.8.8 G The exclusions from the regulated activity of safeguarding and administering investments are as follows.

- ...
- (4) The following exclusions (~~outlined in AUTH 2.9~~) apply in specified circumstances where a person safeguards and administers assets (or arranges for another to do so):
    - (a) while acting as trustee or personal representative (see AUTH 2.9.3G);
    - (b) in connection with the carrying on of a profession or of a business not otherwise consisting of regulated activities (see AUTH 2.9.5G);
    - (c) in connection with the sale of goods or supply of services (see AUTH 2.9.7G);
    - (d) which belong to a group member or participator in a joint enterprise (see AUTH 2.9.9G);
    - (e) in connection with an employee share scheme (see AUTH 2.9.13G);
    - (f) as an incoming ECA provider (see AUTH 2.9.18G); and



(g) that are *contracts of insurance* and, in so doing, provides information to *policyholders* or potential *policyholders* on an incidental basis in the course of his carrying on a business or profession not otherwise consisting of *regulated activities* (see *AUTH 2.9.19G(2)*).

2.8.9 G Exclusions from the *regulated activity* of *sending dematerialised instructions* apply in relation to certain types of instructions sent in the operation of the system maintained under the Uncertificated Securities Regulations 2001. The various exclusions relate to the roles played by participating issuers, settlement *banks* and network providers (such as Internet service providers) and to instructions sent in connection with takeover offers (as long as specified conditions are met). In addition, the following exclusions (outlined in *AUTH 2.9G*) apply in specified circumstances where a *person* sends dematerialised instructions:

(1) while acting as trustee or personal representative (see *AUTH 2.9.3G*);

(2) on behalf of a *group* member (see *AUTH 2.9.3G*);

...

...

2.8.12 G In certain circumstances, advice that takes the form of a regularly updated news or information service and advice which is given in one of a range of different media (for example, newspaper or television) is excluded from the ~~regulated activity~~ *regulated activities* of *advising on investments* and *advising on regulated mortgage contracts* (see *AUTH 7 (Periodical publications: news services and broadcasts: applications for certification)*). Advice given in the course of the administration of a *regulated mortgage contract* by an *authorised person* is also excluded subject to certain conditions. In addition,:

(1) the following exclusions (~~outlined in *AUTH 2.9*~~) apply in specified circumstances where a *person* ~~gives advice~~ is *advising on investments* or *regulated mortgage contracts*:

(1a) while acting as trustee or personal representative (see *AUTH 2.9.3G*);

(2b) in connection with the carrying on of a profession or of a business not otherwise consisting of *regulated activities* (see *AUTH 2.9.5G*); and

(c) as an *incoming ECA provider* (see *AUTH 2.9.18G*);

(2) the following exclusions apply in specified circumstances where a *person* is *advising on investments*:

(3a) in connection with the sale of goods or supply of services (see *AUTH 2.9.7G*);

- (4b) to a *group* member or participator in a *joint enterprise* (see *AUTH 2.9.9G*);
- (5c) in connection with the sale of a *body corporate* (see *AUTH 2.9.11G*);
- (6d) as an *overseas person* (see *AUTH 2.9.15G*);
- (e) that are limited to certain *contracts of insurance* covering risks to non-motor goods or related to travel (see *AUTH 2.9.19G*);
- (f) that are *contracts of insurance* covering large risks situated outside the *EEA* (see *AUTH 2.9.19G*).

More detailed *guidance* on certain of these exclusions is in *AUTH App 4 (Regulated activities connected with mortgages)* and *AUTH App 5 (Insurance mediation activities)*.

...

2.8.14G ...

Administering regulated mortgage contracts

2.8.14A G Exclusions from the *regulated activity* of *administering a regulated mortgage contract* are provided where *persons* arrange for administration by an *authorised person* and where *persons* administer under an agreement with an *authorised person*. These exclusions are subject to certain conditions and are explained in greater detail in *AUTH 4.8 (Administering a regulated mortgage contract)*.

...

2.9.1 G The various exclusions outlined below deal with a range of different circumstances.

- (1) Each set of circumstances described in *AUTH 2.9.3G* to *AUTH 2.9.17G* has some application to several *regulated activities* relating to ~~*securities, or contractually based investments*~~ *relevant investments* or *regulated mortgage contracts*. They have no effect in relation to the separate *regulated activities* of *accepting deposits, effecting or carrying out contracts of insurance, advising on syndicate participation at Lloyd's, managing the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's, or entering as provider into a funeral plan contract* ~~or any regulated activities relating to regulated mortgage contracts~~. Within each set of circumstances, the *Regulated Activities Order* ...

...

...

2.9.3 G This group of exclusions applies, in specified circumstances, to the *regulated activities* of:

- (1) *dealing in investments as principal;*
- (2) *arranging (bringing about) deals in investments, arranging (bringing about) regulated mortgage contracts, and making arrangements with a view to enabling or facilitating transactions in investments and making arrangements with a view to regulated mortgage contracts;*
- (3) *managing investments;*
- (4) *assisting in the administration and performance of a contract of insurance;*
- ~~(4)~~(5) *safeguarding and administering investments;*
- ~~(5)~~(6) *sending dematerialised instructions; and*
- ~~(6)~~(7) *advising on investments or regulated mortgage contracts;*
- (8) *entering into regulated mortgage contracts; and*
- (9) *administering regulated mortgage contracts.*

The exclusion is, however, disapplied where a person is carrying on insurance mediation or reinsurance mediation. This is due to article 4(4A) of the Regulated Activities Order. Guidance on exclusions relevant to insurance mediation activities is in AUTH App 5 (Insurance mediation activities).

2.9.4 G A person carrying on certain *regulated activities* does not require *authorisation* in specified circumstances if he is acting in a representative capacity. The representative capacities covered by the exclusions depend on the *regulated activity* concerned but, in most cases, the focus is on *persons* who are acting as trustee or personal representative. In broad terms, the exclusions apply to specified transactions, or activities, that are part of the discharge of his general obligations by the trustee or representative when he is acting as such. Many of the exclusions require that the trustee or representative must not hold himself out as providing services consisting of the *regulated activity* in question. In addition, he must not receive remuneration that is additional to any he receives for acting in the representative capacity (although a *person* is not to be regarded as receiving additional remuneration merely because his remuneration as trustee or representative is calculated by reference to time spent). The exclusions for entering into and for administering regulated mortgage contracts, however, work on a different basis. They apply where the activity relates to a regulated mortgage contract under which the borrower is a beneficiary.

...

2.9.5 G This group of exclusions applies, in specified circumstances, to the *regulated activities* of:

...

(2) *arranging (bringing about) deals in investments, arranging (bringing about) regulated mortgage contracts, and making arrangements with a view to enabling or facilitating transactions in investments and making arrangements with a view to regulated mortgage contracts*;

(3) *assisting in the administration and performance of a contract of insurance*;

~~(3)~~(4) *safeguarding and administering investments*; and

~~(4)~~(5) *advising on investments or regulated mortgage contracts*.

The exclusion is, however, disapplied where a person is carrying on insurance mediation or reinsurance mediation . This is due to article 4(4A) of the Regulated Activities Order. Guidance on exclusions relevant to insurance mediation activities is in AUTH App 5 (Insurance mediation activities).

...

2.9.7 G This group of exclusions applies, in specified circumstances, to the *regulated activities* of:

...

(3) *arranging (bringing about) deals in investments and making arrangements ~~enabling or facilitating~~ with a view to transactions in investments*;

...

2.9.8 G Broadly speaking, the exclusions focus on cases where the main business of a *person* is to sell goods or supply services but where certain activities may have to be carried on for the purposes of that business which would otherwise be *regulated activities*. The exclusions are not available where the customer to whom goods are sold or services are supplied is an individual. They are also not available where what is at issue is a transaction entered into, or service provided, in relation to rights under a ~~life policy~~ contract of insurance or units in a *collective investment scheme* ...

...

2.9.9 G This group of exclusions applies, in specified circumstances, to the *regulated activities* of:

...

(3) *arranging (bringing about) deals in investments and making arrangements ~~enabling or facilitating~~ with a view to transactions in investments*;

- ...
- 2.9.10 G These exclusions apply to intra-group dealings and activities and to dealings or activities involving participators in a *joint enterprise* which take place for the purposes of, or in connection with, the enterprise. The general principle here is that, as long as activities that would otherwise be *regulated activities* take place wholly within a *group* of companies, then there is no need for *authorisation*. The same principle applies to dealings or activities that take place wholly within a *joint enterprise* entered into for commercial purposes related to the participators' unregulated business. The exclusions in (2), (3), (4) and (7) are disappplied where they concern a *contract of insurance*. *Guidance on exclusions relevant to insurance mediation activities is in AUTH App 5 (Insurance mediation activities)*.
- 2.9.11 G This group of exclusions applies, in specified circumstances, to the *regulated activities* of:
- ...
- (3) *arranging (bringing about) deals in investments and making arrangements ~~enabling or facilitating~~ with a view to transactions in investments;*
- 2.9.12 G The exclusions only apply where the object of the transaction may reasonably be regarded as being the acquisition of day-to-day control of the affairs of a *body corporate*. Whether or not day-to-day control is at stake is a question of fact based on an objective test. The *Regulated Activities Order* contains a non-exhaustive list of circumstances in which the day-to-day control requirement will be regarded as satisfied. These include the case where it is the acquisition or disposal of at least 50 per cent of the voting shares in the *body corporate* that is at issue. Certain additional requirements must also be satisfied. These exclusions do not have effect in relation to *shares* in an *open-ended investment company*. The exclusions in (2), (3) and (4) are disappplied where they concern a *contract of insurance*. *Guidance on exclusions relevant to insurance mediation activities is in AUTH App 5 (Insurance mediation activities)*.
- 2.9.13 G This group of exclusions applies, in specified circumstance, to the *regulated activities* of:
- ...
- (3) *arranging (bringing about) deals in investments and making arrangements ~~enabling or facilitating~~ with a view to transactions in investments;*
- ...
- ...
- 2.9.15 G This group of exclusions applies, in specified circumstance, to the *regulated activities* of:
- ...

- (3) *arranging (bringing about) deals in investments, ~~and making arrangements enabling or facilitating with a view to transactions in investments, arranging (bringing about) regulated mortgage contracts and making arrangements with a view to regulated mortgage contracts;~~*
- (4) *advising on investments;*
- (5) *entering into regulated mortgage contracts;*
- ~~(5)~~ (6) *administering regulated mortgage contracts;*
- (7) *agreeing to carry on the regulated activities of managing investments, arranging (bringing about) deals in investments, making arrangements with a view to transactions in investments, safeguarding and administering investments or sending dematerialised instructions.*

...

2.9.17 G The exclusions are available, for regulated activities other than those that relate to regulated mortgage contracts, in the two broad cases set out below. For some of these regulated activities, the exclusions apply in each case. In others, they apply in only one:

...

2.9.17A G The exclusions for overseas persons who carry on certain regulated activities related to regulated mortgage contracts work in a different way. They depend on the residency of the borrower or borrowers. Guidance on these exclusions is in AUTH App 4.11 (Link between activities and the United Kingdom).

2.9.18 G ...

Insurance mediation activities

2.9.19 G The exclusions in this group apply to certain regulated activities involving certain contracts of insurance. The exclusions and the regulated activities to which they apply are as follows.

- (1) The first exclusion of this kind relates to certain activities carried on by a provider of non-motor goods or services related to travel in connection with general insurance contracts only. The contracts must be for five years duration or less and have an annual premium of no more than €500. The contract must cover breakdown or loss of or damage to non-motor goods supplied by the provider or risks linked to travel services booked with the provider. There must not be any liability risk cover. The insurance must be complementary to the goods or services being supplied by the provider in the course of his carrying on a business or profession not otherwise consisting of regulated activities. This exclusion applies where the regulated activities concerned are:

- (a) dealing in investments as agent;
  - (b) arranging (bringing about) deals in investments and making arrangements with a view to transactions in investments;
  - (c) assisting in the administration and performance of a contract of insurance; and
  - (d) advising on investments.
- (2) The second exclusion applies where information is provided to a policyholder by a person on an incidental basis in the course of that person's profession or business that does not otherwise consist of regulated activities. This exclusion applies where the regulated activities are:
- (a) arranging (bringing about) deals in investments and making arrangements with a view to transactions in investments;
  - (b) managing investments;
  - (c) assisting in the administration and performance of a contract of insurance; and
  - (d) safeguarding and administering investments;
- (3) The third exclusion applies to certain general insurance contracts covering large risks where the risk is situated outside the EEA. This exclusion applies where the regulated activities concerned are:
- (a) dealing in investments as agent;
  - (b) arranging (bringing about) deals in investments and making arrangements with a view to transactions in investments;
  - (c) assisting in the administration and performance of a contract of insurance; and
  - (d) advising on investments.

Guidance on these and other exclusions relevant to insurance mediation activities is in AUTH App 5 (Insurance mediation activities).

...

- 2.10.5 G A person is exempt if he is an appointed representative of an authorised person. See SUP 12 (Appointed representatives). But where an appointed representative carries on insurance mediation or reinsurance mediation he will not be exempt unless he is included on the register kept by the FSA under article 93 of the Regulated Activities Order (Duty to maintain a record of unauthorised persons carrying on insurance mediation activities) (see AUTH App 5.13 (Appointed representatives)).

...

2.10.8 G The exemptions apply so as to confer *exemption* on *persons* from the *general prohibition* in respect of four distinct categories of regulated activities.

...

(3) The third category is carrying on any of those *regulated activities* relating to *securities* or ~~*contractually-based investments*~~ *relevant investments* or to ‘any property’ .....

...

2.10.14 G The *regulated activities* that may be carried on in this way are restricted by an Order made by the Treasury under section 327(6) of the *Act* (Exemption from the general prohibition). Accordingly, under that section, a *person* may not by way of business carry on any of the following activities without *authorisation*:

...

(8) ~~entering into regulated mortgage contracts as lender or administering such contracts;~~ agreeing to do certain of the above activities.

...

2.10.15 G In addition, there are restrictions on carrying on (or agreeing to carry on) certain other *regulated activities*. These relate to *managing investments*, *advising on investments* or *regulated mortgage contracts*, ~~and *advising on syndicate participation at Lloyd’s*~~ and *entering into a regulated mortgage contract* or *administering a regulated mortgage contract*.

2.10.16 G A *person* carrying on *regulated activities* under the regime for members of the professions will be subject to rules made by the professional body designated by the Treasury. Such bodies are obliged to make rules governing the carrying on by their members of those *regulated activities* that they are able to carry on without *authorisation* under the *Act*. Where such a *person* is carrying on *insurance mediation* or *reinsurance mediation*, he must also be included on the register kept by the *FSA* under article 93 of the *Regulated Activities Order* (Duty to maintain a record of unauthorised persons carrying on insurance mediation activities) (see *AUTH* App 5.10 (Exemptions)).

...

## 2 Ann 2 G Regulated activities and the permission regime

1.3 G

...

(2) ...

...

Part III of the *Regulated Activities Order* (Specified investments) specifies the investments referred to at *AUTH* 2 Ann 2, 1.3G(1) 1.23(1).



...

2 Table:

Regulated activity	Specified investment in relation to which the regulated activity (in the corresponding entry in column 1) may be carried on
Regulated Activities [See note 1 to Table 1]	
<u>Accepting deposits</u>	
(a) <i>accepting deposits</i> (Article 5)	<i>deposit</i> (Article 74)
<u>Issuing electronic money</u>	
(aa) <i>issuing electronic money</i> (Article 9B)	<i>electronic money</i> (Article 74A)
Insurance business	
(b) <i>effecting contracts of insurance</i> (Article 10(1)) (c) <i>carrying out contracts of insurance</i> (Article 10(2))	<i>contract of insurance</i> (Article 75) [Expanded in Table 2]
Designated investment business [see note 1A and 1B 7 to Table 1]	
(d) <i>dealing in investments as principal</i> (Article 14) [see note 2 to Table 1] (e) <i>dealing in investments as agent</i> (Article 21) [see notes 1B and 2 to Table 1]	(in relation to (d) to (l)) <i>security</i> [Expanded in Table 3] or <i>contractually based investment</i> [Expanded in Table 3] (in relation to (e) to (g) and (j) only) a <i>long-term care insurance contract</i> which is a <i>pure protection contract</i>
(f) <i>arranging (bringing about) deals in investments</i> (Article 25(1)) [see note 1B to Table 1] [also see Sections of Table 1 headed 'Lloyd's market' Section and 'regulated mortgage activities']	
(g) <i>making arrangements with a view to transactions in investments</i> (Article 25(2)) [see note 1B to Table 1] [also see Sections of Table 1 headed 'Lloyd's market' Section and 'regulated mortgage activities'] (h) <i>managing investments</i> (Article 37) [see note 3 to Table 1] (i) <i>safeguarding and administering investments</i> (Article 40) [see note 3 to Table 1] For the purpose of the <i>permission</i> regime, this <i>regulated activity</i> is subdivided into:	

<p>(i) <i>safeguarding and administration of assets (without arranging);</i></p> <p>(ii) <i>arranging safeguarding and administration of assets</i></p> <p>(j) <i>advising on investments (Article 53) [see note 1B to Table 1] [also see Section of Table 1 headed ‘regulated mortgage activity’]</i></p> <p>For the purpose of the <i>permission</i> regime, this <i>regulated activity</i> is subdivided into:</p> <p>(i) <i>advising on investments (except pension transfers or pension opt- outs);</i></p> <p>(ii) <i>advising on pension transfers or pension opt-outs [see note 4 to Table 1]</i></p> <p>(k) <i>sending dematerialised instructions (Article 45(1))</i></p> <p>(l) <i>causing dematerialised instructions to be sent (Article 45(2))</i></p> <p>(m) <i>establishing, operating or winding up a collective investment scheme (Article 51)</i></p>	<p><i>security and contractually based investment [Expanded in Table 3]</i></p> <p>[see note 5 to Table 1]</p>
<p>For the purpose of the <i>permission</i> regime, this <i>regulated activity</i> is sub-divided into:</p>	
<p>(i) <i>establishing, operating or winding up a regulated collective investment scheme</i></p>	
<p>(ii) <i>establishing, operating or winding up an unregulated collective investment scheme</i></p>	
<p>(n) <i>acting as trustee of an authorised unit trust scheme (Article 51)</i></p> <p>(o) <i>acting as the depositary or sole director of an open-ended investment company (Article 51)</i></p> <p>(p) <i>establishing, operating or winding up a stakeholder pension scheme (Article 52)</i></p>	
<p><u>Insurance mediation activity [see note 5A to Table 1]</u></p>	

<p>(pa) <u>dealing in investments as agent</u> (Article 21)</p> <p>(pb) <u>arranging (bringing about) deals in investments</u> (Article 25(1))</p> <p>(pc) <u>making arrangements with a view to deals in investments</u> (Article 25(2))</p> <p>(pd) <u>assisting in the administration and performance of a contract of insurance</u> (article 39A)</p> <p>(pe) <u>advising on investments</u> (Article 53)</p> <p>For the purpose of the <u>permission regime</u>, this <u>regulated activity</u> is sub-divided into:</p> <p>(i) <u>advising on investments (except pension transfers or pension opt outs)</u>;</p> <p>(ii) <u>advising on pension transfers or pension opt outs</u> [See note 5E to Table 1]</p>	<p><u>life policy</u> [see note 5B to Table 1]</p> <p><u>pure protection contract</u> [see note 5C to Table 1]</p> <p><u>general insurance contract</u> [see note 5D to Table 1]</p> <p><u>rights to or interests in investments</u> (Article 89) in so far as they relate to a <u>life policy</u></p>
<p>The Lloyd's market [see note 6 to Table 1]</p>	
<p>(q) <u>advising on syndicate participation at Lloyd's</u> (Article 56)</p> <p>(r) <u>managing the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's</u> (Article 57)</p>	<p><u>membership of a Lloyd's syndicate</u> (Article 86(2))</p> <p><u>underwriting capacity of a Lloyd's syndicate</u> (Article 86(1))</p>
<p>(s) <u>arranging (bringing about) deals in investments</u> (Article 25(1))</p>	<p><u>underwriting capacity of a Lloyd's syndicate</u> (Article 86(1)), <u>membership of a Lloyd's syndicate</u> (Article 86(2)) or <u>rights to or interests in investments</u> (Article 89) in so far as they relate to <u>underwriting capacity of a Lloyd's syndicate or membership of a Lloyd's syndicate</u></p>
<p>(t) <u>making arrangements with a view to transactions in investments</u> (Article 25(2))</p>	
<p>Funeral plan providers [<del>a regulated activity with effect from 1 January 2002</del>]</p>	
<p>(u) <u>entering as provider into a funeral plan contract</u> (Article 59) [see Note 1A]</p>	<p><u>funeral plan contract</u> (Article 87)</p>
<p><u>Regulated mortgage activity</u></p>	
<p>(v) <u>arranging (bringing about) regulated mortgage contracts</u> (Article 25(A)(1))</p> <p>(w) <u>making arrangements with a view to regulated mortgage contracts</u> (Article 25(A)(2))</p>	<p><u>regulated mortgage contract</u> (Article 88)</p>

<p>(x) <u>advising on regulated mortgage contracts</u> (Article 53A)</p> <p>(y) <u>entering into a regulated mortgage contract</u> (Article 61(1))</p> <p>(z) <u>administering a regulated mortgage contract</u> (Article 61(2))</p>	
--	--

Notes to Table 1
<p>Note 1:</p> <p>In addition to the <i>regulated activities</i> listed in Table 1, Article 64 of the <i>Regulated Activities Order</i> specifies that <u>agreeing to carry on a regulated activity is itself a regulated activity in certain cases. This applies in relation to all the regulated activities listed in Table 1 apart from</u> <del>in relation to any other regulated activity other than:</del></p> <ul style="list-style-type: none"> <li>· <i>accepting deposits</i> (Article 5);</li> <li>· <i>issuing electronic money</i> (Article 9B);</li> <li>· <i>effecting and carrying out contracts of insurance</i> (Article 10);</li> <li>· <i>establishing, operating or winding up a collective investment scheme</i> (Article 51(1)(a));</li> <li>· <i>acting as trustee of an authorised unit trust scheme</i> (Article 51(1)(b));</li> <li>· <i>acting as the sole depository or sole director of an open-ended investment company</i> (Article 51(1)(c)); and</li> <li>· <i>establishing, operating or winding up a stakeholder pension scheme</i> (Article 52).</li> </ul> <p>Permission to carry on the activity of <i>agreeing to carry on a regulated activity</i> will be given automatically by the FSA in relation to those other <i>regulated activities</i> for which an applicant is given <i>permission</i> (other than those activities in Articles 5, 9B, 10, 51 and 52 detailed above).</p>

Note 1A:

Funeral plan contracts are contractually based investments. Accordingly, the following are regulated activities when carried on in relation to a funeral plan contract: (a) arranging (bringing about) deals in investments, (b) making arrangements with a view to transactions in investments, (c) managing investments, (d) safeguarding and administering investments, (e) advising on investments, (f) sending dematerialised instructions and (g) causing dematerialised instructions to be sent (as well as agreeing to carry on each of the activities listed in (a) to (g)).

However, they are not designated investment business.

Note 1B:

Life policies are contractually based investments. Where the regulated activities listed as designated investment business in (e) to (g) and (j) are carried on in relation to a life policy, these activities also count as 'insurance mediation activities'. The full list of insurance mediation activities is set out in (pa) to (pe). The regulated activities of agreeing to carry on each of these activities will, if carried on in relation to a life policy, also come within both designated investment business and insurance mediation activities.

Note 2:

For the purposes of the regulated activities of dealing in investments as principal (Article 14) and dealing in investments as agent (Article 21), the definition of contractually based investments [expanded in Table 3] excludes a funeral plan contract (Article 87) and rights to or interests in funeral plan contracts.

Note 3:

The regulated activities of managing investments (Article 37) and safeguarding and administering investments (Article 40) may apply in relation to any assets, in particular circumstances, if the assets being managed, or safeguarded and administered, include (or may include) any security or contractually based investment.

Note 4:

For the purposes of the permission regime, the activity in (j)(ii) of advising on pension transfers and pension opt-outs is carried on in respect of the following specified investments:

- unit (Article 81);
- stakeholder pension scheme (Article 82);
- life policy (explained in note 5A as defined in Article 3(1));
- rights to or interests in investments in so far as they relate to a unit, a stakeholder pension scheme or a life policy.

Note 5:

Article 4(2) of the Regulated Activities Order specifies the activities (m) to (p) for the purposes of section 22(1)(b) of the Act. That is, these activities will be regulated activities if carried on in relation to any property and are not expressed as relating to a specified investment.

Note 5A:

Where they are carried on in relation to a life policy, the activities listed as insurance mediation activities in (pa) to (pe) (as well as the regulated activity of agreeing to carry on those activities) are also designated investment business.

Note 5B:

Life policy is the term used in the *Handbook* to mean ‘qualifying contract of insurance’ (as defined in Article 3(1) of the *Regulated Activities Order*).

Note 5C:

*Pure protection contract* is the term used in the *Handbook* to mean a *long-term insurance contract* which is not a *life policy*.

Note 5D:

General insurance contract is the term used in the *Handbook* to mean contract of insurance within column 1 of Table 2.

Note 5E:

For the purposes of the *permission* regime, the activity in (pe)(ii) of advising on pension transfers and pension opt-outs is carried on in respect of the following specified investments:

- life policy (explained in note 5A);
- rights to or interests in investments in so far as they relate to a *life policy*.

Note 6:

Section 315 of the *Act* (The Society: authorisation and permission) states that the *Society of Lloyd’s* has *permission* to carry on the *regulated activities* referred to in that section, one of which is specified in Article 58 of the *Regulated Activities Order*. This *permission* is unique to the *Society of Lloyd’s*.

Note 7:

~~In relation to funeral plan contracts (a) managing investments, (b) safeguarding and administering investments, (c) advising on investments, (d) arranging (bringing about) deals in investments and (e) making arrangements with a view to transactions in investments (as well as agreeing to carry on each of those regulated activities) are regulated activities but they are not designated investments business.~~

...

Table 3: Securities, <del>and</del> contractually based investments and relevant investments [see notes 1 and 2 to Table 3]		
Security (article 3(1))	Contractually based investment (article 3(1))	Relevant investment (article 3(1))
<p><i>share</i> (Article 76)</p> <p><i>debenture</i> (Article 77)</p> <p><i>government and public security</i> (Article 78)</p> <p><i>warrant</i> (Article 79)</p> <p><i>certificate representing certain security</i> (Article 80)</p> <p><i>unit</i> (Article 81)</p> <p><i>stakeholder pension scheme</i> (Article 82)</p> <p><i>rights to or interests in investments</i> (Article 89) in so far as they relate to any of the above categories of <i>security</i></p>	<p><i>option</i> (Article 84)</p> <p>For the purpose of the <i>permission</i> regime, <i>option</i> is subdivided into:</p> <p>(i) <i>option</i> (excluding a <i>commodity option</i> and an <i>option</i> on a <i>commodity future</i>);</p> <p>(ii) <i>commodity option</i> and an <i>option</i> on a <i>commodity future</i>.</p> <p><i>future</i> (Article 85)</p> <p>For the purpose of the <i>permission</i> regime, <i>future</i> is subdivided into:</p> <p>(i) <i>future</i> (excluding a <i>commodity future</i> and a <i>rolling spot forex contract</i>);</p> <p>(ii) <i>commodity future</i>;</p> <p>(iii) <i>rolling spot forex contract</i>.</p> <p><i>contract for differences</i> (Article 86)</p> <p>For the purpose of the <i>permission</i> regime, <i>contract for differences</i> is subdivided into:</p> <p>(i) <i>contract for differences</i> (excluding a <i>spread bet</i> and a <i>rolling spot forex contract</i>);</p> <p>(ii) <i>spread bet</i>;</p> <p>(iii) a <i>rolling spot forex contract</i></p> <p><i>life policy</i> [see note 5B to Table 1]</p> <p><i>funeral plan contract</i> (Article 87)</p> <p><del>[from 1 January 2002]</del> [see Note 1A to Table 1]</p> <p><i>rights to or interests in investments</i> (Article 89) in so far as they relate to any of the above categories of <i>contractually based investment</i>.</p>	<p><u><i>contractually based investment</i> (article 3(1))</u></p> <p><u><i>pure protection contract</i> [see note 5C to Table 1]</u></p> <p><u><i>general insurance contract</i> [see note 5D to Table 1]</u></p>

Notes to Table 3

Note 1

*Security, ~~and~~ contractually based investment and relevant investment* are not, in themselves, *specified investments* ~~but~~ they are defined as including a number of *specified investments* as set out in Table 3. *Relevant investments* is the term that is used to cover *contractually based investments* together with rights under a *general insurance contract* and a *pure protection contract*.

Note 2

For the purposes of the *regulated activities of dealing in investments as principal* (article 14) and *dealing in investments as agent* (article 21), the definition of *contractually based investment* excludes a *funeral plan contract* (article 87) and rights to or interests in *funeral plan contracts*.

...

5.4.1 G ...

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**The conditions for establishing a branch**

5.4.2 G Before an *EEA firm* exercises an *EEA right* to establish a *branch* in the *United Kingdom* other than under the *Insurance Mediation Directive*, the *Act* requires it to satisfy the *establishment conditions*, as set out in paragraph 13(1) Part II of Schedule 3 to the *Act* (EEA Rights). These conditions are that:

(1) ...

5.4.2A G Where an *EEA firm* exercises its *EEA right* to establish a *branch* in the *United Kingdom* under the *Insurance Mediation Directive*, the *Act* requires it to satisfy the *establishment conditions*, as set out in paragraph 13(1A) Part II of Schedule 3 to the *Act* (EEA Rights). These conditions are that:

(1) the *EEA firm* has given its *Home State regulator* notice of its intention to establish a *branch* in the *United Kingdom*;

(2) the *FSA* has received notice ("a regulator's notice") from the *EEA firm's Home State regulator* that the *EEA firm* intends to establish a *branch* in the *United Kingdom*;

(3) the *EEA firm's Home State regulator* has informed the *EEA firm* that the regulator's notice has been sent to the *FSA*; and

(4) one month has elapsed beginning with the date when the *EEA firm's Home State regulator* informed the *EEA firm* that it had sent the regulator's notice to the *FSA*.

...

**The notification procedure**

5.4.4 G (1) ...



(2) Although the FSA is not required to notify the applicable provisions to an EEA firm passporting under the Insurance Mediation Directive, these provisions are set out in AUTH 5 Annex 3 G (Application of the Handbook to Incoming EEA Firms).

...

The conditions for providing cross border services into the United Kingdom

5.5.3 G Before an *EEA firm* exercises an *EEA right* to provide *cross border services* into the *United Kingdom*, the *Act* requires it to satisfy the *service conditions*, as set out in paragraph 14 of Part II of Schedule 3 to the *Act*. These conditions are that:

- (1) the *EEA firm* has given its *Home State regulator* notice of its intention to provide *cross border services* in the *United Kingdom* (a notice of intention);
- (2) if the *EEA firm* is passporting under either the *Investment Services Directive* or the *Insurance Directives*, or the *Insurance Mediation Directive*, the *FSA* has received notice (“a regulator’s notice”) from the *EEA firm’s Home State regulator* containing the information prescribed under regulation 3 of the *EEA Passport Rights Regulations* (see *AUTH 5 Annex 2G*); and
- (3) if the *EEA firm* is passporting under the *Insurance Directives* or the *Insurance Mediation Directive*, its *Home State regulator* has informed the *EEA firm* that it has sent the regulator’s notice to the *FSA*; and
- (4) if the *EEA firm* is passporting under the *Insurance Mediation Directive*, one month has elapsed beginning with the date when the *EEA firm’s Home State regulator* informed the *EEA firm* that it had sent the regulator’s notice to the *FSA*.

The notification procedure

5.5.4 G (1) Unless the *EEA firm* is passporting under the *Insurance Mediation Directive*, if the *FSA* receives a regulator’s notice or, where no notice is required (in the case of an *EEA firm* passporting under the *Banking Consolidation Directive*), is informed of the *EEA firm’s* intention to provide *cross border services* into the *United Kingdom*, the *FSA* will, under paragraphs 14(2)(b) and 14(3) of Part II of Schedule 3 to the *Act*, notify the *EEA firm* of the *applicable provisions* (if any) within two months of the day on which the *FSA* received the regulator’s notice or was informed of the *EEA firm’s* intention.

(2) Although the FSA is not required to notify the applicable provisions to an EEA firm passporting under the Insurance Mediation Directive, these provisions are set out in AUTH 5 Annex 3 G (Application of the Handbook to Incoming EEA Firms).

...

- 5.6.4 G Under the *EEA Passport Rights Regulations*, references in section 60 of the *Act* (applications for approval for persons to perform *controlled functions*) to "the authorised person concerned" include an *EEA firm* with respect to which the *FSA* has received a *consent notice* or regulator's notice under paragraph 13 of Schedule 3 to the *Act* (see *AUTH 5.4.2G(1)* and *AUTH 5.4.2A G(2)*) or a regulator's notice under paragraph 14 of that Schedule (see *AUTH 5.5.3G(2)*), and which will be the *authorised person* concerned if the *EEA firm* qualifies for *authorisation* under that Schedule.

...

#### AUTH 5 Annex 2

##### Provision of services: Contents of regulator's notice G

1 Table

Type of Firm	Para n.	Contents of <del>consent notice</del> <u>regulator's notice</u> (Regulation <del>2</del> <u>3</u> )
<i>Investment firm</i>	...	
<i>Insurance undertaking</i>	...	
<u><i>Insurance intermediary</i></u>	<u>(4)</u>	<u>that the firm intends to carry on insurance mediation or reinsurance mediation by providing services in the United Kingdom.</u>

#### AUTH 5 Annex 3

##### Application of the Handbook to Incoming EEA Firms G

2 Table: G

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
...	...	

<i>PRU</i>	<p><u><i>PRU 9.1 (Responsibility for insurance mediation activity) does not apply unless the firm has a top-up permission.</i></u></p> <p><u><i>PRU 9.2 (Professional indemnity insurance requirements for insurance and mortgage mediation activity and mortgage lending and administration) does not apply unless the firm has a top-up permission.</i></u></p>	<p><u>As column (2)</u></p> <p><u>As column (2)</u></p>
<i>PRU</i>	<p><u><i>PRU 9.3 (Capital resources for insurance and mortgage mediation activity and mortgage lending and administration) does not apply unless the firm has a top-up permission. See PRU 9.3.2G for more detailed guidance.</i></u></p> <p><u><i>PRU 9.4 (Insurance undertakings and mortgage lenders using insurance or mortgage mediation services) does not apply unless the firm has a top-up permission.</i></u></p>	<p><u>As column (2)</u></p> <p><u>As column (2)</u></p>
...		

...

7.1.1 G This chapter applies to anyone involved in publishing periodicals, or in providing news services or broadcasts, who gives (or proposes to give) advice about *securities*, ~~or contractually based investments~~ relevant investments or regulated mortgage contracts and who wishes to determine whether he will be carrying on the ~~regulated activity~~ activities of advising on investments or advising on regulated mortgage contracts.

...

7.1.2 G The purpose of this chapter is to provide *guidance* on:

- (1) when a *person* involved in publishing periodicals, or in providing news services or broadcasts, requires *authorisation* to carry on the ~~regulated activity~~ activities of advising on investments or advising on regulated mortgage contracts (see *AUTH 7.3* (Does the activity require authorisation)); and
- (2) if he does, whether he qualifies for the exclusion from ~~that activity~~ those activities that applies to a periodical publication, a regularly updated news or information service ...
- ...
- 7.2.1 G Advice is excluded by Article 54 of the *Regulated Activities Order* from the ~~regulated activity~~ activities of advising on investments and advising on regulated mortgage contracts if:
- (1) the advice is given in a publication or service that is in one of three formats (see *AUTH 7.4.3G* and *AUTH 7.4.4G*); and
- (2) the principal purpose of the particular format is neither to give certain advice nor to lead to (or enable) certain transactions to be carried out (see *AUTH 7.4.5G* and *AUTH 7.4.10G*).
- ...
- 7.2.2 G If a *person* would, but for the exclusion, be carrying on the ~~regulated activity~~ activities of advising on investments or advising on regulated mortgage contracts, or both, and will be doing so as a business in the *United Kingdom* .....
- Advising on investments and advising on regulated mortgage contracts
- ...
- 7.3.1 G Under Article 53 of the *Regulated Activities Order* (Advising on investments), advising a person is a specified kind of activity
- (1) ...
- (2) it is advice on the merits of his doing any of the following (whether as *principal* or agent):
- (a) *buying, selling*, subscribing for or underwriting a particular *investment* which is a *security* or a ~~contractually based investment~~ relevant investment; or
- ...
- 7.3.1A G Under Article 53A of the *Regulated Activities Order* (Advising on regulated mortgage contracts), advising a *person* is a specified kind of activity if :

- (1) the advice is given to the *person* in his capacity as a borrower or potential borrower; and
- (2) it is advice on the merits of his doing any of the following:
  - (a) entering into a particular *regulated mortgage contract*; or
  - (b) varying the terms of a *regulated mortgage contract* entered into by him after *mortgage day* in such a way as to vary his obligations under that contract.

- 7.3.2 G Articles 53 and 53A of the *Regulated Activities Order* contains a number of elements, all of which must be present before a *person* will require *authorisation*. For *guidance* on whether a *person* is carrying on ~~this~~ these *regulated-activity activities* see *AUTH* App 1 (Financial promotion and related activities [to be issued later]) and *AUTH* App 4 (Guidance on regulated activities connected with mortgages).
- 7.3.3 G ...  
 Under Section 22 of the *Act* (Regulated activities), for an activity to be a *regulated activity* it must be carried on ‘by way of business’. There is power in the *Act* for the Treasury to change the meaning of the business-element test by including or excluding certain things. It has exercised this power (see through the Financial Services and Markets Act 2000 (Carrying on Regulated Activities by Way of Business) Order 2001 (SI No 2001/1177) (the *Business Order*). This has been amended by Article 18 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003 (SI No 2003/1476) as explained in *AUTH* App7.3.3AG.
- 7.3.3A G The result of the amendments made to the meaning of the business test in section 22 of the *Act* is that the ~~business element~~ test differs depending on the activity in question. Where ~~the regulated activities carried on in relation to securities or contractually based investments~~ of advising on investments and advising on regulated mortgage contracts are concerned, the business element test is not to be regarded as satisfied unless a *person* carries on the business of engaging in ~~one or more of the~~ those activities. This is a narrower test than that of carrying on *regulated activities* by way of business (as required by section 22 of the *Act*), as it requires the *regulated activities* to represent the carrying on of a business in their own right. Where the advice relates to a *contract of insurance*, the business test is not be regarded as satisfied unless the *person* carrying on the activity of giving the advice is taking up or pursuing the activity for remuneration. This is the test which will apply to the regulated activity of advising on investments. *AUTH* 2.3 (The Business element) and *AUTH* 2.4 (Link between activities and the United Kingdom) together with *AUTH* App 5.4 (The business test) provide further detail on this.

7.3.4 G In the *FSA's* view, for a *person* to be carrying on the business of *advising on investments or advising on regulated mortgage contracts* he will usually need to be doing so with a degree of regularity and for commercial purposes - that is to say, he will normally be expecting to gain some kind of a direct or indirect financial benefit. But, in the *FSA's* view ..... or paid for by advertising. In such cases, if ~~advice on investments~~ advice on securities, relevant investments or regulated mortgage contracts is given, then in the *FSA's* view the business of *advising on investments or advising on regulated mortgage contracts* is being carried on. In addition ..... would not be regarded as carrying on the business of advising on investments or advising on regulated mortgage contracts as he would be acting to prevent crime rather than in the carrying on of a business.

...

7.3.7 G But even if advice is given in the *United Kingdom*, the *general prohibition* will not be contravened if the giving of advice does not amount to the carrying on, in the *United Kingdom*, of the business of *advising on investments or advising on regulated mortgage contracts*. Also, the ~~general prohibition~~ general prohibition will not be contravened if the exclusion for *overseas persons* in Article 72 of the *Regulated Activities Order* (*Overseas persons*) applies. That..... exclusion applies in relation to the giving of advice on securities or relevant investments by an *overseas person* as a result of a 'legitimate approach' ..... this will exclude any advice in a publication or service from being a *regulated activity* if it is given in response to an approach that has not been solicited in any way. It should be noted, however, that the exclusions in Article 72 only apply to the regulated activity of advising on regulated mortgage contracts where both the lender and the borrower are outside the United Kingdom. The effect of this is that, where the principal purpose of an overseas periodical publication is to offer advice on securities or relevant investments and regulated mortgage contracts, the exclusion for an overseas person who provides advice to persons in the United Kingdom as a result of a legitimate approach will not apply to the advice concerning regulated mortgage contracts.

...

7.4.2 G But the exclusion applies only if the principal purpose of the publication or service is ~~neither~~ not:

- (1) ~~to advise on~~ advise on investments (that is, *securities* or ~~contractually based~~ relevant investments) or *regulated mortgage contracts*; ~~nor~~ or
- (2) to lead or enable *persons* to:
  - (a) *buy, sell, subscribe for or underwrite securities* or ~~contractually based investments~~ relevant investments; or (as the case may be)

(b) to enter as borrower into regulated mortgage contracts, or vary the terms of regulated mortgage contracts entered into by the persons to whom the advice is given as borrower.

...

7.4.3 G (1) ...

...

(3) ... this would not generally constitute the *regulated activity of advising on investments* (see *AUTH App 1.28 (Financial promotion and related activities Advice or information)* ~~{to be issued later}~~) or advising on regulated mortgage contracts (see *AUTH App 4.6.10G (Advice or information)*). So the exclusion applies to services ...

7.4.5 G The exclusion applies only if the principal purpose of the publication or service is ~~neither~~ not:

(1) to give advice on ~~investments~~ securities, relevant investments or regulated mortgage contracts (see *AUTH 7.3.1G*); or;

(2) to lead or enable *persons* to:

(a) buy, sell, subscribe for or underwrite securities or contractually based investments relevant investments or to exercise any rights conferred by *securities* or contractually based such investments; or

(b) to enter as borrower into regulated mortgage contracts, or vary the terms of regulated mortgage contracts entered into by persons to whom the advice is given as borrower.

References to leading or enabling persons to do the things mentioned in (a) or (b) are (abbreviated in AUTH 7.4.9G and AUTH 7.4.11G as leading or enabling persons 'to engage in a relevant transaction').

...

- 7.4.8 G Looking at the first disqualifying purpose set out in the exclusion, all the matters relevant to whether the *regulated-activity activities* of *advising on investments* or *advising on regulated mortgage contracts* are ~~is~~ being carried on must be taken into account (see *AUTH* App 1.24 (~~Financial promotion and related activities [to be issued later]~~ *Advising on investments*)). If the principal purpose of a publication or service is to give to *persons*, in their capacity as investors (or potential investors) or as borrowers (as the case may be), advice as referred to in *AUTH* 7.4.5G(1), then the publication or service will not be able to benefit from this exclusion.
- 7.4.9 G For the second disqualifying purpose, the focus switches to assessing whether the principal purpose of a publication or service is to lead a person to engage in a relevant transaction or enable him to do so. This disqualifying purpose is an alternative to the first. So it extends to material not covered by the first. In this respect:
- (1) material in a publication or service that invites or seeks to procure *persons* to engage in a relevant transaction can be said to “lead” to those transactions even if it would not constitute the *regulated activities* of *advising on investments* or *advising on regulated mortgage contracts*; this includes, for example, material that consists of .....
  - (2) .....
- In the *FSA*’s view, material will not lead or enable a *person* to engage in a relevant transaction where the material is intended merely to raise people’s awareness of matters relating to *securities*, ~~or *contractually based investments*~~ *relevant investments* or *regulated mortgage contracts*.
- 7.4.13 G The *persons* who directly benefit from the exclusion will be the *persons* who would otherwise require *authorisation* (see ■*AUTH* 7.3.9 G), that is, the *person* whose business it is to have editorial control over the content of the publication or service. The exclusion will apply regardless of the legal form of the *person* giving the advice so, for example, it will extend to ~~advice on investments~~ advice given by a *company* through its employees.



## APPENDIX 1. FINANCIAL PROMOTION AND RELATED ACTIVITIES

- 1.4.22 G This will be the case provided the *financial promotion* does not identify any particular *investment* or *person* to whom introductions are to be made or identify the introducer as a *person* who carries on a *regulated activity* (typically of *making arrangements with a view to transactions in investments* under Article 25(2) of the *Regulated Activities Order* (see *AUTH App 1.33 (Introducing)*) or *making arrangements with a view to regulated mortgage contracts* under Article 25A(2) of the *Regulated Activities Order* (see *AUTH App 4.5 (Arranging regulated mortgage contracts)*). It is most likely to apply where the *financial promotion* relates to *deposits* or *contracts of insurance* which are not *contractually based investments*. The journalists' exemption in Article 20 of the *Financial Promotion Order (Communications by journalists)* may also be relevant where the introduction is made through or in a publication, broadcast or regularly updated news or information service (see *AUTH App 1.12.23G*). Article 15 (Introductions) may apply where the introduction is a *real time financial promotion* (see *AUTH App 1.12.11G*). In addition, Article 28B (Real time communications: introductions in connection with qualifying credit) may apply where an introduction that is a *real time financial promotion* relates to an agreement for *qualifying credit* (see *AUTH App 1.17.12G*).

...

- 1.7.2 G *Controlled activity* and *controlled investment* are defined in Schedule 1 to the *Financial Promotion Order* and are listed in *AUTH App 1.36.43* and *AUTH App 1.36.54*. Broadly speaking ..... important to note, however, that there are certain differences between *controlled activities* and *regulated activities*; and between *controlled investments* and *specified investments*. - most notably with certain credit agreements and funeral plans. This is most notable where the *financial promotion* is about:

- (1) certain credit agreements (see *AUTH App 1.17 (Financial promotions concerning agreements for qualifying credit)*);
- (2) *funeral plan contracts* (see *AUTH App 1.16 (Financial promotions concerning funeral plans)*); and
- (3) *contracts of insurance other than life policies* (see *AUTH App 1.17A (Financial promotions concerning insurance mediation activities)*).

So, it is quite possible for ...

...

1.9.5 G The restriction in section 21 is also disapplied under section 21(5) where provided for by the Treasury by order. The Treasury made such an order on 2 April 2001 (the *Financial Promotion Order*). This contains a number of specific exemptions which are referred to in *AUTH* App 1.2 to *AUTH* app 1.15 and *AUTH* App 1.21. The *Financial Promotion Order* has been amended by:

...

(4) ... 2002 ((SI 2002/1310); ~~and~~

(5) The Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) (Electronic Commerce Directive) Order 2001 (SI 2002/2157); and

(6) The Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) Order 2003 (SI 2003/ 1676).

...

1.12.15 G The exemption can also be used in certain circumstances where an ~~unauthorised~~ intermediary is advertising its services as an intermediary. This is because advising on and arranging *deposits* and *contracts of insurance other than life policies* are not *controlled activities*. This means that ~~For instance~~, an unauthorised intermediary offering to find the best rates on *deposits* or ~~most competitive premiums on motor insurance~~ will not be carrying on a *controlled activity* himself. So, he may identify himself (but not any particular deposit-taker or *insurer*) in the *financial promotion*-as he will not be carrying on a *controlled activity*. This is provided that the *financial promotion* does not identify any particular deposit-taker. The same considerations would apply to an *authorised* intermediary who offers to advise on the best available motor insurance.

...

1.12.25 G With this objective in mind, the exemption in article 20 (as amended by article 2 of the Financial Services and Markets Act 2000 (Financial Promotion) (Amendment No2) Order 2001) applies to any *non-real time financial promotion* the contents of which are devised by a *person* acting as a journalist where the *financial promotion* is in:

...

(3) ...

In addition ... that the principal purpose must not be to advise on or lead or enable *persons* to buy or sell *securities* or ~~*contractually-based investments*~~ *relevant investments*. See *AUTH* 7 for further guidance .....

...

1.13.4 G Intermediaries involved with arranging and advising on deposits ~~and contracts of insurance other than life policies~~ may be *unauthorised persons* as such activities do not amount to *regulated activities* and so do not require *authorisation* under section 19 of the *Act*. However, the combination of the exemptions in Part V together with certain of the exemptions in Part IV (such as generic promotions – see *AUTH* App 1.12.14G – and follow up communications – see *AUTH* App 1.12.10G) should mean that it will often be possible for such *persons* to avoid any need to seek approval for their *financial promotions* from an *authorised person*. Guidance on the application of these exemptions to *financial promotions* about *insurance mediation activities* is in *AUTH* App 1.17A (Financial promotions concerning insurance mediation activities).

...

1.17.1 G ~~[deleted] Section 21 will not apply to *financial promotions* concerning agreements for qualifying credit until a date in 2004 yet to be specified by the Treasury. The *FSA* will be consulting separately on *guidance* on this subject.~~

After Appendix 1.17.1G, insert the following new text.

Introduction

1.17.1A G Section 21 applies to *financial promotions* concerning agreements for *qualifying credit*. In this respect, it not only covers *financial promotions* about *regulated mortgage contracts* but also *financial promotions* about certain other types of credit agreement. This is explained in more detail in *AUTH* App 1.17.2G to *AUTH* App 1.17.3G.

Controlled investment: agreement for qualifying credit

1.17.2 G Rights under an agreement for *qualifying credit* are a *controlled investment*. *Qualifying credit* is defined in paragraph 10 of Schedule 1 to the *Financial Promotion Order* (Controlled activities) as credit provided pursuant to an agreement under which:

- (1) the lender is a *person* who carries on the *regulated activity* of *entering into a regulated mortgage contract* (whether or not he is an *authorised* or *exempt person* under the *Act*); and
- (2) the obligation of the borrower to repay is secured (in whole or in part) on land.

1.17.3 G An agreement for *qualifying credit* includes the following types of loan in addition to those that would be a *regulated mortgage contract*, but in each case only if the lender carries on the *regulated activity* of *entering into regulated mortgage contracts*:

- (1) loans secured by a second or subsequent charge;
- (2) secured loans for buy-to-let or other purely investment purposes;
- (3) loans secured on land situated outside the *United Kingdom*;
- (4) loans that include some unsecured credit such as a flexible mortgage that includes an unsecured credit card; and
- (5) commercial mortgages.

Controlled activities

1.17.4 G There are four *controlled activities* involving *qualifying credit*:

- (1) *providing qualifying credit*;
- (2) *arranging qualifying credit*;
- (3) *advising on qualifying credit*; and
- (4) *agreeing to carry on any of (1) to (3)*.

1.17.5 G *Providing qualifying credit* is a *controlled activity* under paragraph 10 of Schedule 1 to the *Financial Promotion Order*. In the *FSA's* view, 'providing' means, in this context, providing as lender; an intermediary does not 'provide' *qualifying credit*.

1.17.6 G *Arranging qualifying credit* is a *controlled activity* under paragraph 10A of Schedule 1 to the *Financial Promotion Order*; that is, making arrangements:

- (1) for another *person* to enter as borrower into an agreement for *qualifying credit*; or
- (2) for a borrower under a *regulated mortgage contract* entered into on or after 31 October 2004 to vary the terms of that contract in such a way as to vary his obligations under that contract.

This means that invitations and inducements relating to the services of mortgage arrangers will potentially be within the scope of Section 21 of the *Act*.

1.17.7 G *Advising on qualifying credit* will be a *controlled activity* under paragraph 10B of Schedule 1 to the *Financial Promotion Order*; that is, advising a *person* if the advice is:

- (1) given to the *person* in his capacity as a borrower or potential borrower; and
- (2) advice on the merits of his doing any of the following :
  - (a) entering into an agreement for *qualifying credit*; or
  - (b) varying the terms of a *regulated mortgage contract* entered into by him on or after 31 October 2004 in such a way as to vary his obligations under that contract.

This means that invitations and inducements relating to the services of mortgage advisers will potentially be within the scope of Section 21 of the *Act*.

1.17.8 G Agreeing to carry on each of these three *controlled activities* will also be a *controlled activity* under paragraph 11 of Schedule 1 to the *Financial Promotion Order*.

Application of exemptions to financial promotions about agreements for qualifying credit

1.17.9 G The exemptions in Part IV of the *Financial Promotion Order* (Exempt communications: all controlled activities) will apply to *financial promotions* about *qualifying credit*. Some of the exemptions in Part VI of the *Financial Promotion Order* (Exempt communications: certain controlled activities) will also apply. Those of particular note are referred to in *AUTH* App 1.17.10G to *AUTH* App 1.17.12G.

1.17.10 G Article 46 (Qualifying credit to bodies corporate) exempts any *financial promotion* about *providing qualifying credit* if it is :

- (1) made to or directed at *bodies corporate* only; or
- (2) accompanied by an indication that the *qualifying credit* to which it relates is only available to *bodies corporate*.

1.17.11 G Article 28(4) (One off non-real time communications and solicited real time communications) sets aside the general rule that exemptions in Parts V and VI of the *Financial Promotion Order* cannot be combined by permitting the combination of Article 28 and Article 23 (Deposits: real time communications) where the *financial promotion*:

- (1) is a one-off *solicited real time financial promotion*; and
- (2) is about *providing qualifying credit*.

1.17.12 G

Article 28B (Real time communications: introductions in connection with qualifying credit) exempts a *real time financial promotion* that relates to one or more of the *controlled activities* about *regulated mortgage contracts*. The exemption is subject to the following conditions being satisfied:

- (1) the *financial promotion* must be made for the purpose of, or with a view to, introducing the recipient to a *person* ('N') who is:
  - (a) an *authorised person* who carries on the *controlled activity* to which the communication relates; or
  - (b) an *appointed representative*, where the *controlled activity* is also a *regulated activity* in respect of which the *appointed representative* is exempt; or
  - (c) an overseas person who carries on the *controlled activity* to which the communication relates; for this purpose, an 'overseas person' is a *person* who carries on any of the *controlled activities* about *qualifying credit* but does not do so, or offer to do so, from a permanent place of business maintained by him in the *United Kingdom*; and
- (2) the *person* ('M') communicating the *financial promotion*:
  - (a) must not receive any money paid by the recipient in connection with any transaction that the recipient enters into with or through N as a result of the introduction, other than money payable to M on M's own account; and
  - (b) before making the introduction, must disclose to the borrower the following information where it applies to M:
    - (i) whether M is a member of the same *group* as N;
    - (ii) details of any payment which M will receive from N, by way of fee or commission, for introducing the recipient to N; and
    - (iii) an indication of any other reward or advantage arising out of M's introducing to N.

- 1.17.13 G Introducers can check whether a *person* is an *authorised person* or an *appointed representative* by visiting the *FSA's* register at [www.fsa.gov.uk](http://www.fsa.gov.uk). If an *authorised person* has *permission* to carry on a *regulated activity* (which can be checked on the *FSA's* register) it is reasonable, in the *FSA's* view, to conclude that the *authorised person* carries on that activity (but not a *controlled activity* which is not a *regulated activity*). The *FSA* would normally expect introducers to request and receive confirmation of other facts necessary to satisfy the condition in *AUTH* App 1.17.12G(1), prior to proceeding with an introduction.
- 1.17.14 G In the *FSA's* view, money payable to an introducer on his own account includes money legitimately due to him for services rendered to the borrower, whether in connection with the introduction or otherwise. It also includes sums payable in connection with transfer of property to an introducer (for example, a housebuilder) by a borrower. For example, Article 28B allows a housebuilder to receive the purchase price on a property that he *sells* to a borrower, whom he previously introduced to an *authorised person* or *appointed representative* to help him finance the purchase in return for a fee payable by the borrower, and still take the benefit of the exclusion. This is because the sums that the housebuilder receives in connection with the introduction and the sale of his property to the borrower are both 'payable to him on his own account'. The housebuilder could also receive a commission from the *person* introduced to.
- 1.17.15 G In the *FSA's* view, the provision of details of fees or commission referred to in *AUTH* App. 1.17.12G(2)(b)(ii) does not require an introducer to provide an actual sum to the borrower, where it is not possible to calculate the full amount due prior to the introduction. This may arise in cases where the fee or commission is a percentage of the eventual loan taken out and the amount of the required loan is not known at the time of the introduction. In these cases, it would be sufficient for the introducer to disclose the method of calculation of the fee or commission, for example the percentage of the eventual loan to be made by N.
- 1.17.16 G In the *FSA's* view, the information condition in *AUTH* App. 1.17.12G(2)(b)(iii) requires the introducer to indicate to the borrower any other advantages accruing to him as a result of ongoing arrangements with N relating to the introduction of borrowers. This may include, for example, indirect benefits such as office space, travel expenses, subscription fees. This and other relevant information may, where appropriate, be provided on a standard form basis to the borrower. The *FSA* would normally expect an introducer to keep a written record of disclosures made to the borrower under Article 33A of the *Regulated Activities Order* including those cases where disclosure is made on an oral basis only.

## Interaction with the Consumer Credit Act

1.17.17 G Most credit advertisements are, with various exceptions, regulated under the Consumer Credit Act 1974. However, Article 90(3) (Consequential amendments of the Consumer Credit Act 1974) and Article 91(1) (Consequential amendments to subordinate legislation under the Consumer Credit Act 1974) of the *Regulated Activities Order* disapply the provisions of the Consumer Credit Act 1974 to any *financial promotion* other than an exempt generic communication. An exempt generic communication is a *financial promotion* that is exempt under Article 17 of the *Financial Promotion Order* (Generic promotions) (see *AUTH* App 1.12.14G (Generic promotions (Article 17))). Hence, an advertisement about credit of any kind will either be regulated under Section 21 of the *Act* or under the Consumer Credit Act 1974. Such an advertisement will only be subject to regulation under both statutes if it is about secured and unsecured lending. Typical examples showing which statute regulates particular types of credit advertisements are given in the table in *AUTH* App 1.17.18G (Table - Guide to the application of the Act and the Consumer Credit Act 1974 to credit advertisements).

1.17.18 G Table: Guide to application of the Act and the Consumer Credit Act 1974 to credit advertisements. This table belongs to *AUTH* App 1.17.17G

	Subject of advertising or promotion	FSMA regulated	CCA regulated
(1)	<i>regulated mortgage contracts</i>	Yes	No
(2)	other loans secured on land where the lender also enters into <i>regulated mortgage contracts</i> as lender	Yes	No
(3)	loans not secured on land whether or not the lender also enters into <i>regulated mortgage contracts</i> as lender	No	Yes
(4)	loans not secured on land but which form part of a loan product that is otherwise secured on land and where the lender enters into <i>regulated mortgage contracts</i> as lender	Yes	No



- |     |  |     |     |
|-----|--|-----|-----|
| (5) | loans as in (1), (2) or (4) but where the advertisement is subject to exemptions under the <i>Financial Promotion Order</i> other than Article 17 (Generic promotions) | Yes | No  |
| (6) | loans as in (1), (2) or (4) but where the advertisement is exempt under Article 17 of the <i>Financial Promotion Order</i> (Generic Promotions)                        | No  | Yes |
| (7) | loans with features as in (1), (2), (4) or (5) promoted in combination with other loans  | Yes | Yes |

....

1.17A Financial promotions concerning insurance mediation activities

1.17A.1 G The application of section 21 of the *Act* and of exemptions in the *Financial Promotion Order* to invitations or inducements about *insurance mediation activities* will vary depending on the type of activity. The implementation of the *Insurance Mediation Directive* has not led to any changes in the definitions of a *controlled investment* or a *controlled activity* under the *Financial Promotion Order*. So:

- (1) rights under any *contract of insurance* are a *controlled investment*;
- (2) rights to or interests in rights under *life policies* are *controlled investments* but rights to or interests in rights under other *contracts of insurance* are not;
- (3) the activities of:
  - (a) *dealing in investments as agent*;
  - (b) *arranging (bringing about) deals in investments*;
  - (c) *making arrangements with a view to transactions in investments*; and
  - (d) *advising on investments*,

where they relate to *contracts of insurance*, are *controlled activities* only where the *contract of insurance* is a *life policy*;

- (4) the activity of *assisting in the administration and performance of a contract of insurance* is not a *controlled activity*.

1.17A.2 G This means that an insurance intermediary will not be *communicating a financial promotion*:

- (1) where the only activity to which the promotion relates is *assisting in the administration and performance of a contract of insurance*; or
- (2) purely by reason of his inviting or inducing *persons* to make use of his advisory or arranging services where they relate only to *general insurance contracts* or *pure protection contracts* or both.

But as regards (2), an intermediary will be *communicating a financial promotion* if he is also inviting or inducing *persons* to enter into a *contract of insurance*. This is because the making and performance of the contract by the *insurer* will be a *controlled activity* (of *effecting and carrying out a contract of insurance*). Insurance intermediaries will, however, be able to use the exemptions in Part V of the *Financial Promotion Order* (see *AUTH App 13* (Exemptions applying to financial promotions concerning deposits and certain contracts of insurance) where they promote a *general insurance contract* or a *pure protection contract*. Where an insurance intermediary is promoting *life policies*, he will be able to use any exemptions in Part VI of the *Financial Promotion Order* that apply to a *contractually based investment*.

...

1.23.3 G The *regulated activities* which are likely to be conducted in the circumstances referred to in *AUTH App 1.23.2G* are:

- (1) giving advice on certain investments (Articles 53 (Advising on investments), 53A (Advising on regulated mortgage contracts) and 56 (Advice on syndicate participation at Lloyd's) of the *Regulated Activities Order*) - for example, where the *financial promotion* is the advice;
- (2) *making arrangements with a view to transactions in investments* (Article 25(1) of the *Regulated Activities Order* (Arranging deals in investments)) or making arrangements with a view to regulated mortgage contracts (Article 25A(2) of the *Regulated Activities Order* (Arranging regulated mortgage contracts)) - for example, where the *person* concerned makes arrangements that are intended to lead to a transaction by a third party; and

- (3) agreeing to carry on either (1) or (2) (Article 64 of the *Regulated Activities Order* (Agreeing to carry on specified kinds of activity)).
- 1.23.4 G The *guidance* that follows is concerned with the *regulated activities of making arrangements with a view to transactions in and advising on investments*. *Guidance on the regulated activities of making arrangements with a view to and advising on regulated mortgage contracts* is in *AUTH App 4* (Guidance on regulated activities connected with mortgages).
- 1.24.1 G ...  
 (1) ...  
 (2) is advice on the merits of his (whether as principal or agent) *buying, selling*, subscribing for or underwriting a particular *investment* which is a *security* or a ~~*contractually based investment*~~ *relevant investment* or exercising any right conferred by such an *investment* to *buy, sell*, subscribe for or underwrite such an *investment*.
- 1.24.2 G ...  
 (1) it must relate to an *investment* which is a *security* or a ~~*contractually based investment*~~ *relevant investment*;  
 ...
- 1.25.1 G For the purposes of section 53 of the *Regulated Activities Order*, a *security* or ~~*contractually based investment*~~ *relevant investment* is any one of the following:  
 (1) ...  
 ...  
 (11) ~~*life policies*~~ *contracts of insurance*;  
 ...
- 1.25.2 G Article 53 does not apply to advice given on any of the following:  
 (1) *deposit* or other *bank* or *building society* accounts;  
 (2) ~~contracts of general insurance or of long term insurance which are not *contractually based investments* (for example, most pure term and permanent health insurance);~~ interests under the trusts of an *occupational pension scheme* (but rights under an *occupational pension scheme* that is a *stakeholder pension scheme* will be *securities*).

- (3) mortgages or other loans (but note that advising on *regulated mortgage contracts* is a separate *regulated activity* under Article 53A of the *Regulated Activities Order* - see the *guidance in AUTH App 4 (Regulated activities connected with mortgages)*);
- ...
- (9) ~~interests under the trusts of an *occupational pension scheme* other than a *stakeholder pension scheme*.~~[deleted]
- ...
- 1.26.4 G ...
- (1) ...
- ...
- (5) ~~*contracts of insurance*, which are *contractually based investments* - these are both products and contractual *investments*;~~ so a particular *investment* would include:
- ...
- 1.27.1 G For the purposes of Article 53, advice must be given to or directed at someone who either holds *investments* or is a prospective investor (or their agent). Where the *investment* is a risk only *contract of insurance* such as *house contents insurance*, the *policyholder* or prospective *policyholder* is regarded as an investor.
- ...
- 1.31.4 G ...
- 1.31.5 G Certain of the exclusions in the *Regulated Activities Order* that apply to the *regulated activity* of *advising on investments* are not available where the advice either relates to a *contract of insurance* or amounts to *insurance mediation* or *reinsurance mediation*. This results from the requirements of the *Insurance Mediation Directive* and is explained in more detail in *AUTH App 5 (Insurance mediation activities)*.
- ...
- 1.32.1 G Under Article 25 of the *Regulated Activities Order*, arranging deals in investments covers:
- (1) making arrangements for another *person* (whether as principal or agent) to *buy, sell*, subscribe for or underwrite a particular *investment* which is:
- (a) a *security*; or
- (b) a ~~*contractually based investment*~~ *relevant investment*;
- or
- ...
- 1.32.11 G ...

1.32.12 G     Where *persons* are making arrangements concerning *contracts of insurance* or are carrying on *insurance mediation or reinsurance mediation*, certain exclusions to Article 25 are not available. This results from the requirements of the *Insurance Mediation Directive* and is explained in more detail in *AUTH App 5.6 (Insurance mediation activities)*The regulated activities: arranging deals in, and making arrangements with a view to transactions in, contracts of insurance).

1.33.5    G     ...

1.33.6    G     The exclusions in Articles 29 and 33 of the *Regulated Activities Order* are not available where the *investment* is a *contract of insurance*. However, certain other exclusions do apply. This results from implementation of the requirements of the *Insurance Mediation Directive* and is explained in more detail in *AUTH App 5.6 (Insurance mediation activities)* The regulated activities: arranging deals in, and making arrangements with a view to transactions in, contracts of insurance).

...

1.36.3    G     Table: Controlled activities

1.        ....

...

9.        Providing funeral plan contracts (~~with effect from 1 January 2002~~).

10.       Providing qualifying credit (~~with effect from a date to be announced~~).

10A.    Arranging qualifying credit etc.

10B.    Advising on qualifying credit etc.

11.       Agreeing to do anything in 3 to 10B above.

## Annex E

### Amendments to the Authorisation manual

In this Annex, all the text is new text and is not underlined.

After Appendix 4, insert the following new appendix as Appendix 5.

#### Appendix 5

##### Guidance on Insurance Mediation Activities

##### 5.1. Application and purpose

###### Application

5.1.1G This appendix applies principally to any *person* who needs to know whether he carries on *insurance mediation activities* and is thereby subject to *FSA* regulation. As such it will be of relevance among others to:

- (1) insurance brokers;
- (2) insurance advisers;
- (3) *insurance undertakings*; and
- (4) other *persons* involved in the sale and administration of *contracts of insurance*, even where these activities are secondary to their main business.

###### Purpose of guidance

5.1.2G With effect from 14 January 2005 certain pre-contractual sales and post-contractual administration activities relating to *contracts of insurance* will become regulated by the *FSA* for the first time as part of the implementation by the *United Kingdom* of the *Insurance Mediation Directive (IMD)*.

5.1.3G The *insurance mediation activities* apply to all *contracts of insurance*, but the implementation of the *IMD* brings the mediation of *general insurance contracts* and *pure protection contracts* within the scope of *FSA* regulation for the first time.

5.1.4G The *FSA* already regulates certain activities carried on by intermediaries in relation to *life policies* (see the *guidance* contained in *AUTH 2* (Authorisation and regulated activities)). However, the changes to *FSA* regulation in force from 14 January 2005 will also potentially affect the regulatory position of *firms* already carrying on *regulated activities* in connection with *life policies* including *insurers*. These *firms* should therefore consider whether or not they need to apply for a variation of their *Part IV permission*.

5.1.5G *Insurance mediation activities* will typically be carried out by insurance and reinsurance brokers, financial advisers, agents, consultants and outsourcers. In addition, *persons* whose principal business is not *insurance mediation* may also carry on these activities and will need to consider whether they require *authorisation* or can benefit from an exclusion or exemption.

5.1.6G The purpose of this *guidance* is to help *persons* consider whether they need *authorisation* or a variation of their *Part IV permission*. Businesses new to regulation who act only as introducers of insurance business are directed in particular to *AUTH* App 5.6.2G (Article 25(1): arranging (bringing about) deals in investments) to *AUTH* App 5.6.9G (Exclusion: article 72C provision of information on an incidental basis) and *AUTH* App 5.15.6G (Flow chart: introducers) to help consider whether they require *authorisation*. This *guidance* also explains the availability to *persons* carrying on *insurance mediation activities* of certain exemptions from *FSA* regulation, including the possibility of becoming an *appointed representative* (see *AUTH* App 5.13.1G to *AUTH* App 5.13.6G (Appointed representatives)).

#### Effect of guidance

5.1.7G This *guidance* is issued under section 157 of the *Act* (Guidance). It is designed to throw light on particular aspects of regulatory requirements, not to be an exhaustive description of a *person's* obligations. If a *person* acts in line with the *guidance* and the circumstances contemplated by it, then the *FSA* will proceed on the footing that the *person* has complied with aspects of the requirement to which the *guidance* relates.

5.1.8G Rights conferred on third parties cannot be affected by *guidance* given by the *FSA*. This *guidance* represents the *FSA's* view, and does not bind the courts, for example, in relation to the enforceability of a contract where there has been a breach of the *general prohibition* on carrying on a *regulated activity* in the *United Kingdom* without *authorisation* (see sections 26 to 29 of the *Act* (Enforceability of Agreements)).

5.1.9G A *person* reading this *guidance* should refer to the *Act* and the various Orders that are referred to in this *guidance*. These should be used to find out the precise scope and effect of any particular provision referred to in this *guidance*. A *person* may need to seek his own legal advice.

5.1.10G The text in *AUTH* App 5.1.2G to *AUTH* App 5.1.6G, *AUTH* App 5.2.6G, *AUTH* App 5.11.2G, *AUTH* App 5.13.5G and *AUTH* App 5.13.6G relates only to the period prior to the implementation of the *Insurance Mediation Directive*, that is before 14 January 2005.

#### Guidance on other activities

5.1.11G A *person* may wish to carry on activities related to other forms of *investment* in connection with *contracts of insurance*, such as *advising on* and *arranging regulated mortgage contracts*. Such a *person* should also consult the *guidance* in *AUTH* 2 (Authorisation and Regulated Activities), *AUTH* App 1 (Financial Promotion and Related Activities) and *AUTH* App 4 (Regulated activities connected with mortgages).

## 5.2. Introduction

5.2.1G This *guidance* is based on the statutory instruments made as part of implementing the *IMD* in the *United Kingdom*. This legislation includes the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003 (S.I. 2003/1476), which amends among others the *Regulated Activities Order*, the Financial Services and Markets Act 2000 (Appointed Representatives) Regulations 2001 (S.I. 2003/1217), the *Non-Exempt Activities Order* and the *Business Order*. Other legislation that forms the basis of this *guidance* includes the Financial Services and Markets Act 2000 (Exemption) (Amendment) (No.2) Order 2003 (S.I. 2003/1675), the Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) Order 2003 (S.I. 2003/1676) and the Insurance Mediation Directive (Miscellaneous Amendments) Regulations 2003 (S.I. 2003/1473). For ease of reference, references to the *Regulated Activities Order* below adopt the revised *Regulated Activities Order* numbering indicated in the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003.

### Requirement for authorisation or exemption

5.2.2G Any *person* who carries on a *regulated activity* in the *United Kingdom* by way of business must either be an *authorised person* or exempt from the need for *authorisation*. Otherwise, the *person* commits a criminal offence and certain agreements may be unenforceable. *AUTH 2.2* (Authorisation and regulated activities) has further *guidance* on these consequences. To be *authorised*, a *person* must either:

- (1) hold a *Part IV permission* given by the *FSA* (see *AUTH 1.3* (The Authorisation Manual) and *AUTH 3* (Applications for Part IV Permission)); or
- (2) qualify for *authorisation* (see *AUTH 5* (Qualifying for Authorisation under the Act)); for example, if the *person* is an *EEA firm* or a *Treaty firm*.

### Questions to be considered to decide if authorisation is required

5.2.3G A *person* who is concerned to know whether his proposed *insurance mediation activities* may require *authorisation* will need to consider the following questions (these questions are a summary of the issues to be considered and have been reproduced, in slightly fuller form, in the flow chart in *AUTH App 5.15.2G* (Flow chart: regulated activities related to insurance mediation – do you need authorisation?):

- (1) will the activities relate to *contracts of insurance* (see *AUTH App 5.3* (Contracts of insurance))?
- (2) if so, will I be carrying on any *insurance mediation activities* (see *AUTH App 5.5* (The regulated activities: dealing in contracts as agent) to *AUTH App 5.11* (Other aspects of exclusions))?
- (3) if so, will I be carrying on my activities by way of business (see *AUTH App 5.4* (The business test))?



- (4) if so, is there the necessary link with the *United Kingdom* (see *AUTH* App 5.12 (Link between activities and the United Kingdom))?
- (5) if so, will any or all of my activities be excluded (see *AUTH* App 5.3.7G (Connected contracts of insurance) to *AUTH* App 5.3.8G (Large risks); *AUTH* App 5.6.5G (Exclusion: article 72C provision of information on an incidental basis) to *AUTH* App 5.6.23G (Other exclusions); *AUTH* App 5.7.7G (Exclusions); *AUTH* App 5.8.24G (Exclusion: periodical publications, broadcasts and web-sites) to *AUTH* App 5.8.26G (Other exclusions); *AUTH* App 5.11 (Other aspects of exclusions) and *AUTH* App 5.12.9G to *AUTH* App 5.12.10G (Overseas persons))?
- (6) if it is not the case that all of my activities are excluded, am I a *professional firm* whose activities are exempted under Part XX of the *Act* (see *AUTH* App 5.14.1G to *AUTH* App 5.14.4G (Professionals))?
- (7) if not, am I exempt as an *appointed representative* (see *AUTH* App 5.13 (Appointed representatives))?
- (8) if not, am I otherwise an *exempt person* (see *AUTH* App 5.14.5G (Other exemptions))?

If a *person* gets as far as question (8) and the answer to that question is “no”, that *person* requires *authorisation* and should refer to *AUTH* 3 (Application for Part IV Permission). The order of these questions considers firstly whether a *person* is carrying on *insurance mediation activities* before dealing separately with the questions "will I be carrying on my activities by way of business?" (3) and "if so, will any or all of my activities be excluded?" (5).

5.2.4G It is recognised pursuant to section 22 of the *Act* that a *person* will not be carrying on *regulated activities* in the first instance, including *insurance mediation activities*, unless he is carrying on these activities by way of business. Similarly, where a *person's* activities are excluded he cannot, by definition, be carrying on *regulated activities*. To this extent, the content of the questions above does not follow the scheme of the *Act*. For ease of navigation, however, the questions are set out in an order and form designed to help *persons* consider more easily, and in turn, issues relating to:

- (1) the new activities;
- (2) the business test; and
- (3) the exclusions.

#### Approach to implementation of the IMD

5.2.5G The *IMD* imposes requirements upon *EEA States* relating to the regulation of *insurance* and *reinsurance mediation*. The *IMD* defines “insurance mediation” and “reinsurance mediation” as including the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance and reinsurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim (the text of article 2.3

*IMD* is reproduced in full in *AUTH* App 5.16.2G (Article 2.3 of the Insurance Mediation Directive)).

5.2.6G The *United Kingdom's* approach to implementing the *IMD* by domestic legislation is, in part, through secondary legislation, which will apply pre-existing *regulated activities* (slightly amended) in the *Regulated Activities Order* to the component elements of the *insurance mediation* definition in the *IMD* (see *AUTH* App 5.2.5G and the text of article 2.3 *IMD* in *AUTH* App 5.16.2G (Article 2.3 of the Insurance Mediation Directive)).

5.2.7G The effect of the *IMD* and its implementation described in *AUTH* App 5.2.5G to *AUTH* App 5.2.6G is to vary the application of the existing *regulated activities* set out in *AUTH* App 5.2.8G(1) to (3), (5) and (6), principally by applying these *regulated activities* to *general insurance contracts* and *pure protection contracts* and by making changes to the application of the various exclusions to these *regulated activities*. These *regulated activities* apply prior to 14 January 2005 to qualifying contracts of insurance (as defined by article 3 of the *Regulated Activities Order* and referred to in the *Handbook* as *life policies* (which includes *pension policies*)). The legislation implementing the *IMD* also introduces a new *regulated activity* set out in *AUTH* App 5.2.8G(4), which potentially applies to all *contracts of insurance*.

5.2.8G It follows that each of the *regulated activities* below potentially apply to any *contract of insurance*:

- (1) *dealing in investments as agent* (article 21 (Dealing in investments as agent));
- (2) *arranging (bringing about) deals in investments* (article 25(1) (Arranging deals in investments));
- (3) *making arrangements with a view to transactions in investments* (article 25(2) (Arranging deals in investments));
- (4) *assisting in the administration and performance of a contract of insurance* (article 39A (Assisting in the administration and performance of a contract of insurance));
- (5) *advising on investments* (article 53 (Advising on investments));
- (6) *agreeing to carry on any of the above regulated activities* (article 64 (Agreeing to carry on specified types of activity)).

5.2.9G It is the scope of the *Regulated Activities Order* rather than the *IMD* which will determine whether a *person* requires *authorisation* or exemption. However, the scope of the *IMD* is relevant to the application of certain exclusions under the *Regulated Activities Order* (see, for example, the commentary on article 67 in *AUTH* App 5.11.9G (Activities carried on in the course of a profession or non-investment business)).

Financial promotion

5.2.10G An *unauthorised person* who intends to carry on activities connected with *contracts of insurance* will need to comply with section 21 of the *Act* (Restrictions on financial promotion). This *guidance* does not cover *financial promotions* that relate to *contracts of insurance*. *Persons* should

refer to the general *guidance on financial promotion in AUTH App 1* (Financial promotion and related activities). (See in particular *AUTH App 1.17A* (Financial promotions concerning insurance mediation activities) for information on *financial promotions* that relate to *insurance mediation activities*.)

### 5.3. Contracts of insurance

5.3.1G A person who is concerned to know whether his proposed activities may require *authorisation* will wish to consider whether those activities relate to *contracts of insurance* or *contracts of reinsurance*, or to *insurance business* or *reinsurance business*, which is the business of effecting or carrying out *contracts of insurance* or *reinsurance* as *principal*.

#### Definition

5.3.2G The *Regulated Activities Order* does not attempt an exhaustive definition of a ‘contract of insurance’. Instead, article 3(1) of the order (Interpretation) makes some specific extensions and limitations to the general common law meaning of the concept. For example, article 3(1) expressly extends the concept to fidelity bonds and similar contracts of guarantee, which are not contracts of insurance at common law, and it excludes certain *funeral plan contracts*, which would generally be contracts of insurance at common law.

5.3.3G One consequence of this is that common law judicial decisions about whether particular contracts amount to ‘insurance’ or their being effected or carried out amounts to ‘insurance business’ are relevant in defining the scope of the *FSA’s authorisation* and regulatory activities.

5.3.4G As with any other contract, a *contract of insurance* that is not effected by way of a deed will only be legally binding if, amongst other things, it is entered into for valuable consideration. Determining what amounts to sufficient consideration in any given case is a matter for the courts. In practice, however, the legal definition of consideration is very wide. In particular, just because a *contract of insurance* is ‘free’ in the colloquial sense does not mean that there is no consideration for it. In the vast majority of cases, therefore, ‘free’ insurance policies (such as policies that act as loss leaders for an *insurance undertaking*) will be binding contracts and will amount to *specified investments* and therefore be subject to *FSA* regulation.

5.3.5G The *Regulated Activities Order* does not define a *reinsurance* contract. The essential elements of the common law description of a *contract of insurance* are also the essential elements of a *reinsurance* contract. Whilst the *IMD* addresses insurance and *reinsurance* separately, throughout this *guidance* the term ‘contract of insurance’ (italicised or otherwise) also applies to contracts of *reinsurance*.

5.3.6G The *FSA* has consulted (in CP 150 (The Authorisation manual - consultation on draft guidance on the identification of contracts of insurance)) on draft *guidance* describing how the *FSA* identifies *contracts of insurance*.



## Connected contracts of insurance

5.3.7G Article 72B of the *Regulated Activities Order* (Activities carried on by a provider of relevant goods or services) excludes from *FSA* regulation certain *regulated activities* carried on by providers of non-motor goods and services related to travel in relation to *contracts of insurance* that satisfy a number of conditions. Details about the scope of this exclusion can be found at *AUTH* App 5.11.13G to *AUTH* App 5.11.15G (Activities carried on by a provider of relevant goods or services).

### Large risks

5.3.8G Large risks situated outside the *EEA* are also excluded (described in more detail at *AUTH* App 5.11.16G (Large risks)). The location of the risk or commitment may be determined by reference to the *EEA State* in which the risk is situated, defined in article 2(d) of the Second Non-Life Directive (88/357/EEC) or the *EEA State* of the commitment, defined in article 1(1)(g) of the Consolidated Life Directive (2002/83/EC). Broadly put, this is:

- (1) for insurance relating to buildings and/or their contents, the *EEA State* in which the property is situated;
- (2) for insurance relating to vehicles, the *EEA State* of registration;
- (3) for policies of four months or less duration covering travel or holiday risks, where the *policy* was taken out;
- (4) in all other cases (including those determined by reference to the *EEA State* of the commitment), the *EEA State* where the policyholder has his habitual residence, or if the policyholder is a legal person, where his establishment, to which the contract relates, is situated.

### Specified investments

5.3.9G For an activity to be a *regulated activity*, it must be carried on in relation to 'specified investments' (see section 22 of the *Act* Regulated activities) and Part III of the *Regulated Activities Order* (Specified investments)). For the purposes of *insurance mediation activity*, *specified investments* include the following '*relevant investments*' defined in article 3(1) of the *Regulated Activities Order* (Interpretation):

- (1) rights under any *contract of insurance* (see article 75 (Contracts of insurance)); and
- (2) rights to or interests in *life policies* (see article 89 (Rights to or interests in investments)).

'*Relevant investments*' is the term used in articles 21 (Dealing in investments as agent), 25 (Arranging deals in investments) and 53 (Advising on investments) of the *Regulated Activities Order* to help define the types of *investment* to which the activities in each of these articles relate.

5.3.10G A *person* will have rights under a *contract of insurance* when he is a *policyholder*. The question of whether a *person* has rights under a *contract of insurance* may require careful consideration in the case of group policies (with reference to the *Glossary* definition of *policyholder*). In the

case, in particular, of *general insurance contracts* and *pure protection contracts*, the existence or otherwise of rights under such policies may be relevant to whether a *person* is carrying on *insurance mediation activities*.

5.3.11G A *person* may also have rights or interests in a *life policy* where he is not a *policyholder*, but this will again depend on the terms of the individual *policy*.

5.4. The business test

5.4.1G A *person* will only need *authorisation* or exemption if he is carrying on a *regulated activity* 'by way of business' (see section 22 of the *Act* (Regulated Activities)).

5.4.2G There is power in the *Act* for the Treasury to specify the circumstances in which a *person* is or is not to be regarded as carrying on *regulated activities* by way of business. The *Business Order* has been made using this power (partly reflecting differences in the nature of the different activities). As such, the business test for *insurance mediation activity* is distinguished from the standard test for 'investment business' in article 3 of the *Business Order*. Under article 3(4) of the *Business Order*, a *person* is not to be regarded as carrying on by way of business any *insurance mediation activity* unless he takes up or pursues that activity for remuneration. Accordingly, there are two principal elements to the business test in the case of *insurance mediation activities*:

(1) does a *person* receive remuneration for these activities?

(2) if so, does he take up or pursue these activities by way of business?

5.4.3G As regards *AUTH* App 5.4.2G(1), the *Business Order* does not provide a definition of 'remuneration', but, in the *FSA*'s view, it has a broad meaning and covers both monetary and non-monetary rewards. This is regardless of who makes them. For example, where a *person* pays discounted premiums for his own insurance needs in return for bringing other business to an *insurance undertaking*, the discount would amount to remuneration for the purposes of the *Business Order*. Remuneration can also take the form of an economic benefit which the *person* expects to receive as a result of carrying on *insurance mediation activities*. In the *FSA*'s view, the remuneration does not have to be provided or identified separately from remuneration for other goods or services provided. Nor is there a minimum level of remuneration.

5.4.4G As regards *AUTH* App 5.4.2G(2), in the *FSA*'s view, for a *person* to take up or pursue *insurance mediation activity* by way of business, he will usually need to be carrying on those activities with a degree of regularity. The *person* will also usually need to be carrying on the activities for commercial purposes. That is to say, he will normally be expecting to gain a direct financial benefit of some kind. Activities carried on out of friendship or for altruistic purposes will not normally amount to a business. However, in the *FSA*'s view:

- (1) it is not necessarily the case that services provided free of charge will not amount to a business; for example, advice (including advice available on a website) may be provided free of charge to potential *policyholders* but in the course of a business funded by commission payments; and
- (2) the 'by way of business' test may very occasionally be satisfied by an activity undertaken on an isolated occasion (provided that the activity would be regarded as done 'by way of business' in other respects, for example, because of the size of reward received or its relevance to other business activities).

5.4.5G It follows that whether or not any particular *person* is acting 'by way of business' for these purposes will depend on his individual circumstances. However, a typical example of where the applicable business test would be likely to be satisfied by someone whose main business is not *insurance mediation activities*, is where a *person* recommends or arranges specific insurance *policies* in the course of carrying on that other business and receives a fee or commission for doing so.

5.4.6G Some typical examples of where the business test is unlikely to be satisfied, assuming that there is no direct financial benefit to the arranger, include:

- (1) arrangements which are carried out by a *person* for himself, or for members of his family;
- (2) where employers provide insurance benefits for staff;
- (3) where affinity groups or clubs set up insurance benefits for members.

5.4.7G *AUTH* App 5.4.8G contains a table that summarises the main issues surrounding the business test as applied to *insurance mediation activities* and that may assist *persons* to determine whether they will need *authorisation* or exemption. The approach taken in the table involves identifying factors that, in the *FSA's* view, are likely to play a part in the analysis. Indicators are then given as to the significance of each factor to the *person's* circumstances. By analysing the indicators as a whole, a picture can be formed of the likely overall position. The table provides separate indicators for the two elements of remuneration and by way of business. As a *person* has to satisfy both elements, a clear overall indication against either element being satisfied should mean that the test is failed. This approach cannot be expected to provide a clear conclusion for everyone. But it should enable *persons* to assess the relevant aspects of their activities and to identify where changes could, if necessary, be made so as to make their position clearer. The *person* to whom the indicators are applied is referred to in the table as 'P'.

5.4.8G Table: Carrying on insurance mediation activities 'for remuneration' and 'by way of business'

Carrying on insurance mediation activities 'for remuneration' and 'by way of business'
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'For remuneration'		
Factor	Indicators that P <u>does not</u> carry on activities "for remuneration"	Indicators that P <u>does</u> carry on activities for "for remuneration"
Direct remuneration, whether received from the customer or the insurer/broker (cash or benefits in kind such as tickets to the opera, a reduction in other insurance premiums, a remission of a debt or any other benefit capable of being measured in money's worth)	P does not receive any direct remuneration specifically identified as a reward for his carrying on <i>insurance mediation activities</i> .	P receives direct remuneration specifically identified as being a reward for providing insurance mediation services.
Indirect remuneration (such as any form of economic benefit as may be explicitly or implicitly agreed between P and the insurer/broker or P's customer – including, for example, through the acceptance of P's terms and conditions or mutual recognition of the economic benefit that is likely to accrue to P). An indirect economic benefit can include expectation of making a profit of some kind as a result of carrying on <i>insurance mediation activities</i> as part of other services.	P does not obtain any form of indirect remuneration through an economic benefit other than one which is not likely to have a material effect on P's ability to make a profit from his other activities.	P obtains an economic benefit that: (a) is explicitly or implicitly agreed between P and the insurer/broker or P's customer; and (b) has the potential to go beyond mere cost recovery through fees or other benefits received for providing a package of services that includes <i>insurance mediation activities</i> but where no particular part of the fees is attributable to <i>insurance mediation activities</i> . This could include where <i>insurance mediation activities</i> are likely to: <ul style="list-style-type: none"> <li>• play a material part in the success of P's other business activities or in P's ability to make a profit from them; or</li> </ul>



		<ul style="list-style-type: none"> <li>• provide P with a materially increased opportunity to provide other goods or services; or</li> <li>• be a major selling point for P's other business activities; or</li> <li>• be essential for P to provide other goods or services.</li> </ul> <p>P charges his customers a greater amount for other goods or services than would be the case if P were not also carrying on <i>insurance mediation activities</i> for those customers and this:</p> <ul style="list-style-type: none"> <li>• is explicitly or implicitly agreed between P and the insurer/broker or P's customer; and</li> <li>• has the potential to go beyond mere cost recovery.</li> </ul>
Recovery of costs	P receives no benefits of any kind (direct or indirect) in respect of his <i>insurance mediation activities</i> beyond the reimbursement of his actual costs incurred in carrying on the activity (including receipt by P of a sum equal to the insurance premium that P is to pass on to the <i>insurer</i> or broker).	P receives benefits of any kind (direct or indirect) in respect of his <i>insurance mediation activities</i> which go beyond the reimbursement of his actual costs incurred in carrying on the activity.
"By way of business"		

Factor	Indicators that P <u>does not</u> carry on activities "by way of business"	Indicators that P <u>does</u> carry on activities "by way of business"
Regularity/ frequency	<p>Involvement is one-off or infrequent (for instance, once or twice a year) provided that the transaction(s) is not of such size and importance that it is essential to the success of P's other business activities.</p> <p>Transactions do not result from formal arrangements (for instance, occasional involvement purely as a result of an unsolicited approach).</p>	<p>Involvement is frequent (for instance, once a week).</p> <p>Involvement is infrequent but the transactions are of such size or importance that they are essential to the success of P's other business activities.</p> <p>P has formal arrangements which envisage transactions taking place on a regular basis over time (whether or not such transactions turn out in practice to be regular).</p>
Holding out	P does not hold himself out as providing a professional service that includes <i>insurance mediation activities</i> (by professional is meant not the services of a layman).	P holds himself out as providing a professional service that includes <i>insurance mediation activities</i> .
Relevance to other activities/ business	<p><i>Insurance mediation activities:</i></p> <ul style="list-style-type: none"> <li>• have no relevance to P's other activities; or</li> <li>• have some relevance but could easily be ceased without causing P any difficulty in carrying on his main activities; or</li> </ul> <p>would be unlikely to result in a material reduction in income from P's main</p>	<p><i>Insurance mediation activities:</i></p> <ul style="list-style-type: none"> <li>• are essential to P in carrying on his main activities; or</li> <li>• would cause a material disruption to P carrying on his main activities if ceased; or</li> <li>• would be likely to reduce P's income by a material amount.</li> </ul>

	activities if ceased.	
Commercial benefit	<p>P receives no direct or indirect pecuniary or economic benefit.</p> <p>P is a layman and acting in that capacity.</p> <p>P would not obtain materially less income from his main activities if they did not include <i>insurance mediation activities</i>.</p>	<p>P receives a direct or indirect pecuniary or economic benefit from carrying on <i>insurance mediation activities</i> – such as a fee, a benefit in kind or the likelihood of materially enhanced sales of other goods or services that P provides.</p> <p>P would obtain materially less income from his main activities if they did not include <i>insurance mediation activities</i>.</p>

5.5. The regulated activities: dealing in contracts as agent

5.5.1G Article 21 of the *Regulated Activities Order* (Dealing in investments as agent) makes dealing in *contracts of insurance* as agent a *regulated activity*. The activity is defined in terms of *buying, selling*, subscribing for or underwriting contracts as agent, that is, on behalf of another. Examples include:

- (1) where an intermediary, by accepting on the *insurance undertaking's* behalf to provide the insurance, commits an *insurance undertaking* to provide insurance for a prospective *policyholder*; or
- (2) where the intermediary agrees, on behalf of a prospective *policyholder*, to *buy* an insurance *policy*.

5.5.2G Intermediaries with delegated authority to bind *insurance undertakings* are likely to be *dealing in investments as agent*. It should be noted, in particular, that this is a *regulated activity*:

- (1) whether or not any advice is given (see *AUTH App 5.8* (The regulated activities: advising on contracts of insurance)); and
- (2) whether or not the intermediary deals through an *authorised person* (for example, where he instructs another agent who is an *authorised person* to enter into a *contract of insurance* on his *client's* behalf).

5.5.3G There are also certain exclusions which are relevant to whether a *person* is carrying on the activity of *dealing in investments as agent* (see *AUTH App 5.11* (Other aspects of exclusions)).

- 5.6 The regulated activities: arranging deals in, and making arrangements with a view to transactions in, contracts of insurance
- 5.6.1G Article 25 of the *Regulated Activities Order* (Arranging deals in investments) describes two types of *regulated activities* concerned with arranging deals in respect of *contracts of insurance*. These are:
- (1) *arranging (bringing about) deals in investments* (article 25(1) (Arranging deals in investments));
  - (2) *making arrangements with a view to transactions in investments* (article 25(2) (Arranging deals in investments));
- Article 25(1): arranging (bringing about) deals in investments
- 5.6.2G The activity in article 25(1) is carried on only if the arrangements bring about, or would bring about, the transaction to which the arrangement relates. This is because of the exclusion in article 26 of the *Regulated Activities Order* (Arrangements not causing a deal). Article 26 excludes from article 25(1) arrangements which do not bring about or would not bring about the transaction to which the arrangements relate. In the *FSA*'s view a *person* would bring about a *contract of insurance* if his involvement in the chain of events leading to the *contract of insurance* were important enough that, without it, there would be no *policy*. Examples of this type of activity would include negotiating the terms of the *contract of insurance* on behalf of the *customer* with the *insurance undertaking* and vice versa, or assisting in the completion of a proposal form and sending it to the *insurance undertaking*. Other examples include where an *insurance undertaking* enters into a *contract of insurance* as principal or an intermediary enters into a *contract of insurance* as agent.
- Article 25(2): making arrangements with a view to transactions in investments
- 5.6.3G The activity within article 25(2) contrasts with article 25(1) in that it is not limited by the requirement that the arrangements would bring about the transaction to which they relate.
- 5.6.4G Article 25(2) may, for instance, include activities of *persons* who help potential *policyholders* fill in or check application forms in the context of ongoing arrangements between these *persons* and *insurance undertakings*. A further example of this activity would be a *person* introducing *customers* to an intermediary either for advice or to help arrange an insurance *policy*. The introduction might be oral or written. By contrast, the *FSA* considers that a mere passive display of literature advertising insurance (for example, leaving leaflets advertising insurance in a dentist's or vet's waiting room and doing no more) would not amount to the article 25(2) activity.
- Exclusion: article 72C (Provision of information on an incidental basis)
- 5.6.5G The *Regulated Activities Order* provides an important potential exclusion, however, for *persons* whose principal business is other than *insurance mediation activities*.

- 5.6.6G In broad terms, article 72C of the *Regulated Activities Order* excludes from the activities of *arranging and assisting in the administration and performance of a contract of insurance*:
- (1) activities that consist of the provision of information to the *policyholder* or potential *policyholder*;
  - (2) by a *person* carrying on any profession or business which does not otherwise consist of *regulated activities*;
  - (3) if the provision of information may reasonably be regarded as being incidental to that profession or business.
- 5.6.7G In the *FSA's* view, 'incidental' in this context means that the activity must arise out of, be complementary to or otherwise be sufficiently closely connected with the profession or business. In other words, there must be an inherent link between the activity and the firm's main business. For example, introducing dental insurance may be incidental to a dentist's activities; introducing pet insurance would not be incidental to his activities. In addition, to be considered 'incidental', in the *FSA's* view, the activity must not amount to the carrying on of a business in its own right.
- 5.6.8G This exclusion applies to a *person* whose profession or business does not otherwise consist of *regulated activities*. In the *FSA's* view, the fact that a *person* may carry on *regulated activities* in the course of the carrying on of a profession or business does not, of itself, mean that the profession or business consists of *regulated activities*. This is provided that the main focus of the profession or business does not involve *regulated activities* and that the *regulated activities* that are carried on arise in a way that is incidental and complementary to the carrying on of the profession or business. So, the exclusion may be of relevance to *exempt professional firms*. It might also, for example, be relied on by doctors, vets and dentists as well as many businesses in the non-financial sector, even if they have *permission* to carry on *regulated activities* or are *appointed representatives*. This is assuming that their activities for which they are seeking to use the exclusion in article 72C are limited to providing information in a way which is incidental to their main profession or business. The exclusion only extends to information given to the *policyholder* or potential *policyholder* and not to the *insurance undertaking*. An intermediary who forwards a proposal form to an *insurance undertaking* would not be able to take the benefit of the exclusion. Similarly, where a *person* does more than provide information (for example, by helping a potential *policyholder* fill in an application form), he cannot take the benefit of this exclusion. Nor does it cover the activity of advising a customer under article 53 of the *Regulated Activities Order* (Advising on investments).
- 5.6.9G The exclusion will be of assistance to introducers who would otherwise be carrying on the *regulated activity of making arrangements with a view to transactions in investments* (assuming, as mentioned in *AUTH App 5.6.8G*, that they provide information only to *policyholders* or potential *policyholders*, and not to the intermediary or *insurance undertaking* to whom they introduce these *policyholders* or potential *policyholders*). In order to assist such *introducers* determine whether or not they are likely to

require *authorisation*, a simplified flowchart is included in *AUTH* App 5.15.6G (Flow chart: introducers). Introducers may also find the *guidance* at *AUTH* App 5.9.2G (The regulated activities: agreeing to carry on a regulated activity) helpful. *AUTH* App 5.6.17G (Exclusion from article 25(2) for introducing) has *guidance* to assist *persons* determine whether their introducing activities amount to *making arrangements with a view to transactions in investments*.

Exclusion from article 25(2): arrangements enabling parties to communicate

5.6.10G Article 27 of the *Regulated Activities Order* (Enabling parties to communicate) contains an exclusion that applies to arrangements which might otherwise bring within article 25(2) those who merely provide the means by which one party to a transaction (or potential transaction) is able to communicate with other parties. Simply providing the means by which parties to a transaction (or potential transaction) are able to communicate with each other is excluded from article 25(2) only. This will ensure that *persons* such as internet service providers or telecommunications networks are excluded if all they do is provide communication facilities (and these would otherwise be considered to fall within article 25(2)).

5.6.11G In the *FSA*'s view, the crucial element of the exclusion in article 27 is the inclusion of the word 'merely'. When a publisher, broadcaster or internet website operator goes beyond what is necessary for him to provide his service of publishing, broadcasting or otherwise facilitating the issue of promotions, he may well bring himself within the scope of article 25(2). Further detailed *guidance* relating to the scope of the exclusion in article 27 is contained in *AUTH* 2.8.6G(2) (Arranging deals in investments) and *AUTH* App 1.32.6G to *AUTH* App 1.32.11G (Arranging deals in investments).

Exclusion from article 25(2): transactions to which the arranger is a party

5.6.12G Article 28 of the *Regulated Activities Order* (Arranging transactions to which the arranger is a party) excludes from the *regulated activities* in article 25(1) and 25(2) arrangements made for or with a view to *contracts of insurance* when:

- (1) the *person* (P) making the arrangements is the only *policyholder*; or
- (2) P, as a result of the transaction, would become the only *policyholder*.

5.6.13G Market makers in traded endowment policies may be able to rely on this exclusion to avoid the need to be *authorised*. They must ensure, however, that where they are carrying on the *regulated activity* of *dealing in investments as principal* (article 14) they are also able to rely on the exclusions in articles 15 or 16 (see the *guidance* in *AUTH* 2.8.4G (Dealing in investments as principal)).

5.6.14G *Insurance undertakings* do not fall within the terms of this exclusion and so will be *arranging contracts of insurance*, in addition to *effecting and carrying out contract of insurance*.

5.6.15G In some cases, a *person* may make arrangements to enter into a *contract of insurance* as *policyholder* on its own behalf and also arrange that another

*person* become a *policyholder* under the same *contract of insurance*. If so, the *person* should be aware that the effect of the narrower exclusion in article 28 as part of implementation of the *IMD* is that he may be *arranging* on behalf of the other *policyholder*. This may be relevant, for example, to a *company* which arranges insurance for itself (not *arranging*) as well as other *companies* in a *group* or loan syndicate (potentially *arranging*).

- 5.6.16G The restriction in the scope of article 28 raises an issue where there is a trust with co-trustees, where each trustee will be a *policyholder* with equal rights and obligations. If the activities of one of the trustees include *arranging* in respect of *contracts of insurance*, that trustee could be viewed as *arranging* on behalf of his co-trustees who will also be *policyholders*. Similar issues also arise in respect of trustees *assisting in the administration and performance of a contract of insurance*. The *FSA* is of the view, however, that trustees should not be regarded as carrying on *regulated activities* where they are acting as joint *policyholders* in *arranging* or *assisting in the administration and performance of a contract of insurance*. In this respect, trustees differ from *policyholders* under a group policy, where each *person* covered under the group policy may make claims on the policy in relation to his own risks. In that situation, a *policyholder* who is providing services to other *policyholders* of *arranging* or *assisting in the administration and performance of a contract of insurance* will be carrying on a *regulated activity*.

Exclusion from article 25(2) for introducing

- 5.6.17 G Article 33 of the *Regulated Activities Order* (Introducing) excludes arrangements which would otherwise fall under article 25(2) where:
- (1) they are arrangements under which *persons* will be introduced to another *person*;
  - (2) the *person* to whom introductions are to be made is :
    - (a) an *authorised person*; or
    - (b) an *exempt person* acting in the course of business comprising a *regulated activity* in relation to which he is exempt; or
    - (c) a *person* who is not unlawfully carrying on *regulated activities* in the *United Kingdom* and whose ordinary business involves him in engaging in certain activities; and
  - (3) the introduction is made with a view to the provision of independent advice or the independent exercise of discretion in relation to *investments* generally or in relation to any class of *investments* to which the arrangements relate;
  - (4) the arrangements do not relate to transactions relating to *contracts of insurance*.

- 5.6.18 G The effect of *AUTH* App 5.6.17G(4) is that some *persons* who, in making introductions, are *making arrangements with a view to transactions in*

*investments* under article 25(2) of the *Regulated Activities Order*, cannot use the introducing exclusion. This is if, in general terms, the arrangements for making introductions relate to *contracts of insurance* (AUTH App 5.6.19G has further *guidance* on when arrangements for introductions may be regarded as relating to *contracts of insurance*). However, this does not mean that all introducers whose introductions relate directly or indirectly to *contracts of insurance* will necessarily require *authorisation* if they cannot use the exclusion in article 72C of the *Regulated Activities Order* for merely passing information. For this to be the case, a *person* must first be carrying on the business of *making arrangements with a view to transactions in investments*. In the FSA's view, the following points will be relevant in determining whether this is the case.

- (1) Article 25(2) applies to ongoing arrangements made with a view to transactions taking place from time to time as a result of *persons* having taken part in the arrangements. So, they will not apply to one-off introductions or introductions that are not part of an ongoing pre-existing arrangement between introducer and introducee. An introducer who merely suggests to a *person* that he seeks advice or assistance from an *authorised person* or an *exempt person* with whom the introducer has no pre-existing agreement that anticipates introductions will be made, will not be making arrangements at all. He will simply be offering general advice or information.
- (2) The purpose of the arrangements must be for the *person* who is introduced to, in general terms, enter into a transaction to *buy* or *sell securities* or *relevant investments*. So, arrangements for introducing *persons* for advice only will not be caught (for example, introductions to a financial planner or to the publisher of an investment newsletter). In other cases, it may be likely that transactions will be entered into following the provision of advice. Provided the introducer is completely indifferent as to whether or not a *contract of insurance* may ultimately be bought (or sold) as a result of the advice given to the *person* he has introduced, the introducer will not be *making arrangements with a view to transactions in investments*. This is likely to be the case where the introducer does not receive any pecuniary reward that is linked to the volume of business done as a result of his introductions.

5.6.19G Where a person is *making arrangements with a view to transactions in investments* by way of making introductions, and he is not completely indifferent to whether or not transactions may result, it may still be the case that the exclusion in article 33 will apply. In the FSA's view, this is where:

- (1) the introduction is for independent advice on *investments* generally; and
- (2) the introducer is indifferent as to whether or not a *contract of insurance* may ultimately be bought (or sold) rather than any other type of *investment*.



This is because the arrangements for making introductions do not specifically relate to a *contract of insurance* or to any other type of *investment* but to *investments* generally. Whether or not a *person* is making arrangements for introductions for the purpose of the provision of independent advice on *investments* generally will depend on the facts in any particular case. But, in the *FSA's* view, it is very unlikely that article 33 could apply where introductions are made to a *person* for the purposes of that *person* giving advice on and then *arranging general insurance*.

5.6.20G The table in *AUTH* App 5.6.21G has examples of the application of article 33 to arrangements for making introductions.

5.6.21G Table: application of article 33 to arrangements for making introductions. This table belongs to *AUTH* App 5.6.20G.



	Type of introduction	Applicability of exclusion
1	Introductions are purely for the purpose of the provision of independent advice - Introducer is completely indifferent to whether or not transactions take place after advice has been given.	Exclusion not relevant as introducer is not <i>arranging</i> under article 25(2).
2	Introduction is one-off or otherwise not part of pre-existing ongoing arrangements that envisage such introductions being made.	Exclusion not relevant as introducer is not <i>arranging</i> under article 25(2).
3	Introducer is not indifferent to whether or not transactions take place after advice has been given, but is indifferent to whether or not the transactions may involve a <i>contract of insurance</i> .	Exclusion will be available provided the introduction was made with a view to the provision of independent advice on <i>investments</i> generally.
4	Introducer is not indifferent to whether or not transactions take place after advice has been given (for example, because he expects to receive a percentage of the commission), and introductions specifically relate to <i>contracts of insurance</i> .	Exclusion is not available. If introducer is an <i>unauthorised person</i> , he will need <i>authorisation</i> or exemption as an <i>appointed representative</i> . If introducer is an <i>authorised person</i> (such as an IFA introducing to a <i>general insurance</i> broker), he will need to vary his <i>Part IV permission</i> accordingly. If introducer is an <i>appointed representative</i> , he will need to ensure that his agreement covers making such

arrangements.

Exclusion from article 25(2): arrangements for the provision of finance

5.6.22G An *unauthorised person* who makes arrangements with a view to a *person* who participates in the arrangements *buying or selling contracts of insurance* may be excluded from article 25(2) by article 32 of the *Regulated Activities Order* (Provision of finance). This is provided the sole purpose of the arrangements is the provision of finance to enable the *person* to *buy the contract of insurance*. Premium finance companies may be able to rely on this exclusion provided the arrangements they put in place, taken as a whole, have as their sole purpose the provision of finance to fund premiums.

Other exclusions

5.6.23G The *Regulated Activities Order* contains some other exclusions which have the effect of narrowing or limiting the application of *regulated activities* within article 25 by preventing certain activities from amounting to *regulated activities*. These are referred to in *AUTH App 5.11.8G* (Exclusions applying to more than one regulated activity).

5.7. The regulated activities: assisting in the administration and performance of a contract of insurance

5.7.1G The *regulated activity of assisting in the administration and performance of a contract of insurance* (article 39A) relates, in broad terms, to activities carried on by intermediaries after the conclusion of a *contract of insurance* and for or on behalf of *policyholders*, in particular in the event of a claim. Loss assessors acting on behalf of *policyholders* in the event of a claim are, therefore, likely in many cases to be carrying on this *regulated activity*. By contrast, claims management on behalf of certain insurers is not a *regulated activity* (see *AUTH App 5.7.7G* (Exclusions)).

5.7.2G Neither assisting in the administration nor assisting in the performance of a contract alone will fall within this activity. Generally, an activity will either amount to assisting in the administration or assisting in the performance but not both. Occasionally, however, an activity may amount to both *assisting in the administration and performance of a contract of insurance*. For example, where a *person* assists a claimant in filling in a claims form, in the *FSA's* view this amounts to assisting in the administration of a *contract of insurance*. In some instances, however, this may also amount to assisting in the performance of a *contract of insurance*. In the *FSA's* view, an example of when a *person* may be assisting in the performance of a contract is where a *person* fills in the whole or a significant part of a claims form on behalf of a claimant. This is because, by helping complete a claims form, a *person* may be assisting the *policyholder* to perform his contractual obligation to notify the *insurance undertaking* in the event of a claim and provide details of the claim in the manner and form required by the contract.

5.7.3G Put another way, where an intermediary's assistance in filling in a claims form is material to whether performance takes place of the contractual

obligation to notify claims, it is more likely to amount to *assisting in the administration and performance of a contract of insurance*. Conversely, in the FSA's view, a *person* who merely gives pointers about how to fill in the claims form or merely supplies information in support of a claim will not be assisting in the performance of a *contract of insurance*. Instead, the *person* will only be facilitating rather than assisting in the performance of a *contract of insurance*.

5.7.4G More generally, an example of an activity that, in the FSA's view, is likely to amount to assisting a *policyholder* in both the administration and the performance of a *contract of insurance* is notifying a claim under a *policy* and then providing evidence in support of the claim, or helping negotiate its settlement on the *policyholder's* behalf. Notifying an *insurance undertaking* of a claim assists the *policyholder* in discharging his contractual obligation to do so (assisting in the performance); providing evidence in support of the claim or negotiating its settlement assists management of the claim (assisting in the administration).

5.7.5G On the other hand, where a *person* does no more than advise a *policyholder* generally about making a claim or provide evidence in support of a claim, this is unlikely to amount to both assisting in the administration and performance. Similarly, the mere collection of premiums from *policyholders* is unlikely, without more, to amount to *assisting in the administration and performance of a contract of insurance*. The collection of premiums from customers or clients at the pre-contract stage, however, may amount to *arranging* (see example in AUTH App 5.15.4G (Types of activity – are they regulated activities and, if so, why?)).

5.7.6G Where a *person* receives funds on behalf of a *policyholder* in settlement of a claim, in the FSA's view, the act of receipt is likely to amount to assisting in the performance of a contract. By giving valid receipt, the *person* assists the *insurance undertaking* to discharge its contractual obligation to provide compensation to the *policyholder*. He may also be assisting the *policyholder* to discharge any obligations he may have under the contract to provide valid receipt of funds, upon settlement of a claim. Where a *person* provides valid receipt for funds received on behalf of the *policyholder*, he is also likely to be assisting in the administration of a *contract of insurance* (for example, making prior arrangements relating to transmission and receipt of payment).

Exclusions

5.7.7G By article 39B of the *Regulated Activities Order* (Claims management on behalf of an insurer etc):

- (1) loss adjusting on behalf of a relevant insurer (see AUTH App 5.7.8G);
- (2) expert appraisal; and
- (3) managing claims for a relevant insurer;

are also excluded from the *regulated activity of assisting in the administration and performance of a contract of insurance*. This is where the activity is carried on in the course of carrying on any profession or business (see also *AUTH App 5.14 (Exemptions)*). In determining whether they are carrying on the *regulated activity of assisting in the administration and performance of a contract of insurance*, therefore, *persons* should consider whether they are acting on behalf of the relevant insurer and not the *policyholder*.

5.7.8G A 'relevant insurer' for the purposes of article 39B means:

- (1) an *authorised person* who has *permission* for *effecting and carrying out contracts of insurance*; or
- (2) a member of the Society of Lloyd's or the members of the Society of Lloyd's taken together; or
- (3) an *EEA firm* that is an *insurer*; or
- (4) a reinsurer, being a *person* whose main business consists of accepting risks ceded by a *person* falling under (1), (2) or (3) or a *person* who is established outside the *United Kingdom* and who carries on the activity of *effecting and carrying out contracts of insurance*.

So, a *person* whose activities are excluded under article 12 of the *Regulated Activities Order (Breakdown insurance)* will not be a relevant insurer for these purposes and any *person* who performs loss adjusting or claims management on behalf of such a *person* will not be able to use the exclusion in article 39B.

5.8. The regulated activities: advising on contracts of insurance

5.8.1G Article 53 of the *Regulated Activities Order (Advising on Investments)* makes advising on *contracts of insurance* a *regulated activity*. This covers advice which is both:

- (1) given to a *person* in his capacity as an insured or potential insured, or as agent for an insured or a potential insured; and
- (2) advice on the merits of the insured or his agent:
  - (a) *buying, selling*, subscribing for or underwriting a particular *contract of insurance*; or
  - (b) exercising any right conferred by a *contract of insurance* to *buy, sell*, subscribe for or underwrite a *contract of insurance*.

5.8.2G For advice to fall within article 53, it must:

- (1) relate to a particular *contract of insurance* (that is, one that a *person* may enter into);
- (2) be given to a *person* in his capacity as an investor or potential investor;

- (3) be advice (that is, not just information); and
- (4) relate to the merits of a *person buying, selling*, subscribing for or underwriting (or exercising any right to do so) a *contract of insurance* or rights to or interests in *life policies*.

5.8.3G Each of these aspects is considered in greater detail in the table in *AUTH* App 5.8.5G. Where an activity is identified as not amounting to *advising on investments* it could still form part of another *regulated activity*. This will depend upon whether a *person's* activities, viewed as a whole, amount to *arranging*. Additionally, it should be borne in mind that the provision of advice or information may involve the communication of a *financial promotion* (see *AUTH* App 1 (Financial promotion and related activities)).

Advice must relate to a particular contract of insurance

5.8.4G Advice about *contracts of insurance* will come within the *regulated activity* in article 53 of the *Regulated Activities Order* only if it relates to a particular *contract of insurance*. So, generic or general advice will not fall under article 53. In particular:

- (1) advice would come within article 53 if it took the form of a recommendation that a *person* should *buy* the ABC Insurers motor insurance;
- (2) advice would not relate to a particular contract if it consists of a recommendation only that a *person* should take out insurance of a particular class without identifying any particular *insurance undertaking*, or with ABC Insurers provided that the kind of insurance is not specified (either expressly or by implication): a recommendation only that a *person* should *buy* insurance from ABC Insurers could amount to advice if a specific insurance *policy* would be implied from the context;
- (3) the table in *AUTH* App 5.8.5G identifies several typical recommendations and indicates whether they will be regarded as advice under article 53.

5.8.5G Table: typical recommendations and whether they will be regulated as advice on *contracts of insurance* under article 53 of the *Regulated Activities Order*. This table belongs to *AUTH* App 5.8.4G

Recommendation	Regulated under article 53 or not?
I recommend you take the ABC Insurers motor insurance <i>policy</i>	Yes
I recommend that you take out the GHI Insurers life insurance <i>policy</i>	Yes
I recommend that you do not take out the ABC Insurers motor insurance <i>policy</i>	Yes

Recommendation	Regulated under article 53 or not?
I recommend that you do not take out the GHI Insurers life insurance <i>policy</i>	Yes
I recommend that you take out either the ABC Insurers motor insurance <i>policy</i> or the DEF Insurers motor insurance <i>policy</i>	Yes
I recommend that you take out either the GHI Insurers life insurance <i>policy</i> or the JKL Insurers life insurance <i>policy</i>	Yes
I recommend that you take out (or do not take out) insurance with ABC Insurers	Possibly (depending on whether or not the circumstances relating to the recommendation, including the range of possible products, is such that this amounts to an implied recommendation of a particular <i>policy</i> )
I recommend that you take out (or do not take out) contents insurance	No, unless a specific insurance policy is implied by the context
I recommend that you take out (or do not take out) life insurance	No, unless a specific insurance policy is implied by the context

Advice given to a person in his capacity as an investor or potential investor

5.8.6G For the purposes of article 53, advice must be given to a *person* in his capacity as an investor or potential investor (which, in the context of *contracts of insurance*, will mean as *policyholder* or potential *policyholder*). So, article 53 will not apply where advice is given to *persons* who receive it as:

- (1) an adviser who will use it only to inform advice given by him to others; or
- (2) a journalist or broadcaster who will use it only for journalistic purposes.

5.8.7G Advice will still be covered by article 53 even though it may not be given to any particular *policyholder* (for example, advice given in a periodical publication or on a website).

Advice or information

5.8.8G In the *FSA's* view, advice requires an element of opinion on the part of the adviser. In effect, it is a recommendation as to a course of action. Information, on the other hand, involves statements of facts or figures.

5.8.9G In general terms, simply giving information, without making any comment or value judgement on its relevance to decisions which a *person*

may make, is not advice. In this respect, it is irrelevant that a *person* may be providing information on a single *contract of insurance* or on two or more. This means that a *person* may provide information on a single *contract of insurance* without necessarily being regarded as giving advice on it. *AUTH* App 5.8.11G has *guidance* on the circumstances in which information can assume the form of advice.

5.8.10G In the case of article 53, information relating to *buying or selling contracts of insurance* may often involve one or more of the following:

- (1) an explanation of the terms and conditions of a *contract of insurance*, whether given orally or in writing or by providing leaflets and brochures;
- (2) a comparison of the features and benefits of one *contract of insurance* compared to another;
- (3) the production of pre-purchase questions for a *person* to use in order to exclude options that would fail to meet his requirements; such questions may often go on to identify a range of *contracts of insurance* with characteristics that appear to meet the *person's* requirements and to which he might wish to give detailed consideration (pre-purchase questioning is considered in more detail in *AUTH* App 5.8.15G to 5.8.19G (Pre-purchase questioning (including decision trees)));
- (4) tables that compare the costs and other features of different *contracts of insurance*;
- (5) leaflets or illustrations that help *persons* to decide which type of *contract of insurance* to take out;
- (6) the provision, in response to a request from a *person* who has identified the main features of the type of *contract of insurance* he seeks, of several leaflets together with an indication that all the *contracts of insurance* described in them have those features.

5.8.11G In the *FSA's* opinion, however, such information is likely to take on the nature of advice if the circumstances in which it is provided give it the force of a recommendation. Examples of situations where information provided by a *person* (P) might take the form of advice are given below.

- (1) P may provide information on a selected, rather than balanced and neutral, basis that would tend to influence the decision of a *person*. This may arise where P offers to provide information about *contracts of insurance* that contain features specified by the *person*, but then exercises discretion as to which complying *contract of insurance* to offer to that *person*.
- (2) P may, as a result of going through the sales process, discuss the merits of one *contract of insurance* over another, resulting in advice to enter into a particular one. In contrast, advice on how to complete an application form, without an explicit or implicit recommendation on the merits of *buying or selling the contract of insurance*, whilst 'advice' in the general sense of the word, is not, in the view of the *FSA*, advice within the meaning of article 53. Such advice may,

however, amount to *arranging* (for which see *AUTH* App 5.6.1G to 5.6.4G (The regulated activities: arranging deals in, and making arrangements with a view to transactions in, contracts of insurance)).

Advice must relate to the merits (of buying or selling a contract of insurance)

- 5.8.12G Advice under article 53 relates to the advantages and disadvantages of *buying, selling*, subscribing for or underwriting a particular *contract of insurance*. It is worth noting that, in this context, '*buying*' and '*selling*' are defined widely under article 3 of the *Regulated Activities Order* (Interpretation). '*Buying*' includes acquiring for valuable consideration, and '*selling*' includes surrendering, assigning or converting rights under a *contract of insurance*.
- 5.8.13G The requirements imposed by the *IMD* (see *AUTH* App 5.2.5G (Approach to implementation of the *IMD*) and the text of article 2.3 *IMD* in *AUTH* App 5.16.1G (Article 2.3 of the Insurance Mediation Directive)) are narrower than the scope of the *Regulated Activities Order* (see *AUTH* App 5.2.7G (Approach to implementation of the *IMD*)). This is that, unlike the *Regulated Activities Order*, they do not relate to the assignment of *contracts of insurance*. This is of relevance to, amongst others, *persons* involved in the 'second-hand' market for *contracts of insurance* such as traded endowment policies and certain viatical instruments (that is, arrangements by which a terminally ill person can obtain value from his *life policy*) (see also *AUTH* App 5.6.12G (Exclusion from article 25(2): transactions to which the arranger is a party). *Persons* advising on or arranging assignments of these *contracts of insurance* are therefore potentially carrying on *regulated activities* although they may be able to take the benefit of article 67 of the *Regulated Activities Order* (Activities carried on in the course of a profession or non-investment business) in certain circumstances (see *AUTH* App 5.11.9G to 5.11.12G (Activities carried on in the course of a profession or non-investment business)).
- 5.8.14G Generally speaking, advice on the merits of using a particular *insurance undertaking*, broker or adviser in their capacity as such, does not amount to advice for the purpose of article 53. It is not advice on the merits of *buying* or *selling* a particular *contract of insurance* (unless, in the circumstances, the advice amounts to an implied recommendation of a particular *policy*).

Pre-purchase questioning (including decision trees)

- 5.8.15G Pre-purchase questioning involves putting a sequence of questions in order to extract information from a *person* with a view to facilitating the selection by that *person* of a *contract of insurance* or other product that meets his needs. A decision tree is an example of pre-purchase questioning. The process of going through the questions will usually narrow down the range of options that are available.
- 5.8.16G A key issue for those *firms* proposing to use pre-purchase questioning is whether the specific questioning used may amount to advice. There are two main aspects:



- (1) advice must relate to a particular *contract of insurance* (see *AUTH* App 5.8.4G (Advice must relate to a particular contract of insurance)); and
- (2) the distinction between information and advice (see *AUTH* App 5.8.8G to *AUTH* App 5.8.11G (Advice or information)).

Whether or not pre-purchase questioning in any particular case is advising on *contracts of insurance* will depend on all the circumstances. The process may involve identifying one or more particular *contracts of insurance*. If so, to avoid advising on *contracts of insurance*, the critical factor is likely to be whether the process is limited to, and likely to be perceived by the *person* as, assisting the *person* to make his own choice of product which has particular features which the *person* regards as important. The questioner will need to avoid providing any judgement on the suitability of one or more products for that *person* and in this respect should have regard to the factors set out in *AUTH* App 5.8.2G to *AUTH* App 5.8.4 G (Advice must relate to a particular contract of insurance) and the table in *AUTH* App 5.8.5G. See also *AUTH* App 5.8.12G to *AUTH* App 5.8.14G (Advice must relate to the merits (of *buying* or *selling* a contract of insurance)) for other matters that may be relevant.

5.8.17G The potential for variation in the form, content and manner of pre-purchase questioning is considerable, but there are two broad types. The first type involves providing questions and answers which are confined to factual matters (for example, the amount of the cover). In the *FSA's* view, this does not itself amount to advising on *contracts of insurance*, if it involves the provision of information rather than advice. There are various possible scenarios, including the following:

- (1) the questioner may go on to identify one or more particular *contracts of insurance* which match features identified by the pre-purchase questioning; provided these are selected in a balanced and neutral way (for example, they identify all the matching *contracts of insurance* available without making a recommendation as to a particular one) this need not involve advising on *contracts of insurance*;
- (2) the questioner may go on to advise a *person* on the merits of one particular *contract of insurance* over another; this would be advising on *contracts of insurance*.

5.8.18G The second type of pre-purchase questioning involves providing questions and answers incorporating opinion, judgement or recommendation. There are various possible scenarios, including the following:

- (1) the pre-purchase questioning may not lead to the identification of any particular *contract of insurance*; in this case, the questioner has provided advice, but it is generic advice and does not amount to advising on *contracts of insurance*;
- (2) the pre-purchase questioning may lead to the identification of one or more particular *contracts of insurance*; the key issue then is whether the advice can be said to relate to a particular *contract of insurance* (see further *AUTH* App 5.8.4G (Advice must relate to a particular contract of insurance)).

5.8.19G In the case of *AUTH* App 5.8.18G(2) and similar scenarios, the *FSA* considers that it is necessary to look at the process and outcome of pre-purchase questioning as a whole. It may be that the element of advice incorporated in the questioning can properly be viewed as generic advice if it were considered in isolation. But although the actual advice may be generic, the process has ended in identifying one or more particular *contracts of insurance*. The combination of the generic advice and the identification of a particular or several particular *contracts of insurance* to which it leads may well, in the *FSA*'s view, cause the questioner to be advising on *contracts of insurance*. Factors that may be relevant in deciding whether the process involves advising on *contracts of insurance* may include:

- (1) any representations made by the questioner at the start of the questioning relating to the service he is to provide;
- (2) the context in which the questioning takes place;
- (3) the stage in the questioning at which the opinion is offered and is significant;
- (4) the role played by the questioner who guides a *person* through the pre-purchase questions;
- (5) the outcome of the questioning (whether particular *contracts of insurance* are highlighted, how many of them, who provides them, their relationship to the questioner and so on);
- (6) whether the pre-purchase questions and answers have been provided by, and are clearly the responsibility of, an unconnected third party, and all that the questioner has done is help the *person* understand what the questions or options are and how to determine which option applies to his particular circumstances.

Medium used to give advice

5.8.20G With the exception of:

- (1) periodicals, broadcasts and other news or information services (see *AUTH* App 5.8.24G to *AUTH* App 5.8.25G (Exclusion: periodical publications, broadcasts and web-sites)); and
- (2) situations involving an overseas element (see, generally, *AUTH* App 5.12 (Link between activities and the United Kingdom) and, in particular, *AUTH* App 5.12.8G (Where is insurance mediation carried on?));

the use of the medium itself to give advice should make no material difference to whether or not the advice is caught by article 53.

5.8.21G Advice can be provided in many ways including:

- (1) face to face;
- (2) orally to a group;
- (3) by telephone;

- (4) by correspondence (including e-mail);
- (5) in a publication, broadcast or web-site; and
- (6) through the provision of an interactive software system.

5.8.22G Taking electronic commerce as an example, the use of electronic decision trees does not present any novel problem. The same principles apply as with a paper version (see *AUTH* App 5.8.15G to *AUTH* App 5.8.19G (Pre-purchase questioning (including decision trees))).

5.8.23G Advice in publications, broadcasts and web-sites is subject to a special regime ( see *AUTH* App 5.8.24G (Exclusion: periodical publications, broadcasts and web-sites) and *AUTH* 7 (Periodical publications, news services and broadcasts: applications for certification)).

Exclusion: periodical publications, broadcasts and web-sites

5.8.24G An important exclusion from advising on *contracts of insurance* relates to advice given in periodical publications, regularly updated news and information services and broadcasts (article 54 of the *Regulated Activities Order* (Advice given in newspapers etc)). The exclusion applies if the principal purpose of the publication or service taken as a whole (including any advertising content) is neither to give advice of a kind mentioned in article 53 (Advising on investments) or article 53A (Advising on regulated mortgage activities) nor to lead or enable *persons* to *buy, sell*, subscribe for or underwrite *relevant investments* or, as borrower, to enter into or vary the terms of a *regulated mortgage contract*.

5.8.25G This is explained in greater detail, together with the provisions on the granting of certificates by the *FSA* on the application of the proprietor of a periodical publication or news or information service or broadcast, in *AUTH* 7 (Periodical publications, news services and broadcasts: applications for certification).

Other exclusions

5.8.26G The *Regulated Activities Order* contains other limited exclusions which have the effect of preventing certain activities from amounting to advice on *contracts of insurance*. These are referred to in *AUTH* App 5.11.8G (Exclusions applying to more than one regulated activity) to *AUTH* App 5.11.16G (Large risks).

5.9 The Regulated Activities: agreeing to carry on a regulated activity

5.9.1G Under article 64 of the *Regulated Activities Order* (Agreeing to carry on specified kinds of activity), in addition to the *regulated activities* of:

- (1) *dealing in investments as agent*;
- (2) *arranging (bringing about) deals in investments*;
- (3) *making arrangements with a view to transactions in investments*;
- (4) *assisting in the administration and performance of a contract of insurance*; and
- (5) *advising on investments*;

agreeing to do any of these things is itself a *regulated activity*. In the *FSA*'s opinion, this activity concerns the entering into of a legally binding agreement to provide the services to which the agreement relates. So, a *person* is not carrying on a *regulated activity* under article 64 merely because he makes an offer to do so.

5.9.2G To the extent that an exclusion applies in relation to a *regulated activity*, 'agreeing' to carry on an activity within the exclusion will not be a *regulated activity*. This is the effect of article 4(3) of the *Regulated Activities Order* (Specified activities: general). So, for example, a vet can, without carrying on a *regulated activity*, enter into an agreement with an *insurance undertaking* to distribute marketing literature provided that the vet can rely on the exclusion in article 72C (Provision of information on an incidental basis) in relation to the activity of distributing the literature (see also *AUTH* App 5.6.6G and *AUTH* App 5.6.9G (Exclusion: article 72C (Provision of information on an incidental basis))). However, to be able to rely on the exclusion in article 72C, the vet must not be viewed as providing information to the *insurance undertaking*. More specifically, an unauthorised *introducer* can enter into standing arrangements with *insurance undertakings* or brokers to make introductions, provided that these arrangements do not envisage subsequent provision of information to these *insurance undertakings* or brokers with a view to *arranging (bringing about) deals in investments* or *making arrangements with a view to transactions in investments*.

## 5.10 Renewals

5.10.1G It must be emphasised that activities which concern invitations to renew *policies* and the subsequent effecting of renewal of *policies* are likely to fall within *insurance mediation activity*. Those considering the need for *authorisation* or variation of their *permissions* will wish to consider whether a process of tacit renewal operates: that is, where a *policyholder* need take no action if he wishes to maintain his insurance cover by having his *policy* 'renewed'. This process will typically result in the issue of a new *contract of insurance*, not an extension of the period of the existing one. It may involve the activities of *advising on investments, arranging and dealing in investments as agent*. More specifically, preparing a 'tacit renewal' letter on behalf of an *insurance undertaking* is likely to amount to *arranging*. Where it contains a recommendation to renew existing cover this is likely to constitute *advising on investments* (under article 53 of the *Regulated Activities Order*. If the contract takes effect on the date stipulated in the renewal letter, a contract is concluded with the effect that the letter writer may be *dealing in investments as agent*. The process may also involve a regulated activity under article 64 (*Agreeing to carry on a regulated activity*).

## 5.11 Other aspects of exclusions

5.11.1G This part of the *guidance* deals with:

- (1) exclusions which are disapplied where the *regulated activity* relates to *contracts of insurance*;
- (2) exclusions which are disapplied where a *person* carries on *insurance mediation*;
- (3) the following exclusions applying to more than one *regulated activity*:
  - (a) activities carried on in the course of a profession or non-investment business (article 67 (Activities carried on in the course of a profession or non-investment business));
  - (b) activities carried on by a provider of relevant goods or services (article 72B (Activities carried on by a provider of relevant goods or services)); and
  - (c) *large risks* (article 72D (Large risks contracts where risk situated outside the EEA)).

5.11.2G There are a number of 'pre-*IMD*' exclusions that have the effect of restricting the scope of the *regulated activities* referred to in this *guidance*. Several of these are disapplied or modified as part of implementation of the *IMD*.

Exclusions disapplied where activities relate to contracts of insurance

5.11.3G The exclusions outlined in (1) to (7) have been available to intermediaries (and in some cases *insurance undertakings*) acting in connection with *life policies*. In essence, however, from 14 January 2005 the following exclusions do not apply if they concern transactions relating to *contracts of insurance*:

- (1) *dealing in investments as agent* with or through *authorised persons* (article 22 of the *Regulated Activities Order* (Deals with or through authorised persons));
- (2) *arranging* transactions to which the *arranger* is to be a party, where the *arranger* enters into or is to enter into the transaction:
  - a) as agent for another *person*; or
  - b) as *principal*, unless the *arranger* is the only *policyholder* or will, as a result of the transaction, become the only *policyholder* (article 28 (Arranging transactions to which the arranger is a party));
- (3) *arranging deals* with or through *authorised persons* (article 29 (Arranging deals with or through authorised persons));
- (4) *introducing* (article 33 (Introducing));
- (5) activities carried on in connection with the sale of goods and supply of services (article 68 (Activities carried on in connection with the sale of goods and supply of services));
- (6) *groups and joint enterprises* (article 69 (Groups and joint enterprises)) (see *AUTH App 5.11.6G*); and

- (7) activities carried on in connection with the sale of a *body corporate* (article 70 (Activities carried on in connection with the sale of a body corporate)).

5.11.4G It follows from the restrictions placed on the exclusions listed in *AUTH* App 5.11.3G that, as of 14 January 2005:

- (1) *unauthorised persons* who:
- (a) introduce clients or customers to an independent financial adviser with a view to a transaction;
  - (b) deal as agent on behalf of their clients or customers with or through an *authorised person*; or
  - (c) arrange for their clients or customers to enter into a transaction with or through an *authorised person*,
- will not be able to rely on articles 29 or 33 to avoid the need for *authorisation* where the transaction relates to a *contract of insurance*;
- (2) *unauthorised persons* may, however, be able to rely on the exclusion for the provision of information on an incidental basis in article 72C to continue to avoid the need for *authorisation* (see *AUTH* App 5.6.5G to *AUTH* App 5.6.9G (Exclusion: article 72C (Provision of information on an incidental basis)));
- (3) *authorised persons* who themselves introduce clients or customers to others for the purposes of *buying* or *selling* any kind of *contract of insurance* are likely to require a variation of their *Part IV permission*, as neither article 33 nor generally, article 72C (see *AUTH* App 5.6.5G to *AUTH* App 5.6.9G (Exclusion: article 72C (Provision of information on an incidental basis))) will apply where this activity amounts to *arranging*.

5.11.5G *Insurance undertakings* are referred to *PRU* 9.4 (Insurance undertakings and mortgage lenders using insurance or mortgage mediation services) as regards their obligations relating to the use of intermediaries generally.

5.11.6G The removal of the exclusion for *groups* and *joint enterprises* in article 69 of the *Regulated Activities Order* (Groups and joint enterprises) may have implications for *companies* providing services for:

- (1) other members of its *group*; or
- (2) other participants in a *joint enterprise* of which it is a participant.

Such *companies* might typically provide risk or treasury management or administration services which may include *regulated activities* relating to a *contract of insurance*. If so, such *companies* will need *authorisation* or exemption if they conduct the activities by way of business (see *AUTH* App 5.4 (The business test)). This is unless another exclusion applies.

Exclusions disapplied in connection with insurance mediation

5.11.7G Article 4(4A) of the *Regulated Activities Order* (Specified activities: general) disapplies certain exclusions where a *person*, for remuneration, takes up or pursues *insurance mediation* (as defined in article 2.3 of the

*IMD* (see *AUTH* App 5.2.5G (Approach to implementation of the *IMD*) and *AUTH* App 5.16.2 (Article 2.3 of the Insurance Mediation Directive)) in relation to a risk or commitment located in an *EEA* state. The relevant exclusions which are disapplied are:

- (1) arrangements in connection with lending on the security of insurance policies (article 30 of the *Regulated Activities Order* (Arranging transactions in connection with lending on the security of insurance policies));
- (2) activities carried on by trustees, nominees and personal representatives (article 66 (Trustees, nominees and personal representatives)); and
- (3) activities carried on in the course of a profession or non-investment business (article 67 (Activities carried on in the course of a profession or non-investment business)) (This exclusion is considered in further detail in *AUTH* App 5.11.9G to 5.11.12G (Activities carried on in the course of a profession or non-investment business)).

Exclusions applying to more than one regulated activity

5.11.8G Chapter XVII of the *Regulated Activities Order* (Exclusions applying to several specified kinds of activity) contains various exclusions applying to several kinds of activity. Three exclusions of relevance in relation to *contracts of insurance* are dealt with in this section and a fourth, *overseas persons*, in *AUTH* App 5.12 (Link between activities and the United Kingdom).

Activities carried on in the course of a profession or non-investment business

5.11.9G Article 67 excludes from the activities of *dealing as agent, arranging (bringing about) deals in investments, making arrangements with a view to transactions in investments* and *advising on investments*, any activity which:

- (1) is carried on in the course of carrying on any profession or business which does not otherwise consist of the carrying on of *regulated activities* in the *United Kingdom*; and
- (2) may reasonably be regarded as a necessary part of other services provided in the course of that profession or business.

In the *FSA*'s view, the fact that a *person* may carry on *regulated activities* in the course of the carrying on of a profession or business does not, of itself, mean that the profession or business consists of *regulated activities*. This is provided that the main focus of the profession or business does not involve *regulated activities* and that the *regulated activities* that are carried on arise in a way that is incidental and complementary to the carrying on of the profession or business.

5.11.10G Although the article 67 exclusion is disapplied (by article 4(4A) of the *Regulated Activities Order* (Specified investments: general)) when a *person* takes up or pursues *insurance mediation* or *reinsurance mediation* as defined by articles 2.3 and 2.5 of the *IMD*, there may be cases where a

*person* is not carrying on activities that amount to *insurance mediation*. For example, where a *person's* activities amount simply to the provision of information on an incidental basis in the context of another professional activity, these may fall outside the scope of article 2.3 *IMD* (see *AUTH* App 5.16.2G (Article 2.3 of the Insurance Mediation Directive)) and the exclusion in article 67 may then operate to exclude these activities. Also, it is possible that a professional *person's* activities may not amount to a *regulated activity* at all. For example, a doctor who provides a medical report to an *insurer* may be regarded as making arrangements with a view to providing an expert medical opinion rather than with a view to transactions in *contracts of insurance*. In such cases, article 67 will not be needed.

5.11.11G Article 67 may also apply to activities relating to assignments of insurance policies, as, in the *FSA's* view, article 2.3 of the *IMD* applies essentially to the creation of new *contracts of insurance* and not the assignment of rights under existing policies. As such, where a solicitor or licensed conveyancer arranges an assignment of a *contract of insurance*, the exclusion in article 67 remains of potential application. For similar reasons, trustees advising on or arranging assignments of *contracts of insurance* may, in certain circumstances, be able to rely on the exclusions in article 66 of the *Regulated Activities Order*.

5.11.12G For article 67 to apply in these cases, in addition to *AUTH* App 5.11.9G(1) and (2), the activity in question must not be remunerated separately from other services (article 67(2) of the *Regulated Activities Order*).

Activities carried on by a provider of relevant goods or services

5.11.13G Article 72B (see also *AUTH* App 5.3.7G (Connected contracts of insurance)) may be of relevance to *persons* who supply non-motor goods or provide services related to travel in the course of carrying on a profession or business which does not otherwise consist of carrying on *regulated activities*. In the *FSA's* view, the fact that a *person* may carry on *regulated activities* in the course of the carrying on of a profession or business does not, of itself, mean that the profession or business consists of *regulated activities*. This is provided that the main focus of the profession or business does not involve *regulated activities* and that the *regulated activities* that are carried on arise in a way that is incidental and complementary to the carrying on of the profession or business. For example, a travel agent might carry on *insurance mediation activities* in relation to some *contracts of insurance* that satisfy the conditions of the article 72B and some that do not. The former contracts will be excluded from regulation even though the travel agent must seek *authorisation* or become an *appointed representative* to be permitted to *sell* the latter contracts. The exclusion applies to *insurance mediation activities* when carried on in relation to 'connected contracts of insurance'. In broad terms, a 'connected contract of insurance' is a *contract of insurance* which:

- (1) is not a contract of long-term insurance (as defined by article 3 of the *Regulated Activities Order* (Interpretation));
- (2) has a total duration (including rights to renewal) of five years or less;



- (3) has an annual premium (or the equivalent of annual premium) of €500 or less;
- (4) covers the risk of:
  - (a) breakdown, loss of, or damage to, non-motor goods supplied by the provider; or
  - (b) damage to, or loss of, baggage and other risks linked to travel booked with the provider ('travel risks');
- (5) does not cover any liability risks (except, in the case of a contract which covers travel risks, where the cover is ancillary to the main cover provided by the contract);
- (6) is complementary to the non-motor goods being supplied or service being provided by the provider; and
- (7) is of such a nature that the only information that a *person* requires in order to carry on one of the *insurance mediation activities* is the cover provided by the contract.

5.11.14G In the *FSA's* view, the liability risks referred to in *AUTH* App 5.11.13G(5) cover risks in relation to liabilities that the *policyholder* might have to others (that is, third party claims). Many *policies* will provide this sort of cover and so fall outside the scope of the exclusion. For example, a *policy* that covers the cost of unauthorised calls made when a mobile telephone is stolen includes 'liability risks' and would not be a 'connected contract of insurance'. By contrast, travel *policies* which provide cover in respect of the *policyholder's* personal liability while travelling may fall within the exclusion by virtue of *AUTH* App 5.11.13G(5), where sold as part of a package by travel agents and other providers of services related to travel.

5.11.15G In the *FSA's* view, the condition in *AUTH* App 5.11.13G(7) is likely to be satisfied where the *insurance mediation activities* relate to a standard form *contract of insurance*, the terms of which (other than the cost of the premium) are not subject to negotiation.

#### Large risks

- 5.11.16G Article 72D (Large risks contracts where risk situated outside the EEA) provides an exclusion for large risks situated outside the *EEA*. Broadly speaking, these are risks relating to:
- (1) railway rolling stock, aircraft, ships, goods in transit, aircraft liability and shipping liability;
  - (2) credit and suretyship where relating to the *policyholder's* commercial or professional liability;
  - (3) risks relating to land vehicles, fire and natural forces, property damage, motor vehicle liability;
  - (4) certain financial loss where the *policyholder* is a business of a certain size.

For a fuller definition of *contracts of large risks* see the definition in the *Glossary*.

## 5.12 Link between activities and the United Kingdom

### Introduction

- 5.12.1G Section 19 of the *Act* (The general prohibition) provides that the requirement to be *authorised* under the *Act* only applies in relation to *regulated activities* which are carried on ‘in the *United Kingdom*’. In many cases, it will be quite straightforward to identify where an activity is carried on. But, when there is a cross-border element, for example because a *customer* is outside the *United Kingdom* or because some other element of the activity happens outside the *United Kingdom*, the question may need careful consideration. *AUTH* App 5.15.8G (Flow chart: am I carrying on regulated activities in the United Kingdom?) has a flow chart setting out the questions a *person* needs to consider in determining whether or not his *regulated activities* are carried on ‘in the *United Kingdom*’.
- 5.12.2G Even if a *person* concludes that he is not carrying on a *regulated activity* in the *United Kingdom*, he will need to ensure that he does not contravene other provisions of the *Act* that apply to *unauthorised persons*. These include the controls on *financial promotion* (section 21 (Financial promotion) of the *Act*) (see *AUTH* App 1 (Financial promotion and related activities)), and on giving the impression that a *person* is *authorised* (section 24 (False claims to be authorised or exempt)).
- 5.12.3G The table in *AUTH* App 5.12.4G is a very simplified summary of territorial issues relating to overseas insurance intermediaries carrying on the business of *insurance mediation activities* in or into the *United Kingdom* for remuneration.
- 5.12.4G Table: territorial issues relating to overseas insurance intermediaries carrying on insurance mediation activities in or into the United Kingdom

	Needs Part IV permission	Schedule 3 EEA passport rights available	Overseas persons exclusion available
Registered <i>EEA</i> -based intermediary with <i>UK</i> branch (registered office or head office in another <i>EEA State</i> )	No	Yes	No
Registered <i>EEA</i> -based intermediary with no <i>UK</i> branch providing <i>cross-border services</i>	No	Yes	Potentially available [see Note 1]
Third country intermediary operating from branch in <i>UK</i>	Yes	No	No
Third country intermediary providing services in (or into) <i>UK</i>	Yes unless <i>overseas persons</i>	No	Potentially available

	Needs Part IV permission	Schedule 3 EEA passport rights available	Overseas persons exclusion available
	exclusion applies		

Note 1. This does not, however, affect the *firm's authorisation* under Schedule 3 to the *Act* (see *AUTH* App 5.12.13G to *AUTH* App 5.12.14G (Passporting)).

Where are insurance mediation activities carried on?

- 5.12.5G *Persons carrying on insurance mediation activities* from a registered office or head office in the *United Kingdom* will clearly be carrying on *regulated activities* in the *United Kingdom*. However, a *person* may be considered to be carrying on *regulated activities* in the *United Kingdom* even where not carrying on the activity from a registered office or head office in the *United Kingdom*. This is explained further in *AUTH* App 5.12.5G to *AUTH* App 5.12.7G.
- 5.12.6G In determining the location of an activity, and hence whether it is carried on in the *United Kingdom*, various factors need to be taken into account in turn, notably:
- (1) section 418 of the *Act* (Carrying on regulated activities in the United Kingdom);
  - (2) the nature of the activity; and
  - (3) the *overseas persons* exclusion (see *AUTH* App 5.12.9G to *AUTH* App 5.12.10G (Overseas persons)).
- 5.12.7G Section 418 of the *Act* extends the meaning that ‘carry on regulated activity in the United Kingdom’ would normally have by setting out additional cases in which a *person* who would not otherwise be regarded as carrying on the activity in the *United Kingdom* is to be regarded as doing so. Each of the following cases thus amounts to carrying on a *regulated activity* in the *United Kingdom*:
- (1) where a *UK-based person* carries on a *regulated activity* in another *EEA State* in the exercise of rights under a *Single Market Directive*;
  - (2) where a *UK-based person* carries on a *regulated activity* and the day-to-day management of the activity is the responsibility of an establishment in the *United Kingdom*;
  - (3) where a *regulated activity* is carried on by a *person* who is not based in the *United Kingdom* but is carried on from an establishment maintained by him in the *United Kingdom*;
  - (4) where an *electronic commerce activity* is carried on with or for a *person* in an *EEA State* from an establishment in the *United Kingdom*.

In each of these cases it is irrelevant where the *person* with whom the activity is carried on is situated.

5.12.8G Otherwise, where the cases in *AUTH* App 5.12.7G (1) to (4) do not apply, it is necessary to consider further the nature of the activity in order to determine where *insurance mediation* is carried on. *Persons* that arrange *contracts of insurance* will usually be considered as carrying on the activity of *arranging* in the location where these activities take place. As for dealing activities, the location of the activities will depend on factors such as where the acceptance takes place, which in turn will depend on the method of communication used. In the case of advising, this is generally considered to take place where the advice is received.

Overseas persons

5.12.9G Article 72 of the *Regulated Activities Order* (Overseas persons) provides a potential exclusion for *persons* with no permanent place of business in the *United Kingdom* from which *regulated activities* are conducted or offers to conduct *regulated activities* are made. Where these *persons* carry on *insurance mediation activities* in the *United Kingdom*, they may be able to take advantage of the exclusions in article 72 of the *Regulated Activities Order*. In general terms, these apply where the *overseas person* either:

- (1) deals or arranges deals with or through *authorised* or exempt *persons* only; or
- (2) enters into deals with (or on behalf of) a *person* in the *United Kingdom* or gives advice on investments in the *United Kingdom*, in each case as a result of a 'legitimate approach'.

A 'legitimate approach', for the purposes of (2), is one that results from an unsolicited approach by a *person* (for example, a *customer*) or otherwise is a result of an approach by, or on behalf of, an *overseas person* which complies with the restriction on *financial promotion* under section 21 of the *Act* (see *AUTH* App 1.3.1G (Financial promotion)).

5.12.10G The *overseas person* exclusion is available to *persons* who do not have a permanent place of business in the *United Kingdom* and so is of relevance to third country intermediaries (that is, non *EEA*-based intermediaries) who carry on *insurance mediation activities* in, or into, the *United Kingdom* (for example with or through *authorised* insurance brokers and *insurance undertakings* operating in the Lloyd's market).

How should persons be authorised?

5.12.11G *UK*-based *persons* must obtain *Part IV permission* in relation to their *insurance mediation activities* in the *United Kingdom* as one of the following:

- (1) a *body corporate* whose registered office is situated in the *United Kingdom*;
- (2) a *partnership* or unincorporated association whose head office is situated in the *United Kingdom*;
- (3) an individual (that is, a sole trader) whose residence is situated in the *United Kingdom*.

The *United Kingdom* will, in each case, be the *Home State* for the purposes of the *IMD* for insurance or reinsurance intermediaries (see

further in connection with the *E-Commerce Directive* in *AUTH* App 5.12.15G to *AUTH* App 5.12.17G (E-Commerce Directive)).

5.12.12G Non-UK-based persons wishing to carry on *insurance mediation activities* in the *United Kingdom* must:

- (1) qualify for *authorisation* by exercising passport rights (see section 31 (Authorised persons) and schedule 3 (EEA passport rights) to the *Act* and *AUTH* App 5.12.13G to *AUTH* App 5.12.14G (Passporting)); or
- (2) make use of the *overseas persons* exclusion (which then has the effect that activities are deemed not to be *regulated activities* carried on in the *United Kingdom*); or
- (3) seek *Part IV permission*.

#### Passporting

5.12.13G The effect of the *IMD* is that any *EEA*-based insurance intermediaries must first be registered in their home *EEA State* before carrying on *insurance mediation* in that *EEA State* or other *EEA States*. For these purposes, an *EEA*-based insurance intermediary is either:

- (1) a legal *person* with its registered office or head office in an *EEA State* other than the *United Kingdom*; or
- (2) a natural *person* resident in an *EEA State* other than the *United Kingdom*.

Registered *EEA*-based insurance intermediaries wishing to establish branches in the *United Kingdom* or provide services on a cross-border basis into the *United Kingdom* can do so by notifying their *Home State regulator* which in turn notifies the *FSA*. This enables the intermediary to acquire passporting rights under Schedule 3 to the *Act* (EEA passporting rights) (see Schedule 3(13) and (14) of the *Act* as amended by the Insurance Mediation Directive (Miscellaneous Amendments) Regulations 2003). *AUTH* 5 (Qualifying for authorisation under the Act) has general *guidance* on the exercise of passporting rights by *EEA firms*.

5.12.14G On the other hand, non-*EEA*-based insurance intermediaries wishing to establish a branch in the *UK* for the purpose of carrying on *insurance mediation activities* may only do so with *Part IV permission*.

#### E-Commerce Directive

5.12.15G The *E-Commerce Directive* removes restrictions on the cross-border provision of services by electronic means, introducing a *country of origin* approach to regulation. This requires *EEA States* to impose certain requirements on the outward provision of such services and to lift them from inward providers. The *E-Commerce Directive* defines an e-commerce service (termed an *information society service*) as any service, normally provided for remuneration, at a distance, by electronic means, and at the individual request of the recipient of the service. So, for example, it includes services provided over the internet, by solicited e-mail, and interactive digital television. Further *guidance* is contained in *ECO*.

- 5.12.16G The *E-Commerce Directive* does not remove the *IMD* requirement for *persons* taking up or pursuing *insurance mediation* for remuneration to be registered in their *Home State*. Nor does it remove the requirement for *EEA*-based intermediaries to acquire passporting rights in order to establish branches in the *United Kingdom* (see *AUTH* App 5.12.7G (Where is insurance mediation carried on?) in relation to *electronic commerce activity* carried on from an establishment in the *United Kingdom*) or provide services on a cross-border basis into the *United Kingdom* where the relevant activity is carried on in the *United Kingdom*. An example of *electronic commerce activity* provided on a cross-border basis into the *United Kingdom* could be a recommendation in a (solicited) e-mail from an *EEA*-based intermediary to a *UK*-based customer to *buy* a particular *contract of insurance*.
- 5.12.17G Put shortly, the *E-Commerce Directive* relates to services provided into the *United Kingdom* from other *EEA States* and from the *United Kingdom* into other Member States. In broad terms, such cross-border insurance mediation services provided by an *EEA firm* into the *United Kingdom* (via *electronic commerce activity* or distance means) will generally be subject to *IMD* registration in, and conduct of business regulation of, the intermediary's *EEA State* of origin. By contrast, insurance mediation services provided in the *United Kingdom* will be subject to *UK* conduct of business regulation, although the requirement for registration will again depend upon the intermediary's *EEA State* of origin.
- 5.13 Appointed representatives
- What is an appointed representative?
- 5.13.1G Section 39 of the *Act* (Exemption of appointed representatives) exempts *appointed representatives* from the need to obtain *authorisation*. An *appointed representative* is a *person* who is party to a contract with an *authorised person* which permits or requires him to carry on certain *regulated activities* (see *Glossary* for full definition). *SUP* 12 (Appointed representatives) contains *rules* and *guidance* relating to *appointed representatives*.
- 5.13.2G A *person* who is an *authorised person* cannot be an *appointed representative* (see section 39(1) of the *Act* (Exemption of appointed representatives)).
- Business for which an appointed representative is exempt
- 5.13.3G An *appointed representative* can carry on only those *regulated activities* which are specified in the *Appointed Representatives Regulations*. With effect from 14 January 2005, the *regulated activities* set out in the table in *AUTH* App 5.13.4G will be included in those regulations. As set out in the table, the *insurance mediation activities* that can be carried on by an *appointed representative* differ depending on the type of *contracts of insurance* in relation to which the activities are carried on.
- 5.13.4G Table: insurance mediation activities able to be carried on by an appointed representative. This table belongs to 5.13.3G

Type of contract of insurance	Regulated activities an appointed representative can carry on
<i>General insurance contract</i>	<ul style="list-style-type: none"> <li>• <i>Dealing in investments as agent;</i></li> <li>• <i>Arranging;</i></li> <li>• <i>Assisting in the administration and performance of a contract of insurance;</i></li> <li>• <i>Advising on investments;</i> and</li> <li>• <i>Agreeing to carry on these regulated activities</i></li> </ul>
<i>Pure protection contract</i>	<ul style="list-style-type: none"> <li>• <i>Arranging;</i></li> <li>• <i>Advising on investments;</i> and</li> <li>• <i>Agreeing to carry on these regulated activities.</i></li> </ul>
<i>Life policy (note that this already has effect prior to 14 January 2005)</i>	<ul style="list-style-type: none"> <li>• <i>Arranging;</i></li> <li>• <i>Advising on investments;</i> and</li> <li>• <i>Agreeing to carry on these regulated activities</i></li> </ul>

#### Persons who are not already appointed representatives

5.13.5G A *person* who is not already an *appointed representative* may wish to become one in relation to *the regulated activities* specified in the *Appointed Representatives Regulations* (see table in *AUTH* App 5.13.4G). If so, he must be appointed under a written contract by an *authorised person*, who has *permission* to carry on those *regulated activities* and who accepts responsibility for the *appointed representative's* actions when acting for him. *SUP* 12.4 (What must a firm do when it appoints an appointed representative?) and *SUP* 12.5 (Contracts: required terms) set out the detailed requirements that must be met for an appointment to be made. In particular, an *appointed representative* will not be able to commence an *insurance mediation activity* until he is included on the *FSA Register* for such activities.

#### Persons who are already appointed representatives

5.13.6G Where a *person* is already an *appointed representative* and he proposes to carry on, with effect from 14 January 2005, any *insurance mediation activities*, he will need to consider the following matters.

- (1) He must become *authorised* if his proposed *insurance mediation activities* include activities that do not fall within the table in *AUTH* App 5.13.4G (for example, *dealing as agent* in *pure protection contracts*) and he wishes to carry on these activities. The *Act* does not permit any *person* to be exempt for some activities and *authorised* for others. He will, therefore, need to apply for *permission* to cover all the *regulated activities* that he proposes to carry on from 14 January 2005.
- (2) If he proposes to carry on other *regulated activities* specified in the *Appointed Representatives Regulations* in relation to *contracts of*

*insurance* (see the table in *AUTH* App 5.13.4G), he may be able to do so as an *appointed representative* bearing in mind the following.

- (a) He will need to be appointed by an *authorised person* prepared to accept responsibility for his *insurance mediation activities* when acting for him. The *authorised person* must have *permission* to carry on these *regulated activities*.
- (b) If these *insurance mediation activities* are to be carried on for the same *authorised person* who has already appointed him for his other *regulated activities*, the contract between them will need to be amended to reflect the additional activities. Other amendments to the contract will be required (see *SUP* 12.5.6A R).
- (c) The effect of amendments to the *Appointed Representatives Regulations* is that an *appointed representative* cannot commence an *insurance mediation activity* until he is included on the *FSA Register* as carrying on such activities.
- (d) An *appointed representative* would be entitled to have more than one principal subject to certain restrictions. In relation to *non-investment insurance contracts* (*general insurance contracts* and *pure protection contracts*), an *appointed representative* may have an unlimited number of *principals*. In relation to *regulated mortgage contracts* and *designated investment business*, an *appointed representative* is limited in the number of *principals* he may have. In any case where an *appointed representative* has multiple *principals*, those *principals* are required to enter into a multiple- principal agreement (see *SUP* 12.4.5D R to 12.4.5G G (Appointment of an appointed representative (other than an introducer appointed representative))).
- (e) If the activities of the *appointed representative* are limited to introducing, he should consider the specific *Handbook* provisions relating to *introducer appointed representatives* (see *SUP* 12 (What must a firm do when it appoints an appointed representative?)).

## 5.14 Exemptions

### Professionals

5.14.1G *Professional firms* (broadly firms of solicitors, accountants and actuaries) may carry on *insurance mediation activities* in the course of their professional activities. *Exempt professional firms* carrying on *insurance mediation activities* may continue to be able to use the *Part XX exemption* to avoid any need for *authorisation*. *PROF* 2 (Status of exempt professional firm) contains *guidance* on the *Part XX exemption*. They will, however, need to be shown on the *FSA Register* as carrying on *insurance mediation activities*, in order to benefit from this exemption. The task of registration is the responsibility of the *designated professional bodies* who will need to inform the *FSA* both of member firms carrying on *insurance mediation activities* and individuals within firms' management responsible for these activities.



- 5.14.2G *Professional firms* with practices that involve acting for claimants in litigation against *insurance undertakings* are likely to be carrying on the regulated activity of *assisting in the administration and performance of a contract of insurance*. *Exempt professional firms* whose practices contain a material element of such activity should consider whether they can continue to take advantage of the *Part XX exemption* to avoid any need for *authorisation*, having regard to the relevant provisions of the *Act*, in particular section 327 (Exemption from the general prohibition) and the *guidance* in *PROF 2.1.14* (Exempt regulated activities).
- 5.14.3G *Professional firms* should be aware of the disapplication of the exclusions for trustees (article 66) and activities carried on in the course of a profession or non-investment business (article 67) outlined in *AUTH App 5.11.7G* (Exclusions disapplied in connection with insurance mediation) where their activities would amount to *insurance mediation*. Where they do not, they will still be able to rely upon article 67. Otherwise, the *Non-exempt Activities Order* imposes limitations on the extent to which *professional firms* can give advice to individuals. In particular, a *professional firm* cannot recommend to a *private client* that he buy a *life policy*, unless he is endorsing a corresponding recommendation given to the *client*. The recommendation he endorses must be one given by an *authorised person* permitted to advise on *life policies*, or an *exempt person* for these purposes. No such restrictions apply, however, in relation to *contracts of insurance* other than *life policies*.
- 5.14.4G *Professional firms* relying (prior to 14 January 2005) on the exclusions in articles 29 (Arranging deals with or through authorised persons) and 33 (Introducing) when introducing clients to *authorised persons* in connection with the purchase of *life policies* are directed to *AUTH App 5.11.3G* (Exclusions disapplied where activities relate to contracts of insurance). More generally, as indicated in *AUTH App 5.6.8G*, the article 72C exclusion (Provision of information on an incidental basis) is potentially available to unauthorised *professional firms* including *exempt professional firms*. This may be relevant to *professional firms* arranging *contracts of insurance* for clients on an individual basis.

#### Other exemptions

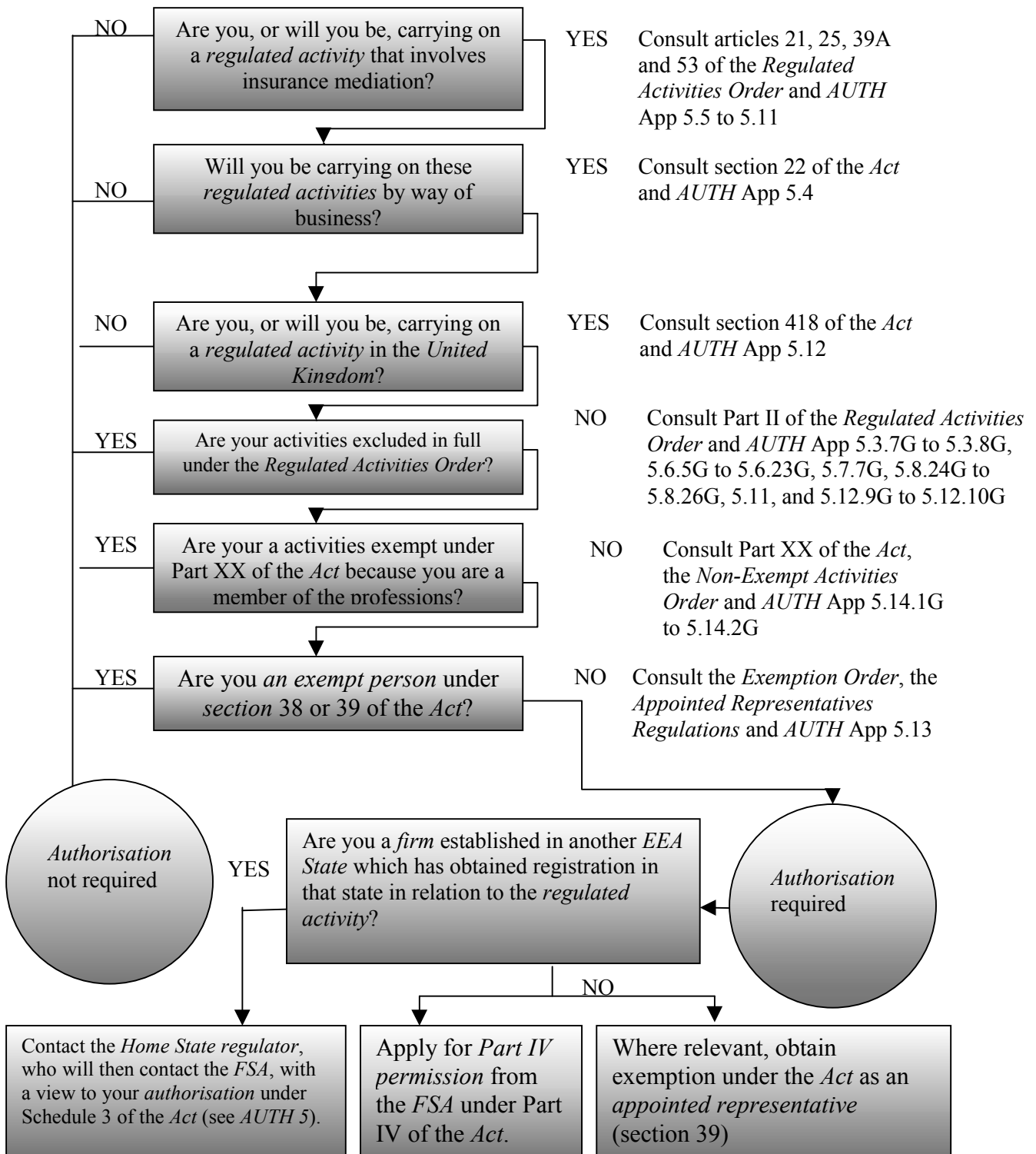
- 5.14.5G In addition to certain named *persons* exempted by the *Exemption Order* from the need to obtain *authorisation*, the following bodies are exempt in relation to *insurance mediation activities* that do not relate to *life policies*:
- (1) local authorities but not their subsidiaries;
  - (2) registered social landlords in England and Wales within the meaning of Part I of the Housing Act 1996 but not their subsidiaries;
  - (3) housing associations or other bodies corporate registered by Scottish Homes but not their subsidiaries;
  - (4) the Housing Corporation;
  - (5) Scottish Homes;

(6) The Northern Ireland Housing Executive.

5.15 Illustrative tables

5.15.1G This flow chart sets out the matters a *person* will need to consider to see if he will need *authorisation* for carrying on *insurance mediation activities*. It is referred to in *AUTH* App 5.2.3G (Questions to be considered to decide if authorisation is required).

5.15.2G Flow chart: regulated activities related to insurance mediation activities – do you need authorisation?



5.15.3G The table in *AUTH* App 5.15.4G is designed as a short, user-friendly guide but should be read in conjunction with the relevant sections of the text of this *guidance*. It is not a substitute for consulting the text of this *guidance* or seeking professional advice as appropriate (see *AUTH* App 5.1.4G to *AUTH* App 5.1.6G on the effect of this *guidance*). References in this Annex to articles are to articles of the *Regulated Activities Order*. In this table, it is assumed that each of the activities described is carried on by way of business (see *AUTH* App 5.4). Save where otherwise indicated, it is assumed that the intermediary is carrying on activities in respect of *policies* where he is not the *policyholder*. Note also that this table does not provide an exhaustive list of all of the exclusions or exemptions that are of relevance to each type of activity. For a full explanation of the exclusions and exemptions under the *Regulated Activities Order* and their applicability see generally *AUTH* App 5.3.7G to *AUTH* App 5.3.8G, *AUTH* App 5.6.5G to *AUTH* App 5.6.23G, *AUTH* App 5.7.7G, *AUTH* App 5.8.24G to *AUTH* App 5.8.26G, *AUTH* App 5.11, *AUTH* App 5.12.9G to *AUTH* App 5.12.10G, *AUTH* App 5.13 and *AUTH* App 5.14. This Table is referred to in *AUTH* App 5.7.5G (The regulated activities: assisting in the administration and performance of a contract of insurance).

5.15.4G Table: Types of activity – are they regulated activities and, if so, why?

Type of activity	Is it a <i>regulated activity</i> ?	Rationale
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MARKETING AND EFFECTING INTRODUCTIONS		
Passive display of information - for example, medical insurance brochures in doctor's surgery (whether or not remuneration is received for this activity)	No.	Merely displaying information does not constitute making arrangements under article 25(2) (see <i>AUTH</i> App 5.6.4G).
Recommending a broker/ <i>insurance undertaking</i> and providing customer with contact details (whether by phone, fax, e-mail, face-to-face or any other means of communication)	Yes, but article 72C may be available.	This will constitute making arrangements under article 25(2). But, the exclusion in article 72C will apply if all the intermediary does is supply information to the customer and the conditions of article 72C are otherwise met (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G). Generally, this will not amount to advice under article 53 unless there is an implied recommendation of a particular <i>policy</i> (see <i>AUTH</i> App 5.8.4G), in which case article 72C would not be available.

Providing an <i>insurance undertaking</i> /broker with contact details of customer	Yes.	This will constitute making arrangements under article 25(2) when undertaken in the context of regular or ongoing arrangements for introducing customers. Article 72C will not apply because the information is supplied to someone other than the <i>policyholder</i> or potential <i>policyholder</i> .
Marketing on behalf of <i>insurance undertaking</i> to intermediaries only (for example, broker consultants)	Yes.	This amounts to work preparatory to the conclusion of <i>contracts of insurance</i> and so constitutes making arrangements under article 25(2). Article 72C is not available because this activity does not involve provision of information to the <i>policyholder</i> or potential <i>policyholder</i> only.
Telemarketing services (that is, companies specialising in marketing an <i>insurance undertaking's</i> products/services to prospective customers)	Yes.	This amounts to introducing and/or other work preparatory to the conclusion of <i>contracts of insurance</i> and so constitutes making arrangements under article 25(2). This could also involve article 25(1) <i>arranging</i> where the telemarketing company actually <i>sells</i> a particular policy and could involve <i>advising on investments</i> . Article 72C will not be available where the provision of information is more than incidental to the telemarketing company's main business or where the telemarketing company is <i>advising on investments</i> .
PRE-PURCHASE DISCUSSIONS WITH CUSTOMERS AND ADVICE		
Discussion with client about need for insurance generally/need to take out a particular type of insurance	Generally, no. Article 72C available if needed.	Not enough, of itself, to constitute making arrangements under article 25(2), but you should consider whether, viewed as a whole, your activities might amount to <i>arranging</i> . If so, article 72C might be of application (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G).
Advising on the level of cover needed	Generally, no. Article 72C available if needed.	Not enough, of itself, to constitute making arrangements under article 25(2), but you

		should consider whether, viewed as a whole, your activities might amount to making arrangements under article 25(2) (see <i>AUTH</i> App 5.8.3G). If so, article 72C might be of application (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G).
Pre-purchase questioning in the context of filtered sales (intermediary asks a series of questions and then suggests several policies which suit the answers given)	Yes. Subject to Article 72 C exclusion where available.	This will constitute <i>arranging</i> although article 72C may be of application (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G). If there is no express or implied recommendation of a particular <i>policy</i> , this activity will not amount to advice under article 53 (see <i>AUTH</i> App 5.8.15G to <i>AUTH</i> App 5.8.19G).
Explanation of the terms of a particular <i>policy</i> or comparison of the terms of different policies	Possibly. Article 72C available.	This is likely to amount to making arrangements under article 25(2). In certain circumstances, it could involve advising on investments (see <i>AUTH</i> App 5.8.8G (Advice or information)). Where the explanation is provided to the potential <i>policyholder</i> , and does not involve <i>advising on investments</i> , article 72C may be of application (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G), and where information is provided by a professional in the course of a profession, article 67 may apply (see <i>AUTH</i> App 5.11.9G to <i>AUTH</i> App 5.11.12G).
Advising that a customer take out a particular <i>policy</i>	Yes.	This amounts to advice on the merits of a particular <i>policy</i> under article 53 (see <i>AUTH</i> App 5.8.4G to <i>AUTH</i> App 5.8.5G).
Advising that a customer does not take out a particular <i>policy</i>	Yes.	This amounts to advice on the merits of a particular <i>policy</i> under article 53 (see <i>AUTH</i> App 5.8.4G to <i>AUTH</i> App 5.8.5G).
Advice by journalists in newspapers, broadcasts etc.	Generally, no because of the article 54 exclusion.	Article 54 provides an exclusion for advice given in newspapers etc (see <i>AUTH</i> App 5.8.24G to <i>AUTH</i> App 5.8.25G).
Giving advice to a customer in relation to his <i>buying</i> a consumer product, where insurance is a	Not necessarily but depends on the circumstances	Where the advice relates specifically to the merits of the consumer product, it is possible that references to the

compulsory secondary purchase and/or a benefit that comes with <i>buying</i> the product		accompanying insurance may be seen to be information and not advice. If, however, the advice relates, in part, to the merits of the insurance element, then it will be <i>regulated activity</i> .
ASSISTING CUSTOMERS WITH COMPLETING/SENDING APPLICATION FORMS		
Providing information to customer who fills in application form	Possibly. Subject to article 67 or 72C exclusions where available.	This activity may amount to <i>arranging</i> although the exclusions in article 67 (see <i>AUTH</i> App 5.11.9G to <i>AUTH</i> App 5.11.12G) and article 72C (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G) may be of application.
Helping a potential <i>policyholder</i> fill in an application form	Yes.	This activity amounts to <i>arranging</i> . Article 72C will not apply because this activity goes beyond the mere provision of information to a <i>policyholder</i> or potential <i>policyholder</i> (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G).
Receiving completed proposal forms for checking and forwarding to an <i>insurance undertaking</i> (for example, an administration outsourcing service provider that receives and processes proposal forms)	Yes.	This amounts to <i>arranging</i> . Article 72C does not apply because this activity goes beyond the mere provision of information to a <i>policyholder</i> or potential <i>policyholder</i> (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G).
Assisting in completion of proposal form and sending to <i>insurance undertaking</i>	Yes.	This activity amounts to <i>arranging</i> . Article 72C does not apply because this activity goes beyond the mere provision of information (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G).
NEGOTIATING AND CONCLUDING CONTRACTS OF INSURANCE		
Negotiating terms of <i>policy</i> on behalf of customer with the <i>insurance undertaking</i>	Yes.	This activity amounts to <i>arranging</i> (see <i>AUTH</i> App 5.6.2G).
Negotiating terms of <i>policy</i> on behalf of <i>insurance undertaking</i> with the customer and signing proposal form on his behalf	Yes.	These activities amount to both <i>arranging</i> and <i>dealing in investments as agent</i> .
Concluding a <i>contract of insurance</i> on insurance	Yes.	A <i>person</i> carrying on this activity will be <i>dealing in investments as agent</i> . He will

company's behalf, for example, motor dealer who has authority to conclude insurance contract on behalf of <i>insurance undertaking</i> when <i>selling</i> a car		also be <i>arranging</i> (as the article 28 exclusion only applies in the limited circumstances envisaged under article 28(3)) (see <i>AUTH</i> App 5.6.12G).
Agreeing, on behalf of a prospective <i>policyholder</i> , to <i>buy</i> a <i>policy</i> .	Yes.	A <i>person</i> who, with authority, enters into a <i>contract of insurance</i> on behalf of another is <i>dealing in investments as agent</i> under article 21, and will also be <i>arranging</i> .
Providing compulsory insurance as a secondary purchase	Yes. It will amount to <i>dealing in investments as agent</i> or <i>arranging</i> .	The fact that the insurance is secondary to the primary product does not alter the fact that arranging the package involves <i>arranging</i> the insurance.
COLLECTION OF PREMIUMS		
Collection of cheque for premium from the customer at the pre-contract stage.	Yes (as part of <i>arranging</i> ).	This activity is likely to form part of <i>arranging</i> . But the mere collection/receipt of premiums from the customer is unlikely, without more, to amount to <i>arranging</i> .
Collection of premiums at post-contract stage	No.	The mere collection of premiums from <i>policyholders</i> is unlikely, without more, to amount to <i>assisting in the administration and performance of a contract of insurance</i> .
MID-TERM ADJUSTMENTS AND ASSIGNMENTS		
Solicitors or licensed conveyancers discharging client instructions to assign <i>contracts of insurance</i> .	Not where article 67 applies.	As the assignment of rights under a <i>contract of insurance</i> (as opposed to the creation of new <i>contracts of insurance</i> ) does not fall within the <i>IMD</i> , article 67 is of potential application (see <i>AUTH</i> App 5.11.9G to <i>AUTH</i> App 5.11.12G).
Making mid-term adjustments to a <i>policy</i> , for example, property manager notifies changes to the names of the leaseholders registered as "interested parties" in the <i>policy</i> in respect of the property.	Yes.	Assuming the freeholder (as <i>policyholder</i> ) is obliged under the terms of the <i>policy</i> to notify the <i>insurance undertaking</i> of changes to the identity of the leaseholders, the property manager is likely to be <i>assisting in the administration and the performance of the contract of insurance</i> .
TRADED ENDOWMENT POLICIES ("TEPs")		
Making introductions for the	Yes, unless article 72C applies.	Making introductions for these purposes is

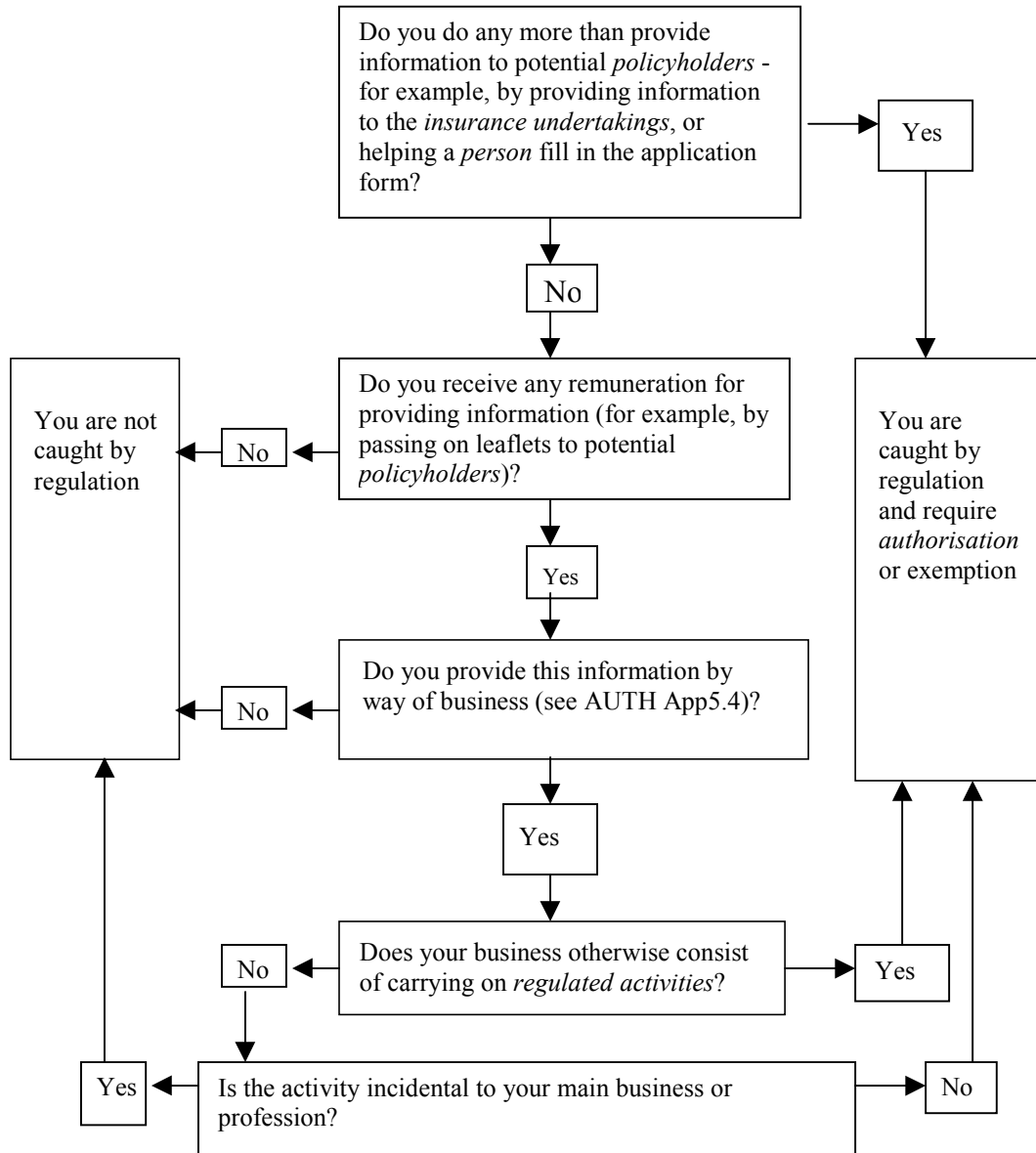


purposes of <i>selling</i> TEPs		<i>arranging</i> unless article 72C applies (see <i>AUTH</i> App 5.6.5G to <i>AUTH</i> App 5.6.9G). The exclusions in article 29 (Arranging deals with or through authorised persons) and 33 (Introducing) no longer apply to arranging <i>contracts of insurance</i> .
Market makers in TEPs	Yes, although the exclusion in article 28 may apply.	Unauthorised market makers can continue to make use of the exclusions in articles 15 (Absence of holding out etc.) and 16 (Dealing in contractually based investments), where appropriate. In order to avoid the need for <i>authorisation</i> in respect of <i>arranging</i> they may be able to rely upon article 28 (see <i>AUTH</i> App 5.6.12G).
ASSISTING POLICYHOLDER WITH MAKING A CLAIM		
Merely providing information to the insured to help him complete a claim form	No.	Of itself, this is likely to amount to assisting in the administration but not the performance of a <i>contract of insurance</i> . In the <i>FSA</i> 's view, the provision of information in these circumstances is more akin to facilitating performance of a <i>contract of insurance</i> rather than assisting in the performance (see <i>AUTH</i> App 5.7.3G to <i>AUTH</i> App 5.7.5G)
Completion of claim form on behalf of insured	Potentially.	This activity amounts to assisting in the administration of a <i>contract of insurance</i> . Whether this activity amounts to <i>assisting in the administration and performance of a contract of insurance</i> will depend upon whether a <i>person</i> 's assistance in filling in a claims form is material to whether performance of the contractual obligation to notify a claim takes place (see <i>AUTH</i> App 5.7.2G to <i>AUTH</i> App 5.7.3G).
Notification of claim to <i>insurance undertaking</i> and helping negotiate its settlement on the <i>policyholder</i> 's behalf	Yes.	This activity amounts to <i>assisting in the administration and performance of a contract of insurance</i> (see 5.7.4G).
ASSISTING INSURANCE UNDERTAKING WITH CLAIMS BY POLICYHOLDERS		

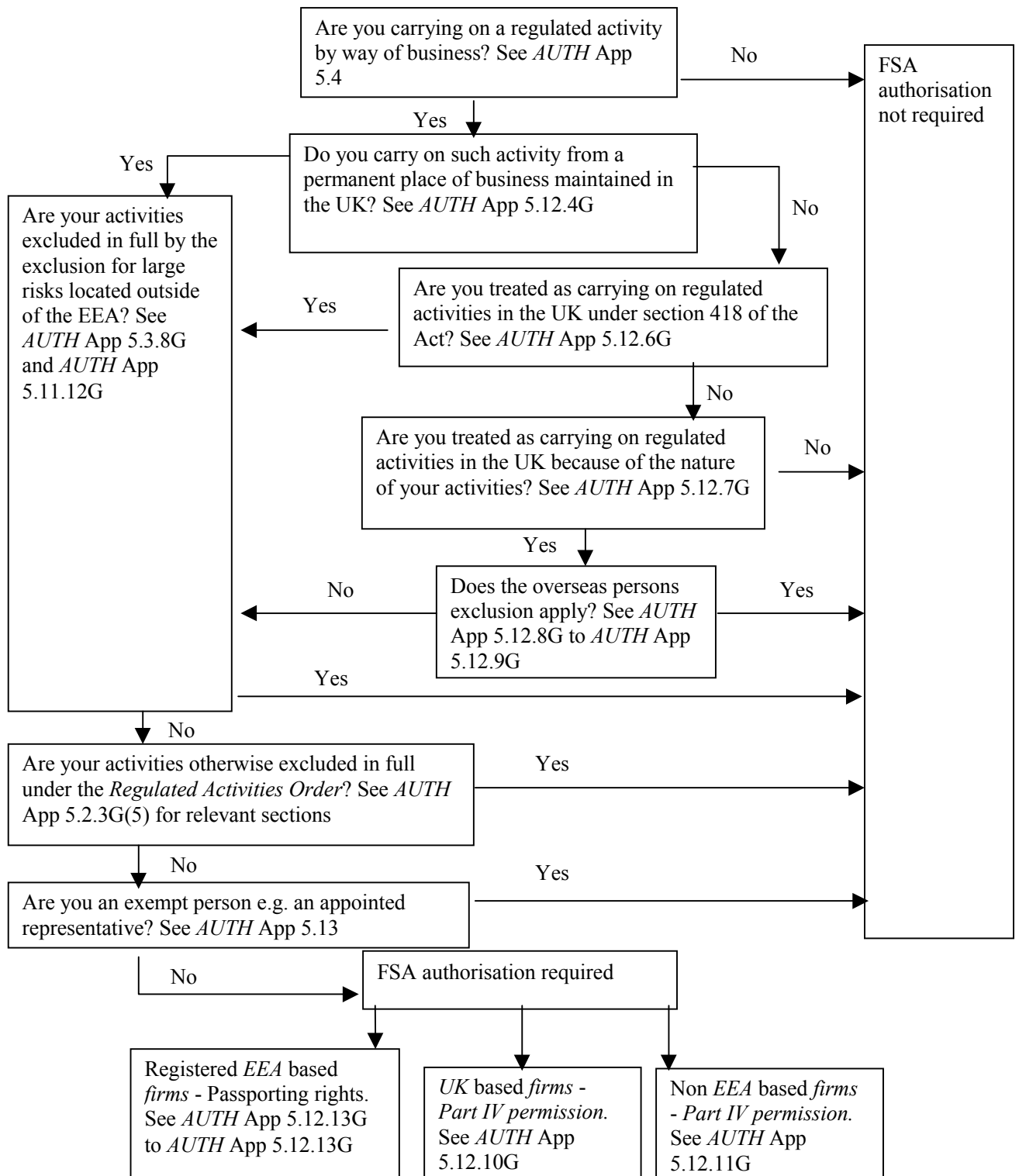
Negotiation of settlement of claims on behalf of an <i>insurance undertaking</i>	No.	Claims management on behalf of an <i>insurance undertaking</i> does not amount to <i>assisting in the administration and performance of a contract of insurance</i> by virtue of the exclusion in article 39B (see <i>AUTH App 5.7.7G</i> ).
Providing information to an <i>insurance undertaking</i> in connection with its investigation or assessment of a claim	No.	This activity does not amount to <i>assisting in the administration and performance of a contract of insurance</i> .
Loss adjusters and claims management services (for example, by administration outsourcing providers)	Potentially.	These activities may amount to <i>assisting in the administration and performance of a contract of insurance</i> . Article 39B excludes these activities, however, when undertaken on behalf of an <i>insurance undertaking</i> only (see <i>AUTH App 5.7.7G</i> ).
Providing an expert appraisal of a claim	No.	This activity does not amount to <i>assisting in the administration and performance of a contract of insurance</i> whether carried out on behalf of an <i>insurance undertaking</i> or otherwise.
Jeweller repairs customer's jewellery pursuant to a <i>policy</i> which permits the jeweller to carry out repairs	No.	This activity does not amount to <i>assisting in the administration and performance of a contract of insurance</i> . It amounts to managing claims on behalf of an <i>insurance undertaking</i> and so falls within the exclusion in article 39B (see <i>AUTH App 5.7.7G</i> ).

5.15.5G The flow chart in *AUTH App 5.15.6G* sets out the matters a *person* whose introducing activities potentially amount to *making arrangements with a view to transactions in investments* will need to consider to see if he can use the exclusion in article 72C (Provision of information on an incidental basis). It is referred to in *AUTH App 5.1.6G* (Purpose of guidance) and *AUTH App 5.6.9G* (Exclusion: article 72C (Provision of information on an incidental basis)).

5.15.6G Flow chart: Introducers.



- 5.15.7G The flow chart in *AUTH* App 5.16.8G sets out the questions a *person* needs to consider in determining whether or not his *regulated activities* are carried on 'in the *United Kingdom*'.
- 5.15.8G Flow chart: am I carrying on regulated activities in the United Kingdom?





5.16.1G *AUTH* App 5.16.2G sets out the text of article 2.3 of the *Insurance Mediation Directive*. It is referred to in *AUTH* App 5.2.5G and *AUTH* App 5.2.5G (Approach to implementation of the IMD), *AUTH* App 5.11.7G (Exclusions disapplied in connection with insurance mediation) and *AUTH* App 5.11.10G (Activities carried on in the course of a profession or non-investment business).

5.16.2G Text of article 2.3 of the Insurance Mediation Directive

“ ‘Insurance mediation’ means the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim.

These activities when undertaken by an insurance undertaking or an employee of an insurance undertaking who is acting under the responsibility of the insurance undertaking shall not be considered as insurance mediation.

The provision of information on an incidental basis in the context of another professional activity provided that the purpose of that activity is not to assist the customer in concluding or performing an insurance contract, the management of claims of an insurance undertaking on a professional basis, and loss adjusting and expert appraisal of claims shall also not be considered as insurance mediation.”

## Annex F

### Amendments to the Supervision manual

- 6.4.22 G In deciding whether to cancel a *firm's Part IV permission*, the *FSA* will take into account all relevant factors in relation to business carried on under that *permission*, including whether:
- (1) there are unresolved, unsatisfied or undischarged complaints against the *firm* from any of its *customers*;
  - (2) the *firm* has complied with *COB 9.3.133R* and *CASS 5.5.80R* (Client money: discharge of fiduciary duty) and *COB 9.3.138R* (Client money: allocated but unclaimed client money) if it has ceased to hold *client money*; these *COB rules* apply to both repayment and transfer to a third party;
  - (3) ...

...

SUP 6 Ann 4 G: Additional guidance for a firm winding down (running off) its business

- 2 Table Specific guidance for firms holding client money or customer assets

1. ...

2. A *firm* must comply with *COB 9.3.133R* and *CASS 5.5.80R* (Client money: discharge of fiduciary duty), and *COB 9.3.138R* (Client money: allocated but unclaimed client money) if it is ceasing to hold *client money*. A *firm* must also cease to hold or control *custody assets* in accordance with instructions received from *clients* (including instructions set out in an agreement entered into in accordance with *COB 9.1.49R* (Custody: client agreement)). These *COB rules* apply to both repayment and transfer to a third party.

...

- 10.1.15 G ...  
Appointed representatives

- 10.1.16 R The description of the following functions apply to an *appointed representative* of a *firm*, except an *introducer appointed representative*, as they apply to a *firm*:

- (1) the *governing functions*, subject to SUP 10.1.16A R;
- (2) the *customer functions* other than the *investment management function*.

- 10.1.16A R (1) SUP 10.1.16R (1) is modified in relation to an appointed representative meeting the conditions in (2) so that only one of the following governing functions:



(a) director function; or

(b) chief executive function; or

(b) partner function; or

(c) director of unincorporated association function;

applies, as appropriate, to an individual within that appointed representative who will be required to be an approved person.

(2) The conditions are that:

(a) the scope of appointment of the appointed representative includes insurance mediation activity in relation to non-investment insurance contracts but no other regulated activity, and

(b) the principal purpose of the appointed representative is to carry on activities other than regulated activities.

10.1.17 G (1) The effect of SUP 10.1.16R is that the directors (or their equivalent) and senior managers (or their equivalent) of an appointed representative must also be approved under section 59 of the Act for the performance of certain controlled functions.

(2) SUP 10.1.16R has a limited application to an appointed representative appointed by a firm to carry on insurance mediation activity or mortgage mediation activity. The description of the customer functions do not apply to such an appointed representative as these functions do not apply to a firm carrying on these regulated activities.

(3) The effect of SUP 10.1.16A R is that only one director (or equivalent) of an appointed representative to which that rule applies must be approved under section 59 of the Act for the performance of a governing function.

10.1.20 G ...

Oil market participants, service companies, and energy market participants, subsidiaries of local authorities or registered social landlords and insurance intermediaries

10.1.21 R The descriptions of significant influence functions, other than the required functions, do not extend to activities carried on by a firm whose principal purpose is to carry on activities other than regulated activities and which is:

(1) an oil market participant; or

(2) a service company; or

(3) an *energy market participant*; or

(4) a wholly owned *subsidiary* of:

(a) a local authority; or

(b) a registered social landlord; or

(5) a *firm with permission to carry on insurance mediation activity in relation to non-investment insurance contracts but no other regulated activity*.

...  
10.6.1

G ...

What the governing functions include

...  
10.6.3

G ...

10.6.3A

G

PRU 9.1.3R provides that an insurance intermediary, other than a sole trader, must allocate to a director or senior manager the responsibility for the firm's insurance mediation activity. PRU 9.1.4R (1) provides that the firm may allocate this responsibility to one or more of the persons performing a governing function.

10.6.3B

G

Where a person performing a governing function is also responsible for the firm's insurance mediation activity, the words "(insurance mediation)" will be inserted after the relevant controlled function (see PRU 9.1.7G).

...

10.7 Required functions

Apportionment and oversight function (CF8)

...  
10.7.4

G ...

10.7.4A

G

PRU 9.1.3R provides that an insurance intermediary, other than a sole trader, must allocate to a director or senior manager the responsibility for the firm's insurance mediation activity. PRU 9.1.4R (2) provides that the firm may allocate this responsibility to the person performing the apportionment and oversight function.

10.7.4B

G

Where the person performing the apportionment and oversight function is also responsible for the firm's insurance mediation activity, the words "(insurance mediation)" will be inserted after this controlled function (see PRU 9.1.7G).

...

Money laundering reporting function (CF11)

...

- 10.7.14 G The *rules* in the *Money Laundering* sourcebook (*ML*) provide that a *firm* must have a *money laundering reporting officer* unless:
- (1) it is a *sole trader* with no *employees*; or
  - (2) its *regulated activities* are certain *insurance business* only; or
  - (3) it is an *incoming firm* providing only services into the *United Kingdom*; or
  - (4) its *regulated activities* are *insurance mediation activity* in relation to a *general insurance contract* or *pure protection contract* or *mortgage mediation activity*.
- ...
- 10.9.11 G ...
- Significant management (other business operations) function (CF17)
- ...
- 10.9.13 G ...
- 10.9.13A G *PRU 9.1.3R* provides that an *insurance intermediary*, other than a *sole trader*, must allocate to a *director* or *senior manager* the responsibility for the *firm's insurance mediation activity*. *PRU 9.1.4R(3)* provides that the *firm* may allocate this responsibility to the *person* performing the *significant management (other business operations) function*.
- 10.9.13B G Where the *person* performing the *significant management (other business operations) function* is also responsible for the *firm's insurance mediation activity*, the words “(insurance mediation)” will be inserted after this *controlled function* (see *PRU 9.1.7G*).
- ...
- 10.10.6 G ...
- Investment adviser function (CF21)
- 10.10.7 R (1) The *investment adviser function* is the function of:
- (a) *advising on investments* other than a *non-investment insurance contract*; and
  - (b) performing functions within the *customer trading function* in connection with *advising on investments* other than a *non-investment insurance contract*.
- ...
- Investment adviser (trainee) function (CF22)
- 10.10.11 R The *investment adviser (trainee) function* is the function of *advising on*

*investments other than a non-investment insurance contract* where the individual performing the function has not yet been assessed as competent in accordance with the *rules* in the Training and Competence sourcebook (TC).

...

Customer trading function (CF26)

10.10.16 R The *customer trading function* is the function of *dealing*, as principal or as agent, and *arranging deals in investments other than a non-investment insurance contract* with or for, or in connection with, *private customers* and *intermediate customers* where:

(1) ...

...

11.1.2 R Table Applicable sections (see SUP 11.1.1R)

	Category of firm	Applicable sections
(1)	A <i>UK domestic firm</i> other than a <i>building society</i> , or a <i>non-directive friendly society</i> or a <i>UK insurance intermediary</i>	All except SUP 11.3, SUP 11.4.2A R and SUP 11.4.4R
(1A)	A <i>building society</i>	(a) ... (b) In any other case, all except SUP 11.3, SUP 11.4.2AR and SUP 11.4.4R
(2)	A <i>non-directive friendly society</i>	...
(2A)	A <i>UK insurance intermediary</i>	all except SUP 11.3, SUP 11.4.2R, SUP 11.4.3G and SUP 11.4.4R
(3)	An <i>overseas firm</i>	All except SUP 11.3, SUP 11.4.2R, SUP 11.4.2A R, SUP 11.4.3, SUP 11.4.9G ...

...

11.2.2 G ...

11.2.2A G Part XII of the Act does not place an obligation on a controller of an UK insurance intermediary to notify the FSA where it becomes or ceases to be a parent undertaking. Nevertheless, the rule in SUP 11.4.2A R(2) requires the UK insurance intermediary to notify the FSA of parent undertakings so that the FSA can monitor the firm's continuing satisfaction of the threshold conditions, which includes consideration of its controllers and parent undertakings (see COND).

...

11.3.1 G ...  
Requirement to notify a change in control

11.3.2 G Part XII of the *Act* requires a *person* (whether or not he is an *authorised person*) to notify the *FSA* in writing if he proposes to take a step which would result in his acquiring *control* or increasing or reducing his *control* over a *firm* in a way described in *SUP* 11.4.2R(1) to (4), or acquiring or reducing his *control* in a way described in *SUP* 11.4.2A R(1) and (2). Failure to notify is an offence under section 191(1) of the *Act* (Offences under this Part). An event described in *SUP* 11.4.2R(1) to (4) and *SUP* 11.4.2A R(1) to (3) is referred to in this chapter as a “change in *control*”.

...

Prior approval of acquiring or increasing control

11.3.4 G If a *person* proposes to acquire *control* or increase his *control* over a *firm* in a way described in *SUP* 11.4.2R(1) to (4) or acquire *control* in a way described in *SUP* 11.4.2A R(1), he must obtain the *FSA*’s approval before doing so. Failure to obtain approval is an offence under section 191(3) of the *Act* (Offences under this Part). The *FSA* has up to three *months* to consider whether to *approve* such a change in *control*. A *controller* or proposed *controller* should take this period into account when deciding when to give his notification.

...

Form of notification when acquiring or increasing control

11.3.7 D A notification (“notice of *control*”) given to the *FSA* by a *person* who is acquiring or increasing his *control* over a *firm*, in a way described in *SUP* 11.4.2R(1) to (4), or acquiring *control* in a way described in *SUP* 11.4.2A R(1), must :

(1) ...

...

Form of notification when reducing control

11.3.15 G A notification given to the *FSA* by a *person* who is reducing his *control* over a *firm*, in a way described in *SUP* 11.4.2R(1) to (4) or *SUP* 11.4.2A R(2), must, in accordance with section 190(4) of the *Act* (Notification):

(1) ...

- ...
- 11.4.1 G ...  
Requirement to notify a change in control
- 11.4.2 R *A UK domestic firm other than a UK insurance intermediary* must notify the *FSA* of any of the following events concerning the *firm*:
- (1) ...
- 11.4.2A R *A UK insurance intermediary* must notify the *FSA* of any of the following events concerning the *firm*:
- (1) a person acquiring control;
- (2) in relation to an existing controller:
- (a) the percentage of shares held in the *firm* decreasing from 20% or more to less than 20%; or
- (b) the percentage of shares held in a *parent undertaking* of the *firm* decreasing from 20% or more to less than 20%; or
- (c) the percentage of *voting power* which it is entitled to exercise, or control the exercise of, in the *firm* decreasing from 20% or more to less than 20%; or
- d) the percentage of *voting power* which it is entitled to exercise, or control the exercise of, in a *parent undertaking* of the *firm* decreasing from 20% or more to less than 20%;
- (3) an existing *controller* becoming or ceasing to be a *parent undertaking*.
- ...
- 11.4.5 G If there is uncertainty whether a particular relationship constitutes *control*, it may be appropriate for the *firm* or *controller* or proposed *controller* to ask the *FSA* for individual *guidance* (see *SUP* 9) and to obtain its own legal advice. For example, if the *control* is to be held through a trust, then certain trustees, beneficiaries and other parties may qualify as *controllers* for the purposes of the *Act* and this chapter. Furthermore, a *person* may qualify as a *controller* if he is able to exercise 10% (20% if the *firm* is an *UK insurance intermediary*) or more of the *voting power* at a *firm's* general meeting as a result of the ability to exercise proxy votes.
- ...
- Content and timing of notification
- 11.4.7 R The notification by a *firm* under *SUP* 11.4.2R, *SUP* 11.4.2A R or *SUP* 11.4.4R must:

(1) ...

- 11.4.8 G *Principle 11* requires *firms* to be open and cooperative with the *FSA*. A *firm* should discuss with the *FSA*, at the earliest opportunity, any prospective changes of which it is aware, in *controllers'* or proposed *controllers'* shareholdings or *voting power* (if the change is material). These discussions may take place before the formal notification requirement in *SUP 11.4.2R*, *SUP 11.4.2A R* or *SUP 11.4.4R* arises. (See also *SUP 11.3.2G*.) As a minimum, the *FSA* considers that such discussions should take place before a *person*:

(1) ...

- 11.4.9 G The obligation in *SUP 11.4.2R* and *SUP 11.4.2A R(1) and (2)* applies whether or not the *controller* himself has given or intends to give a notification, in accordance with his obligations under the *Act*.

...

11.6 Subsequent notification requirements by firms  
Changes in the information provided to the *FSA*

- 11.6.1 G *Firms* are reminded that *SUP 15.6.4R* requires them to notify the *FSA* if information notified under *SUP 11.4.2R*, *SUP 11.4.2A R* or *SUP 11.4.4R* was false, misleading, inaccurate, incomplete, or changes, in a material particular. This would include a *firm* becoming aware of information that it would have been required to provide under *SUP 11.5.1R* if it had been aware of it.

- 11.6.2 R After submitting a notification under *SUP 11.4.2R* or *SUP 11.4.2A R(1) and (2)* and until the change in *control* occurs (or is no longer to take place), *SUP 15.6.4R* and *SUP 15.6.5R* apply to a *UK domestic* in relation to any information its *controller* or proposed *controller* provided to the *FSA* under *SUP 11.5.1R* or *SUP 11.3.7D*.

...

Notification that the change in control has taken place

- 11.6.4 R A *firm* must notify the *FSA*:

(1) when a change in control which was previously notified under *SUP 11.4.2R*, *SUP 11.4.2A R* or *SUP 11.4.4R* has taken place; or

(2) ...

...

- 11.8.1 R A *firm* must notify the *FSA* immediately it becomes aware of any of the following matters in respect of one or more of its *controllers*:

(1) ...

(4) if a *controller*, who is authorised in another *EEA State* as an *ISD*

*investment firm or BCD credit institution or under the Insurance Directives or the Insurance Mediation Directive, ceases to be authorised (registered in the case of an IMD insurance intermediary).*

...

SUP 11 Annex 1G Summary of notifications required in this chapter

Event triggering a notification	Requirement reference	
	When	How
Notifications from a controller or proposed controller of a UK domestic firm <u>other than a UK insurance intermediary</u>		
1 ...	...	...
<u>Notifications from a controller or proposed controller of a UK insurance intermediary</u>		
1. <u>A person proposing to become a controller</u>	<u>SUP 11.3.2G</u> <u>SUP 11.3.6G</u>	<u>SUP 11.3.7D to</u> <u>SUP 11.3.14G</u>
2. <u>An existing controller proposing to reduce his control</u>	<u>SUP 11.3.2G</u> <u>SUP 11.3.6G</u>	<u>SUP 11.3.15G</u>
3. <u>When a change in control actually takes place</u>	<u>SUP 11.3.16G</u>	<u>SUP 11.3.16G</u>
Notification from a UK domestic firm <u>other than a UK insurance intermediary</u> relating to a change in control		
1 ...	...	...
<u>Notification from a UK insurance intermediary relating to a change in control</u>		
1. <u>When a firm becomes aware that a person is becoming or ceasing to be a controller or parent undertaking</u>	<u>SUP 11.4.2A R</u> <u>SUP 11.4.7R</u> <u>SUP 11.4.8G</u>	<u>SUP 11.5.1R</u> <u>SUP 11.5.2R</u> <u>SUP 11.5.3G</u>
2. <u>When a firm becomes aware of any material inaccuracies, omissions or changes in information previously provided to the FSA either by the firm or by the controller</u>	<u>SUP 11.6.1G</u> <u>SUP 11.6.2R</u>	<u>SUP 15.7</u>



3. When a change in <i>control</i> actually takes place or, although a notification has been submitted, is not, after all, going to take place	<u>SUP 11.6.4R</u> <u>SUP 11.6.5R</u>	<u>SUP 15.7</u>
--	--	-----------------

...

...

...

13.3.1

G ...

The conditions for establishing a branch

13.3.2

G *A UK firm cannot establish a branch in another EEA State for the first time under an EEA right unless the conditions in paragraphs 19(2), (4) and (5) of Part III of Schedule 3 to the Act are satisfied. It is an offence for a UK firm which is not an authorised person to contravene this prohibition (paragraph 21 of Part III of Schedule 3 to the Act). These conditions are that:*

(1) ...

...

(3) (a) if the UK firm's EEA right derives from the Insurance Mediation Directive one month has elapsed beginning on the date on which the UK firm received notice that the FSA had given a consent notice as described in SUP 13.3.6 G(1) (see SUP 13.3.2A G);

(b) in any other case:

(a) (i) the Host State regulator has notified the UK firm (or, where the UK firm is passporting under the Insurance Directives, the FSA) of the applicable provisions; or

(b) (ii) two months have elapsed beginning with the date on which the FSA gave the consent notice.

13.3.2A

G If the UK firm is passporting under the Insurance Mediation Directive and the EEA State in which the UK firm is seeking to establish a branch has not notified the European Commission of its wish to be informed of the intention of persons to establish a branch in its territory in accordance with article 6(2) of that directive, SUP 13.3.2G (2) and (3) do not apply. Accordingly, the UK firm may establish the branch to which its notice of intention relates as soon as the conditions referred to in SUP 13.3.2G (1) are satisfied.

13.3.2B

G An appointed representative appointed by a firm to carry on insurance mediation activity on its behalf may establish a branch in another EEA State under the Insurance Mediation Directive. In this case, the notice of intention in SUP 13.3.2G(1) should be given to the FSA by the firm.

13.3.2C

G An exempt professional firm which is included in the record of unauthorised persons carrying on insurance mediation activity maintained by the FSA under article 93 of the Regulated Activities Order may establish a branch in another

EEA State under the Insurance Mediation Directive (see PROF 7.2).

...

How long will the process take?

- 13.3.4 G On receipt of a UK firm's notice of intention (prepared in accordance with SUP 13.3.2G (1) and SUP 13.5.1R) then:
- (1) where the UK firm is passporting under the Insurance Mediation Directive:
- (a) if the UK firm seeking to passport in an EEA State which wishes to be informed of the intention of persons establishing a branch in its territory (see SUP 13.3.2A G), the FSA has one month to notify the relevant Host State regulator;
- (b) otherwise, the UK firm may establish a branch as soon as it satisfies the conditions referred to in SUP 13.3.2G(1);
- (2) in any other case, the FSA has three months from receiving a UK firm's notice of intention to consider it and, if satisfied with the proposal, notify the relevant Host State regulator. The Host State regulator then has a further two months to notify the applicable provisions (if any) and prepare for the supervision, as appropriate, of the UK firm.

- 13.3.4A G The list of the EEA States that have notified the European Commission of their wish to be informed in accordance with article 6(2) of the Insurance Mediation Directive is published on the FSA's website at [www.fsa.gov.uk](http://www.fsa.gov.uk).

Issue of a consent notice to the Host State regulator

- 13.3.5 G (1) If a UK firm has given the FSA a notice of intention in the required form, then:
- (a) ...
- (c) if the UK firm's EEA right derives from the Insurance Mediation Directive and SUP 13.3.2G (2) applies, the FSA will give the Host State regulator a consent notice within one month of the date on which it received the UK firm's notice of intention.

(2) ...

...

- 13.4.1 G ...

The conditions for providing cross border services into another EEA State

- 13.4.2 G A UK firm cannot start providing cross border services into another EEA State under an EEA right unless it satisfies the conditions in paragraphs 20(1) of Part III of Schedule 3 to the Act and, if it derives its EEA right from the Insurance Directives, paragraph 20(4B) of Part III of Schedule 3 to the Act.

It is an offence for a *UK firm* which is not an *authorised person* to breach this prohibition (paragraph 21 of Part III of Schedule 3 to the *Act*). The conditions are that:

- (1) ...
- (2) if the *UK firm* is passporting under the *Insurance Directives*, the *firm* has received written notice from the *FSA* as described in SUP 13.4.6 G –;  
or
- (3) if the *UK firm* is passporting under the *Insurance Mediation Directive* and the *EEA State* in which the *UK firm* is seeking to provide services has notified the European Commission of its wish to be informed of the intention of persons to provide cross border services in its territory in accordance with article 6(2) of that directive, one month has elapsed beginning with the date on which the *UK firm* received written notice from the *FSA* as described in SUP 13.4.5 G (paragraph 20 (3B)(c) of Schedule 3 to the *Act*).

13.4.2A      G      An appointed representative appointed by a firm to carry on insurance mediation activity on its behalf may provide cross border services in another EEA State under the Insurance Mediation Directive. In this case, the notice of intention in SUP 13.4.2G(1) should be given to the FSA by the firm.

13.4.2B      G      An exempt professional firm which is included in the record of unauthorised persons carrying on insurance mediation activity maintained by the FSA under article 93 of the Regulated Activities Order may provide cross border services in another EEA State under the Insurance Mediation Directive (see PROF 7.2).

How long will the process take?

13.4.3      G      On receipt of a *UK firm's* notice of intention (prepared in accordance with SUP 13.4.2(1) and SUP 13.5.2R) then:

- (1) ...
- ...
- (3) if the *EEA right* is derived from the *Insurance Directives*, the *FSA* has one month to consider it and, if satisfied with the proposal, notify the relevant *Host State regulator*–;
- (4) if the *EEA right* is derived from the *Insurance Mediation Directive*:
  - (a) where the *EEA State* in which the *UK firm* is seeking to provide services has notified the European Commission of its wish to be informed of the intention of persons to provide cross border services in its territory in accordance with article 6(2) of that directive, the *FSA* has one month to notify the relevant *Host State regulator*;
  - (b) otherwise, the *UK firm* may start providing *cross border services* as

soon as it satisfies the relevant conditions (see SUP 13.4.2G).

13.4.3A G The list of the *EEA States* that have notified the European Commission of their wish to be informed in accordance with article 6(2) of the *Insurance Mediation Directive* is published on the *FSA's* website at [www.fsa.gov.uk](http://www.fsa.gov.uk).

13.4.4 G If a *UK firm* has given the *FSA* a notice of intention in the required form, then:

(1) ...

(2) (a) ...

(b) The issue or refusal of a *consent notice* under paragraph 20(3A) of Part III of Schedule 3 to the *Act* is the consequence of a regulatory decision, and this *consent notice* (unlike the *consent notice* for establishment of a *branch*) is not a *statutory notice* as set out in section 395 of the *Act*. As such, the *FSA* will follow the decision making procedures set out in *DEC 1* (Application, Purpose and Introduction). A *UK firm* that receives notice that the *FSA* refuses to give a *consent notice* may refer the matter to the *Tribunal* under paragraph 20(4A) of Part III of Schedule 3 to the *Act*. For procedures relating to references to the *Tribunal* see *DEC 5* (References to the *Tribunal*, publication and service of notices) or

(3) if the *UK firm's EEA right* derives from the *Insurance Mediation Directive*, and the *EEA State* in which the *UK firm* is seeking to provide services has notified the European Commission of its wish to be informed of the intention of *persons* to provide *cross border services* in its territory in accordance with article 6(2) of that directive, paragraph 20(3B)(a) of Part III of Schedule 3 to the *Act* requires the *FSA* to send a copy of the notice of intention to the *Host State regulator* within one month of receipt.

13.4.5 G When the *FSA* sends a copy of a notice of intention, or if it gives a *consent notice* to the *Host State regulator*, it must inform the *UK firm* in writing that it has done so (paragraphs 20 (3B)(b) and (4) of Schedule 3 to the *Act*).

...

## 13.5 Notices of intention

Specified contents: notice of intention to establish a branch

13.5.1 R A *UK firm* wishing to establish a *branch* in a particular *EEA State* for the first time under an *EEA right* must include in its notice of intention given to the *FSA*:

(1) (a) ~~the~~ information specified in *SUP 13 Ann 1R*; and

(b) if the *UK firm* is passporting under the *Insurance Directives*, the information specified in *SUP 13 Ann 2R*; or

- (2) if the *UK firm* is passporting under the *Insurance Mediation Directive*, only a statement that it intends to carry on *insurance mediation* in that State by establishing a *branch*.

Specified contents: notice of intention to provide cross border services

13.5.2 R A *UK firm* wishing to provide *cross border services* into a particular *EEA State* for the first time under an *EEA right* must include, in its notice of intention given to the *FSA*:

(1) ...

- (3) if the *UK firm* is passporting under the *Insurance Mediation Directive*, only a statement that it intends to carry on *insurance mediation* in that State by provision of *cross border services*.

...

13.6.1 G Where a *UK firm* is exercising an *EEA right*, other than under the *Insurance Mediation Directive* (see *SUP 13.6.9A G*), and has established a *branch* in another *EEA State*, any changes to the details of the *branch* are governed by the *EEA Passport Rights Regulations*. References to regulations in this section are to the *EEA Passport Rights Regulations*. A *UK firm* which is not an *authorised person* should note that, under regulation 18, contravention of the prohibition imposed by regulation 11(1), 13(1) or 15(1) is an offence. It is a defence, however, for the *UK firm* to show that it took all reasonable precautions and exercised due diligence to avoid committing the offence.

...

13.6.9 G ...  
Firms passporting under the *Insurance Mediation Directive*

13.6.9A G A *UK firm* exercising its *EEA right* under the *Insurance Mediation Directive* to establish a *branch* in another *EEA State* is not required to supply *requisite details* or relevant details. Therefore there are no *requisite details* or relevant details for changes to a *branch* established in another *EEA State* under the *Insurance Mediation Directive*.

...

13.7.1 G Where a *UK firm* is exercising an *EEA right* under the *Investment Services Directive* or *Insurance Directives* ~~other than under the *Banking Consolidation Directive*~~, and is providing *cross border services* into another *EEA State*, any changes to the details of the services are governed by the *EEA Passport Rights Regulations*. References to regulations in this

section are to the *EEA Passport Rights Regulations*. A *UK firm* which is not an *authorised person* should note that contravention of the prohibition imposed by regulation 12(1) or 16(1) is an offence. It is a defence, however, for the *UK firm* to show that it took all reasonable precautions and exercised due diligence to avoid committing the offence.

...

13.7.10 G ...  
Firms passporting under the Banking Consolidation Directive and Insurance Mediation Directive

13.7.11 G A *UK firm* providing *cross border services* under the *Banking Consolidation Directive* or Insurance Mediation Directive is not required to supply *requisite details* or relevant details. Therefore there are no *requisite details* or relevant details for changes to *cross border services* provided under the *Banking Consolidation Directive* or Insurance Mediation Directive.

...

14.2.1 G Where an *incoming EEA firm* is exercising an *EEA right*, other than under the Insurance Mediation Directive, and has established a *branch* in the *United Kingdom*, the *EEA Passport Rights Regulations* govern any changes to the details of that *branch*. Where an *incoming EEA firm* has complied with the relevant requirements in the *EEA Passport Rights Regulations*, then the *firm's permission* given under Schedule 3 to the *Act* is to be treated as varied accordingly. All references to regulations in *SUP 14* are to the *EEA Passport Rights Regulations*.

...

Schedule 2 Notification requirements

...

SUP 2 Table:

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
... <u>SUP 11.4.2A R</u>	<u>Controllers - proposed change of control notification from a UK insurance intermediary</u>	<p><u>When acquiring control:</u></p> <p><u>(1) the name of the firm;</u></p> <p><u>(2) the name of the controller or proposed controller and, if it is a body corporate and is not an authorised person, the names of its directors and its controllers;</u></p> <p><u>(3) a description of the proposed event including the shareholding and voting power of the person concerned, both before and after the proposed event; and</u></p>	<p><u>(1) a person acquiring control or ceasing to have control;</u></p> <p><u>(2) a person becoming or ceasing to be a parent undertaking</u></p>	<p><u>As soon as the firm becomes aware that a person is proposing to take such a step that would result in the event concerned; or if the event takes place without the knowledge of the firm, 14 days of the firm becoming aware of the event concerned</u></p>

		<p><u>(4) any other information of which the FSA would reasonably expect notice, including information which could have a material impact on any of the approval requirements in section 186(2) of the Act and any relevant supporting documentation.</u></p> <p><u>The notification need only contain as much of the information the firm is able to provide, having made reasonable enquiries from persons and other sources as appropriate.</u></p> <p><u>When reducing control:</u></p> <p><u>(1) name of the controller; and</u></p> <p><u>(2) details of the extent of control (if any) which the controller will have following the change in control</u></p>		
<i>SUP 11.6.2R to SUP 11.6.5R</i>	...	...	After submitting a notification under <i>SUP 11.4.2R</i> or <i>SUP 11.4.2A R</i> and until the change in <i>control</i> occurs, ...	...



<i>SUP 11.6.4R</i>	...	...	A change in <i>control</i> previously notified under <i>SUP 11.4.2R</i> , <u><i>SUP 11.4.2A R</i></u> or <i>SUP 11.4.4R</i> taking place; ...	...
<i>SUP 11.8.1R</i>	...	The fact of:  (1) ...  (4) a <i>controller</i> , who is authorised in <i>another EEA State</i> as an <i>ISD investment firm</i> or <i>BCD credit institution</i> or under the <i>Insurance Directives</i> or <u>the <i>Insurance Mediation Directive</i></u> , ceasing to be so authorised (registered in the case of an <u><i>IMD insurance intermediary</i></u> )	The <i>firm</i> becoming aware of:  (1) ...  (4) a <i>controller</i> , who is authorised in <i>another EEA State</i> as an <i>ISD investment firm</i> or <i>BCD credit institution</i> or under the <i>Insurance Directives</i> or <u>the <i>Insurance Mediation Directive</i></u> , ceasing to be so authorised (registered in the case of an <u><i>IMD insurance intermediary</i></u> )	...

...

Schedule 4

Powers exercised

G

1 Table

The following powers and related provisions in the *Act* have been exercised by the *FSA* to make the rules in *SUP*:

...

(15) Section 340 (Appointment)

(15A) Section 341 (Access to books etc.)

...

## Annex G

### Amendments to the Glossary

#### Part I: New definitions

Insert the following new definitions in the appropriate alphabetical position:

<i>administering a regulated mortgage contract</i>	the <i>regulated activity</i> , specified in article 61(2) of the <i>Regulated Activities Order</i> , which is in summary: administering a <i>regulated mortgage contract</i> where the contract was entered into after 31 October 2004.
<i>advising on regulated mortgage contracts</i>	the <i>regulated activity</i> , specified in article 53A of the <i>Regulated Activities Order</i> , which is in summary: advising a <i>person</i> if the advice: <ul style="list-style-type: none"><li>(a) is given to the <i>person</i> in his capacity as a borrower or potential borrower; and</li><li>(b) is advice on the merits of his:<ul style="list-style-type: none"><li>(i) entering into a particular <i>regulated mortgage contract</i>; or</li><li>(ii) varying the terms of a <i>regulated mortgage contract</i> entered into by him after 31 October 2004 in such a way as to vary his obligations under that contract.</li></ul></li></ul>
<i>arranging (bringing about) regulated mortgage contracts</i>	the <i>regulated activity</i> , specified in article 25A(1) of the <i>Regulated Activities Order</i> , which is in summary: making arrangements for another <i>person</i> to: <ul style="list-style-type: none"><li>(a) enter into a <i>regulated mortgage contract</i> as borrower; or</li><li>(b) vary the terms of a <i>regulated mortgage contract</i> entered into by him as borrower after 31 October 2004.</li></ul> (see also <i>arranging</i> (in relation to <i>regulated mortgage contracts</i> ) and <i>making arrangements with a view to regulated mortgage contracts</i> .)
<i>assisting in the administration and performance of a contract of insurance</i>	the <i>regulated activity</i> , specified in article 39A of the <i>Regulated Activities Order</i> (Assisting in the administration and performance of a contract of insurance) of assisting in the administration and performance of a contract of insurance.
<i>Business Order</i>	the Financial Services and Markets Act 2000 (Carrying on Regulated Activities by Way of Business Order) 2001 (SI 2001/1177).

[CASS	the Client Assets sourcebook.] <sup>1</sup>
<i>client money (insurance) distribution rules</i>	the <i>rules</i> in CASS 5.6 (Client money distribution).
<i>commercial customer contracts of large risks</i>	(in <i>ICOB</i> and CASS 5) a <i>customer</i> who is not a <i>retail customer</i> . (in <i>ICOB</i> ) <i>contracts of insurance</i> covering risks within the following categories, in accordance with article 5(d) of the <i>First Non-Life Directive</i> :
	(a) <i>railway rolling stock, aircraft, ships</i> (sea, lake, river and canal vessels), <i>goods in transit, aircraft liability and liability of ships</i> (sea, lake, river and canal vessels);
	(b) <u><i>credit and suretyship, where the policyholder is engaged professionally in an industrial or commercial activity or in one of the liberal professions, and the risks relate to such activity;</i></u>
	(c) <u><i>land vehicles (other than railway rolling stock), fire and natural forces, other damage to property, motor vehicle liability, general liability, and miscellaneous financial loss, in so far as the policyholder exceeds the limits of at least two of the following three criteria:</i></u>
	(i) balance sheet total: € 6.2 million;
	(ii) net turnover: €12.8 million;
	(iii) average number of <i>employees</i> during the financial year: 250.
<i>Distance Marketing Directive</i>	the Directive of the Council and Parliament of 23 September 2002 on distance marketing of consumer financial services (No 2002/65/EC).
<i>entering into a regulated mortgage contract</i>	the <i>regulated activity</i> , specified in article 62(1) of the <i>Regulated Activities Order</i> , which is in summary: entering into a <i>regulated mortgage contract</i> as lender.
<i>ICOB</i>	the Insurance: Conduct of Business sourcebook.
<i>IMD</i>	<i>Insurance Mediation Directive</i> .
<i>IMD insurance intermediary</i>	(as defined in article 2(5) of the <i>IMD</i> ) any natural or legal person who, for remuneration, takes up or pursues <i>insurance mediation</i> .
<i>IMD insurance undertaking</i>	(as defined in article 2(1) of the <i>IMD</i> ) an undertaking which has received official authorisation in accordance with article 6

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<sup>1</sup> The definition of ‘Client Assets sourcebook’ (CASS) was made in December 2003 in the Client Assets Sourcebook Instrument 2003 and came into force on 1 January 2004.

	of the <i>Consolidated Life Directive</i> or article 6 of the <i>First Non-Life Directive</i> .
<i>IMD reinsurance intermediary</i>	(as defined in article 2(6) of the <i>IMD</i> ) any natural or legal person who, for remuneration, takes up or pursues <i>reinsurance mediation</i> .
<i>IMD reinsurance undertaking</i>	(as defined in article 2(2) of the <i>IMD</i> ) an undertaking, other than an <i>IMD insurance undertaking</i> or a non-member-country <i>insurance undertaking</i> , the main business of which consists in accepting risks ceded by an <i>IMD insurance undertaking</i> , a non-member country <i>insurance undertaking</i> or other <i>IMD reinsurance undertaking</i> .
<i>insurance intermediary</i>	a <i>firm</i> carrying on <i>insurance mediation activity</i> .
<i>Insurance Intermediaries Order</i>	the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No. 2) (Insurance Intermediaries) Order 2003 (SI 2003/1476).
<i>insurance mediation</i>	<p>(as defined in article 2(3) of the <i>IMD</i>) the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim.</p> <p>These activities when undertaken by an <i>IMD insurance undertaking</i> or an employee of an <i>IMD insurance undertaking</i> who is acting under the responsibility of the <i>IMD insurance undertaking</i> shall not be considered as <i>insurance mediation</i>.</p> <p>The provision of information on an incidental basis in the context of another professional activity provided that the purpose of that activity is not to assist the customer in concluding or performing an insurance contract, the management of claims of an <i>IMD insurance undertaking</i> on a professional basis, and loss adjusting and expert appraisal of claims shall also not be considered as <i>insurance mediation</i>.</p>
<i>[insurance mediation activity]</i>	<p>any of the following <i>regulated activities</i> carried on in relation to a <i>contract of insurance</i> or <i>rights to or interests in a life policy</i>:</p> <ul style="list-style-type: none"> <li>(a) <i>dealing in investments as agent</i> (article 21);</li> <li>(b) <i>arranging (bringing about) deals in investments</i> (article 25(1));</li> <li>(c) <i>making arrangements with a view to transactions in investments</i> (article 25(2));</li> <li>(d) <i>assisting in the administration and performance of a contract of insurance</i> (article 39A);</li> <li>(e) <i>advising on investments</i> (article 53);</li> <li>(f) <i>agreeing to carry on a regulated activity</i> in (a) to (e)</li> </ul>

(article 64).]<sup>2</sup>

<i>Insurance Mediation Directive</i>	the European Parliament and Council Directive of 9 December 2002 on insurance mediation (No 2002/92/EC).
<i>limit of indemnity</i>	(in PRU 9.2 (Professional indemnity insurance requirements for insurance and mortgage mediation activities)) the sum available to indemnify a <i>firm</i> in respect of each claim made under its professional indemnity insurance.
<i>long-term care insurance contract</i>	(as defined in article 1 of the <i>Insurance Intermediaries Order</i> ) a <i>contract of insurance</i> in respect of which the following conditions are met:  (a) the purpose (or one of the purposes) of the <i>policy</i> is to protect the <i>policyholder</i> against the risk of becoming unable to live independently without assistance in consequence of a deterioration of mental or physical health, injury, sickness or other infirmity;  (b) benefits under the contract are payable in respect of:  (i) services,  (ii) accommodation, or  (iii) goods,  which are (or which is) necessary or desirable due to a deterioration of mental or physical health, injury, sickness or other infirmity;  (c) the contract is expressed to be in effect until the death of the <i>policyholder</i> (except that the contract may give the <i>policyholder</i> the option to surrender the <i>policy</i> ); and  (d) the benefits under the contract are capable of being paid throughout the life of the <i>policyholder</i> .
<i>making arrangements with a view to regulated mortgage contracts</i>	the <i>regulated activity</i> , specified in article 25A(2) of the <i>Regulated Activities Order</i> , which is in summary: making arrangements with a view to a <i>person</i> who participates in the arrangements entering into a <i>regulated mortgage contract</i> as borrower.  (see also <i>arranging</i> (in relation to <i>regulated mortgage contracts</i> ) and <i>arranging (bringing about) regulated mortgage contracts</i> .)
<i>MCOB</i>	the Mortgages: Conduct of Business sourcebook.

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<sup>2</sup> The definition of ‘insurance mediation activity’ was made in September 2003 in the Mortgage Firms and Insurance Intermediaries (Application Fees) (No 1) Instrument 2003 and came into force on 1 November 2003.

<i>mortgage administrator</i>	a firm with <i>permission</i> (or which ought to have <i>permission</i> ) for <i>administering a regulated mortgage contract</i> .
<i>mortgage adviser</i>	a firm with <i>permission</i> (or which ought to have <i>permission</i> ) for <i>advising on regulated mortgage contracts</i> .
<i>mortgage arranger</i>	a firm with <i>permission</i> (or which ought to have <i>permission</i> ) for <i>arranging</i> (see also <i>arranging (bringing about) regulated mortgage contracts and making arrangements with a view to regulated mortgage contracts</i> ).
<i>mortgage intermediary</i>	a firm with <i>permission</i> (or which ought to have <i>permission</i> ) to carry on <i>mortgage mediation activity</i> .
<i>mortgage lender</i>	a firm with <i>permission</i> (or which ought to have <i>permission</i> ) for <i>entering into a regulated mortgage contract</i> .
[ <i>mortgage mediation activity</i> ]	(as defined in article 26 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment)(No. 1) Order 2003 (SI 2003/1475)) any of the following <i>regulated activities</i> : <ul style="list-style-type: none"> <li>(a) <i>arranging (bringing about) regulated mortgage contracts</i> (article 25A(1));</li> <li>(b) <i>making arrangements with a view to regulated mortgage contracts</i> (article 25A(2));</li> <li>(c) <i>advising on regulated mortgage contracts</i> (article 53A);</li> <li>(d) <i>agreeing to carry on a regulated activity in (a) to (c)</i> (article 64).]<sup>3</sup></li> </ul>
<i>non-investment insurance contract</i>	a <i>contract of insurance</i> which is a <i>general insurance contract</i> or a <i>pure protection contract</i> but which is not a <i>long-term care insurance contract</i> .
<i>protected non-investment insurance mediation</i>	<i>insurance mediation activities</i> which are covered by the <i>compensation scheme</i> , as defined in COMP 5.6.1R.
<i>regulated mortgage activity</i>	any of the following activities specified in Part II of the <i>Regulated Activities Order</i> (Specified Activities): <ul style="list-style-type: none"> <li>(a) <i>arranging (bringing about) regulated mortgage contracts</i> (article 25A(1));</li> <li>(b) <i>making arrangements with a view to regulated mortgage contracts</i> (article 25A(2));</li> <li>(c) <i>advising on regulated mortgage contracts</i> (article 53A);</li> <li>(d) <i>entering into a regulated mortgage contract</i> (article 61(1));</li> <li>(e) <i>administering a regulated mortgage contract</i> (article</li> </ul>

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<sup>3</sup> The definition of ‘mortgage mediation activity’ was made in September 2003 in the Mortgage Firms and Insurance Intermediaries (Application Fees) (No 1) Instrument 2003 and came into force on 1 November 2003.

	61(2));
	(f) <i>agreeing to carry on a regulated activity</i> in (a) to (e) (article 64).
<i>regulated mortgage contract</i>	(a) (in relation to a contract) (in accordance with article 61(3) of the <i>Regulated Activities Order</i> ) a contract which, at the time it is entered into, meets the following conditions: <ul style="list-style-type: none"> <li>(i) a lender provides credit to an individual or to trustees (the ‘borrower’); and</li> <li>(ii) the obligation of the borrower to repay is secured by a first legal mortgage on land (other than timeshare accommodation) in the <i>United Kingdom</i>, at least 40% of which is used, or is intended to be used, as or in connection with a dwelling by the borrower or (in the case of credit provided to trustees) by an individual who is a beneficiary of the trust, or by a <i>person</i> who is in relation to the borrower or (in the case of credit provided to trustees) a beneficiary of the trust: <ul style="list-style-type: none"> <li>(A) that <i>person</i>’s spouse; or</li> <li>(B) a <i>person</i> (whether or not of the opposite sex) whose relationship with that <i>person</i> has the characteristics of the relationship between husband and wife; or</li> <li>(C) that <i>person</i>’s parent, brother, sister, child, grandparent or grandchild.</li> </ul> </li> </ul>
	(b) (in relation to a <i>specified investment</i> ) the <i>investment</i> , specified in article 88 of the <i>Regulated Activities Order</i> , which is rights under a <i>regulated mortgage contract</i> within (a).
<i>reinsurance contract</i>	(in <i>ICOB</i> , <i>CASS 5</i> and <i>COMP</i> ) a <i>contract of insurance</i> covering all or part of a risk to which a <i>person</i> is exposed under a <i>contract of insurance</i> .
<i>reinsurance mediation</i>	(as defined in article 2.4 of the <i>IMD</i> ) the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of reinsurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim.  These activities when undertaken by a <i>IMD reinsurance undertaking</i> or an employee of a <i>IMD reinsurance undertaking</i> who is acting under the responsibility of the <i>IMD reinsurance undertaking</i> shall not be considered as <i>reinsurance mediation</i> .  The provision of information on an incidental basis in the

	context of another professional activity provided that the purpose of that activity is not to assist the customer in concluding or performing a reinsurance contract, the management of claims of a <i>IMD reinsurance undertaking</i> on a professional basis, and loss adjusting and expert appraisal of claims shall also not be considered as <i>reinsurance mediation</i> .
<i>relevant investment</i>	(in accordance with article 3(1) of the <i>Regulated Activities Order</i> (Interpretation)): <ul style="list-style-type: none"> <li>(a) a <i>contractually based investment</i>;</li> <li>(b) a <i>pure protection contract</i>;</li> <li>(c) a <i>general insurance contract</i>;</li> <li>(d) rights to or interests in an <i>investment</i> falling within (a).</li> </ul>
<i>renewal</i>	carrying forward a contract, at the point of expiry and as a successive or separate operation of the same nature as the preceding contract, between the same contractual parties.
<i>retail customer</i>	(in accordance with the meaning of ‘consumer’ in article 2(d) of the <i>Distance Marketing Directive</i> an individual who is acting for purposes which are outside his trade, business or profession.
<i>social housing firm</i>	(in <i>PRU 9.3</i> (Capital resources for insurance and mortgage mediation activity and mortgage lending and administration)) a wholly-owned <i>subsidiary</i> of: <ul style="list-style-type: none"> <li>(a) a local authority; or</li> <li>(b) a registered social landlord;</li> </ul> which carries on non-profit <i>regulated activities</i> in connection with housing.
<i>UK insurance intermediary</i>	a <i>UK domestic firm</i> which has <i>Part IV permission</i> to carry on <i>insurance mediation activity</i> but no other <i>regulated activity</i> .

## Part 2: Amended definitions

In this part, underlining indicates new text and striking through indicates deleted text.

<i>advising on investments</i>	the <i>regulated activity</i> , specified in article 53 of the <i>Regulated Activities Order</i> (Advising on investments), which is in summary: advising a <i>person</i> if the advice is: <ul style="list-style-type: none"> <li>(a) given to the <i>person</i> in his capacity as an investor or potential investor, or in his capacity as agent for an investor or a potential investor; and</li> <li>(b) advice on the merits of his doing any of the following (whether as principal or agent): <ul style="list-style-type: none"> <li>(i) <i>buying, selling</i>, subscribing for or underwriting a particular <i>investment</i> which is a <i>security</i> or <u><i>contractually based investment relevant</i></u></li> </ul> </li> </ul>
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investment (that is, any *designated investment*, *funeral plan contract*, *pure protection contract*, *general insurance contract* or right to or interest in a *funeral plan contract*; or

- (ii) exercising any right conferred by such an *investment*, other than a *pure protection contract* or a *general insurance contract*, to buy, sell, subscribe for or underwrite such an *investment*.

arranging

- (a) (except in relation to a *regulated mortgage contract*.) *arranging (bringing about) deals in investments, making arrangements with a view to transactions in investments or agreeing to carry on ~~any~~ either of those regulated activities.*
- (b) (in relation to a *regulated mortgage contract*) *arranging (bringing about) regulated mortgage contracts, making arrangements with a view to regulated mortgage contracts or agreeing to carry on either of those regulated activities.*

arranging (bringing about) deals in investments

the regulated activity, specified in article 25(1) of the *Regulated Activities Order*, which is in summary: making arrangements for another *person* (whether as *principal* or agent) to buy, sell, subscribe for or underwrite a particular *investment* which is:

- (a) a *designated investment*; or
- (b) a *funeral plan contract*; or
- (c) the *underwriting capacity of a Lloyd's syndicate*; or
- (d) *membership of a Lloyd's syndicate*; or
- (da) a *pure protection contract*; or
- (db) a *general insurance contract*; or
- (e) *rights to or interests in investments* in (b), (c) or (d).

branch

- (a) (in relation to a *credit institution*):

...

- (d) (in relation to an *IMD insurance intermediary*):

(i) a place of business which is a part of an *IMD insurance intermediary*, not being the principal place of business, which has no separate legal personality and which provides *insurance mediation* for which the *IMD insurance intermediary* has been registered;

(ii) for the purposes of the *Insurance Mediation Directive*, all the places of business set up in the same *EEA State* by an *IMD insurance intermediary* with headquarters in another *EEA State* are to be regarded as a single *branch*.

- (e) (in relation to an *IMD reinsurance intermediary*):
- (i) a place of business which is a part of an *IMD reinsurance intermediary*, not being the principal place of business, which has no separate legal personality and which provides *reinsurance mediation* for which the *IMD reinsurance intermediary* has been registered;
  - (ii) for the purposes of the *Insurance Mediation Directive*, all the places of business set up in the same *EEA State* by an *IMD reinsurance intermediary* with headquarters in another *EEA State* are to be regarded as a single *branch*.
- client*
- (1) (except in *ML*, in *PROF*; in relation to a regulated mortgage contract) any person with or for whom a firm conducts or intends to conduct *designated investment business* or any other *regulated activity*; and:
  - ...
  - (4) (in relation to a regulated mortgage contract, except in *ML* and *PROF*) the individual or trustee who is the borrower or potential borrower under that contract.
- client money*
- (1) (in *COB* and *CASS 2 to 4* ) subject to the *client money rules*, ...
  - (2) (in *CASS 5*) subject to the *client money rules*, money of any currency which, in the course of carrying on *insurance mediation activity*, a firm holds on behalf of a *client* or which a firm treats as *client money* in accordance with the *client money rules*;
  - (3) (in *PRU 9*):
    - (a) in relation to an *insurance intermediary* when acting as such, money which is *client money* in (2);
    - (b) in relation to a *mortgage intermediary* when acting as such, money of any currency which in the course of carrying on *mortgage mediation activity*, the firm holds on behalf of a *client*, either in a bank account or in the form of cash.
- client money rules*
- (a) (in *CASS* and *COB*) *CASS 4.1 to 4.3*;
  - (b) (in *CASS 5*) *CASS 5.1 to 5.5*.
- COB*
- the Conduct of Business sourcebook.

*commission*

any form of commission, including a benefit of any kind, offered or given in connection with;

- (a) designated investment business; or
- (b) insurance mediation activity in connection with a non-investment insurance contract.

*contracts of insurance*

- (1) ...
- (2) ...
  - (a) ...
  - ...
  - (e) contracts of a kind referred to in article 1(2)(e) of the First Consolidated Life Directive (Collective insurance etc); and
  - (f) contracts of a kind referred to in article 1(3) of the First Consolidated Life Directive (Social insurance);

...

*controller*

- (1) ~~(in accordance with section 422 of the Act (Controller))~~ (in relation to a *firm* or other *undertaking* ("A") other than an UK insurance intermediary) ~~(in accordance with section 422 of the Act (Controller))~~ a *person* who falls within any of the following cases; the cases are where the *person*:
  - (a) holds 10% or more of the shares in A; or
  - (b) is able to exercise significant influence over the management of A through his shareholding in A; or
  - (c) holds 10% or more of the shares in a *parent undertaking* ("P") of A; or
  - (d) is able to exercise significant influence over the management of P through his shareholding in P; or
  - (e) is entitled to exercise, or control the exercise of, 10% or more of the *voting power* in A; or
  - (f) is able to exercise significant influence over the management of A through his *voting power* in A; or
  - (g) is entitled to exercise, or control the exercise of, 10% or more of the *voting power* in P; or
  - (h) is able to exercise significant influence over the management of P through his *voting power* in P;
- (2) (in relation to an UK insurance intermediary) (in accordance with article 17 of the Insurance Intermediaries Order) a person who would fall within

(1) if 20% were substituted for 10%;

in (1) and (2) of this definition:

(i) "the person" means:

...

*customer*

- (1) (except in *COB 3*, *ICOB*, *MCOB 3* and *CASS 5*) a *client* who is not a *market counterparty*.
- (2) (in *COB 3* and *MCOB 3*) a *person* in (1) or a *person* who would be such a *person* if he were a *client*.
- (3) (in *ICOB*) a *person* who is a *policyholder*, or a *prospective policyholder*, of a *policy* other than a *reinsurance contract*.
- (4) (in *CASS 5*) a *client*.

*dealing in investments as agent*

the *regulated activity*, specified in article 21 of the *Regulated Activities Order* (Dealing in investments as agent), which is in summary: *buying, selling, subscribing for or underwriting designated investments, pure protection contracts or general insurance contracts* as agent.

*designated investment business*

any of the following activities, specified in Part II of the *Regulated Activities Order* (Specified Activities), which is carried on by way of business:...

- (b) *dealing in investments as agent* (article 21), but only in relation to *designated investments*;

...

*director*

- (1) (except in *CIS*) (in relation to any of the following (whether constituted in the *United Kingdom* or under the law of a country or territory outside it)):
  - (a) an unincorporated association;
  - (b) a *body corporate*;
  - (c) (in *SYSC*, *PRU 9.1 (Responsibility for insurance mediation activity)* and *SUP 10 (Approved persons)*) a *partnership*;
  - (d) (in *SYSC* and *SUP 10 (Approved persons)*) a *sole trader*;

...

*EEA authorisation*

(in accordance with paragraph 6 of Schedule 3 to the *Act* (EEA Passport Rights))

- (a) in relation to an *IMD insurance intermediary* or an *IMD*

reinsurance intermediary, registration with its Home State regulator under article 3 of the Insurance Mediation Directive;

(b) in relation to any other EEA firm, authorisation granted to an EEA firm by its Home State regulator for the purpose of the relevant Single Market Directive.

EEA firm

(in accordance with paragraph 5 of Schedule 3 to the Act (EEA Passport Rights)) any of the following, if it does not have its ~~head-office~~ relevant office in the United Kingdom:

- (a) an investment firm (as defined in article 1(2) of the *Investment Services Directive*) which is authorised (within the meaning of article 3) by its Home State regulator;
- (b) a credit institution (as defined in article 1 of the *Banking Consolidation Directive*) which is authorised (within the meaning of article 4) by its Home State regulator;
- (c) a financial institution (as defined in article 1 of the *Banking Consolidation Directive*) which is a subsidiary of the kind mentioned in article 19 and which fulfils the conditions in articles 18 and 19;
- (d) an undertaking pursuing the activity of direct insurance (within the meaning of article 1 of the *First Life Directive* or of the *First Non-Life Directive*) which has received authorisation under article 6 from its Home State regulator;
- (e) an IMD insurance intermediary or an IMD reinsurance intermediary (as defined in article 2 of the IMD) which has registered under article 3 of that directive with its Home State regulator;
- (f) a management company (as defined in article 1a of the *UCITS Directive*) which has been authorised under article 5 of that directive by its Home State regulator.

in this definition, relevant office means:

(i) in relation to a firm falling within sub-paragraph (e), which has a registered office, its registered office;

(ii) in relation to any other firm falling within any other paragraph, its head office.

EEA right

(in accordance with paragraph 7 of Schedule 3 to the Act (EEA Passport Rights)) the entitlement of a person to establish a branch or provide services in an EEA State other than that in which he has his ~~head-office~~ relevant office:

- (a) in accordance with the Treaty as applied in the European Economic Area; and

(b) subject to the conditions of the relevant *Single Market Directive*.

in this definition, relevant office means:

(i) in relation to a *person* who has a registered office and whose entitlement is subject to the conditions of the *Insurance Mediation Directive*, his registered office; and

(ii) in relation to any other *person*, his head office.

*energy market participant*

a *firm*:

(a) whose *permission*:

(i) includes a *requirement* that the *firm* must not carry on any *designated investment business* other than *energy market activity*;

(ii) does not include a *requirement* that it comply with *IPRU(INV) 5* (Investment management firms) or 13 (Personal investment firms); and

(b) which is not an *authorised professional firm, bank, building society, credit union, friendly society, ICVC, insurer, ISD investment firm, media firm, oil market participant, service company, insurance intermediary, mortgage administrator, mortgage intermediary, mortgage lender, incoming EEA firm* (without a *top-up permission*), or *incoming Treaty firm* (without a *top-up permission*).

*establishment conditions*

(in relation to the establishment of a *branch* in the *United Kingdom*) the conditions specified in paragraph 13 of Schedule 3 to the *Act* (EEA Passport Rights), which are that:

(a) if the *firm* falls within paragraph (a), (b), (c), ~~(d)~~ or (f) in the definition of "*EEA firm*":

(i) ...

(b) if the *firm* falls within paragraph (e) in the definition of "*EEA firm*":

(i) the *EEA firm* has given its *Home State regulator* notice of its intention to establish a *branch* in the *United Kingdom*;

(ii) the *FSA* has received notice ("a regulator's notice") from the *firm's Home State regulator* that the *firm* intends to establish a *branch* in the *United Kingdom*;

(iii) the *EEA firm's Home State regulator* has informed it that the regulator's notice has been sent to the *FSA*; and

(iv) one *month* has elapsed beginning with the date on which the *EEA firm's Home State regulator* informed the *firm* that it had sent the regulator's notice to the *FSA*.

Home State

(1)

...

(5) (in relation to an *IMD insurance intermediary* or an *IMD reinsurance intermediary*):

(a) where the *insurance intermediary* is a natural person, the Member State in which his residence is situated and in which he carries on business;

(b) where the *insurance intermediary* is a legal person, the Member State in which its registered office is situated or, if under its national law it has no registered office, the Member State in which its head office is situated.

~~(5)~~ (6) (in relation to a market) ...

~~(6)~~ (7) (in relation to a *Treaty firm*) ...

*making arrangements with a view to transactions in investments*

the *regulated activity*, specified in article 25(2) of the *Regulated Activities Order* (Arranging deals in investments), which is in summary: making arrangements with a view to a *person* who participates in the arrangements *buying, selling, subscribing for or underwriting* any of the following *investments* (whether as *principal* or as agent):

(a) a *designated investment*; or

(b) a *funeral plan contract*; or

(c) the *underwriting capacity of a Lloyd's syndicate*; or

(d) *membership of a Lloyd's syndicate*; or

(e) *rights to or interests in investments* in (b), (c) or (d); or

(f) a *pure protection contract*; or

(g) a *general insurance contract*.

*oil market participant*

a *firm*:

(a) whose permission:

(i) includes a *requirement* that the firm must not carry on any *designated investment business* other than *oil market activity*; and

(ii) does not include a *requirement* that it comply with *IPRU(INV) 5* (Investment management firms) or 13 (Personal investment firms); and

(b) which is not an *authorised professional firm, bank, building society, credit union, friendly society, ICVC, insurer, ISD investment firm, media firm, service company, insurance intermediary, mortgage administrator, mortgage intermediary, mortgage lender, incoming EEA firm* (without a *top-up permission*), or *incoming Treaty firm* (without a *top-up*

*permission).*

*overseas person*

(in accordance with article 3(1) of the *Regulated Activities Order (Interpretation)*) a *person* who:

(a) carries on any of the following *regulated activities*:

- (i) *dealing in investments as principal*;
- (ii) *dealing in investments as agent*;
- (iii) *arranging (bringing about) deals in investments*;
- (iv) *arranging (bringing about) regulated mortgage contracts*;
- (v) *making arrangements with a view to regulated mortgage contracts*;
- (~~ix~~) *making arrangements with a view to transactions in investments*;
- (~~x~~) *managing investments*;
- (~~xii~~) *safe custody and administering investments*;
- (~~xiii~~) *sending dematerialised instructions*;
- (~~xiv~~) *causing dematerialised instructions to be sent*;
- (~~xv~~) *establishing, operating or winding up a collective investment scheme*;
- (~~xvi~~) *acting as trustee of an authorised unit trust scheme*;
- (~~xvii~~) *acting as the depositary or sole director of an open-ended investment company*;
- (~~xviii~~) *establishing, operating or winding up a stakeholder pension scheme*;
- (~~xix~~) *advising on investments*;
- (~~xx~~) *advising on regulated mortgage contracts*;
- (~~xxi~~) *entering into a regulated mortgage contract*;
- (~~xxii~~) *administering a regulated mortgage contract*;
- (~~xxiii~~) *agreeing to carry on those regulated activities, disregarding the exclusion in article 72 of the Regulated Activities Order (Overseas persons)*; but

(b) does not carry on any such activity, or offer to do so, from a permanent place of business maintained by him in the *United Kingdom*.

*participant firm*

(1) (except in *COMP 13*) a *firm* or a member other than:

- (a) in accordance with section 213(10) of the *Act* (The compensation scheme) and regulation 2 of the *Electing Participants Regulations* (Persons not to be regarded as relevant persons) an *incoming EEA firm*



which is:

(i) a *credit institution*;

(ii) an *ISD investment firm*;

[(iii) a *UCITS management company*; ~~or~~

(iv)]<sup>4</sup> both (i) and (ii); or

(v) an *IMD insurance intermediary* or an *IMD reinsurance intermediary* which is neither (i) or (ii);

in relation to its *passport activities*, unless it has *top-up cover*;

*premium*

...

(1) (except in *ICOB* and *CASS 5*) ...

(2) (except in *ICOB* and *CASS 5*) ...

(2A) (in *ICOB* and *CASS 5*) as in (1) and (2) except that 'insurance undertaking' is substituted for 'insurer' (except where 'insurer' is used in the heading to *SUP 16.8*).

*primary pooling event*

...

(1) (in *CASS 4*) an event that occurs in the circumstances described in ~~*COB 9.5.5R*~~ *CASS 4.4.5R* (Failure of the authorised firm: primary pooling event).

(2) (in *CASS 5*) an event that occurs in the circumstances described in *CASS 5.6.5R* (Failure of the authorised firm: primary pooling event).

*regulated activity*

(in accordance with section 22 of the *Act* (The classes of activity and categories of investment)) any of the following activities specified in Part II of the *Regulated Activities Order* (Specified Activities):

(a) ...

...

(ga) *arranging (bringing about) regulated mortgage contracts* (article 25A(1));

(gb) *making arrangements with a view to regulated*

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<sup>4</sup> The text in square brackets was made in the Collective Investment Schemes (UCITS Amending Directive) Instrument 2003 but will not to come into force until 13 February 2004.

- mortgage contracts (article 25A(2));
- (h) ...
- (ha) assisting in the administration and performance of a contract of insurance (article 39A);
- ...
- (pa) advising on regulated mortgage contracts (article 53A);
- (q) ...
- ...
- (sa) entering into a regulated mortgage contract (article 61(1));
- (sb) administering a regulated mortgage contract (article 61(2));
- (t) ...
- secondary pooling event* (1) (in CASS 4) an event that occurs in the circumstances described in ~~COB 9.5.14R~~ CASS 4.4.14R (Failure of a bank, intermediate broker, settlement agent or OTC counterparty: secondary pooling events).
- (2) (in CASS 5) an event that occurs in the circumstances described in CASS 5.6.14R (Failure of a bank, other broker or settlement agent: secondary pooling events).
- service conditions* (in accordance with paragraph 14 of Schedule 3 to the Act (EEA Passport Rights)) the conditions that:
- (a) the *firm* has given its *Home State regulator* notice of its intention to provide services in the *United Kingdom*;
- (b) if the *firm* falls within paragraph (a), ~~(d)~~, (e) or (f) in the definition of "*EEA firm*", the *FSA* has received notice from the *firm's Home State regulator* containing such information as may be prescribed; ~~and~~
- (c) if the *firm* falls within paragraph (d) or (e) of that definition, its *Home State regulator* has informed it that the regulator's notice has been sent to the *FSA*; and
- (d) if the *firm* falls within paragraph (e) of that definition, one month has elapsed beginning with the date on which the *firm's Home State regulator* informed the *firm* that it had sent the regulator's notice to the *FSA*.
- Single Market Directives* (as defined in paragraph 1 of Schedule 3 to the Act (EEA Passport Rights));
- (a) the *Banking Consolidation Directive*;;
- (b) the *Insurance Directives* ~~and~~;
- (c) the *Investment Services Directive*;

<i>specified investment</i>	<p>(d) <u>the Insurance Mediation Directive; and</u></p> <p>(e) <u>(from 13 February 2004) the UCITS Directive.</u></p> <p>any of the following <i>investments</i> specified in Part III of the <i>Regulated Activities Order</i> (Specified Investments):</p> <p>...</p>
<i>top-up cover</i>	<p>(o) <i>funeral plan contract</i> (article 87);</p> <p>(oa) <u>regulated mortgage contract</u> (article 61(3));</p> <p>...</p> <p>cover provided by the <i>compensation scheme</i> for <i>claims</i> against an <i>incoming EEA firm</i> (which is a <i>credit institution</i>, <u>an <i>IMD insurance intermediary</i>, an <i>IMD reinsurance intermediary</i></u> or an <i>ISD investment firm</i>) in relation to the <i>firm's passported activities</i> and in addition to, <u>or due to the absence of, any the</u> cover provided by the <i>firm's Home State</i> compensation scheme, (see <i>COMP 14</i> (Participation by EEA firms)).</p>

## Annex H

### Amendments to the Principles for Businesses, Senior Management Arrangements, Systems and Controls, Client Assets sourcebook, Enforcement manual and Compensation sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Amendments to the Principles for Businesses

- 1.1.2 G ...
- Accepting deposits and issuing electronic money, ~~general insurance business and certain long term insurance business~~
- 1.1.3 G The *Principles* apply with respect to *regulated activities* generally, but, in applying the *Principles* with respect to *accepting deposits* and issuing electronic money, ~~general insurance business and long term insurance business involving pure protection contracts or reinsurance contracts~~, the *FSA* will proceed only in a *prudential context*. That is to say, in this context, the *FSA* would not expect to exercise the powers brought into play by a contravention of a *Principle* unless the contravention amounted to a serious or persistent violation which had implications for confidence in the *financial system*, or for the fitness and propriety of the *firm* or for the adequacy of the *firm's* financial resources.
- ...
- 3.2.1 R *PRIN* applies with respect to the carrying on of:
- (1) ...
- ...
- (3) *ancillary activities* in relation to *designated investment business*, *regulated mortgage activity* and *insurance mediation activity*.
- ...

## Amendments to the Senior Management Arrangements, Systems and Controls

1.1.2 G ...

What?

1.1.3 R SYSC 2 and SYSC 3 apply with respect to the carrying on of:

(1) *regulated activities*;

(2) activities that constitute *dealing in investments as principal*, disregarding the exclusion in article 15 of the *Regulated Activities Order* (Absence of holding out etc); and

(3) *ancillary activities* in relation to *designated investment business*, *regulated mortgage activity* and *insurance mediation activity*.

...

Appendix 1

Matters reserved to a Home State regulator

(see SYSC 1.1.1R(1)(b) and SYSC 1.1.1R(1)(c))

...

1.1.2 G The *Single Market Directives* and the *Treaty* (as interpreted by the European Court of Justice) adopt broadly similar approaches to reserving responsibility to the *Home State regulator*. To summarise, the *FSA*, as *Host State regulator*, is entitled to impose requirements with respect to activities carried on within the *United Kingdom* if these can be justified in the interests of the ‘general good’ and are imposed in a non-discriminatory way. This general proposition is subject to the following in relation to activities passported under the *Single Market Directives*:

(1) the *Single Market Directives* expressly reserve responsibility for the prudential supervision of an *ISD investment firm*, *BCD credit institution* or passporting *insurance undertaking* to the *firm’s Home State regulator*. The *IMD* reaches the same position without expressly referring to the concept of prudential supervision. Accordingly, the *FSA*, as *Host State regulator*, is entitled to regulate only the conduct of the *firm’s* business within the *United Kingdom*;

(2) ...

## Amendments to the Client Assets sourcebook

### 4.1 Application and purpose

#### Application

4.1.1 R This section (the *client money rules*) applies to a *firm* that receives or holds *money* from, or on behalf of, a *client* in the course of, or in connection with:

- (1) its *designated investment business*; ~~except where CASS 4.1.2R otherwise provides~~; or
- (2) in the circumstances set out in CASS 4.1.1A R, *insurance mediation activity*;

except where CASS 4.1.2R applies.

4.1.1A R A firm that receives or holds money to which this section applies and money in respect of which CASS 5.1 applies, may elect to comply with the provisions of this section CASS 4 in respect of all such money and if it does so CASS 4 applies as if all such money were money that the firm receives and holds in the course of or in connection with its designated investment business.

4.1.2 R The *client money rules* do not apply with respect to:

- (1) ...
- ...
- (3) ...
  - (a) ...
  - (b) ... ; ~~or~~
- (4) *money* held by *depositories* which are regulated by COB 11 ;
- (5) client money held by a firm which:
  - (a) receives or holds client money in relation to contracts of insurance; but which
  - (b) in relation to such client money elects to act in accordance with CASS 5.1 to 5.6.

4.1.2A R A firm should make and retain a written record of any election which it makes under CASS 4.1.1A R or CASS 4.1.2R (5).

4.1.2B G (1) A firm which receives and holds client money in respect of life assurance business in the course of its designated investment business may:

(a) in accordance with CASS 4.1.1 A R elect to comply with CASS 4 in respect of such *client money* and in doing so avoid the need to comply with CASS 5.1 to 5.6 which would otherwise apply to the *firm* in respect of *client money* received in the course of its *insurance mediation activity*; or

(b) in accordance with CASS 4.1.2R (5), elect to comply with CASS 5.1 to 5.6 in respect of such *client money*.

(2) These options are available to a *firm* irrespective of whether it also receives and holds *client money* in respect of other parts of its *designated investment business*. A *firm* may not however choose to comply with CASS 5.1 to 5.6 in respect of *client money* which it receives and holds in the course of any part of its *designated investment business* which does not involve an *insurance mediation activity*.

...

Money that is not client money: ‘opt outs’ for any business (including ISD business) other than insurance mediation activity

4.1.8 G The ‘opt out’ provisions provide a *firm* with the option of allowing an *intermediate customer* or *market counterparty* to choose whether their *money* is subject to the *client money rules* (unless the *firm* is conducting *insurance mediation activity*).

4.1.9 R Subject to CASS 4.1.11R, *money* is not *client money* when a *firm* (other than a sole trader) holds that *money* on behalf of, or receives it from, a *market counterparty* or an *intermediate customer*, other than in the course of *insurance mediation activity*, and the *firm* has obtained written acknowledgement from the *market counterparty* or *intermediate customer* that:

- (1) the *money* will not be subject to the protections conferred by the *client money rules*;
- (2) as a consequence, this *money* will not be segregated from the *money* of the *firm* in accordance with the *client money rules* and will be used by the *firm* in the course of its own business; and
- (3) the *market counterparty* or *intermediate customer* will rank only as a general creditor of the *firm*.

‘Opt-outs’ for non-ISD business

4.1.10 G For a *firm* whose business is not governed by the *ISD* or the *IMD*, it is possible to ‘opt out’ on a one-way basis. However, in the case of certain non-*ISD investment firms* that undertake ‘*ISD type*’ business from a *branch* in the *United Kingdom*, article 5 of the *ISD* requires the *FSA* not to treat this business any more favourably than business of an *ISD investment firm*. Therefore all *ISD* and ‘*ISD type*’ business should comply with the *client money rules* or be ‘opted out’ on a two-way basis.

- 4.1.11 R *Money is not client money if a firm, in respect of designated investment business which is not a core investment service, a non-core investment service, or a listed activity or insurance mediation activity :*
- (1) holds it on behalf of or receives it from a *market counterparty* who is not an *authorised person* or an *intermediate customer* who is not an *authorised person*; and
  - (2) has sent a separate written notice stating the matters set out in CASS 4.1.9R (1) to (3).

#### **Amendments to the Enforcement manual**

- 3.5.19 G Some relevant Community obligations which the *FSA* may need to consider are those under the following Directives:
- (1) ~~the *Banking Directive* EC 2000/12/EC *Banking Consolidation Directive*;~~
  - (2) ~~the *Insurance Directives*;~~
  - (3) ~~the *Investment Services Directive*;~~
  - (4) the *Insurance Mediation Directive*.
- 3.5.20 G Each of these Directives imposes general obligations on the *relevant EEA competent authorities* to cooperate and collaborate closely in discharging their functions under the Directives relating to the *authorisation* (“*registration*” in the case of *IMD insurance intermediaries* and *IMD reinsurance intermediaries*) and supervision of *credit institutions*, *insurance undertakings*, ~~and *investment firms*, *IMD insurance intermediaries* and *IMD reinsurance intermediaries*.~~

...

#### **Amendments to the Compensation sourcebook**

Text in square brackets was made in the Collective Investment Schemes (UCITS Amending Directive) Instrument 2003 but will not to come into force until 13 February 2004.

- 1.3.3 G Table



Q1	What do I need to do in order to receive compensation?	
A1	In order to receive compensation:	
	(1) you must be an <i>eligible claimant</i> ;	COMP 4.2-3
	(2) you must have a <i>protected claim</i> ;	COMP 5.2-56
	(3) you must be claiming against a <i>relevant person</i> ;	COMP 6.2.1R
	(4) the <i>relevant person</i> must be <i>in default</i> .	COMP 6.3
	...	
Q2	How much compensation will I be offered?	
A2	This depends on whether your <i>protected claim</i> is:	
	(1) a <i>claim</i> for a <i>protected deposit</i> ; or	COMP 5.3
	(2) a <i>claim</i> under a <i>protected contract of insurance</i> ; or	COMP 5.4
	(3) a <i>claim</i> in connection with <i>protected investment business</i> ; or	COMP 5.5
	(4) a <i>claim</i> in connection with <i>protected non-investment insurance mediation</i> .	COMP 5.6
	Different limits apply to different types of <i>claim</i> .	COMP 10.2.3R
Q3	How will the FSCS calculate the compensation that is offered to me?	
A3	Again, this will depend on whether <i>your protected claim</i> is :	
	(1) a <i>claim</i> for a <i>protected deposit</i> ;	COMP 12.2.1R, 12.3.1R and 12.4.1R
	(2) a <i>claim</i> under a <i>protected contract of insurance</i> ; or	COMP 12.2.1R, 12.3.2-4R and 12.4.9R – 12.5.2R
	(3) a <i>claim</i> in connection with <i>protected investment business</i> ; or	COMP 12.2.1R, 12.3.5-6R and 12.4.2-8R
	(4) a <i>claim</i> in connection with <i>protected non-investment insurance mediation</i> .	COMP 12.4.17R – 18R
	.....	

...

#### 1.4.1

G *Incoming EEA firms* which are conducting *regulated activities* in the *United Kingdom* under a *BCD*, *IMD* or *ISD* passport are not required to participate in the *compensation scheme* in relation to those *passport activities*. *Incoming EEA firms* which are conducting business under a *BCD*, *IMD* or *ISD* passport may apply to obtain the cover of, or 'top up' into, the *compensation scheme* if there is no level or scope of cover provided by the *incoming EEA firm's Home State* compensation scheme or if the level or scope of the cover is less

than that provided by the *compensation scheme*. This is covered by COMP 14.

...

4.3.6 R *A person who comes within COMP 4.2.2R is eligible to claim compensation in respect of a liability subject to compulsory insurance if the claim is:*

*(1) a claim under a protected contract of insurance; or*

*(2) a claim in connection with protected non-investment insurance mediation.*

...

5.2.1 R *A protected claim is:*

*(1) a claim for a protected deposit (see COMP 5.3); or*

*(2) a claim under a protected contract of insurance (see COMP 5.4); or*

*(3) a claim in connection with protected investment business (see COMP 5.5);  
or*

*(4) a claim in connection with protected non-investment insurance mediation (see COMP 5.6).*

...

5.5.2 R ...

## 5.6 Protected non-investment insurance mediation

5.6.1 R *Protected non-investment insurance mediation is an insurance mediation activity where the investment concerned is a non-investment insurance contract, provided that the condition in COMP 5.6.2 R is satisfied.*

5.6.2 R *COMP 5.6.1R only applies if the protected non-investment insurance mediation was carried on from:*

*(1) an establishment of the relevant person in the United Kingdom; or*

*(2) a branch of a UK firm established in another EEA State in the exercise of an EEA right derived from the IMD.*

...

6.2.2 G *An incoming EEA firm, which is a credit institution, an IMD insurance intermediary, an IMD reinsurance intermediary or an ISD investment firm, and its appointed representatives are not relevant persons in relation to the firm's passported activities, unless it has top-up cover. (See definition of "participant firm").*

...

- 6.3.4 R For *claims* arising in connection with *protected investment business* or *protected non-investment insurance mediation*, the *FSCS* has the additional power to determine that a *relevant person* is *in default* if it is satisfied that a *protected claim* exists, and:
- (1) the *FSCS* is satisfied that the *relevant person* cannot be contacted at its last place of business and that reasonable steps have been taken to establish a forwarding or current address, but without success; and
  - (2) there appears to the *FSCS* to be no evidence that *the relevant person* will be able to meet claims against it.

...

- 8.2.4 R For *claims* made in connection with *protected investment business* or *protected non-investment insurance mediation*, the *FSCS* may disregard a defence of limitation where the *FSCS* considers that it would be reasonable to do so.

- 8.2.5 R For *claims* made in connection with *protected investment business* or *protected non-investment insurance mediation*, if a *relevant person*, incorporated as a *company*, has been dissolved with the result that its liability to the claimant has been extinguished by operation of law, the *FSCS* must treat the claim, for the purposes of paying compensation, as if the *relevant person* had not been dissolved.

...

- 10.2.3 R Table

Type of claim	Level of cover	Maximum payment
<u><i>Protected non-investment insurance mediation</i></u>	(1) where the <i>claim</i> is in respect of a <i>liability subject to compulsory insurance</i> : 100% of <i>claim</i>	<u>Unlimited</u>
	(2) In all other cases:	<u>Unlimited</u>
	100% x first £2000	
	90% of the remainder of the <i>claim</i>	

...

- 12.3.6 R ...

Protected non-investment insurance mediation

- 12.3.7 R For a *claim* made in connection with *protected non-investment insurance mediation*, the *FSCS* must determine a specific date as the *quantification date*, and this date may be either on, before or after the date of determination of default.

...

- 12.4.16 R ...  
Protected non-investment insurance mediation
- 12.4.17 R The FSCS may pay compensation for any claim made in connection with protected non-investment insurance mediation only to the extent that the FSCS considers that the payment of compensation is essential in order to provide the claimant with fair compensation.
- ...
- 12.4.18 R The FSCS may decide to reduce the compensation that would otherwise be payable for a claim made in connection with protected non-investment insurance mediation if it is satisfied that:
- (1) there is evidence of contributory negligence by the claimant; or
- (2) payment of the full amount would provide a greater benefit than the claimant might reasonably have expected or than the benefit available on similar contracts with other relevant persons; and
- it would be inequitable for FSCS not to take account of (1) or (2).
- ...
- 13.2.14 G *Incoming EEA firms* which obtain cover or 'top up' under the provisions of COMP 14 are *firms* whose *Home State* scheme provides no or limited compensation cover in the event that they are determined to be in default. Under COMP 13.7, the FSCS is required to consider whether *incoming EEA firms* should receive a discount on the amount that they would otherwise pay as their share of the levy, to take account of the availability of their *Home State* cover. The amount of any discount is recoverable from the other members of the *incoming EEA firm's contribution group*.
- ...
- 13.7.1 R If an *incoming EEA firm*, which is a *BCD credit institution*, an IMD insurance intermediary, an IMD reinsurance intermediary or ISD investment firm, is a *participant firm*, the FSCS must give the *firm* such discount (if any) as is appropriate on the share of any levy it would otherwise be required to pay, taking account of the nature of the levy and the extent of the compensation coverage provided by the *firm's Home State* scheme.
- ...
- 14.1.2 R This chapter also applies to an *incoming EEA firm* which is a *credit institution*, ~~or an ISD investment firm~~ (or both), an IMD insurance intermediary, an IMD reinsurance intermediary [or a *UCITS management company*].

- 14.1.3 G This chapter provides supplementary *rules and guidance* for an *incoming EEA firm* which is a *credit institution, an IMD insurance intermediary, an IMD reinsurance intermediary* or an *ISD investment firm*. It reflects in part the implementation of the Deposit Guarantee Directive and Investors Compensation Directive. This sourcebook applies in the usual way to an *incoming EEA firm* which is exercising *EEA rights* under the *Insurance Directives*. Such a firm is not affected by the *Deposit Guarantee Directive* or the *Investors Compensation Directive*.
- 14.1.4 G An *incoming EEA firm*, which is a *credit institution, an IMD insurance intermediary, an IMD reinsurance intermediary* or an *ISD investment firm*, is not a *participant firm* in relation to its *passported activities* unless it obtains the cover of, or 'tops up' into, the *compensation scheme*. This reflects section 213(10) of the Act (the compensation scheme) and regulation 2 of the *Electing Participants Regulations* (Persons not to be regarded as relevant persons). If an *incoming EEA firm* also carries on non-*passported activities* for which the *compensation scheme* provides cover, it will be a *participant firm* in relation to those activities and will be covered by the *compensation scheme* for those activities in the usual way.
- 14.1.5 G In relation to an *incoming EEA firm's passported activities*, its *Home State* compensation scheme must provide compensation cover in respect of business within the scope of the *Deposit Guarantee Directive and Investors Compensation Directive*, whether that business is carried on from a *UK branch* or on a *cross border services* basis. [(For a *UCITS management company*, this is only for certain *passported activities*)]. *Insurance mediation activity relating to non-investment insurance contracts is not within the scope of the Deposit Guarantee Directive and Investors Compensation Directive.*
- 14.1.6 G If ~~there the scope or level of~~ is no cover provided by the incoming EEA firm's Home State or the scope or level of cover is less than that provided by the *compensation scheme*, this chapter enables the *firm* to obtain cover or 'top-up' cover from the *compensation scheme* for its *passported activities* carried on from a *UK branch*, up to the *compensation scheme's* limits (set out in COMP 10). This reflects section 214(5) of the Act (General) and regulation 3 of the *Electing Participants Regulations* (Persons who may elect to participate). If the *firm* 'tops up' and then becomes insolvent, the *Home State* compensation scheme will pay compensation up to the limit and scope of the *Home State* compensation scheme, with the *FSCS* paying compensation for the additional amount in accordance with the provisions in this sourcebook (COMP 12.4.1R and COMP 12.4.4R).
- ...
- 14.2.3 G A notice under COMP 14.2.1R should include details confirming that the *incoming EEA firm* falls within a prescribed category. In summary:

- (1) the *firm* must be a *credit institution, an IMD insurance intermediary, an IMD reinsurance intermediary* or an *ISD investment firm*;
- (2) ...
- (3) ....

Schedule 2

Notification requirements

...

2 Table:

...

COMP 14.2.1R	Application by ... eligible inward passporting <i>EEA firm</i> to <del>top-up</del> <u>obtain</u> <u>top-up cover</u> into <i>compensation</i> <i>scheme</i>	The <i>firm's</i> ... decision that it wishes to <del>top-</del> <del>up</del> <u>obtain top-</u> <u>up cover</u> into UK scheme
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## Annex I

### Amendments to the Prudential sourcebook and to the Authorisation manual

The following text is inserted as indicated (and is not underlined).

#### Part 1

##### Integrated Prudential sourcebook

After 9.2.1R, insert the following.

###### Commencement provisions

- 9.2.1A G (1) In summary, the provisions relating to *regulated mortgage contracts* and *long-term care insurance contracts* come into effect on 31 October 2004 and the provisions relating to *insurance mediation activity* come into effect on 14 January 2005. For convenience, both sets of provisions are published in the on-line version of the *Handbook* as from 31 October 2004.
- (2) Further *guidance* is given on these commencement provisions, and their statutory background, in *AUTH 1.2.7G* and *AUTH 1.2.8G*.
- (3) This provision (*PRU 9.2.1AG*), and the *guidance* in *AUTH*, will be deleted from the text of the on-line version of the *Handbook* on 14 January 2005.

...

After 9.3.1R, insert the following.

###### Commencement provisions

- 9.3.1A G (1) In summary, the provisions relating to *regulated mortgage contracts* and *long-term care insurance contracts* come into effect on 31 October 2004 and the provisions relating to *insurance mediation activity* come into effect on 14 January 2005. For convenience, both sets of provisions are published in the on-line version of the *Handbook* as from 31 October 2004.
- (2) Further *guidance* is given on these commencement provisions, and their statutory background, in *AUTH 1.2.7G* and *AUTH 1.2.8G*.

- (3) This provision (*PRU 9.3.1AG*), and the *guidance* in *AUTH*, will be deleted from the text of the on-line version of the *Handbook* on 14 January 2005.

...

#### Commencement provisions

- 9.4.1A G (1) In summary, the provisions relating to *mortgage* mediation activity come into effect on 31 October 2004 and the provisions relating to *insurance mediation* and *insurance mediation activity* come into effect on 14 January 2005. For convenience, both sets of provisions are published in the on-line version of the *Handbook* as from 31 October 2004.
- (2) Further *guidance* is given on these commencement provisions, and their statutory background, in *AUTH 1.2.7G* and *AUTH 1.2.8G*.
- (3) This provision (*PRU 9.4.1AG*), and the *guidance* in *AUTH*, will be deleted from the text of the on-line version of the *Handbook* on 14 January 2005.

## Part 2

### Authorisation manual

After 1.2.6G, insert the following.

Activities related to regulated mortgage contracts and insurance mediation activities

1.2.7 G In this manual, various references are made to provisions concerning activities related to *regulated mortgage contracts* and to *insurance mediation activities*. Broadly speaking, the provisions concerning activities related to *regulated mortgage contracts* will come into effect on 31 October 2004 and those concerning *insurance mediation activities* will come into effect on 14 January 2005. The exception to this is that the provisions concerning *insurance mediation activities*, so far as they relate to *long-term care insurance contracts*, come into effect on 31 October 2004. These changes to the scope of *regulated activities* result from:

- (1) the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.1) Order 2003 (SI 2003/1475); and



- (2) the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003 (SI 2003/1476).

The commencement date for these provisions is explained in greater detail in *AUTH* 1.2.8G to *AUTH* 1.2.10G.

1.2.8G

Table: Commencement dates for provisions concerning insurance mediation activities and activities related to regulated mortgage contracts

	Provisions relevant to ...	Commence on ...
1.	The following <i>regulated activities</i> and their associated exclusions, so far as relevant to <i>general insurance contracts</i> and <i>pure protection contracts</i> (other than <i>long-term care insurance contracts</i> ): (1) <i>dealing in investments as agent</i> ; (2) <i>arranging (bringing about) deals in investments</i> ; (3) <i>making arrangements with a view to transactions in investments</i> ; (4) <i>advising on investments</i> ; (5) agreeing to do any of the activities in (1) to (4).	14 January 2005
2.	The <i>regulated activities</i> and their associated exclusions referred to in 1(1) to (5) so far as relevant to <i>long-term care insurance contracts</i> .	31 October 2004
3.	The <i>regulated activity of assisting in the administration and performance of a contract of insurance</i> , other than a <i>long-term care insurance contract</i> , and its associated exclusions.	14 January 2005
4.	The <i>regulated activity of assisting in the administration and performance of a contract of insurance</i> that is a <i>long-term care insurance contract</i> , and its associated exclusions.	31 October 2004
5.	The following <i>regulated activities</i> and their associated exclusions: (1) <i>arranging (bringing about) regulated mortgage contracts</i> ; (2) <i>making arrangements with a view to regulated mortgage contracts</i> ; (3) <i>advising on regulated mortgages contracts</i> ; (4) <i>entering into a regulated mortgage-contract</i> ; (5) <i>administering a regulated mortgage-contract</i> ; (6) agreeing to do any of the activities in (1) to (5).	31 October 2004

Appointed representatives and professional firms

- 1.2.9 G References to *regulated activities* in provisions relating to *appointed representatives* and to the *Part XX exemption* for members of a *designated professional body* are subject to similar commencement dates as in *AUTH 1.2.8G*.

EEA firms

- 1.2.10 G The changes in *AUTH 5* (Qualifying for authorisation under the Act) result from the Insurance Mediation Directive (Miscellaneous Amendments) Regulations 2003 (SI 2003/1473). These changes come into effect on 14 January 2005.
- 1.2.11 G This provision (*AUTH 1.2.11G*), and the *guidance* in *AUTH 1.2.7G* to *AUTH 1.2.10G*, will be deleted from the text of the on-line version of the *Handbook* on 14 January 2005.

## ADDENDUM

### INSURANCE MEDIATION AND MORTGAGE MEDIATION, LENDING AND ADMINISTRATION (PRUDENTIAL PROVISIONS) INSTRUMENT 2004

In this Addendum, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being replaced, the place where the change will be made is indicated and the text is not underlined or struck through.

Amend Annex B (Integrated Prudential sourcebook) to this instrument as follows:

#### Transitional Provisions

##### 1 Table

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1	<i>PRU 2.7.2R</i>	<u>R</u>	...	...	...
2	<i>PRU 9.3.53R</i> ...	<u>R</u>	...	...	...

Amend Annex F (Supervision manual) to this instrument as follows:

13.4.4	G	...	
		(2)	...
		<del>(32A)</del>	if the <i>UK firm's EEA right</i> derives ...

Amend Annex G (Glossary of definitions) to this instrument by deleting the text for the definition of 'establishment conditions' in its entirety and replacing it with the following text:

*establishment conditions*

(in relation to the establishment of a *branch* in the *United Kingdom*) the conditions specified in paragraph 13 of Schedule 3 to the *Act* (EEA Passport Rights), which are that:

(a) if the *firm* falls within paragraph (a), (b), (c) or (d) in the definition of "*EEA firm*":

(i) the *FSA* has received notice ("a consent notice") from the *EEA firm's Home State regulator* that it has given the

*EEA firm* consent to establish a *branch* in the *United Kingdom*;

(ii) the consent notice:

(A) is given in accordance with the relevant *Single Market Directive*;

(B) identifies the activities to which consent relates; and

(C) includes the other information prescribed in the Financial Services and Markets Act 2000 (EEA Passport Rights) Regulations 2001 (SI 2001/1376); and

(iii) the *EEA firm* has been informed of the *applicable provisions* or two *months* have elapsed beginning with the date when the *FSA* received the consent notice.

(b) if the *firm* falls within paragraph (e) in the definition of “*EEA firm*”:

(i) the *EEA firm* has given its *Home State regulator* notice of its intention to establish a *branch* in the *United Kingdom*;

(ii) the *FSA* has received notice ("a regulator's notice") from the *firm's Home State regulator* that the *firm* intends to establish a *branch* in the *United Kingdom*;

(iii) the *EEA firm's Home State regulator* has informed it that the regulator's notice has been sent to the *FSA*; and

(iv) one *month* has elapsed beginning with the date on which the *EEA firm's Home State regulator* informed the *firm* that it had sent the regulator's notice to the *FSA*.

Amend the definition of ‘protected non-investment insurance mediation’ in Annex G (Glossary of definitions) to this instrument as follows:

*protected non-investment insurance mediation*

*insurance mediation activities* which are covered by the *compensation scheme*, as defined in *COMP 5.67.1R*

Amend Annex H (Compensation sourcebook) to this instrument to take account of FSA 2003/72 as follows:

1.3.3	G		Table ...
-------	---	--	-----------

...

A2	This depends on whether your <i>protected claim</i> is:		
	...		
	<del>(4)</del> a <i>claim</i> ... ; <u>or</u>		
	<del>(4)</del> (5) a <i>claim</i> in connection with <i>protected non-investment insurance mediation</i> .		<del>COMP 5.6</del> <u>5.7</u>
	...		
A3	Again, this will depend on whether your <i>protected claim</i> is :		
	...		
	<del>(4)</del> a <i>claim</i> ... ; <u>or</u>		
	<del>(4)</del> (5) a <i>claim</i> in connection with <i>protected non-investment insurance mediation</i> .		<del>COMP 12.4.17R –</del> <del>18R</del> <u>12.4.20R –</u> <u>21R</u>
	...		

Amend Annex H (Compensation sourcebook) to this instrument by deleting the text for COMP 1.4.1G in its entirety and inserting the following text:

1.4.1	G	<i>Incoming EEA firms</i> which are conducting <i>regulated activities</i> in the <i>United Kingdom</i> under a <i>BCD, IMD, ISD</i> or <i>UCITS Directive</i> passport are not required to participate in the <i>compensation scheme</i> in relation to those <i>passport activities</i> . They may apply to obtain the cover of, or ‘top up’ into, the <i>compensation scheme</i> if there is no cover provided by the <i>incoming EEA firm’s Home State</i> compensation scheme or if the level or scope of the cover is less than that provided by the <i>compensation scheme</i> . This is covered by <i>COMP 14</i> .
-------	---	---

...

Amend Annex H (Compensation sourcebook) to this instrument to take account of FSA 2003/72 as follows:

5.2.1	R			A <i>protected claim</i> is:
...				
		(4)		a <i>claim</i> ... <del>or</del>
		(4) (5)		a <i>claim</i> in connection with <i>protected non-investment insurance mediation</i> (see <del>COMP 5.6</del> <u>5.7</u> ).
...				
<del>5.6</del> <u>5.7</u>				Protected non-investment insurance mediation
<del>5.6.1</del> <u>5.7.1</u>	R			<i>Protected non-investment insurance mediation</i> is an <i>insurance mediation activity</i> where the <i>investment</i> concerned is a <i>non-investment insurance contract</i> , provided that the condition in <del>COMP 5.6.2</del> <u>5.7.2</u> R is satisfied.
<del>5.6.2</del> <u>5.7.2</u>	R			<del>COMP 5.6.1</del> <u>5.7.1</u> R only applies if the <i>protected non-investment insurance mediation</i> was carried on from:
		(1)		an establishment of the <i>relevant person</i> in the <i>United Kingdom</i> ; or
...				
<del>12.3.7</del> <u>12.3.8</u>	R			For a <i>claim</i> made in connection with <i>protected non-investment insurance mediation</i> , the <i>FSCS</i> must determine a specific date as the <i>quantification date</i> , and this date may be either on, before or after the date of determination of default.
...				
<del>12.4.17</del> <u>12.4.20</u>	R			The <i>FSCS</i> may pay compensation for any <i>claim</i> made in connection with <i>protected non-investment insurance mediation</i> only to the extent that the <i>FSCS</i> considers that the payment of compensation is essential in order to provide the claimant with fair compensation.
<del>12.4.18</del> <u>12.4.21</u>	R			The <i>FSCS</i> may decide to reduce the compensation that would otherwise be payable for a <i>claim</i> made in connection with <i>protected non-investment insurance mediation</i> if it is satisfied that: ...
...				

Addendum  
8 December 2004

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(PROFESSIONAL INDEMNITY INSURANCE FOR PERSONAL INVESTMENT  
FIRMS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (the "Act"):
- (1) section 138 (General rule-making power);
  - (2) section 149 (Evidential provisions);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 February 2004.

**Amendments to the Interim Prudential sourcebook for investment businesses**

- D. IPRU(INV) is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Professional Indemnity Insurance for Personal Investment Firms) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex

### Amendments to IPRU(INV)

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is inserted, the place where it goes is indicated but it is not underlined. Where an entire section of text is deleted, the provisions to be deleted are indicated, but the text is not reproduced.

Delete IPRU(INV) 13.1.3 to IPRU(INV) 13.1.5.

After IPRU(INV) 13.1.2, insert the following new provisions as IPRU(INV) 13.1.3 to IPRU(INV) 13.1.5.

#### REQUIREMENT TO HOLD PROFESSIONAL INDEMNITY INSURANCE

- 13.1.3(1) G Under *Principles 3 and 4* a *firm* is required to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems and to maintain adequate financial resources. Under *Principle 9* a *firm* is obliged to take reasonable care to ensure the suitability of its *advice on investments* and discretionary decisions for any *customer* who is entitled to rely upon its judgement.
- 13.1.3(2) G Although financial resources and appropriate systems and controls can generally mitigate operational risk, professional indemnity insurance has a role in mitigating the risks a *firm* faces in its day to day operations, including those arising from not meeting the legally required standard of care when *advising on investments*. The purpose of 13.1.4(1) to 13.1.4(15) is to ensure that a *firm* has in place the type, and level, of professional indemnity insurance necessary to mitigate these risks. This includes, in the case of a *UK firm* exercising an *EEA right*, cover for breaches of obligations imposed by or under laws, or provisions having the force of law, in each *EEA State* in which the *firm* carries on business.
- 13.1.3(3) R The term "relevant income" in IPRU(INV) 13.1 refers to all income received or receivable which is commission, brokerage, fees or other related income, whether arising from the *firm's permitted activities* or not, for the last accounting year prior to inception or renewal of the professional indemnity insurance policy ("the policy").
- 13.1.4(1) R A *firm* must take out and maintain at all times professional indemnity insurance that is at least equal to the requirements of 13.1.4(2) to 13.1.4(15).

#### POLICY TERMS

- 13.1.4(2) R The policy must incorporate terms which are appropriate and must make provision for:



- (a) cover in respect of any claim for loss or damage, for which the *firm* may be liable as a result of an act or omission by:
  - (i) the *firm*; or
  - (ii) any *person* acting on behalf of the *firm* including *employees*, *appointed representatives* or its other agents;

#### LIMITS OF INDEMNITY – IMD INSURANCE INTERMEDIARY

- (b) appropriate minimum *limits of indemnity* per year, which are, if the *firm* is an *IMD insurance intermediary*, no lower than:
  - (i) €1,000,000 for a single claim against the *firm*; and
  - (ii) €1,500,000 in the aggregate;

#### LIMITS OF INDEMNITY – NON-IMD INSURANCE INTERMEDIARY

- (c) if the *firm* is not an *IMD insurance intermediary*, then the following *limits of indemnity* apply:
  - (i) if the *firm* has relevant income of up to £3,000,000, no lower than £500,000 for a single claim against the *firm* and £500,000 in the aggregate; or
  - (ii) if the *firm* has relevant income of more than £3,000,000, no lower than £650,000 for a single claim against the *firm* and £1,000,000 in the aggregate.

- 13.1.4(3) R If a policy is denominated in any currency other than euros, an *IMD insurance intermediary* must take reasonable steps to ensure that the *limits of indemnity* are, when the policy is effected (i.e. agreed) and at renewal, at least equivalent to those required in 13.1.4(2)(b).

#### READILY REALISABLE OWN FUNDS

- 13.1.4(4) G For the purposes of the following provisions relating to professional indemnity insurance, the *FSA* expects items included in *own funds* to be regarded as "readily realisable" only if they can be realised, at any given time, within 90 days.

#### ADDITIONAL REQUIREMENTS

- 13.1.4(5) E (a) In addition to the specific requirements in 13.1.4(2), to incorporate appropriate terms, the policy should make provision for the following:
- (i) for a *firm* with relevant income of more than £6,000,000, the aggregate limit identified in the table below:

Relevant income is (£)		Minimum aggregate <i>limit of indemnity</i> (£)
more than	up to	
6,000,000	7,000,000	1,150,000
7,000,000	8,000,000	1,300,000
8,000,000	9,000,000	1,450,000
9,000,000	10,000,000	1,600,000
10,000,000	12,500,000	2,000,000
12,500,000	15,000,000	2,400,000
15,000,000	17,500,000	2,800,000
17,500,000	20,000,000	3,150,000
20,000,000	25,000,000	3,800,000
25,000,000	30,000,000	4,250,000
30,000,000	35,000,000	4,500,000
35,000,000	40,000,000	4,750,000
40,000,000	50,000,000	5,500,000
50,000,000	60,000,000	6,000,000
60,000,000	70,000,000	6,750,000
70,000,000	80,000,000	7,250,000
80,000,000	90,000,000	7,750,000
90,000,000	100,000,000	8,500,000
100,000,000	150,000,000	11,250,000
150,000,000	200,000,000	14,000,000
200,000,000	250,000,000	17,000,000
250,000,000	300,000,000	19,750,000
300,000,000	n/a	22,500,000

- (ii) full retroactive cover in respect of the kinds of liabilities described in 13.1.4(2) for claims arising from work carried out by the *firm*, or on its behalf, in the past; and
  - (iii) cover in respect of *Ombudsman* awards made against the *firm*.
- (b) Compliance with (a) may be relied on as tending to establish compliance with the requirement in 13.1.4(2) for the *professional indemnity insurance* terms to be appropriate.
  - (c) Contravention of (a) may be relied on as tending to establish contravention of the requirement in 13.1.4(2) for the professional indemnity insurance terms to be appropriate.

13.1.4(6) G A *firm* should consider whether the overall cover is adequate taking account of 13.1.4(9)(b) and whether the *firm* should seek additional cover or legal expenses insurance. (Legal defence costs are costs of defence against claims that fall under the terms of the policy.)

- 13.1.4(7) G The cover provided by the policy should be wide enough to include the liability of the *firm*, its *appointed representatives*, *employees* and its agents for breaches of the *firm's* duty of skill and care, fiduciary duty, duty to look after documents or assets, fraud, and breaches of obligations imposed by or under *the Act* (or the Financial Services Act 1986 if relevant). If the *firm* operates outside the *UK* then the policy should cover other regulatory requirements imposed under the laws of other countries in which the *firm* operates.

#### EXCLUSIONS

- 13.1.4(8) R The policy must not be subject to conditions or exclusions which unreasonably limit the cover provided for in 13.1.4(2) (whether by exclusion of cover, by policy excesses or otherwise).
- 13.1.4(9) G (a) The *FSA* considers it reasonable for a *firm's* policy to exclude cover for:
- (i) specific business lines if that type of business has not been carried out by the *firm* in the past and will not be carried out by the *firm* during the life of the policy; or
  - (ii) specific claims that have been previously notified to the *firm's insurer* and claimed for under another policy.
- (b) The *FSA* does not consider it reasonable for a *firm's* policy to treat legal defence costs cover as part of the *limits of indemnity* if this reduces the cover available for any individual substantive claim.
- 13.1.4(10) E (a) The policy should not:
- (i) make provision for payment by the *firm* of an excess on any claim of more than £5,000. (This does not apply to the extent that the *firm* holds additional *own funds* in a readily realisable form, in accordance with 13.1.4(12)); or
  - (ii) exclude any type of business or activity that has been carried out by the *firm* in the past or will be carried out by the *firm* during the time for which the policy is in force. (This does not apply to the extent that the *firm* holds, by way of additional *own funds* in a readily realisable form, an amount equivalent to a reasonable provision against its potential liabilities for that business or activity. Guidance on this is given in 13.1.4(13) and (14)); or
  - (iii) exclude liability which is identified or crystallised as a result of regulatory action against the *firm* (either individually or as a member of a class of *authorised person*).
- (b) Contravention of (a) may be relied on as tending to establish contravention of 13.1.4(8).

## EXCESS LEVEL

- 13.1.4(11) E The reference to "excess" in 13.1.4(10)(a)(i) is to the highest excess level required to be paid under the policy unless that excess relates to a type of business that has not been carried out by the *firm* in the past. In those circumstances, the reference is to the next highest excess level required by the policy.

## ADDITIONAL OWN FUNDS

- 13.1.4(12) E The amount of additional *own funds* in 13.1.4(10)(a)(i) should be calculated by referring to the *firm's* relevant income and excess obtained in the following table:

All amounts are shown in £000s		Excess obtained, up to and including											
Relevant income is		5	10	15	20	25	30	40	50	75	100	150	200+
more than	up to												
0	100	0	4	7	9	12	14	18	21	28	34	45	54
100	200	0	7	11	14	17	20	25	29	38	46	59	70
200	300	0	9	14	18	21	24	30	35	45	54	69	82
300	400	0	11	16	21	24	28	34	39	50	60	77	91
400	500	0	13	18	23	27	30	37	43	55	66	83	98
500	600	0	14	20	25	29	33	40	46	59	70	89	105
600	700	0	16	22	27	31	35	42	49	63	74	94	111
700	800	0	17	23	28	33	37	45	52	66	78	99	117
800	900	0	18	24	30	35	39	47	54	69	82	103	122
900	1,000	0	19	26	31	36	41	49	56	72	85	107	126
1,000	1,500	0	23	31	37	43	48	57	66	83	99	124	146
1,500	2,000	0	26	35	42	48	54	64	73	93	109	138	161
2,000	2,500	0	29	38	46	53	59	71	81	102	121	152	179
2,500	3,000	0	32	42	51	58	65	78	89	112	132	166	195
3,000	3,500	0	35	46	55	63	71	84	96	121	142	179	210
3,500	4,000	0	38	50	59	68	76	90	102	129	152	191	223
4,000	4,500	0	41	53	63	72	80	95	108	137	161	202	236
4,500	5,000	0	43	56	67	76	85	100	114	144	169	212	248
5,000	6,000	0	48	62	73	84	93	110	125	157	185	231	271
6,000	7,000	0	52	67	79	90	101	119	135	169	199	249	291
7,000	8,000	0	56	72	85	97	107	127	144	181	212	265	310
8,000	9,000	0	59	76	90	103	114	134	152	191	224	280	328
9,000	10,000	0	63	80	95	108	120	141	160	201	236	294	344
10,000	100,000	0	63y	80y	95y	108y	120y	141y	160y	201y	236y	294y	344y
100,000	n/a	0	630	800	950	1080	1200	1410	1600	2010	2360	2940	3440

For *firms* with relevant income more than £10m but up to £100m value y is calculated by relevant income/ £10m

## EXCLUSIONS

- 13.1.4(13) G A *firm* should take into account the following when assessing the amount of additional *own funds* to be held as provision as described in 13.1.4(10)(a)(ii):
- (a) the type of business line or activity excluded and the types of claim which might arise from it;
  - (b) the number of contracts written or volume of activity;
  - (c) the number of complaints received by the *firm* relating to the excluded business or activity;
  - (d) generally accepted accounting principles applicable to provisions; and
  - (e) any other relevant information.
- 13.1.4(14) G If the *firm* holds additional *own funds* in accordance with 13.1.4(13) then the amount should be reviewed regularly. The reviews should take account of changes in the status of the policy exclusion(s) and any relevant changes to the *firm*'s circumstances.

## POLICIES PROVIDING COVER FOR MORE THAN ONE FIRM

- 13.1.4(15) R If the policy provides cover to more than one *firm* then in relation to 13.1.4(2) and (3):
- (a) the relevant income for calculating the *limits of indemnity* is that of all the *firms* named in the policy combined;
  - (b) each *firm* named in the policy must have the benefit of the minimum *limits of indemnity* as required in 13.1.4(2);
  - (c) each *firm* named in the policy must notify the *FSA* if the aggregate cover in the policy falls below the minimum in 13.1.4(2).

## EXEMPTION FROM HOLDING PROFESSIONAL INDEMNITY INSURANCE

- 13.1.5 R A *firm* is not required to effect or maintain professional indemnity insurance if:
- (a) it is a member of the same *group* as a *bank, building society, insurer or friendly society*; and
  - (b) there exists between the *firm* and an entity specified in (a) above an enforceable, written agreement to provide equivalent cover to that required for professional indemnity insurance in 13.1.4(2).

- 13.1.6 GR (1) ~~Firms may insure with any insurer which is authorised to transact professional indemnity insurance in the United Kingdom;~~  
A firm must take out professional indemnity insurance from:
- (a) any insurance undertaking which is authorised to transact professional indemnity insurance in the EEA; or
  - (b) a person of equivalent status in:
    - (i) a Zone A country;
    - (ii) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.
- (2) ~~Firms should seek advice from their broker on renewal of their professional indemnity insurance cover and to check that their broker is in possession of appendix 13(2)E and the requirements of 13.1.6E.~~

...

13.1.9 R ...

Table 13.1(1)

This table forms part of 13.1.9

NOTIFIABLE EVENTS	
1.	<p><del>professional indemnity insurance cover, required in accordance with rule 13.1.3, being refused or cancelled;</del> In relation to professional indemnity insurance, required in accordance with 13.1.4(1) to 13.1.4(15) and 13.1.5, if:</p> <ul style="list-style-type: none"> <li>(a) it cannot be obtained within 28 days of the inception or renewal date;</li> <li>(b) it is cancelled;</li> <li>(c) the amount of aggregate cover is exhausted;</li> <li>(d) the <i>firm</i> commences business lines for which it had not obtained cover;</li> <li>(e) the <i>firm</i> is relying on 13.1.4(15); or</li> <li>(f) the <i>firm</i> is relying on 13.1.5.</li> </ul>
2.	...

Delete all of Appendix 13(2)E 'Professional Indemnity Insurance Provisions'.

**CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT NO 15)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act (the "Act"):
- (1) section 138 (General rule-making power);
  - (2) section 145 (Financial promotion rules);
  - (3) section 149 (Evidential provisions);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force as follows:
- (1) to the extent that a provision relates to structured capital-at-risk products that provide an agreed level of income, on 20 February 2004;
  - (2) otherwise, on 16 July 2004.

**Amendments to the Conduct of Business sourcebook**

- D. COB is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Conduct of Business (Amendment No.15) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex A

### Amendments to the Conduct of Business Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section is inserted, the place that it goes is indicated and the text is not underlined.

COB TR 4 Transitional Rules for ex-RPB firms

...

~~4~~COB TR 5 ~~Table:~~ Miscellaneous Transitional Rules applying to all firms

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
...					
9	...				
<u>10</u>	<u>COB 3.9.31G(3)</u>	<u>G</u>	Until 16 July 2004, a <u>firm</u> may regard the reference in <u>COB 3.9.31G(3)</u> to the <u>FSA's factsheet entitled 'Capital at risk products' as including the FSA's factsheet entitled 'High-income products – Make sure you understand the risks'</u> .	From <u>20 February 2004</u> until <u>16 July 2004</u>	<u>20 February 2004</u>

...

3.2.3 R (1) To the extent that a *financial promotion* relates to one or more of the following:

~~(1)~~(a) a *deposit*; or

~~(2)~~(b) a *general insurance contract, pure protection contract, or reinsurance contract*



only *COB 3.1 to COB 3.5 and COB 3.8.4R to COB 3.8.6G and COB 3.14* apply, unless the *financial* promotion relates to a *cash deposit* ISA in which case *COB 3.9.6R(1) and COB 3.9.8R* also apply; and

- (2) if the *financial promotion* relates to a *structured deposit*, the following will also apply: *COB 3.8.8R, COB 3.8.9G, COB 3.8.11R, COB 3.8.12G, COB 3.8.15R and COB 3.8.16G.*

3.8.9 G (1) ...

- (2) The details of the commitment which is required by *COB 3.8.8R(1)(b)* will depend on the nature of the *investment* being promoted. This could be, for example, the minimum amount which can be invested, minimum or maximum period of *investment* or, where it is the case, the fact that it could be some time before a *person* may see a return on his *investment*. Where an investor's capital would be tied up for more than one month following the last fixed payment due to be made under the contract, this should be made clear in any *financial promotion* for that product.

- (3) In giving a fair and adequate explanation of the *investment* or service being provided *firms* should avoid:

....

- (e) using prominent headline rates of return where these rates are unrealistic and unlikely to be obtained by most investors.

....

- (5) To assist *firms*' compliance with *COB 3.8.4R (1) and COB 3.8.8R (1)* in relation to a *specific non-real time financial promotion* further guidance ~~on potential problem areas~~ is given in *COB 3 Annex 4*.

....

- (7) In giving a fair and adequate explanation of the risk involved, *firms* should, where relevant:

- (a) have regard to the provisions in *COB 5.4.12E and COB 5.4.13G*; and

- (b) identify where there is a possibility of loss of initial capital invested and disclose this as one of the main points in the *specific non-real time financial promotion*.

- (8) *Firms* are reminded that, when *communicating or approving a financial promotion relating to a structured capital-at-risk product*, *COB 8.2.1R and COB 8.2.4R (2)* apply.

3.9.3 G Table Location of the provisions applicable to *direct offer financial promotions*

This table belongs to COB 3.9.2G

...		
(8)	...	
(9)	Information to be contained in direct offer financial promotions regarding:	
(i)	...	
(j)	<u>Structured capital-at-risk products</u>	<u>COB 3.9.31R</u>

3.9.14 G To assist *firms*' compliance with COB 3.8.4R (1) and COB 3.8.8R(1) in relation to a *specific non-real time financial promotion* further ~~guidance on potential problem areas~~ is given in COB 3 Annex 4.

After COB 3.9.30R, insert the following:

3.9.31 R When *communicating* or *approving* a *direct offer financial promotion* for a *structured capital-at-risk product* a *firm* must ensure that the following information is included in the mailing pack or included by a clearly visible electronic link if using e-mail, the Internet or other electronic media:

- (1) an explanation of the types of capital-at-risk products generally available and how they would typically work;
- (2) an explanation of the risks associated with investing in these capital-at-risk products;
- (3) details of the key issues that *consumers* should consider before investing in a capital-at-risk product; and
- (4) information about how to complain to the *firm* and how complaints can subsequently be referred to the *Financial Ombudsman Service*.

3.9.32 G (1) When a *firm* complies with its obligations under COB 3.9.31R it should ensure that the information it provides includes in particular the following:

- (a) reference to the different risk profiles of generally available capital-at-risk products when compared with capital secure products such as *deposits*;
- (b) reference to the fact that, because of the risk to capital, capital-at-risk products should only form part of an *investment* portfolio;

- (c) reference to the fact that, before buying, investors should check they understand the way the product is priced, the charges involved, the length of time their money will be tied up and the consequences of cashing in the product early; and
  - (d) contact details for the *FSA's* consumer helpline and website.
- (2) The *FSA* would regard a *firm* that provides a copy of the *FSA's* factsheet about capital-at-risk products entitled 'Capital-at-risk products' as complying with its obligations under *COB* 3.9.31R. *Firms* can obtain copies or buy the artwork by using the *FSA's* online order form at [www.fsa.gov/pubs](http://www.fsa.gov/pubs), Consumer publications.
- (3) Where a *firm* provides a copy of the *FSA's* factsheet, it may wish to include the following wording in its covering literature:
- "The enclosed factsheet about capital-at-risk products is from the Financial Services Authority (FSA), the independent watchdog set up by Parliament. Please read this document carefully."

COB 3 Annex 4

**Additional guidance on particular types of financial promotion**~~Guidance on potential problem areas for financial promotions which identify and promote specific investments and for direct offer financial promotion (G)~~

- 1 This annex forms part of *COB* 3.8.9G(5) and *COB* 3.9.14G. More than one table may be relevant to any one *financial promotion*.
- 2 Table Contents

<b><u>Section I : Guidance relevant to specific non-real time financial promotions for particular product types</u></b>	
A	<del>AVC Schemes (including FSAVCs)</del>
B	<del>PEP or ISA transfers</del> <u>Bond Funds</u>
C	<del>Corporate bond funds or similar contracts</del> <u>With-profits bonds</u>
D	<del>'Guaranteed' products</del> <u>Pensions – phased retirement</u>
<b><u>Section II : Guidance relevant to direct offer financial promotions for PEP or ISA transfers and personal pensions and stakeholder pension schemes</u></b>	
E	<del>With profit bonds</del> <u>PEP or ISA transfers</u>
F	<del>Pensions – phased retirement</del> <u>Personal pensions and stakeholder pension schemes</u>
<b><u>Section III: Guidance relevant to specific non-real time financial promotions for products with identified characteristics</u></b>	
G	<del>'High Income' products</del> <u>Guaranteed or protected products</u>
H	<del>'Stock market bonds'</del> <u>High income products</u>

I	<del>'Hybrid bonds'</del> <u>Stock market products</u>
J	<del>Personal pensions and stakeholder pension schemes</del> <u>[deleted]</u>

...

Renumber the following tables in COB 3 Annex 4 as indicated below, and amend as shown.

**4 7 Table B E**

**PEP or ISA transfers**

...

...

**5 4 Table C. B**

**Bond Funds**

A firm constructing a financial promotion for corporate bond funds or similar contracts should take account of the following:

(1) Clear description of the risk

...

(2) Quoting out of date yields

Financial promotions often feature prominently the yield on the fund. In some cases the actual yield being paid at the time the promotion is communicated is materially different to the yield quoted. Owing to lead times, inaccuracies can occur if the market is moving rapidly, but yields several weeks or months out of date are misleading. The promotion should quote the date at which the rate applied. It is ~~unwise~~ misleading for ~~items~~ financial promotions with a long shelf life to feature prominently a rate which may become invalid.

(3) Funds not fully invested

.....

**6 9 Table D. G**

**Guaranteed or protected products**

1. Equal prominence to guaranteed and not guaranteed benefits
  - (a) Firms should give equal prominence to the description of benefits which are guaranteed and of benefits which are not.
  - (b) ~~If the word 'guaranteed' is highlighted, or otherwise emphasised, equal high lighting, or emphasis should be given to the fact that any elements which are 'not guaranteed' are not guaranteed.~~
  - (c) ~~If the reference to guaranteed income is highlighted in, for example, a 'back to back' scheme combining an annuity which is guaranteed with a five year policy or ISA, the proceeds of which are not guaranteed, the fact that the benefits under a life assurance policy or ISA are not guaranteed must be stated with equal prominence.~~
  
2. ~~Past performance – Guaranteed income but not capital~~

~~The FTSE index began in 1984 and reference is often made to its performance. Examples of 'back testing' are often given to show that the index has not fallen in any five year period since 1984. The experience may not, however, be representative of current conditions and if so the results are capable of being misunderstood. Including earlier experience may result in a more balanced presentation of risk.~~

  - (a) A clear statement should be made where relevant benefits are not guaranteed.
  - (b) If any guarantee is given, the guarantor should be named.
  - (c) An equivalent annualised rate of return should be quoted if the cash rate is quoted.
  
3. ~~Averaging – Guaranteed or protected amount payable at the end of the term~~

~~Contracts are normally based on the assumption that the index being used will rise. The use of the average level of the index will reduce the investment potential of the contract. Where the averaging periods cover more than the last six months of the contract term, it should not be implied that averaging is to protect against falls at the end of the term. It should be made clear that investors benefit only from some of the performance of the index and that one effect of averaging is likely to be to constrain the final level of the index used to calculate benefits.~~

The words 'guarantee', 'protected element' or similar may be used to describe the minimum amount payable at the end of the term. This is usually provided at some cost to the investor and *financial promotions* therefore need to make clear what that cost is and how it is imposed.

4. ~~Maximum benefits~~ Counterparty risk  
 These should not be promoted as a particular feature if the economic circumstances required to meet those benefits require investment conditions more favourable than those which would need to prevail to achieve the higher of the growth assumptions specified by the FSA. Firms should ensure that financial promotions for products with a protected element to them, which is not guaranteed, include an explanation of the associated risk of counterparty failure. Firms should avoid giving a misleading impression of the capital security.

~~7 5~~ **Table E C**

**With-profits bonds**

..

~~8 6~~ **Table F D**

**Pensions - phased retirement**

..

~~9 10~~ **Table G H**

**High income products**

1. Income Term  
 .....
2. Problem of disclosure of risks
  - (a) If the rate of income available is at some capital risk or at the expense of growth, or the income or a portion of it comprises a return of capital, these facts should be clearly explained.
  - (b) If direct or indirect comparison is made with a deposit, there should be a prominent statement that the investment does not include the security of capital which is afforded under a deposit.
- ~~3. ——— Guaranteed income but not capital~~
- ~~———— (a) A clear statement should be made where:~~
  - (i) the relevant benefits are not guaranteed; or

- ~~(ii) no benefits are guaranteed.~~
  - ~~(b) If direct or indirect comparison is made with a building society or with other forms of deposit, there should be a prominent statement that the investment does not include the security of capital which is afforded under a deposit with a bank or building society.~~
  - ~~(c) If any guarantee is given, the guarantor should be named.~~
  - ~~(d) An equivalent annualised rate of return (for example 8.16% relating to a cash return payable of 8% per annum half yearly) may be quoted if the cash rate is quoted more prominently than the equivalent annualised rate and the nature of the equivalent annualised rate is described.~~
  - ~~(e) An equivalent gross return (allowing for notional income tax) may be quoted provided that it is:-~~
    - ~~(i) less prominent than the actual cash return; and~~
    - ~~(ii) stated that tax is not recoverable by investors.~~
- 4.3. High income bonds, high income unit trusts and similar types of collective investment schemes
- .....

**10 11 Table H I**

**Stock market ~~bonds~~ products**

Stock market ~~bonds~~ products are those investments which offer returns linked to the price of equities or an index such as the FTSE 100.

~~(1) Minimum amount payable at the end of the term~~

The word 'guarantee' is usually used to describe the minimum amount payable at the end of the term. This guarantee is usually provided at some cost to the investor and promotions therefore need to make clear what that cost is and whether it is levied:-

- ~~(a) from the start, for example by means of an additional initial charge; or~~
- ~~(b) only if the guarantee is invoked, for example by reference to an index or other indicator which includes capital growth but excludes investment income.~~

~~(2) (1) Potential for Growth~~

.....

~~(3) (2) Amount invested~~

.....

~~(4) (3) Gross returns and tax on underlying fund~~

.....

~~(5) (4) Taxation of investor~~

.....

~~(6) (5) Early Encashment~~

.....

(6) Averaging

Contracts are normally based on the assumption that the index being used will rise. The use of the average level of the index will reduce the investment potential of the contract. Where the averaging periods cover more than the last six months of the contract term, it should not be implied that averaging is to protect against falls at the end of the term. It should be made clear that investors benefit only from some of the performance of the index and that one effect of averaging is likely to be to constrain the final level of the index used to calculate benefits.

(7) Maximum benefits

These should not be promoted as a particular feature if the economic circumstances required to meet those benefits require investment conditions more favourable than those which would need to prevail to achieve the higher of the growth assumptions specified by the FSA.

11. Table I.

**Hybrid bonds**

A hybrid bond refers to those life policy investments which combine one investment designed to provide income with another designed to return all or part of the capital. Potential problems with the promotion of 'hybrid bonds' are listed below. These should all be clearly explained, where applicable, in a direct offer financial promotion:

- (1) although the word 'income' is used to describe the regular payments generated from part of the investment, only part of each payment derives from interest earned on that money. The balance consists of a return of the capital itself;
- (2) although payments may be promised at a pre-defined level for a set period, there should be no implication that the original capital is guaranteed to be returned;
- (3) part of the investment is often invested in vehicles which offer opportunities for rapid growth, with risks of loss;
- (4) whilst the larger tranche is typically invested in a unit linked bond, the income producing tranche is given the greater prominence resulting in an unbalanced picture of the investment and the risks.

12.8 Table J F

**Personal pensions and stakeholder pension schemes**

....

...



5.4.4 E The reasonable steps in COB 5.4.3R should include the steps set out in COB 5.4.6E to ~~COB 5.4.10E~~ COB 5.4.12E as appropriate, in relation to transactions in the following types of *investment* or activity:

.....

(7) *structured capital-at-risk products* (see COB 5.4.12E).

...

After COB 5.4.11E, insert the following:

5.4.12 E (1) Unless (2) applies, in relation to a transaction in a *structured capital-at-risk product*, the *firm* should provide the *private customer* with a notice containing a clear, fair and adequate description of the *structured capital-at-risk product* which is to be the subject of the transaction, in a manner calculated to bring to the attention of the *private customer* the risks involved, in particular (and if applicable):

- (a) that the return of initial capital invested at the end of the investment period is not guaranteed and therefore the *private customer* may get back less than what was originally invested;
- (b) that the amount of initial capital repaid may be geared, which means that a small percentage fall in the related index may result in a larger reduction in the amount paid out to the *private customer*;
- (c) that any maximum benefit advertised to the *private customer* is only available after a set period, indicating how long that period is;
- (d) that redeeming a product early may result in redemption penalties and a poor return;
- (e) that the initial capital invested may be placed into high risk investments, such as non-investment grade bonds;
- (f) that the rate of income or growth advertised to *private customers* may depend on specified conditions being met, indicating what these conditions are;
- (g) that the *private customer* should not enter into the transaction unless he is prepared to lose some or all of the money he has invested;
- (h) that the *private customer* should satisfy himself that the *structured capital-at-risk product* is suitable for him, in the light of his circumstances and financial position, and if the *private customer* is in any doubt he should seek professional advice; and

(i) a clear, fair and adequate description of any other relevant risks affecting the value, trading price, and realisation of the value of the structured capital-at-risk product.

(2) If the firm is acting as an investment manager, it should provide the notice referred to in (1) as part of its terms of business, but need not provide a notice before each transaction in a structured capital-at-risk product, provided that the structured capital-at-risk product is within the range of structured capital-at-risk products described in the terms of business.

5.4.13 G In relation to a transaction in a structured capital-at-risk product, if it is relevant, firms should comply with COB 5.4.7E.

...

6.6.5 R COB 6.6.4R does not apply to a firm when it provides a projection:

...

(7) provided in accordance with COB 8.2.4R and COB 8.2.17E where the life policy, scheme or stakeholder pension scheme is a structured capital-at-risk product.

...

8.2.1 R This section applies to a firm when it:

(1) ...

.....

(3) (a) sells a structured capital-at-risk product to a private customer;  
or

(b) advises a private customer on a structured capital-at-risk product; or

(c) communicates or approves a financial promotion relating to a structured capital-at-risk product to a person who is a private customer; or

(d) manages the relevant assets of the issuer of a structured capital-at-risk product.

...

8.2.4 R (1) A firm to which COB 8.2.1R (1) or (2) applies must, promptly and at suitable intervals, provide the customer with a written statement containing adequate information on the value and composition of the customer's account or portfolio with the firm, as at the end of the period covered by the statement, unless COB 8.2.6R applies.

(2) A firm must not carry out any activity in COB 8.2.1R (3) unless it:

(a) provides; or

(b) takes reasonable steps to ensure that there are arrangements for providing;

promptly, and at suitable intervals, investors in a structured capital-at-risk product with a written statement containing adequate information on the value and composition of the investor's structured capital-at-risk product, as at the end of the period covered by the statement.

(3) A firm need not comply with (2) if COB 8.2.6R (Exceptions from the requirement to provide a periodic statement) applies.

...

8.2.10 E Table: Periodic statements – timing and content

This table belongs to COB 8.2.7E.

Periodic statements: timing and content	
...	
Suitable intervals	(2) A periodic statement should be provided:
	(a) six-monthly, to a private customer or an intermediate customer not subject to 2(d), unless the customer's account or portfolio consists entirely of structured capital-at-risk products, in which case the periodic statement may be provided once in any period not exceeding 12 months;
...	
Adequate information	(3) A periodic statement should contain:
	(a) (i) the information set out in COB 8.2.11E;
	(ii) if applicable the additional information in COB 8.2.12E, COB 8.2.13E, COB 8.2.14E, and COB 8.2.15E and COB 8.2.17E; and
	(iii) ...

After COB 8.2.16G, insert the following:

8.2.17 E Table: Periodic statements – additional information required for a structured capital-at-risk product

This table belongs to COB 8.2.10E (3)(a)(ii)

Additional information required when a *firm sells, advises on or communicates* or *approves a financial promotion* relating to a *structured capital-at-risk product* to a *person who is a private customer*, or manages the relevant assets of the issuer of a *structured capital-at-risk product*

1 Statement of ‘snap shot’ maturity value

A statement of the maturity value of the *investment*, on the assumption that the relevant index, indices, ‘basket’ of selected stocks, or other factor remained at the level they were on the closing date of the period covered.

2 Changes in maturity value

A statement of the levels of the relevant index, indices, ‘basket’ of selected stocks, or other factor, at which the maturity value of the *investment* would be less than the amount of the initial capital invested, and an indication of by how much less the maturity value would be.

3 Risk warning

A warning that the value of the relevant index, indices, ‘basket’ of selected stocks, or other factor can go up or down.

## Annex B

### Amendments to the Glossary

Insert the following new definitions in the appropriate alphabetical position.

- structured capital-at-risk product a product, other than a *derivative*, which provides an agreed level of income or growth over a specified investment period and displays the following characteristics:
- (a) the customer is exposed to a range of outcomes in respect of the return of initial capital invested;
  - (b) the return of initial capital invested at the end of the investment period is linked by a pre-set formula to the performance of an index, a combination of indices, a 'basket' of selected stocks (typically from an index or indices), or other factor or combination of factors; and
  - (c) if the performance in (b) is within specified limits, repayment of initial capital invested occurs but if not, the customer could lose some or all of the initial capital invested.

- structured deposit a deposit paid on terms under which any interest or premium will be paid, or is at risk, according to a formula which involves the performance of:
- (a) an index (or combination of indices)(other than money market indices);
  - (b) a stock (or combination of stocks); or
  - (c) a commodity (or combination of commodities).

**CONFLICTS OF INTEREST (CORPORATE FINANCE AND INVESTMENT ANALYSTS) (POSTPONEMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 149 (Evidential provisions);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force immediately.

**Amendments to the Conflicts of Interest (Corporate Finance and Investment Analysts) Instrument 2003**

- D. Paragraph C of the Conflicts of Interest (Corporate Finance and Investment Analysts) Instrument 2003 is amended to replace "1 February 2004" with "1 May 2004".

**Citation**

- E. This instrument may be cited as the Conflicts of Interest (Corporate Finance and Investment Analysts) (Postponement) Instrument 2004.

By Order of the Board  
15 January 2004

**IMA STATEMENT OF RECOMMENDED PRACTICE INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers and related provisions in:
- (1) the following sections of the Financial Services and Markets Acts 2000 (the “Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 156 (General supplementary powers);
    - (c) section 247 (Trust scheme rules); and
    - (d) section 248 (Scheme particulars rules); and
  - (2) regulation 6 (FSA rules) of the Open-Ended Investment Companies Regulations 2001.
- B. The rule-making powers identified above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 February 2004.

**Amendments to the Collective Investment Schemes sourcebook, the Conduct of Business sourcebook and the Glossary**

- D. (1) The Collective Investment Schemes sourcebook is amended in accordance with Annex A to this instrument.
- (2) The Conduct of Business sourcebook is amended in accordance with Annex B to this instrument.
- (3) The Glossary is amended in accordance with Annex C to this instrument.

**Citation**

- E. This instrument may be cited as the IMA Statement of Recommended Practice Instrument 2004.

By Order of the Board  
15 January 2004

## Annex A

### Amendments to the Collective Investment Schemes sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Table: Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which transitional provision applies		Transitional Provision	Transitional provision: dates in force	Handbook provision coming into force
...					
23	<u>CIS 10.1.4G(2),</u> <u>CIS 10.3.3R(1)(a),</u> <u>CIS 10.3.4R(1)(a),</u> <u>CIS 10.3.6R(3)</u> <u>CIS 10.4.8R(1),</u> and <u>CIS</u> <u>10.4.9R(2)(a)</u>	<u>R</u> and <u>G</u>	<u>Reports for any <i>half-yearly</i></u> <u><i>accounting period</i> or <i>annual</i></u> <u><i>accounting period</i></u> <u>commencing before 1</u> <u>December 2003 can comply</u> <u>with the <u>Statement of</u></u> <u><u>Recommended Practice,</u></u> <u><u>Financial Statements of</u></u> <u><u>authorised <i>open-ended</i></u></u> <u><u><i>investment companies,</i></u></u> <u><u>issued by the <i>FSA</i> in</u></u> <u><u>November 2000) or with the</u></u> <u><u>Statement of Recommended</u></u> <u><u>Practice, <u>Financial</u></u></u> <u><u>Statements of <i>authorised</i></u></u> <u><u><i>unit trust schemes,</i> issued by</u></u> <u><u><i>IMRO</i> in January 1997.</u></u>	<u>From</u> <u>1 February</u> <u>2004</u> <u>for</u> <u>12 months</u>	<u>From</u> <u><i>commencement</i></u> <u>but</u> <u>amended as at</u> <u>1 February</u> <u>2004</u>



...

## 10.1 Introduction

...

### Contents of this chapter

- 10.1.4 G (1) ...
- (2) This chapter requires the accounts contained in the annual and half-yearly reports to comply with the *IMA SORP Statement of Recommended Practice, Financial Statements of Authorised open-ended investment companies*, issued by the *FSA* in November 2000 (“SORP relating to Authorised open-ended investment companies”) (for a report on an *ICVC*) or with the *Statement of Recommended Practice, Financial Statements of Authorised unit trust schemes*, issued by *IMRO* in January 1997 (“SORP relating to Authorised unit trust schemes”) (for a report on an *AUT*).
- ...

...

## 10.3 Contents of annual and half-yearly reports

### Annual reports

- 10.3.3 R (1) An annual report on an *authorised fund* other than an *umbrella scheme* must contain:
- (a) full accounts for the *annual accounting period* which must, subject to the *rules* in this chapter, include all the matters required to be included in them by the *IMA SORP Statement of Recommended Practice relating to Authorised open-ended investment companies* or by the *Statement of Recommended Practice relating to authorised unit trust schemes*. Accordingly, references to those accounts (and to short form accounts mentioned in *CIS 10.3.6R*) are not to be construed to relate only to the balance sheet and the statement of total return;
- ...

...

### Half-yearly reports

- 10.3.4 R (1) A half yearly report on an *authorised fund*, other than an *umbrella scheme* must contain:
- (a) full accounts for the *half-yearly accounting period* which must, subject to the *rules* in this chapter, consist of the matters required by the *IMA SORP Statement of*

~~Recommended Practice relating to Authorised open-ended investment companies or by the Statement of Recommended Practice relating to Authorised unit trust schemes ; and~~

...

...

### Short form accounts in reports

10.3.6 R (1) ...

...

(3) Short-form accounts must comply with the relevant requirements of the *IMA SORP* Statement of Recommended Practice mentioned in CIS 10.3.3R(1)(a).

...

...

## 10.4 Information to be included in annual and half-yearly reports

### Report of the auditor

10.4.8 R The report of the auditor to the *holders* on the accounts of the *authorised fund*, or on the aggregated accounts of the *umbrella scheme* (or for a report prepared for the purposes of CIS 10.3.3R(3), on the accounts of the *sub-fund*) must state:

(1) whether, in the auditor's opinion, the accounts have been properly prepared in accordance with the *IMA SORP* Statement of Recommended Practice relating to ~~Authorised open-ended investment companies~~, or the Statement of Recommended Practice relating to *authorised unit trust schemes*, the rules in this sourcebook, and the *instrument constituting the scheme*;

...

...

### Auditor's statement relating to short form accounts

10.4.9 R In relation to short-form accounts for any *annual accounting period*, the auditor must state whether, in the auditor's opinion, the short-form accounts are:

(1) ...

(2) prepared in accordance with:

(a) the *IMA SORP* Statement of Recommended Practice relating to ~~Authorised open-ended investment companies~~ or in accordance with the Statement of Recommended Practice relating to *authorised unit trust schemes* so far as they it relates to short-form accounts; and

(b) ...

...

## Annex B

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 6.6 Projections

...

#### **Changes and expenses disclosure for authorised ~~unit trusts~~ funds**

6.6.65 G (1) ...

- (2) Those expenses that were, or would be, reported in the Annual report and Financial Statements of authorised funds ~~authorised unit trust schemes~~ in accordance with the IMA SORP 'Statement of Recommended Practice' (SORP) issued by the FSA, will normally provide a suitable starting point for any assessment of the level of charges and expenses. The same principles apply to funds and *schemes* which are not within the scope of the IMA SORP.

...

## **Annex C**

### **Amendment to the Glossary**

Insert the following new definition in the appropriate alphabetical position.

*IMA SORP* the Statement of Recommended Practice for financial statements of *authorised funds* issued by the Investment Management Association and effective as at 1 December 2003.

**INSURANCE: CONDUCT OF BUSINESS SOURCEBOOK INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes the rules and gives the guidance in this instrument in the exercise of the powers listed in Schedule 4 to the Annex to this instrument (Powers exercised).
- B. The rule-making powers listed in that schedule are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 14 January 2005.

**Citation**

- D. (1) This instrument may be cited as the Insurance: Conduct of Business Sourcebook Instrument 2004.
  - (2) The Annex to this instrument (including its schedules) may be cited as the Insurance: Conduct of Business sourcebook (or ICOB).

By Order of the Board  
15 January 2004

## ICOB Transitional Rules

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1	Every <i>rule</i> in <i>ICOB</i> unless the context otherwise requires and subject to any more specific transitional provision relating to the matter.	R	If the application of any provision in <i>ICOB</i> is dependent on the occurrence of a series of events, some of which occur before, and some of which occur after 14 January 2005, the provision applies with respect to the events that occur after 14 January 2005.	14 January 2005 - 15 July 2005	14 January 2005
2		G	For example, if a <i>firm</i> were to <i>advise</i> a <i>customer</i> before 14 January 2005 to <i>buy</i> a <i>non-investment insurance contract</i> , the <i>firm</i> would not be required to comply with the provisions relating to <i>personal recommendations</i> in <i>ICOB</i> 4 if the <i>customer</i> were to <i>buy</i> the <i>non-investment insurance contract</i> after 14 January 2005. However, if the <i>firm</i> were to repeat the <i>personal recommendation</i> to the <i>customer</i> after 14 January 2005, those provisions in <i>ICOB</i> 4 would apply.		
3		G	Where a <i>non-investment insurance contract</i> is concluded before 14 January 2005, the cancellation provisions (if any) applying at the date the cancellation period commences apply.		
4	<i>ICOB</i> 4.4	G	Where, before 14 January 2005, an <i>insurance intermediary</i> makes a <i>personal recommendation</i> to a <i>customer</i> of a specific <i>non-investment insurance contract</i> , or <i>arranges</i> for the <i>customer</i> to enter into a <i>non-investment insurance contract</i> , but the contract is concluded after that date, the <i>insurance intermediary</i> will need to provide the <i>customer</i> with a statement of demands and needs in accordance with <i>ICOB</i> 4.4.1R.		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
5	<i>ICOB 4.7.1R</i> and <i>ICOB 8.4.1R</i>	G	<i>ICOB 4.7.1R</i> and <i>ICOB 8.4.1R</i> apply equally to contracts sold before 14 January 2005 and which come up for <i>renewal</i> after that date as they do to contracts newly entered into after 14 January 2005. <i>Firms</i> may, if they wish, get consent for future <i>renewals</i> when the contract is first sold or at the next <i>renewal</i> .		
6	<b><i>ICOB 2.2.3R(1)</i></b> and <b><i>ICOB 3.8.1R(1)</i></b>	R	A <i>firm</i> may continue to use stationery and similar materials which refer to its membership of the General Insurance Standards Council (GISC) without being considered to be in breach of <i>ICOB 2.2.3R(1)</i> (clear, fair and not misleading communication) or <i>ICOB 3.8.1R(1)</i> (clear, fair and not misleading comparisons).	14 January 2005 - 15 July 2005	14 January 2005
7	<b><i>ICOB 5</i></b>	R	(1) <b><i>ICOB 5.3.1R</i></b> to <b><i>ICOB 5.3.8R</i></b> and <b><i>ICOB 5.4.1R</i></b> to <b><i>ICOB 5.4.9G</i></b> do not apply in respect of any <i>non-investment insurance contract</i> concluded before 14 January 2005, provided that the <i>firm</i> follows the requirements in <b><i>COB 6.8</i></b> that would have applied before 14 January 2005 to such a contract before the contract was entered into.	Indefinitely	14 January 2005

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			(2) If a <i>non-investment insurance contract</i> is concluded before 14 January 2005 and the <i>customer</i> has not previously received a <i>policy document</i> , the <i>insurer</i> or <i>insurance intermediary</i> (as the case may be) must ensure that the <i>customer</i> is provided with a copy of the <i>policy document</i> in good time prior to the commencement of any <i>renewal</i> of or mid-term change to the <i>policy</i> .		



## **Insurance: Conduct of Business**

- 1. Application and purpose**
  - 1.1 Application and purpose
  - 1.2 General application: who? what?
  - 1.3 General application: where?
  - 1.4 Application in respect of electronic commerce activities and communications
  - 1.5 Summary of Handbook provisions for insurance intermediaries
  - 1.6 Application to appointed representatives
  - 1.7 Guidance on application of the Distance Marketing Regulations and expressions derived from the Distance Marketing Directive
- Annex 1G Summary of the application of the chapters of ICOB
- Annex 2G Summary of Handbook provisions for insurance intermediaries
- 2. General rules (including unfair inducements)**
  - 2.1 Application: who?
  - 2.2 Communication
  - 2.3 Inducements
  - 2.4 Reliance on others
  - 2.5 Exclusion of liability
  - 2.6 Application to electronic media
  - 2.7 General provision related to distance contracts
  - 2.8 Record keeping
- 3. Financial promotion**
  - 3.1 Application: general
  - 3.2 Application: who?
  - 3.3 Application: what?
  - 3.4 Application: where?
  - 3.5 Purpose
  - 3.6 General
  - 3.7 Confirmation of compliance
  - 3.8 Form and content of non-investment financial promotions
  - 3.9 The Internet and other electronic media
- 4. Advising and selling standards**
  - 4.1 Application and purpose
  - 4.2 Status disclosure
  - 4.3 Suitability
  - 4.4 Statement of demands and needs
  - 4.5 Excessive charges to retail customers
  - 4.6 Commission disclosure for commercial customers
  - 4.7 Unsolicited services
  - 4.8 Language of the information provided to customers
- Annex 1G Initial disclosure document ("IDD")
- Annex 2R Combined initial disclosure document ("CIDD")

- 5. Product disclosure**
  - 5.1 Application and purpose
  - 5.2 Information - responsibilities of insurers and intermediaries
  - 5.3 Provision of information to retail customers
  - 5.4 Provision of information to commercial customers
  - 5.5 Information form and content
  - 5.6 White labelling
  - 5.7 Record keeping
  
- 6. Cancellation**
  - 6.1 Application and purpose
  - 6.2 Cancellation rights and period
  - 6.3 Notification of cancellation by the customer
  - 6.4 Effects of cancellation
  
- 7. Claims handling**
  - 7.1 Application and purpose
  - 7.2 Group policies and third party claimants
  - 7.3 Claims handling: general
  - 7.4 Duties of insurance intermediaries
  - 7.5 Retail customers: performance standards for handling claims
  - 7.6 Motor vehicle liability insurers: claims representatives
  - 7.7 Record keeping
  
- 8. Distance non-investment mediation contracts with retail customers**
  - 8.1 Application and purpose
  - 8.2 General rules
  - 8.3 Disclosure requirements
  - 8.4 Unsolicited services
  - 8.5 Cancellation requirements

# ICOB 1

## Application and purpose

### 1.1 Application and purpose

#### Application

1.1.1 G *ICOB* applies to every *firm* as specified in the remainder of this chapter.

#### Purpose

- 1.1.2 G (1) The purpose of this chapter is to set out to whom, for what activities, and within what territorial limits the *rules, evidential provisions* and *guidance* in *ICOB* apply. The purpose of other chapters in *ICOB* is set out at the beginning of each chapter.
- (2) *ICOB* implements, in part, provisions contained in a number of EC directives:
- (a) the *Insurance Mediation Directive*, in respect of *non-investment insurance contracts*;
  - (b) the *Distance Marketing Directive*, in respect of *non-investment insurance contracts* and *distance non-investment mediation contracts*;
  - (c) the *Consolidated Life Directive*, in respect of cancellation rights and information requirements relating to *non-investment insurance contracts* which are *pure protection contracts*;
  - (d) the *Third Non-Life Directive*, in respect of information requirements relating to *general insurance contracts*; and
  - (e) the *Fourth Motor Insurance Directive*, in respect of *claims* made by an *EEA* resident arising from a motor accident in the *EEA* but outside his country of residence.
- (3) This chapter also provides *guidance* on the application of other parts of the *Handbook* to an *insurance intermediary* that carries on *insurance mediation activities* to which *ICOB* applies.

### 1.2 General application: who? what?

1.2.1 R Except as provided for in *ICOB* 1.2.8R to *ICOB* 1.2.16G, *ICOB* applies to:

- (1) **an insurance intermediary, including an insurer, when it carries on insurance mediation activities for a customer in relation to a non-investment insurance contract or enters into a distance non-investment mediation contract with a retail customer;**
- (2) **an insurer when acting as product provider in relation to a non-investment insurance contract;**
- (3) **a firm when it manages the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's, in relation to a non-investment insurance contract;**
- (4) **a firm which communicates or approves a non-investment financial promotion;**
- (5) **a motor vehicle liability insurer; and**
- (6) **the Society in relation to motor vehicle liability insurance business.**

- 1.2.2 G (1) The definition of *insurance intermediary* includes an *insurer* when the *insurer* is carrying on *insurance mediation activities*, for example when, through its sales force, it *advises on* or *arranges* its own *non-investment insurance contracts* or those of another *insurer*.
- (2) In relation to (1), *insurers* should note that *IPRU(INS) 1.3R* prevents an *insurer* from carrying on an *insurance mediation activity* in respect of a third party's products, unless the *insurer* can show that there is a natural fit or necessary connection between the *insurer's* insurance business and the third party's products.

- 1.2.3 R (1) **In the case of a non-investment insurance contract that is underwritten at Lloyd's by its members, the firm responsible for the management of the insurance business of the member (that is, the managing agent) discharges the obligations of the product provider, which would otherwise be discharged by an insurer. References to managing agents in ICOB therefore relate to their functions in managing the obligations of the member as product provider.**
- (2) **Where there is a chain of insurance intermediaries between the insurer and the customer, ICOB applies only to the insurance intermediary in contact with the customer.**

### **Summary of the application of the chapters of ICOB**

- 1.2.4 G A table summarising the application of the various chapters of *ICOB* to *firms* is set out in *ICOB 1 Ann 1G*. For the detailed application of each chapter, see the application *rule* at the start of that chapter.

- 1.2.5 G All chapters of *ICOB* are relevant to a *firm* that deals with a *retail customer*. Certain chapters of *ICOB* apply in part only or not at all if a *firm* is dealing with a *commercial customer*. *Guidance* on the term *retail customer* is set out in *ICOB* 1.7.3G(1).

**Customer to be treated as retail customer when status uncertain**

- 1.2.6 R **If it is not clear in a particular case whether a *customer* is a *retail customer* or a *commercial customer*, an *insurance intermediary* or an *insurer*, in relation to a *non-investment insurance contract* or a *distance non-investment mediation contract*, must comply with *ICOB* as if the *customer* were a *retail customer*.**

**Application to insurers where the intermediary is unauthorised or where the sale involves a connected contract**

- 1.2.7 G (1) An *insurer* must comply with the following *ICOB* requirements, which are applicable to *insurers* as *product providers*, if its *non-investment insurance contracts* are sold through an intermediary to whom *ICOB* does not apply (because the intermediary is not a *firm*) or if its *non-investment insurance contracts* are *connected contracts*:
- (a) *ICOB* 2 (General rules (including unfair inducements));
  - (b) *ICOB* 3 (Financial promotion) if the *insurer communicates* or *approves a financial promotion*;
  - (c) *ICOB* 4.7 (Unsolicited services);
  - (d) *ICOB* 5 (Product disclosure) as explained in *ICOB* 5.2;
  - (e) *ICOB* 6 (Cancellation) except for *general insurance contracts* and *connected contracts* that are not *distance contracts* (*ICOB* 6.1.5R(5) and (6)); and
  - (f) *ICOB* 7 (Claims handling).
- (2) The circumstances in (1) may occur where article 72B of the *Regulated Activities Order* excludes certain *regulated activities* from regulation when carried on by providers of non-motor goods and services related to travel in relation to *connected contracts*. *Guidance* on the conditions that need to be satisfied by *connected contracts* is contained in *AUTH* App 5.11.13G to *AUTH* App 5.11.15G.

### Large risks within the EEA

- 1.2.8 R Where an *insurance intermediary* carries on *insurance mediation activities* for *commercial customers* in relation to *contracts of large risks* where the risk is located within the *European Economic Area*, the only provisions of *ICOB* that apply are:
- (1) *ICOB 5.4.5R* (provision of a *policy document* to *commercial customers*);
  - (2) *ICOB 5.4.8R* and *ICOB 5.4.9G* (Group policies sold to commercial customers); and
  - (3) *ICOB 7.6* (Motor vehicle liability insurers: claims representatives).
- 1.2.9 G Other parts of the *Handbook* apply where relevant to an *insurance intermediary* within *ICOB 1.2.8R*, including *Principle 7* (Communications with customers) instead of *ICOB 2.2.3R*, which restates *Principle 7* in slightly amended form.

### Authorised professional firms

- 1.2.10 R *ICOB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for:
- (1) *ICOB 2.2.3R* to *ICOB 2.2.7G* (Clear, fair and not misleading communication);
  - (2) *ICOB 3* (Financial promotion);
  - (3) *ICOB 4.2.2R* in relation to the information for *customers* in table *ICOB 4.2.8R* items numbered (8), (9) and note 4 covering complaints and compensation; and
  - (4) those sections in *ICOB* which implement articles 12 and 13 of the *IMD*, unless:
    - (a) the *designated professional body* of the *firm* has made rules which implement articles 12 and 13 of the *IMD*;
    - (b) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and
    - (c) the *firm* is subject to the rules in the form in which they were approved.
- 1.2.11 G (1) Compliance by an *authorised professional firm* with provisions of the *Distance Marketing Regulations* is dealt with in *PROF 5.4*.

- (2) The effect of *ICOB* 1.2.10R(4) is that if the relevant *designated professional body* of an *authorised professional firm* does not make rules implementing articles 12 and 13 of the *IMD* applicable to *authorised professional firms* those *authorised professional firms* will need to comply with those sections of *ICOB* which implement articles 12 and 13 of the *IMD*, namely *ICOB* 4.1 to *ICOB* 4.4 and *ICOB* 4.8.

#### **Service companies**

**1.2.12 R** *ICOB* does not apply to a *service company*, except for:

- (1) *ICOB* 1.4 (Application in respect of electronic commerce activities and communications);
- (2) *ICOB* 3 (Financial promotion); and
- (3) any provision of *ICOB* incorporated into (1) or (2) by reference.

#### **What contracts?**

##### **Reinsurance contracts**

**1.2.13 R** *ICOB* does not apply if the activities within *ICOB* 1.2.1R relate to a *reinsurance contract*.

##### **Contracts of large risks outside the EEA**

**1.2.14 R** *ICOB* does not apply to the mediation of *contracts of large risks* where the risk is located outside the *European Economic Area*.

##### **Group policies**

- 1.2.15 R**
- (1) If a *non-investment insurance contract* is a *group policy*, *ICOB* (except for *ICOB* 7 (Claims handling)) does not apply with respect to a *person* under such a *policy* who is not the legal holder of the *policy*, subject to (2).
  - (2) If a *firm* makes a *personal recommendation* that a *person* becomes a *policyholder* member of a *group policy*, *ICOB* 4.3 and *ICOB* 4.4 apply to that *personal recommendation* as if the contract were being concluded.
- 1.2.16 G** (1) All chapters of *ICOB* are relevant to a *firm* that deals with a *retail customer* unless *ICOB* 1.2.15R applies. Certain chapters of *ICOB* apply in part only or not at all if a *firm* is dealing with a *commercial customer*.

- (2) In *ICOB* a *customer* is a *policyholder* or a prospective *policyholder*. A *policyholder* includes anyone who, upon the occurrence of the contingency insured against, could expect to have a *claim*, made by him directly to the *insurance undertaking*, accepted by the *insurance undertaking*. *Policyholder* includes a member of a *group policy* who did not conclude the *group policy* with the *insurance undertaking* but who is entitled under the terms of that *policy* to make a *claim* on the *insurance undertaking*. This would include a dependant of a *policyholder* member of a *group policy* if that dependant has a direct right to *claim*. Where such a *person* does not conclude a *group policy* only limited provisions in *ICOB* will apply to him as specified in *ICOB* 1.2.15R.
- (3) A *person* whose right or interest in a *contract of insurance* that is a *group policy* does not entitle him to make a *claim* directly to an *insurance undertaking* (for example, because he is required to make his *claim* to an employer or trustees) is not a *customer*.
- (4) The *rule* at *ICOB* 5.4.8R provides for *commercial customers* who conclude *group policies* to be given a *policy summary* and to be informed that they should give that *policy summary* to each *policyholder*.
- (5) *ICOB* 1.2.15R applies regardless of how a *person* becomes a *policyholder* under a *group policy*, for example, automatically as part of a contract of employment, or voluntarily as part of a flexible benefits package.

### 1.3 General application: where?

#### UK establishments – Territorial scope of *ICOB* 2 to *ICOB* 8

- 1.3.1 R Except as set out in this section, *ICOB* 2 to *ICOB* 8 apply in relation to activities carried on from an establishment maintained by the *firm* (or its *appointed representative*) in the *United Kingdom* only.
- 1.3.2 R In addition to the situation in *ICOB* 1.3.1R, *ICOB* 4.2.19R (Overseas business for UK retail customers) applies wherever the activity is conducted.

#### Financial promotions: Territorial scope of *ICOB* 3

- 1.3.3 R Notwithstanding *ICOB* 1.3.1R, the territorial scope of *ICOB* 3 (Financial promotion) is set out in *ICOB* 3.4 (Application: where?).

#### General insurance contracts: Territorial scope of *ICOB* 5

- 1.3.4 R In addition to the situation in *ICOB* 1.3.1R, but subject to *ICOB* 1.3.6R, *ICOB* 5.5.20R(1) to (3) (Directive-required information) and the other *rules* in *ICOB* 5 (in so far as they relate to such information) apply to *firms* in relation to business in respect of *general insurance contracts* if the *State of the risk* is the *United Kingdom*.



**Pure protection contracts: Territorial scope of ICOB 5 and ICOB 6**

- 1.3.5 R In addition to the situation in *ICOB 1.3.1R*, but subject to *ICOB 1.3.6R*, *ICOB 5.5.20R(4)* to (15) and (22) (Directive-required information), the other rules in *ICOB 5* (in so far as they relate to such information), and *ICOB 6* apply to *firms* in relation to business in respect of *non-investment insurance contracts* which are *pure protection contracts* if the *habitual residence* of the customer is in the *United Kingdom*.

**Exception to extended territorial scope of ICOB 5 and ICOB 6 for distance contracts provided from other EEA States**

- 1.3.6 R The rules in *ICOB 1.3.4R* and *ICOB 1.3.5R* do not apply with respect to an activity exclusively concerning a *distance contract* with a *retail customer*, if the following conditions are satisfied:
- (1) the *firm* carries on the activity from an establishment maintained by the *firm* in an *EEA State* other than the *United Kingdom*;
  - (2) either that *EEA State*:
    - (a) has implemented the *DMD*; or
    - (b) has obligations in its domestic law corresponding to those provided for by the *DMD*;and, in either case, with the result that the obligations provided for by the *DMD* (or corresponding obligations) are applied by that *EEA State* when the *firm* carries on that activity; and
  - (3) the *firm* is a national of an *EEA State* or a company or firm mentioned in article 48 of the *Treaty*.

- 1.3.7 G The restriction in *ICOB 1.3.6R* reflects the fact that the provisions of the *Distance Marketing Directive* will be for the country of origin of the *insurance intermediary* to enforce. This is the state of the *firm's* establishment (head office or *branch*) carrying on the *insurance mediation activity*.

- 1.3.8 R The territorial scope of this sourcebook is modified by *ECO* in relation to *electronic commerce activities* and *electronic commerce communications*.

- 1.3.9 G *ICOB 1.4* contains *guidance* on how this sourcebook is modified by *ECO*.

**1.4 Application in respect of electronic commerce activities and communications**

**Application and purpose**

- 1.4.1 G (1) *ICOB 1.4* applies to a *firm*:

- (a) which is an *electronic commerce activity provider*, that is, any *firm* which carries on an *electronic commerce activity*;
  - (b) in relation to a *financial promotion* which is an *electronic commerce communication*;
  - (c) which concludes *distance contracts*, the making or performance of which constitutes, or is part of, *insurance mediation activity* in relation to *non-investment insurance contracts*.
- (2) Paragraph (1) means that *firms* need to be aware of this section whenever they are providing a service which:
- (a) is normally provided for remuneration;
  - (b) is provided at a distance;
  - (c) is so provided by means of electronic equipment for the processing (including digital compression) and storage of data;
  - (d) is so provided at the individual request of a recipient of the service.

**Modification of ICOB resulting from the E-Commerce Directive**

- 1.4.2 G The modifications made to *ICOB* resulting from the introduction of the *E-Commerce Directive* are of three kinds:
- (1) *ECO 1.1.6R* modifies *ICOB* so that a *firm* providing an *electronic commerce activity* from an establishment elsewhere in the *EEA* to a recipient who is in the *United Kingdom* (an *incoming ECA provider*) is not required to comply with any provisions of *ICOB*.
  - (2) *ECO 2*:
    - (a) modifies *ICOB* so that, in relation to a *financial promotion* which is an *outgoing electronic commerce communication*, *ICOB 3* has an extended application to cover the whole of the *EEA*; and
    - (b) obliges such a *firm*, in providing an *electronic commerce activity* within the *EEA*, to comply with the minimum information and other requirements in the *E-Commerce Directive*;

otherwise *ICOB* applies in the usual way to such a *firm*.
  - (3) *ECO 3* applies to a *firm* providing an *electronic commerce activity* from an establishment in the *United Kingdom* to a recipient who is in the *United Kingdom* or in a non-*EEA State* (a *domestic ECA provider*). Such a *firm* has to comply with *ICOB* in the usual way and so the requirements in *ECO 3* are in addition to *ICOB*. *ECO 3* sets out the minimum information and other requirements in the *E-Commerce Directive*.

## 1.5 Summary of Handbook provisions for insurance intermediaries

- 1.5.1 G A table summarising the application of the *Handbook* to *firms* carrying on *insurance mediation activities* is set out in *ICOB* 1 Ann 2G. For the detailed application of each module, see the application provision at the start of the module, or its chapter or section.

## 1.6 Application to appointed representatives

- 1.6.1 G (1) Although *ICOB* does not apply directly to a *firm's appointed representatives*, a *firm* will always be responsible for the acts and omissions of its *appointed representatives* in carrying on business for which the *firm* has accepted responsibility (section 39(3) of the *Act*). In determining whether a *firm* has complied with any provision of *ICOB*, anything done or omitted by a *firm's appointed representative* (when acting as such) will be treated as having been done or omitted by the *firm* (section 39(4) of the *Act*).
- (2) *ICOB* 8.5 (Cancellation requirements) does not apply to a *distance non-investment mediation contract* entered into by an *appointed representative* itself to provide *insurance mediation activity* services to a *retail customer*. Regulations 8 (Right to cancel) to 12 (Payment for services provided before cancellation) of the *Distance Marketing Regulations* apply instead (see regulation 4(5)). See also *ICOB* 1.7.3G(2)(e), (f) and (g) (*guidance* on when a *distance non-investment mediation contract* is concluded).
- (3) *Firms* should refer to *SUP* 12 (Appointed representatives), which sets out requirements which apply to *firms* using *appointed representatives*.

## 1.7 Guidance on application of the Distance Marketing Regulations and expressions derived from the Distance Marketing Directive

- 1.7.1 G The purpose of *ICOB* 1.7.2G and *ICOB* 1.7.3G is to provide:
- (1) *guidance* on the application of parts of the *Distance Marketing Regulations* for *non-investment insurance contracts* and *distance non-investment mediation contracts*; and
- (2) *guidance* on expressions in *ICOB* derived from the *Distance Marketing Directive*.

### Application of parts of the Distance Marketing Regulations

- 1.7.2 G *ICOB* implements most of the *Distance Marketing Directive* for *non-investment insurance contracts* that are *distance contracts* and for *distance non-investment mediation contracts*. However, certain aspects of the *Distance Marketing Directive* are implemented by provisions of the *Distance Marketing Regulations*, which apply in addition to *ICOB*, in particular:
- (1) Regulation 11 (Automatic cancellation of an attached distance contract); and

- (2) Regulation 13 (Payment cards).

**Guidance on expressions derived from the Distance Marketing Directive**

1.7.3 G *ICOB* adopts certain expressions derived from the *Distance Marketing Directive*, as follows:

(1) Retail customer

(a) The *Distance Marketing Directive* applies to 'any natural person who... is acting for purposes which are outside his trade, business or profession'. In *ICOB* the term '*retail customer*' has been adopted. In practice, private individuals may act in a number of capacities. In the *FSA's* view, a *customer* will be a *commercial customer* and not a *retail customer* if he is an individual acting, for example:

- (i) as trustee of a trust such as a housing or NHS trust;
- (ii) as member of the governing body of a club or other unincorporated association such as a trade body and a student union;
- (iii) as pension trustee;
- (iv) as a *person* taking out, or who has taken out, a *non-investment insurance contract* relating to property bought under a buy-to-let mortgage;
- (v) as *partner* in a *partnership* when taking out insurance for purposes wholly related to his profession.

(b) Examples of individuals who would be regarded as *retail customers* include:

- (i) personal representatives, including executors, unless they are acting in a professional capacity, for example, a solicitor acting as executor;
- (ii) private individuals acting in personal or other family circumstances, for example, as trustee of a family trust; and
- (iii) a *customer* who *buys* a *non-investment insurance contract* that covers him in both a private and business capacity, for example motor insurance for a driving instructor which also provides cover for social and domestic use, or insurance taken out by a sole trader which provides cover for him in both a private and a business capacity.

(2) Distance contract

- (a) To be a *distance contract*, a contract must be concluded under an 'organised distance sales or service-provision scheme' run by the contractual provider of the service who, for the purpose of the contract, makes exclusive use (directly or through an *insurance intermediary*) of one or more *means of distance communication* up to and including the time at which the contract is concluded. So:
- (i) the *insurance intermediary* must have put in place facilities designed to enable a *retail customer* to deal with it exclusively at a distance, such as facilities for a *retail customer* to deal with it purely by *post*, telephone, fax or the Internet. If an *insurance intermediary* normally operates face-to-face and has no facilities in place enabling a *retail customer* to deal with it customarily by distance means, the *DMD* will not apply. A one-off transaction effected exclusively by distance means to meet a particular contingency or emergency will not be a *distance contract*; and
  - (ii) there must have been no simultaneous physical presence of the *insurance intermediary* and the *retail customer* throughout the offer, negotiation and conclusion of the contract. So, for example, contracts offered, negotiated and concluded over the Internet, through a telemarketing operation or by *post*, will normally be *distance contracts*. A *retail customer* may visit the local office of the *insurance intermediary* in the course of the offer, negotiation or conclusion of a contract with that *insurance intermediary*. Wherever, in the literal sense, there has been "simultaneous physical presence" of the *insurance intermediary* and the *retail customer* at the time of such a visit, any ensuing contract will not be a *distance contract*.
- (b) The mere fact that an intermediary (acting for the *insurance undertaking* or for the *retail customer*) is involved, does not make the sale of a financial product or service a *distance contract*.

(3) Conclusion of a contract

- (a) A contract is concluded when an offer to be bound by the *non-investment insurance contract* has been accepted. An offer in the course of negotiations (for example, an offer by an *insurance undertaking* to consider an application) is not an offer to be bound, but is part of a pre-contractual negotiation. A *customer* will provide all the information an *insurance undertaking* needs to decide whether to accept a risk and to calculate the *premium*. The *customer* may do this orally, in writing or by completing a proposal form. The response by an *insurance undertaking*, giving a quotation to the *customer* specifying the *premium* and the terms, is likely to amount to an offer of the terms on which the *insurance undertaking* will insure the risk. Agreement by the *customer* to those terms is likely to be an acceptance which concludes the contract. In other cases where the *insurance undertaking* requires a signed proposal form (for example, some *pure protection contracts*), the proposal form may amount to an offer by the *customer* on which the *insurance undertaking* decides whether to insure the risk and in such cases the *insurance undertaking's* response is likely to be the acceptance.
  - (b) Where the parties to a contract agree that insurance cover should commence before all the terms and conditions have been agreed, the *customer* should be provided with information required by *rules* in *ICOB* to be provided before conclusion of the contract to the extent that agreement has been reached.
- (4) Distance non-investment mediation contracts
- (a) Some of the services which some *insurance intermediaries* provide will themselves fall within the scope of the *Distance Marketing Directive*. *ICOB 8* applies to an *insurance intermediary* which enters into a *distance non-investment mediation contract* with a *retail customer*. The *FSA* expects the requirements in *ICOB 8* to be relevant in a small minority of cases. *ICOB 8* will not apply in the typical case where an *insurance intermediary* sells an *insurance contract* to a *retail customer* on a one-off basis, even if the *insurance intermediary* is involved in the *renewal* of that contract and handling *claims* under it. *ICOB 8* will also not apply if an *insurance intermediary*, in its terms of business, makes clear that it does not, in conducting *insurance mediation activities*, act contractually on behalf of, or for, its *retail customer*, in which case the *insurance intermediary* can proceed on the basis that no *distance non-investment mediation contract* will arise.
  - (b) *ICOB 8* is only relevant if both of the following conditions are satisfied:
    - (i) an *insurance intermediary* concludes a *distance contract* with a *retail customer* covering its *insurance mediation activities* which is additional to any *insurance contract* which it is marketing;

- (ii) the *insurance intermediary's distance contract* is concluded other than merely as a stage in the *effecting* or *carrying out* of an *insurance contract* by the *firm* or another *person*, in other words it has some continuity independent of an *insurance contract*, as opposed, for example, to being concluded as part of marketing an *insurance contract*.
- (c) An example of a *distance non-investment mediation contract* would be a *distance contract* under which an *insurance intermediary* agrees to provide *advice* on a *retail customer's* insurance needs as and when they arise.

## ICOB 1: Application and purpose

### Annex 1G

#### Summary of the application of the chapters of ICOB

1 This annex belongs to *ICOB* 1.2.4G and summarises the application of the various chapters of *ICOB* to *firms* that carry on *insurance mediation activities*. For the detailed application of each chapter, see the application *rule* at the start of that chapter.

2 Table

Chapter	Who does the chapter apply to?
<i>ICOB</i> 2 (General rules, including unfair inducements)	(1) <i>ICOB</i> 2 applies to:  (a) an <i>insurer</i> ;  (b) an <i>insurance intermediary</i> ;  (c) a <i>managing agent</i> .  (2) <i>ICOB</i> 2.3, 2.4, 2.5, 2.6, 2.7 and 2.8 apply to a <i>firm</i> that <i>communicates</i> or <i>approves</i> a <i>non-investment financial promotion</i> .
<i>ICOB</i> 3 (Financial promotion)	<i>ICOB</i> 3 applies to every <i>firm</i> which <i>communicates</i> or <i>approves</i> a <i>non-investment financial promotion</i> .
<i>ICOB</i> 4 (Advising and selling standards)	(1) <i>ICOB</i> 4 applies to an <i>insurance intermediary</i> .  (2) <i>ICOB</i> 4.7 (Unsolicited services) applies to:  (a) an <i>insurer</i> ;  (b) a <i>managing agent</i> .
<i>ICOB</i> 5 (Product disclosure)	<i>ICOB</i> 5 applies to:  (1) an <i>insurer</i> ;  (2) an <i>insurance intermediary</i> other than when <i>introducing</i> ;  (3) a <i>managing agent</i> .
<i>ICOB</i> 6 (Cancellation)	<i>ICOB</i> 6 applies to:  (1) an <i>insurer</i> ;  (2) a <i>managing agent</i> .
<i>ICOB</i> 7 (Claims handling)	(1) <i>ICOB</i> 7, except for <i>ICOB</i> 7.6, applies to:  (a) an <i>insurer</i> ;



Chapter	Who does the chapter apply to?
	<p>(b) an <i>insurance intermediary</i>;</p> <p>(c) a <i>managing agent</i>.</p> <p>(2) <i>ICOB 7.6</i> applies in respect of <i>motor vehicle liability insurance business</i> to:</p> <p>(a) a <i>motor vehicle liability insurer</i>;</p> <p>(b) the <i>Society</i>.</p>
<p><i>ICOB 8</i> (Distance non-investment mediation contracts with retail customers)</p>	<p><i>ICOB 8</i> applies to an <i>insurance intermediary</i>.</p>

## ICOB 1: Application and purpose

### Annex 2G

#### Summary of Handbook provisions for insurance intermediaries

- 1 This table belongs to *ICOB 1.5.1G*.
- 2 This table sets out the provisions in the *Handbook* that apply to *firms* which are *insurance intermediaries* where they:

- (1) carry on *insurance mediation activities* in relation to a *non-investment insurance contract*; or
- (2) *communicate* or *approve* a *non-investment financial promotion*.

It also sets out the provisions in the *Handbook* that apply to *approved persons*.

For convenience, the former activity is referred to in the table as (1) and the latter as (2).

- 3 Table

	Module	Application
High Level Standards	General provisions, <i>GEN</i>	Applies (at least in part) in respect of (1) and (2).
	Principles for Businesses, <i>PRIN</i>	
	Threshold Conditions, <i>COND</i>	
	Statements of Principle and Code of Practice for Approved Persons, <i>APER</i>	Applies to every <i>approved person</i> who performs a <i>controlled function</i> under an <i>arrangement</i> entered into by an <i>insurance intermediary</i> when doing either (1) or (2).
	The Fit and Proper test for Approved Persons, <i>FIT</i>	Applies to an <i>insurance intermediary</i> in respect of any application that it makes for the approval of a <i>person</i> to perform a <i>controlled function</i> , and in respect of the continuing approval of that <i>person</i> .
	Senior Management Arrangements, Systems and Controls, <i>SYSC</i>	Applies in respect of (1) and (2).

	<b>Module</b>	<b>Application</b>
Business Standards	Interim Prudential sourcebooks	
	<i>IPRU (BANK)</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also a <i>bank</i> .
	<i>IPRU (BSOC)</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also a <i>building society</i> .
	<i>IPRU (FSOC)</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also a <i>friendly society</i> .
	<i>IPRU (INS)</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also an <i>insurer</i> .
	<i>IPRU(INV)</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also an <i>investment firm</i> .
	Prudential sourcebook	
	<i>PRU 9.1 – PRU 9.3</i>	Applies in respect of (1).
	<i>PRU 9.4</i>	Applies in respect of (1) where the <i>insurance intermediary</i> is also an <i>insurer</i> or a <i>mortgage lender</i> .
	Market conduct, <i>MAR</i>	Does not apply to a <i>firm</i> when doing either (1) or (2). However, certain chapters of <i>MAR</i> will apply if: <ul style="list-style-type: none"> <li>(a) the <i>insurance intermediary</i> also engages in <i>behaviour</i> in relation to <i>qualifying investments</i> traded on <i>prescribed markets</i> - then <i>MAR 1</i> applies;</li> <li>(b) the <i>insurance intermediary</i> undertakes or is concerned with <i>offers of securities</i> that may involve <i>price stabilising</i> activity - then <i>MAR 2</i> applies;</li> <li>(c) the <i>insurance intermediary</i> carries on <i>inter-professional business</i> - then <i>MAR 3</i> applies;</li> <li>(d) the <i>insurance intermediary</i> carries on <i>designated investment business</i> - then <i>MAR 4</i> applies.</li> </ul>

	<b>Module</b>	<b>Application</b>
	Conduct of Business sourcebook, <i>COB</i>	Does not apply to an <i>insurance intermediary</i> when doing (1) or (2) unless it opts to provide <i>key features</i> instead of a <i>policy summary</i> (see <i>ICOB 5.5.4R</i> ). However, <i>COB</i> may apply to an <i>insurance intermediary</i> if it also carries on any other <i>regulated activity</i> or <i>communicates</i> or <i>approves a financial promotion</i> not relating to <i>non-investment insurance contracts</i> or <i>qualifying credit</i> .
	Mortgages: Conduct of Business sourcebook, <i>MCOB</i>	Does not apply to an <i>insurance intermediary</i> when doing (1) or (2). However, <i>MCOB</i> may apply to an <i>insurance intermediary</i> if it is also a <i>mortgage lender</i> or carries on <i>mortgage mediation activities</i> .
	Training and Competence sourcebook, <i>TC</i>	<i>TC 1</i> applies when a <i>firm</i> is doing (1) or (2).  <i>TC 2</i> applies only in circumstances where an <i>insurance intermediary</i> has <i>employees advising on non-investment insurance contracts</i> with or for a <i>retail customer</i> as listed in <i>TC 2.1.4R</i> .
	Money Laundering sourcebook, <i>ML</i>	Does not apply when the <i>firm</i> is doing (1) or (2). However <i>ML</i> will apply to an <i>insurance intermediary</i> if it also carries on <i>relevant regulated activities</i> as defined in <i>ML 1.1.4R</i> .
	Client Assets sourcebook, <i>CASS</i>	<i>CASS 5</i> applies when a <i>firm</i> is doing (1) if it receives and holds <i>money</i> from or on behalf of a <i>client</i> , or receives and holds <i>money</i> as agent for an <i>insurance undertaking</i> .

	<b>Module</b>	<b>Application</b>
Regulatory processes	Authorisation manual, <i>AUTH</i>	<p>Applies to:</p> <p>(1) a <i>person</i>, other than an <i>authorised person</i>, considering carrying on the <i>regulated activities</i> that include <i>insurance mediation activities</i> in the <i>United Kingdom</i>, and who requires <i>guidance</i> on whether <i>authorisation</i> is required and, if so, how to apply to the <i>FSA</i> for <i>Part IV permission</i>;</p> <p>(2) an <i>EEA firm</i> or a <i>Treaty firm</i> that wishes to establish a <i>branch</i> or provide <i>cross border services</i> into the <i>United Kingdom</i> in relation to <i>insurance mediation activities</i> or wishes to apply for a <i>top-up permission</i> that includes <i>insurance mediation activities</i>;</p> <p>(3) a <i>person</i> wishing to obtain approval for <i>persons</i> to perform <i>controlled functions</i> in relation to <i>insurance mediation activities</i>; and</p> <p>(4) a <i>person</i> wishing to understand how the <i>FSA</i> will use its powers in relation to <i>authorisation</i> to determine applications.</p>
	Supervision manual, <i>SUP</i>	<p>The following chapters of <i>SUP</i> apply to an <i>insurance intermediary</i> when doing (1) or (2): 1, 2, 3, 5, 6, 7, 8, 9, 10, 11, 12, 15, 16, 18 (but only if the <i>insurance intermediary</i> is an <i>insurer</i>), 20.</p> <p>The following chapters of <i>SUP</i> do not apply to an <i>insurance intermediary</i> when doing (1) or (2): 4, 13, 14, 17, 18 (unless the <i>insurance intermediary</i> is an <i>insurer</i>), 19.</p>
	Enforcement manual, <i>ENF</i>	Applies to an <i>insurance intermediary</i> when doing (1) or (2).
	Decision making manual, <i>DEC</i>	Applies to an <i>insurance intermediary</i> when doing (1) or (2).
Redress	Dispute resolution: Complaints, <i>DISP</i>	Applies to an <i>insurance intermediary</i> when doing (1) or (2).
	Compensation, <i>COMP</i>	An <i>insurance intermediary</i> , as a <i>participant firm</i> for the purposes of <i>COMP</i> in respect of <i>insurance mediation activities</i> relating to <i>non-investment insurance contracts</i> , is liable to contribute to a levy raised by the <i>FSCS</i> for the purposes of paying compensation.

	<b>Module</b>	<b>Application</b>
Specialist sourcebooks	Credit Unions, <i>CRED</i>	Applies to an <i>insurance intermediary</i> doing (1) or (2) where it is also a <i>credit union</i> .
	Electronic Commerce Directive, <i>ECO</i>	Applies to an <i>insurance intermediary</i> doing (1) or (2).
	Electronic money, <i>ELM</i>	Does not apply to an <i>insurance intermediary</i> doing (1).  May apply to an <i>insurance intermediary</i> doing (2).
	Professional firms, <i>PROF</i>	Applies to an <i>insurance intermediary</i> doing (1) or (2) where it is also a <i>professional firm</i> .
	Lloyd's sourcebook, <i>LLD</i>	Applies only to the <i>Society</i> but some requirements are relevant to an <i>insurance intermediary</i> doing (1) or (2) where it is also an <i>underwriting agent</i> .
	Collective Investment Schemes sourcebook, <i>CIS</i>	Applies to an <i>insurance intermediary</i> doing (1) or (2) where it is also an <i>operator</i> or a <i>depository</i> of an <i>AUT</i> , <i>ICVC</i> or certain other <i>collective investment schemes</i> .
	Recognised Investment Exchanges and Recognised Clearing Houses, <i>REC</i>	Does not apply.

## ICOB 2

### General rules (including unfair inducements)

#### 2.1 Application: who?

##### 2.1.1 R (1) This chapter applies to:

- (a) an *insurer*;
- (b) an *insurance intermediary*;
- (c) a *managing agent*.

(2) *ICOB 2.3, 2.4, 2.5, 2.6, 2.7 and 2.8 apply to a firm that communicates or approves a non-investment financial promotion to which ICOB 3 applies.*

#### 2.2 Communication

2.2.1 G The purpose of *ICOB 2.2.3R* is to restate, in slightly amended form, and as a separate *rule*, the part of *Principle 7* (Communications with customers) that relates to communication of information. This enables a *customer*, who is a *private person*, to bring an action for damages under section 150 of the *Act* (Contravention of rules) to recover loss resulting from a *firm* referred to in *ICOB 2.1.1R* communicating information in the course of *regulated activities* in a way that is not clear or fair or that is misleading.

##### 'Key facts' logo

2.2.2 R A *firm* must not use the key facts logo unless it is required by a *rule*.

##### Clear, fair and not misleading communication

2.2.3 R (1) When a *firm* communicates information to a *customer*, it must take reasonable steps to communicate in a way that is clear, fair and not misleading.

(2) Paragraph (1) does not apply to a *firm* when it *communicates a non-investment financial promotion* in circumstances in which *ICOB 3 (Financial promotion)* applies to the *firm*.

2.2.4 G When considering how to comply with the requirements of *ICOB 2.2.3R*, a *firm* should have regard to the *customer's* knowledge of the *contract of insurance* to which the information relates.

- 2.2.5 G *ICOB 2.2.3R* covers all communications with *customers*, for example, any oral or written statements, telephone calls and any correspondence which is not a *non-investment financial promotion* to which *ICOB 3* (Financial promotion) applies. In respect of *non-investment financial promotions*, *firms* should note the separate requirements of *ICOB 3*.
- 2.2.6 G Prominence of relevant information can play a key role in ensuring that a communication is clear, fair and not misleading. Where this is the case, the *FSA* will assess prominence in the context of the communication as a whole. Use can be made of the positioning of text, background and text colour and type size to ensure that specified information meets the requirements of *ICOB*.
- 2.2.7 G A *firm* should make every effort to ensure that information is presented clearly, fairly and in a way that does not mislead, whether it is to be viewed as a hard copy, as an electronic document on screen or presented on some other medium (such as audio-tape for visually-impaired *customers*). A *firm* should:
- (1) use materials and design (including paper size, colour, font type and font size, tone and volume) to present the information legibly and accessibly, and in a balanced way;
  - (2) use emphasis sparingly; and
  - (3) not use differential font sizes or positioning so that the impact on a *customer* of some information (e.g. significant conditions, exclusions from the scope of cover or charges made to *customers*) is likely to be materially less than other provisions, parts or pages of the document.

## 2.3 Inducements

- 2.3.1 G *Principles 1* and *6* require a *firm* to conduct its business with integrity, to pay due regard to the interests of its *customers* and to treat them fairly. The purpose of *ICOB 2.3* is to ensure that a *firm* does not conduct business under arrangements that might give rise to a conflict with its duty to *customers* or to unfair treatment of them.

- 2.3.2 R **A *firm* must take reasonable steps to ensure that it, and any *person* acting on its behalf, does not:**

- (1) offer, give, solicit or accept an inducement; or**
- (2) direct or refer any actual or potential business in relation to an *insurance mediation activity* to another *person* on its own initiative or on the instructions of an *associate*;**

**if it is likely to conflict to a material extent with any duty that the *firm* owes to its *customers* in connection with an *insurance mediation activity* or any duty which such a recipient *firm* owes to its *customers* in connection with an *insurance mediation activity*.**



- 2.3.3 G The purpose of *ICOB* 2.3.2R(2) is to prevent the requirement in *ICOB* 2.3.2R(1) being circumvented by an inducement being given or received by an unregulated *associate*. There may be instances where a *firm* is able to demonstrate that it could not reasonably have knowledge of an *associate* giving or receiving an inducement. It should not, however, direct business to another *person* on the instruction of an *associate* if this is likely to conflict with the interests of its *customers*.
- 2.3.4 G An inducement is a benefit offered to a *firm*, or any *person* acting on its behalf, with a view to that *firm*, or that *person*, adopting a particular course of action. This can include, but is not limited to, cash, cash equivalents, *commission*, goods, hospitality or training programmes.
- 2.3.5 G *ICOB* 2.3.2R does not prevent a *firm*:
- (1) assisting an *insurance intermediary* so that the quality of the *insurance intermediary's* service to *customers* is enhanced; or
  - (2) giving or receiving indirect benefits (such as gifts, hospitality or promotional competition prizes);
- providing in either case this is not likely to give rise to a conflict with the duties that the recipient owes to the *customer*. In particular, such benefits should not be of a kind or value that is likely to impair the ability of a *firm* to act in compliance with any *rule* in *ICOB*, for example the suitability requirements in *ICOB* 4.3 (Suitability).
- 2.3.6 G The inducement offered does not need to be related to the sales process itself. For example, an *insurance intermediary* has a duty to its *customers* to act with due care, skill and diligence, where it is acting for them at the *claims* stage.
- 2.3.7 G (1) *ICOB* 2.3.2R states that an inducement will only be considered unfair if it conflicts to a material extent with any duty that the *firm* owes to its *customers*. This means that the circumstances surrounding an inducement may determine whether or not it is unfair. It is a *firm's* responsibility to determine this.
- (2) A *firm* that is offered an inducement should consider whether accepting that inducement might cause it, or any *person* acting on its behalf, to act in a way which conflicts with the duty that the *firm* owes to its *customers*.
- 2.3.8 G (1) Inducements that operate at a distance from the sales process may not be unfair, if they do not have an effect on the sales person's selling of a particular product.
- (2) Incentives offered to staff should not encourage sales staff to sell products unsuited to *customers'* needs.

2.3.9 G A *firm* should have in place its own internal procedures for identifying unfair inducements. For example, it should be able to identify situations where the existence of an inducement has caused a course of action to be adopted, that conflicts to a material extent with any duty that the *firm* owes to its *customers*, and which would not have been taken in the absence of the inducement. It should also have in place a mechanism for remedying such situations should they occur.

## 2.4 Reliance on others

2.4.1 G *Principle 2* requires a *firm* to conduct its business with due skill, care and diligence. *ICOB 2.4* indicates the extent to which *firms* that carry on *insurance mediation activities* and that *communicate* or *approve a non-investment financial promotion* can meet this requirement by relying on others.

2.4.2 R **A *firm* will be taken to be in compliance with any rule in *ICOB* that requires a *firm* to obtain information, to the extent that the *firm* can show that it was reasonable for it to rely on information provided to it in writing by another person.**

2.4.3 E (1) In relying on *ICOB 2.4.2R*, a *firm* should take reasonable steps to establish that the other *person* providing written information:

(a) is either:

(i) not connected with the *firm* and competent to provide the information; or

(ii) provides information given by the *customer* or the *insurer*.

(2) Compliance with (1) may be relied on as tending to establish compliance with *ICOB 2.4.2R*.

(3) Contravention of (1) may be relied on as tending to establish contravention of *ICOB 2.4.2R*.

2.4.4 R (1) **Any information which a rule in *ICOB* requires to be sent to a *customer* may be sent to another *person* on the instruction of the *customer*.**

(2) **There is no need for a *firm* to supply information to a *customer* where it has taken reasonable steps to establish that this has been or will be supplied by another *person*.**

## 2.5 Exclusion of liability

2.5.1 G *Principle 6* (Customers' interests) requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly. A *firm* may not exclude the duties it owes or the liabilities it has to a *customer* under the *regulatory system*. It may exclude other duties and liabilities only if it is reasonable for it to do so.

2.5.2 R A *firm* must not, in any written or oral communication, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability it may have to the *customer* under the *regulatory system*.

2.5.3 R A *firm* must not in any written or oral communication to a *customer*, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability not referred to in *ICOB 2.5.2R* unless it is reasonable for it to do so.

## 2.6 Application to electronic media

2.6.1 G *GEN 2.2.14R* (References to writing) has the effect that electronic media may be used to make communications that are required by the *Handbook* to be “in writing” unless a contrary intention appears. In *ICOB*, the use of an electronic medium is restricted in certain circumstances to a *durable medium* as required by the *DMD* and the *IMD*.

2.6.2 G For any electronic communication with a *customer* in relation to a *non-investment insurance contract*, a *firm* should:

- (1) have in place appropriate arrangements, including contingency plans, to ensure the secure transmission and receipt of the communication; it should also be able to verify the authenticity and integrity of the communication, together with the date and time sent and received; the arrangements should be proportionate and take into account the different levels of risk in a *firm*'s business;
- (2) be able to demonstrate that the *customer* wishes to communicate using this medium; and
- (3) if entering into an agreement, make it clear to the *customer* that a contractual relationship is created that has legal consequences.

2.6.3 G A *firm* should note that *GEN 2.2.14R* does not affect any other legal requirement that may apply in relation to the form or manner of *executing* a document or agreement.

## 2.7 General provision related to distance contracts

2.7.1 R During the course of a *distance contract* with a *retail customer*, the making of which constitutes or is part of a *non-investment insurance contract*:

- (1) the *firm* must, at the *retail customer*'s request, provide a paper copy of the contractual terms and conditions of the *non-investment insurance contract*; and
- (2) the *firm* must comply with the *retail customer*'s request to change the *means of distance communication* used, unless this is incompatible with the *non-investment insurance contract*.

- 2.8 Record keeping**
- 2.8.1 G General record-keeping standards, which continue to apply, can be found in SYSC 3.2.20R. *ICOB* 2.8 provides further details of the standard expected of *firms* where there is an obligation in *ICOB* requiring *firms* to maintain adequate records to evidence compliance. An overall view of the record-keeping requirements in *ICOB* is in *ICOB* Schedule 1.
- 2.8.2 R The records required in *ICOB* must be readily accessible for inspection by the *FSA*.**
- 2.8.3 G A record would be “readily accessible” if it was available for inspection within two *business days* of the request being received.
- 2.8.4 G Where a *firm* keeps standard, generic documents as records it should be able to identify which version, by date or reference number, was provided to the *customer*.
- 2.8.5 G (1) A *firm* may arrange for records to be kept in such form as it chooses provided the record is readily accessible for inspection by the *FSA*.
- (2) Where a *firm* chooses to maintain records in electronic form, it should take reasonable steps to ensure that:
- (a) the electronic record accurately records the original information; and
  - (b) the electronic record cannot be subject to unauthorised or accidental alteration.
- 2.8.6 G Each *rule* in *ICOB* that requires a record to be made and retained specifies that the record must be kept for a minimum period of three years. A *firm* should consider retaining records for longer periods in case *customers* complain or take legal action against the *firm*. A *firm* should, in particular, consider what constitutes an appropriate retention period for records which relate to *non-investment insurance contracts* which may give rise to *claims* some time after the inception of the contract (e.g. *employers' liability insurance*).

# ICOB 3

## Financial promotion

### 3.1 Application: general

3.1.1 G (1) *ICOB 3.2.1R* states that this chapter applies generally to *firms* in relation to all *non-investment financial promotions*. But, this wide application is cut back by *ICOB 3.3* (Application: what?) and *ICOB 3.4* (Application: where?) which limit the application of this chapter for:

- (a) *non-investment financial promotions* which fall within the scope of the exemptions in the *Financial Promotion Order* or the additional exemptions set out in *ICOB 3.3.6R*; and
- (b) *non-investment financial promotions to persons* outside the *United Kingdom*.

(2) *ICOB 3.1.2G* contains a table summarising some of the exemptions in the *Financial Promotion Order* that are likely to be of particular interest to *firms*. A *firm* which *communicates* or *approves* only *financial promotions* that fall within an exemption need not concern itself with *ICOB 3*.

3.1.2 G Table: Financial Promotion Order exemptions

This table belongs to *ICOB 3.1.1G(2)*. In this table references to ‘relevant insurance activity’ are to *effecting* and *carrying out a non-investment insurance contract as principal*.

Financial Promotion Order article no. and name of exemption	Summary of exemption
Article 17 (Generic promotions)	A <i>non-investment financial promotion</i> that does not identify (directly or indirectly) an <i>insurer</i> or any <i>person</i> as a <i>person</i> who carries on a <i>controlled activity</i> in relation to a <i>non-investment insurance contract</i> is exempt from <i>ICOB 3</i> . So an <i>insurance intermediary</i> advertising <i>insurance mediation services</i> is exempt from <i>ICOB 3</i> providing the advertisement does not name an <i>insurer</i> . This is because the activities of the <i>insurance intermediary</i> do not constitute <i>controlled activities</i> .

Financial Promotion Order article no. and name of exemption	Summary of exemption
	For further <i>guidance</i> see <i>AUTH</i> App 1.12.14G to <i>AUTH</i> App 1.12.17G.
Article 24 (Relevant insurance activity: non-real time communications)	<p>A <i>non-investment financial promotion</i> which contains the following information is exempt from <i>ICOB</i> 3:</p> <ol style="list-style-type: none"> <li>(1) the full name of the <i>insurance undertaking</i>;</li> <li>(2) the country or territory in which the <i>insurance undertaking</i> is incorporated (described as such);</li> <li>(3) if different from (2), the country or territory in which the <i>insurance undertaking's</i> principal place of business is situated (described as such);</li> <li>(4) whether or not the <i>insurance undertaking</i> is regulated in respect of its insurance business;</li> <li>(5) if the <i>insurance undertaking</i> is regulated, the name of the regulator in its principal place of business or, if there is more than one regulator, the name of the prudential regulator;</li> <li>(6) whether any transaction to which the <i>non-investment financial promotion</i> relates would be covered by a dispute resolution scheme or compensation scheme, if so identifying each such scheme.</li> </ol>
Article 25 (Relevant insurance activity: non-real time communications: reinsurance and large risks)	A <i>financial promotion</i> which concerns only a <i>reinsurance contract</i> or a <i>contract of large risks</i> is exempt from <i>ICOB</i> 3.
Article 26 (Relevant insurance activity: real time)	<i>ICOB</i> 3 does not apply to a <i>financial promotion</i> which is <i>communicated</i> in the course of a personal visit, telephone conversation or other interactive dialogue. This does not include interactive dialogue by means of the exchange of

Financial Promotion Order article no. and name of exemption	Summary of exemption
communications)	<p>letters or e-mails or in a publication. Such communication will be deemed to be non-real time and will be subject to <i>ICOB 3</i>, unless another exemption applies.</p> <p>For further <i>guidance</i> see <i>AUTH</i> App 1.10.2G.</p>

- 3.1.3 G A communication may contain both a *non-investment financial promotion* and one or more of a *financial promotion* and a *qualifying credit promotion*, for example, a leaflet from a *firm* which describes the range of insurance, savings and mortgage products it provides. In such cases, *ICOB 3*, *COB 3* and *MCOB 3* will all be relevant.

### 3.2 Application: who?

- 3.2.1 R **This chapter applies to every *firm* which *communicates* or *approves* a *non-investment financial promotion*.**

#### Appointed representatives

- 3.2.2 G Under section 39(3) of the *Act*, a *firm* is responsible for *financial promotions communicated* by its *appointed representatives* when acting as such (see *ICOB 1.6* (Appointed representatives)).

#### Nationals of other EEA States

- 3.2.3 G A national of an *EEA State* (other than the *United Kingdom*) wishing to take advantage of the exemption in article 36 of the *Financial Promotion Order* in relation to any *controlled activity* lawfully carried on by him in that State, should act in conformity with the *rules* in this chapter.

#### Authorised professional firms

- 3.2.4 R (1) ***ICOB 3* does not apply to an *authorised professional firm* in relation to the *communication* of a *non-investment financial promotion* if the following conditions are satisfied:**
- (a) **the *firm*'s main business is the practice of its profession** (see *IPRU(INV) 2.1.2R(3)*);
  - (b) **the *financial promotion* is made for the purposes of and incidental to the promotion or provision by the *firm* of:**

- (i) its professional services; or
- (ii) its *non-mainstream regulated activities* (see *PROF 5.2*); and
- (c) the *financial promotion* is not communicated on behalf of another person who would not be able lawfully to communicate the *financial promotion* if he were acting in the course of business.

(2) In (1)(b)(i), “professional services” means services:

- (a) which do not constitute a *regulated activity*; and
- (b) the provision of which is supervised and regulated by a *designated professional body*.

3.2.5 G *Authorised professional firms* are reminded that, in circumstances in which *ICOB 3* does not apply to the *firm*, *ICOB 2.2.3R* (Clear, fair and not misleading communication) may apply.

### 3.3 Application: what?

#### What do “communicate” and “non-investment financial promotion” mean?

3.3.1 G The *rules* in this chapter adopt various concepts from the restriction on *financial promotion* by *unauthorised persons* in section 21(1) of the *Act* (Restrictions on financial promotion). *Guidance* on that restriction is contained in *AUTH App 1* (Financial promotion and related activities) and that *guidance* will be relevant to interpreting these *rules*. In particular, *guidance* on the meaning of:

- (1) “*communicate*” is in *AUTH App 1.6* (Communicate);
- (2) “invitation or inducement” and “*engage in investment activity*” (two elements which, with “*communicate*”, make up the definition of “*financial promotion*”) are in *AUTH App 1.4* (Invitation and inducement) and *AUTH App 1.7* (Engage in investment activity).

#### Definition of “non-investment financial promotion”.

3.3.2 G The *rules* in this chapter apply to *non-investment financial promotions* only. These are *financial promotions* which relate to *non-investment insurance contracts*. A *non-investment financial promotion* is, by definition, not a *real time financial promotion*.

#### Media of communication

3.3.3 G (1) There is no restriction on the media of communication to which this chapter applies. It applies to a *non-investment financial promotion*



*communicated* by any means, including by way of printed advertising, radio and television broadcast, e-mail, the Internet and electronic media such as digital and other forms of interactive television and media. Both solicited and unsolicited communications are covered.

- (2) *Financial promotions* may be *communicated*, for example, by means of:
- (a) product brochures;
  - (b) general advertising in magazines, newspapers, radio and television programmes and websites;
  - (c) mailshots (whether distributed by *post*, fax, e-mail or other media);
  - (d) written correspondence;
  - (e) sales aids which themselves constitute a *financial promotion*; and
  - (f) other publications, which may contain *non-personal recommendations* as to the acquisition, retention or disposal of *non-investment insurance contracts*.

3.3.4 G *Guidance* on the use of the Internet for *communicating non-investment financial promotions* is in *ICOB 3.9* (The Internet and other electronic media) and *AUTH App 1.22* (The Internet).

**Exemptions**

3.3.5 R **This chapter does not apply to a *firm* in relation to a *non-investment financial promotion* of a kind listed in *ICOB 3.3.6R*.**

3.3.6 R **Table: Exemptions**

**This table belongs to *ICOB 3.3.5R*.**

<b>Exemptions</b>	
<b>This chapter does not apply to the following:</b>	
<b>(1)</b>	<b>a <i>non-investment financial promotion</i> to a <i>commercial customer</i>, that is a <i>financial promotion</i> which:</b>
<b>(a)</b>	<b>is made only to recipients who the <i>firm</i> has taken reasonable steps to establish are <i>commercial customers</i>; or</b>

<b>Exemptions</b>	
	(b) may reasonably be regarded as directed only at recipients who are <i>commercial customers</i> ;
(2)	a <i>non-investment financial promotion</i> which can lawfully be <i>communicated</i> by an <i>unauthorised</i> communicator without <i>approval</i> ;
(3)	a <i>non-investment financial promotion communicated</i> from outside the <i>United Kingdom</i> which would be exempt under articles 30, 31, 32 or 33 of the <i>Financial Promotion Order</i> (Overseas communicators) if the office from which the <i>non-investment financial promotion</i> is <i>communicated</i> were a separate <i>unauthorised person</i> (but see <i>ICOB 4.2.19R</i> ) (Overseas business for UK retail customers) and <i>GEN 4.4</i> (Business for private customers from non-UK offices));
(4)	a "one-off" <i>non-investment financial promotion</i> : if the conditions set out in (a) to (c) are satisfied, a <i>non-investment financial promotion</i> is to be regarded as "one-off"; if not, the fact that any one or more of these conditions is met is to be taken into account in determining if a <i>non-investment financial promotion</i> is "one-off", but a <i>non-investment financial promotion</i> may be regarded as "one-off" even if none of the conditions are met. The conditions are that:
	(a) the <i>non-investment financial promotion</i> is <i>communicated</i> only to one recipient or only to one group of recipients in the expectation that they would engage in any investment activity jointly;
	(b) the identity of the contract or service to which the <i>non-investment financial promotion</i> relates has been determined having regard to the particular circumstances of the recipient;
	(c) the <i>non-investment financial promotion</i> is not part of an organised marketing campaign;
(5)	a <i>non-investment financial promotion</i> which contains only one or more of the following:
	(a) the name of the <i>firm</i> (or its <i>appointed representative</i> );
	(b) the name of the <i>non-investment insurance contract</i> ;
	(c) a logo;

Exemptions		
	(d)	a contact point (address (including an e-mail address), telephone or fax number);
	(e)	a brief, factual description of the <i>firm's</i> (or its <i>appointed representative's</i> ) activities;
	(f)	a brief, factual description of the <i>firm's</i> (or its <i>appointed representative's</i> ) fees;
	(g)	a brief, factual description of the <i>firm's</i> products.

### Combination of exemptions

- 3.3.7 R A *firm* may rely on more than one exemption (and also on *ICOB 3.4.1R* (Territorial scope)) in relation to the same *non-investment financial promotion*.

### Guidance on the exemptions

- 3.3.8 G (1) Under *ICOB 3.3.6R(1)*, a *non-investment financial promotion* which is *communicated* only to a *commercial customer* is exempt. See *ICOB 3.6.3R* and *ICOB 3.6.4R*, which amplify this exemption. A *firm* will need to take particular note of the conditions in *ICOB 3.6.4R* when designing *non-investment financial promotions* for trade publications that may also be available to a *retail customer*.
- (2) *ICOB 3.3.6R(4)* reflects the exemption in article 28 of the *Financial Promotion Order* (one-off non-real time communications and solicited real time communications) but goes further, exempting all such *non-investment financial promotions*. It exempts, among other things, correspondence which is specifically written for a recipient, whether hard copy or e-mail. A *firm* should note, however, that such correspondence will, if *personal recommendations* are made, be subject to other obligations such as *ICOB 4.3* and *ICOB 4.4*. It does not exempt *non-investment financial promotions communicated* in the form of mass mailshots, which may appear to be items of personalised correspondence but which in fact comprise the same, or virtually the same, material sent to a number of recipients, without tailoring the material to the circumstances of each recipient. Such mailshots must meet the requirements of *ICOB 3. AUTH App 1.14.3G* (One-off financial promotions (articles 28 and 28A)) provides further *guidance* on the scope of the exemption in article 28.
- (3) *ICOB 3.3.6R(5)(e)*, (f) and (g) exempt a *non-investment financial promotion* made by a *firm* which refers only to its activities in general

terms in image advertising. Acceptable examples include ‘general insurance’ or ‘life and general insurance business’. In addition a *firm* or its *appointed representative* may include its name, address and telephone number in accordance with *ICOB* 3.3.6R(5)(a) and (d). *AUTH* App 1.4.20G (Image advertising) provides *guidance* on when image advertising may involve a *financial promotion*.

- (4) A *non-investment financial promotion* included in a newspaper, magazine or periodical which is printed and published overseas, but which may be brought into the *United Kingdom* and made available to *persons* in the *United Kingdom*, will be exempt provided that the *non-investment financial promotion* is not *communicated to persons* inside the *United Kingdom* (see *ICOB* 3.4 and *AUTH* App 1.12.2G (Financial promotions to overseas recipients (article 12))).

### **Other Handbook rules relevant to financial promotions**

- 3.3.9 G (1) A *firm* is reminded that *non-investment financial promotions* (including those which are exempt) may be subject to more general *rules* including *Principle 7* (Communications with clients), *SYSC* 3 (Systems and controls) *ICOB* 2.2.3R (Clear, fair and not misleading communication) and *ICOB* 5 (Product disclosure).
- (2) A *firm* is reminded that, although *ICOB* 3 makes no specific *rules* relating to the content of a *non-investment financial promotion*, the disclosure requirements in *ICOB* 4 and *ICOB* 5 may apply.
- (3) A *firm* is reminded that if, in the course of making a *non-investment financial promotion* of any kind, it gives a *personal recommendation* to a *customer* about the suitability of a *non-investment insurance contract* for that individual, the *firm* is subject to the relevant *rules* on advising and selling in *ICOB* 4 (Advising and selling standards).

### **3.4 Application: where?**

#### **Territorial scope**

#### **3.4.1 R This chapter applies to a *firm* only in relation to:**

- (1) **the *communication* of a *non-investment financial promotion* to a *person* inside the *United Kingdom*; and**
- (2) **the *approval* of a *non-investment financial promotion* for *communication* to a *person* inside the *United Kingdom*;**

**subject to *ICOB* 3.4.3R (Exceptions to territorial scope).**

- 3.4.2 G (1) The application under *ICOB* 3.4.1R is relevant both when a *firm communicates a non-investment financial promotion* itself and when a *firm approves a non-investment financial promotion for communication* by others. But see also *ICOB* 3.4.3R.
- (2) The exemptions in *ICOB* 3.3.6R (Application: what?; Exemptions) also incorporate some territorial elements. In particular, the exemption for *financial promotions* originating outside the *United Kingdom* (section 21(3) of the *Act* (Restrictions on financial promotion)) (see *ICOB* 3.3.6R(2)) and *AUTH* App 1.12.2G (Financial promotions to overseas recipients (article 12)), the exemptions for overseas communicators (see *ICOB* 3.3.6R(3)) and the exemption for *incoming electronic commerce communications* (see *AUTH* App 1.12.38G (article 20B)).
- (3) In the context of the provision of an *electronic commerce activity* to an *EEA ECA recipient*, the scope of *ICOB* 3 is extended by *ECO* 2.2.3R (Financial promotion). This means that *ICOB* 3 will apply for *communications to EEA ECA recipients*.

#### **Exceptions to territorial scope**

3.4.3 R **The following parts of this chapter apply without any territorial limitation if a *firm approves a non-investment financial promotion*:**

- (1) ***ICOB* 3.1 to *ICOB* 3.6 (Application, Purpose and General); and**
- (2) ***ICOB* 3.8.1R(1) (Non-investment financial promotions: clear, fair and not misleading: comparisons).**

#### **Meaning of "communicated to a person inside or outside the United Kingdom"**

3.4.4 R **For the purposes of this chapter:**

- (1) **a *non-investment financial promotion* is *communicated to a person outside the United Kingdom* if it is:**
  - (a) **made to a *person* who receives it outside the *United Kingdom*; or**
  - (b) **directed only at *persons* outside the *United Kingdom*; and**
- (2) **a *non-investment financial promotion* is *communicated to a person inside the United Kingdom* if it is *communicated to a person other than as described in (1)*;**

**and see *ICOB* 3.4.5R and *ICOB* 3.6.3R, which amplify this rule.**

### Meaning of "directed only at persons outside the United Kingdom"

- 3.4.5 R (1) If the conditions set out in 4(a), (b), (c) and (d) are met, a *non-investment financial promotion* directed from a place inside the *United Kingdom* will be regarded as directed only at *persons* outside the *United Kingdom*.
- (2) If the conditions set out in 4(c) and (d) are met a *non-investment financial promotion* directed from a place outside the *United Kingdom* will be regarded as directed only at *persons* outside the *United Kingdom*.
- (3) In any other case where one or more of the conditions in 4(a) to (e) is met, that fact will be taken into account in determining whether a *non-investment financial promotion* is directed only at *persons* outside the *United Kingdom* (but a *non-investment financial promotion* may still be regarded as directed only at *persons* outside the *United Kingdom* even if none of these conditions is met).
- (4) The conditions are that:
- (a) the *non-investment financial promotion* is accompanied by an indication that it is directed only at *persons* outside the *United Kingdom*;
- (b) the *non-investment financial promotion* is accompanied by an indication that it must not be acted upon by *persons* in the *United Kingdom*;
- (c) the *non-investment financial promotion* is not referred to in, or directly accessible from, any other *non-investment financial promotion* which is made to a *person* or directed at *persons* in the *United Kingdom* by or on behalf of the same *person*;
- (d) there are in place proper systems and procedures to prevent recipients in the *United Kingdom* (other than those to whom the *non-investment financial promotion* might otherwise lawfully have been made) *engaging in the investment activity* to which the *non-investment financial promotion* relates with the *person* directing the *non-investment financial promotion*, a *close relative* of his or a member of the same *group*; and
- (e) the *non-investment financial promotion* is included in:
- (i) a website, newspaper, journal, magazine or periodical publication which is principally accessed in or intended for a market outside the *United Kingdom*;

- (ii) a radio or television broadcast or teletext service transmitted principally for reception outside the *United Kingdom*.

### 3.5 Purpose

3.5.1 G (1) Section 21(1) of the *Act* (Restrictions on financial promotion) imposes a restriction on the *communication* of *financial promotions* (*non-investment financial promotions* in *ICOB*) by *unauthorised persons*. A person must not, in the course of business, *communicate* a *non-investment financial promotion* unless:

- (a) he is an *authorised person*; or
- (b) the content of the *non-investment financial promotion* is *approved* by an *authorised person*.

(2) However, the *Financial Promotion Order* exempts from the restriction created by section 21(1) of the *Act* certain types of *financial promotion*.

3.5.2 G (1) The purpose of this chapter is to provide *rules* and *guidance* for a *firm* that wishes to *communicate* or *approve* a *non-investment financial promotion*. *AUTH* App 1 (Financial promotion and related activities) provides further detailed *guidance* on the *financial promotion* regime under section 21 of the *Act* (Financial promotion) which will be relevant in interpreting these *rules*.

(2) This chapter amplifies, for activities within its scope:

- (a) *Principle 6* (Customers' interests) which requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly; and
- (b) *Principle 7* (Communications with clients) which requires a *firm* to pay due regard to the information needs of its *clients* and *communicate* information to them in a way which is clear, fair and not misleading.

### 3.6 General

#### Other regulations and guidelines

3.6.1 G A *firm* *communicating* a *non-investment financial promotion* may also be subject to other regulations and guidelines, outside the remit of the *FSA*, such as:

- (1) the codes issued from time to time by the Advertising Standards Authority;
- (2) regulations from any *overseas regulator* (where relevant) if the *firm* intends to market from the *United Kingdom* into any other country; and

- (3) the Privacy and Electronic Communication (EC Directive) Regulations 2003 (SI 2003/2426).

#### **Non-investment financial promotions**

- 3.6.2 R (1) A *non-investment financial promotion* includes a *financial promotion* for a *non-investment insurance contract* made by letter or e-mail or contained in a newspaper, journal, magazine, other periodical publication, website, television or radio programme, or teletext service.
- (2) The following are to be regarded as indications that a *financial promotion* for a *non-investment insurance contract* is a *non-investment financial promotion* rather than a *real time financial promotion*:
- (a) the *financial promotion* is *communicated* to more than one *person* in identical terms (save for details of the recipient's identity);
- (b) the *financial promotion* is *communicated* by way of a system which in the normal course constitutes or creates a record of the communication which is available to the recipient to refer to at a later time; and
- (c) the *financial promotion* is *communicated* by way of a system which in the normal course does not enable or require the recipient to respond immediately to it.

#### **Meaning of "made", "directed at" and "recipient" in this chapter**

- 3.6.3 R In accordance with article 6 of the *Financial Promotion Order* (Interpretation: communications) any reference in this chapter to:
- (1) a *communication* being made to another *person* is a reference to a *communication* being addressed in legible form to a particular *person* or *persons* (for example, where it is contained in a letter);
- (2) a *communication* being directed at *persons* is a reference to a *communication* being addressed to *persons* generally (for example where it is contained in a television broadcast or website); and
- (3) a recipient of a *communication* is the *person* to whom the *communication* is made or, in the case of a *financial promotion* which is directed at *persons* generally, any *person* who reads or hears the *communication*.

#### **When is a financial promotion "directed only at" certain persons?**

- 3.6.4 R (1) This *rule* applies for the purposes of determining whether a *communication* is directed only at *commercial customers* under *ICOB*



### 3.3.6R(1).

- (2) If all the conditions set out in (4) are met, a *communication* is to be regarded as directed as in (1).
- (3) In any other case in which one or more of those conditions is met, that fact is to be taken into account in determining whether the *communication* is directed as in (1) (but a *communication* may still be regarded as so directed even if none of the conditions in (4) are met).
- (4) The conditions are that:
  - (a) the *communication* includes an indication of the description of *persons* to whom it is directed and an indication of the fact that the contract to which it relates is available only to such *persons*;
  - (b) the *communication* includes an indication that *persons* of any other description should not rely upon it; and
  - (c) there are in place proper systems and procedures to prevent recipients other than *persons* to whom it is directed entering into the contract to which the *communication* relates with the *person* directing the *communication*, a *close relative* of his or a member of the same *group*.

## 3.7 Confirmation of compliance

### Confirmation of compliance

- 3.7.1 R (1) Before a *firm* communicates or approves a *non-investment financial promotion*, it must confirm that the *non-investment financial promotion* complies with the *rules* in this chapter.
  - (2) A *firm* must arrange for the confirmation exercise in (1) to be carried out by an individual or individuals with appropriate expertise.
- 3.7.2 G (1) In *ICOB* 3.7.1R(2) 'appropriate expertise' will vary depending on the complexity of the *financial promotion* and the *non-investment insurance contract* to which it relates. The individuals engaged by a *firm* to confirm the compliance of its *financial promotions* with this chapter may have different levels of expertise and therefore a different level of authority for confirmation depending on the type of *financial promotion* and the *non-investment insurance contract* involved.
  - (2) A *firm* may arrange for a third party with appropriate expertise to carry out the confirmation exercise on the *firm's* behalf, but the responsibility for the *non-investment financial promotion* remains with the *firm*.

### Withdrawing confirmation

**3.7.3 R** If, at any time after it has completed a confirmation exercise in *ICOB 3.7.1R(1)* a *firm* becomes aware that a *non-investment financial promotion* no longer complies with the *rules* in this chapter, it must ensure that the *non-investment financial promotion* is withdrawn as soon as reasonably practicable by:

- (1) ceasing to *communicate* it;
- (2) withdrawing its *approval* (if applicable); and
- (3) notifying any *person* that the *firm* knows to be relying on its *approval* (if applicable) or confirmation (under *ICOB 3.7.5R*).

**3.7.4 G** (1) *ICOB 3.7.3R* is of particular importance to a *non-investment financial promotion*, such as a product brochure, that a *firm* uses over a period of time. It has little application to a *non-investment financial promotion* which is of its nature ephemeral, for example, a mobile phone text message. Further, a *non-investment financial promotion* which clearly speaks as at a particular date will not cease to comply with the *rules* in this chapter merely because the passage of time has rendered it out-of-date.

- (2) For compliance with *ICOB 3.7.3R* the *FSA* will expect a *firm* to monitor its relevant *non-investment financial promotions* as part of the *firm's* routine compliance monitoring procedures. A *firm* may find it helpful to designate a relevant *non-investment financial promotion* with a 'review date', a date at which the *non-investment financial promotion* should be checked once more against the *rules* of this chapter. If it is found no longer to meet these requirements it should be withdrawn as soon as reasonably practicable.
- (3) If at any time a *firm* becomes aware that a *retail customer* may have been misled by a *non-investment financial promotion* it should consider whether the *retail customer* who has responded to the *non-investment financial promotion* should be contacted with a view to explaining the position and offering any appropriate form of redress to those who have suffered financial loss.

### Communicating a financial promotion where another firm has confirmed compliance

**3.7.5 R** A *firm* will not contravene any of the *rules* in this chapter in the circumstances where it (*firm "A"*) communicates a *non-investment financial promotion* which has been produced by another *person* provided that:

- (1) A takes reasonable care to establish that another *firm* (*firm "B"*) has already confirmed the compliance of the *non-investment financial*

*promotion* in accordance with *ICOB 3.7.1R*;

- (2) A takes reasonable care to establish that A *communicates* the *non-investment financial promotion* only to recipients of the type for whom it was intended at the time B carried out the confirmation exercise; and
- (3) so far as A is, or ought to be, aware:
  - (a) the *non-investment financial promotion* has not ceased to be clear, fair and not misleading since that time; and
  - (b) B has not withdrawn the *non-investment financial promotion*.

### 3.8 Form and content of non-investment financial promotions

**Clear, fair and not misleading: comparisons and restrictions on the use of the key facts logo**

- 3.8.1 R (1) A *firm* must be able to show that it has taken reasonable steps to ensure that a *non-investment financial promotion* is clear, fair and not misleading.
- (2) A *non-investment financial promotion* which includes a comparison or contrast must:
  - (a) compare contracts meeting the same needs or which are intended for the same purpose;
  - (b) objectively compare one or more material, relevant, verifiable and representative features of those contracts, which may include price;
  - (c) not create confusion in the marketplace between the *firm* itself (or the *person* whose *non-investment financial promotion* it approves) and a competitor or between the *firm's* trademarks, trade names, other distinguishing marks, contracts or services (or those of the *person* whose *non-investment financial promotion* it approves) and those of a competitor;
  - (d) not discredit or denigrate the trademarks, trade names, other distinguishing marks, contracts, services, activities or circumstances of a competitor;
  - (e) not take unfair advantage of the reputation of a trademark, trade name or other distinguishing marks of a competitor;

- (f) not present contracts as imitations or replicas of contracts bearing a protected trademark or trade name; and
  - (g) indicate in a clear and unequivocal way in any comparison referring to a special offer the date on which the offer ends or, where appropriate, that the special offer is subject to the availability of the contracts and services, and, where the special offer has not yet begun, the date of the start of the period during which the special price or other specific conditions shall apply.
- (3) A *non-investment financial promotion* must not contain the key facts logo unless it is required by a rule.

- 3.8.2 E (1) A *firm* should take reasonable steps to ensure that, for a *non-investment financial promotion*:
- (a) its promotional purpose is not in any way disguised or misrepresented;
  - (b) any statement of fact, promise or prediction is clear, fair and not misleading and discloses any relevant assumptions;
  - (c) any statement of opinion is honestly held and, unless consent is impracticable, given with the consent of the *person* concerned;
  - (d) the facts on which any comparison or contrast is made are verified, or, alternatively, that relevant assumptions are disclosed and that the comparison or contrast is presented in a fair and balanced way, which is not misleading and includes all factors which are relevant to the comparison or contrast;
  - (e) it does not contain any false indications, in particular as to:
    - (i) the *firm's* independence;
    - (ii) the *firm's* resources and scale of activities; or
    - (iii) the scarcity of any contract;
  - (f) the design, content or format does not disguise, obscure or diminish the significance of any statement, warning or other matter which the *non-investment financial promotion* is required by this chapter to contain;
  - (g) it does not include any reference to approval by the *FSA* or any government body, unless such approval has been obtained in writing from the *FSA* or that body (see also *GEN* 1.2 (Referring to approval

by the *FSA*));

- (h) it does not omit any matters the omission of which causes the *non-investment financial promotion* not to be clear, fair and not misleading; and
  - (i) the accuracy of all material statements of fact in it can be substantiated.
- (2) (a) Compliance with *ICOB 3.8.2E(1)* may be relied on as tending to show compliance with *ICOB 3.8.1R(1)*.
- (b) Contravention of *ICOB 3.8.2E(1)* may be relied on as tending to show contravention of *ICOB 3.8.1R(1)*.

### **Guidance on clear, fair and not misleading**

- 3.8.3 G (1) It cannot be assumed that recipients necessarily have an understanding of the contract being promoted. If a *non-investment financial promotion* is specially designed for a targeted collection of recipients who are reasonably believed to have particular knowledge of the contract being promoted, this fact should be made clear.
- (2) In relation to quotations of opinion:
- (a) where only part of an opinion is quoted, it should nevertheless be a fair representation; and
  - (b) any connection between the holder of the opinion and the *firm* should be made clear.
- (3) *Firms* should avoid the use of small print to qualify prominent claims.
- (4) If a *firm* communicates a *non-investment financial promotion* which contains a quotation of *premium* and it is unable to give the *retail customer* a precise quotation it should ensure that the *premium* quoted is representative of the *premium* that would be charged for a *person* in a similar position to the *retail customer*.
- (5) Unless the *firm* is prepared to give a precise quotation, the *non-investment financial promotion* should be accompanied by a prominent statement making clear that the *premium* quoted is an estimate only and that the actual *premium* will depend on individual circumstances.
- (6) Where a *non-investment financial promotion* indicates or implies that a *firm* can:

- (a) reduce the *premium*; or
- (b) provide the cheapest *premium*; or
- (c) reduce a *retail customer's* costs;

it should include, with equal prominence, a statement of the basis on which the reduction is to be achieved. The *FSA* will assess prominence in the context of the *non-investment financial promotion* as a whole. Use can be made of the positioning of text, background and text colour and type size to ensure that *ICOB* 3.8.1R(1) is satisfied.

- (7) Where (6) applies, and there are significant limitations on any savings, these should be given equal prominence in the *non-investment financial promotion* to the claimed savings. For example, if the *non-investment financial promotion* states that a *firm* can achieve a *premium* reduction in the form of either a percentage or monetary amount, but the saving is only available if the *retail customer* meets certain specific criteria, the criteria should be given equal prominence and not placed in small print.

### **3.9 The Internet and other electronic media**

- 3.9.1 G This section contains *guidance* on the use of the Internet and other electronic media to *communicate financial promotions*. *Firms* are also referred to the *guidance* in *ICOB* 2.6 (Application to electronic media).

#### **Approach and general guidance**

- 3.9.2 G Any material which meets the definition of a *non-investment financial promotion*, including any video or moving image material incorporated in any website containing a *non-investment financial promotion*, should comply with the *rules* in this chapter. See *AUTH* App 1.22 (The Internet) for further *guidance* on *non-investment financial promotions* on the Internet, including the treatment of hyperlinks and banners.
- 3.9.3 G
  - (1) Before using the Internet, digital or any other form of interactive television or other electronic media to promote its services a *firm* should refer to legislation such as the Data Protection Act 1998 and the Computer Misuse Act 1990, as well as to this chapter.
  - (2) When designing websites and other electronic media, *firms* should be aware of the difficulties that can arise when reproducing certain colours and printing certain types of text. These difficulties could cause problems with the presentation and retrieval of required information. Any *non-investment financial promotion* communicated by the Internet, digital or other forms of interactive television is subject to the requirements set out in *ICOB* 3.8 as applicable.

### Specific guidance

- 3.9.4 G The *FSA's* website <http://www.fsa.gov.uk> contains a wide range of information, including pages of specific relevance to *customers*. *Firms* may, if they wish, include a reference or hyperlink to the *FSA's* website; this will not, however, replace any requirements of *ICOB 3*.

## ICOB 4

### Advising and selling standards

#### 4.1 Application and purpose

##### Application: who and what?

- 4.1.1 R (1) Subject to *ICOB 4.1.4R*, this chapter applies to an *insurance intermediary* in accordance with *ICOB 4.1.3R*.
- (2) *ICOB 4.7 (Unsolicited services)* also applies to an *insurer* or *managing agent* when acting as a *product provider*.
- (3) Throughout this chapter, references to an *insurer* apply equally to a *managing agent*.
- 4.1.2 G (1) The definition of *insurance intermediary* includes an *insurer* when the *insurer* is carrying on *insurance mediation activities*, for example when, through its sales force, it *advises on* or *arranges* its own *non-investment insurance contracts* or those of another *insurer*.
- (2) For the limited application of this chapter to *authorised professional firms* in respect of their *non-mainstream regulated activities*, see *ICOB 1.2.10R(3)* and *ICOB 1.2.10R(4)*.
- 4.1.3 R **Table: Application of ICOB 4 by activity and customer type**

This table belongs to *ICOB 4.1.1R*.

Insurance mediation activity	Type of customer	Applicable section
<i>arranging except introducing</i>	<i>retail customer</i>	Whole chapter except <i>ICOB 4.3</i> and <i>ICOB 4.6</i>
<i>arranging except introducing</i>	<i>commercial customer</i>	Whole chapter except <i>ICOB 4.2.19R</i> , <i>ICOB 4.3</i> , <i>ICOB 4.5</i> and <i>ICOB 4.7</i>
<i>Advising</i>	<i>retail customer</i>	Whole chapter except <i>ICOB 4.6</i>
<i>advising</i>	<i>commercial customer</i>	Whole chapter except <i>ICOB 4.2.19R</i> , <i>ICOB 4.5</i> and <i>ICOB 4.7</i>
<i>Introducing</i>	<i>retail customer and commercial</i>	<i>ICOB 4.2.9R</i> and <i>ICOB 4.2.10G</i> only



4.1.4 R The following provisions in *ICOB* do not apply to an *insurance intermediary* that is an *insurer* when dealing with a *commercial customer*:

- (1) *ICOB* 4.2 (Status disclosure);
- (2) *ICOB* 4.4 (Statement of demands and needs), unless the *insurer* makes a *personal recommendation to the commercial customer*; and
- (3) *ICOB* 4.6 (Commission disclosure for commercial customers).

#### Renewals

4.1.5 G When a *contract of insurance* is renewed, the parties enter into a new *contract of insurance*, even if the terms and conditions of the new contract are identical to the old one. *ICOB* 4 therefore applies to the *renewed contract of insurance* as it would to the original *contract of insurance*, unless stated otherwise in *ICOB* 4.2.20R.

#### Purpose

- 4.1.6 G
- (1) This chapter amplifies *Principle 6* (Customers' interests), *Principle 7* (Communications with clients) and *Principle 9* (Customers: relationships of trust). *Principle 6* requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly. *Principle 7* requires a *firm* to pay due regard to the information needs of its *clients* and communicate information to them in a way which is clear, fair and not misleading. *Principle 9* requires a *firm* to take reasonable care to ensure the suitability of its *advice*.
  - (2) This chapter also implements articles 12 and 13 of the *Insurance Mediation Directive* for *non-investment insurance contracts* (which means that, in respect of communications by telephone, it follows the approach in article 3 of the *Distance Marketing Directive*).
  - (3) This chapter also implements article 9 of the *DMD* for *non-investment insurance contracts* concluded by *distance means*.
- 4.1.7 G The purpose of this chapter is to ensure that:
- (1) *customers* are adequately informed about the nature of the service that they have received from an *insurance intermediary* in relation to *non-investment insurance contracts*. In particular, *insurance intermediaries* need to make clear to *customers* the scope and type of the products and *insurance undertakings* on which their service is based;
  - (2) where a *personal recommendation* is made it is suitable for a *customer's* demands and needs. The nature of the steps an *insurance intermediary* will need to take to ensure that the *customer* receives a *personal recommendation* that is suitable will vary depending on the demands and needs of the *customer*, the type of *non-investment insurance contract*

being offered, and the type of *customer* (*retail customer* or *commercial customer*);

- (3) *customers* receive a statement of their demands and needs and the reasons for any *personal recommendation* made by an *insurance intermediary*;
- (4) the charges that an *insurance intermediary* imposes on a *retail customer* are not excessive;
- (5) if requested by a *commercial customer*, the *insurance intermediary* discloses its *commission*; and
- (6) *retail customers* are not charged for *non-investment insurance contracts* concluded by *distance means* without their prior consent.

## 4.2 Status disclosure

### Retail and commercial customers: disclosure before or immediately after conclusion of the contract

- 4.2.1 G (1) *ICOB 4.2.2R to ICOB 4.2.14R* set out the status disclosure requirements that an *insurance intermediary* must meet to comply with the *IMD*.
- (2) The *rules* in *ICOB 4.2* state the timing by which status disclosure information must be given to the *customer*, in accordance with the *IMD* and the *DMD*. The *insurance intermediary* may provide information to the *customer* earlier than the time specified in the *rules*. For example, an *insurance intermediary* who is also providing services in connection with *packaged products* or *regulated mortgage contracts* may wish to combine the information required by *ICOB 4.2* with the status disclosure requirements in *COB* or *MCOB*, and provide the information to the *customer* on initial contact, using the combined initial disclosure document in *ICOB 4 Ann 2R*.
- (3) For certain types of *general insurance contract*, such as motor insurance, it is customary for a *customer* to contact various *insurance intermediaries* for quick quotes which he can then compare. In these circumstances, it is not necessary for the *insurance intermediary* to give the status disclosure information at the time that the quick quote is provided, if the quote cannot be accepted (and a contract cannot be formed) without the *insurance intermediary* obtaining further information from the *customer*.
- (4) The *rules* in *ICOB 4.2* do not specify the format in which information must be provided to the *customer*. An *insurance intermediary* may use the initial disclosure document in *ICOB 4 Ann 1G*, the combined initial disclosure document in *ICOB 4 Ann 2R*, a terms of business letter, or another document to provide information to the *customer*.
- 4.2.2 R (1) **An *insurance intermediary* must provide the information in *ICOB 4.2.8R* to the *customer* in a *durable medium* at any time before conclusion of a *non-investment insurance contract*, unless an**

exemption in (2) or (3) applies.

**(2) Exemption: oral disclosure**

The information in *ICOB 4.2.8R* need not be provided in a *durable medium* before conclusion of the contract but may be provided orally before the conclusion of the contract if:

- (a) the *customer* requests this; or
- (b) the *customer* requires immediate cover.

**(3) Exemption: telephone sales**

(a) This exemption applies if the service is being provided on the telephone and the *customer* wishes to enter into a *non-investment insurance contract*.

(b) If the *customer* gives his explicit consent to receiving only limited disclosure, the *insurance intermediary* must provide the *customer* with the following information:

- (i) the name of the *insurance intermediary*;
- (ii) (if the call is initiated by the *insurance intermediary*) the commercial purpose of the call;
- (iii) the identity of the *person* in contact with the *retail customer* and his link with the *insurance intermediary*; and
- (iv) that other information is available on request, and the nature of the information.

**(4) Where (2) or (3) applies, the *customer* must be provided with the information in *ICOB 4.2.8R* in a *durable medium* immediately after the conclusion of the contract.**

- 4.2.3 G (1) The *insurance intermediary* may, if it so chooses, make the *customer* aware that he is able to receive the information in *ICOB 4.2.8R* orally, in accordance with *ICOB 4.2.2R(2)*, or (in the case of telephone communications) that the more limited information requirements of *ICOB 4.2.2R(3)* may apply.
- (2) If the *customer* requires immediate cover and the *non-investment insurance contract* is concluded over the telephone, the *insurance intermediary* may take advantage of either of the exemptions in *ICOB 4.2.2R(2)* or *ICOB 4.2.2R(3)*, subject to the *customer* giving his explicit consent.

## Use of the initial disclosure document and combined initial disclosure document

- 4.2.4 G (1) The requirement in *ICOB* 4.2.2R(1) can be met by use of the initial disclosure document set out in *ICOB* 4 Ann 1G. Alternatively, in circumstances where the *insurance intermediary* has reasonable grounds to be satisfied that the services which it is likely to provide will, in addition to relating to *non-investment insurance contracts*, also relate to *regulated mortgage contracts, regulated lifetime mortgage contracts or packaged products*, the *insurance intermediary* may use the combined initial disclosure document set out in *ICOB* 4 Ann 2R.
- (2) Subject to *ICOB* 4.2.5R, an *insurance intermediary* may use all or part of the wording and format of the initial disclosure document at *ICOB* 4 Ann 1G (though if it chooses to omit any of the information required by *ICOB* 4.2.8R, the *insurance intermediary* must still provide this information to the *customer* in a *durable medium* before the conclusion of the *non-investment insurance contract* in accordance with *ICOB* 4.2.2R). This flexibility does not apply if an *insurance intermediary* uses the combined initial disclosure document (see *ICOB* 4.2.7R), because the *COB* and *MCOB* rules require that the wording and the format of the document must not be changed.
- (3) The combined initial disclosure document must be given in accordance with the *rules* in *COB* and *MCOB*. In particular (and in contrast with the initial disclosure document set out in *ICOB* 4 Ann 1G), it will need to be provided on initial contact.
- 4.2.5 R **If an *insurance intermediary* chooses to use the initial disclosure document at *ICOB* 4 Ann 1G, it must not include the key facts logo and the heading and text in Section 1 unless it uses the document in full and makes no changes to the text other than changes allowed by the notes to the document.**
- 4.2.6 R **If an *insurance intermediary* uses the initial disclosure document and includes the key facts logo, the key facts logo:**
- (1) **must be positioned as shown in *ICOB* 4 Ann 1G;**
- (2) **must be accompanied by the words 'about our insurance services' as shown in *ICOB* 4 Ann 1G;**
- (3) **may be a different size from that in *ICOB* 4 Ann 1G, but it must be reasonably prominent and its proportions must not be distorted; and**
- (4) **may be in colour, but this must not diminish its prominence.**
- 4.2.7 R **If an *insurance intermediary* chooses to use the combined initial disclosure document at *ICOB* 4 Ann 2R, it must use the document in full and make no change to the text other than changes allowed by the notes to the document.**

4.2.8 R Table: Information to be provided before conclusion of the contract or immediately after conclusion of the contract

This table belongs to *ICOB 4.2.2R*.

(1)	The name and address of the <i>insurance intermediary</i> .
(2)	The <i>insurance intermediary's</i> statutory status (in accordance with <i>GEN 4 Ann 1R</i> (Statutory status disclosure)).
(3)	That items 1 and 2 can be checked on the <i>FSA's Register</i> by visiting the <i>FSA's</i> website <a href="http://www.fsa.gov.uk/register">http://www.fsa.gov.uk/register</a> or by contacting the <i>FSA</i> on 0845 606 1234.
(4)	Unless the <i>insurance intermediary</i> is an <i>insurer</i> , details of any holding, direct or indirect, that an <i>insurance intermediary</i> has that represents more than 10 per cent of the voting rights or of the capital in an <i>insurance undertaking</i> .
(5)	Unless the <i>insurance intermediary</i> is an <i>insurer</i> , details of any holding, direct or indirect, that an <i>insurance undertaking</i> or parent of an <i>insurance undertaking</i> has that represents more than 10 per cent of the voting rights or of the capital in the <i>insurance intermediary</i> .
(6)	<p>In relation to the <i>non-investment insurance contract</i> provided, whether the <i>insurance intermediary</i> has provided, or will provide, <i>advice</i> or <i>information</i>:</p> <p>(a) on the basis of a fair analysis of the market; or</p> <p>(b) from a limited number of <i>insurance undertakings</i>; or</p> <p>(c) from a single <i>insurance undertaking</i>.</p> <p>If (b) or (c) applies, the <i>insurance intermediary</i> must also disclose whether it is contractually obliged to conduct <i>insurance mediation activity</i> in this way.</p>
(7)	If the contract provided has not been selected on the basis of a fair analysis of the market, that the <i>customer</i> can request a copy of the list of the <i>insurance undertakings</i> the <i>insurance intermediary</i> selects from or deals with in relation to the contract provided.
(8)	How to complain to the <i>insurance intermediary</i> and that complaints may subsequently be referred to the <i>Financial Ombudsman Service</i> or any other applicable named complaints scheme.
(9)	That the <i>customer</i> may be entitled to compensation from the <i>compensation scheme</i> should the <i>insurance intermediary</i> be unable to meet its liabilities.

## Notes

<p>(1)</p>	<p>If the <i>customer</i> is dealing with an <i>appointed representative</i> of an <i>insurance intermediary</i>, the <i>insurance intermediary</i> is responsible for ensuring that the <i>appointed representative</i> makes the appropriate disclosures (see <i>ICOB 1.6</i>). In that case, the <i>insurance intermediary</i> must ensure that:</p> <ul style="list-style-type: none"><li>(a) for item 1, the <i>appointed representative</i> provides its own name and address;</li><li>(b) for item 2, the <i>appointed representative</i> makes the disclosure required by <i>GEN 4 Ann 1R(4)</i>;</li><li>(c) for item 4, the <i>appointed representative</i> discloses its own holding and not the holding of the <i>insurance intermediary</i>;</li><li>(d) for item 5, the holding disclosed is the holding in the <i>appointed representative</i> and not in the <i>insurance intermediary</i>;</li><li>(e) for item 6, the <i>appointed representative</i> discloses the basis on which it provides <i>advice</i> or information; and</li><li>(f) for item 8, the details provided are details of how to complain to the <i>appointed representative</i>.</li></ul>
<p>(2)</p>	<p>Under item 1, where the <i>insurance intermediary</i> trades under a different name from that under which it is <i>authorised</i>, it must disclose the name under which it is <i>authorised</i> and listed on the <i>FSA Register</i>. For an <i>appointed representative</i>, the same applies in relation to the name under which it is registered and listed on the <i>FSA Register</i>.</p>
<p>(3)</p>	<p>Under item 1, the address should be the head office address or, if more appropriate, the principal place of business from which the <i>insurance intermediary</i> or <i>appointed representative</i> expects to conduct business with the <i>customer</i>.</p>
<p>(4)</p>	<p>In addition to the disclosure required by item 9, the <i>insurance intermediary</i> must ensure that, where relevant, it describes the extent and level of compensation cover and how further information can be obtained, after the conclusion of the contract and in a <i>durable medium</i>. The <i>insurance intermediary</i> may provide this information before the contract is concluded, along with the information required by item 9, if it so chooses.</p>

### Disclosure by insurance intermediaries when introducing

- 4.2.9 R Where contact by the *insurance intermediary* with the *customer* is limited to *introducing the customer to another insurance intermediary (or to an insurer as product provider)*, the *customer* must be given the following information in good time before the introduction is made:
- (1) the information in *ICOB 4.2.8R(1) and (2)*;
  - (2) details of *fees*, if any, that the *customer* will be charged for the service being provided; and
  - (3) whether the *insurance intermediary introducing the customer* is a member of the same *group* as the *firm to whom the introduction is to be made*.

- 4.2.10 G As article 33 of the *Regulated Activities Order* makes clear, the activity of *introducing* falls within article 25(2) of the *Regulated Activities Order* (Arranging deals in investments). *ICOB 4.2.9R* applies in the limited circumstances where the arrangements made are confined to putting the *customer* in contact with another *person*. If the *insurance intermediary* goes further, for example by *advising the customer* on a particular *contract of insurance* which can be obtained from that *person*, *ICOB 4.2.2R* applies.

### Fair analysis

- 4.2.11 R An *insurance intermediary* cannot hold itself out as giving information or advice to customers on *non-investment insurance contracts* on the basis of a fair analysis of the market in accordance with *ICOB 4.2.8R(6)(a)* unless:
- (1) it has considered a sufficiently large number of *non-investment insurance contracts* available in the relevant sector or sectors of the market; and
  - (2) the consideration in (1) is based on criteria which reflect adequate knowledge of *non-investment insurance contracts* in the relevant sector or sectors of the market.

- 4.2.12 G (1) If an *insurance intermediary* holds itself out as giving information or advice to customers on certain types of *non-investment insurance contracts* on the basis of a fair analysis of the market (or any sector of that market), the selection of *insurance undertakings* the *insurance intermediary* considers for this purpose will need to be sufficiently large to enable the *insurance intermediary* to satisfy the requirement in *ICOB 4.2.11R*. One way in which this requirement may be satisfied is by the *insurance intermediary* using "panels" of *insurance undertakings* which are sufficient to enable the *insurance intermediary* to give advice or information on a fair analysis basis and which are reviewed on a regular basis. An *insurance intermediary* which provides a service based on a

fair analysis of the market (or from a sector of the market) should ensure that its analysis of the market and the available *non-investment insurance contracts* is kept adequately up-to-date. For example, an *insurance intermediary* would need to update its selection of *non-investment insurance contracts* if it became aware that a *non-investment insurance contract* had generally become available offering an improved product feature, or a better *premium*, when compared with the *non-investment insurance contracts* currently in the *insurance intermediary's* selection. The frequency with which the selection of contracts needs to be updated will depend on the extent to which new contracts are made available on the market.

- (2) Where a “panel” of *insurance undertakings* is used, the criteria the *insurance intermediary* uses to select the panel will be important in determining whether the panel is sufficient for the *insurance intermediary* to provide a service based on a fair analysis of the market. The selection should be based on the product features, *premiums* and services offered by *insurance undertakings* to *customers*, and not solely on the benefit that the *insurance undertakings* offer to the *insurance intermediary*.

4.2.13

- G (1) An *insurance intermediary* may provide *advice* or information on a different basis to the same *customer* for different types of *non-investment insurance contracts*. For example, an *insurance intermediary* may give *advice* or information on the basis of a fair analysis of the market in respect of motor insurance contracts, but give *advice* or information only on a single *insurance undertaking's* contract for home contents insurance. The disclosure at *ICOB 4.2.8R(6)* should be based on the service that the *insurance intermediary* is providing in relation to a particular *non-investment insurance contract* for that *customer*.
- (2) *IPRU(INS) 1.3R* (Restriction of business to insurance) in practice restricts the business which an *insurer* can carry on.

#### **Information to be provided to customers on request**

4.2.14

- R (1) **An *insurance intermediary* that provides a service under *ICOB 4.2.8R (6)(b)* or *(c)* must maintain, and keep up-to-date, for each type of *non-investment insurance contract* it deals with, a list of *insurance undertakings* it selects from or deals with.**
- (2) **An *insurance intermediary* must provide a copy of the list in (1) in a *durable medium* to a *customer* on request, in accordance with *ICOB 4.2.8R(7)*.**



**Retail customers and commercial customers: information on fees**

- 4.2.15 **R** An *insurance intermediary* must provide a *customer* with details of the amount of any *fees* (or where an actual *fee* cannot be given the basis for calculating any *fees*, enabling the *customer* to verify them) for an *insurance mediation activity* before the *customer* incurs liability to pay the *fee*, or before conclusion of the contract, whichever is earlier.
- 4.2.16 **G** *ICOB* 4.2.15R means that *fees* charged over the life of the contract by the *insurance intermediary*, including *fees* for mid-term adjustments, must be disclosed before the *non-investment insurance contract* is concluded.
- 4.2.17 **R** The information in *ICOB* 4.2.15R can be provided in any medium before the conclusion of the contract but must be provided in a *durable medium* immediately after the conclusion of the contract.
- 4.2.18 **G** (1) The *fees* referred to in *ICOB* 4.2.15R are *fees* for mediation services. *Fees* for *non-investment insurance contracts* are covered in *ICOB* 5.5.14R(3).
- (2) *Fees* do not include *premiums*, or *commissions* that are part of *premiums*.

**Overseas business for UK retail customers**

- 4.2.19 **R** (1) An *insurance intermediary* must not conduct *insurance mediation activities* in respect of *non-investment insurance contracts*:
- (a) from an office of its own (or of any *appointed representative*) outside the *United Kingdom*;
- (b) with or for a *retail customer* who is in the *United Kingdom*;
- unless it has, where relevant, made a disclosure in accordance with (2) to the *retail customer*.
- (2) The required disclosure in (1) means a written statement making it clear that in some or all respects the *regulatory system* applying, including any complaints handling or compensation arrangements, will be different from that of the *United Kingdom*. The statement may also indicate the protections or compensation available under another system of regulation.

**Application for renewals and amendments where information has already been provided**

- 4.2.20 R (1) ***ICOB 4.2 does not apply in relation to any insurance mediation activity that an insurance intermediary carries on with a customer in the course of renewing or amending a contract of insurance, if the information required by ICOB 4.2 has already been given to the customer in relation to the initial contract and is still accurate and up-to-date.***
- (2) ***If the information in relation to the initial contract that the insurance intermediary has previously disclosed to the customer in accordance with ICOB 4.2 has changed, the insurance intermediary must give the customer the updated information in accordance with the provisions of ICOB 4.2, but does not need to provide the other information required by ICOB 4.2.***
- 4.2.21 G ***An insurance intermediary will normally need to provide updated information within ICOB 4.2.20R(2) to the customer in a durable medium before the conclusion of the contract, unless an exemption in ICOB 4.2.2R(2) (oral disclosure) or ICOB 4.2.2R(3) (telephone sales) applies.***

**4.3 Suitability**

**Requirement for suitability**

- 4.3.1 R (1) ***An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal recommendation to a customer to buy or sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made.***
- (2) ***The personal recommendation in (1) must be based on the scope of the service disclosed in accordance with ICOB 4.2.8R(6).***
- (3) ***An insurance intermediary may make a personal recommendation of a non-investment insurance contract that does not meet all of the customer's demands and needs, provided that:***
- (a) ***there is no non-investment insurance contract within the insurance intermediary's scope, as determined by ICOB 4.2.8R(6), that meets all of the customer's demands and needs; and***

- (b) the *insurance intermediary* identifies to the *customer*, at the point at which the *personal recommendation* is made, the demands and needs that are not met by the contract that it *personally recommends*.

**Information about the customer's demands and needs**

- 4.3.2 R In assessing the *customer's* demands and needs, the *insurance intermediary* must:
- (1) seek such information about the *customer's* circumstances and objectives as might reasonably be expected to be relevant in enabling the *insurance intermediary* to identify the *customer's* requirements. This must include any facts that would affect the type of insurance recommended, such as any relevant existing insurance;
  - (2) have regard to any relevant details about the *customer* that are readily available and accessible to the *insurance intermediary*, for example, in respect of other *contracts of insurance* on which the *insurance intermediary* has provided *advice* or information; and
  - (3) explain to the *customer* his duty to disclose all circumstances material to the insurance and the consequences of any failure to make such a disclosure, both before the *non-investment insurance contract* commences and throughout the duration of the contract; and take account of the information that the *customer* discloses.
- 4.3.3 G In relation to *ICOB 4.3.2R(3)*, an *insurance intermediary* should make clear to the *customer* what the *customer* needs to disclose. For example, in relation to private medical insurance, this could include any existing medical condition where relevant, or in relation to motor insurance, any modifications carried out to the vehicle.
- 4.3.4 G An *insurance intermediary* should base his *personal recommendation* on what the *customer* tells him. Subject to *ICOB 4.3.2R(1)*, *ICOB 4.3.2R(2)* and *ICOB 4.3.5R*, the *insurance intermediary* is not required to take into account the *customer's* existing insurance cover, or details of that cover, if the *customer* is not able to provide this information.
- 4.3.5 R If the *insurance intermediary* is aware that the *customer's* existing insurance cover is likely to significantly affect the suitability of any *personal recommendation* that the *insurance intermediary* might make, the *insurance intermediary* must either:
- (1) not make a *personal recommendation* until details of the insurance cover are made available to him; or
  - (2) if it makes a *personal recommendation*, make clear to the *customer* that this may not be suitable because the *insurance intermediary* has not taken into account full details of the *customer's* existing insurance cover.

**Assessing the suitability of a contract against the customer's demands and needs**

- 4.3.6 R** In assessing whether a *non-investment insurance contract* is suitable to meet a *customer's* demands and needs, an *insurance intermediary* must take into account at least the following matters:
- (1)** whether the level of cover is sufficient for the risks that the *customer* wishes to insure;
  - (2)** the cost of the contract, where this is relevant to the *customer's* demands and needs; and
  - (3)** the relevance of any exclusions, excesses, limitations or conditions in the contract.
- 4.3.7 G** (1) Where *ICOB* 4.3.6R(2) applies, an *insurance intermediary* should take into account the cost of the contract when compared to other *non-investment insurance contracts* that cover a similar range of demands and needs on which the *insurance intermediary* can provide *advice* or information.
- (2) In meeting the requirements of *ICOB* 4.3.6R, an *insurance intermediary* need not consider the following:
- (a) alternatives to *non-investment insurance contracts*; and
  - (b) the needs of the *customer* that are not relevant to the type of contract in which the *customer* is interested.
- 4.4 Statement of demands and needs**
- 4.4.1 R** (1) Unless *ICOB* 4.4.2R applies, where an *insurance intermediary* arranges for a *customer* to enter into a *non-investment insurance contract* (including at *renewal*), it must, before the conclusion of that contract, provide the *customer* with a statement that:
- (a)** sets out the *customer's* demands and needs;
  - (b)** confirms whether or not the *insurance intermediary* has *personally recommended* that contract; and
  - (c)** where a *personal recommendation* has been made, explains the reasons for *personally recommending* that contract.
- (2) The statement in (1) must reflect the complexity of the *contract of insurance* proposed.
- (3) Unless (4) applies, the statement in (1) must be provided in a *durable medium*.

- (4) An *insurance intermediary* may provide the statement in (1) orally if:
- (a) the *customer* requests it; or
  - (b) the *customer* requires immediate cover;

but in both cases the *insurance intermediary* must provide the information in (1) immediately after the conclusion of the contract, in a *durable medium*.

#### Exemptions

#### 4.4.2 R (1) Commercial customers

- (a) *ICOB 4.4.1R(1)* does not apply to an *insurance intermediary* that is an *insurer* when dealing with a *commercial customer*, unless the *insurer* makes a *personal recommendation* to that *commercial customer*.
- (b) If an *insurance intermediary* that is an *insurer* makes a *personal recommendation* to a *commercial customer*, it need not provide the *commercial customer* with a statement of demands and needs, provided that:
  - (i) it has obtained the consent of the *commercial customer* not to receive the statement of demands and needs; and
  - (ii) it has explained to the *commercial customer* the consequences of giving that consent before it is given.

#### (2) Telephone sales

Where a contract is concluded by telephone with a *customer*, the statement of demands and needs:

- (a) must be provided immediately after the conclusion of the contract in a *durable medium*;
- (b) may also be provided orally before the contract is concluded.

#### 4.4.3

- G (1) An *insurance intermediary* may provide the demands and needs statement as part of another document, such as an application form.
- (2) For quick quotes (see *ICOB 4.2.1G(3)*), there is no requirement for the *insurance intermediary* to provide a demands and needs statement, but one must be provided before contract conclusion.
- (3) A statement of demands and needs is, by definition, relevant to (and generated by) the specific circumstances of the *customer*. However, the degree of knowledge of the *customer's* circumstances that is required will vary from case to case.

### **Demands and needs statement for non-advised sales**

4.4.4 G *ICOB 4.4.3G* gives an *insurance intermediary* flexibility as to the format of the demands and needs statement. Some examples of approaches that may be appropriate where the *insurance intermediary* has not made a *personal recommendation* include:

- (1) providing a demands and needs statement as part of an application form, so that the demands and needs statement is made dependent upon the *customer* providing personal information on the application form. For instance, the application form might include a statement along the lines of:

"If you answer "yes" to questions a, b and c your demands and needs are those of a pet owner who wishes and needs to ensure that the veterinary needs of your pet are met now and in the future";

- (2) producing a demands and needs statement in product documentation that will be appropriate for anyone wishing to buy the product. For example, "This product meets the demands and needs of those who wish to ensure that the veterinary needs of their pet are met now and in the future"; and
- (3) giving a *customer* a record of all his demands and needs that have been discussed.

### **Demands and needs statement when a personal recommendation is made**

- 4.4.5 G
- (1) Where a *personal recommendation* has been made the demands and needs statement will need to record the reasons for the *personal recommendation* as well as the *customer's* demands and needs.
  - (2) In accordance with *ICOB 4.4.7R*, the demands and needs statement is the record that the *insurance intermediary* must maintain to demonstrate that he has given a suitable *personal recommendation*. Accordingly, the statement will need to contain sufficient information to act as this record.
  - (3) *ICOB 4.4.6G* contains *guidance* on the content of the statement of demands and needs required by *ICOB 4.4.1R(1)*.

## 4.4.6

- G Table: Guidance on the content of the statement of demands and needs required by ICOB 4.4.1R(1)

This table belongs to *ICOB 4.4.5G(3)*.

	Introduction
(1)	Where relevant, the statement should explain simply and clearly why the <i>personal recommendation</i> is viewed as suitable, having regard to the <i>customer's</i> demands and needs.
	Style and Presentation
(2)	The style and presentation of the statement is left for the <i>insurance intermediary</i> to decide, so that he can design a statement which works best for the market in which he transacts business. A statement is more likely to be effective if it demonstrates these features:
	(a) simplicity and plain English: when technical terms need to be incorporated, they should be explained if the <i>customer</i> is unlikely to understand their meaning; and
	(b) concise and clear messages: lengthy explanations and extensive statements are likely to reduce the effectiveness of the statement, and make the <i>customer</i> less likely to read the statement properly.
(3)	An <i>insurance intermediary</i> should take the following into account when constructing a statement following a <i>personal recommendation</i> :
	(a) the statement should explain why the <i>customer's</i> demands and needs combine to make the recommended contract suitable for the <i>customer</i> . It should not merely state what contract is being recommended with no link to the <i>customer's</i> demands and needs; and
	(b) an <i>insurance intermediary</i> that offers contracts from more than one <i>insurance undertaking</i> should include a statement of why a particular <i>insurance undertaking</i> has been recommended; reasons may include contract features not available anywhere else, price, or service levels.

### Record keeping where a personal recommendation is made

- 4.4.7 R (1) **An *insurance intermediary* that makes a *personal recommendation* to a *customer* must, if the *customer* acts on the *personal recommendation* by concluding the *non-investment insurance contract* with that *insurance intermediary*:**

- (a) unless *ICOB 4.4.2R(1)(b)* applies, retain a copy of the statement required by *ICOB 4.4.1R(1)*; or
- (b) if *ICOB 4.4.2R(1)(b)* applies, make and retain, in a *durable medium*, a record of the reasons for the *personal recommendation*.

(2) Both the copy of the statement in (1)(a) and the record in (1)(b) must be retained for a minimum period of three years from the date on which the *personal recommendation* was made.

4.4.8 G The effect of *ICOB 4.4.7R(1)* is that if the *customer* does not act on the *personal recommendation*, the *insurance intermediary* need not retain a copy of the statement.

#### 4.5 Excessive charges to retail customers

4.5.1 R An *insurance intermediary* must ensure that its *charges to a retail customer* are not excessive.

4.5.2 G When determining whether a *charge* is excessive, an *insurance intermediary* should consider:

- (1) the amount of its *charges* for the services or product in question, compared with *charges* for similar services or products in the market;
- (2) whether the *charges* are an abuse of the trust that the *retail customer* has placed in the *insurance intermediary*; and
- (3) the nature and extent of the disclosure of the *charges* to the *retail customer*.

4.5.3 G In assessing whether an *insurance intermediary's* charges are excessive, the *FSA* will take account of the *charges* imposed by *insurance intermediaries* of similar size and that conduct a similar volume of business.

4.5.4 G *ICOB 4.5.1R* does not apply to *premiums*, but does cover *fees* (including any *fees* that an *insurance intermediary* charges where it receives no *commission* from an *insurer* in respect of the *contract of insurance*).

#### 4.6 Commission disclosure for commercial customers

4.6.1 R Before the conclusion of a *non-investment insurance contract*, or at any other time, an *insurance intermediary* that conducts *insurance mediation activities* for a *commercial customer* must, if that *commercial customer* asks, promptly disclose the *commission* that he and any *associate* of his receives in connection with the *non-investment insurance contract* in question, in cash terms, in a *durable medium*.

4.6.2 G *ICOB 4.6.1R* does not replace the general law on the fiduciary obligations of an agent. In relation to *contracts of insurance* the essence of these obligations is generally a duty on the agent to account to his *principal*. However, in certain circumstances, the duty is one only of disclosure. Where a *customer* employs an *insurance intermediary* by way of business and does not remunerate him, and



where it is usual for the *insurance intermediary* to be remunerated by way of *commission* paid by the *insurer* out of *premium* payable by the *customer*, then if the *customer* asks what the *insurance intermediary's* remuneration is, the *insurance intermediary* must tell him. *ICOB* 4.6.1R is additional to this requirement in that it applies whether or not the *insurance intermediary* is an agent of the *commercial customer*.

- 4.6.3 G *ICOB* 4.1.4R(3) states that *ICOB* 4.6 does not apply to an *insurance intermediary* that is an *insurer*. This means that there is no obligation on an *insurer* to disclose a *commission* equivalent to a *commercial customer* on request.
- 4.6.4 G The disclosures required by *ICOB* 4.6.1R should be made in a manner that is clear, fair and not misleading, as required by *ICOB* 2.2.3R (Clear, fair and not misleading communication).
- 4.6.5 G If the precise value of *commission* is not known in advance, the *insurance intermediary* should estimate the rate likely to apply in relation to the *contract of insurance* in question.
- 4.6.6 G *ICOB* 4.6.1R does not require the disclosure of *commission* throughout the distribution chain between the *insurer* and *commercial customer*; but it does require disclosure of *commission* paid to any *associate*, regardless of whether the *associate* is part of the distribution chain.
- 4.7 **Unsolicited services**
- 4.7.1 R **Unless *ICOB* 4.7.2R applies, an *insurance intermediary* or an *insurer* must not, in relation to a *non-investment insurance contract* that is a *distance contract*:**
- (1) ***advise on, arrange, enter into, renew, carry out or assist in the administration and performance of such a contract for a retail customer without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or***
  - (2) ***enforce any obligation against a retail customer in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.***
- 4.7.2 R ***ICOB* 4.7.1R does not prevent an *insurance intermediary* or an *insurer* from exercising any right that he may have, by contract or otherwise, to *renew a distance contract with a retail customer without any request made by or on behalf of that retail customer prior to the renewal of the contract.***
- 4.7.3 G (1) *ICOB* 4.7.1R(1) prohibits an *insurance intermediary* (or an *insurer* when acting as *product provider*) from *advising on, arranging, entering into, renewing, carrying out or assisting in the administration and performance of a non-investment insurance contract that is a distance contract for a retail customer without the prior consent of that retail customer*. This prohibition includes the continuation of insurance after a specified period where the insurance has been free of charge to the *retail customer* during that period unless the *retail customer* has agreed before the period expires to pay for the insurance once the period has expired.

- (2) Where the payment for the contract is made by regular instalments (for example, by direct debit), the effect of *ICOB 4.7.2R* is that an *insurance intermediary* (or an *insurer* when acting as *product provider*) will be required to seek the *retail customer's* consent on *renewal* to continue to provide insurance only if the contract does not give it the right to do so without further reference to the *retail customer*.
- (3) The prior consent of the *retail customer* can either be express, or deduced from the circumstances of the case (for instance, by the *retail customer* providing an updated direct debit mandate to the *firm*).

## **4.8 Language of the information provided to customers**

- 4.8.1 R All information provided to *customers* in accordance with this chapter must be in English, unless the *customer* requests it to be, and the *firm* agrees to it being, in another language.**

This Annex belongs to *ICOB 4.2.4G(1)*.

An *insurance intermediary* should omit the notes and square brackets in the following IDD. If the IDD contains the key facts logo and Section 1, the *insurance intermediary* must follow the headings and text in the order shown in accordance with *ICOB 4.2.5R* and the notes.

[Note 1]

## about our insurance services [Note 2]

**keyfacts**



Financial Services

[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

### 1 The Financial Services Authority (FSA)

The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

### 2 Whose products do we offer? [Note 6] [Note 7]

We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].

We [can] [Note 8] only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of insurers we offer insurance from. [Note 9]

We [can] [Note 8] only offer [a] product[s] from [a single insurer] [name of single

*insurance undertaking*] [for] [list the types of *non-investment insurance contracts*].  
[Note 10] [Note 11]

[or] [Note 12]

We only offer our own products for [list the types of *non-investment insurance contracts*].

---

### 3 Which service will we provide you with? [Note 13] [Note 14]

---

We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].

You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

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### 4 What will you have to pay us for our services?

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A fee [of £ [ ]]. [Note 15]

No fee.

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

---

### 5 Who regulates us? [Note 16]

---

[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 17] [Note 18] is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. [Note 19]

Our permitted business is [ ]. [Note 20]

[or] [Note 21]

[Name of *appointed representative*] [Notes 3 and 4] is an appointed representative of [name of authorised *firm*] [address of authorised *firm*] [Note 17] [Note 18] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ]. [Note 20]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

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### 6 Ownership [Note 22]

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[B&C Insurer owns 20% of our share capital.] [Note 23]

[XYZ Financial Services (or We) have 20% of the voting rights in Royal Edinburgh]. [Note 24]

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## **7 What to do if you have a complaint [Note 16]**

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234] [Note 25]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 26]

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## **8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 16] [Note 27]**

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.

[or] [Note 28]

For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.

Further information about compensation scheme arrangements is available from the FSCS.

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The following notes do not form part of the IDD.

**Note 1** – subject to this, an *insurance intermediary* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common key facts logo to be used on significant pieces of information directed to *customers*. *ICOB 4.2.6R* sets out requirements on the use of the key facts logo. A specimen of the key facts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *insurance intermediary's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** - if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the IDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *insurance intermediary* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* should not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – the *insurance intermediary* should select, for example by ticking, the box(es) which are appropriate for the service that it expects to provide to the *customer*.

**Note 7** – the *insurance intermediary* can select more than one box if the scope of the service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance. In the case where more than one box is selected, the *insurance intermediary* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the IDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 8** – insert “can” if the *insurance intermediary's* range of *non-investment insurance contracts* is determined by any contractual obligation. This does not apply where a *product provider* or *insurer* is selling its own products.

**Note 9** – this is the list required by *ICOB 4.2.14R*.

**Note 10** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the types of contract to which they relate on the IDD. This needs to be done only in relation to the service it is offering to a particular *customer*. For example, "we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance".

**Note 11** – if the *insurance intermediary* does not select this box, it should replace the words on the specimen form with the following: "We only offer products from a single insurer".

**Note 12** – if the *insurance intermediary* is an *insurer* offering only its own *non-investment insurance contracts*, or is part of an *insurer* offering only the *non-investment insurance contracts* sold under that part's trading name, it should use this alternative text.

### **Section 3: Which service will we provide you with?**

**Note 13** – this section may be omitted if the *insurance intermediary* intends to provide, or already has provided, the *customer* with this information as part of the demands and needs statement in accordance with *ICOB 4.4*. If this section is omitted, the other sections of the *IDD* should be renumbered accordingly.

**Note 14** – the *insurance intermediary* should select, for example by ticking, the box which is appropriate for the service that it expects to provide to the *customer*. Both boxes can be selected if the *insurance intermediary* offers different services in relation to different types of *non-investment insurance contracts* to a particular *customer*. In the case where more than one box is selected, the *IDD* should specify which box relates to which type of *non-investment insurance contract*.

### **Section 4: What will you have to pay us for our services?**

**Note 15** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, the *insurance intermediary* should insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* and *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'.

### **Section 5: Who regulates us?**

**Note 16** – a *firm* may omit this section if it provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. If this section is omitted the other sections of the *IDD* should be renumbered accordingly.

**Note 17** – if the *firm's* address on the *FSA Register* differs from that given on the *IDD* under note 5, the address on the *FSA Register* should be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 18** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it should include the name under which it is *authorised* and listed on the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 19** - an *incoming EEA firm* will need to modify this section if it chooses to use this *IDD* (see *GEN 4 Ann 1R(2)*).

**Note 20** – the *insurance intermediary* should insert a plain language description of the business for which it has *permission* which relates to the service it provides in relation to *non-investment insurance contracts*.

**Note 21** – where the information is provided by an *appointed representative*, the *appointed representative* should use this text instead. The *appointed representative* should give the



details of the *authorised firm* that is its *principal* for each type of *non-investment insurance contract* that it is offering to a particular *customer*.

## **Section 6: Ownership**

**Note 22** – the *insurance intermediary* should omit this section where there are no relevant ownership arrangements under the following notes or the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections should be renumbered accordingly.

**Note 23** – the *insurance intermediary* should insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

**Note 24** – the *insurance intermediary* should insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

## **Section 7: What to do if you have a complaint**

**Note 25** - if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 26** – this text may be omitted if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

## **Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 27** – when an *incoming EEA firm* provides the IDD, it should modify this section as appropriate.

**Note 28** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employer's liability insurance*, it should use this alternative text.

This Annex belongs to *ICOB 4.2.7R*.

This specimen covers services in relation to *packaged products, non-investment insurance contracts and regulated mortgage contracts* (including *regulated lifetime mortgage contracts* and home reversion schemes). If the *firm* is only providing services in relation to two types of these products, the parts of the CIDD that are not relevant must be omitted. *Firms* must omit the notes and square brackets that appear in the following CIDD. The CIDD must contain the key facts logo, headings and text in the order shown and in accordance with the notes. [Note 1]

## about our services [Note 2]



Financial Services

[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

### 1 The Financial Services Authority (FSA)

The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

### 2 Whose products do we offer? [Note 6] [Note 7]

#### Investment

- We offer products from the whole market.
- We [can] [Note 8] only offer products from a limited number of companies.

Ask us for a list of the companies and products we offer. [Note 12]

- We [can] **[Note 8]** only offer [a] [a limited range of the] product[s] from [a single group of companies] [name of single company]. **[Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own products.

Ask us for a list of the products we offer. **[Note 12]**

- We will advise you about group personal pensions.

### Insurance

- We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].

- We [can] **[Note 8]** only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. **[Note 12]**

- We [can] **[Note 8]** only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. **[Note 9] [Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own products for [list the types of *non-investment insurance contracts*].

### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We offer mortgages from the whole market.

- We [can] **[Note 8]** only offer mortgages from a limited number of lenders.

Ask us for a list of the lenders we offer mortgages from. **[Note 11]**

- We [can] **[Note 8]** only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender]. **[Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own mortgages.

---

## 3 Which service will we provide you with? **[Note 6]**

### Investment

- We will advise and make a recommendation for you after we have assessed your needs.

- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

### Insurance

- We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].
- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

### [Lifetime] Mortgages [and home reversion schemes] [Note 14]

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

---

## 4 What will you have to pay us for our services?

### Investment

- Before we provide you with advice, we will give you our key facts guide to the cost of our services. [Note 15]

### Insurance

- A fee [of £ [ ]]. [Note 16]
- No fee.

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

### [Lifetime] Mortgages [and home reversion schemes] [Note 14]

- No fee. [We will be paid by commission from the [lender/company].] [Note 17]
- A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] mortgage [or home reversion scheme]. [We will also be paid commission from the [lender/company].] [Note 17] [Note 18]

You will receive a key facts illustration when considering a particular [lifetime] mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. [Note 14]

### **Refund of fees [Note 19] [Note 14]**

If we charge you a fee, and your [lifetime] mortgage [or home reversion scheme] does not go ahead, you will receive:

#### **[Note 20]**

- A full refund [if the [lender/company] rejects your application]. [Note 21]
- A refund of £ [ ] [if your application falls through]. [Note 21] [Note 22]
- No refund [if you decide not to proceed]. [Note 21]

---

### **5 Who regulates us? [Note 23]**

[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 24] [Note 25] is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. [Note 26]

Our permitted business is [ ]. [Note 27]

[or] [Note 28]

[Name of *appointed representative*] [Notes 3 and 4] is an appointed representative of [name of *firm*] [address of *firm*] [Note 24] [Note 25] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] [Note 27]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

[Home reversion schemes are not regulated by the FSA.] [Note 14]

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### **6 Loans and ownership [Note 29]**

[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.] [Note 29][Note 31][Note 32][Note 33][Note 34]

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## 7 What to do if you have a complaint [Note 23]

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234]. [Note 35]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 36] [Note 37] [The Financial Ombudsman Service does not consider complaints about home reversion schemes.] [Note 14]

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## 8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 23] [Note 38]

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

### Investment

Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.

### Insurance

Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.

[or] [Note 39]

For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.

### [Lifetime] Mortgages [and home reversion schemes] [Note 14]

Mortgage advising and arranging is covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000. [Home reversion schemes are not covered by the Financial Services Compensation Scheme.] [Note 14]

Further information about compensation scheme arrangements is available from the FSCS.

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## 9 Group personal pensions [Notes 40, 41 and 42]

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This meeting has been arranged so that we can provide you with [information about] [advice upon whether or not you should join] the Group Personal Pension scheme which your employer has established. You should be aware that we cannot advise upon or recommend any other specific investment products during this meeting.

---

**[Note 43] Message from the Financial Services Authority**

**Think carefully about this information before deciding whether you want to go ahead.  
If you are at all unsure about which lifetime mortgage or home reversion scheme is right for  
you, you should ask your adviser to make a recommendation.**

**Please remember that home reversion schemes are not regulated by the FSA.**

The following notes do not form part of the CIDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common key facts logo to be used on significant pieces of information directed to *customers*. *ICOB 4.2.6R* sets out the requirements on the use of the key facts logo. A specimen of the key facts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the CIDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – for services in relation to *packaged products* and *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes the *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. For services in relation to *non-investment insurance contracts*, the *firm* must select more than one box if the scope of the service or the type of service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance or if it provides *advice* on some types of contract but not others. In the case where more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the CIDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 7** - if the CIDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with *COB 5*, *ICOB 4.2.8R* note 1(e) and *MCOB 4.3.10R*.

**Note 8** – insert “can” if the *firm's* range of products is determined by any contractual obligation. This does not apply where a *product provider*, *insurer*, lender or company is selling its own products.

**Note 9** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the CIDD. This only needs to be done in relation to the service it is offering a particular *customer*. For example, “we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance”.

**Note 10** – if the *firm* selects this box, it will be offering the products of one provider to the *customer* for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In



the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*. If the *firm* does not select this box, then the text must follow that set out in note 13 below.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the lender for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the company for home reversion schemes. For example: "We can only offer products from [name of *product provider*]". For *non-investment insurance contracts* the type of insurance offered should also be included. For example: "We only offer XYZ's household insurance and ABC's motor insurance." If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a mortgage from [name of lender]". If the *firm* does not offer all of the *packaged products* or mortgages or home reversion schemes generally available from that provider, it must insert the words "a limited range of" as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part's trading name, it should use this alternative text.

**Note 11** – for services provided in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes, this sentence may be omitted if the *firm* chooses to list all of the companies it offers products from instead of the text "a limited number of lenders" in the previous line, so long as the *firm* offers all the products generally available from each provider.

**Note 12** – for services provided in relation to *packaged products* the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOB 4.2.14R*.

**Note 13** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies" for *packaged products*, "a single insurer" for *non-investment insurance contracts*, "a single lender" for *regulated mortgage contracts* or *regulated lifetime mortgage contracts* and "a single company" for home reversion schemes. For example: "We only offer the products from a single group of companies" should replace the text in the specimen CIDD.

**Note 14** – change "mortgage" to "lifetime mortgage" where the *firm* sells only *regulated lifetime mortgage contracts*. *Firms* must insert the text relating to home reversion schemes and change "mortgage" to "product", and "lender" to "company", if they advise or give personalised information on home reversion schemes in addition to *advising* or giving personalised information on *regulated lifetime mortgage contracts*.

#### **Section 4: What will you have to pay us for our services?**

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate "key facts guide to the costs of services" (i.e. a menu) if they propose to give that *customer advice* on *packaged products*. Where a *firm* is not required to provide that *customer* with a menu

because the *firm* does not give *advice* on *packaged products*, the *firm* may omit the part of section 4 of the CIDD that relates to *packaged products*.

**Note 16** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* or *arranging* a *non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'.

**Note 17** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer* for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes, it must insert a plain language explanation of this (see specimen for a plain language example).

**Note 18** – insert a plain language description of when any *fees* are payable for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If a *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

**Note 19** – omit this part of the CIDD on 'Refund of fees' if the *firm* has indicated that there will be "No fee" for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes.

**Note 20** – *firms* may select as many boxes as appropriate.

**Note 21** – insert a plain language description of the circumstances in which the *fee* for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes is refundable or not refundable as described.

**Note 22** – a *firm* may delete this line if it does not offer a partial refund for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes in any circumstances.

### **Section 5: Who regulates us?**

**Note 23** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information, including the *firm's permitted business*. This section may be omitted for services relating to *non-investment insurance contracts* if the *firm* provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. This section may be omitted for services relating to *regulated mortgage contracts* (including *regulated lifetime mortgage contracts*) and home reversion schemes in accordance with *MCOB 4.4.1R(3)*. If this section is omitted, the other sections of the CIDD must be renumbered accordingly.

**Note 24** – if the *firm's* address on the *FSA Register* differs from that given on the CIDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 25** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 26** - an *incoming EEA firm* will need to modify this section if it chooses to use this CIDD (see *GEN 4 Ann 1R(2)*).

**Note 27** – insert a plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 28** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

## **Section 6: Loans and ownership**

**Note 29** – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the CIDD must be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section must be changed to 'Ownership'.

**Notes 30, 31 and 32** apply only to a *firm advising on, dealing in, or arranging* in relation to *packaged products* for *private customers*.

**Note 30** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 31** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 32** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

**Notes 33 and 34** apply to an *insurance intermediary* that is not an *insurer* providing services in relation to *non-investment insurance contracts*.

**Note 33** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

**Note 34** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

### **Section 7: What to do if you have a complaint**

**Note 35** – if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 36** – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

**Note 37** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

### **Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 38** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 39** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it must use this alternative text.

### **Section 9: Group personal pensions**

**Note 40** – *firms* should only include section 9 if they intend to give information about, or *advise on*, the opportunity for *employees* to join a *group personal pension scheme* established by their employer. In all other cases it should be omitted entirely.

**Note 41** – the words in square brackets should be omitted or included, as appropriate, depending upon whether the *firm* is *advising employees* whether or not to join a *group personal pension scheme*, or merely providing them with factual information about the scheme.

**Note 42** – although *firms* must not use the occasion of a meeting to discuss a *group personal pension scheme* as an opportunity to give *advice on other designated investments*, this does not preclude the provision of *advice on non-investment insurance contracts, regulated mortgage contracts or regulated lifetime mortgage contracts*. A *firm* may also, when giving *advice on a group personal pension scheme*, suggest that a further meeting be arranged to discuss *designated investments* and if so must provide a further appropriate IDD or CIDD.

### **Lifetime mortgage warning**

**Note 43** - This warning box should be added when the *firm* sells *regulated lifetime mortgage contracts* or home reversion schemes or both.

# ICOB 5

## Product disclosure

### 5.1 Application and purpose

#### Application: who and what?

#### 5.1.1 R This chapter applies to:

- (1) an *insurer*;
- (2) an *insurance intermediary* other than when *introducing*;
- (3) a *managing agent*.

#### 5.1.2 R Throughout this chapter references to an *insurer* apply equally to a *managing agent*.

5.1.3 G The definition of *insurance intermediary* includes an *insurer* when the *insurer* is carrying on *insurance mediation activities*, for example when, through its sales force, it *advises on* or *arranges* its own *non-investment insurance contracts* or those of another *insurer*.

5.1.4 G This chapter applies to the sale, *renewal* and certain changes to a *non-investment insurance contract* with a *retail customer* or a *commercial customer*.

5.1.5 G *ICOB 5.1.6G* shows the provisions in this chapter which apply when a *firm* deals with a *retail customer* and those which apply when a *firm* deals with a *commercial customer*.

5.1.6 G Table: Application of *ICOB 5* by customer type

This table belongs to *ICOB 5.1.5G*.

Retail customer	Commercial customer
The whole chapter except <i>ICOB 5.4</i>	The whole chapter except <i>ICOB 5.3</i>

5.1.7 G *ICOB 5.5.18R* to *ICOB 5.5.19R* (relating to directive-required information) qualify the general provisions on territorial scope set out in *ICOB 1.3*.

5.1.8 R If information required by this chapter to be provided to a *customer* duplicates information required in *ICOB 4* (Advising and selling standards), that information does not need to be provided twice unless required by a specific *rule*. However, the *policy summary* must always contain the information set out in *ICOB 5.5.5R* except as specified in *ICOB 5.4.8R(1)* and

## **ICOB 5.5.1R.**

### **Purpose**

- 5.1.9 G (1) This chapter reinforces *Principle 7* (Communications with clients), which requires a *firm* to pay due regard to the needs of its *clients* and communicate information to them in a way that is clear, fair and not misleading.
- (2) The purpose of this chapter is to ensure that *customers* have the necessary information to make an informed choice about whether or not to *buy* a specific *non-investment insurance contract* and whether a contract continues to meet their needs.
- 5.1.10 G This chapter also implements relevant requirements of the *Distance Marketing Directive*, the *Consolidated Life Directive* and *Third Non-Life Directive*.

## **5.2 Information - responsibilities of insurers and intermediaries**

- 5.2.1 G This section covers the responsibility for content, production and provision to the *customer* of information. It provides first for the typical situation in which both *insurer* and *insurance intermediary* are *UK*-based, and also provides for cross-border situations and those in which *insurance undertakings* or intermediaries are not *firms* or where the sale involves a *connected contract*.

### **If both the insurer and the insurance intermediary are UK-based**

- 5.2.2 R **If an *insurer* and an *insurance intermediary* (other than an *authorised professional firm* carrying on *non-mainstream regulated activities* or a *firm* selling *connected contracts*) each operates from an establishment maintained by it in the *United Kingdom*, the *insurer* is responsible for the content and production of the information referred to at **ICOB 5.2.9R** and the *insurance intermediary* is responsible for providing that information to the *customer*.**

### **If either the insurance undertaking or the insurance intermediary is not UK-based, not authorised, an authorised professional firm or a firm selling connected contracts**

- 5.2.3 R (1) **If an *insurance intermediary* operates from an establishment maintained by it in the *United Kingdom*, but an *insurance undertaking* does not, the *insurance intermediary* is responsible for the content and production of the information in **ICOB 5.2.9R** as well as for providing it to the *customer*.**
- (2) **If an *insurer* operates from an establishment maintained by it in the *United Kingdom* but the intermediary does not, is not *authorised*, is a *firm* selling *connected contracts*, or is an *authorised professional firm* carrying on *non-mainstream regulated activities*, the *insurer* is responsible for the provision of the information in **ICOB 5.2.9R** to the *customer*, subject to **ICOB 5.2.5R**, as well as for the content and production of it.**

- 5.2.4 G **ICOB 5.2.3R(2)** makes the *insurer* responsible for the content, production and

provision of information to *customers* dealing through:

- (1) intermediaries in the *United Kingdom* who do not have *Part IV permission* (for example, travel agents selling *connected contracts*, *exempt professional firms* and intermediaries who do not have an establishment in the *United Kingdom*); or
- (2) *firms* selling *connected contracts*; or
- (3) *authorised professional firms* carrying on *non-mainstream regulated activities*.

#### Exceptions where insurers deal with certain other intermediaries

- 5.2.5 R (1) If an *insurer* deals with an intermediary who operates from an establishment in the *United Kingdom* but does not need to be *authorised*, who is a *firm* selling *connected contracts*, or who is an *authorised professional firm* carrying on *non-mainstream regulated activities*, despite *ICOB 5.2.3R(2)* the *insurer* need not produce or provide:
- (a) a *policy summary*; and
  - (b) in respect of a *distance sale*, the directive-required information at *ICOB 5.5.20R(16)* to (21).
- (2) If the *insurer* deals with an intermediary who does not operate from an establishment maintained by the intermediary in the *United Kingdom*, despite *ICOB 5.2.3R(2)* the *insurer* need not produce or provide a *policy summary*.
- 5.2.6 R If *ICOB 5.2.3R* requires an *insurer* to provide information to the *customer*, the rules at *ICOB 5.3* and *ICOB 5.4*, where they refer to an *insurance intermediary*, must be read as applying to an *insurer*.

#### Insurers not operating from establishments in the United Kingdom

- 5.2.7 R Where an *insurer* is not operating from an establishment maintained by it in the *United Kingdom*, and there is no *insurance intermediary* which operates from an establishment maintained by it in the *United Kingdom*, the *insurer* need produce and provide only the directive-required information at *ICOB 5.5.20R(1)* to (15) when *ICOB 1.3.4R* or *ICOB 1.3.5R* applies.
- 5.2.8 G If an *insurer* does not operate from an establishment in the *United Kingdom* and deals with an *insurance intermediary* which does not have an establishment in the *United Kingdom*, and *ICOB 1.3.4R* or *ICOB 1.3.5R* applies, the *insurer* is responsible for the content and must produce and provide the information required by those *rules*.

#### Information to be provided to customers

- 5.2.9 R The information which is required is:

- (1) a *policy summary* (ICOB 5.5.1R to ICOB 5.5.13G);
- (2) directive-required information (ICOB 5.5.16R to ICOB 5.5.26G);
- (3) a *policy document* (ICOB 5.5.27R to ICOB 5.5.28G);
- (4) information about the *claims handling process* (ICOB 5.3.9R to ICOB 5.3.11G);
- (5) information, where relevant, about cancellation rights (ICOB 5.3.12R to ICOB 5.3.14G); and
- (6) for any applicable compensation scheme mentioned in the *policy summary* in accordance with ICOB 5.5.1R, the extent and level of cover and how further information can be obtained, if not already included in the *policy summary* in accordance with ICOB 5.5.1R(2)(b).

5.2.10 G The directive-required information referred to in ICOB 5.2.9R(2) does not need to be in a separate document. It may be incorporated into another document such as the *policy document* or included in a document of which the *policy summary* is a part.

5.2.11 R If an *insurer* agrees with an *insurance intermediary* that it will take on any part of the *insurance intermediary's* responsibilities required by this chapter, then the relevant *rule* will apply to the *insurer* as if it were the *insurance intermediary*.

5.2.12 R If an *insurance intermediary* is required by this chapter to provide information to a *customer* in relation to a *non-investment insurance contract*, the *insurer* must produce that information in good time to enable the *insurance intermediary* to comply with the *rules* in this chapter, or must produce it promptly in response to a request by the *insurance intermediary*.

#### Provision of information to customers "in good time"

5.2.13 G Some of the *rules* in this chapter require information to be provided to *retail customers* "in good time" before the conclusion of a contract and to *commercial customers* "in good time" before expiry of an existing contract. In determining what is "in good time" an *insurance intermediary* should consider the importance of the information to the *customer* in helping him to decide whether a contract meets his needs and the point in the sales process or *renewal* process at which the information may be most useful.

5.2.14 G If the *rules* in this chapter require a *policy document* to be given to a *customer* before conclusion of the contract, this must be the *policy document* and not a specimen. If an *insurance intermediary* provides a copy of the *policy terms* to a *customer* for information before conclusion of the contract, in circumstances where the *rules* in this chapter do not require it, a specimen of the terms can be given to the *customer*.

### 5.3 Provision of information to retail customers



**Before the conclusion of a contract which is not a distance contract**

- 5.3.1 R If a *non-investment insurance contract* is not a *distance contract*, an *insurance intermediary* must, in good time before the conclusion of the contract:
- (1) provide a *retail customer* with the following information in a *durable medium*:
    - (a) a *policy summary* (ICOB 5.5.1R to ICOB 5.5.13G);
    - (b) a statement of price (ICOB 5.5.14R to ICOB 5.5.15G);
    - (c) the relevant directive-required information set out in ICOB 5.5.20R (subject to ICOB 5.5.17G to ICOB 5.5.19R); and
  - (2) draw the attention of the *retail customer* orally to the importance of reading the *policy summary*, and in particular the section of the *policy summary* on significant and unusual exclusions or limitations.

**On conclusion of a contract which is not a distance contract**

- 5.3.2 G Where the *retail customer* does not have the opportunity to read the information provided in accordance with ICOB 5.3.1R(1) before conclusion of the contract, for example, because it is provided in a sealed pack, the *insurance intermediary* should provide a specimen copy of all the information in such a way that the *retail customer* is able to read it before conclusion of the contract. For example, a stand with sealed packs could be accompanied by a copy of the *policy summary* and other required information, with a notice that they contain important information the *retail customer* should read before *buying* the *policy*. Oral disclosure at the point of sale must still be given in accordance with ICOB 5.3.1R(2).
- 5.3.3 G *Guidance* on what constitutes a significant or unusual exclusion or limitation is set out in ICOB 5.5.8G to ICOB 5.5.10G.
- 5.3.4 R When a *non-investment insurance contract* which is not a *distance contract* is concluded, an *insurance intermediary* must provide a *retail customer* in a *durable medium*, immediately after conclusion of the contract, with:
- (1) a *policy document* (ICOB 5.5.27R to ICOB 5.5.28G);
  - (2) information about the *claims handling* process (ICOB 5.3.9R to ICOB 5.3.11G);
  - (3) information, where relevant, about cancellation rights (ICOB 5.3.12R to ICOB 5.3.14G);
  - (4) for any applicable compensation scheme mentioned in the *policy summary* in accordance with ICOB 5.5.1R, the extent and level of cover and how further information can be obtained, if not already included in the *policy summary* in accordance with ICOB 5.5.1R(2)(b).

- 5.3.5 G *ICOB 5.3.4R* does not prevent an *insurance intermediary* providing the information in *ICOB 5.3.4R(1)* to (4) before the conclusion of the *non-investment insurance contract*.

**Before the conclusion of a distance contract**

- 5.3.6 R (1) If a *non-investment insurance contract* is a *distance contract*, an *insurance intermediary* must provide a *retail customer*, in good time before the conclusion of the contract, with the following information in a *durable medium*, unless an exemption in (2) applies:

- (a) a *policy summary* (*ICOB 5.5.1R* to *ICOB 5.5.13G*);
- (b) a statement of price (*ICOB 5.5.14R* to *ICOB 5.5.15G*);
- (c) the relevant directive-required information set out in *ICOB 5.5.20R* (subject to *ICOB 5.5.17G* to *ICOB 5.5.19R*);
- (d) the *policy document* (*ICOB 5.5.27R* to *ICOB 5.5.28G*);
- (e) information about the *claims handling* process (*ICOB 5.3.9R* to *ICOB 5.3.11G*); and
- (f) information, where applicable, about cancellation rights (*ICOB 5.3.12R* to *ICOB 5.3.14G*).

- (2) The following exemptions from (1) apply:

- (a) Telephone sales

If a *non-investment insurance contract* is concluded by telephone and the *retail customer* gives explicit consent to receiving only the limited information specified in (i) to (ix) below, an *insurance intermediary* must give this information to the *retail customer* orally before the conclusion of the contract:

- (i) Name of the *insurance undertaking*;
- (ii) type of insurance and cover;
- (iii) significant features and benefits;
- (iv) significant and unusual exclusions or limitations;
- (v) the total price to be paid by the *retail customer* for the *non-investment insurance contract* (or, if an exact price cannot be indicated, the basis for calculation of the price enabling the *retail customer* to verify it);
- (vi) notice of the possibility that other taxes or costs may exist in respect of the *non-investment insurance contract* that are not

payable via the *insurance intermediary* or imposed by him;

- (vii) the existence or absence of the right of cancellation and, where applicable, the duration of the cancellation period and the conditions for exercising the right to cancel, including information on the amount which the *retail customer* may be required to pay;
- (viii) a telephone number or address to which a *claim* may be notified; and
- (ix) that other information is available on request and the nature of that information.

**(b) Certain other means of distance communication**

If the *non-investment insurance contract* is concluded at the *retail customer's* request using a *means of distance communication* (other than by telephone) which does not enable provision of the information referred to in *ICOB 5.3.6R(1)* in a *durable medium* before the conclusion of the contract, the *insurance intermediary* must provide the following information by other means before the conclusion of the contract:

- (i) Name of the *insurance undertaking*;
- (ii) type of insurance and cover;
- (iii) significant features and benefits;
- (iv) significant and unusual exclusions or limitations;
- (v) the total price to be paid by the *retail customer* for the *non-investment insurance contract* (or, if an exact price cannot be indicated, the basis for calculation of the price enabling the *retail customer* to verify it);
- (vi) notice of the possibility that other taxes or costs may exist in respect of the *non-investment insurance contract* that are not payable via the *insurance intermediary* or imposed by him;
- (vii) the existence or absence of the right of cancellation and, where applicable, the duration of the cancellation period and the conditions for exercising the right to cancel, including information on the amount which the *retail customer* may be required to pay; and
- (viii) a telephone number or address to which a *claim* may be notified.

5.3.7 G If the *retail customer* does not give explicit consent to receiving only limited information before conclusion of the contract in accordance with *ICOB*

5.3.6R(2)(a), the exemption at *ICOB* 5.3.6R(2)(a) does not apply and the information in *ICOB* 5.3.6R(1) must be provided to the *retail customer* in a *durable medium* before conclusion of the contract.

**On conclusion of a contract which is a distance contract**

- 5.3.8 R When a *non-investment insurance contract* which is a *distance contract* is concluded in accordance with *ICOB* 5.3.6R(2)(a) or (b), an *insurance intermediary* must provide a *retail customer* with the information in *ICOB* 5.3.6R(1) in a *durable medium* immediately after conclusion of the contract.

**Information about the claims handling process**

- 5.3.9 R The information about the *claims handling* process that the *insurance intermediary* must provide to the *retail customer* in accordance with *ICOB* 5.3.4R(2) and *ICOB* 5.3.6R(1)(e) is:

- (1) the address, telephone number or other point of initial contact for notifying a *claim*; and
- (2) the information the *retail customer* must provide to the *insurance undertaking* when notifying a *claim*.

- 5.3.10 R The information in *ICOB* 5.3.9R(1) and (2) must be provided in the same document.

- 5.3.11 G The information in *ICOB* 5.3.9R may be incorporated into another document or provided as a stand-alone document.

**Information about cancellation**

- 5.3.12 R The information about cancellation that the *insurance intermediary* must provide to the *retail customer* in accordance with *ICOB* 5.3.4R(3) or *ICOB* 5.3.6R(1)(f) is:

- (1) the existence or absence of a right to cancel in accordance with *ICOB* 6.2.1R; and
- (2) where a right to cancel exists:
  - (a) the duration of the cancellation period, in accordance with *ICOB* 6.2.2R;
  - (b) the conditions for exercising the right to cancel, including information on the amount which the *retail customer* may be required to pay;
  - (c) the consequences of not exercising the right to cancel; and
  - (d) how the right to cancel may be exercised, including the address to which the notification of cancellation should be sent.

- 5.3.13 G The information in *ICOB 5.3.12R* should be sufficiently clear, prominent and informative to enable the *retail customer* to understand the right to cancel.
- 5.3.14 G Where the notice of the right to cancel forms part of another document, or is one of a number of documents provided to the *retail customer* at the same time, the *insurance intermediary* should ensure that the presence of the notice of the right to cancel is drawn to the *retail customer's* attention.

### **Renewal**

- 5.3.15 R **If a *non-investment insurance contract* with a *retail customer*, with a duration of no more than one year, is due for *renewal*, *ICOB 5.3.16R* to *ICOB 5.3.23G* apply in place of *ICOB 5.3.1R* to *ICOB 5.3.8R*.**
- 5.3.16 R **If a *non-investment insurance contract* is of no more than one *month's* duration and its terms provide for automatic *renewal* and for cancellation at the *retail customer's* option, *ICOB 5.3.1R* to *ICOB 5.3.8R* and *ICOB 5.3.18R* to *ICOB 5.3.23G* do not apply, except that *ICOB 5.3.12R* to *ICOB 5.3.14G* apply if cancellation rights exist under *ICOB 6*, but if any changes are made to the terms or conditions of the *policy*, *ICOB 5.3.21R* applies.**
- 5.3.17 G An example of a *non-investment insurance contract* referred to at *ICOB 5.3.16R* is a health cash plan with a monthly *renewal* cycle.
- 5.3.18 R **An *insurance intermediary* must:**
- (1) **if the *insurance undertaking* is willing to invite *renewal* of the *policy*, provide the *retail customer* with *renewal* terms in a *durable medium* in accordance with *ICOB 5.3.21R* no less than 21 days before the expiry of the *policy*; or**
  - (2) **notify the *retail customer* no less than 21 days before the expiry of the *policy* if the *insurance undertaking* is not willing to invite *renewal* or that the *insurance intermediary* no longer deals with the *insurance undertaking*.**
- 5.3.19 G *ICOB 5.3.18R(2)* includes circumstances where the *insurance undertaking* is not willing to invite *renewal* through the *insurance intermediary* in contact with the *retail customer*.
- 5.3.20 G *ICOB 5.3.15R* has the effect that a *renewal* of a *non-investment insurance contract* of more than one year's duration must be treated as a new sale, in order to comply with the *DMD*. A *renewal* of a *non-investment insurance contract* which has been extended in accordance with *ICOB 5.3.22R(4)*, so that it is longer than one year, must also be treated as a new sale. For these contracts an *insurance intermediary* should provide information in accordance with the *rules* in *ICOB 5.3.1R* to *ICOB 5.3.8R* and not *ICOB 5.3.15R*.
- 5.3.21 R **The information to be provided to the *retail customer* in accordance with *ICOB 5.3.16R* or *ICOB 5.3.18R(1)* is:**

- (1) a statement of any changes to the terms of the *policy*;
- (2) an explanation of those changes, where necessary;
- (3) any changes to the directive-required information in *ICOB 5.5.20R* (subject to *ICOB 5.5.17G* to *ICOB 5.5.19R*);
- (4) the statement of price at *ICOB 5.5.14R*;
- (5) information about cancellation (*ICOB 5.3.12R* to *ICOB 5.3.14G*); and
- (6) a prominent statement of the *retail customer's* right to request a new *policy document*.

5.3.22 R *ICOB 5.3.18R* and *ICOB 5.3.21R* do not apply where:

- (1) the *insurance intermediary* has reason to believe that the *retail customer* does not wish to *renew* the *policy* through it;
- (2) the *insurance intermediary* has notified the *retail customer* that it does not wish to act for him on *renewal*;
- (3) the *retail customer* has already been notified that the *insurance undertaking* will not invite *renewal*; or
- (4) the *retail customer* requests an extension to the *non-investment insurance contract* for a period less than that of the original *non-investment insurance contract*.

- 5.3.23 G (1) Examples of situations where the *insurance intermediary* would have reason to believe that the *retail customer* does not intend to *renew* are travel insurance for a single trip, mortgage payment protection insurance where the mortgage has been repaid, or creditor insurance tied to the term of a loan.
- (2) An *insurance intermediary* who contacts a *retail customer* at least 21 *days* before expiry of the *policy* to check whether the *retail customer* wishes to *renew*, can rely on an oral statement by the *retail customer* that he does not wish to *renew* or on the *retail customer's* failure to respond to a request in a *durable medium* to contact the *insurance intermediary* by a specified date if he wishes to *renew*.

#### Mid-term changes

5.3.24 R For the duration of a *non-investment insurance contract* an *insurance intermediary* must notify a *retail customer* of:

- (1) changes to the *premium*, unless the change conforms to a previously disclosed formula;
- (2) changes to any term or condition of the contract, together with an explanation of any implications of the change where necessary; and

- (3) changes to the directive-required information in *ICOB 5.5.20R(22)*, for a *non-investment insurance contract* that is a *pure protection contract* (subject to *ICOB 5.5.19R*).
- 5.3.25 R (1) If an *insurance undertaking* changes the *premium* or any term or condition of a *non-investment insurance contract* the *insurance intermediary* must provide the *retail customer* with the information referred to in *ICOB 5.3.24R*, in a *durable medium*, in good time before the change takes effect, unless (2) applies.
- (2) If the change referred to in (1) is at the request of the *retail customer*, and it is impracticable to provide the information in *ICOB 5.3.24R* in a *durable medium* before the change takes effect, the *insurance intermediary* must:
- (a) explain the implications of the change to the *retail customer* before the change takes effect; and
- (b) provide the *retail customer* with the information referred to in *ICOB 5.3.24R* promptly after the change takes effect, in a *durable medium*.
- 5.3.26 G *ICOB 5.3.24R(1)* means that an *insurance intermediary* does not need to notify a *retail customer* of a change to a *premium* which has previously been disclosed to the *retail customer*, such as a periodic percentage increase, or if the *premium* for creditor insurance adjusts according to a previously disclosed formula, depending on the level of the debt. However, if, for example, the *insurance undertaking* alters the formula for calculating the changes to the *premium*, this would need to be notified to the *retail customer* by the *insurance intermediary*.
- 5.3.27 G When explaining the implications of a change in accordance with *ICOB 5.3.24R(2)* or *ICOB 5.3.25R(2)(a)* to a *retail customer*, an *insurance intermediary* should explain any changes to the benefits and significant and unusual exclusions arising from the change.
- 5.3.28 G *Insurers* and *insurance intermediaries* will need to consider whether mid-term changes are compatible with the original *non-investment insurance contract*, in particular whether that *non-investment insurance contract* included terms reserving the right to vary *premiums*, charges or contract terms and conditions. *Insurers* and *insurance intermediaries* also need to ensure that any contract terms which reserve the right to make variations are not themselves unfair under the *Unfair Terms Regulations*. The *FSA* may, as a qualifying body under the *Unfair Terms Regulations*, issue from time to time case summaries or *guidance* of potential relevance to such variation terms (see *ENF 20*).

## 5.4 Provision of information to commercial customers

### Before the conclusion of the contract

- 5.4.1 R Before the conclusion of a *non-investment insurance contract*, an *insurance*

*intermediary* must provide a *commercial customer* with:

- (1) sufficient information to enable the *commercial customer* to make an informed decision about the contract being proposed;
- (2) the directive-required information in *ICOB 5.5.20R(1) to (3)* or *ICOB 5.5.20R(4) to (15)* in writing (subject to *ICOB 5.5.17G to ICOB 5.5.19R*), unless the contract is being concluded by telephone; and
- (3) the *premium* and any *fees* relating to the *non-investment insurance contract*.

5.4.2 G Where a *non-investment insurance contract* with a *commercial customer* is concluded by telephone, *ICOB 5.4.1R(2)* does not apply. The *insurance intermediary* must comply with *ICOB 5.4.1R(1)* and (3) before conclusion of the contract and provide the information in *ICOB 5.4.1R(2)* immediately after conclusion of the contract in accordance with *ICOB 5.4.4R*.

- 5.4.3 G (1) The information in *ICOB 5.4.1R(1)* that an *insurance intermediary* provides may vary according to the *commercial customer's* knowledge, experience and ability.
- (2) In deciding what information is sufficient, the *insurance intermediary* should take account of the main benefits, exclusions, limitations and conditions of a *policy*.

#### **On conclusion of the contract**

5.4.4 R If the information referred to in *ICOB 5.4.1R(2)* and (3) was not provided in writing before the *non-investment insurance contract* was concluded, it must be provided in writing immediately afterwards.

5.4.5 R An *insurance intermediary* must provide a *commercial customer* with a *policy document* promptly after the conclusion of the *non-investment insurance contract*.

- 5.4.6 G (1) In considering how to comply with the requirement to be prompt in *ICOB 5.4.5R*, the *insurance intermediary* should take account of the complexity of the contract and the needs and expectations of the *commercial customer*.
- (2) Where insurance cover commences before the full terms and conditions have been agreed, the *policy document* should be provided to the *commercial customer* promptly after the terms and conditions have been finalised.

5.4.7 G As stated in *ICOB 1.2.8R*, *ICOB 5.4.5R* applies to contracts with *commercial customers* that are *contracts of large risks* where the risk is located within the *European Economic Area* as well as other *non-investment insurance contracts*.

#### **Group policies sold to commercial customers**

5.4.8 R When an *insurance intermediary* sells a *group policy* to a *commercial customer* the terms of which provide for *persons*, other than the *commercial customer*



who concludes the *non-investment insurance contract*, to become *policyholders*, the *insurance intermediary* must, promptly after the conclusion of the contract:

- (1) provide a *policy document* and a *policy summary* containing the information in *ICOB 5.5.5R* except *ICOB 5.5.5R(6)* (cross-references to the *policy document*) to the *commercial customer*;
- (2) inform the *commercial customer* that he should provide the *policy summary* containing the information in (1) to each *policyholder* and inform them that a copy of the *policy document* is available on request; and
- (3) if the *policy* replaces a previous *group policy*, inform the *commercial customer* that he should inform each *policyholder* of any changes to the information in the *policy summary*.

- 5.4.9 G (1) The *policyholder* referred to in *ICOB 5.4.8R* is a *person* who has rights under the *policy* to make a *claim* on the *insurance undertaking* of the *policy* (as distinct from a *person* who can only make a *claim* on, for example, his employer or on trustees in respect of the *policy*) (see *ICOB 1.2.15R* and *ICOB 1.2.16G*). Such a *policyholder* will typically be a *retail customer* under *ICOB*. Examples of types of *group policies* that may fall within the scope of *ICOB 5.4.8R* are a group health *policy* for *employees* or a personal accident *policy* for an affinity group such as a sports club or trades union.
- (2) The *policy summary* information to be provided to *policyholders* in accordance with *ICOB 5.4.8R(2)* can be provided in any form, for example, on an employer's intranet, in a staff handbook or in a separate booklet, providing it is in writing.

#### Renewal

- 5.4.10 R Where a *commercial customer's non-investment insurance contract* is due for renewal, *ICOB 5.4.11R* to *ICOB 5.4.14R* apply instead of *ICOB 5.4.1R* to *ICOB 5.4.7G*.
- 5.4.11 R Unless the *insurance intermediary* has reason to believe that the *commercial customer* does not wish to renew the *policy* or the *insurance intermediary* has notified the *commercial customer* that it will not act for him on renewal, the *insurance intermediary* must, in good time before the expiry of the *policy*:
- (1) provide *renewal terms* to the *commercial customer*; or
  - (2) notify the *commercial customer* that the *insurance undertaking* is not willing to invite *renewal* of the *policy* or that the *insurance intermediary* no longer deals with the *insurance undertaking*.
- 5.4.12 G *ICOB 5.4.11R(2)* includes circumstances where the *insurance undertaking* is not willing to invite *renewal* through the *insurance intermediary* in contact with the *commercial customer*.

- 5.4.13 R *A commercial customer* may consent not to receive the information in *ICOB 5.4.11R* if the *insurance intermediary* has explained to the *commercial customer* the consequences of giving that consent before it is given.
- 5.4.14 R *ICOB 5.4.11R* and *ICOB 5.4.13R* do not apply to *renewal* of a *non-investment insurance contract* of no more than one *month's* duration whose terms provide for automatic *renewal* and for cancellation at the *commercial customer's* option. Instead, the *commercial customer* must be notified of changes to the terms and conditions of the contract, including the *premium*, before the changes take effect.

#### Mid-term changes

- 5.4.15 R For the duration of a *non-investment insurance contract* that is a *pure protection contract* an *insurance intermediary* must notify a *commercial customer* of any changes to the information in *ICOB 5.5.20R(22)* (subject to *ICOB 5.5.19R*) and should take reasonable steps to do so in good time before the change takes effect.

### 5.5 Information form and content

#### Policy summary

- 5.5.1 R A *policy summary* must contain only:
- (1) the information specified in *ICOB 5.5.5R* in relation to a *non-investment insurance contract*; and
  - (2) at the option of the *insurer* or *insurance intermediary*:
    - (a) all or part of the information in *ICOB 5.5.14R* (Statement of price);
    - (b) for any applicable compensation scheme mentioned in *ICOB 5.5.5R(12)*, the extent and level of cover and how further information can be obtained; and
    - (c) the information on cancellation in *ICOB 5.3.12R*.
- 5.5.2 R A *policy summary*, if not set out in a separate document, must be:
- (1) in a prominent place within the other document and clearly identifiable as key information that the *retail customer* should read; and
  - (2) separate from the other content of the document in which it is included.
- 5.5.3 G (1) A *policy summary* is a generic document, but the information in *ICOB 5.5.5R* can be personalised if the *insurer* or *insurance intermediary* wishes, with the details applicable to the insurance cover being provided for a particular *retail customer*.
- (2) A *policy summary* should be produced as an informative document. It is not intended to communicate the full terms and conditions of a *non-investment*

*insurance contract* to the *retail customer*. The content should properly describe the contract but should not overload the *retail customer* with detail.

#### Key features as an alternative to a policy summary

**5.5.4 R** A *firm* may provide *key features* that meet the requirements of *COB 6* on the content of the *key features*, instead of a *policy summary*. The *key features* must include the information required in *ICOB 5.5.5R(6), (10) and (13)* (cross-references from significant and unusual exclusions or limitations to related sections of the *policy document*, a telephone number or address for notification of *claims* and the key facts logo), in addition to that required by *COB 6*.

**5.5.5 R** Table: Policy summary content

This table belongs to *ICOB 5.5.1R*.

Policy summary content	
(1)	a statement that the <i>policy summary</i> does not contain the full terms and conditions of the <i>non-investment insurance contract</i> , which can be found in the <i>policy document</i> ;
(2)	Name of the <i>insurance undertaking</i> ;
(3)	type of insurance and cover;
(4)	significant features and benefits;
(5)	significant and unusual exclusions or limitations;
(6)	Cross-references from (5) to the related sections of the <i>policy document</i> ;
(7)	the duration of the <i>non-investment insurance contract</i> ;
(8)	(for <i>policies</i> of more than one year) a statement, where relevant, that the <i>retail customer</i> may need to review and update his cover periodically to ensure it remains adequate;
(9)	the existence or absence of the right of cancellation and, where applicable, the duration of the cancellation period;
(10)	A telephone number or address to which a <i>claim</i> may be notified;
(11)	how to complain to the <i>insurance undertaking</i> and that complaints may subsequently be referred to the <i>Financial Ombudsman Service</i> or any other applicable named complaints scheme;
(12)	that the <i>retail customer</i> may be entitled to compensation from the <i>compensation scheme</i> , or from any other applicable named compensation scheme, should the <i>insurance undertaking</i> be unable to meet its liabilities; and

**(13) the key facts logo.**

- 5.5.6 G When producing the information in *ICOB 5.5.5R* a *firm* should have regard to the nature and complexity of the *non-investment insurance contract* in deciding:
- (1) how much detail the *policy summary* should contain; and
  - (2) what constitutes a significant or unusual exclusion or limitation.
- 5.5.7 G The requirement in *ICOB 5.5.5R(3)* (type of insurance and cover) can be met in the following ways:
- (1) by describing the broad type of *non-investment insurance contract*, for example:
    - (a) for motor insurance, whether the cover is comprehensive or third party;
    - (b) for household insurance, whether accidental damage is included; and
    - (c) for a *pure protection contract*, whether the *premium* is guaranteed, reviewable or renewable; or
  - (2) if a *policy summary* provided to a *retail customer* in a *durable medium* describes different types of cover available, for example, both comprehensive and third party motor insurance, the *retail customer* should be informed which type of cover is being offered at the time he is given the *policy summary*.
- 5.5.8 G A significant exclusion or limitation is one that would tend to affect the decision of *retail customers* generally to buy. In determining what exclusions or limitations are significant an *insurer* should, in particular, consider the exclusions or limitations that relate to the significant features and benefits in *ICOB 5.5.5R(4)*. Another type of significant limitation might be that the contract only operates through certain means of communication e.g. telephone or Internet.
- 5.5.9 G An unusual exclusion or limitation is one that is not normally found in comparable contracts.
- 5.5.10 G Some examples of significant and unusual exclusions or limitations are as follows:
- (1) for *non-investment insurance contracts* that are *pure protection contracts* or medical insurance: deferred payment periods; exclusion of certain conditions or diseases; exclusion of pre-existing medical conditions, and moratorium periods;
  - (2) for *general insurance contracts*: “high risk” electrical items from a household policy; audio equipment from motor insurance; winter sports from travel insurance; and

- (3) for all types of *non-investment insurance contracts*: limits on the amounts of cover; limits on the period for which benefits will be paid; restrictions on eligibility to claim such as age or employment status; excesses.

**5.5.11 R** The key facts logo must be included in a prominent position at the top of the *policy summary*, as shown in *ICOB 4 Ann 1G* for the initial disclosure document, or in a prominent position at the top of the relevant section of the document if the *policy summary* information is included in another document. The logo may be a different size from that in *ICOB 4 Ann 1G*, but its proportions must not be distorted.

5.5.12 G The *FSA* has developed a common 'key facts' logo to be used on significant pieces of information directed to *customers*. When reproducing the logo, *insurers* and *insurance intermediaries* may use colour, providing this does not diminish the prominence of the logo. A specimen of the 'key facts' logo can be obtained from the *FSA* website: [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

5.5.13 G A *firm* should produce a *policy summary* to a standard of quality and presentation consistent with that used for other documents in relation to the *non-investment insurance contract*, so that *retail customers* are not deterred by its appearance from reading it.

#### Statement of price

**5.5.14 R** A statement of price must include the following information:

- (1) the total amount of the *premium* for the *non-investment insurance contract* or, if the *premium* cannot be indicated, the basis for the calculation of the *premium* enabling the *retail customer* to verify it;
- (2) for *non-investment insurance contracts* of more than one year, details of the period for which the *premium* is valid, whether it will be reviewed at a certain time or at set periods and, if so, when it will be reviewed;
- (3) *fees*, administrative charges and taxes payable by the *retail customer* via the *insurance intermediary* in addition to the *premium*. *Fees* and administrative charges include any interest payable on the *premium*, including where the *premium* is paid by way of a credit agreement taken out either for payment of the *premium* only or for the purpose of purchasing goods or services as well;
- (4) a statement identifying separately the possibility of any taxes not payable via the *insurance intermediary*;
- (5) where the *non-investment insurance contract* is purchased in connection with other goods or services:
  - (a) the *premium* for the *non-investment insurance contract*, separately from all other prices in relation to the other goods or services, if an additional price is charged; and

(b) whether purchase of the *non-investment insurance contract* is a requirement of purchasing the other goods or services or not; and

(6) the total price to be paid by the *retail customer* for the *non-investment insurance contract*.

5.5.15 G An example of a situation where a *premium* could not be stated under *ICOB 5.5.14R(1)* is a creditor insurance *policy* where the *premium* varies according to the level of debt. The statement of price should instead show the basis of calculation, for example, the *premium* as a percentage of the debt outstanding at specified dates.

#### **Directive-required information**

5.5.16 R **The directive-required information referred to in this chapter is set out in *ICOB 5.5.20R*, subject to *ICOB 5.5.18R* to *ICOB 5.5.19R*.**

5.5.17 G *ICOB 5.5.20R* brings together all the directive-required information that must be provided under this chapter. Where information required under *ICOB 5.5.20R* has already been provided to a *customer* in another document, for example a *policy summary*, it does not need to be provided a second time for the same contract unless required by a specific *rule*. In some instances it may be possible to meet similar requirements of more than one directive by a single statement, including requirements in *ICOB 4*.

5.5.18 R **The information in *ICOB 5.5.20R(2)* and (3) need not be provided for a *general insurance contract*, if the *United Kingdom* is not the *State of the risk*.**

5.5.19 R (1) **The information in (2) need not be provided for a *non-investment contract* which is a *pure protection contract* if, at the time of application, the *customer*, other than an *EEA ECA recipient*, is *habitually resident*:**

(a) in an *EEA State* other than the *United Kingdom*; or

(b) outside the *EEA* and he is not present in the *United Kingdom*.

(2) **The information referred to in (1) is:**

(a) *ICOB 5.5.20R(4)* to (15); or

(b) *ICOB 5.5.20R(22)*, if the *non-investment insurance contract* was entered into before 1 July 1994.

5.5.20 R Table: Directive-required information to be provided to customers

This table belongs to *ICOB 5.5.16R*.

<b>Directive-required information to be provided to customers</b>	
<b>For <i>general insurance contracts (Third Non-Life Directive)</i> other than certain<sup>1</sup> <i>distance contracts with retail customers</i>:</b>	
<b>(1)</b>	<p>if the <i>insurance undertaking</i> is an <i>EEA firm</i>:</p> <p>(a) the <i>insurance undertaking's Home State</i> and, where appropriate, the <i>EEA State</i> of the <i>branch</i> through which the <i>non-investment insurance contract</i> is to be concluded <sup>2</sup>; and</p> <p>(b) the address of the <i>insurance undertaking's</i> head office (and <i>branch</i>, if appropriate)<sup>2</sup>;</p>
<b>(2)</b>	<p>if the <i>policyholder</i> is a natural person, the law applicable to the <i>general insurance contract</i> where the parties do not have a free choice, or the fact that the parties are free to choose the law applicable and, in the latter case, the law the <i>insurance undertaking</i> proposes to choose; and</p>
<b>(3)</b>	<p>if the <i>policyholder</i> is a natural person, the arrangements for handling <i>policyholders' complaints concerning general insurance contracts</i> including, where appropriate, the existence of a complaints body, without prejudice to the <i>policyholder's</i> right to take legal proceedings.</p>
<p><b>Note 1:</b> The information at (1) to (3) need not be provided for <i>distance contracts</i> where information is provided under the <i>Distance Marketing Directive</i> or equivalent legal requirement.</p>	
<p><b>Note 2:</b> The information in (1) must be stated in the <i>policy document</i> and any other document granting cover.</p>	
<p><b>For <i>non-investment insurance contracts</i> that are <i>pure protection contracts (Consolidated Life Directive)</i><sup>3</sup> other than certain<sup>4</sup> <i>distance contracts with retail customers</i>:</b></p>	
<b>(4)</b>	<p>the name and legal form of the <i>insurance undertaking</i>;</p>
<b>(5)</b>	<p>the name of the <i>EEA State</i> in which the head office of the <i>insurance undertaking</i> and, where appropriate, the agency or <i>branch</i> concluding the <i>non-investment insurance contract</i> is situated;</p>

(6)	the address of the <i>insurance undertaking's</i> head office and, where appropriate, of the agency or <i>branch</i> concluding the <i>non-investment insurance contract</i> ;
(7)	the definition of each benefit and each option;
(8)	the term of the <i>non-investment insurance contract</i> ;
(9)	the means of terminating the <i>non-investment insurance contract</i> ;
(10)	the means of payment of <i>premiums</i> and duration of payments;
(11)	information on the <i>premiums</i> for each benefit, both main benefits and supplementary benefits, where appropriate;
(12)	information about cancellation in accordance with <i>ICOB 5.3.12R</i> ;
(13)	general information on the tax arrangements applicable to the type of <i>non-investment insurance contract</i> ;
(14)	the arrangements for handling complaints concerning <i>non-investment insurance contracts</i> by <i>policyholders</i> , lives assured or beneficiaries under <i>policies</i> , including, where appropriate, the existence of a complaints body, making clear that its existence is without prejudice to the right to take legal proceedings; and
(15)	the law applicable to the <i>non-investment insurance contract</i> where the parties do not have a free choice or, if the parties are free to choose the law applicable, the law the <i>insurance undertaking</i> proposes to choose.
<p><b>Note 3:</b> The directive-required information at (4) to (15) must be in English unless the <i>customer</i> requests it to be, and the <i>insurance undertaking</i> agrees to it being, in another language.</p>	
<p><b>Note 4:</b> The information at (4) to (15) need not be provided for <i>distance contracts</i> where information is provided under the <i>Distance Marketing Directive</i> or equivalent legal requirement.</p>	
<p><b>For <i>non-investment insurance contracts</i> with <i>retail customers</i> concluded by a means of <i>distance communication</i>, other than by telephone (<i>Distance Marketing Directive</i>):</b></p>	
(16)	the <i>insurance undertaking</i>
(a)	the name, main business of the <i>insurance undertaking</i> , and the geographical address of the <i>insurance undertaking's</i> head office and <i>branch</i> , where appropriate;



	(b)	the trade register in which the <i>insurance undertaking</i> is entered and its registration number or an equivalent means of identification in that register;
	(c)	where the <i>insurance undertaking's</i> activity is subject to an authorisation scheme, the particulars of the relevant supervisory authority;
(17)	the financial service	
	(a)	a description of the main characteristics of the <i>non-investment insurance contract</i> ;
	(b)	the total price to be paid by the <i>retail customer</i> to the <i>insurance intermediary</i> for the <i>non-investment insurance contract</i> including all related <i>fees</i> , charges and expenses and all taxes paid via the <i>insurance intermediary</i> or, when an exact price cannot be indicated, the basis for the calculation of the price enabling the <i>retail customer</i> to verify it;
	(c)	notice of the possibility that other taxes and/or costs may exist that are not paid via the <i>insurance intermediary</i> or imposed by him;
	(d)	any limitations of the period for which the information provided is valid;
	(e)	the arrangements for payment and for performance of the <i>non-investment insurance contract</i> ;
	(f)	any specific additional cost for the <i>retail customer</i> of using the <i>means of distance communication</i> ;
(18)	the <i>distance contract</i>	
	(a)	information about cancellation in accordance with <i>ICOB 5.3.12R</i> ;
	(b)	information on any rights the <i>insurance undertaking</i> or the <i>retail customer</i> may have to terminate the <i>non-investment insurance contract</i> early or unilaterally, including any penalties imposed by the <i>non-investment insurance contract</i> in such cases;
	(c)	the <i>EEA State</i> or <i>States</i> whose laws are taken by the <i>insurance undertaking</i> as a basis for the establishment of relations with the <i>retail customer</i> prior to the conclusion of the <i>distance contract</i> ;
	(d)	any contractual clause on law applicable to the <i>policy</i> or on competent court or both;

	(e)	in which language, or languages, the contractual terms and conditions, and the prior information referred to in these <i>rules</i> are supplied, and furthermore in which language, or languages, the <i>insurance undertaking</i> , with the agreement of the <i>retail customer</i> , undertakes to communicate during the duration of the <i>policy</i> ;
(19)	redress	
	(a)	whether or not there is an out-of-court complaint redress mechanism for the <i>retail customer</i> and, if so, the methods for having access to it; and
	(b)	the existence of guarantee funds or other compensation arrangements.
<p><b>For <i>non-investment insurance contracts</i> concluded by telephone with a <i>retail customer</i> who has agreed to limited information being provided before conclusion of the contract (<i>Distance Marketing Directive</i>):</b></p>		
(20)	<p>before conclusion of the contract:</p> <p>the information specified in <i>ICOB 5.3.6R(2)(a)</i> other than <i>ICOB 5.3.6R(2)(a)(viii)</i>.</p>	
(21)	<p>immediately after conclusion of the contract:</p> <p>the information referred to in sub-paragraphs (16) to (19) of this table.</p>	
<p><b>Provisions applying during <i>non-investment insurance contracts</i> that are <i>pure protection contracts</i>:</b></p>		
(22)	any change to the information in sub-paragraphs (4) to (11) of this table.	

- 5.5.21 R Where a *non-investment insurance contract* is effected jointly, the information required by *ICOB 5.5.20R* may be sent only to the first-named *customer*.

- 5.5.22 **R** Where a *non-investment insurance contract* is underwritten by more than one *insurance undertaking*, any rules in this chapter requiring information to be provided to a *customer* about the *insurance undertaking* before conclusion of the contract apply only to the first-named *insurance undertaking*. Details of all the *insurance undertakings* providing cover must be provided promptly after conclusion of the contract.
- 5.5.23 G The relevant supervisory authority in *ICOB 5.5.20R(16)(c)* will in most cases be the *FSA*. Where an *incoming EEA firm* is providing *cross border services*, the relevant supervisory authority will be its *Home State Regulator*.
- 5.5.24 G A description of the main characteristics of a *non-investment insurance contract* in *ICOB 5.5.20R(17)(a)* would include the information referred to at *ICOB 5.5.5R(3)* to (5) and (7). For a *non-investment insurance contract* that is a *pure protection contract* a description would also include a definition of each benefit and each option; information on the *premiums* for each benefit and the means and duration of payment of them.
- 5.5.25 G The relevant out-of-court complaint redress mechanism at *ICOB 5.5.5R(11)* and *ICOB 5.5.20R(3), (14)* and (19)(a) will in most cases be the *Financial Ombudsman Service*.
- 5.5.26 G The relevant guarantee funds or other compensation arrangements referred to at *ICOB 5.5.5R(12)* and *ICOB 5.5.20R(19)(b)* will in most cases be the *compensation scheme*.

#### **Policy document**

- 5.5.27 **R** A *policy document* must contain all the contractual terms and conditions.
- 5.5.28 G The *policy document* provided to a *customer* should contain all the contractual terms and conditions of the *contract of insurance* with that *customer*. The *policy document* can consist of more than one document, but all the documents making up the *policy document* must be provided to the *customer* at the same time.

#### **5.6 White labelling**

- 5.6.1 G The *rules* in this chapter and in *ICOB 4* (Advising and selling standards) require the *customer* to be informed of the identity of both the *insurance undertaking* and the *insurance intermediary*. *ICOB 2.2.3R* (Clear, fair and not misleading communication) requires all communications with *customers* to be clear, fair and not misleading. *ICOB 5.5.5R* (Policy summary content) includes the name of the *insurance undertaking* but not that of the *insurance intermediary* and *ICOB 5.5.1R* does not allow any information to be added to the *policy summary* in addition to that specified in *ICOB 5.5.1R*. The combined effect of these *rules* is that an *insurance intermediary* must clearly communicate the identity of the *insurance undertaking* to the *customer*.

5.7 Record keeping

5.7.1 R An *insurer*, or an *insurance intermediary* where an *insurance undertaking* does not operate from an establishment in the *United Kingdom*, must retain for a minimum period of three years after the information has been provided to the *customer*:

(1) a *policy summary*; and

(2) a *policy document*;

in relation to each *non-investment insurance contract* concluded.

5.7.2 G If the *policy summary* and *policy document* are generic documents that are not specific to the *customer*, an *insurer* or an *insurance intermediary* can keep one copy of each document that it produces, but must retain a copy of any schedule for each *customer* that forms part of the *policy document* if the schedule is *customer* specific.

5.7.3 G *ICOB 2.8.6G* notes that a *firm* should consider keeping records for longer than three years in case *customers* complain or take legal action against the *firm*. An *insurer* or an *insurance intermediary* should in particular consider what constitutes an appropriate retention period for records which relate to *non-investment insurance contracts* which may give rise to *claims* some time after the inception of the contract (e.g. *employers' liability insurance*).

# ICOB 6

## Cancellation

### 6.1 Application and purpose

#### Application: who?

#### 6.1.1 R This chapter applies to:

- (1) an *insurer*;
- (2) a *managing agent*.

#### 6.1.2 R (1) Throughout this chapter references to an *insurer* apply equally to a *managing agent*.

- (2) A *managing agent* must give effect to the policy in *ICOB 6* that a *retail customer* must be offered cancellation rights.

#### 6.1.3 G This chapter sets out the cancellation rights that a *firm* must offer to a *retail customer* upon inception or *renewal* of specified contracts. A *renewal* only occurs if a further *policy* is entered into at the expiry of an existing *policy*. For example, a creditor *policy* that remains in existence from *month* to *month* until the *policyholder* attains a certain age, until cancelled by either party, or until lapse because of non-payment of *premiums* would not be considered as a *policy* with *monthly renewal* under the *ICOB rules*.

#### Application: what?

#### 6.1.4 R Apart from the exemptions set out in *ICOB 6.1.5R*, this chapter applies to all *non-investment insurance contracts*.

#### 6.1.5 R This chapter does not apply to the following contracts:

- (1) a travel and baggage insurance *policy* or similar short-term insurance *policy* of less than one *month's* duration;
- (2) a *non-investment insurance contract*, the performance of which has been fully completed by both parties at the *retail customer's* express request before the *retail customer* exercises his right to cancel;
- (3) a *non-investment insurance contract* that is a *pure protection contract* of six *months'* duration or less that is not a *distance contract*;
- (4) a *pure protection contract* effected by the trustees of an *occupational pension scheme*, an employer or a *partnership* to secure benefits for the *employees* or the *partners* in the *partnership*; and

(5) a *general insurance contract* that is not a *distance contract* sold by an intermediary who is an *unauthorised person*.

(6) a *connected contract* that is not a *distance contract*.

6.1.6 G In *ICOB* 6.1.5R(1) the 'similar short-term insurance *policy*' referred to is any *contract of insurance* where the event or activity being insured is less than one *month's* duration. The reference to 'duration' is to the period of the cover rather than the period of the contract. So the exemption will cover travel insurance for a fortnight's holiday, even if the insurance was taken out two *months* before the holiday began. However, if the period of cover includes cancellation of the holiday from the point at which the contract is taken out, the *policy* will not benefit from the exemption.

6.1.7 G In relation to *ICOB* 6.1.5R(2):

(1) a contract is not fully completed simply because an event has occurred which allows a *claim* to be made under the contract (for example, a *claim* for a cancelled flight or lost baggage); and

(2) a contract is fully completed where a *claim* has been made that leads to the contract being terminated. This could include a total loss *claim* (for example, a motor *claim* where the vehicle is written off and this results in termination of the contract).

6.1.8 G For the purposes of this chapter, cancellation refers to the initial period of cover during which the contract may be voided. It does not refer to mid-term cancellation that a *firm* may choose to offer its *customers*.

6.1.9 G The cancellation rights described in this chapter apply to all *renewals* and not just those where there have been significant changes.

6.1.10 G Where *ICOB* 6.1.5R applies and there is no cancellation right, a *firm* should inform the *retail customer* of that fact in accordance with *ICOB* 5.3.12R(1).

### **Purpose**

6.1.11 G (1) This chapter reinforces *Principle 6* (Customers' interests) which requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly. In certain circumstances, *retail customers* who have entered into a *non-investment insurance contract* will be entitled to a period of reflection during which they can decide whether to proceed with their purchase.

(2) This chapter also implements, where relevant, elements of the *DMD* and the *Consolidated Life Directive* relating to the cancellation of *distance contracts* and *non-investment insurance contracts* that are *pure protection contracts*.

- 6.2 Cancellation rights and period**
- 6.2.1 R** *A retail customer has a right to cancel a non-investment insurance contract in accordance with ICOB 6.2, ICOB 6.3 and ICOB 6.4.*
- 6.2.2 R** *The period of cancellation is:*
- (1)** *30 days for a non-investment insurance contract that is a pure protection contract; and*
- (2)** *14 days for a general insurance contract.*
- 6.2.3 R** *Where the terms of an insurer's contract give a retail customer a longer period to cancel (that is, in excess of the 14 or 30 days specified), the insurer must disclose in the information about the right to cancel the differences between the retail customer's right under ICOB 6.2.1R and the terms of the contract, which operate independently.*
- 6.2.4 R** *Where a contract is a mixed contract, that is, it has elements of both a general insurance contract and a pure protection contract, a 30 day cancellation period must apply.*
- 6.2.5 R** *The cancellation period in ICOB 6.2.2R must begin on the later of:*
- (1)** *(for a non-investment insurance contract that is a pure protection contract) the day the retail customer is informed that the contract has been concluded; or*
- (2)** *(for a general insurance contract) the day of the conclusion of the contract; or*
- (3)** *the day on which the retail customer receives the contractual terms and conditions and information in accordance with ICOB 5.3.4R, ICOB 5.3.6R(1) or ICOB 5.3.8R in a durable medium.*
- 6.2.6 G** **(1)** *Where ICOB 6.2.5R(3) applies, an insurer is entitled to assume that documents have been received in accordance with generally accepted principles of law. That is:*
- (a)** *that provided the document is sent to the correct address or number, documents posted first class on business day 1 are received on business day 2;*
- (b)** *that a fax is received when sent, if an appropriate transmission report is generated by the transmitter's machine; and*
- (c)** *that an e-mail is received when sent.*

- (2) The general assumptions in *ICOB* 6.2.6G(1) can be contradicted by a *retail customer*. In such cases the burden would be on the *retail customer* to show that the evidence on which the *insurer* was relying was not correct. If the *retail customer* could show this then unless the *insurer* itself had information to suggest that this was not the case, the *insurer* should generally accept the *retail customer's* evidence.
- 6.2.7 G The provisions in *ICOB* 6.2.5R(3), under which time may run from the *day* on which the *retail customer* receives the contractual terms and conditions and information in accordance with *ICOB* 5.3.4R, *ICOB* 5.3.6R(1) or *ICOB* 5.3.8R, as applicable, would cover situations where:
- (1) the contract has been concluded by a *means of distance communication* by which the contractual information could not reasonably have been provided prior to the conclusion of the contract in a *durable medium* (for example, by telephone) and is therefore provided subsequently; or
- (2) the contract is not a *distance contract* and the *retail customer* has not received the contractual terms and conditions in a *durable medium* before the conclusion of the contract.
- 6.2.8 R **If an *insurer* has provided information in accordance with *ICOB* 5.3.4R, *ICOB* 5.3.6R(1) or *ICOB* 5.3.8R in a *durable medium*, it need not accept a notice of cancellation if it is served later than the period specified for that contract.**
- 6.2.9 R **If a *firm* does not give a *retail customer* information about his cancellation rights in a *durable medium* in accordance with *ICOB* 5.3.12R, the contract is cancellable.**
- 6.3 Notification of cancellation by the retail customer
- 6.3.1 R **A *retail customer* who has a right to cancel under *ICOB* 6.2.1R may, without giving any reason, cancel the contract by serving notice upon the *insurer*, its *appointed representative* or any agent of the *insurer* with authority to accept notice on the *insurer's* behalf before expiry of the relevant cancellation period, in accordance with the practical instructions given to him in accordance with *ICOB* 5.3.12R.**
- 6.3.2 R **Where the notice of cancellation is in a *durable medium* and served in accordance with *ICOB* 6.3.1R, it must be treated as being served on the *insurer* on the date it is despatched by the *retail customer*.**
- 6.3.3 G In the event of any dispute, unless there is clear written evidence to the contrary, an *insurer* should treat the date cited by the *retail customer* as being the date when the notice of cancellation was given, *posted* or otherwise sent.



- 6.3.4 G In order to ensure that a *retail customer* returns to the *insurer* any insurance certificate that the *insurer* may provide as part of the *non-investment insurance contract* (for example, the motor insurance certificate), the *insurer* may wish to consider putting the notice of cancellation on the insurance certificate itself and instructing the *retail customer*, prior to the conclusion of the contract in accordance with *ICOB 5.3.12R(2)(d)*, to exercise this right of cancellation by returning the certificate. Unless these instructions are given to the *retail customer* in accordance with *ICOB 5*, an *insurer* will not be able to require cancellation to be exercised in this way.

## 6.4 Effects of cancellation

- 6.4.1 R **By exercising his right to cancel under *ICOB 6.2.1R*, a *retail customer* withdraws from the contract.**

### **Automatic cancellation of an attached distance contract**

- 6.4.2 G (1) Regulation 11 (Automatic cancellation of an attached distance contract) of the *Distance Marketing Regulations* has the effect that, when notice of cancellation is given in relation to a contract, that notice also operates to cancel any attached contract which is also a distance financial services contract. Whether a contract will be "attached" to the main contract will depend on the circumstances in each case. Regulation 11(1)(b) provides that the contract will be attached if:
- (a) it has been entered into in accordance with a term of the main contract;
  - (b) the main contract is financed or is to be financed by the contract;
  - (c) the *retail customer* has entered into the contract for a purpose related to the main contract; or
  - (d) performance of the contract requires performance of the main contract.
- (2) A *retail customer* will also have an independent right to cancel an attached distance contract and may do so without cancelling the main contract.

### **Payments**

- 6.4.3 R **Where a *retail customer* exercises a right to cancel under *ICOB 6.2.1R*:**
- (1) **the *insurer* must pay to the *retail customer* without delay, and no later than 30 days after the date on which the *insurer* received notice of cancellation from the *retail customer*, any sums which the *retail customer* has paid to, or for, the benefit of the *insurer* in connection with the contract (including sums paid by the *retail customer* to agents of the *insurer*) except for the amount referred to in (2);**

- (2) where the contract is a *general insurance contract*, subject to (3), the *insurer* is permitted to require the *retail customer* to pay for the services it has actually provided in connection with the contract. The amount payable, however, must not:
  - (a) exceed an amount which is in proportion to the extent of the service already provided to the *retail customer* by the *insurer* in comparison with the full coverage of the contract; and
  - (b) be such that it could be construed as a penalty;
- (3) sub-paragraph (2) applies only:
  - (a) where performance of the contract has commenced before expiry of the cancellation period and this was requested by the *retail customer*; and
  - (b) where the *insurer* can demonstrate that the *retail customer* was provided with details of the amount which he may be required to pay if exercising his right to cancel in accordance with *ICOB 6.2.1R*;
- (4) the *insurer* is entitled to receive without delay, and no later than 30 days after the date on which the *retail customer* posted or otherwise sent notice of cancellation to the *insurer* any sums and property that became the *retail customer's* under the contract.

- 6.4.4 G (1) The amount referred to in *ICOB 6.4.3R(2)* may include any sums that the *insurer* has reasonably incurred in concluding the *general insurance contract* but should not include any element of profit.
- (2) An *insurer* and an *insurance intermediary* should take reasonable steps to ensure that double recovery of selling costs is avoided, particularly where:
  - (a) there is also a *distance non-investment mediation contract* (see *ICOB 8*); or
  - (b) both *commission* and *fees* are recouped by an *insurer* and an *intermediary* respectively.

- 6.4.5 G The amount referred to in *ICOB 6.4.3R(2)* may include:
- (1) an amount for the cover provided (i.e. a proportion of the *contract of insurance's* exposure that relates to the time on risk);
  - (2) a proportion of the *commission* paid to the *insurance intermediary* sufficient to cover that *insurance intermediary's* costs; and
  - (3) a proportion of any *fees* charged by the *insurance intermediary*, which, when aggregated with any *commission* to be repaid, would be sufficient to cover the *insurance intermediary's* costs.

- 6.4.6 G In the event that a *retail customer* exercises his right to cancel, the amount described in *ICOB 6.4.3R(2)* will normally be retained by the *insurer* (although in some circumstances it could be retained by the *insurance intermediary*). The *insurer* and the *insurance intermediary* should, therefore, agree the terms by which the *insurer* reimburses the *insurance intermediary* (or the reverse).
- 6.4.7 G In calculating the charge in accordance with *ICOB 6.4.3R(2)*, an *insurer* should use a reasonable method of estimating the proportion of the *contract of insurance's* exposure that relates to the time on risk.
- 6.4.8 G In most cases, the *FSA* would expect the proportion of the *insurance contract's* exposure that relates to the time on risk to be a pro rata apportionment. However, where there is material unevenness in the incidence of risk, the *insurer* could employ a more accurate method, which may result in a lower or higher charge to the *retail customer*. In such cases, the *insurer* may charge what it believes to be a reasonable sum, but it should bear in mind that the sum should not exceed an amount commensurate to the risk incurred.
- 6.4.9 R **Where an *insurer* has made a charge for services provided in accordance with *ICOB 6.4.3R(2)*, the sums and property referred to in *ICOB 6.4.3R(4)* must not include any money or property that the *insurer* has provided to the *retail customer* in connection with a *claim*.**
- 6.4.10 R **Any sum payable under *ICOB 6.4.3R* is owed as a simple contract debt, and any sums payable in respect of the cancellation of the same contract may where relevant be set off against each other.**

# ICOB 7

## Claims handling

### 7.1 Application and purpose

#### Application: who and what?

- 7.1.1 R (1) This chapter applies, except for *ICOB 7.6*, in respect of *claims handling* under a *non-investment insurance contract* to:
- (a) an *insurer*;
  - (b) an *insurance intermediary*;
  - (c) a *managing agent*.
- (2) *ICOB 7.6* applies in respect of *motor vehicle liability insurance business* to:
- (a) a *motor vehicle liability insurer*; and
  - (b) the *Society*.
- 7.1.2 R Throughout this chapter, references to an *insurer* apply equally to a *managing agent*.
- 7.1.3 G An *insurer* is responsible for *claims handling*. A *managing agent* is responsible for *claims handling* for *policies* underwritten at Lloyd's. An *insurer* or *managing agent* remains responsible for *claims handling* if it outsources any of its *claims* related activities, including where it gives an intermediary authority to *handle claims* on its behalf. An *insurer* or a *managing agent* is not responsible for the *administration and performance* activities that an *insurance intermediary* carries out on behalf of a *customer* in connection with a *claim*. In relation to these activities, the *insurance intermediary* should refer to *ICOB 7.4*.
- 7.1.4 G An *insurer* should refer to the *rules and guidance* set out in *SUP 2.3.5R* to *SUP 2.3.10G* in respect of any *person* to whom it outsources its *claims handling* functions.
- 7.1.5 G All of this chapter, except *ICOB 7.6*, applies to *claims* made by *retail customers*. Part of *ICOB 7.3*, all of *ICOB 7.4* and all of *ICOB 7.7* apply to *claims* made by *commercial customers*. *ICOB 7.6* applies to *claims* by *injured parties* arising from an accident occurring in an *EEA State* other than the *EEA State* of residence of the *injured party*, involving the use of a vehicle insured and normally based in an *EEA State*.

## Purpose

- 7.1.6 G (1) The purpose of this chapter is to ensure that:
- (a) *claims* are handled fairly;
  - (b) *claims* are settled promptly;
  - (c) *customers* are provided with information on the *claims handling* process, and with an explanation of why a *claim* is rejected or not settled in full, where relevant; and
  - (d) *insurance intermediaries* disclose and manage any conflicts of interest that may exist.
- (2) This chapter reinforces:
- (a) *Principle 3* (Management and control), which requires a *firm* to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems;
  - (b) *Principle 6* (Customers' interests), which requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly; and
  - (c) *Principle 8* (Conflicts of interest), which requires a *firm* to manage conflicts of interest fairly, both between itself and its *customers* and between a *customer* and another *client*.
- (3) The purpose of *ICOB 7.6* is to transpose certain requirements of the *Fourth Motor Insurance Directive*.

## 7.2 Group policies and third party claimants

- 7.2.1 G Any *person* who, under the terms of a *policy*, has a right to *claim* directly on the *insurer*, is a *policyholder* (see *ICOB 1.2.15R* to *ICOB 1.2.16G*). When dealing with *claims* under *group policies*, *insurers* should consider whether the *person claiming* is a *commercial customer* or a *retail customer* and should apply the *rules* in this chapter accordingly when dealing with a *customer's claim*.
- 7.2.2 G When an *insurer* deals directly with a third party who *claims* against his *customer* because the third party has a legal right to bypass the *customer* and *claim* directly against the *insurer* (for example, certain motor *claims* or because of the insolvency of the *customer*), these *rules* do not require the *insurer* to treat the third party as a *customer*. However, the *insurer* should have regard to *Principle 1* (Integrity), *Principle 2* (Skill, care and diligence) and *Principle 5* (Market conduct) in its dealings with the third party and should not deal with the *claim* in any way less favourably than it would have done had the *claim* been proceeded against its *customer*.

## 7.3 Claims handling: general

### **Requirement to handle claims promptly and fairly**

- 7.3.1 **R** An *insurer* must carry out *claims handling* promptly and fairly.
- 7.3.2 **G** When handling the *claim* of a *retail customer*, an *insurer* should comply with the *rules* and *guidance* in *ICOB 7.5*. When handling the *claim* of a *commercial customer*, an *insurer* should ensure that:
- (1) the *commercial customer* is kept reasonably informed of how his *claim* is progressing; and
  - (2) payment is made promptly once settlement terms have been agreed.
- 7.3.3 **G** An *insurer* should refer to the *guidance* in *SYSC 3.2* (Areas covered by systems and controls) in its procedures for *claims handling*. For example, an *insurer* should have in place systems and controls which take account of reasonably foreseeable peaks in demand, to allow it to deal with *claims* promptly in such circumstances.
- 7.3.4 **G** An *insurer* should refer to the *guidance* set out in *TC 1* (Commitments) in respect of the competence of any *person* who carries out *claims handling* on its behalf.

### **Giving customers guidance on claiming**

- 7.3.5 **R** When an *insurer* is informed that a *customer* wishes to *claim* under his *policy* it must give the *customer* reasonable guidance to help him make a *claim* under his *policy*.

### **Rejecting or refusing claims**

- 7.3.6 **R** An *insurer* must not:
- (1) unreasonably reject a *claim* made by a *customer*;
  - (2) except where there is evidence of fraud, refuse to meet a *claim* made by a *retail customer* on the grounds:
    - (a) of non-disclosure of a fact material to the risk that the *retail customer* could not reasonably be expected to have disclosed;
    - (b) of misrepresentation of a fact material to the risk, unless the misrepresentation is negligent;
    - (c) in the case of a *general insurance contract*, of breach of warranty or condition, unless the circumstances of the *claim* are connected with the breach; or

(d) in the case of a *non-investment insurance contract* which is a *pure protection contract*, of breach of warranty, unless the circumstances of the *claim* are connected with the breach and unless:

(i) under a ‘life of another’ contract, the warranty relates to a statement of fact concerning the life to be assured and that statement would have constituted grounds for rejection of a *claim* by the *insurer* under *ICOB 7.3.6R(2)(a)* or (b) if it had been made by the life to be assured under an ‘own life’ contract; or

(ii) the warranty is material to the risk and was drawn to the attention of the *retail customer* before the conclusion of the contract.

#### 7.4 Duties of insurance intermediaries

7.4.1 R *ICOB 7.4* applies to an *insurance intermediary*.

7.4.2 G *ICOB 7.4* will usually apply to an *insurance intermediary* that is not an *insurer*, but it may also apply to an *insurer*, for example, if it were dealing with a *claim* on a *policy* insured by another *insurance undertaking*.

##### An insurance intermediary’s duty of care, skill and diligence

7.4.3 R An *insurance intermediary*, when acting for a *customer* in relation to a *claim*, must act with due care, skill and diligence.

7.4.4 G The *rules* and *guidance* in *ICOB 7.4* do not seek to set out the full extent of the duties owed by the *insurance intermediary* to any *person* for whom it acts, nor do they displace the general law on the duties of an *insurance intermediary*.

##### An insurance intermediary’s duty to avoid conflicts of interest

7.4.5 R (1) An *insurance intermediary* must not, in connection with any *claim*, put itself in a position where its own interest, or its duty to any *person* for whom it acts, conflicts with its duty to any *customer*, unless:

(a) it made proper disclosure to its *customer* of all information needed to put its *customer* in a position where he can give informed consent to the arrangement; and

(b) it has obtained the prior informed consent of the *customer*.

(2) An *insurance intermediary* must decline to act for the *person* or *customer* referred to in (1) or any of them unless, in the particular circumstances of the case, disclosure and informed consent are sufficient to enable it to reconcile the conflict.

- 7.4.6 G *ICOB 7.4.5R* imposes a requirement on an *insurance intermediary* to avoid conflicts of interest in relation to *claims* where it acts on behalf of a *customer*, unless it can manage them by disclosure to, and the obtaining of consent from, its *customer*.
- 7.4.7 G An *insurance intermediary* should consider whether it is possible to manage the conflict by disclosing the conflict to the *customer* and obtaining his consent. Where an *insurance intermediary* acts for a *customer* in *arranging a policy*, it is likely to be the agent for the *customer* in connection with the preparation and handling of any *claim* against the *insurance undertaking*. If the *insurance intermediary* intends to be the agent of an *insurance undertaking* in relation to *claims* under that *policy*, it will need to consider whether it is at risk of putting itself in the position where it cannot act without some breach of duty either to the *insurance undertaking* or the *customer*. The *insurance intermediary* should consider whether disclosure and consent are sufficient to reconcile the conflicting obligations. An example of a circumstance in which disclosure and consent are unlikely to be sufficient, and when an *insurance intermediary* may well consider that it should not act for the *insurance undertaking* or the *customer* (or both), is where the *insurance intermediary* knows that its *customer* will, to obtain a quick payment, accept a low amount in settlement of a *claim* and also knows the *insurance undertaking* is willing to settle for a higher amount.

#### **Other notifications and actions in relation to claims**

- 7.4.8 R **If an *insurance intermediary* acts for an *insurance undertaking* and not a *customer* in relation to a *claim* on a contract which it *arranged* for that *customer*, the *insurance intermediary* must inform the *customer* that, in relation to that *claim*, it is acting on behalf of the *insurance undertaking*, and not the *customer*.**
- 7.4.9 G *ICOB 7.4.8R* would apply, for example, where an *insurance intermediary* has delegated authority for *claims handling* and deals with a *claim* in relation to a contract that it sold to a *customer*, if the *insurance intermediary* is not acting on behalf of that *customer* in relation to the *claim*.
- 7.4.10 R **If an *insurance intermediary* is notified of a *claim* in relation to a *policy* which it has *arranged*, and the *insurance undertaking* has not given it the authority to deal with that *claim*, it must:**
- (1) **forward the notification to the *insurance undertaking* promptly; or**
  - (2) **inform the *customer* immediately that it cannot deal with the notification.**

#### **7.5 Retail customers: performance standards for handling claims**

##### **Responding to notification of the claim**

- 7.5.1 R **An *insurer* must respond promptly to a notification by a *retail customer* of a *claim*.**



- 7.5.2 G Notification of a *claim* is a demand of the *insurer* to pay or provide a benefit insured under the *policy*, e.g. by submitting a *claim* form or giving the equivalent information orally, where permitted by the *policy*. An enquiry that precedes such a demand, for example, as to whether a particular loss is covered, and therefore whether a *claim* could be made under the terms of the *policy*, is not notification of a *claim*.
- 7.5.3 G *ICOB 7.5.1R* requires an *insurer* to respond promptly once it has received notification of a *claim*. Generally a prompt response would be one within five *business days* of a *retail customer* making a *claim*, although in some circumstances a prompt response could be less than five *business days*, such as where the *retail customer* would expect a swifter response because of the nature of the *claim* or the terms of the *policy* (for example, a roadside assistance *policy*).
- 7.5.4 R The response referred to in *ICOB 7.5.1R* must:
- (1) provide the information set out in *ICOB 7.5.5R*;
  - (2) be in a *durable medium*, unless the notification by the *retail customer* is made orally and the *insurer* does not require the *retail customer* to complete a *claim* form; and
  - (3) provide the *retail customer* with a *claim* form, if the *insurer* requires one to be completed.
- 7.5.5 R The information referred to in *ICOB 7.5.4R(1)* is:
- (1) that the *claim* relates to a risk that is clearly outside the scope of the *policy*, if that is the case (in which case no further information need be provided);
  - (2) the action that will be taken by the *insurer*, and when that action will be taken;
  - (3) if the *insurer* is appointing any other parties to contact the *retail customer* on the *insurer's* behalf, in respect of each other party appointed the following information, if known (but, if the purpose of the appointment is to investigate the validity of a *claim*, the information need not be given if to give it would limit or prevent the effective investigation of the *claim* or any part of it):
    - (a) its name (unless the other party trades under the name of the *insurer*);
    - (b) its function; and
    - (c) the work it will carry out in relation to the *claim*.

- 7.5.6 G The purpose of the *rules and guidance* in *ICOB 7.5.1R to ICOB 7.5.5R* is to provide the *retail customer* at an early stage with information in relation to the processing and settlement of his *claim* by the *insurer*. *ICOB 7.5.5R(1)* is intended to prevent a *retail customer* pursuing a *claim* for which he is clearly not covered, for example, making a *claim* on a contents insurance *policy* for possessions away from home, when the *policy* only covers possessions in the home. It is not intended to pre-empt the outcome of an investigation of a *claim*.
- 7.5.7 G The purpose of *ICOB 7.5.5R(3)* is to ensure that a *retail customer* knows the name and function of any party who will contact him in relation to a *claim* as a representative of the *insurer* e.g an outsourced *claims handling* company or a loss adjuster. An *insurer* would not be expected to notify the *retail customer* of other parties who are appointed to investigate the validity of a *claim*, if this would limit or prevent an effective investigation. However, if a third party such as a loss adjuster is appointed to liaise with the *retail customer* on the *insurer's* behalf, as well as assess the validity of the *claim*, the *insurer* would be expected to disclose the information in *ICOB 7.5.5R(3)* unless it would limit or prevent an effective investigation.

#### **Investigation and processing of the claim**

- 7.5.8 R **An *insurer* must keep the *retail customer* reasonably informed about the progress of his *claim*.**
- 7.5.9 G Where the investigation of a *claim* is likely to be protracted, an *insurer* should provide periodic progress or status reports, when appropriate, to a *retail customer*, including providing the *retail customer* with any relevant update in relation to the information provided under *ICOB 7.5.5R*. The *insurer* should also respond without undue delay to any reasonable request by the *retail customer* for information.

#### **Determining the claim**

- 7.5.10 R **An *insurer* must notify the *retail customer* as soon as practicable whether it:**
- (1) rejects all of his *claim*;
  - (2) rejects his *claim* but, without prejudice to the rejection, makes an offer in compromise; or
  - (3) accepts all or part of his *claim*.
- 7.5.11 R **If the *insurer* rejects the *claim*, but without prejudice to the rejection makes an offer in compromise, it must notify the *retail customer* of the terms of that offer as soon as practicable.**
- 7.5.12 R **If the *insurer* accepts all or part of the *retail customer's claim*, it must notify the *retail customer* as soon as practicable whether:**
- (1) as to the parts it accepts, it agrees to provide the money, property or service *claimed* by the *retail customer* in full; or

- (2) it makes some other offer in compromise. In that event, it must notify the *retail customer* of the terms of its offer.
- 7.5.13 R (1) Unless the *insurer* accepts the *retail customer's claim* in full, the *insurer* must explain why it rejects all or part of the *retail customer's claim* or makes a compromise offer, specifying any relevant term of the *policy*.
- (2) The *insurer* must offer the *retail customer* the choice of receiving the information at *ICOB 7.5.13R(1)* in a *durable medium*.
- 7.5.14 G *Motor vehicle liability insurers* should refer to the *rules* and *guidance* at *ICOB 7.6.8R* to *ICOB 7.6.11G* in respect of a *claim* for damages by an *injured party* in the circumstances set out in *ICOB 7.6.11G(1)*.
- 7.5.15 R The *insurer* must, in respect of each part of the *claim* that it accepts, inform the *retail customer* whether the *claim* will be settled by paying him, or by paying another *person* to provide goods or services, or by providing those goods or services.
- 7.5.16 G Examples of a payment to others for the provision of goods or services are: to a garage for repairs carried out to a vehicle, to a supplier for the provision of replacement electrical goods, or to a doctor for medical treatment.

#### Settling a claim

- 7.5.17 R An *insurer* must settle a *claim* by a *retail customer* promptly.
- 7.5.18 G (1) Settlement terms are agreed when:
- (a) the *insurer* accepts the *retail customer's claim*; and
  - (b) the *retail customer* accepts the *insurer's* offer of settlement.
- (2) When the *insurer* settles the *claim* by paying the *retail customer*, the *insurer* should aim to make payment within five *business days* after the *insurer* and the *retail customer* have agreed settlement terms, subject to any pre-conditions laid down by the *insurer* or in law being met by the *retail customer*. This does not prevent the *insurer* paying a *claim* before the *retail customer* has finally agreed settlement terms.
- (3) The *guidance* in (2) would not apply if the *non-investment insurance contract* otherwise provides, or the *insurer* settles the *claim* by:
- (a) payment against a liability due on a future date;
  - (b) the provision of goods or services;
  - (c) making payments on a date specified by the *retail customer*; or
  - (d) payment of the *claim* through an employer or other party on a monthly or some other basis;

and in the case of (a) or (b) the *insurer* should make prompt payment or arrange for prompt provision of the goods or services after the *insurer* and the *retail customer* have agreed settlement terms.

- 7.5.19 G The arrangements for settlement set out in *ICOB 7.5.18G(3)(a)* are likely to apply, for example, when payments are made under a creditor insurance *policy* to meet periodic repayments due under a loan agreement.
- 7.5.20 G The arrangements for settlement set out in *ICOB 7.5.18G(3)(b)* apply to arrangements to supply goods or services to the *retail customer*. In such situations, the goods or services should be provided promptly, but where they cannot be the *insurer* should tell the *retail customer* when to expect them.
- 7.5.21 G An *insurer* should note that unless it has previously informed a *retail customer* that a *claim* will not be met in full or in part until *premiums* have been paid, the *insurer* may not delay payment of a *claim* on the grounds that *premiums* are outstanding.

#### **Pre-action protocols**

- 7.5.22 G A *customer* who does not accept an *insurer's* rejection of his *claim* (or part of it) may challenge that rejection. If he chooses to do so through the courts, *firms* should be aware that in England and Wales there are pre-action protocols which lay down certain requirements as to the steps to be taken before proceedings are issued. This chapter does not displace these requirements, to which *firms* should have regard in the event that a rejection of a *claim* moves towards litigation.

#### **7.6 Motor vehicle liability insurers: claims representatives**

- 7.6.1 G (1) Under *threshold condition 2A* (Appointment of claims representatives), if it appears to the *FSA* that any *person* is seeking to carry on, or is carrying on, *motor vehicle liability insurance business*, that *person* must have a *claims representative* in each *EEA State* other than the *United Kingdom*.
- (2) If any *person* carrying on *motor vehicle liability insurance business* becomes aware, or has information which reasonably suggests, that that *person* has failed to satisfy, may have failed to satisfy or may not in the foreseeable future be able to satisfy, *threshold condition 2A* (or any *threshold condition*), that *person* must notify the *FSA* immediately (see *SUP 15.3.1R*).
- 7.6.2 R **The *Society* must ensure that no *member* carries on *motor vehicle liability insurance business* at Lloyd's unless a *claims representative* has been appointed to act for that *member* in each *EEA State* other than the *United Kingdom*, with responsibility for handling and settling *claims* arising from an accident in the cases referred to in Article 1 of the *Fourth Motor Insurance Directive*.**

- 7.6.3 R (1) When a *motor vehicle liability insurer* appoints a *claims representative*, it must give the *MIIC*, and each other *information centre*, the *claims representative's* name, business address, telephone number and effective date of appointment within ten *business days* of that appointment being made.
- (2) If the information at (1) changes in any material way, the *motor vehicle liability insurer* must give the *MIIC*, and each other *information centre*, details of that change within ten *business days* of that change.
- 7.6.4 R A *motor vehicle liability insurer* must ensure that each *claims representative* is:
- (1) resident or established in the *EEA State* for which it is appointed;
- (2) capable of examining cases in the official language or languages of the *EEA State* of residence of the *injured party*;
- (3) responsible for, and has sufficient delegated authority from the *motor vehicle liability insurer* for which it is appointed, to be able to:
- (a) handle and settle;
- (b) collect all information, and take all measures, reasonably necessary to negotiate a settlement of; and
- (c) represent, or arrange appropriate representation for, the *motor vehicle liability insurer* (whether in negotiations, in court or otherwise) in relation to;
- claims*, arising from an accident occurring in an *EEA State* other than the *EEA State* of residence of the *injured party*, involving the use of a vehicle insured and normally based in an *EEA State*.
- 7.6.5 G *ICOB 7.6.4R(3)* does not prevent a *claims representative* from seeking additional authority or instructions from a *motor vehicle liability insurer*, if its existing authority or instructions are insufficient to allow it to handle and settle a *claim*. However, it does prevent a *claims representative* from purporting to decline to deal with, or transfer responsibility for, *claims* properly referred to that *claims representative* by an *injured party*, or an *injured party's* representative.
- 7.6.6 G Nothing in the *rules* and *guidance* at *ICOB 7.6* prevents, or is intended to prevent:
- (1) a *motor vehicle liability insurer* from appointing more than one *claims representative* in one, or more than one, *EEA State*; or
- (2) a *claims representative* from acting for more than one *insurer* or *member*; or

- (3) a representative, appointed by a *motor vehicle liability insurer* under SUP 13.5.2R or regulation 3(d) of the *EEA Passport Rights Regulations*, from acting as that *motor vehicle liability insurer's claims representative* as well.

7.6.7 G The appointment of a *claims representative* does not in itself constitute the opening of a *branch* or the creation of an establishment (see article 4(8) of the *Fourth Motor Insurance Directive*).

**Motor vehicle liability insurers: claims handling**

7.6.8 R (1) **Within three *months* of receipt of a *claim* for damages from an *injured party*, or his representative, the *motor vehicle liability insurer* must (directly, or through a *claims representative*):**

- (a) **make a reasoned offer of settlement if liability is admitted and damages have been fully quantified; or**
- (b) **provide a reasoned reply to the points made in the *injured party's claim* if liability is denied, or not admitted, or the *claim* for damages has not been fully quantified.**

(2) **If liability is initially denied, or not admitted, within three *months* of any subsequent admission of liability, the *motor vehicle liability insurer* must (directly, or through a *claims representative*) make a reasoned offer of settlement, if, by that time, the relevant *claim* for damages has been fully quantified.**

(3) **If an *injured party's claim* for damages is not fully quantified when it is first made, within three *months* of the subsequent receipt of a fully quantified *claim* for damages, the *motor vehicle liability insurer* must (directly, or through a *claims representative*) make a reasoned offer of damages, if liability is admitted at that time.**

(4) **A *claim* for damages will be fully quantified under (1)(a), (2) or (3) when the *injured party* provides written evidence which substantiates or supports the amounts *claimed*.**

7.6.9 R (1) **If the *motor vehicle liability insurer*, or its *claims representative*, does not comply with *ICOB 7.6.8R*(1)(a), (2) or (3), the *motor vehicle liability insurer* must pay simple interest on any damages eventually paid, unless interest is awarded by any tribunal which determines the *injured party's claim*.**

(2) **If (1) applies, the amount of interest that the *motor vehicle liability insurer* must pay must be calculated as follows:**

- (a) **the interest calculation period begins three months after:**

- (i) receipt of the *claim* for damages, if the *motor vehicle liability insurer* or its *claims representative* breaches *ICOB 7.6.8R(1)(a)*; or
  - (ii) any subsequent admission of liability, if the *motor vehicle liability insurer* or its *claims representative* complies with *ICOB 7.6.8R(1)(a)* but breaches *ICOB 7.6.8R(2)*; or
  - (iii) the subsequent receipt of a fully quantified *claim* for damages, if the *motor vehicle liability insurer* or its *claims representative* complies with *ICOB 7.6.8R(1)(a)* and (2) but breaches *ICOB 7.6.8R(3)*; and
- (b) the interest calculation period ends on the date when the *motor vehicle liability insurer* pays compensation to the *injured party*, or the *injured party's* authorised representative;
  - (c) the interest rate to be applied throughout the period in (a) to (b) is the Bank of England's base rate (from time to time), plus four per cent.
- 7.6.10 R A *motor vehicle liability insurer* will be taken to have received a *claim*, or a fully quantified *claim*, for damages when that *claim*, or fully quantified *claim*, for damages is delivered to the *motor vehicle liability insurer*, or a *claims representative*, by any *person* by any method of delivery which is lawful in the *motor vehicle liability insurer's*, or its *claims representative's*, respective State of residence or establishment.
- 7.6.11 G (1) *ICOB 7.6.8R* to *ICOB 7.6.10R* apply only to *claims* for damages for loss or injury suffered in, or as a result of, an accident which occurs in an *EEA State* other than an *injured party's* usual state of residence, which is caused by the use of a motor vehicle insured and normally based in an *EEA State*.
- (2) The *rules* and *guidance* at *ICOB 7.6.1R* to *ICOB 7.6.10R* are not intended to, and do not, restrict any rights which the *injured party*, or its *motor vehicle liability insurer*, or any other *insurer* acting on its behalf, may have and which would enable any of them to begin legal proceedings against the *person* causing the accident or that *person's*, or the motor vehicle's, *insurers*.
- 7.7 Record keeping
- 7.7.1 R An *insurer* must make and retain for the duration of the *claim* and for a minimum of three years after it has been settled or rejected, the following information in relation to each *claim* made against a *policy* issued by it or handled by it:
- (1) details of the *claim*;

- (2) **the date the *claim* was settled or rejected and details of settlement or rejection including information relevant to the basis for the settlement or rejection.**



## ICOB 8

### Distance non-investment mediation contracts with retail customers

- 8.1 Application and purpose**
- Application: who? and what?**
- 8.1.1 R This chapter applies to an *insurance intermediary* in relation to a *distance non-investment mediation contract* with a *retail customer*.**
- Purpose**
- 8.1.2 G The purpose of *ICOB 8* is to set out the *rules* that apply in relation to a *distance non-investment mediation contract*.
- 8.1.3 G This chapter implements articles 3, 5, 6, 7 and 9 of the *DMD* for *distance non-investment mediation contracts* with *retail customers*.
- 8.1.4 G As *ICOB 1.7.3G(4)* indicates, the *FSA* expects the requirements set out in *ICOB 8* to be relevant only in a small minority of cases.
- 8.2 General rules**
- 8.2.1 R The provisions of *ICOB 2* apply in relation to a *distance non-investment mediation contract*.**
- 8.3 Disclosure requirements**
- 8.3.1 R An *insurance intermediary* must provide a *retail customer* with:**
- (1) the information in *ICOB 8.3.3R*; and**
- (2) the full terms of the *distance non-investment mediation contract*;**
- in a *durable medium* in good time before the conclusion of the *distance non-investment mediation contract*, unless an exemption in *ICOB 8.3.6R* applies or the information has already been provided under the *rules* in *ICOB 4*.**
- 8.3.2 G For the purposes of *ICOB 8.3.1R*, information will be provided 'in good time' if provided in sufficient time to enable the *retail customer* to consider properly the services on offer.

**8.3.3 R Table: Status disclosure requirements for distance non-investment mediation contracts**

This table belongs to *ICOB 8.3.1R(1)*.

1.	The name and address of the <i>insurance intermediary</i> , and his main business.
2.	Where relevant, the name and address of the representative of the <i>insurance intermediary</i> established in the <i>retail customer's EEA State</i> of residence.
3.	Where the <i>retail customer's</i> dealings are with any professional other than the <i>insurance intermediary</i> , the name and address of the professional and the capacity in which he is acting with respect to the <i>retail customer</i> .
4.	The <i>insurance intermediary's</i> statutory status (in accordance with <i>GEN 4 Ann 1R</i> (Statutory status disclosure)), and that this can be checked on the <i>FSA's Register</i> by visiting the <i>FSA's</i> website <a href="http://www.fsa.gov.uk/register">http://www.fsa.gov.uk/register</a> or by contacting the <i>FSA</i> on 0845 606 1234.
5.	A description of the main characteristics of the <i>distance non-investment mediation contract</i> .
6.	The total price to be paid by the <i>retail customer</i> , including all related <i>fees</i> , charges and expenses, and all taxes paid via the <i>insurance intermediary</i> (or, where an exact price cannot be indicated, the basis for the calculation, enabling the <i>retail customer</i> to verify it).
7.	The possibility that other taxes, costs or both may exist which are not paid through or imposed by the <i>insurance intermediary</i> .
8.	Any limitations of the period for which the information provided is valid.
9.	The arrangements for payment and performance.
10.	If such an additional cost is charged, the specific additional cost of using the <i>means of distance communication</i> .
11.	The existence or absence of a right to cancel in accordance with <i>ICOB 6.2.1R</i> , and where there is such a right: <ul style="list-style-type: none"> <li>(a) the duration of the cancellation period in accordance with <i>ICOB 6.2.2R</i>;</li> <li>(b) the conditions for exercising the right to cancel, including</li> </ul>

	<p>information on the amount which the <i>retail customer</i> may be required to pay, in accordance with <i>ICOB 6.3 to ICOB 6.4</i>;</p> <p>(c) the consequences of not exercising the right to cancel; and</p> <p>(d) how the right to cancel may be exercised, including the address to which the cancellation notice should be sent.</p>
12.	The minimum duration of the <i>distance non-investment mediation contract</i> .
13.	Information on any rights the <i>insurance intermediary</i> or the <i>retail customer</i> may have to terminate the contract early or unilaterally, including any penalties imposed by the contract in such cases.
14.	<p>Details of:</p> <p>(a) the <i>EEA State</i> or <i>States</i> whose laws are taken by the <i>insurance intermediary</i> as a basis for the establishment of relations with the <i>retail customer</i> prior to the conclusion of the <i>distance non-investment mediation contract</i>;</p> <p>(b) any contractual clause on law applicable to the <i>distance non-investment mediation contract</i>, any competent court, or both; and</p> <p>(c) the language in which the contract is supplied, and in which the <i>insurance intermediary</i> will communicate during the duration of the <i>distance non-investment mediation contract</i>.</p>
15.	The information contained in <i>ICOB 4.2.8R(8) and (9)</i> on complaints and compensation that applies in respect of <i>retail customers</i> .

- 8.3.4 G A description of the main characteristics of a *distance non-investment mediation contract* (*ICOB 8.3.3R(5)*) includes the duration for which that service or services will be provided and the type of services offered. Examples include *arranging* a sale, *advising*, handling mid-term adjustments and assisting in the making of a *claim*.
- 8.3.5 R All information provided to a *retail customer* in accordance with *ICOB 8.3.1R* must be in English, unless the *customer* requests it to be, and the *firm* agrees to it being, in another language.
- 8.3.6 R The following exemptions from *ICOB 8.3.1R* apply:
- (1) Exemption: telephone sales

- (a) This exemption applies if the service is being provided on the telephone and the *retail customer* wishes to enter into a *distance non-investment mediation contract*.
- (b) If the *retail customer* gives his explicit consent to receiving only limited disclosure, the *insurance intermediary* must, prior to the conclusion of the *distance non-investment mediation contract* on the telephone, provide the *retail customer* with the following information:
  - (i) the identity of the *person* in contact with the *retail customer* and his link with the *insurance intermediary*;
  - (ii) the information required by *ICOB 8.3.3R(5), (6), (7) and (11)*; and
  - (iii) that other information is available on request, and the nature of that information.
- (c) Where (b) applies, the *insurance intermediary* must provide the information required by *ICOB 8.3.1R* in a *durable medium* immediately after the conclusion of the *distance non-investment mediation contract*.

**(2) Exemption: certain other means of distance communication**

This exemption applies if the contract is concluded at the *retail customer's* request using a *means of distance communication* (other than telephone) which does not enable provision of the information referred to in *ICOB 8.3.1R* in a *durable medium* before the conclusion of the contract. In that case, the *insurance intermediary* does not need to provide the information in *ICOB 8.3.1R* before conclusion of the contract but must provide it to the *retail customer* in a *durable medium* immediately after the conclusion of the *distance non-investment mediation contract*.

**(3) Exemption: successive operations or separate operations of the same nature under an initial service agreement**

This exemption applies if the *insurance intermediary* has an initial service agreement with the *retail customer* and the contract is in relation to a successive operation or a separate operation of the same nature under that agreement. In this case, the information referred to in *ICOB 8.3.1R* applies to the initial service agreement and not to the successive operations or separate operations of the same nature.

**(4) Exemption: other successive or separate operations**

This exemption applies if:

- (a) the *insurance intermediary* has no initial service agreement with the *retail customer*; and
- (b) the *insurance intermediary* has performed an operation with the *retail customer* within the last year; and
- (c) the *distance non-investment mediation contract* is in relation to a successive operation or separate operation of the same nature.

#### 8.4 Unsolicited services

8.4.1 R Unless *ICOB 8.4.2R* applies, an *insurance intermediary* must not in relation to a *distance non-investment mediation contract*:

- (1) *advise on, arrange, enter into, renew, carry out or assist in the administration and performance* of such a contract for a *retail customer* without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or
- (2) enforce any obligation against a *retail customer* in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.

8.4.2 R *ICOB 8.4.1R* does not prevent an *insurance intermediary* from exercising any right that he may have, by contract or otherwise, to *renew a distance non-investment mediation contract* with a *retail customer* without any request made by or on behalf of that *retail customer* prior to the *renewal* of the contract.

8.4.3 G (1) Where the payment for the contract is made by regular instalments (for example, by direct debit), the effect of *ICOB 8.4.2R* is that an *insurance intermediary* will be required to seek the *retail customer's* consent on *renewal* to continue to provide mediation services only if the contract does not give him the right to do so without further reference to the *retail customer*.

(2) The prior consent of the *retail customer* can either be express or deduced from the circumstances of the case (for instance, by the *retail customer* providing an updated direct debit mandate to the *firm*).

#### 8.5 Cancellation requirements

8.5.1 R The provisions of *ICOB 6 (Cancellation)* apply in respect of a *distance non-investment mediation contract* with a *retail customer* as they do in respect of a *general insurance contract* concluded by *distance means*, with the amendments listed in *ICOB 8.5.2R*.

8.5.2 R Table of amended cross-references to rules in ICOB 6

This table belongs to *ICOB 8.5.1R*.

<b>Rule or guidance</b>	<b>Reference in rule or guidance</b>	<b>To be read as a reference to:</b>
<i>ICOB 6.1.10G</i>	<i>ICOB 5.3.12R</i>	<i>ICOB 8.3.3R(11)</i>
<i>ICOB 6.2.5R(3)</i>	<i>ICOB 5.3.4R, ICOB 5.3.6R(1) or ICOB 5.3.8R</i>	<i>ICOB 8.3.1R(1) and (2), ICOB 8.3.6R(1)(c) and ICOB 8.3.6R(2)</i>
<i>ICOB 6.2.7G</i>	<i>ICOB 5.3.4R, ICOB 5.3.6R(1) or ICOB 5.3.8R</i>	<i>ICOB 8.3.1R(1) and (2), ICOB 8.3.6R(1)(c) and ICOB 8.3.6R(2)</i>
<i>ICOB 6.2.8R</i>	<i>ICOB 5.3.4, ICOB 5.3.6R(1) or ICOB 5.3.8R</i>	<i>ICOB 8.3.1R(1) and (2), ICOB 8.3.6R(1)(c) and ICOB 8.3.6R(2)</i>
<i>ICOB 6.2.9R</i>	<i>ICOB 5.3.12R</i>	<i>ICOB 8.3.3R(11)</i>
<i>ICOB 6.3.1R</i>	<i>ICOB 5.3.12R</i>	<i>ICOB 8.3.3R(11)</i>

8.5.3 G The effect of *ICOB 8.5.1R* is that, among other things, the *retail customer* will have a 14 *day* period within which he may cancel the contract from the *day* the contract is concluded or the *day* on which he receives the contractual terms and conditions and information in a *durable medium* in accordance with *ICOB 8.3.1R*, whichever is the later.

## Insurance: Conduct of Business

### Schedule 1

#### Record keeping requirements

G

- 1 The aim of the *guidance* in the following table is to give the reader a quick overall view of the relevant record-keeping requirements.
- 2 It is not a complete statement of those requirements and should not be relied on as if it were.
- 3 Table

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
ICOB 4.4.7R	<i>Personal recommendation to customer</i>	Explanation of why the <i>personal recommendation</i> is suitable for the <i>customer's</i> demands and needs	The date on which <i>personal recommendation</i> is made	Three years
ICOB 5.7.1R	<i>Policy summary</i>	As set out in ICOB 5.5.5R	The date on which <i>policy summary</i> is provided to the <i>customer</i>	Three years
ICOB 5.7.1R	<i>Policy document</i>	All the contractual terms and conditions	The date on which <i>policy document</i> is provided to the <i>customer</i>	Three years
ICOB 7.7.1R	<i>Claims information</i>	Details of <i>claim</i> , the date on which the <i>claim</i> was settled or rejected and details of settlement or rejection including information relevant to the basis for settling or rejecting the <i>claim</i>	The date on which <i>claim</i> is settled or rejected.	Three years

## **Insurance: Conduct of Business**

### **Schedule 2**

#### **Notification requirements**

G

- 1 There are no notification requirements in *ICOB*.



**Insurance: Conduct of Business**

**Schedule 3**

**Fees and other required payments**

G

1 There are no requirements for fees or other payments in *ICOB*.

## Insurance: Conduct of Business

### Schedule 4

#### Powers exercised

1 Table G

The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the *rules* in *ICOB*:

section 138 (General rule-making power)

section 139(4) (Miscellaneous ancillary matters)

section 145 (Financial promotion rules)

section 149 (Evidential provisions)

section 156 (General supplementary powers)

regulation 2 of the Financial Services and Markets Act 2000 (Fourth Motor Insurance Directive) Regulations 2002 (SI 2002/2706).

The following powers in the *Act* have been exercised by the *FSA* to give the *guidance* in *ICOB*:

section 157(1) (Guidance).

## Insurance: Conduct of Business

### Schedule 5

#### Rights of action for damages

G

- 1 The table below sets out the *rules* in *ICOB* contravention of which by an *authorised person* may be actionable under section 150 of the *Act* (Actions for damages) by a *person* who suffers loss as a result of the contravention.
- 2 If a "yes" appears in the column headed "For private person?", the *rule* may be actionable by a *private person* under section 150 (or in certain circumstances, his fiduciary or representative; see article 6(2) of the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001/2256)). A "yes" in the column headed "Removed?" indicates that the *FSA* has removed the right of action under section 150(2) of the *Act*. If so, a reference to the *rule* in which it is removed is also given.
- 3 The column headed "For other person?" indicates whether the *rule* may be actionable by a *person* other than a *private person* (or his fiduciary or representative) under article 6(2) and 6(3) of those Regulations. If so, an indication of the type of *person* by whom the *rule* may be actionable is given.
- 4 Table

Rule	Right of action under section 150			
	For private person?	Removed?	For other person?	
All <i>rules</i> in <i>ICOB</i> with the status letter "E"	No	No	No	
Any <i>rule</i> in <i>ICOB</i> which prohibits an <i>authorised person</i> from seeking to make provision excluding or restricting any duty or liability	Yes	No	Yes	Any other <i>person</i>
<i>ICOB</i> 7.6.9R	Yes	No	Yes	Any other <i>person</i>
All other <i>rules</i> in <i>ICOB</i>	Yes	No	No	

## **Insurance: Conduct of Business**

### **Schedule 6**

#### **Rules that can be waived**

G

The *rules* in *ICOB* may be *waived* by the *FSA* under section 148 of the *Act* (Modification or waiver of rules). However, if the *rules* incorporate requirements laid down in European directives, it will not be possible for the *FSA* to grant a *waiver* that would be incompatible with the *United Kingdom's* responsibilities under those directives. It therefore follows that if a *rule* in *ICOB* contains provisions which derive partly from a directive, and partly not, the *FSA* will be able to consider a *waiver* of the latter requirements only, unless the directive provisions are optional rather than mandatory.

**CONDUCT OF BUSINESS SOURCEBOOK (CONSEQUENTIAL  
AMENDMENTS ON INTRODUCTION OF ICOB) INSTRUMENT 2004**

**Powers exercised**

- A The Financial Services Authority makes this instrument in the exercise of the powers and related provisions in or under:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 139(1) and (4) (Miscellaneous ancillary matters);
    - (c) section 145 (Financial promotion rules);
    - (d) section 147 (Control of information rules);
    - (e) section 156 (General supplementary powers);
    - (f) section 157(1) (Guidance); and
    - (g) section 238(5) (Restrictions on promotion);
  - (2) regulation 2 of the Financial Services and Markets Act 2000 (Fourth Motor Insurance Directive) Regulations 2002 (SI 2002/2706).
- B The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C This instrument comes into force on 14 January 2005.

**Amendments to the Conduct of Business sourcebook**

- D COB is amended in accordance with the Annex to this instrument.

**Citation**

- E This instrument may be cited as the Conduct of Business Sourcebook (Consequential Amendments on Introduction of ICOB) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex

In this Annex, underlining indicates new text and striking through indicates deleted text.

### 1.2 General application: who?

1.2.1 R *COB* applies to every *firm* in respect of the activities set out in *COB* 1.3.1R, except that:

...

1.2.1A G If a *firm* engages in *insurance mediation activities for non-investment insurance contracts*, *ICOB* applies and *COB* does not apply.

...

### 1.3 General application: what?

1.3.1 R *COB* applies to *firms* with respect to the carrying on of:

(1) all *regulated activities* except:

(a) *regulated mortgage activities*; or

(b) to the extent that a provision of *COB* provides for a narrower application; or ~~and~~

(c) *insurance mediation activities in connection with non-investment insurance contracts*; and

(2) *unregulated activities* to the extent specified in any provision of *COB*.

1.3.2 G (1) ...

(2) Most of *COB* applies in relation to *regulated activities*, conducted by *firms*, which fall within the definition of *designated investment business*. In relation to *deposits*, ~~*pure protection contracts*~~ and ~~*general insurance contracts*~~, *COB* has only limited application.

...

(8) *ICOB* applies to a *firm* in relation to *insurance mediation activities in connection with non-investment insurance contracts*.

...

1.4 General application: where?

...

~~Long term insurance business~~ Life policies

- 1.4.7 R In addition to the situations in *COB 1.4.2R* and *COB 1.4.3R*, *COB 6* (Product disclosure and the customer's right to cancel or withdraw), other than *COB 6.3* (Post-sale confirmation: life policies) and *COB 6.9* (With-profits guides), applies in relation to *long-term insurance business life policies*<sup>1</sup> if the *habitual residence* of the *client* is in the *United Kingdom*.

General insurance business

- 1.4.8 R ~~[Deleted] In addition to the situations in *COB 1.4.2R* and *COB 1.4.3R*, *COB 6.8* (Insurance contracts: life and general) applies in relation to *general insurance business* if the *State of the risk* is the *United Kingdom*.~~

...

- 3.2 Application: what?

...

Financial promotions for deposits and contracts of insurance which are not life policies, pure protection contracts which are long-term care insurance contracts and certain reinsurance contracts

- 3.2.3 R To the extent that a *financial promotion* relates to ~~one or more of the following~~:
- (1) a *deposit*; or
  - (2) ~~a *general insurance contract*, *pure protection contract* which is a *long-term care insurance contract* or reinsurance contract covering a *person* against all or part of his loss in relation only to an obligation taken on by him under a *long-term insurance contract* which is not a *non-investment insurance contract*;~~
- only *COB 3.1* to *COB 3.5* and *COB 3.8.4R* to *COB 3.8.6G* and *COB 3.14* apply, unless the *financial promotion* relates to a *cash deposit ISA* in which case *COB 3.9.6R(1)* and *COB 3.9.8R* also apply.

Financial promotions for non-investment insurance contracts

- 3.2.3B R This chapter does not apply to a *firm* to the extent that a *financial promotion* is in respect of a *non-investment insurance contract* (but see *ICOB 3* (Financial Promotion)).

...

- 3.8 Form and content of financial promotions

...

---

<sup>1</sup> The current definition of life policy does not include long-term care insurance. However we are consulting on an amendment to the definition which would include long-term care insurance in CP200.

Non-real time financial promotions: guidance for deposits, ~~general insurance~~ and pure protection policies which are long-term care insurance contracts

3.8.6 G When designing *non-real time financial promotions* relating to *deposits*, ~~*general insurance contracts*~~ or *pure protection contracts* which are *long-term care insurance contracts* with a view to complying with the general requirements of COB 3.8.4R, *firms* may find it helpful to take account of:

- (1) (for *deposits*) the British Bankers' Association/Building Societies Association Code of Conduct for the Advertising of Interest Bearing Accounts;
- (2) ~~[Deleted] (for *general insurance contracts*) the General Insurance Standards Council Code;~~
- (3) (for *pure protection contracts* which are *long-term care insurance contracts*) the ABI Life Insurance (Non-Investment Business) Selling Code of Practice.

...

3.9 Direct offer financial promotions

...

3.9.3 G Table: Location of the provisions applicable to direct offer financial promotions  
This table belongs to COB 3.9.2G.

(1)	Exemptions for <i>deposits</i> , <del><i>general insurance contracts</i></del> , <i>pure protection contracts</i> <u>which are <i>long-term care insurance contracts</i></u> and certain reinsurance contracts	COB 3.9.4G
...	...	...

Exemptions

3.9.4 G *Firms* are reminded that under COB 3.2.3R:

- (1) COB 3.9 does not apply to a *direct offer financial promotion* relating to:
  - (a) a *deposit* (except a *cash deposit ISA*); or
  - (b) a ~~*general insurance contract*~~, *pure protection contract* which is a *long-term care insurance contract* or certain reinsurance contracts; and

...



COB 3 Annex 1

An overview of some of the main exemptions contained in the Financial Promotion Order G

...

1 Table

This annex belongs to *COB 3.2.7G(2)* and summarises some of the main exemptions in the *Financial Promotion Order*. It is not an exhaustive list and does not seek to replace the Order itself.....

References to articles are to articles of the *Financial Promotion Order* and to paragraphs are to paragraphs of schedule 1 to the *Financial Promotion Order*. For non-investment insurance contracts, firms should refer to *ICOB*.

....

4.1 Client classification

Application

4.1.1 R (1) ...

(2) For the purposes of *COB* only, the following provisions in *COB 4.1* also apply to a *firm* intending to carry on, or carrying on, any other *regulated activity* to which *COB* applies:

...

...

Purpose

4.1.3 G (1) ...

(2) Some of the *rules* in *COB* relating to activities other than *designated investment business* are disapplied if the activity is carried on with or for a *market counterparty* rather than a *customer*, for example *rules* in *COB 6.8* (*Insurance contracts: life and general policies*). For *guidance* on how a *firm* carrying on these other activities may approach *client* classification, see *PRIN 1.2.4 G* (*Classification: other activities*).

...

6.7 Cancellation and withdrawal

Application

6.7.1 R COB 6.7 applies to:

- (1) a product provider except when providing a non-investment insurance contract;
- (2) an insurer which provides pure protection contracts which are long-term care insurance contracts;

...

6.7.2 G The firms in COB 6.7.1R (except those in COB 6.7.1R(3)) are *product providers, insurers, deposit-taking firms or stakeholder pension scheme operators*, that is, the firms responsible for issuing *life policies, selling units, issuing long-term insurance contracts other than non-investment insurance contracts, accepting deposits for ISAs,* or acting as operators of *stakeholder pension schemes*.

...

6.7.5 G Table Cancellable investment agreements.

This table belongs to COB 6.7.4G.

Cancellable investment agreements			
	Post-sale right to cancel?	Pre-sale right to withdraw?	Maximum period of reflection
A. Agreements where the right arises regardless of whether advice is given			
...			
pension contract	...		
<i>pure protection contract which is a long-term care insurance contract</i>	Yes	No	14 days <sup>2</sup>
...			

...

6.7.15 R Table: Cancellable investment agreements – life

This table belongs to *COB 6.7.7R(1)*.

Cancellable investment agreements	
Investment agreements for a long-term insurance contract for which an individual customer has:	
Column 1	Column 2
a right to cancel under <i>COB 6.7.7R(1)</i> (subject to column 2)	...
...	...
<u>C. Pure protection contract which is a long-term care insurance contract.</u>	...
...	...
	<del>9. Pure protection contract effected by the trustees of an occupational pension scheme, an employer or a partnership to secure benefits for employees or the partners in the partnership.</del>

6.7.16 R Table: Notes to cancellable investment agreements – life

This table belongs to *COB 6.7.15R*.

Notes to <i>COB 6.7.15R</i> :	
...	...
...	

Notes to COB 6.7.15R:

2. Multiple agreements: Where a *customer* enters into a set of *investment agreements* at the same time (for example, the different components held within a *maxi-ISA* and with the same *firm* (or another *person* in the same *marketing group* as that *firm*)), and that set is being purchased to fulfil one investment objective of the *customer*, the *firm* may treat the multiple agreements as being one agreement for the purposes of *COB 6.7*. But if it does so, the *firm* must ensure that the *customer* retains the right to cancel each *investment agreement* separately. See also *COB 6.7.37R* in relation to a *maxi-ISA*. This note applies also to a group of life policies ~~contracts of insurance, for example, term assurance~~ contracts which have been established as part of a specific marketing arrangement. Such an arrangement may not have an investment objective. The cancellation rights for any non-investment insurance contracts are set out in *ICOB 6*.

...

...

...

6.8 Insurance contracts: life and ~~general~~ policies

Application

6.8.1 R *COB 6.8* applies to a *firm* which *effects* or *carries out* ~~pure protection contracts, life policies or general insurance contracts.~~

Purpose

6.8.2 G (1) *Principle 7* (Communications with clients) requires a *firm* to pay due regard to the information needs of its *clients*. This section reinforces *Principle 7* by requiring certain information to be provided to a *client* before a ~~pure protection contract or general insurance contract~~ is entered into. ~~Certain information must also be provided~~ on a continuing basis to a *client* with a ~~pure protection contract or life policy~~. (*COB 6.1* to *COB 6.5* deal with pre-sale information for *life policies*).

(2) This section implements certain requirements of the ~~Fourth Motor Insurance and the Third Life and Non-Life Directives~~.

(3) For ~~general non-investment insurance contracts~~, firms should refer to *ICOB* ~~may find it helpful to take account of the requirements issued by the General Insurance Standards Council ("GISC"). The provisions in this section relating to~~

~~general insurance contracts are broadly in line with those requirements.~~

~~Pure protection contracts : Information to be provided before the contract is made~~

- 6.8.3 R ~~[Deleted]A firm must ensure that, before entering into a pure protection contract with a client, it provides the client with the information specified in COB 6.5.49R, unless, at the time of application, the client, other than an EEA ECA recipient, is habitually resident:~~
- ~~(1) in an EEA State other than the United Kingdom; or~~
  - ~~(2) outside the EEA and he is not present in the United Kingdom.~~
- 6.8.4 R ~~[Deleted]The information required by COB 6.8.3R must be:~~
- ~~(1) provided to the customer either by the firm itself or by an intermediary authorised by the firm to act on its behalf; and~~
  - ~~(2) in English, unless the customer requests it to be, and the firm agrees to it being, in another language.~~

~~Pure protection contracts and Life policies: Information to be provided during the term of the contract~~

...

- 6.8.7 R ~~If during the term of a pure protection contract or life policy entered into on or after 1 July 1994 there is any proposed change in the information referred to in COB 6.5.49R items (1) to (12), the long-term insurer must inform the policyholder of the effect of the change before the change is made.~~
- 6.8.8 R ~~If a pure protection contract or life policy entered into on or after 1 July 1994 provides for the payment of bonuses and the amounts of bonuses are unspecified, the long-term insurer must, in every calendar year except the first, either:~~

...

...

~~General insurance contracts: Information required to be provided before the contract is made~~

- 6.8.11 G ~~[Deleted]COB 6.8.12R and COB 6.8.13R cover information to be provided before the sale of a general insurance contract. They contain no requirements for information during the term of the contract.~~

- 6.8.12 R ~~[Deleted] Before entering into a *general insurance contract* with an individual when the *United Kingdom* is the *State of the risk*, or the individual is an *EEA ECA recipient*, a *firm* must, subject to *COB 6.8.13* provide the individual with:~~
- ~~(1) details of its complaints procedure including, where appropriate, the existence of a complaints body, making it clear that its existence is without prejudice to the *policyholder's* right to take legal proceedings; and~~
  - ~~(2) a statement whether the *firm* or *policyholder* is entitled to choose the law applicable to the contract and, if so, the law which the *firm* proposes to choose.~~
- 6.8.13 R ~~[Deleted] *COB 6.8.12R* does not apply if the contract has been submitted to the *firm* on behalf of a *customer* by an intermediary and:~~
- ~~(1) the intermediary is a member of the General Insurance Standards Council; or~~
  - ~~(2) the *firm* has taken reasonable steps to determine that the intermediary has provided the information required by *COB 6.8.12R*.~~
- 6.8.14 G ~~[Deleted] Situations for information delivery will differ depending on the channels used. For example, leaflets will be sufficient at point of sale. For telephone sales the information may be given orally but then must be followed up in writing within five *business days* (see *COB 6.8.15R(2)*).~~

...

- 6.8.17 R Where a *pure protection contract*, *life policy* or *general insurance contract* is effected jointly, the information required by ~~*COB 6.8.3R*, *COB 6.8.7R*, or *COB 6.8.8R*~~, or *COB 6.8.12R* may be sent to the first named *customer*.

#### Record keeping

- 6.8.18 R A *firm* must make an adequate record of information provided to a *customer* under *COB 6.8* and retain that record for a minimum period after the information is provided of:
- ~~(1) six years in the case of a *pure protection contract* or *life policy*;~~  
or
  - ~~(2) three years in the case of a *general insurance contract*.~~

#### ~~Motor Vehicle Liability Insurers: claims representatives~~

- 6.8.19 G (1) ~~[Deleted] Under *threshold condition 2A* (Appointment of claims representatives), if it appears to the *FSA* that any *person* is seeking to carry on, or carrying on, *motor vehicle liability*~~

*insurance business, that person must have a claims representative in each EEA State other than the United Kingdom.*

- (2) *If any person carrying on motor vehicle liability insurance business becomes aware, or has information which reasonably suggests, that that person has failed to satisfy, may have failed to satisfy or may not in the foreseeable future be able to satisfy, threshold condition 2A (or any threshold condition), that person must notify the FSA immediately (see SUP 15.3.1R).*

6.8.20 R ~~[Deleted]~~The Society must ensure that no member carries on motor vehicle liability insurance business at Lloyd's unless a claims representative has been appointed to act for that member in each EEA State other than the United Kingdom, with responsibility for handling and settling claims arising from an accident in the cases referred to in article 1 of the Fourth Motor Insurance Directive.

- 6.8.21 R (1) ~~[Deleted]~~When a motor vehicle liability insurer appoints a claims representative, it must give the MHC and each other information centre the claims representative's name, business address, telephone number and effective date of appointment within ten business days of that appointment being made.
- (2) *If the information at (1) changes in any material way, the motor vehicle liability insurer must give the MHC and each other information centre details of that change within ten business days of that change.*

- 6.8.22 R ~~[Deleted]~~A motor vehicle liability insurer must ensure that each claims representative is:
- (1) resident or established in the EEA State for which it is appointed;
  - (2) capable of examining cases in the official language or languages of the EEA State of residence of the injured party;
  - (3) responsible for, and has sufficient delegated authority from the motor vehicle liability insurer for which it is appointed, to be able to:
    - (a) handle and settle;
    - (b) collect all information, and take all measures, reasonably necessary to negotiate a settlement of; and
    - (c) represent, or arrange appropriate representation for, the motor vehicle liability insurer (whether in negotiations, in court or otherwise) in relation to;
- claims, arising from an accident occurring in an EEA State other than the EEA State of residence of the injured party;*

involving the use of a vehicle insured and normally based in an *EEA State*.

- 6.8.23 G ~~[Deleted] COB 6.8.22R(3) does not prevent a *claims representative* from seeking additional authority or instructions from a *motor vehicle liability insurer*, if its existing authority or instructions are insufficient to allow it to handle and settle a claim. However, it does prevent a *claims representative* from purporting to decline to deal with, or transfer responsibility for, claims properly referred to that *claims representative* by an *injured party*, or an *injured party's* representative.~~
- 6.8.24 G ~~[Deleted] Nothing in the *rules and guidance* at COB 6.8.19G to COB 6.8.29G prevents, or is intended to prevent:~~
- ~~(1) a *motor vehicle liability insurer* from appointing more than one *claims representative* in one, or more than one, *EEA State*; or~~
  - ~~(2) a *claims representative* from acting for more than one *insurer* or *member*; or~~
  - ~~(3) a representative, appointed by a *motor vehicle liability insurer* under SUP 13.5.2R or regulation 3(d) of the *EEA Passport Rights Regulations*, from acting as that *motor vehicle liability insurer's claims representative* as well.~~
- 6.8.25 G ~~[Deleted] The appointment of a *claims representative* does not in itself constitute the opening of a branch or the creation of an establishment (see article 4(8) of the *Fourth Motor Insurance Directive*).~~

Motor Vehicle Liability Insurers: claims handling

- 6.8.26 R (1) ~~[Deleted] Within three months of receipt of a claim for damages from an *injured party*, or his representative, the *motor vehicle liability insurer* must (directly, or through a *claims representative*):~~
- ~~(a) make a reasoned offer of settlement, if liability is admitted and damages have been fully quantified; or~~
  - ~~(b) provide a reasoned reply to the points made in the *injured party's* claim, if liability is denied, or not admitted, or the claim for damages has not been fully quantified.~~
- (2) If liability is initially denied, or not admitted: within three months of any subsequent admission of liability, the *motor vehicle liability insurer* must (directly, or through a *claims representative*) make a reasoned offer of settlement, if, by that time, the relevant claim for damages has been fully quantified.
- (3) If an *injured party's* claim for damages is not fully quantified when it is first made: within three months of the subsequent



receipt of a fully quantified claim for damages, the *motor vehicle liability insurer* must (directly, or through a *claims representative*) make a reasoned offer of damages, if liability is admitted at that time.

(4) A claim for damages will be fully quantified under (1)(a), (2) or (3) when the *injured party* provides written evidence which substantiates or supports the amounts claimed.

6.8.27 R (1) ~~[Deleted] If the *motor vehicle liability insurer*, or its *claims representative*, does not comply with COB 6.8.26R(1)(a), (2) or (3), the *motor vehicle liability insurer* must pay simple interest on any damages eventually paid, unless interest is awarded by any tribunal which determines the *injured party's* claim.~~

(2) If (1) applies, the amount of interest that the *motor vehicle liability insurer* must pay must be calculated as follows:

(a) the interest calculation period:

(i) begins three months after:

(A) receipt of the claim for damages, if the *motor vehicle liability insurer* or its *claims representative* breaches COB 6.8.26R(1)(a); or

(B) any subsequent admission of liability, if the *motor vehicle liability insurer* or its *claims representative* complies with COB 6.8.26R(1)(a) but breaches COB 6.8.26R(2); or

(C) the subsequent receipt of a fully quantified claim for damages, if the *motor vehicle liability insurer* or its *claims representative* complies with COB 6.8.26R(1)(a) and (2) but breaches COB 6.8.26R(3); and

(ii) ends on the date when the *motor vehicle liability insurer* pays compensation to the *injured party*, or the *injured party's* authorised representative;

(b) the interest rate to be applied throughout the period in (a) is the Bank of England's base rate (from time to time), plus four per cent.

6.8.28 R ~~[Deleted] A *motor vehicle liability insurer* will be taken to have received a claim, or a fully quantified claim, for damages when that claim, or fully quantified claim, for damages is delivered to the *motor vehicle liability insurer*, or a *claims representative*, by any person by any method of delivery which is lawful in the *motor vehicle liability insurer's*, or its *claims representative's*, respective State of residence or establishment.~~

- 6.8.29 G (1) ~~[Deleted] COB 6.8.26R to COB 6.8.28R apply only to claims for damages for loss or injury suffered in, or as a result of, an accident which occurs in an EEA State other than an injured party's usual state of residence, which is caused by the use of a motor vehicle insured and normally based in an EEA State.~~
- (2) ~~COB 6.8.19G to COB 6.8.28R are not intended to, and do not, restrict any rights which the injured party, or its motor vehicle liability insurer, or any other insurer acting on its behalf, may have and which would enable any of them to begin legal proceedings against the person causing the accident or that person's, or the motor vehicle's, insurers.~~

...

12.1 Application

12.1.1 R This chapter applies to a *firm* when it carries on any of the following activities:

(1) ...

...

(4) *communicating or approving a financial promotion* in relation to:

(a) ...

...

(c) *effecting or carrying out contracts of insurance life policies* written at Lloyd's; or

...

...

12.1.15 R Table: This table applies *COB* to *firms* when carrying on the activity to which *COB* 12.1.7R(2) relates except where *ICOB* applies in relation to non-investment insurance contracts.

Chapter	Description	Application
1	...	
...		
6.8	Insurance contracts – life <u>policies</u> and general	Applied

12.1.16 G The tables at *COB* 12.1.17G to *COB* 12.1.21G are provided to help *firms* when carrying on those activities to which this chapter applies locate those ~~*COB*~~-rules that are particularly relevant to their activities. *Firms* should be aware that these tables may not include all *rules*

which apply to an individual *firm* as these will vary depending on the *firm's* particular circumstances and that there may be other *COB-rules* that apply.

...

- 12.1.20 G Table: Location of *rules* of particular relevance to a *firm* managing the underwriting capacity of a Lloyd's *syndicate* as a *managing agent* at Lloyd's.

This table forms part of *COB* 12.1.16G

Chapter	Description
<i>COB</i> 6.7	Cancellation and withdrawal
<i>COB</i> 6.8	Insurance contracts – life <u>policies and general</u>
<i>ICOB</i>	Insurance: Conduct of Business Sourcebook

...

Schedule 1  
Record keeping requirements

...

3 Table

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
COB 6.8.18R(1)	Firm effecting or carrying out pure protection contracts <u>which are life policies</u>	Adequate details of information provided	After information provided	6 years
COB 6.8.18R(2)	Firm effecting or carrying out <u>general insurance contracts</u>	Adequate details of information provided	After information provided	3 years
...				

...

Schedule 4

Powers Exercised

1 Table: G

The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the *rules* in *COB*:

...

Regulation 6(1) of The Open-Ended Investment Companies Regulations 2001  
~~Regulation 2 of the Financial Services and Markets Act 2000 (Fourth Motor Insurance Directive) Regulations 2002 (SI 2002/2706).~~

...

Schedule 5

Rights of action for damages

...

4 Table:

Chapter/ Appendix	Section/ Annex	Paragraph	Right of action under section 150			
			For private person?	Removed ?	For other person?	
...						
		Any <i>rule</i> in <i>COB</i> which is directed at ensuring that transactions in <i>designated investments</i> are not effected with the benefit of unpublished information that, if made public, would be likely to affect the price of that <i>designated investment</i>	Yes	No	Yes	Any other person
		<del>COB 6.8.27R</del>	<del>Yes</del>	<del>No</del>	<del>Yes</del>	<del>Any other person</del>
		All other <i>rules</i> in <i>COB</i>	Yes	No	No	

**INSURANCE: CONDUCT OF BUSINESS SOURCEBOOK (CONSEQUENTIAL  
AMENDMENTS TO THE HANDBOOK) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers and related provisions in or under:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 139(4) (Miscellaneous ancillary matters);
    - (c) section 145 (Financial promotion rules);
    - (d) section 146 (Money laundering rules);
    - (e) section 149 (Evidential provisions);
    - (f) section 150(2) (Actions for damages);
    - (g) section 156 (General supplementary powers);
    - (h) section 157(1) (Guidance); and
    - (i) section 332(1) (Rules in relation to persons to whom the general prohibition does not apply);
  - (2) regulation 3 of the Electronic Commerce Directive (Financial Services and Markets Act) Regulations 2002 (S.I. 2002/1775); and
  - (3) schedule 4 to the General provisions.
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).<sup>1</sup>

**Commencement**

- C. This instrument comes into force as follows:
- (1) the amendments to *MCOB* in Annex D, Part 1 come into force on 31 October 2004;
  - (2) all other amendments come into force on 14 January 2005.

**Amendments to the Handbook**

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<sup>1</sup> The amendments in this instrument take account of the amendments contained in the instrument - Mortgage: Conduct of Business (Consequential Amendments to the Handbook) 2003/72. Those amendments were made on 15 October 2003 and will come into force on 31 October 2004.

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2):

(1)	(2)
Reader's Guide Reader's Short Guide	Annex A
COND	Annex B
GEN	Annex C
MCOB	Annex D, Parts 1 and 2
TC	Annex E
ML	Annex F
AUTH	Annex G
SUP	Annex H
DISP	Annex I
CRED	Annex J
ECO	Annex K
ELM	Annex L
Glossary	Annex M

### **Citation**

- E. This instrument may be cited as the Insurance: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2004.

By Order of the Board  
15 January 2004

Amended by Addendum  
19 October 2004

## Annex A

### Amendments to the Reader's Guide

In this Annex, underlining indicates new text.

...

#### Contents of the Handbook

	Sourcebook or manual	Reference code
Business Standards	...	
	Conduct of Business	COB
	<u>Insurance: Conduct of Business</u>	<u>ICOB</u>
	Mortgages: Conduct of Business	MCOB
...		

### Amendments to the Reader's Short Guide

...

#### Contents of the Handbook

	Sourcebook or manual	Reference code
Business Standards	...	
	Conduct of Business	COB
	<u>Insurance: Conduct of Business</u>	<u>ICOB</u>
	Mortgages: Conduct of Business	MCOB
...		

## Annex B

### Amendments to COND

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 2.2A.3 G *Rules and guidance concerning a motor vehicle liability insurer's obligations in relation to the appointment of its claims representatives, and the responsibilities and duties that the motor vehicle liability insurer must give to, or impose on, its claims representatives are set out in ~~COB 6.8.19G to COB 6.8.29G~~ ICOB 7.6.*



## Annex C

### Amendments to GEN

In this Annex, underlining indicates new text and striking through indicates deleted text.

Transitional provisions

...  
3 G Table (2) Transitional provisions applying to *GEN* only

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1	<i>GEN</i> 2.2.7	R	...		
2	<i>GEN</i> 4.3.1	R	<p>(1) For the purpose of <i>GEN</i> 4.3.1R (Disclosure in letters to private customers), a <i>regulated activity</i> does not include a <i>regulated mortgage activity</i> or an <u><i>insurance mediation activity in relation to a non-investment insurance contract.</i></u></p> <p>(2) If a <i>firm</i> in a letter (or electronic equivalent) which it or its <i>employees</i> send to a <i>customer</i>, with a view to or in connection with the <i>firm</i> carrying out a <i>regulated mortgage activity</i> or an <u><i>insurance mediation activity.</i></u> makes a statement about its statutory or regulated status under the <i>Act</i> for carrying on a <i>regulated mortgage activity</i> or <u><i>insurance mediation activity.</i></u> the <i>firm</i> must include the disclosure in <i>GEN</i> 4 Ann 1R.</p>	From 31 October 2004 until 15 July 2005.	Apply in relation to <i>regulated mortgage activities</i> from 31 October 2004 and to <u><i>insurance mediation activities</i></u> from <u>14 January 2005.</u>

3	GEN 4.3.1R	G	<p>(1) Transitional provision 2R defers the application of <i>GEN rules</i> so that a <i>firm</i> need only make one change to its statutory status to reflect the onset of mortgage and non-investment insurance regulation. <u>However, a <i>firm</i> which undertakes other regulated activities will nevertheless need to comply with GEN 4.3.1R in relation to those regulated activities, subject to the transitional provision in GEN TR 2.</u></p> <p>(2) <del>Until 1 August 2005, a</del> A <i>firm</i> may continue to use stationery and similar materials which refer to its membership of self-regulatory schemes superseded by <i>FSA regulation</i>. <del>However, a <i>firm</i> will need to ensure that any such reference is adequately qualified so that the <i>customer</i> is not misled as to the regulatory arrangements in place.</del> <u>In addition, <i>firms</i> undertaking insurance mediation activities in relation to non-investment insurance contracts may wish to take account of the transitional provision in <i>ICOB TR 4</i>.</u></p>	From 31 October 2004 until 15 July 2005.	Apply in relation to regulated mortgage activities from 31 October 2004 and insurance mediation activities from 14 January 2005.
---	------------	---	--	--	--

...

4.2.2 G There are other pre-contract information requirements outside this chapter, including:

...

- (3) ~~for general insurance contracts and pure protection contracts~~ *non-investment insurance contracts*, in ~~COB 6.8 (Insurance contracts: life and general)~~ *ICOB 4* (Advising and selling standards); and *ICOB 5* (Product disclosure);

...  
...

- 4.4.1 R (1) If, in any communication:
- (a) made to a *private customer* or, in the case of a communication relating to non-investment insurance contract, a retail customer,
  - (b) in connection with a *regulated activity* carried on from an establishment of the *firm* (or its *appointed representative*) that is not in the *United Kingdom*;

the *firm* indicates that it is an *authorised person*, it must also, where relevant, and with equal prominence, give the information in (2) in writing.

...  
4.4.2 G *ICOB 4.2.19R contains provisions relating to communications by insurance intermediaries from outside the United Kingdom in connection with non-investment insurance contracts with or for a retail customer. The definition of insurance intermediary includes an insurer when the insurer is carrying on insurance mediation activities.*

## Annex D

### Amendments to MCOB

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being replaced, the place the new text goes is indicated and it is not underlined.

#### Part 1

##### Amendments taking effect on 31 October 2004.

###### Use of intermediaries

- 1.3.6 G The mere fact that an intermediary (acting for the supplier or for the *retail customer*) is involved, does not make the sale of a financial product or service a *distance contract*. There will not be a *distance contract* if there has been simultaneous physical presence of the intermediary and the *retail customer* at some stage in the offer, negotiation and conclusion of the contract, ~~which has been meaningful in terms of the contract which ensues.~~

...

- 4.5 Additional disclosure for distance mortgage mediation contracts with retail customers

- 4.5.1 G (1) There are certain additional disclosure requirements laid down by the *Distance Marketing Directive* that will have to be provided by a *mortgage intermediary* to a *retail customer* prior to the conclusion of a *distance mortgage mediation contract*. The purpose of this section, *MCOB 4.5*, is to set out those additional requirements. *MCOB 4.6* sets out the cancellation rights that apply in relation to a *distance mortgage mediation contract*.
- (2) The *FSA* expects the requirements in *MCOB 4.5* and *MCOB 4.6* to be relevant only in a small minority of cases. Mediation at a distance (see *MCOB 1.3.5G* and *MCOB 1.3.6G*) is unlikely in the mortgage market. *MCOB 4.5* and *MCOB 4.6* will only be relevant if a *mortgage intermediary* enters into a *distance contract* in respect of its *mortgage mediation activities* quite independent of any contractual arrangement with a *retail customer* relating to a particular *regulated mortgage contract*. An example of a *distance mortgage mediation contract* would be a *distance contract* under which a *mortgage intermediary* agreed to review and provide *advice* on a *retail customer's* mortgage needs from time to time.

...

Delete *MCOB 4.5.4R* and *MCOB 4.5.5G* and replace with the following:

Unsolicited services

- 4.5.4 R Unless *MCOB 4.5.5R* applies, a *firm* must not:
- (1) *advise on, arrange, enter into or renew a distance mortgage mediation contract with a retail customer* without a prior request on his part, when the supply of such service includes a request for immediate or deferred payment; or
  - (2) enforce any obligation against a *retail customer* in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.
- 4.5.5 R *MCOB 4.5.4R* does not prevent a *firm* from exercising any right that it may have, by contract or otherwise, to *renew a distance contract with a retail customer* without any request made by or on behalf of that *retail customer* prior to the *renewal* of the contract.

## Part 2

### Amendments taking effect on 14 January 2005

MCOB 1 Ann 4G

	Module	Application
....		
Business Standards	....	
	Conduct of Business Sourcebook, <i>COB</i>	....
	<u>Insurance: Conduct of Business sourcebook, <i>ICOB</i></u>	<u>Does not apply to a <i>firm</i> when <i>entering into or administering a regulated mortgage contract</i> or when <i>communicating or approving a qualifying credit promotion</i>. However, <i>ICOB</i> may apply to any such <i>firm</i> if it also carries on an <i>insurance mediation activity in relation to a non-investment insurance contract or communicates or approves non-investment financial promotions</i>.</u>
	....	

...

4.4.1 R (1) A *firm* must ensure that, on first making contact with a *customer* when it anticipates giving personalised information or *advice* on a *regulated mortgage contract*, it:

...

(c) (unless (2) applies) provides the *customer* with either:

- (i) the initial disclosure document in *MCOB 4 Ann 1R*; or
- (ii) if the *firm* has reasonable grounds to be satisfied that the services which it is likely to provide to the *customer* will, in addition to relating to *regulated mortgage contracts* or *regulated lifetime mortgage contracts*, relate to one or more of *non-investment insurance contracts* or *packaged products* in circumstances where the rules in *MCOB 4 Ann 2R* allow this, the combined initial disclosure document in *MCOB 4 Ann 2R*;

subject to (3) and in a *durable medium*.

This Annex belongs to *MCOB 4.4.1R(1)*.

This specimen covers services in relation to *packaged products, non-investment insurance contracts and regulated mortgage contracts* (including *regulated lifetime mortgage contracts* and home reversion schemes). If the *firm* is only providing services in relation to two types of these products, the parts of the CIDD that are not relevant must be omitted. *Firms* must omit the notes and square brackets that appear in the following CIDD. The CIDD must contain the key facts logo, headings and text in the order shown and in accordance with the notes. [Note 1]

## about our services [Note 2]



Financial Services

[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

### 1 The Financial Services Authority (FSA)

The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

### 2 Whose products do we offer? [Note 6] [Note 7]

#### Investment

- We offer products from the whole market.
- We [can] [Note 8] only offer products from a limited number of companies.

Ask us for a list of the companies and products we offer. [Note 12]

- We [can] [Note 8] only offer [a] [a limited range of the] product[s] from [a single group of companies] [name of single company]. [Note 10(1)] [Note 13]

[or] [Note 10(2)]

We only offer our own products.

Ask us for a list of the products we offer. **[Note 12]**

- We will advise you about group personal pensions.

#### **Insurance**

- We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].

- We [can] **[Note 8]** only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. **[Note 12]**

- We [can] **[Note 8]** only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. **[Note 9] [Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own products for [list the types of *non-investment insurance contracts*].

#### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We offer mortgages from the whole market.

- We [can] **[Note 8]** only offer mortgages from a limited number of lenders.

Ask us for a list of the lenders we offer mortgages from. **[Note 11]**

- We [can] **[Note 8]** only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender]. **[Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own mortgages.

---

### **3 Which service will we provide you with? [Note 6]**

#### **Investment**

- We will advise and make a recommendation for you after we have assessed your needs.

- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

#### **Insurance**



- We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].
- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

#### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

---

#### **4 What will you have to pay us for our services?**

##### **Investment**

- Before we provide you with advice, we will give you our key facts guide to the cost of our services. [Note 15]

##### **Insurance**

- A fee [of £ [ ]]. [Note 16]
- No fee.

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

#### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- No fee. [We will be paid by commission from the [lender/company].] [Note 17]
- A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] mortgage [or home reversion scheme]. [We will also be paid commission from the [lender/company].] [Note 17] [Note 18]

You will receive a key facts illustration when considering a particular [lifetime] mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. [Note 14]

## Refund of fees [Note 19] [Note 14]

If we charge you a fee, and your [lifetime] mortgage [or home reversion scheme] does not go ahead, you will receive:

[Note 20]

- A full refund [if the [lender/company] rejects your application]. [Note 21]
- A refund of £ [ ] [if your application falls through]. [Note 21] [Note 22]
- No refund [if you decide not to proceed]. [Note 21]

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## 5 Who regulates us? [Note 23]

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[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 24] [Note 25] is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. [Note 26]

Our permitted business is [ ]. [Note 27]

[or] [Note 28]

[Name of *appointed representative*] [Notes 3 and 4] is an appointed representative of [name of *firm*] [address of *firm*] [Note 24] [Note 25] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] [Note 27]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

[Home reversion schemes are not regulated by the FSA.] [Note 14]

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## 6 Loans and ownership [Note 29]

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[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.] [Note 29][Note 31][Note 32][Note 33][Note 34]

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## 7 What to do if you have a complaint [Note 23]

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234]. [Note 35]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 36] [Note 37] [The Financial Ombudsman Service does not consider complaints about home reversion schemes.] [Note 14]

---

## 8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 23] [Note 38]

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

### **Investment**

Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.

### **Insurance**

Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.

[or] [Note 39]

For compulsory classes of insurance advising and arranging is covered for 100% of the claim, without any upper limit.

### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

Mortgage advising and arranging is covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000. [Home reversion schemes are not covered by the Financial Services Compensation Scheme.] [Note 14]

Further information about compensation scheme arrangements is available from the FSCS.

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## 9. Group personal pensions [Notes 40, 41 and 42]

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This meeting has been arranged so that we can provide you with [information about] [advice upon whether or not you should join] the Group Personal Pension scheme which your employer has established. You should be aware that we cannot advise upon or recommend any other specific investment products during this meeting.

---

**[Note 43]** Message from the Financial Services Authority

Think carefully about this information before deciding whether you want to go ahead. If you are at all unsure about which lifetime mortgage or home reversion scheme is right for you, you should ask your adviser to make a recommendation.

Please remember that home reversion schemes are not regulated by the FSA.

The following notes do not form part of the CIDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common key facts logo to be used on significant pieces of information directed to *customers*. *ICOB 4.2.6R* sets out the requirements on the use of the key facts logo. A specimen of the key facts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the CIDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

**Section 2: Whose products do we offer?**

**Note 6** – for services in relation to *packaged products* and *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes the *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. For services in relation to *non-investment insurance contracts*, the *firm* must select more than one box if the scope of the service or the type of service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance or if it provides *advice* on some types of contract but not others. In the case where more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the CIDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 7** - if the CIDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with *COB 5*, *ICOB 4.2.8R* note 1(e) and *MCOB 4.3.10R*.

**Note 8** – insert “can” if the *firm's* range of products is determined by any contractual obligation. This does not apply where a *product provider*, *insurer*, lender or company is selling its own products.

**Note 9** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the CIDD. This only needs to be done in relation to the service it is offering a particular *customer*. For example, “we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance”.

**Note 10** – if the *firm* selects this box, it will be offering the products of one provider to the *customer* for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*. If the *firm* does not select this box, then the text must follow that set out in note 13 below.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the lender for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the company for home reversion schemes. For example: "We can only offer products from [name of *product provider*]". For *non-investment insurance contracts* the type of insurance offered should also be included. For example: "We only offer XYZ's household insurance and ABC's motor insurance." If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a mortgage from [name of lender]". If the *firm* does not offer all of the *packaged products* or mortgages or home reversion schemes generally available from that provider, it must insert the words "a limited range of" as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part's trading name, it should use this alternative text.

**Note 11** – for services provided in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes, this sentence may be omitted if the *firm* chooses to list all of the companies it offers products from instead of the text “a limited number of lenders” in the previous line, so long as the *firm* offers all the products generally available from each provider.

**Note 12** – for services provided in relation to *packaged products* the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by ICOB 4.2.14R.

**Note 13** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies" for *packaged products*, "a single insurer" for *non-investment insurance contracts*, "a single lender" for *regulated mortgage contracts* or *regulated lifetime mortgage contracts* and "a single company" for home reversion schemes. For example: "We only offer the products from a single group of companies" should replace the text in the specimen CIDD.

**Note 14** – change “mortgage” to “lifetime mortgage” where the *firm* sells only *regulated lifetime mortgage contracts*. *Firms* must insert the text relating to home reversion schemes and change “mortgage” to “product” and “lender” to “company” if they advise or give personalised information on home reversion schemes in addition to *advising* or giving personalised information on *regulated lifetime mortgage contracts*.

#### **Section 4: What will you have to pay us for our services?**

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate “key facts guide to the costs of services” (i.e. a menu) if they propose to give that *customer advice* on *packaged products*. Where a *firm* is not required to provide that *customer* with a menu because the *firm* does not give *advice* on *packaged products*, the *firm* may omit the part of section 4 of the CIDD that relates to *packaged products*.

**Note 16** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on or arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'.

**Note 17** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer* for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes, it must insert a plain language explanation of this (see specimen for a plain language example).

**Note 18** – insert a plain language description of when any *fees* are payable for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If a *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

**Note 19** – omit this part of the CIDD on ‘Refund of fees’ if the *firm* has indicated that there will be “No fee” for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes.

**Note 20** – *firms* may select as many boxes as appropriate.

**Note 21** – insert a plain language description of the circumstances in which the *fee* for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes is refundable or not refundable as described.

**Note 22** – a *firm* may delete this line if it does not offer a partial refund for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes in any circumstances.

#### **Section 5: Who regulates us?**

**Note 23** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information including the *firm's permitted business*. This section may be omitted for services relating to *non-investment insurance contracts* if the *firm* provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. This section may be omitted for services relating to *regulated mortgage contracts* (including *regulated lifetime mortgage contracts*) and home reversion schemes in accordance with *MCOB 4.4.1R(3)*. If this section is omitted, the other sections of the CIDD must be renumbered accordingly.

**Note 24** – if the *firm's* address on the *FSA Register* differs from that given on the CIDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 25** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 26** - an *incoming EEA firm* will need to modify this section if it chooses to use this CIDD (see *GEN 4 Ann 1R(2)*).

**Note 27** – insert a plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 28** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

## **Section 6: Loans and ownership**

**Note 29** – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the CIDD must be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section must be changed to 'Ownership'.

**Notes 30, 31 and 32** apply only to a *firm advising on, dealing in, or arranging* in relation to *packaged products* for *private customers*.

**Note 30** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 31** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 32** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an

indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

**Notes 33 and 34** apply to an *insurance intermediary* that is not an *insurer* providing services in relation to *non-investment insurance contracts*.

**Note 33** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

**Note 34** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

### **Section 7: What to do if you have a complaint**

**Note 35** – if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 36** – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

**Note 37** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

### **Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 38** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 39** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it must use this alternative text.

### **Section 9: Group personal pensions**

**Note 40** – *firms* should only include section 9 if they intend to give information about, or *advise on*, the opportunity for *employees* to join a *group personal pension scheme* established by their employer. In all other cases it should be omitted entirely.

**Note 41** – the words in square brackets should be omitted or included, as appropriate, depending upon whether the *firm* is *advising employees* whether or not to join a *group personal pension scheme*, or merely providing them with factual information about the scheme.

**Note 42** – although *firms* must not use the occasion of a meeting to discuss a *group personal pension scheme* as an opportunity to give *advice on* other *designated investments*, this does



not preclude the provision of *advice on non-investment insurance contracts, regulated mortgage contracts or regulated lifetime mortgage contracts*. A *firm* may also, when giving *advice on a group personal pension scheme*, suggest that a further meeting be arranged to discuss *designated investments* and if so must provide a further appropriate IDD or CIDD.

**Lifetime mortgage warning**

**Note 43** - This warning box should be added when the *firm* sells *regulated lifetime mortgage contracts* or home reversion schemes or both.

...

8.1.5 G If a *firm* is an *authorised professional firm*, *MCOB* 1.2.10R(3) has the effect that when the *firm* conducts *non-mainstream regulated activities* with a *customer*, *MCOB* 4.4 (Initial disclosure requirements) (as modified by *MCOB* 8) applies. The *firm* is only required to provide the initial disclosure information in *MCOB* 8 Ann 1R or ~~*MCOB*~~ 4 Ann 2R section 7 (What to do if you have a complaint) and section 8 (Are we covered by the Financial Services Compensation Scheme (FSCS)?).

...

8.3.3 R .....

Initial disclosure requirements for <i>packaged products or non-investment insurance contracts</i> (in addition to <i>regulated lifetime mortgage contracts</i> )	<del><i>MCOB</i></del> 4.4.1R(1)(e) and (3)	<del><i>MCOB</i></del> 4 Ann 2R	<del><i>MCOB</i></del> 8 Ann 2R
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...

8.4.1 R If a *firm* gives, or anticipates giving, advice or personalised information on home reversion schemes in addition to *regulated lifetime mortgage contracts*, the initial disclosure information in *MCOB* 4.4.1R and *MCOB* 4.4.7R must be provided in respect of the home reversion schemes, as well as the *regulated lifetime mortgage contracts*, using the text set out in *MCOB* 8 Ann 1R and ~~*MCOB*~~ 4 Ann 2R.

...

***MCOB* 8 Ann 2R Delete annex**

**Amendments to TC**

In this Annex, underlining indicates new text.

2.1.4 R Table Activities to which TC 2 applies

	Activity	Extent of Application
1. <i>Employees</i> engaging in:	...	...
	(r) <u>advising on investments</u> which are <u>non-investment insurance contracts</u> .	3. In relation to <i>advising on investments</i> which are <i>non-investment insurance contracts</i> if the activity is carried on with or for a <u>retail customer</u> (see <u>ICOB</u> ), the whole of <u>TC 2</u> applies, except for <u>TC 2.5</u> , as if in <u>TC 2.2</u> , <u>2.3</u> , <u>2.4</u> and <u>2.7</u> each reference to <i>private customer</i> were a reference to <i>retail customer</i> .
	...	...
2. <i>Employees</i> overseeing on a day-to-day basis:	...	

	Activity	Extent of Application
	(b) safeguarding and administering investments or holding of client money (unless held in the course of carrying on a mortgage mediation activity, <u>or an insurance mediation activity only in relation to a non-investment insurance contract</u> );	

...

- 2.4.2 R (1) A *firm* which permits an *employee* to engage in an activity with or for a *private customer* under supervision must ensure that:
- ~~(1)~~ (a) the *employee* has first passed the relevant regulatory module of an appropriate *approved examination*; and
  - ~~(2)~~ (b) the *firm* has satisfied itself that the *employee* has an adequate level of knowledge and skills to act with or for *private customers* while under supervision.
- (2) (1) (a) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract*.

...

#### Assessing competence

- 2.4.5 R (1) A *firm* must not assess an *employee* as competent to engage in or oversee an activity unless that *employee*:
- ~~(1)~~ (a) has been assessed as competent to apply the knowledge and skills necessary to engage in or oversee the activity without supervision; and
  - ~~(2)~~ (b) has passed each module of the appropriate *approved examination* specified in the annexes to *TC 2*.
- (2) (1)(b) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract*.

## Annex F

### Amendments to ML

In this Annex, underlining indicates new text.

1.1.3 G The scope of this sourcebook is very wide. It includes all *firms* except:

- (1) ....
- (2) those within the exception for *firms* carrying on any insurance mediation activity in relation to a general insurance contract or pure protection contract (see ML 1.1.4R(1A)) or any mortgage mediation activity (see ML 1.1.4R(5)); in this respect, the chapter follows [article [] of the [] [to be added when 2003 Money Laundering Regulations are in final form].

The scope extends to *incoming firms*...

1.1.4 R In this sourcebook, “*relevant regulated activities*” means any *regulated activity* apart from:

- (1) *general insurance business*;
- (1A) *insurance mediation activity in relation to a general insurance contract or pure protection contract*;
- (2) *long-term insurance business* which is outside the *First Life Directive* (and is not otherwise a *relevant regulated activity*);
- (3) ....

## Annex G

### Amendments to AUTH

In this Annex, underlining indicates new text.

- 1.5.3 G As a general guide, all applicants for *Part IV permission* should be familiar with the *threshold conditions (COND)* and the *Principles for Businesses (PRIN)* in the High Level Standards part of the *Handbook*. To complete an application for *Part IV permission*, an applicant will also need to have regard to the following matters:
- (1) ...
  - ...
  - (4) Other regulatory obligations:
    - (a) the detailed regulatory obligations that apply to certain types of *firm* or *regulated activity* in *COB*, *ICOB*, *MCOB*, the Market Conduct sourcebook (*MAR*) and *SUP*;
    - ...

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom.	(2) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom.
<i>COB</i>	....	....
<u><i>ICOB</i></u>	<u><i>ICOB</i></u> applies.	<u>Only the following provisions of <i>ICOB</i> apply:</u>  <u>(a) <i>ICOB</i> 3 (Financial promotion), but see the territorial scope in <i>ICOB</i> 3.4 (Application: where?)</u>  <u>(b) <i>ICOB</i> 5.5.20R(1)-(3), but only in relation to general insurance contracts if the state of the risk is the United Kingdom;</u>  <u>(c) <i>ICOB</i> 5.5.20R(4)-(15) and (22), but only in respect of non-investment insurance contracts which are pure protection contracts where the habitual residence of the customer, other than an EEA ECA recipient, is in the United Kingdom;</u>  <u>(d) <i>ICOB</i> 6 (Cancellation), but only in respect of non-investment insurance contracts which are pure protection contracts where the habitual residence of the customer, other than an EEA ECA recipient, is in the United Kingdom.</u>
<i>MCOB</i>	...	...

## Annex H

### Amendments to SUP

In this Annex, underlining indicates new text.

SUP 8.2.7G Rules which can be waived (see SUP 8.2.6G)

Rules	Section of the Act or other provision under which rules are made	Chapters of the Handbook where such rules appear (Note 1)
....		
Financial promotion rules	Section 145	<i>COB 3, <u>ICOB 3</u>, MCOB 3, PRIN and SYSC</i>
....		



## Annex I

### Amendments to DISP

In this Annex, underlining indicates new text. Where a new provision is inserted the place where it goes is indicated and it is not underlined.

After *DISP* 1.2.1R, insert the following:

1.2.1A R If the expression of dissatisfaction is from, or on behalf of, a *person* who is not an *eligible complainant*, and relates to *insurance mediation activity* carried on by an *insurance intermediary*, then unless the *insurance intermediary* is an *insurer*, the *insurance intermediary* must have in place and operate appropriate and effective procedures for registering, and responding to, the expression of dissatisfaction.

...

1.2.11 G In order to comply with *DISP* 1.2.9R(1), a *firm* may include reference to its complaints handling procedure in contractual documentation, for example:

- (1) (where the *firm* is subject to the requirements in *COB*), in a *terms of business letter, key features document or client agreement*;
- (2) (where the *firm* is subject to the requirements in *ICOB*), as part of status disclosure (see *ICOB* 4.2 and *ICOB* 8.3), in a *policy summary or policy document*, or
- (3) (where the *firm* is subject to the requirements in *MCOB*) in an initial disclosure document or *offer document*.

## Annex J

### Amendments to CRED

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 1.1.2 G *CRED* does not encompass the requirements associated with any regulatory *permission* other than a *Part IV permission to accept deposits*. Other *permissions* are covered elsewhere in the *Handbook*. Thus, for example, a *credit union* seeking a *permission* to undertake a regulated mortgage-lending activity would need to comply with the requirements in ~~the specialist sourcebook on mortgage lending (MORT) MCOB~~; and a *credit union* seeking a permission to undertake insurance mediation activity in relation to non-investment insurance contracts would need to comply with the requirements in ICOB.

## Annex K

### Amendments to ECO

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 1.2.3R ...
- Exceptions: deposits, ~~general insurance contracts, pure protection contracts~~  
non-investment insurance contracts and reinsurance
- 1.2.4 R (1) *ECO 1.2.1R* does not apply to an *incoming ECA provider* with respect to an *electronic commerce activity* relating to:
- (a) a *deposit* (other than a *cash deposit ISA*); or
  - (b) (if *ECO 1.2.3R* does not apply) a ~~*general insurance contract, pure protection contract*~~ *non-investment insurance contract* or reinsurance contract;
- but, instead, the *incoming ECA provider* must comply with (2).
- (2) Unless the contract concerned is a *non-investment insurance contract*, before entering into a contract with a *UK ECA recipient* who is a *consumer*, an *incoming ECA provider* must indicate to the recipient whether the contract falls within the jurisdiction of:
- (a) any dispute resolution service operating in the *EEA*; and
  - (b) in the case of services within (1)(b), any compensation scheme operating in the *EEA*;
- and, if either or both of (a) and (b) apply, must identify each such scheme.
- 1.2.5 G (1) *ECO 1.2.4R(2)(b)* does not require a deposit-taking *incoming ECA provider* to mention a deposit guarantee scheme, but its *Home State* will require it to do so in accordance with the *Deposit Guarantee Directive*.
- (2) *ECO 1.2.4R* does not require an *incoming ECA provider* carrying on *electronic commerce activities* in relation to *non-investment insurance contracts* to mention a dispute resolution service or a compensation scheme, but its *country of origin* will require it to do so in accordance with the *Distance Marketing Directive*.
- ...
- ...
- 2.1.2 G (1) ...

...

- (3) *ECO 2.2* also extends the territorial scope of *COB 3* (Financial promotion), *ICOB 3 (Financial promotion)* and *MCOB 3* (Financial promotion) in relation to a *financial promotion* which is an *outgoing electronic commerce communication*, whether or not the recipient is a *consumer*.

...

#### Financial promotion

- 2.2.3 R (1) In relation to a *financial promotion* which is an *outgoing electronic commerce communication*, a *firm* must comply with *COB 3* (Financial promotion), *ICOB 3 (Financial promotion)* and *MCOB 3* (Financial promotion) as if the *person* to whom the *communication* is made or directed was in the *United Kingdom*.
- (2) Accordingly, (1) overrides *COB 3.3 (Application: where?)*, *ICOB 3.4 (Application: where?)* and *MCOB 3.3 (Application: where?)*.
- (3) But (1) is subject to *ECO 2.2.1R*, which disapplies certain *COB rules* applicable to *incoming ECA providers* when dealing with *consumers*.
- 2.2.4 G The effect of *ECO 2.2.3R* is to apply the whole of *COB 3*, *ICOB 3* and *MCOB 3*, where relevant, to *outgoing electronic commerce communications*, except those provisions of *COB 3*, *ICOB 3* and *MCOB 3*, identified in *ECO 2.2.1R*. (See *ECO 2.2.2G* for an explanation of this approach.)

## Annex L

### Amendments to ELM

In this Annex, underlining indicates new text.

1.5.2 G Table: Application of other parts of the Handbook to ELMIs

Block	Module	Application
...		
Block 2 (Business Standards)	.....	
...	Conduct of Business sourcebook ( <i>COB</i> )	.....
	<u>Insurance: Conduct of Business sourcebook (<i>ICOB</i>)</u>	<u>Does not apply to an <i>ELMI</i> when issuing <i>e-money</i>.</u>
	Mortgage: Conduct of Business sourcebook ( <i>MCOB</i> )	Does not apply to an <i>ELMI</i> when issuing <i>e-money</i>

## Annex M

### Amendments to the Glossary

Insert the following new definitions in the appropriate alphabetical position:

- claims handling* (in *ICOB*) in relation to a *claim* under a *non-investment insurance contract*, carrying out the contract (by an *insurer*) or paying or declining to pay a *claim* on behalf of a *member* (by a *managing agent*).
- connected contract* a *non-investment insurance contract* which:
- (a) is not a contract of long-term insurance (as defined by article 3 of the *Regulated Activities Order*);
  - (b) has a total duration (including *renewals*) of five years or less;
  - (c) has an annual *premium* (or the equivalent of annual *premium*) of €500 or less;
  - (d) covers the risk of:
    - (i) breakdown, loss of, or damage to, non-motor goods supplied by the provider; or
    - (ii) damage to, or loss of, baggage and other risks linked to travel booked with the provider (“travel risks”);
  - (e) does not cover any liability risks (except, in the case of a contract which covers travel risks, where the cover is ancillary to the main cover provided by the contract);
  - (f) is complementary to the non-motor goods being supplied or service being provided by the provider; and
  - (g) is of such a nature that the only information that a *person* requires in order to carry on one of the *insurance mediation activities* is the cover provided by the contract.

*distance non-investment mediation contract*

a *distance contract* (other than a contract concluded merely as a stage in the *effecting* or *carrying out* of an *insurance contract* by the *firm* or another *person*) the making or performance of which constitutes, in relation to a *non-investment insurance contract*, any of the following activities:

- (a) *dealing in investments as agent*;
- (b) *making arrangements with a view to transactions in investments*;
- (c) *assisting in the administration and performance of a contract of insurance*;
- (d) *arranging (bringing about) deals in investments*;
- (e) *advising on investments*;
- (f) *agreeing to carry on a regulated activity* in (a) to (e).

*group policy*

a *non-investment insurance contract* which a *person* enters into as legal holder of the *policy* on his own behalf and for other *persons* who are or will become *policyholders* and:

- (a) those other *persons* are or become *policyholders* by virtue of a common employment, occupation or activity which has arisen independently of the *contract of insurance*;
- (b) the common employment, occupation or activity is not brought about, in relation to the *contract of insurance*, by
  - (i) the *insurance undertaking* which *effects* it or carries it out; or
  - (ii) any activity which if carried on by a *firm* would be an *insurance mediation activity*; and
- (c) the risks insured under the *policy* are related to the common employment, occupation or activity of the *policyholders*.

*introducing*

(in *ICOB*) the activity of effecting introductions carried on by a *firm* with *permission* for *making arrangements with a view to deals in investments* which are *non-investment insurance contracts*.

*non-investment*

a *non-real time financial promotion* for a *non-investment*

<i>financial promotion</i>	<i>insurance contract.</i>
<i>policy document</i>	a <i>policy</i> in a <i>durable medium</i> .
<i>policy summary</i>	a summary of a <i>non-investment insurance contract</i> in a <i>durable medium</i> containing the information specified in <i>ICOB 5.5.5R</i> .

Amend the following definitions as shown (underlining indicates new text and striking through indicates deleted text):

<i>charge</i>	<p>any <i>fee</i> or <i>charge</i> made to a <i>client</i> in connection with:</p> <p>(a) <u><i>designated investment business</i></u>; <u>or</u></p> <p>(b) <u>any <i>insurance mediation activities</i> in respect of a <i>non-investment insurance contract</i></u>;</p> <p>whether levied by the <i>firm</i> or any other <i>person</i>, including a <i>mark-up</i> or <i>mark-down</i>.</p>
<i>claim</i>	<p>(1) (in <i>COMP</i>) a valid <i>claim</i> made in respect of a civil liability owed by a <i>relevant person</i> to the claimant.</p> <p>(2) (in <u><i>ICOB</i></u>, <i>LLD</i>, <i>SUP</i>, and <i>TC</i>) a <i>claim</i> under a <i>contract of insurance</i>.</p>
<i>commission</i>	<p><del>any form of commission, including a benefit of any kind, offered or given in connection with <i>designated investment business</i>.</del></p> <p>any form of commission, including a benefit of any kind, offered or given in connection with:</p> <p>(a) <u><i>designated investment</i></u>; <u>or</u></p> <p>(b) <u><i>insurance mediation activity</i> in connection with a <i>non-investment insurance contract</i></u>.</p>
<i>durable medium</i> <sup>2</sup>	<p><del>(in accordance with article 2(f) of the <i>Distance Marketing Directive</i> and article 2(12) of the <i>Insurance Mediation Directive</i>) (in relation to information addressed personally to a recipient) in a form which:</del></p>

<sup>2</sup> This is an amendment to the proposed definition in Annex Q to the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003.



- ~~(a) is capable of being used by the recipient;~~
- ~~(b) enables the recipient to store the information in a way accessible for future reference for a period of time adequate for the purposes of the information; and~~
- ~~(c) allows the unchanged reproduction of the information;~~

and includes paper, floppy disks, CD-ROMs, DVDs and the hard drive of the recipient's computer on which electronic mail is stored, but not Internet websites unless they fulfil the criteria in (a),(b) and (c).

- (a) paper; or
- (b) (in accordance with recital 20 and article 2(f) of the Distance Marketing Directive and article 2(12) of the Insurance Mediation Directive) any instrument which enables the recipient to store information in a way accessible for future reference for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored; this includes in particular floppy disks, CD-ROMs, DVDs and the hard drive of the recipient's computer on which electronic mail is stored, but not Internet websites unless they fulfil the criteria in this definition.

*financial promotion rules*

COB 3 and ICOB 3.

*injured party*

(in ICOB 6:87.6) a *person* who claims damages as a result of any loss or injury suffered in, or as a result of, an accident which occurs in an *EEA State* other than his usual *EEA State* of residence which is caused by the use of a motor vehicle insured and normally based in an *EEA State*.

*product provider*

- (1) (except in ICOB) a firm which is:
  - (i) a *long-term insurer*;
  - (ii) a *friendly society*;
  - (iii) the *operator* of a *regulated collective investment scheme* or an *investment trust savings scheme*.
- (2) (in ICOB) in relation to a non-investment insurance contract, an insurer not acting as an insurance intermediary.

## ADDENDUM

### INSURANCE: CONDUCT OF BUSINESS SOURCEBOOK (CONSEQUENTIAL AMENDMENTS TO THE HANDBOOK) INSTRUMENT 2004

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex C of this instrument is amended as follows:

#### Transitional Provisions

...

(1)	(2)	(3)	(4)	(5)	(6)
1	<i>GEN</i> <u>2.2.7R</u>	R	...		
<del>26</del>	<i>GEN</i> <u>4.3.1R</u>	R	(1) For the purpose ...	From 31 October ...	Apply in relation to ...
<u>37</u>	<i>GEN</i> 4.3.1R	G	(1) Transitional provision <del>26</del> R defers ... the transitional provision in <i>GEN</i> TR <del>26</del> . ...	From 31 October ...	Apply in relation to ...

...

Annex E of this instrument is amended as follows:

2.1.4R Table: Activities to which *TC 2* applies

	Activity	Extent of application
1. <i>Employees</i> engaging in:	...  ( <del>fg</del> ) advising on <i>investments</i> ...	...

## APPOINTED REPRESENTATIVES INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance);
  - (4) section 213 (The compensation scheme);
  - (5) section 214 (General); and
  - (6) section 395 (The Authority’s procedures).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

### Commencement

- C. This instrument comes into force as follows:

Annex	Commencement date
A	30 June 2004
B	30 June 2004
C	31 October 2004
D	14 January 2005

### Amendments relating to multiple principals of appointed representatives for investment business

- D. The Supervision manual is amended in accordance with Annex A to this instrument.
- E. The Dispute resolution: Complaints sourcebook, the Compensation sourcebook and the Collective Investment Schemes sourcebook are amended in accordance with Annex B to this instrument.

### Amendments to the Supervision manual and the Glossary relating to regulation of mortgages and long-term care insurance

- F. The Supervision manual and the Glossary are amended in accordance with Annex C to this instrument.

**Amendments to the Supervision manual, the Decision making manual and the Glossary relating to regulation of insurance mediation**

G. The Supervision manual, Decision making manual and the Glossary are amended in accordance with Annex D to this instrument.

**Citation**

H. This instrument may be cited as the Appointed Representatives Instrument 2004.

By Order of the Board  
15 January 2004

Amended by Addendum  
9 August 2004

## Annex A

### Amendments to the Supervision manual relating to multiple principals of appointed representatives for investment business coming into force on 30 June 2004

In this Annex, underlining indicates new text and striking through indicates deleted text.

SUP Transitional provisions, Table 2

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
9	...				
<u>9A*</u>	<u>SUP 12.5</u>	<u>R</u>	<u>A firm conducting designated investment business need not amend its written contract with an appointed representative (appointed before 15 January 2004) to take account of amendments to SUP 12.5 coming into force between 30 June 2004 and 30 June 2005, until 30 June 2005 or the date on which the contract is next updated (whichever is earlier).</u>	<u>From 30 June 2004 until 30 June 2005, that is, 12 months.</u>	<u>Commencement, and as amended with effect from 30 June 2004</u>
...					

...

#### 12.1 Application and purpose

##### Application

- 12.1.1 R
- (1) This chapter applies to a *firm* ~~with permission to carry on designated investment business and~~ which is considering appointing, has decided to appoint or has appointed an *appointed representative*.
  - (2) ~~The rules, and guidance on rules, in this~~ This chapter ~~do~~ does not apply to a *UCITS qualifier*.

...

\* see Addendum p33

12.2.2 G ...

Who can be an appointed representative?

12.2.3G ...

Can an appointed representative have more than one principal?

12.2.4 G The *Act* and the *Appointed Representatives Regulations* do not prevent an *appointed representative* from acting for more than one *principal*.  
However, SUP 12.5.6A R (Prohibition of multiple principals for certain activities) prevents this for particular kinds of business.

12.2.5 G ...

What is a "network"?

12.2.6 G (1) ~~An appointed representative may be appointed by any firm with permission to carry on designated investment business of the type described in SUP 12.2.7G(1), including a provider firm or an independent intermediary.~~

(2) An *independent intermediary* is referred to as a 'network' if it appoints five or more *appointed representatives* or if it appoints less than five *appointed representatives* which have, between them, twenty-six or more *financial advisers*.

...

What is an introducer appointed representative?

12.2.8 G (1) An *introducer appointed representative* is an *appointed representative* appointed by a *firm* whose scope of appointment must, under SUP 12.5.7 R, be limited to:

(a) effecting introductions ~~between customers and to the firm~~ or other members of the *firm's marketing group*; and

(b) distributing *non-real time financial promotions which relate to products or services available from or through the firm approved by the firm* or other members of the *firm's marketing group* or the producer of an *adopted packaged product*.

(2) The permitted scope of appointment of an *introducer appointed representative* does not include in particular:

(a) arranging (bringing about) deals in investments; or

(b) advising on investments or other activity that might reasonably lead a *customer* to believe that he had received

*advice on investments* or that the *introducer appointed representative* is permitted to give *advice on investments*.

(3) An introducer appointed representative may have more than one principal, but will need a contract with each principal.

(4) The approved persons regime does not apply to an introducer appointed representative (see SUP 10.1.16R).

12.2.9 G

(4) To become an *introducer appointed representative*, a person must meet the conditions in the *Act* to become an *appointed representative* (see SUP 12.2.2G).

~~(2) In considering the appointment of a person as an *introducer appointed representative*, a firm should have regard to the requirements in SUP 12.5.7R. In particular, these requirements mean that the *introducer appointed representative* cannot be an *appointed representative* for a member of another *marketing group*.~~

12.2.10 G

All rules in SUP 12 apply in relation to *introducer appointed representatives* except for:

(1) ~~SUP 12.4.2R, SUP 12.4.5B R and SUP 12.4.5C R~~, on the appointment of *appointed representatives*, which is replaced by SUP 12.4.6R; ~~and~~

(2) ~~SUP 12.5.5R SUP 12.5.6A R~~ on required contract terms, which is replaced by SUP 12.5.7R; ~~and~~

~~(3) SUP 12.9.1R(4) (Record keeping).~~

...

12.2.14 G

(1) A *representative* is an individual who is appointed by a *firm* or by an *appointed representative* ~~of that firm~~, to carry out on, ~~in the course of designated investment business~~, either or both any of the following activities in (1)(a) to (c):

~~(a) advising customers on the merits of packaged products offered by that firm (or any other provider firm within the same marketing group);~~

~~(b) arranging (bringing about) deals in investments in relation to such products.~~

(a) advising on investments;

(b) arranging (bringing about) deals in investments;

(c) dealing in investments as agent.

- (2) If a *provider firm* appoints an *appointed representative* who is an individual in (1), that *appointed representative* will also be a *representative*. The individual ~~must~~ may need to be approved to perform the *investment adviser function* or the *customer trading function* or both, and possibly also the *sole trader function* (see SUP 12.6.8G and SUP 12.6.9G). In these circumstances, in addition to complying with the requirements of SUP 12 and other regulatory requirements, the *firm* should ensure that the *rules* for *representatives* in COB 5 (Advising and selling) are complied with.

...

The permission that the firm needs

~~12.4.1 R A firm may only appoint an appointed representative to carry on regulated activities on its behalf if the firm has permission to carry on those regulated activities. [Deleted]~~

12.4.1A G The effect of sections 20 (Authorised persons acting without permission) and 39(4) (Exemption of appointed representatives) of the Act is that the regulated activities covered by an appointed representative's appointment need to:

- (1) fall within the scope of the principal's permission; or
- (2) be excluded from being regulated activities when carried on by the principal, for example because they fall within article 28 of the Regulated Activities Order (Arranging transactions to which the arranger is a party).

Appointment of an appointed representative (other than an introducer appointed representative)

12.4.2 R Before a *firm* appoints a *person* as an *appointed representative* (other than an *introducer appointed representative*) and on a continuing basis, it must take reasonable care to ensure that:

- (1) ...
- (2) the *person*:
- (a) ...
  - (b) ...
  - (c) ... ; ~~and~~
- (3) the *firm* has adequate:
- (a) ...
  - (b) ... ; and
- (4) the *firm* is ready and organised to comply with the other applicable requirements contained or referred to in this chapter.

...



Appointment representative who may be appointed by other principals

12.4.5A G If a *firm* proposes to appoint an *appointed representative*, but not to prohibit its appointment by any other *principals* (see SUP 12.5.2G(3)), the *firm* should, in particular:

- (1) require, in the contract, that the *appointed representative* notifies the *firm* about other *principals* (see SUP 12.5.5R(3)); and
- (2) unless the *appointed representative* is an *introducer appointed representative*:
  - (a) take reasonable steps to check whether the *appointed representative* is already appointed by one or more other *principals* and, if it is, contact those other *principals*; such steps should include asking the *appointed representative* and checking the *Register*;
  - (b) if there are any other *principals*, agree arrangements with the other *principals* (see SUP 12.4.5B R); and
  - (c) establish effective systems and controls for ensuring that the *appointed representative* complies with all contractual restrictions imposed, including those relating to multiple *principals* under the *Appointed Representatives Regulations* and under SUP 12.5.6A R (see SUP 12.6.11A R).

Multiple principals

12.4.5B R (1) A *firm* must not appoint a *person* as its *appointed representative* until it has entered into a written agreement (a “multiple principal agreement”) with every other *principal* the *person* may have; but this does not apply to the appointment of an *introducer appointed representative* nor does it require an agreement with another *principal* which has appointed a *person* as an *introducer appointed representative*.

(2) A *firm* must not unreasonably decline to enter into a multiple principal agreement with any *principal* of his *appointed representative* unless the *firm* is relying on a prohibition on the *appointed representative* from representing any other *firms* (or is seeking to impose such a prohibition) as permitted by article 3 of the *Appointed Representative Regulations*.

(3) A multiple principal agreement must contain all the provisions which are necessary or desirable to:

- (a) set out the relationship between the *principals* of that *appointed representative*; and
- (b) protect the interests of *clients*;

including the matters set out in SUP 12.4.5C R.

12.4.5C R Table: Multiple principal agreement

	<u>Matter</u>	<u>Explanation</u>
1.	<u>Scope of appointment</u>	<u>The scope of appointment given by each <i>principal</i> to the <i>appointed representative</i>.</u>
2.	<u>Complaints handling</u>	<u>The identity of the <i>principal</i> which will be the point of contact for a complaint from a <i>client</i> (referred to as the “lead-principal” in <u>SUP 12.4.5D G</u> to <u>SUP 12.4.5E G</u>).</u> <u>An agreement that each <i>principal</i> will co-operate with each other <i>principal</i> in resolving a complaint from a <i>client</i> in relation to the <i>appointed representative’s</i> conduct.</u> <u>The arrangements for complaints handling, including arrangements for resolving disputes between the <i>principals</i> in relation to their liability to a <i>client</i> in respect of a complaint and arrangements for dealing with referrals to the <i>Financial Ombudsman Service</i>.</u>
3.	<u>Financial promotions</u>	<u>The arrangements for <i>approving financial promotions</i>.</u>
4.	<u>Control and monitoring</u>	<u>The arrangements for the control and monitoring of the activities of the <i>appointed representative</i> (see in particular <u>SUP 12.6.6R</u> (Regulated activities and investment services outside the scope of appointment) and <u>SUP 12.6.7G</u> (Senior management responsibility for appointed representatives)).</u>
5.	<u>Approved person status</u>	<u>The arrangements for making applications for <i>approved person</i> status (see <u>SUP 10</u> (Approved persons)).</u>
6.	<u>Training and competence</u>	<u>The arrangements for training and competence (see <u>TC</u>).</u>
7.	<u>Co-operation</u>	<u>The arrangements for co-operation over any other issues which may arise from the multiple appointments, including issues which may damage the interests of <i>clients</i> dealing with the <i>appointed representative</i> and administrative issues.</u> <u>An agreement by each <i>principal</i> to take reasonable steps to ensure that it does not cause the <i>appointed representative</i> or any of its other <i>principals</i> to be in breach of their obligations to each other or under the <i>regulatory system</i>.</u>
8.	<u>Sharing information</u>	<u>The arrangements for sharing information on matters relevant to the matters covered under the multiple principal agreement and each <i>principal’s</i> obligations under <u>SUP 12.6</u> (Continuing obligations of firms with appointed representatives).</u> <u>An agreement that each <i>principal</i> will notify each other <i>principal</i> of any information which is materially relevant to the multiple principal agreement.</u>

12.4.5D G One effect of the multiple principal agreement is to introduce a ‘lead-principal’ concept in relation to complaints handling for the benefit of the *client*. For example, where the *client* has been given advice by an *appointed representative* who has two *principals*, and the advice could have led to a transaction being arranged with either *principal*, the *client* will know that he may pursue his complaint with (but not necessarily against) one of the *principals*. Whether he later decides to refer his complaint to the *Financial Ombudsman Service*, and if so, against which *principal*, will depend on the circumstances.

- 12.4.5E G (1) Under the relevant Advising and Selling chapters of *COB*, *ICOB* and *MCOB*, the *customer* will receive details of how to complain to the *appointed representative* and, when a product is purchased, details of the complaints procedure for the *product provider*, *insurer* or *mortgage lender*.
- (2) Under *DISP* 1.2.9R, a *firm* must among other things, supply a copy of its internal complaint handling procedures to the *customer* when it receives a complaint. In complying with *DISP* 1.2.9R, a *firm* should ensure that the "lead-principal" is clearly identified in the procedures.
- (3) The complaints procedure should also explain that the *customer* has a choice of whether to contact the *appointed representative*, the "lead-principal" or the *product provider*, *insurer* or *mortgage lender* and that the "lead-principal" will be the appropriate point of contact where the *customer* does not wish to complain about a specific product or is unsure who to contact.
- (4) In other words, where the *customer* has a doubt who to complain to the "lead-principal" is to be the point of contact for all complaints arising out of the activities of the *appointed representative*.

12.4.5F G When considering the provisions for complaints handling (see *SUP* 12.4.5C R(2)) *firms* should consider the use of a mediation clause. If a complaint is made by a *client*, *principals* which are unable to resolve a dispute about liability to the *client* should consider all quick and effective ways of resolving the dispute, including referring the matter to the *Financial Ombudsman Service* and mediation.

12.4.5G G It is for the *principals* to consider in each case whether it would be appropriate to show the multiple principal agreement to their *appointed representative*, or in some circumstances make their *appointed representative* a party to it.

Appointment of an introducer appointed representative

12.4.6 R Before a *firm* appoints a *person* as an *introducer appointed representative*, and on a continuing basis, it must take reasonable care to ensure that:

- (1) the *person* is suitable to act for the *firm* in that capacity (having regard, in particular, to other *persons* connected with the *person* who will be, or who are, directly responsible for its activities); ;  
and
- (2) the *firm* is ready and organised to comply with the other applicable requirements contained or referred to in this chapter.

...

12.5.4 G ...

~~Required contract terms for an appointed representative (other than an introducer appointed representative)~~

12.5.5 R

~~A firm must ensure that its written contract with each of its appointed representatives (other than introducer appointed representatives):~~

- ~~(1) complies with the requirements prescribed in regulation 3 of the *Appointed Representatives Regulations* (see SUP 12.5.2G); and~~
- ~~(2) requires the appointed representative to comply with, and to ensure that any persons who provide services to the appointed representative under a contract of services or a contract for service comply, with the relevant requirements in or under the Act (including the rules) that apply to the activities which it carries on as appointed representative of the firm - ; and~~
- ~~(3) (unless the written contract prohibits appointments by other principals) requires the appointed representative to notify the firm:
  - ~~(a) that it is seeking appointment as an appointed representative of another person, who the person is and the business for which the other person will accept responsibility;~~
  - ~~(b) (as soon as possible) of any change in the business notified under (a); and~~
  - ~~(c) (as soon as possible) of the termination of any such appointment.~~~~

...

12.5.6 G

...

Prohibition of multiple principals for certain activities

12.5.6A R

- (1) A firm must ensure that, if appointing an appointed representative (other than an introducer appointed representative), to carry on any designated investment business for private customers, its written contract prohibits the appointed representative from carrying on any of those specified activities as an appointed representative for another firm.
- (2) As an exception to (1), if the firm is a long-term insurer or an operator of a UCITS scheme, it may permit an appointed representative to carry on designated investment business as the appointed representative of one or more other firms provided that:
  - (a) each of those other firms is a long-term insurer or an operator of a UCITS scheme;

- (b) the first *firm* and each of those other *firms* is a member of the same group; “group” means for this purpose a group of *bodies corporate* all having the same *holding company* including the *holding company*; and
- (c) the scope of each appointment does not overlap, as to both activities and *investments*.

12.5.6B G      The effect of SUP 12.5.6A R(1) is that, in relation to *designated investment business with private customers, appointed representatives* are restricted to one *principal*.

Required contract terms for an introducer appointed representative

12.5.7 R      ~~A *firm* must ensure that its written contract with each of its *introducer appointed representatives* prohibits the *introducer appointed representative* from~~ limits the scope of the appointment to:

~~(1) in relation to a *designated investment* or *designated investment business*~~

~~(a 1) effecting an introduction between a *customer* and a *person* other than to the *firm* or another *other* members of the *firm’s marketing group*; and~~

~~(b 2) distributing *non-real time financial promotions* which relate to products or services available from or through the *firm-approved* by a *person* other than the *firm* or another members of the *firm’s marketing group* or the producer of an *adopted packaged product*; and~~

~~(2) carrying on any *regulated activity* on behalf of any *person* other than the *firm* or another member of the *firm’s marketing group*.~~

...

12.6.11 G      ...

Compliance by an appointed representative with the contract

12.6.11A R      A *firm* must take reasonable steps to establish and maintain effective systems and controls for ensuring that each of its *appointed representatives* complies with those terms of its contract which are imposed under the requirements contained or referred to in SUP 12.5 (Contracts: required terms).

~~Additional obligations for introducer appointed representatives~~

12.6.12 R      ~~A *firm* must take reasonable steps to ensure that each of its *introducer appointed representatives*:~~

- (1) ~~does not, in relation to a *designated investment* or *designated investment business*:~~
  - (a) ~~effect an introduction between a *customer* and a *person* other than the *firm* or another member of the *firm's marketing group*; and~~
  - (b) ~~distribute *non-real time financial promotions* approved by a *person* other than the *firm* or another member of the *firm's marketing group* or the producer of an *adopted packaged product*; and~~
- (2) ~~does not carry on any *regulated activity* on behalf of any *person* other than the *firm* or another member of the *firm's marketing group*. [Deleted]~~

...

## 12.8 Termination of a relationship with an appointed representative

### Notification of termination or prohibited amendment of the contract

12.8.1 R If either the *firm* or the *appointed representative* notifies the other that it proposes to terminate a the contract of appointment or to amend it so that it no longer meets the requirements ~~prescribed in the *Appointed Representative Regulations* (see *SUP 12.5.2G*) and, in the case of an *introducer appointed representative*, *SUP 12.5.7R* contained or referred to in *SUP 12.5* (Contracts: required terms), the *firm* must:~~

...

...

### Steps to be taken on termination or prohibited amendment of the contract

12.8.3 R If a contract with an *appointed representative* is terminated, or if it is amended in a way which gives rise to a requirement to notify under *SUP 12.8.1R*, a *firm* must take all reasonable steps to ensure that:

- (1) ...
- (2) ...; ~~and~~
- (3) ... ; and
- (4) all the other *principals* of the *appointed representative* of which the *firm* is aware are notified.

...

## 12.9 Record keeping

12.9.1 R A *firm* must make the following records on each of its *appointed representatives*:

- (1) ...
- (2) ...; ~~and~~
- (3) ...; and
- (4) any arrangements agreed with other *principals* under SUP 12.4.5B R (Multiple principals).

...

Schedule 1  
Record keeping requirements G

3 Table:

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
<i>SUP</i> 4.3.17R(3)	...			
<i>SUP</i> 12.9.1R <i>SUP</i> 12.9.2R	<i>Appointed representatives</i>	(1) ... ... (4) <u>arrangements agreed with other <i>principals</i> under <i>SUP</i> 12.4.5B R</u>	...	...
...				

## Annex B

### Amendments to the Dispute resolution: Complaints sourcebook, Compensation sourcebook and the Collective Investment Schemes sourcebook relating to multiple principals for investment business coming into force on 30 June 2004

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Amendments to the Dispute resolution: Complaints sourcebook

2.6.5 G Complaints about acts or omissions by a *firm* include complaints about acts or omissions in respect of activities for which the *firm* is responsible (~~that is the activities~~ including business of their any appointed representatives for which the *firm* has accepted responsibility).

#### Amendments to the Compensation sourcebook

9.2.2 R The *FSCS* may postpone paying compensation if:

- (1) in the case of a *claim* against a *relevant person* who is an *appointed representative*, the *FSCS* considers that the claimant should make and pursue an application for compensation against the *appointed representative's relevant principal*; or

#### Amendments to the Collective Investment Schemes sourcebook

16.2.4 G (1) Independence ~~and polarisation~~: the *FSA* considers that independence will need to be specifically appraised in the event of a proposal by the *depository* to ~~become an appointed representative of~~ enter into any arrangement with the *ICVC* or any corporate *director* of it by which the *depository* might agree to act on an exclusive (or near exclusive) basis, or for a *director* to become an *appointed representative* of enter into a similar arrangement with the *depository*.

(2) ...

(3) ...

...

16.3.2 G (1) ...

...

- (8) Independence ~~and polarisation~~: The *FSA* considers that independence will need to be specifically appraised in the event of a proposal by the *trustee* or *manager* (or any of either's *associates*) to enter into any arrangement with ~~become an appointed representative of~~ the other by which either party might agree to act on an exclusive (or near exclusive) basis in relation to the marketing of packaged products. ~~The status of a "tied agent" will~~



~~mean that the trustee of an AUT is prohibited by contract from procuring or endeavouring to procure persons to enter into investment agreements (or certain kinds of investment agreements including those relating to AUTs) with persons other than the manager.~~

- (9) If such a ~~tie~~ relationship should be contemplated, then arrangements may need to be put in to place to satisfy the FSA that the necessary independence is preserved. The FSA would therefore expect to be consulted in advance of such proposal.

## Annex C

### Amendments to the Supervision manual and the Glossary relating to mortgages and long-term care insurance coming into force on 31 October 2004

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Amendments to the Supervision manual

- 12.2.7 G (1) The *Appointed Representatives Regulations* are made by the Treasury under section 39(1) of the *Act*. These regulations describe, among other things, the business for which an *appointed representative* may be exempt, which is business which comprises any of:
- (a) arranging (bringing about) deals in investments (article 25(1) of the *Regulated Activities Order*) (that is in summary, deals in a designated investment, funeral plan contract or right to or interest in a funeral plan); ~~or~~
  - (b) making arrangements with a view to transactions in investments (article 25(2) of the *Regulated Activities Order*) where the arrangements are for or with a view to transactions relating to securities or contractually based investments (that is in summary, transactions in a designated investment, funeral plan contract or right to or interest in a funeral plan);
  - (c) arranging (bringing about) regulated mortgage contracts (article 25A(1) of the *Regulated Activities Order*);
  - (d) making arrangements with a view to regulated mortgage contracts (article 25A(2) of the *Regulated Activities Order*);
  - (~~b~~ e) *arranging safeguarding and administration of assets* (part of article 40 of the *Regulated Activities Order*);
  - (~~e~~ f) advising on investments (article 53 of the *Regulated Activities Order*) (that is in summary, on any designated investment, funeral plan contract or right to or interest in a funeral plan);  
~~and~~
  - (g) advising on regulated mortgage contracts (article 53A of the *Regulated Activities Order*); and
  - (~~d~~ h) *agreeing to carry on a regulated activity* (article 64 of the *Regulated Activities Order*) where the *regulated activity* is one of those in (a) to (e g).
- ...
- 12.2.8 G (1) ...

- (2) The permitted scope of appointment of an *introducer appointed representative* does not include in particular:
- (a) arranging (bringing about) deals in investments or arranging (bringing about) regulated mortgage contracts; or
  - (b) advising on investments, advising on regulated mortgage contracts or other activity that might reasonably lead a *customer* to believe that he had received *advice on investments or on regulated mortgage contracts* or that the *introducer appointed representative* is permitted to give *advice on investments or on regulated mortgage contracts*.
- (3) ...

...

12.4.7 G

In assessing, under SUP 12.4.6R, whether an *introducer appointed representative* or prospective *introducer appointed representative* is otherwise suitable to act for the *firm* in that capacity, the *firm* should determine whether ~~it~~ the *introducer appointed representative* and those *persons* who will be, or who are, directly responsible for its activities are of sufficiently good reputation and otherwise fit and proper for that appointment. The *firm* should, as a minimum, verify the identity of a prospective *introducer appointed representative* and relevant *persons* but need not carry out the more extensive due diligence required for the appointment of an *appointed representative* under SUP 12.4.2R.

...

12.5.2 G

- (1) Regulations 3(1) to (3) of the *Appointed Representatives Regulations* makes it a requirement that the contract between the *firm* and the *appointed representative* (unless it prohibits the *appointed representative* from representing other counterparties) contains a provision enabling the *firm* to:

...

- (2) Under the *Appointed Representative Regulations*, an *appointed representative* is treated as representing other counterparties if, broadly, it:
- (a) makes arrangements (within article 25 of the *Regulated Activities Order* (Arranging deals in investments)) for *persons* to enter into investment transactions with other counterparties; or
  - (b) *arranges the safeguarding and administration of assets* by other counterparties; or

- (c) gives advice (within article 53 of the *Regulated Activities Order (Advising on investments)*) on the merits of entering into investment transactions with other counterparties;

where an "investment transaction" means a transaction to *buy, sell, subscribe for or underwrite a security, or a contractually based investment or long-term care insurance;* or

- (d) arranges:

(i) for persons to enter (or with a view to persons entering) as borrowers into regulated mortgage contracts with other counterparties; or

(ii) for a person to vary a regulated mortgage contract entered into by a person as borrower on or after 31 October 2004 with other counterparties; or

- (e) gives advice (within article 53 of the *Regulated Activities Order (Advising on investments)*) on the merits of:

(i) persons entering as borrowers into regulated mortgage contracts with other counterparties; or

(ii) persons varying regulated mortgage contracts entered into by them as borrower on or after 31 October 2004 with other counterparties.

...

#### Prohibition of multiple principals for certain activities

12.5.6A R

- (1) A firm must ensure that, if appointing an *appointed representative* (other than an *introducer appointed representative*), to carry on any *designated investment business for private customers* of the following *regulated activities*, its written contract prohibits the *appointed representative* from carrying on any of these the specified activities as an *appointed representative* for another firm:

(a) any designated investment business for private customers: the prohibition must cover all designated investment business for private customers;

(b) any regulated mortgage activities (other than in relation to lifetime mortgages): the prohibition must cover all regulated mortgage activities (other than lifetime mortgages);

(c) any regulated mortgage activities in relation to lifetime mortgages: the prohibition must cover all lifetime mortgages.

12.5.6B G (1) The effect of SUP 12.5.6A R(1)(a) is that, in relation to *designated investment business* with *private customers*, *appointed representatives* are restricted to one *principal*.

(2) The effect of SUP 12.5.6A R(1)(b) and (1)(c) is that, in relation to *regulated mortgage activities* with *customers*, *appointed representatives* are restricted to having two *principals*: one for *regulated mortgage contracts* and one for *lifetime mortgages*.

...

12.6.5 R ...

Regulated activities and investment services outside the scope of appointment

12.6.6 R A *firm* must take reasonable steps to ensure that each of its *appointed representatives*:

(1) ...

(2) carries on the *regulated activities* for which the *firm* has accepted responsibility in a way which is, and is held out as being, clearly distinct from any of the *appointed representative's* other business:

(a) ...

(b) which:

(i) is, or is held out as being, primarily for the purposes of investment or obtaining credit; and

(ii) is not a *regulated activity*.

...

Obligations of firms under the approved persons regime

12.6.8G (1) Some of the *controlled functions*, as set out in SUP 10.4.1R, apply to an *appointed representative* of a *firm*, other than an *introducer appointed representative*, just as they apply to a *firm* (see SUP 10.1.16R). These are the *governing functions* and the *customer functions* (other than the *investment management function*) such as, for example, CF21, the *investment adviser function*. As explained in SUP 10.1.17G(1), SUP 10.1.17G(2) and SUP 10.3.2G respectively:

(4 a) the effect of SUP 10.1.16R is that the *directors* (or their equivalent) and *senior managers* (or their equivalent) of an *appointed representative*, other than an *introducer appointed representative*, must also be approved under

section 59 of the *Act* for the performance of certain *controlled functions*;

(b) although the *customer functions* (other than the *investment manager function*) apply to an *appointed representative*, the descriptions of the functions themselves do not extend to *mortgage mediation activity*; and

(c) sections 59(1) and 59(2) of the *Act* (Approval for particular arrangements) provide that approval is necessary in respect of a *controlled function* which is performed under an *arrangement* entered into by a *firm*, or its contractors (typically an *appointed representative*), in relation to a *regulated activity*.

...

Schedule 2  
Notification requirements

2 Table:

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...	...	...	...	...
SUP 12.8.1R	<i>Appointed representatives</i> - termination of appointment	(1) ...  (2) ...  (3) ...	Either the <i>firm</i> or the <i>appointed representative</i> notifying the other that it proposes to terminate a <u>the contract of appointment</u> or to amend it so that it no longer meets the requirements <del>in the</del> <u><i>Appointed Representatives Regulations</i> contained in or referred to in SUP 12.5.</u>  <del>Also, in the case of an <i>introducer appointed representative</i>, if the contract no longer meets the requirements of SUP 12.5.7 R, namely that the contract prohibits the <i>introducer</i> from:</del>  (1) in relation to a <i>designated investment or designated investment business</i> :  (a) effecting an introduction between a <i>customer</i> and a <i>person</i>	...

			<p>other than the <i>firm</i> or another member of the <i>firm's marketing group</i>; and</p> <p><del>(b) distributing non-real-time financial promotions approved by a person other than the <i>firm</i> or another member of the <i>firm's marketing group</i> or the producer of an <i>adopted packaged product</i>; and</del></p> <p><del>(2) carrying on any regulated activity on behalf of any person other than the <i>firm</i> or another member of the <i>firm's marketing group</i>.</del></p>	
...	...	...	...	...

### Amendments to the Glossary

Amend the following definition as shown. Underlining indicates new text and striking through indicates deleted text.

*designated investment* a security or a contractually-based investment (other than a funeral plan contract and a right to or interest in a funeral plan contract), that is, any of the following investments, specified in Part III of the *Regulated Activities Order* (Specified Investments), and a long-term care insurance contract which is a pure protection contract:

(a) ...

...

(l) *rights to or interests in investments* in (a) to (k) (article 89) but not including rights to or interests in rights under a long-term care insurance contract which is a pure protection contract.

## Annex D

### Amendments to the Supervision manual, Decision making manual and the Glossary relating to insurance mediation coming into force on 14 January 2005

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Amendments to the Supervision manual

Business for which an appointed representative is exempt

- 12.2.7 G (1) The *Appointed Representatives Regulations* are made by the Treasury under section 39(1) of the *Act*. These regulations describe, among other things, the business for which an *appointed representative* may be exempt, which is business which comprises any of:
- (a) dealing in investments as agent (article 21 of the *Regulated Activities Order*) where the transaction relates to a *general insurance contract*;
  - (a b) *arranging (bringing about) deals in investments (article 25(1) of the *Regulated Activities Order*) (that is in summary, deals in a *designated investment, funeral plan contract, pure protection contract, general insurance contract* or right to or interest in a funeral plan);*
  - (b c) *making arrangements with a view to transactions in investments (article 25(2) of the *Regulated Activities Order*) (that is in summary, transactions in a *designated investment, funeral plan contract, pure protection contract, general insurance contract* or right to or interest in a funeral plan);*
  - (e d) *arranging (bringing about) regulated mortgage contracts (article 25A(1) of the *Regulated Activities Order*);*
  - (d e) *making arrangements with a view to regulated mortgage contracts (article 25A(2) of the *Regulated Activities Order*);*
  - (e f) assisting in the administration and performance of a contract of insurance (article 39A of the *Regulated Activities Order*) where the activity relates to a *general insurance contract*;
  - (e g) *arranging safeguarding and administration of assets (part of article 40 of the *Regulated Activities Order*);*
  - (f h) *advising on investments (article 53 of the *Regulated Activities Order*) (that is in summary, on any *designated investment, funeral plan contract pure protection contract, general insurance contract* or right to or interest in a funeral plan);*  
and



- (g i) *advising on regulated mortgage contracts* (article 53A of the *Regulated Activities Order*); and
- (h j) *agreeing to carry on a regulated activity* (article 64 of the *Regulated Activities Order*) where the *regulated activity* is one of those in (a) to (e i).

...

12.2.8 G

- (1) ...
- (2) The permitted scope of appointment of an *introducer appointed representative* does not include in particular:
  - (a) *dealing in investments as agent*; or
  - (a b) *arranging (bringing about) deals in investments* or *arranging (bringing about) regulated mortgage contracts*; or
  - (c) *assisting in the administration and performance of a contract of insurance where the transaction relates to a general insurance contract*; or
  - (b d) *advising on investments, advising on regulated mortgage contracts* or other activity that might reasonably lead a *customer* to believe that he had received *advice on investments* or on *regulated mortgage contracts* or that the *introducer appointed representative* is permitted to give *advice on investments* or on *regulated mortgage contracts*.

...

...

Appointment of an appointed representative (other than an introducer appointed representative)

12.4.2 R

Before a *firm* appoints a *person* as an *appointed representative* (other than an *introducer appointed representative*) and on a continuing basis, it must ~~take reasonable care to ensure~~ establish on reasonable grounds that:

- (1) ...
- (2) the *person*:
  - (a) is solvent;
  - (b) is otherwise suitable to act for the *firm* in that capacity; and
  - (c) has no *close links* which would be likely to prevent the effective supervision of the *person* by the *firm*;

...

12.4.3 G In assessing, under *SUP* 12.4.2R(2)(a) and (b), whether an *appointed representative* or prospective *appointed representative* is solvent and otherwise suitable, a *firm* should determine, **among other matters, whether the person is likely to be adversely influenced by its financial position in the conduct of the business for which the firm is responsible.** This might arise, for example, if the *person* has cashflow problems and is not able to service its debts. Guidance for *firms* on assessing the financial position of an *appointed representative* or prospective *appointed representative* is given in *SUP* 12 Ann 1G.

...

12.4.4 G In assessing, under *SUP* 12.4.2R(2)(b), whether an *appointed representative* or prospective *appointed representative* is otherwise suitable to act for the *firm* in that capacity, a *firm* should consider:

...

...

12.4.7 G In assessing, under *SUP* 12.4.6R(1), whether an *introducer appointed representative* or prospective *introducer appointed representative* is otherwise suitable to act for the *firm* in that capacity, the *firm* should determine whether the *introducer appointed representative* and those *persons* who will be, or who are, directly responsible for its activities

...

12.4.8 G ...

Appointed representative carrying on insurance mediation

12.4.8A R Before a firm appoints a person as an appointed representative to carry on insurance mediation activity, it must in relation to insurance mediation activity ensure that the person will comply on appointment, and will continue to comply with, the provisions of PRU 9.1.8R and PRU 9.1.10R (Knowledge and ability, and good repute) as if the appointed representative were a firm.

12.4.8B G In assessing, under SUP 12.4.8A R, whether an appointed representative, or prospective appointed representative, has established the knowledge and ability requirements for persons within its management structure and for those directly involved in its insurance mediation activity, a firm should refer to TC.

12.4.9 G (1) An appointed representative must not commence an insurance mediation activity until he is included on the Register as carrying on such activities (see SUP 12.5.2G(3)).

(2) If an appointed representative's scope of appointment is to include an insurance mediation activity, the principal must notify the FSA of the appointment before the appointed representative commences that activity (see SUP 12.7.1R(1)).

(3) As an exception, pre-notification is not required if the *appointed representative* is already included on the *Register* as carrying on *insurance mediation activities* in another capacity (for example, as the *appointed representative* of another *principal*).

12.4.10 G

(1) The *FSA* has the power to decide not to include on the *Register* (or to remove from the *Register*) an *appointed representative* whose scope of appointment includes an *insurance mediation activity*, if it appears to the *FSA* that he is not a fit and proper person to carry on those activities (article 95 of the *Regulated Activities Order*).

(2) If the *FSA* proposes to use the power in (1), it must give the *appointed representative* a *warning notice*. If the *FSA* decides to proceed with its proposal, it must give the *appointed representative* a *decision notice*. The procedures followed by the *FSA* in relation to the giving of *warning notices* and *decision notices* are set out in *DEC 2*.

(3) An *appointed representative* may apply to the *FSA* for a determination of the kind referred to in (1) to be revoked. If the *FSA* proposes to refuse the application, it must give the *appointed representative* a *warning notice*, and if the *FSA* decides to proceed with the refusal, it must give the *appointed representative* a *decision notice*.

...

12.5.2 G

...

(2) Under the *Appointed Representative Regulations*, an *appointed representative* is treated as representing other counterparties if, broadly, it:

...

(d) assists in the administration and performance of a contract of insurance (article 39A of the *Regulated Activities Order*) where the activity relates to a *general insurance contract*;

where an "investment transaction" means a transaction to buy, sell, subscribe for or underwrite a security or a *contractually based investment-relevant investment* (that is, a *designated investment, funeral plan contract, pure protection contract, general insurance contract or right to or interest in a funeral plan*; or

(e) arranges:

(i) ...

(ii) ...

(f) gives advice on the merits of:

(i) ...

(ii)...

(3) If the scope of appointment covers, in relation to a *contract of insurance, dealing in investments as agent, arranging, assisting in the administration and performance of a contract of insurance or advising on investments*, regulation 3(4) of the *Appointed Representatives Regulations* makes it a requirement that the contract between the *firm* and the *appointed representative* contains a provision providing that the *appointed representative* is not permitted or required to carry on such business unless he is included in the *Register* as carrying on *insurance mediation activities*.

...

12.5.6B G ...

12.5.6C G As SUP 12.5.6A R does not apply to *non-investment insurance contracts*, there are no restrictions on the number of *principals* an *appointed representative* may have in relation to those contracts.

...

## 12.6 Continuing obligations of firms with appointed representatives

Suitability etc. of appointed representatives

12.6.1R If at any time a *firm* has reasonable grounds to believe that the conditions in SUP 12.4.2R, ~~or~~ SUP 12.4.6R or SUP 12.4.8A R (as applicable) are not satisfied, or are likely not to be satisfied, in relation to any of its *appointed representatives*, the *firm* must:

...

Appointed representatives not to hold client money

12.6.5R (1) A *firm* must not permit an *appointed representative* to hold *client money* unless the *firm* is an *insurance intermediary* acting in accordance with CASS 5.5.18R to CASS 5.5.23R (which include provision for periodic segregation and reconciliation).

(2) The *firm* must take reasonable steps to ensure that if *client money* is received by the *appointed representative*, it is paid into a *client bank account* of the *firm*, or forwarded to the *firm*, in accordance with: ~~COB 9.3.49R to COB 9.3.51R.~~

(a) CASS 4.3.15R to CASS 4.3.17R; or

(b) CASS 5.5.18R to CASS 5.5.21R unless acting in accordance with CASS 5.5.23R (Periodic segregation and reconciliation).

Regulated activities and investment services outside the scope of appointment

12.6.6 R

A *firm* must take reasonable steps to ensure that each of its *appointed representatives*:

...

(2) carries on the *regulated activities* for which the *firm* has accepted responsibility in a way which is, and is held out as being, clearly distinct from any of the *appointed representative's* other business:

(a) ...

(b) which:

(i) is, or is held out as being, primarily for the purposes of investment or obtaining credit, or obtaining insurance cover; and

(ii) ....

...

Obligations of firms under the approved persons regime

12.6.8G

(1) ...

(a) ...

(b) although the *customer functions* (other than the *investment manager function*) apply to an *appointed representative*, the descriptions of the functions themselves do not extend to *insurance mediation activity* or *mortgage mediation activity*; and

(c) ...

(2) The *approved persons* regime applies differently to an *appointed representative* whose scope of appointment includes *insurance mediation activity* in relation to *non-investment insurance contracts* but no other *regulated activity* and whose principal purpose is to carry on activities other than *regulated activities*. These *appointed representatives* need only one person performing one of the governing functions. This means that only one *director* (or equivalent) of these *appointed representatives* must be approved under section 59 of the *Act* for the performance of the *director function*, the *chief executive function*, the *partner function* or the *director of unincorporated association function*, whichever is the most appropriate (see SUP 10.1.16A R and SUP 10.1.17G(3)).

...

## 12.7 Notification requirements

### Notification of appointment of an appointed representative

- 12.7.1 R
- (1) A *firm* which appoints an *appointed representative* must give written notice of the appointment to the *FSA*;
- (a) if the appointment covers *insurance mediation activities* and the *appointed representative* is not included on the *Register* as carrying on such *activities* in another capacity before (see *SUP 12.4.9G*); or
- (b) (otherwise) not more than ten *business days* after ~~the date the appointment takes effect.~~ ;
- the *appointed representative* begins to carry on *regulated activities* under the contract.

(2) ...

...

12.7.2 G A *firm's* notice under *SUP 12.7.1R* should give details of the *appointed representative* and the *regulated activities* which the *firm* is, or intends to, carry on through the *appointed representative*, including:

(1) ...

...

(3) ...; and

(4) ...; and

(5) where the *appointed representative* is not an individual, the name of the individuals who are responsible for the management of the business carried on by the *appointed representative* so far as it relates to *insurance mediation activity*.

...

12.7.4G (1) *Firms* can obtain a standard notification form from either the *FSA* website at [www.fsa.gov.uk](http://www.fsa.gov.uk) or by post from the Corporate Authorisation Department Monitoring and Notifications Department.

~~(2) A *firm's* notice under *SUP 12.7.1R* should be returned to the Corporate Authorisations Division at the address below.~~

...

Notification of changes in information given to the FSA

12.7.7 R

(1) If:

- (a) the scope of appointment of an appointed representative is extended to cover insurance mediation activities for the first time;
- (b) the appointed representative is not included on the Register as carrying on insurance mediation activities in another capacity; and
- (c) the scope of appointment of an appointed representative ceases to include insurance mediation activity;

the appointed representative's principal must give written notice to the FSA of that change before the appointed representative begins to carry on insurance mediation activities under the contract (see SUP 12.4.9G).

(+ 2) A firm must give written notice to the FSA of a any other change in any information provided to the FSA under SUP 12.7.1R, within ten *business days* of a the change being made or, if later, as soon as it becomes aware of the change. The notice must state the information that has changed.

(2 3) A firm's notification under (1) and (2) must be given to a member of or addressed for the attention of the Monitoring and Notifications Department ~~Corporate Authorisation department~~ at the address given in SUP 12.5.7R.

Notification of changes in conditions of appointment

12.7.8R

(1) A firm must give written notice to the FSA as soon as it has reasonable grounds to believe that any of the conditions in SUP 12.4.2R, ~~or SUP 12.4.6R~~ or SUP 12.4.8A R (as applicable) are not satisfied, or are likely not to be satisfied, in relation to any of its *appointed representatives*.

...

...

12.8.4 G

...

Removal of an appointed representative from the Register

12.8.5 G

The FSA has the power to remove from the Register an appointed representative, whose scope of appointment covers insurance mediation activities (see SUP 12.4.9G and SUP 12.4.10G).

...

Schedule 2  
Notification requirements

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
SUP 12.7.1R	<i>Appointed representatives</i>	...	A firm appointing an appointed representative	(1) (if the <u>appointment covers insurance mediation activities and the appointed representative is not included on the Register as carrying on such activities in another capacity</u> ) before; or  (2) (otherwise) <u>Ten business days after the appointment takes effect;</u>  <u>the appointed representative begins to carry on regulated activities under the contract.</u>
SUP 12.7.7R(1)	<u>Appointed representatives - extension of scope of appointment to cover insurance mediation activities for the first time</u>	<u>That fact</u>	<u>Extension of scope of appointment to cover insurance mediation activities for the first time and the appointed representative is not included on the Register as carrying on insurance mediation activities in another capacity</u>	<u>Before the appointed representative begins to carry on insurance mediation activities under the contract</u>
SUP 12.7.7R(2)	<i>Appointed representatives - change in other informatio</i>	...	A change being made to <del>the other</del> information provided under SUP 12.7.1R or the firm	...



	n		becoming aware of the change	
SUP 12.7.8R	<i>Appointed representatives</i> belief that appointment conditions not met		The <i>firm</i> having reasonable grounds for believing that the conditions in <i>SUP 12.4.2R</i> , <del>or</del> <i>SUP 12.4.6R</i> or <i>SUP 12.4.8A R</i> are not being satisfied.	
...			...	

### Amendments to the Decision making manual

DEC 2 Ann1 Statutory notice procedure: Warning notice and decision notice procedure

1 Table: List of warning notices and decision notices under the Act (other than Part VI) and certain other enactments

Note: Third party rights and access to *FSA* material apply to the powers listed in this table where indicated by an asterisk \* (see *DEC 2.4*)

...	...	...	...
Paragraph 20 of schedule 5	When the <i>FSA</i> is proposing/deciding to use the disqualification powers under section 249(1)*	<i>ENF 17</i>	<i>RDC</i>
<u>Insurance Intermediaries Order reference</u>	<u>Description</u>	<u>Handbook reference</u>	<u>Decision maker</u>
<u>Article 95(2)/(3)</u>	when the <i>FSA</i> is proposing/deciding not to include, or to remove, an <i>appointed representative</i> from the <i>Register</i> *	<i>SUP 12.4.10G</i>	<i>RDC</i>
<u>Article 95(7)/(8)</u>	when the <i>FSA</i> is proposing/deciding to refuse an application to revoke a determination not to include, or to remove, an <i>appointed representative</i> from the <i>Register</i> *	<i>SUP 12.4.10G</i>	<i>RDC</i>
Note 1: ...			
...			

...

4.1.4G The RDC has responsibility for *statutory notice decisions* and *statutory notice associated decisions* if the FSA proposes or takes any of the following actions:

(1) ...

...

(17) ...; ~~and~~

(18) ...; ~~and~~

(19) not to include, or to remove, an appointed representative from the Register, or to refuse an application to revoke such a determination.

### Amendments to the Glossary

Insert the following new definition in the appropriate alphabetical position.

*relevant investment* (in accordance with article 3(1) of the *Regulated Activities Order* (Interpretation)):

- (a) a *contractually based investment*;
- (b) a *pure protection contract*;
- (c) a *general insurance contract*;
- (d) rights to or interests in an *investment* falling within (a).

Amend the following definition as shown. Underlining indicates new text and striking through indicated deleted text.

*making arrangements with a view to transactions in investments* the *regulated activity*, specified in article 25(2) of the *Regulated Activities Order*, which is in summary: making arrangements with a view to a *person* who participates in the arrangements *buying, selling*, subscribing for or underwriting any of the following *investments* (whether as principal or as agent):

- (a) a *designated investment*;
- (b) a *funeral plan contract*;
- (c) the *underwriting capacity of a Lloyd's syndicate*;
- (d) *membership of a Lloyd's syndicate*;
- (e) *rights to or interests in investments* in (b), (c) or (d);
- (f) a *pure protection contract*;
- (g) a *general insurance contract*.

## ADDENDUM

### APPOINTED REPRESENTATIVES INSTRUMENT 2004

Annex A of this instrument is amended by the substitution of 9B for 9A in column 1 of SUP Transitional provisions, Table 2. In this Addendum, underlining indicates new text and striking through indicates deleted text.

SUP Transitional provisions, Table 2

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
9	...				
<del>9A</del> <u>B</u>	<i>SUP 12.5</i>	R	<i>A firm conducting designated investment business need not amend its written contract with an appointed representative (appointed before 15 January 2004) to take account of amendments to SUP 12.5 coming into force between 30 June 2004 and 30 June 2005, until 30 June 2005 or the date on which the contract is next updated (whichever is earlier).</i>	From 30 June 2004 until 30 June 2005, that is, 12 months.	<i>Commencement, and as amended with effect from 30 June 2004</i>
...					

...

**BANK AND BUILDING SOCIETY REPORTING  
CHANGES INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (the "Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 March 2004.

**Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with the Annexes A to C to this instrument.

**Citation**

- E. This instrument may be cited as the Bank and Building Society Reporting Changes Instrument 2004.

By Order of the Board  
15 January 2004

## Annex A

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

16.7.12R Table: Financial reports from a bank established outside the EEA (see SUP 16.7.11R):

Content of report	Form (Note)	Frequency	Due date
<u>Annual report and audited accounts, in English</u>	<u>N/A</u>	<u>Annually</u>	<u>9 months after the firm's accounting reference date</u>
...			

#### Method of submission

16.7.13R A bank, other than an EEA bank with permission for cross-border services only, must submit the reports described in SUP 16.7.8R, SUP 16.7.10R and SUP 16.7.12R to the following

(1) ...

...

16.7.15R ~~Electronic submission to the Bank of England~~

A bank must submit the reports referred to in SUP 16.7.13R(1) either:

- (1) on paper by post, or by hand delivery to the Bank of England on any business day between 9am and 5pm; or
- (2) in electronic format using the specifications for the Bank of England Reporting System and sent either:
  - (a) by the AT&T Global Network to one of the addresses specified in the above specification; ~~or~~
  - (b) by e-mail to mfsd\_beers@bofe.co.uk; or
  - (c) on computer diskette but to paper reporting deadlines by post, or by hand delivery to the Bank of England on any business day between 9am and 5pm.

...

16.7.19R A building society must submit the reports in SUP 16.7.17R (other than the “analysis of interest rate gap”) either:

- (1) by means of the Remote Data Entry system supplied by the FSA (and previously the Building Societies Commission); or, should

this be inoperable.

- (2) by post or fax to the address in *SUP* 16.3.10R using:
- (a) the pre-printed forms supplied by the FSA for that purpose  
the corresponding forms available from the FSA's website;  
or
  - (b) its own version of the *FSA's* specified forms, provided that the version is equivalent in terms of content and layout.

Notwithstanding a paper submission in accordance with (2), once the Remote Data Entry system is operable again, the reports must be submitted by its means.

...

SUP16, Ann 2G: Guidance notes on completion of banks' reporting forms (including validations)

...

Analysis of Profits, Large Exposures and Certain Other Miscellaneous Information (Form B7)

...

## **1.6 Other operating income**

...

Investment securities are defined as securities intended for use on a continuing basis in the activities of the bank, but securities should not be treated as investment securities unless they are held for identified purpose and the securities held are clearly identifiable. From March 2004, no further breakdown of this figure is needed. ~~Amounts within other operating income that represent more than 5% of the total income figure (item 1) should be entered in items 1.6A, 1.6B and 1.6C in descending order of size. Ignore further items if there are more than three breaking the 5% limit.~~

...

## **2.7 Other operating charges**

Include here those items of expenditure which do not fall within items 2.1 to 2.56. No further breakdown of this figure is needed from March 2004. ~~Amounts within other operating charges which represent more than 5% of the total expenditure figure (item 2) should be entered in items 2.7A, 2.7B and 2.7C in descending order of size. Ignore further items if there are more than three breaking the 5% limit.~~

...

## **LARGE EXPOSURES**

### **11 Twenty largest exposures to banks and building societies**

From March 2004, this item should not be completed. ~~List in descending order of magnitude (ie the largest exposure first) the twenty largest credit exposures to banks and building societies. The listing should commence on line 11A. Each large exposure should only be~~

reported once, at the top level. The total of each column of the large exposures should be entered on the first line.

For the definitions of exposures and counterparties which should be used (see SGN9 to SGN13), for banks, see SGN20 (excluding investment firms).

Exposures of up to and including 1 year remaining maturity at the reporting date should be reported in column 4.

For interest rate and foreign exchange rate contracts, the amounts at risk should be reported as the “credit equivalent amount” using the same basis of valuation as in item 9.

## 12 Twenty largest exposures to other counterparties

From March 2004, this item should not be completed. List in descending order of magnitude (ie the largest exposure first) the twenty largest credit exposures to counterparties other than those covered in item 11 (both UK and overseas). Include the non-bank private sector, central banks, international organisations (including regional development banks and the Bank for International Settlements (BIS)), and the UK and overseas public sectors. The listing should commence on line 12A. Each large exposure should only be reported once, at the top level. The total of each column of the large exposures should be entered on the first line.

See SGN9 to SGN13, SGN18, SGN20 to SGN23.

Exposures of up to and including 1 year remaining maturity at the reporting date should be reported in column 4.

For interest rate and foreign exchange rate contracts, the amounts at risk should be reported as the “credit equivalent amount” using the same basis of valuation as in item 9.

Exposures should be valued in accordance with the Supervisory Guidance Notes, except that, in the circumstances below, the exposure should be measured as less than the nominal exposure. In reporting large exposures, credit balances should not be offset against debit balances unless consistent with Chapter NE (Collateral and netting) of the FSA Banking Supervisory Policy Guide or the Interim Prudential Sourcebook for Banks, whichever is current at the reporting date.

### Underwriting commitments

The exposure arising from underwriting commitments should be taken as the full amount of the sum underwritten, less amounts of the issue which the reporting bank has sub-underwritten with, or sold to, another counterparty.

...

## INTERNAL VALIDATIONS

Ref no                    B7 item  
                                  numbers

...

28	11LE1	=	11LE1A + 11LE1B + 11LE1C + 11LE1D + 11LE1E + 11LE1F + 11LE1G + 11LE1H + 11LE1J + 11LE1K + 11LE1L + 11LE1M + 11LE1N + 11LE1P + 11LE1Q + 11LE1R + 11LE1S + 11LE1T + 11LE1U + 11LE1V <u>Removed March 2004</u>
----	-------	---	--

29	11LE2	=	11LE2A + 11LE2B + 11LE2C + 11LE2D + 11LE2E + 11LE2F + 11LE2G + 11LE2H + 11LE2J + 11LE2K + 11LE2L + 11LE2M + 11LE2N + 11LE2P + 11LE2Q + 11LE2R + 11LE2S + 11LE2T + 11LE2U + 11LE2V <u>Removed March 2004</u>
30	11LE3	=	11LE3A + 11LE3B + 11LE3C + 11LE3D + 11LE3E + 11LE3F + 11LE3G + 11LE3H + 11LE3J + 11LE3K + 11LE3L + 11LE3M + 11LE3N + 11LE3P + 11LE3Q + 11LE3R + 11LE3S + 11LE3T + 11LE3U + 11LE3V <u>Removed March 2004</u>
31	11LE4	=	11LE4A + 11LE4B + 11LE4C + 11LE4D + 11LE4E + 11LE4F + 11LE4G + 11LE4H + 11LE4J + 11LE4K + 11LE4L + 11LE4M + 11LE4N + 11LE4P + 11LE4Q + 11LE4R + 11LE4S + 11LE4T + 11LE4U + 11LE4V <u>Removed March 2004</u>
32	11LE5	=	11LE5A + 11LE5B + 11LE5C + 11LE5D + 11LE5E + 11LE5F + 11LE5G + 11LE5H + 11LE5J + 11LE5K + 11LE5L + 11LE5M + 11LE5N + 11LE5P + 11LE5Q + 11LE5R + 11LE5S + 11LE5T + 11LE5U + 11LE5V <u>Removed March 2004</u>
33	12LE1	=	12LE1A + 12LE1B + 12LE1C + 12LE1D + 12LE1E + 12LE1F + 12LE1G + 12LE1H + 12LE1J + 12LE1K + 12LE1L + 12LE1M + 12LE1N + 12LE1P + 12LE1Q + 12LE1R + 12LE1S + 12LE1T + 12LE1U + 12LE1V <u>Removed March 2004</u>
34	12LE2	=	12LE2A + 12LE2B + 12LE2C + 12LE2D + 12LE2E + 12LE2F + 12LE2G + 12LE2H + 12LE2J + 12LE2K + 12LE2L + 12LE2M + 12LE2N + 12LE2P + 12LE2Q + 12LE2R + 12LE2S + 12LE2T + 12LE2U + 12LE2V <u>Removed March 2004</u>
35	12LE3	=	12LE3A + 12LE3B + 12LE3C + 12LE3D + 12LE3E + 12LE3F + 12LE3G + 12LE3H + 12LE3J + 12LE3K + 12LE3L + 12LE3M + 12LE3N + 12LE3P + 12LE3Q + 12LE3R + 12LE3S + 12LE3T + 12LE3U + 12LE3V <u>Removed March 2004</u>
36	12LE4	=	12LE4A + 12LE4B + 12LE4C + 12LE4D + 12LE4E + 12LE4F + 12LE4G + 12LE4H + 12LE4J + 12LE4K + 12LE4L + 12LE4M + 12LE4N + 12LE4P + 12LE4Q + 12LE4R + 12LE4S + 12LE4T + 12LE4U + 12LE4V <u>Removed March 2004</u>
37	12LE5	=	12LE5A + 12LE5B + 12LE5C + 12LE5D + 12LE5E + 12LE5F + 12LE5G + 12LE5H + 12LE5J + 12LE5K + 12LE5L + 12LE5M + 12LE5N + 12LE5P + 12LE5Q + 12LE5R + 12LE5S + 12LE5T + 12LE5U + 12LE5V <u>Removed March 2004</u>
38	8	=	8.1 + 8.2 + 8.3 + 8.4 + 8.5 (Replaces validation 8, SRN/2001/1)
39	1.6A	≤	1.6 (Replaces validation 20, SRN/2001/1) <u>Removed March 2004</u>
40	1.6B	≤	1.6 (Replaces validation 21, SRN/2001/1) <u>Removed March 2004</u>
41	1.6C	≤	1.6 (Replaces validation 22, SRN/2001/1) <u>Removed March 2004</u>
42	1.6	≥	1.6A + 1.6B + 1.6C (Replaces validation 23, SRN/2001/1) <u>Removed March 2004</u>
43	2.7A	≤	2.7 (Replaces validation 24, SRN/2001/1) <u>Removed March 2004</u>
44	2.7B	≤	2.7 (Replaces validation 25, SRN/2001/1) <u>Removed March 2004</u>
45	2.7C	≤	2.7 (Replaces validation 26, SRN/2001/1) <u>Removed March 2004</u>
46	2.7	≥	2.7A + 2.7B + 2.7C (Replaces validation 27, SRN/2001/1) <u>Removed March 2004</u>
47	...		



...

## **BSD3 REPORTING INSTRUCTIONS**

...

### **SECTION A: BANKING BOOK**

...

#### **A330 Encumbered assets**

List in these lines any assets not freely available to meet the claims of the generality of creditors in a liquidation of the reporting institution because they are subject to charge, pledge or other restriction.

~~From March 2004, no further breakdown is needed for this item. So items A330.1 and A 330.2 should be zero. Under item A330.1, list the assets and the item number (indicating whether in the Banking Book or Trading Book) within the return to which they refer, which have been given as security in connection with the reporting institution's participation in a payments/settlements system such as CREST or Euroclear. The particular payments/settlements system should be listed with the liabilities being secured at the reporting date recorded under column 1. For the purposes of detailing the total amount of assets securing liabilities, assets pledged in excess of the actual liability to individual systems at the reporting date should not be reported.~~

~~Under item A330.2, list the assets and the item number on the return to which they refer, which have been given as security to secure the reporting institution's other liabilities (for example, property which has been mortgaged and hire purchase agreements pledged as collateral). Assets reported should exclude any element of unearned finance charges.~~

~~Total liabilities being secured at the reporting date (item A330, column 1) should equal the sum of items A330.1 and A330.2 below. Total assets at the reporting date securing liabilities reported in column 1 (item A330, column 2) will not necessarily equal the sum of items A330.1 and A330.2 below as any asset which is securing more than one creditor should not be double counted in the total.~~

...

#### **A790 Subordinated term debt**

...

~~Dated preference shares and subordinated, unsecured loan stocks of over 5 years' original maturity issued by the reporting institution should be shown after amortisation in item A790.2. From March 2004, no further breakdown of this figure is needed. So items A790.21 and A790.22 should be zero.The amount shown in item A790.2 should be further divided between items A790.21 and A790.22 as necessary in the relevant sub-total boxes. The amount of principal outstanding before amortisation should also be entered in the sub-total boxes in the "amount" column in the currency of repayment, which should be entered in the "currency" column. The "sterling equivalent" is then this amount converted to sterling at the current exchange rate for the currency concerned on the day of the report unless, via a subordinated swap or some other hedging mechanism that is an integral part of the original~~

~~preference share or subordinated loan stock agreement, the exchange rate has effectively been fixed – in which case that fixed rate may with be used. The reporting institution should obtain the FSA’s agreement before doing this.~~

~~Individual stocks which are repayable in full on maturity should be listed in item A790.21 in lines a to e. Where there are more than five stocks issued (ie a to e) annotate the form “see attached list” in this section and attach a full list of such stocks. The amounts to be reported after amortisation are shown below and relate to the period between the date of the return and maturity date:~~

<u>Years to maturity</u>	<u>Amortised amount</u>
<del>more than 4</del>	<del>100% of nominal</del>
<del>less than and including 4 but more than 3</del>	<del>80% of nominal</del>
<del>less than and including 3 but more than 2</del>	<del>60% of nominal</del>
<del>less than and including 2 but more than 1</del>	<del>40% of nominal</del>
<del>less than and including 1</del>	<del>20% of nominal</del>

~~The amount of subordinated, unsecured loan stock should be multiplied by the amortisation values shown above. In the case of optional repayment dates the longest date should be used to determine the final maturity if the exercise of the option lies with the issuer, and the shortest date if with investors.~~

~~Report in item A790.22 in lines a to h the original outstanding value of individual stocks which are repayable in instalments. Where banks have more than 10 such holdings, they may aggregate the smallest holdings (by value) and record the total under A190.21j and A790.22j. The amortised amount shown should be agreed with the FSA.~~

...

## **BSD3-SECTION B: TRADING BOOK FOR SOLO BANK AND LINE BY LINE CONSOLIDATED ENTITIES**

...

### **APPENDIX B-IV: COUNTERPARTY RISK ON REPOS AND REVERSE REPOS**

...

#### **Counterparty Risk On Documented Repos/Reverse Repos**

...

~~When completing Lines 60 to 90 and Lines 110 to 140, it should be assumed that each individual repo or reverse repo cannot be over collateralised in the absence of netting any over-collateralisation should be shown. However, ~~Regarding regarding~~ repos (lines 60 to 90): if collateral held is worth more than 100% of the market value of the securities sold or lent, then ~~the reported value of the collateral on that deal should be the same as the market value of the securities~~ the figure reported as the amount at risk in Column 3 should be the higher of zero or the excess of Column 1 over Column 2. Excess collateral held for a repo with one counterparty should not offset a shortfall in collateral held for another repo with the same counterparty or another counterparty. Regarding reverse repos (lines 110 to 140): if the market value of securities bought or borrowed on a reverse repo is more than 100% of the~~

market value of the collateral given, ~~the reported value of the securities on that deal should be the same as the market value of the collateral~~ the figure reported as the amount at risk in Column 3 should be the higher of zero or the excess of column 1 over column 2. Excess securities received under a reverse repo with one counterparty should not offset a shortfall in securities received under another reverse repo with the same counterparty or another counterparty.

...

In ~~both~~ all cases, Column 3 should be Column 1 minus Column 2 (or zero, in the case of items 60 to 90 and 110 to 140 if that is greater). The weighted amount in Column 5 should be the multiple of the amount at risk (Column 3) and the Weight (Column 4). Item 100 is the sum of the Weighted Amount (Column 5) in rows 60 to 90. Item 150 is the sum of the Weighted Amount (Column 5) in rows 110 to 140.

...

## **BSD SECTION C – CONSOLIDATION VIA AGGREGATION PLUS INTO THE TRADING BOOK**

...

### **Column B ~~Trigger~~ Individual capital ratio applied**

Where the *FSA*'s requirements are applied, the ~~trigger~~ individual capital ratio applied should be the consolidated Trading Book ~~trigger ratio~~ individual capital ratio. The ratio (ie percentage rounded to 2 decimal places) should be multiplied by 100 and reported as integers (eg, a ratio of 8.50% should be reported as 850).

...

### **Column C ~~Trigger~~ Individual capital requirement**

Institutions should report here for each subsidiary the total capital requirement set by the supervisor whose rules or requirements are applied. If the *FSA* requirements are applied, the capital charges should be calculated for the subsidiary in accordance with Chapters CS (Consolidated supervision) and CO (Capital adequacy overview) of ~~the FSA Policy Guide~~ *IPRU(BANK)* and should be scaled up (ie the capital charge divided by 8% and multiplied by the ~~trigger~~ individual capital ratio) by the institution's consolidated Trading Book ~~trigger~~ individual capital ratio.

If another (CAD-equivalent) supervisor's rules are applied, the capital requirement is the amount set by that supervisor. *FSA*'s consolidated Trading Book ~~trigger~~ individual capital ratio should not be applied.

...

### **Column L Target capital requirement**

For banks which have been set a Trading Book individual capital requirement, this column should equal Column C. Report here the capital requirement when the target ratio is applied. Where the *FSA* requirements are applied to a subsidiary, the capital requirements reported in Column C should be multiplied by the consolidated Trading Book target ratio and divided by the consolidated Trading Book ~~trigger~~ individual capital ratio. Capital requirements for subsidiaries consolidated using local regulators' rules need not be scaled up.

...

### **BSD3 SECTION D: CAPITAL ADEQUACY SUMMARY**

...

#### **D50 Banking Book ~~trigger~~ individual capital ratio**

This item equals the Banking Book ~~trigger~~ individual capital ratio (formerly the trigger ratio) set by the *FSA*. The ratio (ie percentage rounded to 2 decimal places) should be multiplied by 100 and reported as integers (eg, a ratio of 10.5% should be reported as 1050).

#### **D60 Banking Book target ratio**

Where an institution has had an individual capital ratio set by the *FSA*, this box should be left blank (ie zero). Prior to the introduction of individual capital ratios, ~~This~~ this item equals equalled the Banking Book target ratio set by the *FSA*. The ratio (ie percentage rounded to 2 decimal places) ~~should be~~ was multiplied by 100 and reported as integers (eg, a ratio of 12% should be reported as 1200).

...

#### **D140 Trading Book ~~trigger~~ individual capital ratio**

This is the Trading Book individual capital ~~trigger~~ ratio set by the *FSA* for CAD banks. The ratio (ie percentage rounded to 2 decimal places) should be multiplied by 100 and reported as integers (eg, a ratio of 11% should be reported as 1100).

#### **D150 Trading Book target ratio**

Where an institution has a Trading Book individual capital ~~This is the Trading Book target~~ ratio set by the *FSA* for CAD banks, this box should be left blank (ie zero). Prior to the introduction of Trading Book individual capital ratios, this item equalled the Trading Book target ratio set by the *FSA*. The ratio (ie percentage rounded to 2 decimal places) ~~should be~~ was multiplied by 100 and reported as integers (eg, a ratio of 11.50% should be reported as 1150).

...

#### **D530 ~~Trigger~~ Individual capital adequacy ratio**

This is the institution's capital adequacy relative to its individual capital ~~trigger~~ requirements. It is the ratio of the institution's adjusted capital base to its supervisory capital requirement according to the ~~trigger~~ individual capital ratios set by the *FSA* (or by the local regulator for entities consolidated using the aggregation plus methodology). The ratio is expressed as a percentage: an institution with a trigger an individual capital adequacy ratio less than 100 has insufficient capital to meet its regulatory requirements and it should contact its line supervisor immediately. This item should equal (item D490 multiplied by 100) and divided by item D500.

...

#### **D540 Target capital adequacy ratio**

~~This is the institution's capital adequacy relative to its supervisory target capital requirements. It is the ratio of the institution's adjusted capital base to its supervisory capital requirement according to the target ratios set by the *FSA*. The ratio is~~

expressed as a percentage: an institution with a target capital adequacy ratio less than 100 has insufficient capital to meet its regulatory requirements and it should contact its line supervisor immediately. This item should equal item D490 multiplied by 100 and divided by the sum of (item D70 multiplied by item D60/1000, item D150 divided by item D140 and multiplied by items [D220 plus D250], and item C30 column L).

The ratio (ie percentage rounded to 2 decimal places) should be multiplied by 100 and reported as integers (eg, a ratio of 105.35% should be reported as 110535).

For institutions where an individual capital ratio has been set by the FSA this item, like items D60 and D150, should be left blank (ie be zero).

...

...

## SECTION A: BANKING BOOK

### INTERNAL VALIDATIONS

Ref no	Item number	
...		
30	<del>A330.01</del>	<del>=A330.11 + A330.21</del> <u>Removed March 2004</u>
31	<del>A330.02</del>	<del>≤ A330.12 + A330.22</del> <u>Removed March 2004</u>
32	<del>A330.01</del>	<del>≤ A770</del> <u>Removed March 2004</u>
33	<del>A330.02</del>	<del>≤ AB270 + AT270</del> <u>Removed March 2004</u>
...		
67	<del>A790.2</del>	<del>= AA790.21 + AA790.22</del> <u>Removed March 2004</u>
...		
<u>71</u>	<u>A472</u>	<u>= 0 (from SRN/1999/2)</u>
<u>72</u>	<u>A474</u>	<u>= 0 (from SRN/1999/2)</u>
...		

### APPENDIX A-V VALIDATIONS

Ref No	Appx A-V Item No	
...		
4	150	=80S <u>(Withdrawn March 2004)</u>
...		

## APPENDIX B-IV VALIDATIONS

Ref No	Appx B-IV Item No	
...		
12	<u>A60</u>	<u>=<del>S60 - C60</del> Replaced by validation 30, March 2004</u>
13	<u>W60</u>	<u>= Zero</u>
14	<u>A70</u>	<u>=<del>S70 - C70</del> Replaced by validation 31, March 2004</u>
15	<u><del>W70</del></u>	<u>=<del>10% x (S70 - C70)</del> Replaced by validation 32, March 2004</u>
16	<u>A80</u>	<u>=<del>S80 - C80</del> Replaced by validation 33, March 2004</u>
17	<u><del>W80</del></u>	<u>=<del>20% x (S80 - C80)</del> Replaced by validation 34, March 2004</u>
18	<u>A90</u>	<u>=<del>S90 - C90</del> Replaced by validation 35, March 2004</u>
19	<u><del>W90</del></u>	<u>=<del>S90 - C90</del> Replaced by validation 36, March 2004</u>
20	<u>W100</u>	<u>= W60 + W70 + W80 + W90</u>
21	<u>A110</u>	<u>=<del>C110 - S110</del> Replaced by validation 37, March 2004</u>
22	<u>W110</u>	<u>= Zero</u>
23	<u>A120</u>	<u>=<del>C120 - S120</del> Replaced by validation 38, March 2004</u>
24	<u><del>W120</del></u>	<u>=<del>10% x (C120 - S120)</del> Replaced by validation 39, March 2004</u>
25	<u>A130</u>	<u>=<del>C130 - S130</del> Replaced by validation 40, March 2004</u>
26	<u><del>W130</del></u>	<u>=<del>20% x (C130 - S130)</del> Replaced by validation 41, March 2004</u>
27	<u>A140</u>	<u>=<del>C140 - S140</del> Replaced by validation 42, March 2004</u>
28	<u><del>W140</del></u>	<u>=<del>C140 - S140</del> Replaced by validation 43, March 2004</u>
29	<u>W150</u>	<u>= W110 + W120 + W130 + W140</u>
<u>30</u>	<u>A60</u>	<u>= S60 - C60 if positive, else zero Introduced March 2004</u>
<u>31</u>	<u>A70</u>	<u>= S70 - C70 if positive, else zero Introduced March 2004</u>
<u>32</u>	<u>W70</u>	<u>= 10% x (S70 - C70) if positive, else zero Introduced March 2004</u>
<u>33</u>	<u>A80</u>	<u>= S80 - C80 if positive, else zero Introduced March 2004</u>
<u>34</u>	<u>W80</u>	<u>= 20% x (S80 - C80) if positive, else zero Introduced March 2004</u>
<u>35</u>	<u>A90</u>	<u>= S90 - C90 if positive, else zero Introduced March 2004</u>
<u>36</u>	<u>W90</u>	<u>= S90 - C90 if positive, else zero Introduced March 2004</u>
<u>37</u>	<u>A110</u>	<u>= S110 - C110 if positive, else zero Introduced March 2004</u>
<u>38</u>	<u>A120</u>	<u>= S120 - C120 if positive, else zero Introduced March 2004</u>
<u>39</u>	<u>W120</u>	<u>= 10% x (S120 - C120) if positive, else zero Introduced March 2004</u>
<u>40</u>	<u>A130</u>	<u>= S130 - C130 if positive, else zero Introduced March 2004</u>

41	<u>W130</u>	<u>= 20% x (S130 – C130) if positive, else zero</u> Introduced March 2004
42	<u>A140</u>	<u>= S140 – C140 if positive, else zero</u> Introduced March 2004
43	<u>W140</u>	<u>= S140 – C140 if positive, else zero</u> Introduced March 2004

...

## LIQUIDITY RETURN (FORM LR)

...

### D1F Total deposits

...

(f) All other issues of commercial paper and medium term notes, bonds, FRNs and other instruments, with the exception of subordinated loan capital of over two years' original maturity;

~~(g) Working capital provided by non-resident offices of the reporting institution.~~

~~Exclude any certificates of deposit which the reporting institution holds which it itself has issued;~~

~~(a) Any certificates of deposit which the reporting institution holds which it itself has issued;~~

~~(b) Working capital provided by non-resident offices of the reporting institution.~~

...

## M1 REPORTING INSTRUCTIONS

...

### 80 Holdings in excess of 10% of other credit and financial institutions' capital

~~This is the value of all holdings in List all credit and financial institutions in which the reporting institution has direct or indirect holdings which amount to more than 10% of the acquired institutions' capital; this the calculations may be based on information contained in public financial statements. Identify both the total value of the holdings and the amount by which they exceed 10% of the other credit or financial institutions' capital. Details of individual holdings are not needed from March 2004. Where banks have more than 10 such holdings, they may aggregate the smallest holdings (by value) and record the total under 80.10.~~

...

### 140 Five largest holdings in credit and financial institutions, at reporting date

~~From March 2004, this item should be zero, as no details are needed thereafter. Include the five largest holdings (taking direct and indirect together) in credit and financial institutions, ranked by the value of holdings. Include holdings taken in the Banking and Trading Books. Include the name of the credit and financial institution and the book value of the reporting institution's holding. Banks may agree a de minimis reporting level with their line supervisor.~~

...

...

### INTERNAL VALIDATIONS

Ref no	Item numbers	
3	80	= 80.01E + 80.02 E+ 80.03E + 80.04 E + 80.05E + 80.06E + 80.07E + 80.08E + 80.09E + 80.10E <u>Removed March 2004</u>
6	130	= <del>70-70.4-100</del> <u>Replaced by validation 13, March 2004</u>
13	130	= <u>70-70.4-110 From March 2004</u>

...

### Supervisory Guidance Notes (SGN)

...

3 The reporting dates for the various supervisory returns are set out on the front of the individual forms and are summarised below. The reporting schedule for January 2001 to December 2001 is contained in Appendix I detailed in SUP 16.7.

Frequency	Report	Reporting dates	Basis of reporting
Monthly	SLR1	Second Wednesday	Consolidated (unless agreed otherwise), UK banks
Quarterly	BSD3, M1	End calendar quarters, or at dates coinciding with the financial year end	Unconsolidated or solo consolidated, UK banks
	LE2	End calendar quarters, or at dates coinciding with the financial year end	Unconsolidated or solo consolidated and consolidated, UK banks
	LR	End February, May, August and November for Form BT monthly reporter, or end calendar quarters for Form BT quarterly reporter	Unconsolidated including any overseas branches or solo consolidated if capital and large exposures are reported on a solo-consolidated basis



(UK banks), or  
business conducted  
by EEA banks and  
banks established  
outside the EEA

Half yearly	<del>BSD3, M1</del>	<del>End June and December, or at dates coinciding with the financial year end</del>	<del>Consolidated, UK banks</del>
	B7	End June and December, or at dates coinciding with accounting periods	UK branches of banks incorporated outside the EEA <sup>1</sup> (banks established outside the EEA)

Footnote 1 ~~The EEA comprises the European Union and Norway, Iceland and Liechtenstein.~~

Note: As a consequence of removing this footnote, all subsequent footnotes in the Supervisory Reporting Notes will be renumbered.

...

## Appendix D

### Central banks (central monetary institutions)

...

European Union

...

Greece

Bank of Greece

Ireland

~~Central Bank of Ireland~~ Central Bank and Financial  
Services Authority of Ireland

...

## Appendix G

---

Eligible banks (banks whose acceptances are eligible for discount at the Bank of England)

An up-to-date list of eligible banks is available from the Bank of England's Internet site on [www.bankofengland.co.uk/markets/money/eligiblebanks.htm](http://www.bankofengland.co.uk/markets/money/eligiblebanks.htm).

~~This list (21 May 2001) is issued by the Bank of England.~~

~~An institution's appearance on the list should not be misconstrued as evidence that it is qualitatively different in terms of financial soundness, standards of conduct or otherwise, from institutions which are not included on the list. The inclusion of an institution on this list does not mean that the Bank of England in any way guarantees its obligations.~~

<del>ABN AMRO Bank NV</del>	<del>Robert Fleming &amp; Co Ltd</del>
<del>Allied Irish Banks plc</del>	<del>Fortis Bank S.A./N.V.</del>
<del>The Asahi Bank, Ltd</del>	<del>The Fuji Bank, Ltd</del>
<del>Australia &amp; New Zealand Banking Group Ltd</del>	<del>Halifax plc</del>
<del>Banca di Roma SpA</del>	<del>HSBC Bank plc</del>
<del>Banca Nazionale del Lavoro SpA</del>	<del>The Industrial Bank of Japan, Ltd</del>
<del>Banco Bilbao Vizcaya Argentaria SA</del>	<del>ING Bank NV</del>
<del>Banco Santander Central Hispano SA</del>	<del>IntesaBei SpA (Banca Intesa Banca Commerciale Italiana SpA)</del>
<del>Bank Austria AG</del>	<del>KBC Bank NV</del>
<del>Bank Brussels Lambert</del>	<del>Lloyds TSB Bank plc</del>
<del>Bank of America, NA</del>	<del>Lloyds TSB Scotland plc</del>
<del>The Bank of Ireland</del>	<del>Mellon Bank, NA</del>
<del>Bank of Montreal</del>	<del>Merita Bank plc</del>
<del>The Bank of Nova Scotia</del>	<del>The Mitsubishi Trust and Banking Corporation</del>
<del>Bank One, NA</del>	<del>Natexis Banques Populaires</del>
<del>Bank of Scotland</del>	<del>National Australia Bank Ltd</del>
<del>The Bank of Tokyo - Mitsubishi, Ltd</del>	<del>National Westminster Bank plc</del>
<del>Barelays Bank plc</del>	<del>Northern Bank Ltd</del>
<del>Bayerische Hypo- und Vereinsbank AG</del>	<del>Rabobank International (Coöperatieve Centrale Raiffeisen Boerenleenbank BA)</del>
<del>Bayerische Landesbank Girozentrale</del>	<del>N M Rothschild &amp; Sons Ltd</del>
<del>BNP Paribas</del>	<del>Royal Bank of Canada</del>
<del>Brown, Shipley &amp; Co Ltd</del>	<del>The Royal Bank of Scotland plc</del>
<del>The Chase Manhattan Bank</del>	<del>Sanpaolo IMI SpA</del>
<del>CIBC World Markets plc</del>	

Citibank NA	The Sanwa Bank, Ltd
Clydesdale Bank plc	Singer & Friedlander Ltd
Commerzbank AG	Skandinaviska Enskilda Banken AB (publ)
Commonwealth Bank of Australia	Société Générale
The Co-operative Bank plc	Standard Chartered Bank
Crédit Agricole Indosuez	Sumitomo Mitsui Banking Corporation
Crédit Industriel et Commercial	The Sumitomo Trust & Banking Co Ltd
Crédit Lyonnais	Svenska Handelsbanken AB (publ)
Credit Suisse First Boston	The Tokai Bank, Ltd
The Dai-ichi Kangyo Bank, Ltd	The Toronto-Dominion Bank
Danske Bank A/S	UBS AG
Den norske Bank ASA	UniCredito Italiano SpA
Deutsche Bank AG	Westdeutsche Landesbank Girozentrale
Dexia Banque Internationale à Luxembourg SA	Westpac Banking Corporation
Dresdner Bank AG	Yorkshire Bank plc <sup>22</sup>
Fleet National Bank	

...

## Appendix I

### REPORTING SCHEDULE FOR SUPERVISORY RETURNS 2001

- ~~This schedule covers the period from **January 2001 to December 2001**. Not all the forms listed may be required from every reporting institution. The most common exceptions are covered in the footnotes. Individual reporting institutions which have been requested specifically by the FSA not to complete certain forms, or complete them less frequently or at different days from those shown below, should continue to follow their special arrangements.~~
- ~~The submission of these forms is covered by the rules and guidance set out in *SUP 16.7.7R*—*SUP 16.7.15R*. Failure to submit a report in accordance with the rules in *SUP* Chapter 16 may lead to the imposition of a financial penalty and other disciplinary actions (see ENF 13.5) once the Financial Services and Markets Act 2001 comes into force.~~
- ~~**Institutions should note that the due dates set out below are based on the Bank Holidays applicable in England. The due dates should be adjusted to take account of local Bank Holidays (but not Public Holidays) and any waivers or concessions agreed with the FSA.** Reporting institutions should telephone their regular supervisor in the FSA in advance of any difficulty they may have in meeting a deadline.~~
- ~~Banks with any questions on this reporting schedule may also ring Financial Risk Analysis and Monitoring Unit, FSA on 020 7676 0660.~~

**Reporting date**      **Forms**

**Due dates**

**2001**

		<u>Paper reporters</u>	<u>Electronic reporters</u>		<u>Submitted to FSA</u>			
					Via MFSD, Bank of England	Direct to supervisor at FSA		
JANUARY	10	SLR1 <sup>1</sup>	Thursday	18/01/01	Thursday	18/01/01	X	
FEBRUARY	14	SLR1 <sup>1</sup>	Thursday	22/02/01	Thursday	22/02/01	X	
	28	LR <sup>7</sup>	Wednesday	14/03/01	Friday	16/03/01	X	
MARCH	14	SLR1 <sup>1</sup>	Thursday	22/03/01	Thursday	22/03/01	X	
	30	BSD3 <sup>3</sup> , M1 <sup>3,4</sup> , LR <sup>7</sup> , B7 <sup>5</sup>	Tuesday	17/04/01	Thursday	19/04/01	X	
	30	LE2 <sup>6</sup>	Tuesday	17/04/01	Thursday	19/04/01		X <sup>2</sup>
APRIL	11	SLR1 <sup>1</sup>	Monday	23/04/01	Monday	23/04/01	X	
MAY	9	SLR1 <sup>1</sup>	Thursday	17/05/01	Thursday	17/05/01	X	
	31	LR <sup>8</sup>	Thursday	14/06/01	Monday	18/06/01	X	
JUNE	13	SLR1 <sup>1</sup>	Thursday	21/06/01	Thursday	21/06/01	X	
	29	BSD3 <sup>3</sup> , M1 <sup>3,4</sup> , LR <sup>7</sup> , B7 <sup>5</sup>	Friday	13/07/01	Tuesday	17/07/01	X	
	29	LE2 <sup>6</sup> ,	Friday	13/07/01	Friday	13/07/01		X <sup>2</sup>
JULY	11	SLR1 <sup>1</sup>	Thursday	19/07/01	Thursday	19/07/01	X	
AUGUST	8	SLR1 <sup>1</sup>	Thursday	16/08/01	Thursday	16/08/01	X	
	31	LR <sup>8</sup>	Friday	14/09/01	Tuesday	18/09/01	X	
SEPTEMBER	12	SLR1 <sup>1</sup>	Thursday	20/09/01	Thursday	20/09/01	X	
	28	BSD3 <sup>3</sup> , M1 <sup>3,4</sup> , LR <sup>8</sup> , B7 <sup>5</sup>	Friday	12/10/01	Tuesday	16/10/01	X	
	28	LE2 <sup>6</sup> ,	Friday	12/10/01	Friday	12/10/01		X <sup>2</sup>
OCTOBER	10	SLR1 <sup>1</sup>	Thursday	18/10/01	Thursday	1/10/01	X	
NOVEMBER	14	SLR1 <sup>1</sup>	Thursday	22/11/01	Thursday	22/11/01	X	
	30	LR <sup>8</sup>	Friday	14/12/01	Tuesday	18/12/01	X	
DECEMBER	12	SLR1 <sup>1</sup>	Thursday	20/12/01	Thursday	20/12/01	X	
	31	BSD3 <sup>3</sup> , M1 <sup>3,4</sup> , LR <sup>7</sup> , B7 <sup>5</sup>	Tuesday	15/01/02	Thursday	17/01/02	X	
	31	LE2 <sup>6</sup> ,	Tuesday	15/01/02	Tuesday	15/01/02		X <sup>2</sup>

For footnotes, see over.

1. Form SLR1 should also be completed for any exception during the month. These exception reports should be submitted directly to your supervisor (and not the Bank of England).
2. Until notified by the FSA, these returns should be sent direct to your supervisor.
3. Forms BSD3 and M1 apply only to UK banks. They may be submitted alternatively on a different quarterly cycle to coincide with a reporting institution's accounting year end. Institutions wishing to report at dates which coincide with the financial year end should agree this with the FSA. For institutions reporting on an unconsolidated / solo consolidated basis, these forms must be completed within 10 business days of the reporting date (12 business days if reported electronically). Institutions reporting on a consolidated basis are required to submit Forms BSD3 and M1 at the reporting group's accounting year end and half year end. The consolidated forms must be returned within 20 business days of the reporting date (22 business days for electronic reporters).
4. Form M1 applies only to market makers holding loan capital issued by banks and non resident banks. These reporting institutions are required to submit Form M1 in conjunction with Form BSD3.

- ~~5. Form B7 applies only to UK branches of banks established outside the EEA. Banks may complete Form B7 at dates coinciding with their accounting year end: this should be agreed with the FSA.~~
- ~~6. Form LE2 applies only to UK banks. Those banks which complete Form LE2 on an unconsolidated basis should report at dates which coincide with Form BSD3. The form must be completed within 10 business days of the reporting date on an unconsolidated / solo consolidated basis, or 20 business days when completed on a consolidated basis.~~
- ~~7. Banks (other than those which report to the Bank of England on Form BT quarterly), should complete the Form LR as at end February, May, August and November. For those banks reporting to the Bank of England on Form BT quarterly, Form LR should be completed at end March, June, September and December.~~
- ~~8. These returns should be sent direct to your supervisor unless the FSA has requested otherwise.~~
- ~~9. Forms BSD3 and M1 apply only to UK banks. They may be submitted alternatively on a different quarterly cycle to coincide with a reporting institution's accounting year end. Institutions wishing to report at dates which coincide with the financial year end should agree this with the FSA. For institutions reporting on an unconsolidated / solo consolidated basis, these forms must be completed within 10 business days of the reporting date (12 business days if reported electronically). Institutions reporting on a consolidated basis are required to submit Forms BSD3 and M1 at the reporting group's accounting year end and half year end. The consolidated forms must be returned within 20 business days of the reporting date (22 business days for electronic reporters).~~
- ~~10. Form M1 applies only to UK banks which have been granted a trading book concession, or have qualifying holdings in non financial companies. These reporting institutions are required to submit Form M1 in conjunction with Form BSD3.~~

SUP 16.7 sets out the submission times allowed for the various reports required from banks.

## **Annex B**

### **Amendments to the Supervision manual**

In SUP16 Annex 1R, make the following changes.

In Form BSD3, amend pages 1, 42, 44 and 46 as shown.



# FORM BSD3 - Capital Adequacy Return



**Reporting institution** \_\_\_\_\_

as at.. 

--	--	--

  
(eg 31 12 2001)

FSA number \* 

--	--	--	--	--	--

Unconsolidated/solo consolidated/consolidated - tick as appropriate  
 Unconsolidated  Solo consolidated  Consolidated

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on Completion**

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA for guidance.
- 2 Complete the return quarterly on an unconsolidated/solo consolidated basis as at end of March, June, September and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (see SUP 8).
- 3 Complete the return half-yearly on a consolidated basis as at end of June and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (see SUP 8).
- 4 Enter amounts to the nearest thousands omitting £000s/€000s. Calculated amounts should be rounded to the nearest thousands, or two decimal places as appropriate.
- 5 For definitions of items, refer to the Guidance Notes
- 6 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 7 Submit within 10 business days for unconsolidated/solo consolidated returns and 20 business days for consolidated returns or 12 and 22 business days respectively for those institutions reporting electronically to:

**The Financial Services Authority  
 c/o Monetary and Financial Statistics Division  
 Domestic Banking Statistics (HO-4)  
 Bank of England  
 Threadneedle Street  
 London EC2R 8AH**

- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
--------------	-----------	--------------

September 2004 March 2004

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

# SECTION C - CONSOLIDATION VIA AGGREGATION PLUS (INTO THE TRADING BOOK)

## INVESTMENT FIRM SUBSIDIARIES

	A	B	C	D	E
	FSA=1 or local regulator's rules= 0 applied	Trigger Individual capital ratio applied = (% to 2d.px100)	(000)s Trigger/Individual capital requirement	(000)s Notional risk weighted assets	(000)s Incremental capital for large exposures
C10.1					
C10.2					
C10.3					
C10.4					
C10.5					
C10.6					
C10.7					
C10.8					
C10.9					
C10.10					
C10.11					
C10.12					
C10.13					
C10.14					

C10	TOTAL FOR INVESTMENT FIRMS.....				
-----	---------------------------------	--	--	--	--

## BANKING SUBSIDIARIES

C20.1					
C20.2					
C20.3					
C20.4					
C20.5					
C20.6					
C20.7					
C20.8					
C20.9					
C20.10					
C20.11					
C20.12					
C20.13					
C20.14					

C20	TOTAL FOR BANKING SUBSIDIARIES.....				
-----	-------------------------------------	--	--	--	--

C30	GRAND TOTAL				
-----	-------------	--	--	--	--



# SECTION D - CAPITAL ADEQUACY SUMMARY

## CAPITAL BASE

000s

D10	Tier 1 (A550) .....	
D20	Eligible Tier 2 (A630) .....	
D30	Eligible Tier 3 (A638) .....	
D40	TOTAL ELIGIBLE CAPITAL (D10 to D30) .....	

## BANKING BOOK CAPITAL REQUIREMENTS/RISK WEIGHTED ASSETS

D50	Banking Book Trigger <u>Individual Capital</u> Ratio (% multiplied by 100, ie input as integers)	
D60	Banking Book Target Ratio ( % multiplied by 100, ie input as integers) .....	
D70	Total Banking Book Risk Weighted Assets by risk weighting bands:..... by weighting bands:	
D70.1	Risk weighted at 0%.....	
D70.2	Risk weighted at 10%.....	
D70.3	Risk weighted at 20%.....	
D70.4	Risk weighted at 50%.....	
D70.5	Risk weighted at 100%.....	
D70.6	Items A452, A472 and A474 of Section A.....	
D80	<b>Banking Book Capital Requirements</b> .....	

## CAPITAL ALLOCATED TO THE BANKING BOOK

D90	Tier 1 capital.....	
D100	Eligible Tier 2 capital.....	
D110	Total capital allocated to the Banking Book (items D90 + D100) .....	

## TRADING BOOK CAPITAL REQUIREMENT/NOTIONAL RISK WEIGHTED ASSETS

D120	Exempt from CAD capital requirements at reporting date ? (please tick if yes) .....	Yes	<input type="checkbox"/>
D130	If yes, number of days over threshold in reporting period .....		
D140	Trading Book Trigger <u>Individual Capital</u> Ratio (% multiplied by 100, ie input as integers).....		
D150	Trading Book Target Ratio ( % multiplied by 100, ie input as integers) .....		

**DEDUCTIONS**

000s

D400	Investments in subsidiaries and associated companies (item A160).....	
D410	Connected lending of a capital nature (A280) .....	
D420	Off-balance sheet items of a capital nature.....	
D430	Investments in bank and financial firm capital (item A171).....	
D440	Qualifying holdings (item A180.4).....	
D450	Deduction plus consolidation.....	
D460	Other deductions.....	
D470	Total Deductions (items D400 to D460) .....	
D480	<b>OWN FUNDS</b> .....	
D490	<b>ADJUSTED CAPITAL BASE</b> .....	
D500	<b>TOTAL CAPITAL REQUIREMENTS</b> .....	
D510	<b>TOTAL RISK-WEIGHTED ASSETS</b> .....	
D520	<b>'PUBLISHED' RISK ASSET RATIO</b> ( % multiplied by 100, ie input as integers) .....	
D530	<b>TRIGGER <u>INDIVIDUAL</u> CAPITAL ADEQUACY RATIO</b> (% multiplied by 100, ie input as integers)	
D540	<b>TARGET CAPITAL ADEQUACY RATIO</b> ( % multiplied by 100, ie input as integers) .....	

## **Annex C**

### **Amendments to the Supervision manual**

In SUP16 Annex 2G, make the following changes.

Immediately before the BSD3 definitions, insert the following:

To be used for all reports completed as at 1 December 2001 or after

# FORM B7 - Analysis of profits, large exposures and certain other miscellaneous information



Reporting institution \_\_\_\_\_

Reporting date 

--	--	--

  
 eg            31            12            2001

FSA Number \* 

		F	S	A	
--	--	---	---	---	--

Please tick if this return is completed in Euros (Item A).....

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm that the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

\_\_\_\_\_ Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on Completion**

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA.
- 2 Complete the return half yearly as at end of June and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (see SUP 8).
- 3 Enter amounts to the nearest thousand omitting £000s/€000s. Calculated amounts should be rounded to the nearest thousand, or two decimal places as appropriate.
- 4 For definitions of items, refer to the Guidance Notes for the form.
- 5 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return
- 6 Submit the form within **10 business days**, or **12 business days** for those institutions reporting electronically, clearly addressed to:
 

**The Financial Services Authority**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**
- 7 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered

September 2001

\* This should be the FSA firm reference number. This box must be filled in by all reporters (SUP 16.3.7R).

# CURRENT YEAR'S PROFIT AND LOSS

Item No		000s	000s
<b>1</b>	<b>TOTAL INCOME</b> .....		<b>1</b>
1.1	Interest received and receivable.....	<b>1.1</b>	
1.2	Dividend income.....	<b>1.2</b>	
1.3	Fees and commissions received and receivable.....	<b>1.3</b>	
1.4	Dealing profit/(loss).....	<b>1.4</b>	
1.5	Intra-group income.....	<b>1.5</b>	
1.6	Other operating income including:.....	<b>1.6</b>	
	<i>of which:</i>		
1.6A		<b>1.6A</b>	
1.6B		<b>1.6B</b>	
1.6C		<b>1.6C</b>	
<b>2</b>	<b>TOTAL EXPENDITURE</b> .....		<b>2</b>
2.1	Interest paid and payable.....	<b>2.1</b>	
2.2	Fees and commissions paid and payable.....	<b>2.2</b>	
2.3	Staff expenses.....	<b>2.3</b>	
2.4	Other administrative expenses.....	<b>2.4</b>	
2.5	Depreciation.....	<b>2.5</b>	
2.6	Intra-group expenditure.....	<b>2.6</b>	
2.7	Other operating charges including:.....	<b>2.7</b>	
	<i>of which:</i>		
2.7A		<b>2.7A</b>	
2.7B		<b>2.7B</b>	
2.7C		<b>2.7C</b>	
<b>3</b>	<b>OPERATING PROFIT</b> .....		<b>3</b>
<b>4</b>	<b>TOTAL PROVISIONS</b> .....		<b>4</b>
4.1	Provisions for bad and doubtful debts.....	<b>4.1</b>	
4.2	Provisions for contingent liabilities and commitments.....	<b>4.2</b>	
4.3	Taxation.....	<b>4.3</b>	
4.4	Provisions / amounts written off fixed asset investments.....	<b>4.4</b>	
<b>5</b>	<b>CURRENT YEAR'S PROFIT AND LOSS</b> .....		<b>5</b>
		<b>B7.1.1</b>	

# BALANCE SHEET ANALYSIS

Item No		000s	000s
		Market valuation	Book value
		┌	┐
<b>6</b>	<b>TOTAL INVESTMENTS .....</b>		<b>6</b>
6.1	Quoted: British Government stock.....	<b>M6.1</b>	<b>B6.1</b>
6.2	Other public sector (UK only).....	<b>M6.2</b>	<b>B6.2</b>
6.3	Equities.....	<b>M6.3</b>	<b>B6.3</b>
6.4	Overseas Government stock.....	<b>M6.4</b>	<b>B6.4</b>
6.5	Other investments.....	<b>M6.5</b>	<b>B6.5</b>
6.6	Unquoted: Public sector (UK only).....		<b>B6.6</b>
6.7	Equities.....		<b>B6.7</b>
6.8	Overseas Public sector.....		<b>B6.8</b>
6.9	Other investments.....		<b>B6.9</b>
		┌	┐
		<b>B7.1.2</b>	

# OFF-BALANCE-SHEET ITEMS

Item No

000s

000s

**7 TOTAL CONTINGENT LIABILITIES**.....

7.1 Acceptances and endorsements.....

7.2 Guarantees and irrevocable letters of credit.....

7.3 Assets pledged by the bank as collateral security.....

7.4 Other contingent liabilities.....

		<b>7</b>
	<b>7.1</b>	
	<b>7.2</b>	
	<b>7.3</b>	
	<b>7.4</b>	

**8 TOTAL COMMITMENTS**.....

8.1 Sale and option to resell transactions.....

8.2 Documentary credits and short-term trade-related transactions.....

8.3 Forward asset purchases and forward deposits placed.....

8.4 Undrawn facilities.....

8.5 Other commitments.....

		<b>8</b>
	<b>8.1</b>	
	<b>8.2</b>	
	<b>8.3</b>	
	<b>8.4</b>	
	<b>8.5</b>	

**9 EXCHANGE RATE AND INTEREST RATE RELATED CONTRACTS**

9.1 Exchange rate contracts principal amount.....

9.2 credit equivalent.....

9.3 Interest rate contracts principal amount.....

9.4 credit equivalent.....

	Less than 1 year	1 year and over
	<b>L9.1</b>	<b>M9.1</b>
	<b>L9.2</b>	<b>M9.2</b>
	<b>L9.3</b>	<b>M9.3</b>
	<b>L9.4</b>	<b>M9.4</b>

**Original exposure method / replacement cost method**

9M Please tick if using replacement cost method

**B7.1.3**

# MEMORANDUM ITEMS

Item No		000s	000s	000s		
<b>10</b>	<b>PROVISIONS AGAINST BAD AND DOUBTFUL DEBTS</b>					
		mm	yyyy	Specific	General	Total
10.1	Previous balance as at (mm/yyyy).....			<b>S10.1</b>	<b>G10.1</b>	<b>T10.1</b>
10.2	Adjustments for exchange rate movements.....			<b>S10.2</b>	<b>G10.2</b>	<b>T10.2</b>
10.3	Charge (credit) to profit and loss*.....			<b>S10.3</b>	<b>G10.3</b>	<b>T10.3</b>
10.4	Amounts written off.....			<b>S10.4</b>	<b>G10.4</b>	<b>T10.4</b>
10.5	Recoveries of amounts previously written off.....			<b>S10.5</b>	<b>G10.5</b>	<b>T10.5</b>
10.6	Other.....			<b>S10.6</b>	<b>G10.6</b>	<b>T10.6</b>
10.7	Current balance.....			<b>S10.7</b>	<b>G10.7</b>	<b>T10.7</b>

\* This should equal item 4.1

**B7.1.4**



## 11 TWENTY LARGEST EXPOSURES TO BANKS AND BUILDING SOCIETIES

000s

(irrespective of currency)

	Counterparty	Total Exposure*	of which the total exposure is:			Specific bad debt provisions made against exposures reported in column 1
			On balance sheet	Denominated in sterling	1 year or less to maturity	
		1	2	3	4	5
	<b>TOTAL</b>	<b>11LE1</b>	<b>11LE2</b>	<b>11LE3</b>	<b>11LE4</b>	<b>11LE5</b>
A	11LENA	11LE1A	11LE2A	11LE3A	11LE4A	11LE5A
B	11LENB	11LE1B	11LE2B	11LE3B	11LE4B	11LE5B
C	11LENC	11LE1C	11LE2C	11LE3C	11LE4C	11LE5C
D	11LEND	11LE1D	11LE2D	11LE3D	11LE4D	11LE5D
E	11LENE	11LE1E	11LE2E	11LE3E	11LE4E	11LE5E
F	11LENF	11LE1F	11LE2F	11LE3F	11LE4F	11LE5F
G	11LENG	11LE1G	11LE2G	11LE3G	11LE4G	11LE5G
H	11LENH	11LE1H	11LE2H	11LE3H	11LE4H	11LE5H
J	11LENJ	11LE1J	11LE2J	11LE3J	11LE4J	11LE5J
K	11LENK	11LE1K	11LE2K	11LE3K	11LE4K	11LE5K
L	11LENL	11LE1L	11LE2L	11LE3L	11LE4L	11LE5L
M	11LENM	11LE1M	11LE2M	11LE3M	11LE4M	11LE5M
N	11LENN	11LE1N	11LE2N	11LE3N	11LE4N	11LE5N
P	11LENP	11LE1P	11LE2P	11LE3P	11LE4P	11LE5P
Q	11LENQ	11LE1Q	11LE2Q	11LE3Q	11LE4Q	11LE5Q
R	11LENR	11LE1R	11LE2R	11LE3R	11LE4R	11LE5R
S	11LENS	11LE1S	11LE2S	11LE3S	11LE4S	11LE5S
T	11LENT	11LE1T	11LE2T	11LE3T	11LE4T	11LE5T
U	11LENU	11LE1U	11LE2U	11LE3U	11LE4U	11LE5U
V	11LENV	11LE1V	11LE2V	11LE3V	11LE4V	11LE5V

\* Gross of bad debt provisions in column 5

B7.1.5

## 12 TWENTY LARGEST EXPOSURES TO OTHER COUNTERPARTIES

000s

(irrespective of currency)

	Counterparty	Total Exposure*	of which the total exposure is:			Specific bad debt provisions made against exposures reported in column 1
			On balance sheet	Denominated in sterling	1 year or less to maturity	
		1	2	3	4	5
	<b>TOTAL</b>	<b>12LE1</b>	<b>12LE2</b>	<b>12LE3</b>	<b>12LE4</b>	<b>12LE5</b>
A	<b>12LENA</b>	<b>12LE1A</b>	<b>12LE2A</b>	<b>12LE3A</b>	<b>12LE4A</b>	<b>12LE5A</b>
B	<b>12LENB</b>	<b>12LE1B</b>	<b>12LE2B</b>	<b>12LE3B</b>	<b>12LE4B</b>	<b>12LE5B</b>
C	<b>12LENC</b>	<b>12LE1C</b>	<b>12LE2C</b>	<b>12LE3C</b>	<b>12LE4C</b>	<b>12LE5C</b>
D	<b>12LEND</b>	<b>12LE1D</b>	<b>12LE2D</b>	<b>12LE3D</b>	<b>12LE4D</b>	<b>12LE5D</b>
E	<b>12LENE</b>	<b>12LE1E</b>	<b>12LE2E</b>	<b>12LE3E</b>	<b>12LE4E</b>	<b>12LE5E</b>
F	<b>12LENF</b>	<b>12LE1F</b>	<b>12LE2F</b>	<b>12LE3F</b>	<b>12LE4F</b>	<b>12LE5F</b>
G	<b>12LENG</b>	<b>12LE1G</b>	<b>12LE2G</b>	<b>12LE3G</b>	<b>12LE4G</b>	<b>12LE5G</b>
H	<b>12LENH</b>	<b>12LE1H</b>	<b>12LE2H</b>	<b>12LE3H</b>	<b>12LE4H</b>	<b>12LE5H</b>
J	<b>12LENJ</b>	<b>12LE1J</b>	<b>12LE2J</b>	<b>12LE3J</b>	<b>12LE4J</b>	<b>12LE5J</b>
K	<b>12LENK</b>	<b>12LE1K</b>	<b>12LE2K</b>	<b>12LE3K</b>	<b>12LE4K</b>	<b>12LE5K</b>
L	<b>12LENL</b>	<b>12LE1L</b>	<b>12LE2L</b>	<b>12LE3L</b>	<b>12LE4L</b>	<b>12LE5L</b>
M	<b>12LENM</b>	<b>12LE1M</b>	<b>12LE2M</b>	<b>12LE3M</b>	<b>12LE4M</b>	<b>12LE5M</b>
N	<b>12LENN</b>	<b>12LE1N</b>	<b>12LE2N</b>	<b>12LE3N</b>	<b>12LE4N</b>	<b>12LE5N</b>
P	<b>12LENP</b>	<b>12LE1P</b>	<b>12LE2P</b>	<b>12LE3P</b>	<b>12LE4P</b>	<b>12LE5P</b>
Q	<b>12LENQ</b>	<b>12LE1Q</b>	<b>12LE2Q</b>	<b>12LE3Q</b>	<b>12LE4Q</b>	<b>12LE5Q</b>
R	<b>12LENR</b>	<b>12LE1R</b>	<b>12LE2R</b>	<b>12LE3R</b>	<b>12LE4R</b>	<b>12LE5R</b>
S	<b>12LENS</b>	<b>12LE1S</b>	<b>12LE2S</b>	<b>12LE3S</b>	<b>12LE4S</b>	<b>12LE5S</b>
T	<b>12LENT</b>	<b>12LE1T</b>	<b>12LE2T</b>	<b>12LE3T</b>	<b>12LE4T</b>	<b>12LE5T</b>
U	<b>12LENU</b>	<b>12LE1U</b>	<b>12LE2U</b>	<b>12LE3U</b>	<b>12LE4U</b>	<b>12LE5U</b>
V	<b>12LENV</b>	<b>12LE1V</b>	<b>12LE2V</b>	<b>12LE3V</b>	<b>12LE4V</b>	<b>12LE5V</b>

\* Gross of bad debt provisions in column 5

B7.1.6

Immediately before the LE2 definitions, insert the following:



# FORM BSD3 - Capital Adequacy Return

Reporting institution \_\_\_\_\_

as at.. 

--	--	--

  
 (eg 31 12 2001)

FSA number \* 

		F	S	A	
--	--	---	---	---	--

Unconsolidated/solo consolidated/consolidated - tick as appropriate

Unconsolidated  Solo consolidated  Consolidated

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

Tel No \_\_\_\_\_ Ext \_\_\_\_\_

## Notes on Completion

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA for guidance.
- 2 Complete the return quarterly on an unconsolidated/solo consolidated basis as at end of March, June, September and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (SUP 8).
- 3 Complete the return half-yearly on a consolidated basis as at end of June and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (SUP 8).
- 4 Enter amounts to the nearest thousands omitting £000s/€000s. Calculated amounts should be rounded to the nearest thousands, or two decimal places as appropriate.
- 5 For definitions of items, refer to the Guidance Notes
- 6 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 7 Submit within 10 business days for unconsolidated/solo consolidated returns and 20 business days for consolidated returns or 12 and 22 business days respectively for those institutions reporting electronically to:

**The Financial Services Authority**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**

- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
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March 2004

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

A1 Please tick if completion in Euros .....

## SECTION A: BANKING BOOK

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Weight	Weighted Banking Book Amount (000s)
<b>ASSETS</b>					
A10	Cash.....	AT10	AB10	0%	
A20	Gold Bullion and coin.....	AT20	AB20	0%	
A30	Cash items in course of collection.....	AT30	AB30	20%	
A40	Items in suspense.....	AT40	AB40		
A40.1	.....		AB40.1	0%	
A40.2	.....		AB40.2	10%	
A40.3	.....		AB40.3	20%	
A40.4	.....		AB40.4	50%	
A40.5	.....		AB40.5	100%	

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Weight	Weighted Banking Book Amount (000s)
<b>LOANS, ADVANCES AND BILLS HELD</b>					
A50	Central governments and central banks	AT50	AB50		
A50.1	.....		AB50.1	0%	
A50.2	.....		AB50.2	10%	
A50.3	.....		AB50.3	20%	
A50.4	.....		AB50.4	100%	
A60	Lending to group companies	AT60	AB60		
A60.1	.....		AB60.1	0%	
A60.2	.....		AB60.2	10%	
A60.3	.....		AB60.3	20%	
A60.4	.....		AB60.4	100%	
A70	Banks and investment firms (inc building societies & MDBs) .....	AT70	AB70		
A70.1	.....		AB70.1	0%	
A70.2	.....		AB70.2	10%	
A70.3	.....		AB70.3	20%	
A70.4	.....		AB70.4	100%	
A80	Public sector entities	AT80	AB80		
A80.1	.....		AB80.1	0%	
A80.2	.....		AB80.2	10%	
A80.3	.....		AB80.3	20%	
A80.4	.....		AB80.4	100%	
A90	Loans secured on residential property..	AT90	AB90	50%	
A100	Other loans, advances and bills held....	AT100	AB100		
A100.1	.....		AB100.1	0%	
A100.2	.....		AB100.2	10%	
A100.3	.....		AB100.3	20%	
A100.4	.....		AB100.4	100%	
A110	Unanalysed.....	AT110	AB110	100%	

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Weight	Weighted Banking Book Amount (000s)
<b>INVESTMENTS</b>					
A120	Central governments and central banks..	AT120	AB120		
Banking Book Net Long					
A120.1	ANL120.1		AB120.1	0%	
A120.2	ANL120.2		AB120.2	10%	
A120.3	ANL120.3		AB120.3	20%	
A120.4	ANL120.4		AB120.4	100%	
A130	Public sector entities.....	AT130	AB130		
A130.1			AB130.1	10%	
A130.2			AB130.2	20%	
A130.3			AB130.3	100%	
A140	Banks (Unsubordinated FRNs etc)..	AT140	AB140		
A140.1			AB140.1	10%	
A140.2			AB140.2	20%	
A140.3			AB140.3	100%	
A150	Mortgage backed securities.....	AT150	AB150		
A150.1			AB150.1	10%	
A150.2			AB150.2	20%	
A150.3			AB150.3	50%	
A150.4			AB150.4	100%	
A160	Investments in subsidiaries ..... and associated companies	AT160	AB160		Deducted from Tier 1 & 2
A170	Investments in bank and financial firm capital	AT170	AB170		
A171		AT171	AB171		Deducted from Tier 1 & 2
A172	Trading Book or other concession (from Form M1).....	AT172	AB172	100%	
A180	Qualifying holdings / other investment.	AT180	AB180		
A180.1			AB180.1	10%	
A180.2			AB180.2	20%	
A180.3			AB180.3	100%	
A180.4	Deductions from Form M1 .....		AB180.4		Deducted from Tier 1 & 2
A190	Unanalysed.....	AT190	AB190	100%	

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Weight	Weighted Banking Book Amount (000s)
<b>OTHER ASSETS</b>					
A200	Goodwill.....	AT200	AB200		Deducted from Tier 1
A210	Other intangible assets.....	AT210	AB210		
A210.1	.....	AT210.1	AB210.1	100%	
A210.2	.....	AT210.2	AB210.2		Deducted from Tier 1
A220	Own premises .....	AT220	AB220	100%	
A230	Other property/real estate.....	AT230	AB230	100%	
A240	Operating leases.....	AT240	AB240		
A240.1	.....		AB240.1	0%	
A240.2	.....		AB240.2	20%	
A240.3	.....		AB240.3	100%	
A250	Plant, equipment and other fixed assets	AT250	AB250	100%	
A260	Other.....	AT260	AB260		
A260.1	.....		AB260.1	0%	
A260.2	.....		AB260.2	10%	
A260.3	.....		AB260.3	20%	
A260.4	.....		AB260.4	100%	
A265	Assets consolidated via aggregation plus.	AT265			
A270	<b>Total assets</b> (items A10 to A265).....	AT270	AB270		



Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Weight	Weighted Banking Book Amount (000s)
<b>MEMORANDUM ITEMS</b>					
A280	Connected lending of a capital nature..	AT280	AB280		Deducted from Tier 1 & Tier 2
A280.1	.....	AT280.1	AB280.1	0%	
A280.2	.....	AT280.2	AB280.2	10%	
A280.3	.....	AT280.3	AB280.3	20%	
A280.4	.....	AT280.4	AB280.4	50%	
A280.5	.....	AT280.5	AB280.5	100%	
A290	Loans to directors, controllers and their associates.....		AB290		
A290.1	.....		AB290.1	0%	
A290.2	.....		AB290.2	10%	
A290.3	.....		AB290.3	20%	
A290.4	.....		AB290.4	50%	
A290.5	.....		AB290.5	100%	
A300	Loans to non-group companies with which directors and controllers are associated.....		AB300		
A300.1	.....		AB300.1	0%	
A300.2	.....		AB300.2	10%	
A300.3	.....		AB300.3	20%	
A300.4	.....		AB300.4	50%	
A300.5	.....		AB300.5	100%	
A310	Direct credit substitutes given on behalf of connected counterparties.....		AB310		
A310.1	.....		AB310.1	0%	
A310.2	.....		AB310.2	10%	
A310.3	.....		AB310.3	20%	
A310.4	.....		AB310.4	50%	
A310.5	.....		AB310.5	100%	

**Item No**

**Item**

**MEMORANDUM ITEMS  
(Continued)**

Banking Book Amount (000s)

Weighted Banking Book Amount (000s)

A320	Investments in central governments and central banks..... (net short positions)	AB320		
A320.1	.....	AB320.1	0%	
A320.2	.....	AB320.2	10%	
A320.3	.....	AB320.3	20%	
A320.4	.....	AB320.4	100%	

	Col 1 Liabilities being secured at the reporting date	Col 2 Assets at the reporting date securing liabilities reported in column 1
A330	Encumbered assets.....	A330.01      A330.02
A330.1	Payment/settlement systems.....	A330.11      A330.12
	.....	.....
	.....	.....
	.....	.....
	.....	.....
A330.2	Other.....	A330.21      A330.22
	.....	.....
	.....	.....
	.....	.....
	.....	.....
A335	Total assets of "deduction plus" subsidiaries .....	A335

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Credit Conversion Factor	Weight	Weighted Banking Book Amount (000s)
<b>OFF BALANCE SHEET ITEMS</b>						
A340	Direct credit substitutes.....	AT340	AB340			
A340.1	.....		AB340.1	100%	0%	
A340.2	.....		AB340.2	100%	10%	
A340.3	.....		AB340.3	100%	20%	
A340.4	.....		AB340.4	100%	50%	
A340.5	.....		AB340.5	100%	100%	
A340.6	.....	AT340.6	AB340.6	Deducted from Tier 1 & 2		
A340.7	Unanalysed.....		AB340.7	100%	100%	
A350	Transaction-related contingents.....	AT350	AB350			
A350.1	.....		AB350.1	50%	0%	
A350.2	.....		AB350.2	50%	10%	
A350.3	.....		AB350.3	50%	20%	
A350.4	.....		AB350.4	50%	50%	
A350.5	.....		AB350.5	50%	100%	
A350.6	Unanalysed.....		AB350.6	50%	100%	
A360	Trade-related contingents.....	AT360	AB360			
A360.1	.....		AB360.1	20%	0%	
A360.2	.....		AB360.2	20%	10%	
A360.3	.....		AB360.3	20%	20%	
A360.4	.....		AB360.4	20%	50%	
A360.5	.....		AB360.5	20%	100%	
A360.6	Unanalysed.....		AB360.6	20%	100%	
A370	Sale and repurchase agreements...	AT370	AB370			
A370.1	.....		AB370.1	100%	0%	
A370.2	.....		AB370.2	100%	10%	
A370.3	.....		AB370.3	100%	20%	
A370.4	.....		AB370.4	100%	50%	
A370.5	.....		AB370.5	100%	100%	
A370.6	.....	AT370.6	AB370.6	Deducted from Tier 1 & 2		
A370.7	Unanalysed.....		AB370.7	100%	100%	

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Credit Conversion Factor	Weight	Weighted Banking Book Amount (000s)
<b>OFF BALANCE SHEET ITEMS (CONTINUED)</b>						
A380	Asset sales with recourse	AT380	AB380			
A380.1	.....		AB380.1	100%	0%	
A380.2	.....		AB380.2	100%	10%	
A380.3	.....		AB380.3	100%	20%	
A380.4	.....		AB380.4	100%	50%	
A380.5	.....		AB380.5	100%	100%	
A380.6	.....	AT380.6	AB380.6	Deducted from Tier 1 & 2		
A380.7	Unanalysed.....		AB380.7	100%	100%	
A390	Forward asset purchases	AT390	AB390			
A390.1	.....		AB390.1	100%	0%	
A390.2	.....		AB390.2	100%	10%	
A390.3	.....		AB390.3	100%	20%	
A390.4	.....		AB390.4	100%	50%	
A390.5	.....		AB390.5	100%	100%	
A390.6	.....	AT390.6	AB390.6	Deducted from Tier 1 & 2		
A390.7	Unanalysed.....		AB390.7	100%	100%	
A400	Forward deposits placed	AT400	AB400			
A400.1	.....		AB400.1	100%	0%	
A400.2	.....		AB400.2	100%	10%	
A400.3	.....		AB400.3	100%	20%	
A400.4	.....		AB400.4	100%	100%	
A400.5	Unanalysed		AB400.5	100%	100%	
A410	Uncalled partly-paid shares and..... securities	AT410	AB410			
A410.1	.....		AB410.1	100%	0%	
A410.2	.....		AB410.2	100%	10%	
A410.3	.....		AB410.3	100%	20%	
A410.4	.....		AB410.4	100%	100%	
A410.5	.....	AT410.5	AB410.5	Deducted from Tier 1 & 2		
A410.6	Unanalysed.....		AB410.6	100%	100%	

Item No	Item	Trading Book Amount (000s)	Banking Book Amount (000s)	Credit Conversion Factor	Weight	Weighted Banking Book Amount (000s)
<b>OFF BALANCE SHEET ITEMS (CONTINUED)</b>						
A420	NIFs and RUFs	AT420	AB420			
A420.1	.....		AB420.1	50%	0%	
A420.2	.....		AB420.2	50%	10%	
A420.3	.....		AB420.3	50%	20%	
A420.4	.....		AB420.4	50%	100%	
A420.5	Unanalysed.....		AB420.5	50%	100%	
A430	Endorsements of bills	AT430	AB430			
A430.1	Accepted by banks.....		AB430.1	0%	0%	
A430.2	Not accepted by banks		AB430.2	100%	20%	
A430.3	.....		AB430.3	100%	100%	
A430.4	Unanalysed.....		AB430.4	100%	100%	
A440	Other commitments.....	AT440	AB440			
A440.1	1 year or less or unconditionally cancellable.....		AB440.1	0%	0%	
A440.2	Over 1 year.....		AB440.2	50%	0%	
A440.3	.....		AB440.3	50%	10%	
A440.4	.....		AB440.4	50%	20%	
A440.5	.....		AB440.5	50%	50%	
A440.6	.....		AB440.6	50%	100%	
A440.7	(report 50% of nominal values).....	AT440.7	AB440.7	Deducted from Tier 1 & 2		
A440.8	Unanalysed.....		AB440.8	50%	100%	
A452	OTC Derivative Contracts (Replacement Cost Methods) (from Appendix A-I).....					AW452
A462	Foreign Exchange Position (NSOP) [CAD Exempt banks only].				100%	AW462
A472	Interest Rate Related Contracts (Original Exposure Method).....					AW472
A474	Exchange Rate Related Contracts (Original Exposure Method).....					AW474

## LIABILITIES

Item No	Item	Amount (000s)
<b>CORE CAPITAL - TIER 1</b>		
A480	Ordinary shares/common stock (issued and paid up).....	A480
A490	Perpetual non-cumulative preferred share/stock (issued and paid up).....	A490
A500	Reserves.....	A500
A500.1	Share Premium Account.....	A500.1
A500.2	Disclosed prior years reserves (excluding item 580) etc.....	A500.2
A500.3	Current year's retained profit verified by external audit.....	A500.3
A510	Current year's losses.....	A510
A520	Minority Interests (in Tier One Capital).....	A520
A530	Total of Items A480 to A520.....	A530
A540	Goodwill and other intangible assets (items A200 and A210.2).....	A540
A550	<b>TOTAL TIER ONE CAPITAL</b> (Item A530 less A540).....	A550
<b>SUPPLEMENTARY CAPITAL - TIER 2</b>		
A580	Fixed asset revaluation reserve.....	A580
A590	General provisions.....	A590
A600	Hybrid (debt/equity) instruments.....	A600
A610	Subordinated term debt.....	A610
A620	Minority Interests (in Tier 2 capital).....	A620
<b>LESS ADJUSTMENTS TO CAPITAL</b>		
A621	Excess general provisions.....	A621
A622	Excess Tier 2 subordinated debt.....	A622
A623	Amortisation on Tier 2 subordinated debt.....	A623
A624	Total of (items A580 to A620) less total of (items A621 to 623) .....	A624
A625	Tier 2 capital in excess of the overall limit/Excess Tier 2 capital .....	A625
A630	<b>TOTAL ELIGIBLE TIER TWO CAPITAL</b> (Items A624 less A625) .....	A630

Item No	Item	Amount (000s)
<b>TRADING BOOK CAPITAL - TIER 3</b>		
A631	Short term subordinated debt.....	A631
A633	Minority Interests (in short term subordinated debt).....	A633
LESS ADJUSTMENTS TO CAPITAL		
A635	Excess Tier 3 Subordinated debt.....	A635
A638	<b>TOTAL ELIGIBLE TIER THREE CAPITAL</b> (Items A631 plus A633 less A635).	<b>A638</b>
<b>OTHER CAPITAL</b>		
A660	Total ineligible Tier 2 and Tier 3 capital.....	A660
A670	Other capital .....	A670

**Item  
No Item**

		Amount (000s)
<b>OTHER NON-CAPITAL LIABILITIES</b>		
A680	Own bank notes issued.....	A680
A690	Deposits.....	A690
A690.1	<i>Banks</i> .....	A690.1
A690.2	<i>Other</i> .....	A690.2
A700	Marketable securities issued.....	A700
A700.1	<i>Certificates of deposit</i> .....	A700.1
A700.2	<i>Promissory notes and bills</i> .....	A700.2
A700.3	<i>Unsubordinated FRNs and other long term paper</i> .....	A700.3
A710	Investments (gross short positions).....	A710
A710.1	<i>Central governments and central banks</i> .....	A710.1
A710.2	<i>Other</i> .....	A710.2
A720	Liabilities in respect of sale and repurchase agreements.....	A720
A730	Tax provisions.....	A730
A730.1	<i>Current tax</i> .....	A730.1
A730.2	<i>Deferred tax liabilities</i> .....	A730.2
A740	Provisions for dividends payable.....	A740
A750	Other provisions.....	A750
A760	Other.....	A760
A760.1	<i>Credit items in course of settlement</i> .....	A760.1
A760.2	<i>Other</i> .....	A760.2
A765	Liabilities consolidated via consolidated plus.....	A765
A770	<b>Total Liabilities</b> (Item A530, A630 and A638 to A765).....	A770



**Item No**    **Item**

Amount  
(000)s

**MEMORANDUM ITEMS**

A780	Deposits from connected customers.....	A780
A790	Subordinated term debt.....	A790
A790.1	Mandatorily convertible subordinated bonds.....	A790.1
A790.2	Dated preference shares and subordinated term loan capital.....	A790.2

A790.21 *Repayable in full on maturity*

	Amount	Currency		Repayment Date		Sterling equivalent	Amortisation factor
				mm	yyyy	AS790.21	AA790.21
a							
b							
c							
d							
e							
f							
g							
h							
i							
j							

A790.22 *Repayable in instalments*

	Amount	Currency		Repayment Date		Sterling equivalent	Amortisation factor
				mm	yyyy	AS790.22	AA790.22
a							
b							
c							
d							
e							
f							
g							
h							
i							
j							

**APPENDIX A-I: COUNTERPARTY EXPOSURE ON OTC DERIVATIVE CONTRACTS (BANKING BOOK)**

**REPLACEMENT COST METHOD (000s)**

	OTC CONTRACTS Counterparty Risk Weight All maturities	Replacement cost	Potential Future Exposure	Credit Equivalent Amount	Weight	Weighted Amount
10	0%.....	R10	P10	C10	0%	W10
20	10%.....	R20	P20	C20	10%	W20
30	20%.....	R30	P30	C30	20%	W30
40	50%.....	R40	P40	C40	50%	W40
50	Unanalysed.....	R50	P50	C50	50%	W50
60	TOTAL (to be carried forward to item A452)	R60	P60	C60		W60

**APPENDIX A-II: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS (BANKING BOOK)**

**REPLACEMENT COST METHOD (000s)**

Notional Principal Amounts By Residual Maturity

INTEREST RATE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
10	0%.....	NA10	NB10	NC10	ND10
20	10%.....	NA20	NB20	NC20	ND20
30	20%.....	NA30	NB30	NC30	ND30
40	50%.....	NA40	NB40	NC40	ND40
50	Exchange-traded.....	NA50	NB50	NC50	ND50
of which					
60	OTC Options.....	NA60	NB60	NC60	ND60
70	Exchange Traded Options	NA70	NB70	NC70	ND70

Notional Principal Amounts By Residual Maturity

FOREIGN EXCHANGE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
80	0%.....	NA80	NB80	NC80	ND80
90	10%.....	NA90	NB90	NC90	ND90
100	20%.....	NA100	NB100	NC100	ND100
110	50%.....	NA110	NB110	NC110	ND110
120	Exchange-traded.....	NA120	NB120	NC120	ND120
of which					
130	OTC Options.....	NA130	NB130	NC130	ND130
140	Exchange Traded Options	NA140	NB140	NC140	ND140

Notional Principal Amounts By Residual Maturity

EQUITY CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
150	0%.....	NA150	NB150	NC150	ND150
160	10%.....	NA160	NB160	NC160	ND160
170	20%.....	NA170	NB170	NC170	ND170
180	50%.....	NA180	NB180	NC180	ND180
190	Exchange-traded.....	NA190	NB190	NC190	ND190
of which					
200	OTC Options.....	NA200	NB200	NC200	ND200
210	Exchange Traded Options.....	NA210	NB210	NC210	ND210

**APPENDIX A-II: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS (BANKING BOOK)**

*Continued*

**REPLACEMENT COST METHOD (000S)**

INTEREST RATE CONTRACTS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
10	0%.....	RA10	RB10	RC10	RD10
20	10%.....	RA20	RB20	RC20	RD20
30	20%.....	RA30	RB30	RC30	RD30
40	50%.....	RA40	RB40	RC40	RD40

FOREIGN EXCHANGE CONTRACTS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
80	0%.....	RA80	RB80	RC80	RD80
90	10%.....	RA90	RB90	RC90	RD90
100	20%.....	RA100	RB100	RC100	RD100
110	50%.....	RA110	RB110	RC110	RD110

EQUITY CONTRACTS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
150	0%.....	RA150	RB150	RC150	RD150
160	10%.....	RA160	RB160	RC160	RD160
170	20%.....	RA170	RB170	RC170	RD170
180	50%.....	RA180	RB180	RC180	RD180

**APPENDIX A-II: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS (BANKING BOOK)**

*Continued*

**REPLACEMENT COST METHOD (000s)**

COMMODITY CONTRACTS		Notional Principal Amounts By Residual Maturity			
		<=1 Year	1-5 Years	over 5 Years	Total
220	0%.....	NA220	NB220	NC220	ND220
230	10%.....	NA230	NB230	NC230	ND230
240	20%.....	NA240	NB240	NC240	ND240
250	50%.....	NA250	NB250	NC250	ND250
260	Exchange Traded Options....	NA260	NB260	NC260	ND260
of which					
270	OTC Options	NA270	NB270	NC270	ND270
280	Exchange Traded Options.....	NA280	NB280	NC280	ND280

PRECIOUS METALS		Notional Principal Amounts By Residual Maturity			
		<=1 Year	1-5 Years	over 5 Years	Total
290	0%.....	NA290	NB290	NC290	ND290
300	10%.....	NA300	NB300	NC300	ND300
310	20%.....	NA310	NB310	NC310	ND310
320	50%.....	NA320	NB320	NC320	ND320
330	Exchange Traded Options....	NA330	NB330	NC330	ND330
of which					
340	OTC Options.....	NA340	NB340	NC340	ND340
350	Exchange Traded Options....	NA350	NB350	NC350	ND350

TOTAL CONTRACTS		Notional Principal Amounts By Residual Maturity			
		<=1 Year	1-5 Years	over 5 Years	Total
360	0%.....	NA360	NB360	NC360	ND360
370	10%.....	NA370	NB370	NC370	ND370
380	20%.....	NA380	NB380	NC380	ND380
390	50%.....	NA390	NB390	NC390	ND390
400	Exchange Traded Options....	NA400	NB400	NC400	ND400
of which					
410	OTC Options.....	NA410	NB410	NC410	ND410
420	Exchange Traded Options....	NA420	NB420	NC420	ND420

**APPENDIX A-II: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS (BANKING BOOK)**

*Continued*

**REPLACEMENT COST METHOD (000s)**

COMMODITY CONTRACTS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
220	0%.....	RA220	RB220	RC220	RD220
230	10%.....	RA230	RB230	RC230	RD230
240	20%.....	RA240	RB240	RC240	RD240
250	50%.....	RA250	RB250	RC250	RD250

PRECIOUS METALS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
290	0%.....	RA290	RB290	RC290	RD290
300	10%.....	RA300	RB300	RC300	RD300
310	20%.....	RA310	RB310	RC310	RD310
320	50%.....	RA320	RB320	RC320	RD320

TOTAL CONTRACTS		Replacement Cost By Residual Maturity			Total
		<=1 Year	1-5 Years	over 5 Years	
360	0%.....	RA360	RB360	RC360	RD360
370	10%.....	RA370	RB370	RC370	RD370
380	20%.....	RA380	RB380	RC380	RD380
390	50%.....	RA390	RB390	RC390	RD390

## APPENDIX A-III: EXPOSURES COLLATERALISED/GUARANTEED/NETTED

This return records the adjustments made by the reporting institution in respect of exposures collateralised or guaranteed or netting, where the collateral/guarantee has been used to reduce the risk weight coefficient of the underlying asset, eg show the amounts in column 3 transferred from item A100.4 (100% weight) to item A100.1 (0% weight).

		1	2	3	4	5
		From Item Number	To Item Number	Amount Collateralised <u>000s</u>	Amount Guaranteed <u>000s</u>	Amount Netted <u>000s</u>
1	A					
2	A					
3	A					
4	A					
5	A					
6	A					
7	A					
8	A					
9	A					
10	A					
11	A					
12	A					
13	A					
14	A					
15	A					
16	A					
17	A					
18	A					
19	A					
20	A					
21	A					
22	A					
23	A					
24	A					
25	A					
26	A					
27	A					
28	A					
29	A					
30	A					
31	A					
32	A					
33	A					
34	A					
35	A					

## APPENDIX A-IV: CURRENT YEAR'S PROFIT & LOSS

based on management accounts to .....(dd/mm/yyyy)

	/		/	
--	---	--	---	--

Quarterly reporters (input reporting period as appropriate: Qtr1=1, Qtr2=2, etc) .....

--

Half-yearly reporters (input reporting period as appropriate: H1=1, H2=2) .....

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Item	000s	000s	000s
<b>INCOME</b>			
10 Interest received and receivable.....	10		
20 Interest paid and payable.....	20		
30 Net interest income		30	
40 Profit/(Loss) on foreign exchange dealing		40	
50 Profit/(Loss) on investments held for dealing		50	
60 Sub-total .....			60
70 Income from fees and commissions.....			70
80 Dividends/share of profits from subsidiary and associated companies.....			80
90 Profit/(Loss) on fixed assets (inc. revaluation of fixed assets).....			90
100 Other Income.....			100
<b>EXPENSES</b>			
110 Operation expenses for: staff.....		110	
120 occupancy.....		120	
130 other.....		130	
140 Net Charge/(credit) provisions: capital.....		140	
150 suspended interest.....		150	
160 Provisions for: taxation.....		160	
170 dividends.....		170	
180 Sub-total.....			180
190 Current year's Profit/(Loss).....			190
200 Extraordinary items.....			200
210 <b>TOTAL</b> .....			210



**APPENDIX A-V: PROVISIONS AGAINST BAD AND DOUBTFUL DEBTS AND INVESTMENTS**

Item No	Item	Col 1 000s SPECIFIC	Col 2 000s GENERAL	Col 3 000s TOTAL
10	Previous balance as at.. (mm / yyyy) <input type="text"/> / <input type="text"/>	10S	10G	10T
20	Adjustments for acquisitions/disposals.....	20S	20G	20T
30	Adjustments for exchange rate movements.....	30S	30G	30T
40	Charge/credit to profit & loss *.....	40S	40G	40T
50	Amounts written off (gross).....	50S	50G	50T
60	Recoveries of amounts previously written off.....	60S	60G	60T
70	Other.....	70S	70G	70T
80	Current balance **.....	80S	80G	80T

**Specific provisions against bad and doubtful debts**

90	for assets of 0% weight.....			90
100	for assets of 10% weight.....			100
110	for assets of 20% weight.....			110
120	for assets of 50% weight.....			120
130	for assets of 100% weight.....			130
140	for assets deducted from capital base.....			140
150	Total specific provisions.....			150
160	Gross value of loans against which specific provisions have been made.....			160

**SPECIFIC PROVISIONS AGAINST THE VALUE OF INVESTMENTS OTHER THAN TRADING INVESTMENTS**

170	for assets of 0% weight.....			170
180	for assets of 10% weight.....			180
190	for assets of 20% weight.....			190
200	for assets of 50% weight.....			200
210	for assets of 100% weight.....			210
220	for assets deducted from capital base.....			220
230	Total specific provisions against investments.....			230

\* Column 3 to equal items 140 & 150 on Form BSD3 (Appendix A-IV)

\*\* Column 2 to equal items A590 in Section A, and column 1 to equal items 150 and 230 in this section (from November 2001)

# SECTION B: TRADING BOOK

## NON-MARKET RISK IN THE TRADING BOOK

	Amount 000s		Weighted amount 000s		Capital Requirement 000s
<b>COUNTERPARTY RISK ARISING FROM:</b>					
B10	Free Deliveries.....				B10
B10.1	.....		0%		B10.1
B10.2	.....		10%		B10.2
B10.3	.....		20%		B10.3
B10.4	.....		100%		B10.4
B20	Margins.....				B20
B20.1	.....		0%		B20.1
B20.2	.....		10%		B20.2
B20.3	.....		20%		B20.3
B20.4	.....		100%		B20.4
B30	Fees.....				B30
B30.1	.....		0%		B30.1
B30.2	.....		10%		B30.2
B30.3	.....		20%		B30.3
B30.4	.....		100%		B30.4
B40	Other counterparty risk in the trading book.....				B40
B40.1	.....		0%		B40.1
B40.2	.....		10%		B40.2
B40.3	.....		20%		B40.3
B40.4	.....		100%		B40.4
B50	Unsettled transactions (from Appendix B-I).....				B50
B60	OTC Derivatives (from Appendix B-II).....			BW60	8% B60
B70	Undocumented repos/reverse repos (from Appendix B-IV).....			BW70	8% B70
B80	Documented repos (from Appendix B-IV).....			BW80	8% B80
B90	Documented reverse repos (from Appendix B-IV).....			BW90	8% B90
B100	<b>TOTAL COUNTERPARTY RISK IN THE TRADING BOOK.....</b>				<b>B100</b>

## LARGE EXPOSURES IN THE TRADING BOOK

		Amount 000s	
B110	Adjusted Large Exposures Capital Base (from Form LE2 Part 5).....		B110
		Specific Risk Charge (000s)	Capital Requirement (000s)
B120	Excesses that have existed for 10 days or less.....	BS120	200% B120
B130	Excesses that have existed for more than 10 days.....	BS130	B130
B130.1	>25% and <=40% of adjusted capital base.....	BS130.1	200% B130.1
B130.2	>40% and <=60% of adjusted capital base.....	BS130.2	300% B130.2
B130.3	>60% and <=80% of adjusted capital base.....	BS130.3	400% B130.3
B130.4	>80% and <=100% of adjusted capital base.....	BS130.4	500% B130.4
B130.5	>100% and <=250% of adjusted capital base.....	BS130.5	600% B130.5
B130.6	>250%.....	BS130.6	900% B130.6
B140	<b>CAPITAL REQUIREMENT FOR LARGE EXPOSURES.....</b>	BS140	B140

# MARKET RISKS IN THE TRADING BOOK

		Capital Requirement (000)s	
<b>I</b>	<b>STANDARD APPROACH</b>		
	<b>FOREIGN EXCHANGE RISK</b>		
B150	For basic approach (from Appendix B-V).....		B150
B160	For backtesting approach (from Appendix B-V).....		B160
B170	Additional Capital Charge for Options.....		B170
B170.1	Using Curve Out.....		B170.1
B170.2	Using CAD1 Models Approach.....		B170.2
B180	<b>Total foreign exchange risk</b> .....		B180
	<b>INTEREST RATE POSITION RISK</b>	Amount (000s)	Specific Risk Weights Capital Requirement (000)s
B190	Specific Risk.....		B190
B190.1	.....		0.00% B190.1
B190.2	.....		0.25% B190.2
B190.3	.....		1.00% B190.3
B190.4	.....		1.60% B190.4
B190.5	.....		8.00% B190.5
B200	General Market Risk (from Appendix B-VI).....		B200
B210	Additional Capital Charge for Options:.....		B210
B210.1	Using Curve Out.....		B210.1
B210.2	Using CAD1 Models Approach.....		B210.2
B215	Embedded Interest Rate Risk in Equity Derivatives.....		B215
B220	<b>Total interest rate position risk</b> .....		B220
	<b>EQUITY POSITION RISK</b>		Capital Requirement (000s)
B230	Specific Risk (from Appendix B-VII).....		B230
B240	General Market Risk (from Appendix B-VII).....		B240
B250	Additional Capital Charge for Options:.....		B250
B250.1	Using Curve Out.....		B250.1
B250.2	Using CAD1 Models Approach.....		B250.2
B270	<b>Total equity position risk</b> .....		B270

**COMMODITY POSITION RISK**

Capital Requirement (000s)

B280	Commodity position risk (from Appendix B-VIII).....	B280
B282	Additional Capital Charge for Options:.....	B282
B282.1	Using Curve Out.....	B282.1
B282.2	Using CAD1 Models Approach.....	B282.2
B284	<b>Total commodity position risk</b> .....	B284

**II INTERNAL MODELS APPROACH**

Capital Requirement (000s)

B290	Previous day's value at risk.....	B290
B300	Average of previous 60 days' value at risk .....	B300
B310	Multiplication factor (rounded to 2 decimal places and multiplied by 100) .	B310
B320	Capital requirement for general market risk .....	B320
B330	Capital surcharge for specific risk .....	B330
B340	<b>Total capital requirement for risks subject to internal models</b> (items B320 + B330) ....	B340

## APPENDIX B-I: COUNTERPARTY RISK ON UNSETTLED TRANSACTIONS (000s)

### Standard Method (Capital Charge based on potential loss)

	Unsettled Transactions	Potential Loss		Capital Charge
10	0 - 4 days.....	P10	0%	C10
20	5 - 15 days.....	P20	8%	C20
30	16 - 30 days.....	P30	50%	C30
40	31 - 45 days.....	P40	75%	C40
50	46 or more days.....	P50	100%	C50
60	Total.....			C60

### Alternative Method (Capital Charge based on agreed settlement price)

	Unsettled Transactions	Agreed Settlement price		Capital Charge
70	0 - 4 days.....	P70	0%	C70
80	5 - 15 days.....	P80	0.5%	C80
90	16 - 30 days.....	P90	4%	C90
100	31 - 45 days.....	P100	9%	C100
	46 or more days	Use Standard Method		
110	Total.....			C110
120	Total unsettled transactions.....			C120

**APPENDIX B-II: COUNTERPARTY EXPOSURE ON OTC DERIVATIVE CONTRACTS  
(TRADING BOOK)  
REPLACEMENT COST METHOD (000s)**

	OTC CONTRACTS Counterparty Risk Weight All maturities	Replacement cost	Potential Future Exposure	Credit Equivalent Amount	Weight	Weighted Amount
10	0%.....	R10	P10	C10	0%	<b>W10</b>
20	10%.....	R20	P20	C20	10%	W20
30	20%.....	R30	P30	C30	20%	W30
40	50%.....	R40	P40	C40	50%	W40
50	Unanalysed.....	R50	P50	C50	50%	W50
60	TOTAL.....	R60	P60	C60		W60

**APPENDIX B-III: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS  
(TRADING BOOK)  
REPLACEMENT COST METHOD (000s)**

Notional Principal Amounts By Residual Maturity

INTEREST RATE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
10	0%.....	NA10	NB10	NC10	ND10
20	10%.....	NA20	NB20	NC20	ND20
30	20%.....	NA30	NB30	NC30	ND30
40	50%.....	NA40	NB40	NC40	ND40
50	Exchange-traded.....	NA50	NB50	NC50	ND50
of which					
60	OTC Options.....	NA60	NB60	NC60	ND60
70	Exchange Traded Options	NA70	NB70	NC70	ND70

Notional Principal Amounts By Residual Maturity

FOREIGN EXCHANGE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
80	0%.....	NA80	NB80	NC80	ND80
90	10%.....	NA90	NB90	NC90	ND90
100	20%.....	NA100	NB100	NC100	ND100
110	50%.....	NA110	NB110	NC110	ND110
120	Exchange-traded.....	NA120	NB120	NC120	ND120
of which					
130	OTC Options.....	NA130	NB130	NC130	ND130
140	Exchange Traded Options	NA140	NB140	NC140	ND140

Notional Principal Amounts By Residual Maturity

EQUITY CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
150	0%.....	NA150	NB150	NC150	ND150
160	10%.....	NA160	NB160	NC160	ND160
170	20%.....	NA170	NB170	NC170	ND170
180	50%.....	NA180	NB180	NC180	ND180
190	Exchange-traded.....	NA190	NB190	NC190	ND190
of which					
200	OTC Options.....	NA200	NB200	NC200	ND200
210	Exchange Traded Options	NA210	NB210	NC210	ND210



**APPENDIX B-III: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS  
(TRADING BOOK) - continued  
REPLACEMENT COST METHOD (000s)**

		Replacement Cost By Residual Maturity			
INTEREST RATE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
10	0%.....	RA10	RB10	RC10	RD10
20	10%.....	RA20	RB20	RC20	RD20
30	20%.....	RA30	RB30	RC30	RD30
40	50%.....	RA40	RB40	RC40	RD40

		Replacement Cost By Residual Maturity			
FOREIGN EXCHANGE CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
80	0%.....	RA80	RB80	RC80	RD80
90	10%.....	RA90	RB90	RC90	RD90
100	20%.....	RA100	RB100	RC100	RD100
110	50%.....	RA110	RB110	RC110	RD110

		Replacement Cost By Residual Maturity			
EQUITY CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
150	0%.....	RA150	RB150	RC150	RD150
160	10%.....	RA160	RB160	RC160	RD160
170	20%.....	RA170	RB170	RC170	RD170
180	50%.....	RA180	RB180	RC180	RD180

**APPENDIX B-III: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS  
(TRADING BOOK) - continued  
REPLACEMENT COST METHOD (000s)**

Notional Principal Amounts By Residual Maturity

COMMODITY CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
220	0%.....	NA220	NB220	NC220	ND220
230	10%.....	NA230	NB230	NC230	ND230
240	20%.....	NA240	NB240	NC240	ND240
250	50%.....	NA250	NB250	NC250	ND250
260	Exchange-traded.....	NA260	NB260	NC260	ND260
of which					
270	OTC Options.....	NA270	NB270	NC270	ND270
280	Exchange Traded Options	NA280	NB280	NC280	ND280

Notional Principal Amounts By Residual Maturity

PRECIOUS METALS		<=1 Year	1-5 Years	over 5 Years	Total
290	0%.....	NA290	NB290	NC290	ND290
300	10%.....	NA300	NB300	NC300	ND300
310	20%.....	NA310	NB310	NC310	ND310
320	50%.....	NA320	NB320	NC320	ND320
330	Exchange-traded.....	NA330	NB330	NC330	ND330
of which					
340	OTC Options.....	NA340	NB340	NC340	ND340
350	Exchange Traded Options	NA350	NB350	NC350	ND350

Notional Principal Amounts By Residual Maturity

TOTAL CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
360	0%.....	NA360	NB360	NC360	ND360
370	10%.....	NA370	NB370	NC370	ND370
380	20%.....	NA380	NB380	NC380	ND380
390	50%.....	NA390	NB390	NC390	ND390
400	Exchange-traded.....	NA400	NB400	NC400	ND400
of which					
410	OTC Options.....	NA410	NB410	NC410	ND410
420	Exchange Traded Options	NA420	NB420	NC420	ND420

**APPENDIX B-III: SUPPLEMENTARY INFORMATION ON DERIVATIVE CONTRACTS  
(TRADING BOOK) - continued  
REPLACEMENT COST METHOD (000s)**

		Replacement Cost By Residual Maturity			
PRECIOUS METALS		<=1 Year	1-5 Years	over 5 Years	Total
220	0%.....	RA220	RB220	RC220	RD220
230	10%.....	RA230	RB230	RC230	RD230
240	20%.....	RA240	RB240	RC240	RD240
250	50%.....	RA250	RB250	RC250	RD250

		Replacement Cost By Residual Maturity			
PRECIOUS METALS		<=1 Year	1-5 Years	over 5 Years	Total
290	0%.....	RA290	RB290	RC290	RD290
300	10%.....	RA300	RB300	RC300	RD300
310	20%.....	RA310	RB310	RC310	RD310
320	50%.....	RA320	RB320	RC320	RD320

		Replacement Cost By Residual Maturity			
TOTAL CONTRACTS		<=1 Year	1-5 Years	over 5 Years	Total
360	0%.....	RA360	RB360	RC360	RD360
370	10%.....	RA370	RB370	RC370	RD370
380	20%.....	RA380	RB380	RC380	RD380
390	50%.....	RA390	RB390	RC390	RD390

**APPENDIX B-IV: COUNTERPARTY EXPOSURE FOR REPOS, REVERSE REPOS AND SIMILAR TRANSACTIONS (000s)**

	1	2	3	4	5
<b>UNDOCUMENTED REPOS/ REVERSE REPOS</b>	Replacement Cost	Potential Future Credit Exposure	Amount at Risk (1 + 2)	Weight	Weighted Amount (3 * 4)
10 .....	R10	P10	A10	0%	W10
20 .....	R20	P20	A20	10%	W20
30 .....	R30	P30	A30	20%	W30
40 .....	R40	P40	A40	100%	W40
50 TOTAL.....					W50
	1	2	3	4	5
<b>DOCUMENTED REPOS</b>	Market value of securities sold or lent	Market value of collateral taken	Amount at Risk (1 - 2)	Weight	Weighted Amount (3 * 4)
60 .....	S60	C60	A60	0%	W60
70 .....	S70	C70	A70	10%	W70
80 .....	S80	C80	A80	20%	W80
90 .....	S90	C90	A90	100%	W90
100 TOTAL.....					W100
	1	2	3	4	5
<b>DOCUMENTED REVERSE REPOS</b>	Market value of collateral given	Market value of securities bought or borrowed	Amount at Risk (1 - 2)	Weight	Weighted Amount (3 * 4)
110 .....	C110	S110	A110	0%	W110
120 .....	C120	S120	A120	10%	W120
130 .....	C130	S130	A130	20%	W130
140 .....	C140	S140	A140	100%	W140
150 TOTAL.....					W150

# APPENDIX B-V: CAPITAL REQUIREMENT FOR FOREIGN EXCHANGE RISK (000s)

			Column 1 Net Overall Long (short) Position	Column 2 Positions to be treated under basic method	Column 3 Positions being treated under backtesting approach
BASE CURRENCY	<input type="text"/>	<input type="text"/>	(1 = 2 + 3)		
Other Currencies					
Belgium/Luxembourg Francs	BE	BELG			
Canadian Dollars	CA	CANA			
Danish Kronor	DK	DENM			
EUROS	ER	EURO			
French Francs	FR	FRAN			
Deutschmarks	DE	RGER			
Irish Pounds	IE	EIRE			
Italian Lire	IT	ITAL			
Japanese Yen	JP	JAPA			
Netherlands Guilders	NL	NETH			
Spanish Pesetas	ES	SPAI			
Swedish Kroner	SE	SWED			
Swiss Francs	CH	SWIT			
Sterling	UK	UKIN			
US Dollars	US	USA			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
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.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
Other Material currencies .....	U9	UNAL			
Other Aggregate Net Long Positions		OTHL			
Other Aggregate Net Short Positions		OTHS			
TOTAL			ZERO		
Higher of aggregate net short/long open positions				NSOP	NSOP
GOLD	GO	GOLD			
.....					
SUM OF GROSS POSITION.....			SUMG	SUMG	SUMG
CAPITAL REQUIREMENT.....			CAPR	CAPR	CAPR

**APPENDIX B-VI: CAPITAL REQUIREMENT INTEREST RATE GENERAL MARKET RISK (000s)**

			1	2	3	4	5
			Zone One	Zone One	Zone Two	Zone Two	Zone Three
			Net Long position	Net Short Position	Net Long position	Net Short Position	Net Long position
Australia	AU	AUSL					
Austria	AT	AUSR					
Belgium	BE	BELG					
Brazil	BR	BRAZ					
Canada	CA	CANA					
Denmark	DK	DENM					
EUROS	ER	EURO					
Finland	FI	FINL					
France	FR	FRAN					
Germany	DE	RGER					
Greece	GR	GREE					
Ireland	IE	EIRE					
Italy	IT	ITAL					
Japan	JP	JAPA					
Malaysia	MY	MALA					
Mexico	MX	MEXI					
Netherlands	NL	NETH					
Norway	NO	NORW					
Portugal	PT	PORT					
Singapore	SG	SING					
South Africa	RA	SAFR					
Spain	ES	SPAI					
Sweden	SE	SWED					
Switzerland	CH	SWIT					
Turkey	TR	TURK					
UK	UK	UKIN					
Sterling Index Linked Gilts							
USA	US	USA					
Other Material Countries							
.....							
.....							
.....							
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.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
Other.....	U9	UNAL					
Non Material Countries	XF	NONM					
TOTAL	.....						

**APPENDIX B-VI: CAPITAL REQUIREMENT INTEREST RATE GENERAL MARKET RISK - continued (000s)**

			6	7	8	9	10
			Zone Three Net Short Position	Maturity based approach (Method one)	Duration based Approach (Method two)	Simplified Method	Total General Market Interest Rate Risk (7 + 8 + 9)
Australia	AU	AUSL					
Austria	AT	AUSR					
Belgium	BE	BELG					
Brazil	BR	BRAZ					
Canada	CA	CANA					
Denmark	DK	DENM					
EUROS	ER	EURO					
Finland	FI	FINL					
France	FR	FRAN					
Germany	DE	RGER					
Greece	GR	GREE					
Ireland	IE	EIRE					
Italy	IT	ITAL					
Japan	JP	JAPA					
Malaysia	MY	MALA					
Mexico	MX	MEXI					
Netherlands	NL	NETH					
Norway	NO	NORW					
Portugal	PT	PORT					
Singapore	SG	SING					
South Africa	RA	SAFR					
Spain	ES	SPAI					
Sweden	SE	SWED					
Switzerland	CH	SWIT					
Turkey	TR	TURK					
UK	UK	UKIN					
Sterling Index Linked Gilts							
USA	US	USA					
Other Material Countries							
.....							
.....							
.....							
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.....							
.....							
.....							
.....							
.....							
.....							
.....							
.....							
Other.....	U9	UNAL					
Non Material Countries	XF	NONM					
TOTAL	.....						

**APPENDIX B-VII: EQUITY POSITION RISK (000s)**

			<b>Gross Positions for Specific Risk</b>			
			1	2	3	4
			Positions attracting 8% specific / Execution risk	Positions attracting 4% specific/ Execution risk	Positions attracting 0% execution risk	Total Gross Equity Positions for specific / Execution risk (1 + 2 + 3)
<b>Positions, including positions in indices, allocated by country</b>						
Australia	AU	AUSL.....				
Belgium	BE	BELG.....				
Canada	CA	CANA.....				
France	FR	FRAN.....				
Germany	DE	RGER....				
Japan	JP	JAPA.....				
Netherlands	NL	NETH.....				
Spain	ES	SPAI.....				
Sweden	SE	SWED....				
Switzerland	CH	SWIT.....				
United Kingdom	UK	UKIN.....				
United States	US	USA.....				
Denmark	DK	DENM....				
Finland	FI	FINL.....				
Greece	GR	GREE.....				
Ireland	IE	EIRE.....				
Italy	IT	ITAL.....				
Luxembourg	LU	LUXE.....				
Portugal	PT	PORT.....				
.....						
.....						
.....						
.....						
.....						
Other material ctry.	U9	UNAL				
Non material ctry...	XF	NONM				
TOTAL.....						



**APPENDIX B-VII: EQUITY POSITION RISK - continued (000s)**

**Positions for General Market Risk**

			5	6	7
			Excess amount of concentrated positions (Gross)	Other Positions	Total Equity Positions for General Market Risk (5 + 6)
<b>Positions, including positions in indices, allocated by country</b>					
Australia	AU	AUSL.....			
Belgium	BE	BELG.....			
Canada	CA	CANA.....			
France	FR	FRAN.....			
Germany	DE	RGER....			
Japan	JP	JAPA.....			
Netherlands	NL	NETH.....			
Spain	ES	SPAI.....			
Sweden	SE	SWED....			
Switzerland	CH	SWIT.....			
United Kingdom	UK	UKIN.....			
United States	US	USA.....			
Denmark	DK	DENM....			
Finland	FI	FINL.....			
Greece	GR	GREE.....			
Ireland	IE	EIRE.....			
Italy	IT	ITAL.....			
Luxembourg	LU	LUXE.....			
Portugal	PT	PORT.....			
.....					
.....					
.....					
.....					
.....					
Other material ctry.	U9	UNAL			
Non material ctry...	XF	NONM			
TOTAL	.....				

**APPENDIX B-VIII: COMMODITY POSITION RISK (000s)**

Commodity types	Positions			Capital Charges		
	Column A Gross Long	Column B Gross Short	Column C Net Open position	Column D Simplified approach	Column E Maturity approach	Column F Total charges
10 Precious metals (excluding gold) ..	10A	10B	10C	10D	10E	10F
20 Base metals .....	20A	20B	20C	20D	20E	20F
30 Energy contracts (including oil) ....	30A	30B	30C	30D	30E	30F
40 Other contracts ..	40A	40B	40C	40D	40E	40F

50 Total capital requirement .....						50F
------------------------------------	--	--	--	--	--	-----

**Top ten commodities by capital charge**

60 1 .....						
70 2 .....						
80 3 .....						
90 4 .....						
100 5 .....						
110 6 .....						
120 7 .....						
130 8 .....						
140 9 .....						
150 10 .....						

## APPENDIX B-IX: BACKTESTING RESULTS

### Multiplication factor

10	Minimum multiplication factor (rounded to 2 decimal places x 100, ie input as integers) .....	
20	Number of regulatory backtesting exceptions recorded over last 250 business days. ....	
30	Plus factor (rounded to 2 decimal places x 100, ie input as integers) .....	
40	Multiplication factor (items 10 and 30) .....	

### Backtesting on total portfolio

50	Number of recorded backtesting exceptions in last reporting period .....	
----	--	--

51.0 Exceptions recorded during last reporting period:

	Date (dd / mm / yyyy)	VaR measure (note 1) (000s)	Actual loss (note 2) (000s)
51.01			
51.02			
51.03			
51.04			
51.05			
51.06			
51.07			
51.08			
51.09			
51.10			
51.11			
51.12			

52.0 Five largest daily losses over last reporting period:

	Date (dd / mm / yyyy)	VaR measure (note 1) (000s)	Actual loss (note 2) (000s)
52.1			
52.2			
52.3			
52.4			
52.5			

53.0 Five largest backtesting VaRs<sup>1</sup> over last reporting period:

	Date (dd / mm / yyyy)	VaR measure (note 1) (000s)	Actual loss (note 2) (000s)
53.1			
53.2			
53.3			
53.4			
53.5			

Note 1. The VaR measure for backtesting purposes should be calibrated to a one-day holding period and a 99% one-tailed confidence limit.

Note 2 Actual profit/loss is the day's actual P&L arising from trading activities within the scope of the model.

**Backtesting on portfolios for specific risk**

60 Number of backtesting exceptions on interest rate portfolio in last reporting period .....

60.1 Exceptions reported during last reporting period:

	Date (dd / mm / yyyy)		VaR measure (note 3) (000s)		Actual loss (note 4) (000s)
60.11		/			
60.12		/			
60.13		/			
60.14		/			
60.15		/			
60.16		/			
60.17		/			
60.18		/			
60.19		/			
60.20		/			
60.21		/			
60.22		/			

If the reporting institution conducts backtesting on a sub-portfolio level, this should be repeated for each sub-portfolio that is subject to interest rate specific risk

70 Number of backtesting exceptions on equities portfolio in last reporting period .....

70.1 Exceptions reported during last reporting period:

	Date (dd / mm / yyyy)		VaR measure (note 3) (000s)		Actual loss (note 4) (000s)
70.11		/			
70.12		/			
70.13		/			
70.14		/			
70.15		/			
70.16		/			
70.17		/			
70.18		/			
70.19		/			
70.20		/			
70.21		/			
70.22		/			

If the reporting institution conducts backtesting on a sub-portfolio level, this should be repeated for each sub-portfolio that is subject to interest rate specific risk

Note 3 This is the VaR measure (99% confidence limit, one-day holding period) related to specific risk on the sub-portfolio.

Note 4 This is the actual loss related to specific risk on the sub-portfolio.

## APPENDIX B-X: EXPOSURES COLLATERALISED/GUARANTEED/NETTED

This return records the adjustments made by the reporting institution in respect of exposures collateralised or guaranteed or netting, where the collateral/guarantee has been used to reduce the risk weight coefficient of the underlying asset, eg show the amounts in column 3 transferred from item B40.4 (100% weight) to item B40.1 (0% weight).

		1 From Item Number		2 To Item Number		3 Amount Collateralised 000s	4 Amount Guaranteed 000s	5 Amount Netted 000s
1	B							
2	B							
3	B							
4	B							
5	B							
6	B							
7	B							
8	B							
9	B							
10	B							
11	B							
12	B							
13	B							
14	B							
15	B							
16	B							
17	B							
18	B							
19	B							
20	B							
21	B							
22	B							
23	B							
24	B							
25	B							
26	B							
27	B							
28	B							
29	B							
30	B							
31	B							
32	B							
33	B							
34	B							
35	B							

# SECTION C - CONSOLIDATION VIA AGGREGATION PLUS (INTO THE TRADING BOOK)

## INVESTMENT FIRM SUBSIDIARIES

	A	B	C	D	E
	FSA=1 or local regulator's rules= 0 applied	Individual capital ratio applied = (% to 2d.px100)	(000)s Individual capital requirement	(000)s Notional risk weighted assets	(000)s Incremental capital for large exposures
C10.1					
C10.2					
C10.3					
C10.4					
C10.5					
C10.6					
C10.7					
C10.8					
C10.9					
C10.10					
C10.11					
C10.12					
C10.13					
C10.14					

C10	TOTAL FOR INVESTMENT FIRMS.....		10C	10D	10E
-----	---------------------------------	--	-----	-----	-----

## BANKING SUBSIDIARIES

C20.1					
C20.2					
C20.3					
C20.4					
C20.5					
C20.6					
C20.7					
C20.8					
C20.9					
C20.10					
C20.11					
C20.12					
C20.13					
C20.14					

C20	TOTAL FOR BANKING SUBSIDIARIES.....		20C	20D	20E
-----	-------------------------------------	--	-----	-----	-----

<b>C30</b>	<b>GRAND TOTAL</b>		30C	30D	30E
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**SECTION C - CONSOLIDATION VIA AGGREGATION PLUS  
(INTO THE TRADING BOOK) - continued**

INVESTMENT FIRM SUBSIDIARIES	CAPITAL REQUIREMENT					L (000)s Target capital requirement
	F (000)s MR against which Tier 3 may be held	G (000)s MR against which Tier 3 may not be held	H (000)s Non-MR against which Tier 3 may be held	J (000)s Non-MR against which Tier 3 may not be held	K (no) Plus factor (nox100)	
C10.1 .....						
C10.2 .....						
C10.3 .....						
C10.4 .....						
C10.5 .....						
C10.6 .....						
C10.7 .....						
C10.8 .....						
C10.9 .....						
C10.10 .....						
C10.11 .....						
C10.12 .....						
C10.13 .....						
C10.14 .....						
C10 TOTAL.....	10F	10G	10H	10J		10L
<b>BANKING SUBSIDIARIES</b>						
C20.1 .....						
C20.2 .....						
C20.3 .....						
C20.4 .....						
C20.5 .....						
C20.6 .....						
C20.7 .....						
C20.8 .....						
C20.9 .....						
C20.10 .....						
C20.11 .....						
C20.12 .....						
C20.13 .....						
C20.14 .....						
C20 TOTAL.....	20F	20G	20H	20J		20L
C30 GRAND TOTAL	30F	30G	30H	30J		30L

## SECTION D - CAPITAL ADEQUACY SUMMARY

### CAPITAL BASE

000s

D10	Tier 1 (A550) .....	D10
D20	Eligible Tier 2 (A630) .....	D20
D30	Eligible Tier 3 (A638) .....	D30
D40	TOTAL ELIGIBLE CAPITAL (D10 to D30) .....	D40

### BANKING BOOK CAPITAL REQUIREMENTS/RISK WEIGHTED ASSETS

D50	Banking Book Individual Capital Ratio ( % multiplied by 100, ie input as integers) .....	D50
D60	Banking Book Target Ratio ( % multiplied by 100, ie input as integers) .....	D60
D70	Total Banking Book Risk Weighted Assets by risk weighting bands:..... by weighting bands:	D70
D70.1	Risk weighted at 0%.....	D70.1
D70.2	Risk weighted at 10%.....	D70.2
D70.3	Risk weighted at 20%.....	D70.3
D70.4	Risk weighted at 50%.....	D70.4
D70.5	Risk weighted at 100%.....	D70.5
D70.6	Items A452, A472 and A474 of Section A.....	D70.6
D80	<b>Banking Book Capital Requirements</b> .....	D80

### CAPITAL ALLOCATED TO THE BANKING BOOK

D90	Tier 1 capital.....	D90
D100	Eligible Tier 2 capital.....	D100
D110	Total capital allocated to the Banking Book (items D90 + D100) .....	D110

### TRADING BOOK CAPITAL REQUIREMENT/NOTIONAL RISK WEIGHTED ASSETS

D120	Exempt from CAD capital requirements at reporting date ? (please tick if yes) .....	Yes	<input type="checkbox"/>
D130	If yes, number of days over threshold in reporting period .....		<input type="text"/>
D140	Trading Book Individual Capital Ratio ( % multiplied by 100, ie input as integers) .....	D140	<input type="text"/>
D150	Trading Book Target Ratio ( % multiplied by 100, ie input as integers) .....	D150	<input type="text"/>



000S

<b>Standard approach</b>		
D160	Counterparty/Settlement Risk .....	D160
D170	Incremental capital for large exposures .....	D170
D180	Foreign exchange risk .....	D180
D190	Interest Rate Position Risk.....	D190
D200	Equity Position Risk.....	D200
D210	Commodity Position Risk.....	D210
D220	Total capital requirement for trading book risks not subject to models (items D160 to D210) ....	D220
<b>Internal models approach</b>		
D230	Capital requirement for market risk.....	D230
D240	Capital surcharge for specific risk.....	D240
D250	Total capital requirement for risks subject to internal models (items D230+D240).....	D250
<b>Capital requirements for entities consolidated via aggregation plus</b>		
D260	Market Risks against which Tier 3 capital may be held.....	D260
D270	Market Risks against which Tier 3 capital may not be held.....	D270
D280	Non-Market Risk against which Tier 3 capital may be held.....	D280
D290	Non-Market Risk against which Tier 3 capital may not be held.....	D290
D300	Total capital requirement for entities consolidated via aggregation plus .....	D300
D310	<b>Total Trading Book Capital Requirements (items D220+D250+D300).....</b>	D310
D320	<b>Total Trading Book Notional Risk Weighted Assets.....</b>	D320
<b>CAPITAL ALLOCATED TO THE TRADING BOOK</b>		
D330	Tier 1 capital.....	D330
D340	Eligible Tier 2 capital.....	D340
D350	Eligible Tier 3 capital.....	D350
D360	Total capital allocated to the trading book (items D330 to D350).....	D360
<b>ELIGIBLE CAPITAL NOT USED TO SUPPORT EITHER BOOK</b>		
D370	Tier 1.....	D370
D380	Eligible Tier 2.....	D380
D390	Total excess Tier 1 and eligible Tier 2 capital before deduction.....	D390

## DEDUCTIONS

000s

D400	Investments in subsidiaries and associated companies (item A160).....	D400
D410	Connected lending of a capital nature (A280) .....	D410
D420	Off-balance sheet items of a capital nature.....	D420
D430	Investments in bank and financial firm capital (item A171).....	D430
D440	Qualifying holdings (item A180.4).....	D440
D450	Deduction plus consolidation.....	D450
D460	Other deductions.....	D460
D470	Total Deductions (items D400 to D460) .....	D470
D480	<b>OWN FUNDS</b> .....	D480
D490	<b>ADJUSTED CAPITAL BASE</b> .....	D490
D500	<b>TOTAL CAPITAL REQUIREMENTS</b> .....	D500
D510	<b>TOTAL RISK-WEIGHTED ASSETS</b> .....	D510
D520	<b>'PUBLISHED' RISK ASSET RATIO</b> ( % multiplied by 100, ie input as integers) .....	D520
D530	<b>INDIVIDUAL CAPITAL ADEQUACY RATIO</b> ( % multiplied by 100, ie input as integers) .....	D530
D540	<b>TARGET CAPITAL ADEQUACY RATIO</b> ( % multiplied by 100, ie input as integers) .....	D540

Immediately before the M1 definitions, insert the following;

To be used for all reports completed as at 1 December 2001 or after



# FORM LR - Liquidity Return

Reporting institution \_\_\_\_\_

Reporting date 

--	--	--

  
 eg            31            12            2001

FSA number \* 

		F	S	A	
--	--	---	---	---	--

Unconsolidated / Solo consolidated (tick as appropriate).....

Unconsolidated	Solo consolidated

Please tick if this return is completed in Euros (Item A).....

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary action or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on Completion**

1. If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA.
2. Complete the return quarterly on an unconsolidated / solo consolidated basis.
3. Monthly BT reporters should complete Form LR as at the end of February, May, August and November. Quarterly BT reporters should complete Form LR as at the end March, June, September and December.
4. Enter amounts to the nearest thousand omitting £000s/€000s.
5. For definitions of items, refer to the Guidance Notes
6. To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return
7. Submit the form within **10 business days** or **12 business days** for those institutions reporting electronically, clearly addressed to:
 

**The Financial Services Authority**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**
- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
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September 2001

\* This should be the FSA firm reference number. This box must be filled in by all reporters (SUP 16.3.7R).

# PART 1

## Marketable Assets

Zone A currencies

Mark to market  
value

Item No

1

A1A Cash held.....

***Debt instruments issued in Zone A countries***

A2A Central government/central government guaranteed, including Treasury bills, eligible Local Authority paper and eligible bank bills with a residual maturity of up to 1 year.....

**A2A01**

A2B Central government/central government guaranteed and Local Authority marketable debt of 1 to 5 years...

**A2B01**

A2C Central government/central government guaranteed and Local Authority marketable debt of over 5 years..

**A2C01**

A2D Non-government of 6 months or less.....

**A2D01**

A2E Non-government of 6 months to 5 years.....

**A2E01**

A2F Non-government of over 5 years.....

**A2F01**

***Debt instruments issued in Zone B countries***

A3A Central government/central government guaranteed with a residual maturity of up to 1 year.....

**A3A01**

A3B Central government/central government guaranteed of 1 to 5 years.....

**A3B01**

A3C Central government/central government guaranteed of over 5 years.....

**A3C01**

A3D Eligible non-government of 6 months or less.....

**A3D01**

A3E Eligible non-government of 6 months to 5 years.....

**A3E01**

A3F Eligible non-government of over 5 years.....

**A3F01**

A4A ***Brady bonds***.....

**A4A01**

A5A ***Highly liquid equities/equity indices***.....

**A5A01**

A6A **Total discounted amount**.....

**LR.2.1**

**Zone B currencies**

Discount where  
denominated in zone A  
currency (%)

Discount where  
denominated in zone B  
currency (%)

**Discounted to**

**Mark to market  
value**

**8 days  
and under**

**Over 8 days  
to 1 month**

2

3

4

Item No

┌

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.....

<b>A1A03</b>
--------------

A1A

<b>A2A02</b>
<b>A2B02</b>
<b>A2C02</b>
<b>A2D02</b>
<b>A2E02</b>
<b>A2F02</b>

0  
5  
10  
5  
10  
15

20  
25  
30  
25  
30  
35

<b>A2A03</b>	<b>A2A04</b>
<b>A2B03</b>	<b>A2B04</b>
<b>A2C03</b>	<b>A2C04</b>
<b>A2D03</b>	<b>A2D04</b>
<b>A2E03</b>	<b>A2E04</b>
<b>A2F03</b>	<b>A2F04</b>

A2A  
A2B  
A2C  
A2D  
A2E  
A2F

<b>A3A02</b>
<b>A3B02</b>
<b>A3C02</b>
<b>A3D02</b>
<b>A3E02</b>
<b>A3F02</b>

20  
30  
40  
30  
40  
50

20  
30  
40  
30  
40  
50

<b>A3A03</b>	<b>A3A04</b>
<b>A3B03</b>	<b>A3B04</b>
<b>A3C03</b>	<b>A3C04</b>
<b>A3D03</b>	<b>A3D04</b>
<b>A3E03</b>	<b>A3E04</b>
<b>A3F03</b>	<b>A3F04</b>

A3A  
A3B  
A3C  
A3D  
A3E  
A3F

<b>A4A02</b>
--------------

20

40

<b>A4A03</b>	<b>A4A04</b>
--------------	--------------

A4A

<b>A5A02</b>
--------------

20

40

<b>A5A03</b>	<b>A5A04</b>
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A5A

.....

<b>A6A03</b>	<b>A6A04</b>
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A6A

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<b>LR.2.2</b>
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# PART 2

## Contractual basis: residual maturity

Item No	<u>Cashflow basis</u>			
	1	2	3	4
	Overdue	Demand (incl. next day)	8 days and under (excl. next day)	Over 8 days to 1 month

### Inflows

B Please tick if reported on a Cashflow basis (blank represents Maturity basis).....

#### Retail

B1A Mortgages.....  
 B1B Personal loans.....  
 B1C Overdrafts.....  
 B1D Credit card inflows.....  
 B1E Repayment of advances.....  
 B1F Other retail inflows.....

<b>B1A01</b>	<b>B1A02</b>	<b>B1A03</b>	<b>B1A04</b>
<b>B1B01</b>	<b>B1B02</b>	<b>B1B03</b>	<b>B1B04</b>
<b>B1C01</b>	<b>B1C02</b>		
<b>B1D01</b>	<b>B1D02</b>	<b>B1D03</b>	<b>B1D04</b>
<b>B1E01</b>	<b>B1E02</b>	<b>B1E03</b>	<b>B1E04</b>
<b>B1F01</b>	<b>B1F02</b>	<b>B1F03</b>	<b>B1F04</b>

#### Wholesale

B2A Non-marketable securities and debt instruments and marketable assets maturing within 1 month...  
 B2B Intragroup / connected.....  
 B2C Interbank (excluding any intragroup).....  
 B2D Corporate (non interbank, non intragroup).....  
 B2E Government / Public sector.....  
 B2F Repos / reverse repos.....  
 B2G Trade related letters of credit.....  
 B2H Overdrafts.....

<b>B2A01</b>	<b>B2A02</b>	<b>B2A03</b>	<b>B2A04</b>
<b>B2B01</b>	<b>B2B02</b>	<b>B2B03</b>	<b>B2B04</b>
<b>B2C01</b>	<b>B2C02</b>	<b>B2C03</b>	<b>B2C04</b>
<b>B2D01</b>	<b>B2D02</b>	<b>B2D03</b>	<b>B2D04</b>
<b>B2E01</b>	<b>B2E02</b>	<b>B2E03</b>	<b>B2E04</b>
<b>B2F01</b>	<b>B2F02</b>	<b>B2F03</b>	<b>B2F04</b>
<b>B2G01</b>	<b>B2G02</b>	<b>B2G03</b>	<b>B2G04</b>
<b>B2H01</b>	<b>B2H02</b>		

B3A Swaps and FRAs.....  
 B3B Forward foreign exchange.....  
 B3C Forward sales and purchases.....  
 B3D Other off balance sheet.....

<b>B3A01</b>	<b>B3A02</b>	<b>B3A03</b>	<b>B3A04</b>
<b>B3B01</b>	<b>B3B02</b>	<b>B3B03</b>	<b>B3B04</b>
<b>B3C01</b>	<b>B3C02</b>	<b>B3C03</b>	<b>B3C04</b>
<b>B3D01</b>	<b>B3D02</b>	<b>B3D03</b>	<b>B3D04</b>

B4A Fees and other income.....  
 B4B Other funding sources.....

<b>B4A01</b>	<b>B4A02</b>	<b>B4A03</b>	<b>B4A04</b>
<b>B4B01</b>	<b>B4B02</b>	<b>B4B03</b>	<b>B4B04</b>

B5A **Total inflows**.....

<b>B5A01</b>	<b>B5A02</b>	<b>B5A03</b>	<b>B5A04</b>
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LR.2.3

5 Over 1 months to 3 months  
 6 Over 3 months to 6 months  
 7 Total (Cashflow basis)

Assets: Maturity analysis

8 Over 6 months to 1 year  
 9 Over 1 year to 3 years  
 10 Over 3 years to 5 years  
 11 Total (Maturity basis) Item No

BCF05	BCF06
-------	-------

B1A05	B1A06	B1A07
B1B05	B1B06	B1B07
		B1C07
B1D05	B1D06	B1D07
B1E05	B1E06	B1E07
B1F05	B1F06	B1F07

B1A08	B1A09	B1A10	B1A11	B1A
B1B08	B1B09	B1B10	B1B11	B1B
				B1C
B1D08	B1D09	B1D10	B1D11	B1D
B1E08	B1E09	B1E10	B1E11	B1E
B1F08	B1F09	B1F10	B1F11	B1F

B2A05	B2A06	B2A07
B2B05	B2B06	B2B07
B2C05	B2C06	B2C07
B2D05	B2D06	B2D07
B2E05	B2E06	B2E07
B2F05	B2F06	B2F07
B2G05	B2G06	B2G07
		B2H07

B2A08	B2A09	B2A10	B2A11	B2A
B2B08	B2B09	B2B10	B2B11	B2B
B2C08	B2C09	B2C10	B2C11	B2C
B2D08	B2D09	B2D10	B2D11	B2D
B2E08	B2E09	B2E10	B2E11	B2E
B2F08	B2F09	B2F10	B2F11	B2F
B2G08	B2G09	B2G10	B2G11	B2G
				B2H

B3A05	B3A06	B3A07
B3B05	B3B06	B3B07
B3C05	B3C06	B3C07
B3D05	B3D06	B3D07

B3A08	B3A09	B3A10	B3A11	B3A
B3B08	B3B09	B3B10	B3B11	B3B
B3C08	B3C09	B3C10	B3C11	B3C
B3D08	B3D09	B3D10	B3D11	B3D

B4A05	B4A06	B4A07
B4B05	B4B06	B4B07

B4A08	B4A09	B4A10	B4A11	B4A
B4B08	B4B09	B4B10	B4B11	B4B

B5A05	B5A06	B5A07
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B5A08	B5A09	B5A10	B5A11	B5A
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LR.2.4



## PART 2 (continued)

### Contractual basis: residual maturity

Item No	<u>Cashflow basis</u>			
	1	2	3	4
	Overdue	Demand (incl. next day)	8 days and under (excl. next day)	Over 8 days to 1 month
<b>Outflows</b>				
C Please tick if reported on a Cashflow basis (blank represents Maturity basis).....				
<b>Retail</b>				
C1A	Time deposits.....	C1A02	C1A03	C1A04
C1B	No notice / current accounts.....	C1B02		
C1C	Additional advances committed.....	C1C02	C1C03	C1C04
<b>Wholesale</b>				
Non-marketable securities and debt instruments and marketable assets				
C2A	maturing within 1 month.....	C2A02	C2A03	C2A04
C2B	Additional advances committed.....	C2B02	C2B03	C2B04
C2C	Intragroup / Connected.....	C2C02	C2C03	C2C04
C2D	Interbank (excluding any intragroup).....	C2D02	C2D03	C2D04
C2E	Corporate (non-interbank and non-intragroup).....	C2E02	C2E03	C2E04
C2F	Government / Public sector.....	C2F02	C2F03	C2F04
C2G	Repos / Reverse Repos.....	C2G02	C2G03	C2G04
C2H	Trade related letters of credit.....	C2H02	C2H03	C2H04
C3A	Swaps and FRAs.....	C3A02	C3A03	C3A04
C3B	Forward foreign exchange.....	C3B02	C3B03	C3B04
C3C	Forward sales and purchases.....	C3C02	C3C03	C3C04
C3D	Other off balance sheet.....	C3D02	C3D03	C3D04
C4A	Dividends, tax, other costs and outflows.....	C4A02	C4A03	C4A04
C5A	<b>Total outflows</b> .....	C5A02	C5A03	C5A04
<b>Memo Items</b>				
D1A	Option inflows.....	D1A		
D1B	Option outflows.....	D1B		
D1C	Undrawn committed facilities granted to the bank.....	D1C		
D1D	Undrawn committed facilities granted by the bank.....	D1D		
D1E	Commitments to lend under credit card and other revolving credit type facilities.....	D1E		
D1F	<b>Total deposits</b> .....	D1F		
D2A	Undrawn treasury concessions granted by the bank.....	D2A		
D2B	Amount of total cash inflows in arrears.....	D2B		
<b>LR.2.5</b>				

5 Over 1 months to 3 months  
6 Over 3 months to 6 months  
7 Total (Cashflow basis)

Liabilities: Maturity analysis

8 Over 6 months to 1 year  
9 Over 1 year to 3 years  
10 Over 3 years to 5 years  
11 Total (Maturity basis)

Item No

CCF05	CCF06
-------	-------

C1A05	C1A06	C1A07
		C1B07
C1C05	C1C06	C1C07

C1A08	C1A09	C1A10	C1A11	C1A
				C1B
C1C08	C1C09	C1C10	C1C11	C1C

C2A05	C2A06	C2A07
C2B05	C2B06	C2B07
C2C05	C2C06	C2C07
C2D05	C2D06	C2D07
C2E05	C2E06	C2E07
C2F05	C2F06	C2F07
C2G05	C2G06	C2G07
C2H05	C2H06	C2H07

C2A08	C2A09	C2A10	C2A11	C2A
C2B08	C2B09	C2B10	C2B11	C2B
C2C08	C2C09	C2C10	C2C11	C2C
C2D08	C2D09	C2D10	C2D11	C2D
C2E08	C2E09	C2E10	C2E11	C2E
C2F08	C2F09	C2F10	C2F11	C2F
C2G08	C2G09	C2G10	C2G11	C2G
C2H08	C2H09	C2H10	C2H11	C2H

C3A05	C3A06	C3A07
C3B05	C3B06	C3B07
C3C05	C3C06	C3C07
C3D05	C3D06	C3D07

C3A08	C3A09	C3A10	C3A11	C3A
C3B08	C3B09	C3B10	C3B11	C3B
C3C08	C3C09	C3C10	C3C11	C3C
C3D08	C3D09	C3D10	C3D11	C3D

C4A05	C4A06	C4A07
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C4A08	C4A09	C4A10	C4A11	C4A
-------	-------	-------	-------	-----

C5A05	C5A06	C5A07
-------	-------	-------

C5A08	C5A09	C5A10	C5A11	C5A
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LR.2.6

# PART 3

## Behavioural basis

Item No

1	2	3
Overdue	Demand (incl. next day)	8 days and under (excl. next day)

### Inflows

#### Retail

E1A	Mortgages.....	E1A01	E1A02	E1A03
E1B	Personal loans.....	E1B01	E1B02	E1B03
E1C	Overdrafts.....	E1C01	E1C02	E1C03
E1D	Credit card inflows.....	E1D01	E1D02	E1D03
E1E	Repayment of advances.....	E1E01	E1E02	E1E03
E1F	Other retail inflows.....	E1F01	E1F02	E1F03

#### Wholesale

E4A	Non-marketable securities and debt instruments and marketable assets maturing within 1 month...	E4A01	E4A02	E4A03
E4B	Intragroup / connected.....	E4B01	E4B02	E4B03
E4C	Interbank (excluding any intragroup).....	E4C01	E4C02	E4C03
E4D	Corporate (non interbank, non intragroup).....	E4D01	E4D02	E4D03
E4E	Government / Public sector.....	E4E01	E4E02	E4E03
E4F	Repos / reverse repos.....	E4F01	E4F02	E4F03
E4G	Trade related letters of credit.....	E4G01	E4G02	E4G03
E4H	Overdrafts.....	E4H01	E4H02	E4H03
E5A	Swaps and FRAs.....	E5A01	E5A02	E5A03
E5B	Forward foreign exchange.....	E5B01	E5B02	E5B03
E5C	Forward sales and purchases.....	E5C01	E5C02	E5C03
E5D	Other off balance sheet.....	E5D01	E5D02	E5D03
E2A	Fees and other income.....	E2A01	E2A02	E2A03
E2B	Other funding sources.....	E2B01	E2B02	E2B03
E3A	<b>Total inflows.....</b>	<b>E3A01</b>	<b>E3A02</b>	<b>E3A03</b>

LR.2.7

4	5	6	7	8	9	Item No
Over 8 days to 1 month	Over 1 months to 3 months	Over 3 months to 6 months	Over 6 months to 1 year	Over 1 year	Total (Columns 1 to 8)	

E1A04	E1A05	E1A06	E1A07	E1A08	E1A09	E1A
E1B04	E1B05	E1B06	E1B07	E1B08	E1B09	E1B
E1C04	E1C05	E1C06	E1C07	E1C08	E1C09	E1C
E1D04	E1D05	E1D06	E1D07	E1D08	E1D09	E1D
E1E04	E1E05	E1E06	E1E07	E1E08	E1E09	E1E
E1F04	E1F05	E1F06	E1F07	E1F08	E1F09	E1F

E4A04	E4A05	E4A06	E4A07	E4A08	E4A09	E4A
E4B04	E4B05	E4B06	E4B07	E4B08	E4B09	E4B
E4C04	E4C05	E4C06	E4C07	E4C08	E4C09	E4C
E4D04	E4D05	E4D06	E4D07	E4D08	E4D09	E4D
E4E04	E4E05	E4E06	E4E07	E4E08	E4E09	E4E
E4F04	E4F05	E4F06	E4F07	E4F08	E4F09	E4F
E4G04	E4G05	E4G06	E4G07	E4G08	E4G09	E4G
E4H04	E4H05	E4H06	E4H07	E4H08	E4H09	E4H

E5A04	E5A05	E5A06	E5A07	E5A08	E5A09	E5A
E5B04	E5B05	E5B06	E5B07	E5B08	E5B09	E5B
E5C04	E5C05	E5C06	E5C07	E5C08	E5C09	E5C
E5D04	E5D05	E5D06	E5D07	E5D08	E5D09	E5D

E2A04	E2A05	E2A06	E2A07	E2A08	E2A09	E2A
E2B04	E2B05	E2B06	E2B07	E2B08	E2B09	E2B

E3A04	E3A05	E3A06	E3A07	E3A08	E3A09	E3A
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LR.2.8

# PART 3 (continued)

## Behavioural basis

Item No	1	2	3
	Overdue	Demand (incl. next day)	8 days and under (excl. next day)
<b>Outflows</b>			
<i>Retail</i>			
F1A	Time deposits.....	<b>F1A02</b>	<b>F1A03</b>
F1B	No notice / current accounts.....	<b>F1B02</b>	<b>F1B03</b>
F1C	Additional advances committed.....	<b>F1C02</b>	<b>F1C03</b>
<i>Wholesale</i>			
Non-marketable securities and debt instruments and marketable assets			
F5A	maturing within 1 month.....	<b>F5A02</b>	<b>F5A03</b>
F2A	Additional advances committed.....	<b>F2A02</b>	<b>F2A03</b>
F5C	Intragroup / Connected.....	<b>F5C02</b>	<b>F5C03</b>
F5D	Interbank (excluding any intragroup).....	<b>F5D02</b>	<b>F5D03</b>
F5E	Corporate (non-interbank and non-intragroup).....	<b>F5E02</b>	<b>F5E03</b>
F5F	Government / Public sector.....	<b>F5F02</b>	<b>F5F03</b>
F5G	Repos / Reverse Repos.....	<b>F5G02</b>	<b>F5G03</b>
F5H	Trade related letters of credit.....	<b>F5H02</b>	<b>F5H03</b>
F6A	Swaps and FRAs.....	<b>F6A02</b>	<b>F6A03</b>
F6B	Forward foreign exchange.....	<b>F6B02</b>	<b>F6B03</b>
F6C	Forward sales and purchases.....	<b>F6C02</b>	<b>F6C03</b>
F6D	Other off balance sheet.....	<b>F6D02</b>	<b>F6D03</b>
F3A	Dividends, tax, other costs and outflows.....	<b>F3A02</b>	<b>F3A03</b>
F4A	<b>Total outflows</b> .....	<b>F4A02</b>	<b>F4A03</b>
		<b>LR.2.9</b>	

4	5	6	7	8	9	Item No
Over 8 days to 1 month	Over 1 months to 3 months	Over 3 months to 6 months	Over 6 months to 1 year	Over 1 year	Total (Columns 2 to 8)	

F1A04	F1A05	F1A06	F1A07	F1A08	F1A09	F1A
F1B04	F1B05	F1B06	F1B07	F1B08	F1B09	F1B
F1C04	F1C05	F1C06	F1C07	F1C08	F1C09	F1C

F5A04	F5A05	F5A06	F5A07	F5A08	F5A09	F5A
F2A04	F2A05	F2A06	F2A07	F2A08	F2A09	F2A
F5C04	F5C05	F5C06	F5C07	F5C08	F5C09	F5C
F5D04	F5D05	F5D06	F5D07	F5D08	F5D09	F5D
F5E04	F5E05	F5E06	F5E07	F5E08	F5E09	F5E
F5F04	F5F05	F5F06	F5F07	F5F08	F5F09	F5F
F5G04	F5G05	F5G06	F5G07	F5G08	F5G09	F5G
F5H04	F5H05	F5H06	F5H07	F5H08	F5H09	F5H

F6A04	F6A05	F6A06	F6A07	F6A08	F6A09	F6A
F6B04	F6B05	F6B06	F6B07	F6B08	F6B09	F6B
F6C04	F6C05	F6C06	F6C07	F6C08	F6C09	F6C
F6D04	F6D05	F6D06	F6D07	F6D08	F6D09	F6D

F3A04	F3A05	F3A06	F3A07	F3A08	F3A09	F3A
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F4A04	F4A05	F4A06	F4A07	F4A08	F4A09	F4A
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LR.2.10

# PART 4

## Calculation of liquidity mismatches

Item No	1 Overdue (excluded)	2 Demand (incl. next day)	3 8 days and under	4 1 month and under	Item No
<b>Contractual Basis</b>					
<b>Inflows</b>					
G1A	Cumulative discounted marketable assets.....		<b>G1A03</b>	<b>G1A04</b>	G1A
G1B	Plus total cumulative standard inflows.....	<b>G1B02</b>	<b>G1B03</b>	<b>G1B04</b>	G1B
G1C	Plus Y% * committed lines granted to the bank.....				G1C
G1D	Y% .....				G1D
G1E	<b>Equals total inflows (A).....</b>	<b>G1E02</b>	<b>G1E03</b>	<b>G1E04</b>	G1E
<b>Outflows</b>					
G2A	Total cumulative standard outflows.....	<b>G2A02</b>	<b>G2A03</b>	<b>G2A04</b>	G2A
G2B	Plus undrawn commitments to lend granted by the bank.....	<b>G2B02</b>			G2B
G2C	Z%.....				G2C
G2D	Plus undrawn credit card and other revolving commitments to lend..	<b>G2D02</b>			G2D
G2E	W% .....				G2E
G2F	<b>Equals total outflows (B).....</b>	<b>G2F02</b>	<b>G2F03</b>	<b>G2F04</b>	G2F
<b>Mismatch</b>					
G3A	Net mismatch: standard basis (A - B).....	<b>G3A02</b>	<b>G3A03</b>	<b>G3A04</b>	G3A
G4A	Total deposits (X).....	<b>G4A02</b>			G4A
G5A	<b>Mismatch as % of deposits [(A-B)/X] (to 2 decimal places)</b>	<b>G5A02</b>	<b>G5A03</b>	<b>G5A04</b>	G5A
<b>Behaviourally Adjusted Basis</b>					
<b>Inflows</b>					
G6A	Cumulative discounted marketable assets.....		<b>G6A03</b>	<b>G6A04</b>	G6A
G6B	Plus total cumulative behaviourally adjusted inflows.....	<b>G6B02</b>	<b>G6B03</b>	<b>G6B04</b>	G6B
G6C	Plus Y% * committed lines granted to the bank.....	<b>G6C02</b>	<b>G6C03</b>	<b>G6C04</b>	G6C
G6D	Y%.....	<b>G6D02</b>	<b>G6D03</b>	<b>G6D04</b>	G6D
G6E	<b>Equals total inflows (C).....</b>	<b>G6E02</b>	<b>G6E03</b>	<b>G6E04</b>	G6E
<b>Outflows</b>					
G7A	Total cumulative behaviourally adjusted outflows.....	<b>G7A02</b>	<b>G7A03</b>	<b>G7A04</b>	G7A
G7B	Plus undrawn commitments to lend granted by the bank.....	<b>G7B02</b>	<b>G7B03</b>	<b>G7B04</b>	G7B
G7C	Z% .....	<b>G7C02</b>	<b>G7C03</b>	<b>G7C04</b>	G7C
G7D	Plus undrawn credit card and other revolving commitments to lend..	<b>G7D02</b>	<b>G7D03</b>	<b>G7D04</b>	G7D
G7E	W% .....	<b>G7E02</b>	<b>G7E03</b>	<b>G7E04</b>	G7E
G7F	<b>Equals total outflows (D).....</b>	<b>G7F02</b>	<b>G7F03</b>	<b>G7F04</b>	G7F
<b>Mismatch</b>					
G8A	Net mismatch: behaviourally adjusted basis (C - D).....	<b>G8A02</b>	<b>G8A03</b>	<b>G8A04</b>	G8A
G8B	Total deposits (X).....	<b>G8B02</b>			G8B
G8C	<b>Mismatch as % of deposits [(C-D)/X] (to 2 decimal places)</b>	<b>G8C02</b>	<b>G8C03</b>	<b>G8C04</b>	G8C

In order to assist with the scanning process please enter decimal points clearly and do not enter the % symbol in any of the boxes of this form

# PART 4 (continued)

## Exceptions to Guidelines

**Net cumulative mismatch  
as a percentage of total deposits**

Item No	1				2	3	Item No
	Date (ddmm format)				Sight to eight days (to 2 decimal places)	Sight to one month (to 2 decimal places)	
H1A					H1A02	H1A03	H1A
H1B					H1B02	H1B03	H1B
H1C					H1C02	H1C03	H1C
H1D					H1D02	H1D03	H1D
H1E					H1E02	H1E03	H1E
H1F					H1F02	H1F03	H1F
H1G					H1G02	H1G03	H1G
H1H					H1H02	H1H03	H1H
H1J					H1J02	H1J03	H1J
H1K					H1K02	H1K03	H1K
H1L					H1L02	H1L03	H1L
H1M					H1M02	H1M03	H1M
H1N					H1N02	H1N03	H1N
H1P					H1P02	H1P03	H1P
H1Q					H1Q02	H1Q03	H1Q
H1R					H1R02	H1R03	H1R
H1S					H1S02	H1S03	H1S
H1T					H1T02	H1T03	H1T
H1U					H1U02	H1U03	H1U
H1V					H1V02	H1V03	H1V
					<b>LR.2.12</b>		

In order to assist with the scanning process please enter decimal points clearly and do not enter the % symbol in any of the boxes of this form



# PART 5

## Deposit Concentration

### Part A: Large Deposits

	1	2					3				
Item No	Customer (a)	Maturity date (b) (ddmmyy format blank=undated, V=various)					Currency (c) (using international country codes blank=sterling, V=various)				
J1A	J1A01										
J1B	J1B01										
J1C	J1C01										
J1D	J1D01										
J1E	J1E01										
J1F	J1F01										
J1G	J1G01										
J1H	J1H01										
J1J	J1J01										
J1K	J1K01										
J1L	J1L01										
J1M	J1M01										
J1N	J1N01										
J1P	J1P01										
J1Q	J1Q01										
J1R	J1R01										
J1S	J1S01										
J1T	J1T01										
J1U	J1U01										
J1V	J1V01										
K1A	K1A01										
K1B	K1B01										
K1C	K1C01										
K1D	K1D01										
K1E	K1E01										
K1F	K1F01										
K1G	K1G01										
K1H	K1H01										
K1J	K1J01										
K1K	K1K01										
K1L	K1L01										
K1M	K1M01										
K1N	K1N01										
K1P	K1P01										
K1Q	K1Q01										
K1R	K1R01										
K1S	K1S01										
K1T	K1T01										
K1U	K1U01										
K1V	K1V01										

4

5

6

7

8

Amount (d)	Maximum amount in reporting period (e)	Client money (C) (f) (please tick)	Mandated accounts (M) (g) (please tick)	Customers connected to reporting bank (CC) (please tick)	Item No
J1A04	J1A05	J1A06	J1A07	J1A08	J1A
J1B04	J1B05	J1B06	J1B07	J1B08	J1B
J1C04	J1C05	J1C06	J1C07	J1C08	J1C
J1D04	J1D05	J1D06	J1D07	J1D08	J1D
J1E04	J1E05	J1E06	J1E07	J1E08	J1E
J1F04	J1F05	J1F06	J1F07	J1F08	J1F
J1G04	J1G05	J1G06	J1G07	J1G08	J1G
J1H04	J1H05	J1H06	J1H07	J1H08	J1H
J1J04	J1J05	J1J06	J1J07	J1J08	J1J
J1K04	J1K05	J1K06	J1K07	J1K08	J1K
J1L04	J1L05	J1L06	J1L07	J1L08	J1L
J1M04	J1M05	J1M06	J1M07	J1M08	J1M
J1N04	J1N05	J1N06	J1N07	J1N08	J1N
J1P04	J1P05	J1P06	J1P07	J1P08	J1P
J1Q04	J1Q05	J1Q06	J1Q07	J1Q08	J1Q
J1R04	J1R05	J1R06	J1R07	J1R08	J1R
J1S04	J1S05	J1S06	J1S07	J1S08	J1S
J1T04	J1T05	J1T06	J1T07	J1T08	J1T
J1U04	J1U05	J1U06	J1U07	J1U08	J1U
J1V04	J1V05	J1V06	J1V07	J1V08	J1V
K1A04	K1A05	K1A06	K1A07	K1A08	K1A
K1B04	K1B05	K1B06	K1B07	K1B08	K1B
K1C04	K1C05	K1C06	K1C07	K1C08	K1C
K1D04	K1D05	K1D06	K1D07	K1D08	K1D
K1E04	K1E05	K1E06	K1E07	K1E08	K1E
K1F04	K1F05	K1F06	K1F07	K1F08	K1F
K1G04	K1G05	K1G06	K1G07	K1G08	K1G
K1H04	K1H05	K1H06	K1H07	K1H08	K1H
K1J04	K1J05	K1J06	K1J07	K1J08	K1J
K1K04	K1K05	K1K06	K1K07	K1K08	K1K
K1L04	K1L05	K1L06	K1L07	K1L08	K1L
K1M04	K1M05	K1M06	K1M07	K1M08	K1M
K1N04	K1N05	K1N06	K1N07	K1N08	K1N
K1P04	K1P05	K1P06	K1P07	K1P08	K1P
K1Q04	K1Q05	K1Q06	K1Q07	K1Q08	K1Q
K1R04	K1R05	K1R06	K1R07	K1R08	K1R
K1S04	K1S05	K1S06	K1S07	K1S08	K1S
K1T04	K1T05	K1T06	K1T07	K1T08	K1T
K1U04	K1U05	K1U06	K1U07	K1U08	K1U
K1V04	K1V05	K1V06	K1V07	K1V08	K1V

## PART 5 (continued)

### Deposit Concentration

#### Part B: Client money and mandated accounts held

Item No	1	2	3	Item No
		Amount	Maximum amount in reporting period	
L1A	Client Money (f).....	<b>L1A02</b>	<b>L1A03</b>	L1A
L1B	Mandated accounts (g).....	<b>L1B02</b>	<b>L1B03</b>	L1B
	.			
	.			

#### Notes for completing Part 5

- a) Principal customer in the case of closely related depositors/lenders.
- b) Where an individual deposit comprises 25% or more of the total for a particular depositor / group of depositors and has a different maturity from the remainder, it should be reported separately and bracketed. Otherwise where deposits have been received with a variety of maturity dates, reporting institutions need not supply a full list of dates but may write the letter V in the first section of column 2. Where the deposit is undated, this column should be left blank.
- c) Enter the currency and not the amount. The codes used for each currency should be consistent with the international codes used for the Bank of England returns. Where an individual deposit comprises 25% or more of the total for a particular depositor/group of depositors and has a different currency from the remainder, it should be reported separately and bracketed. Otherwise, where deposits are received in a variety of currencies, reporting institutions need not supply details of each currency amount but may write the letter V in the first section of column 3. Where the deposit is in sterling, this column should be left blank.
- d) Enter the sterling (or euro amount, if appropriate) or the sterling equivalent (or euro equivalent) if the deposit/loan is in currency other than sterling (or euro).
- e) Only complete this column for deposits still outstanding at the reporting date.
- f) Funds subject to the FSA's (previously SIB's) client money regulations.
- g) Funds held in accounts operated by a Financial Services Act authorised firm under a mandate signed by the account holder.

**LR.2.15**

Immediately before the SLR1 definitions, insert the following:

To be used for all reports completed as at 1 December 2001 or after

# FORM M1 - Holdings of credit and financial institutions' and non-financial companies' capital instruments



Reporting institution \_\_\_\_\_

as at. 

--	--	--

  
(eg 31 12 2001)

FSA number \* 

		F	S	A	
--	--	---	---	---	--

Unconsolidated/solo consolidated/consolidated - tick as appropriate

Unconsolidated  Solo consolidated  Consolidated

(sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

\_\_\_\_\_ Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on Completion**

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA.
- 2 Complete the return quarterly on an unconsolidated/solo consolidated basis in conjunction with Form BSD3.
- 3 Complete the return half-yearly on a consolidated basis in conjunction with Form BSD3.
- 4 Enter amounts to the nearest thousands omitting £000s/€000s
- 5 For definitions of items, refer to the Guidance Notes
- 6 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 7 Submit within 10 business days for unconsolidated/solo consolidated returns and 20 business days for consolidated returns or 12 and 22 business days respectively for those institutions reporting electronically to:
 

**The Financial Services Authority**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**
- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
--------------	-----------	--------------

September 2001

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

1 Please tick if completion in Euros .....

**SECTION 1: Holdings in credit and financial institutions' capital instruments**

10	Trading Book concession granted (tick if yes).....	<input type="checkbox"/>	
			000s
20	If Trading Book concession granted, what amount.....		20
30	Concession to hold own group paper in Trading Book (tick if yes)	<input type="checkbox"/>	
40	If concession granted, what amount.....		40
	<b>Total amount of credit and financial institutions' capital instruments held</b>		
50	<b>Total amount held</b> (items 60 + 70)		50
60	Banking Book		60
70	Trading Book (items 70.1 to 70.4).....		70
70.1	other institutions' paper eligible for a Trading Book concession.....		70
70.2	holdings eligible for own group concession.....		70
70.3	paper not eligible for Trading Book concession (deductible from Tiers 1 & 2).		70
70.4	holdings of own Tier 1 instruments (deductible from Tier 1).....		70
80	<b>Holdings in excess of 10% of other credit and financial institutions' capital</b>		80
	<b>Credit or financial institution</b>	<b>Amount</b>	<b>Excess</b>
80.01	.....		80.01E
80.02	.....		80.02E
80.03	.....		80.03E
80.04	.....		80.04E
80.05	.....		80.05E
80.06	.....		80.06E
80.07	.....		80.07E
80.08	.....		80.08E
80.09	.....		80.09E
80.10	.....		80.10E
<b>Total</b>	.....		

**Total amount deducted from Tier 1 and Tier 2 capital or risk weighted as at reporting date:**

000s

90	Banking Book on-Balance sheet (deductions).....	90
100	Banking Book off-Balance sheet (deductions).....	100
110	Trading Book (deductions).....	110
120	Banking Book (risk weighted) .....	120
130	Trading Book (non deductible) .....	130

**140 Five largest holdings in credit and financial institutions, at reporting date**

**Credit or financial institution**

**Amount**

140.1	.....	
140.2	.....	
140.3	.....	
140.4	.....	
140.5	.....	

**SECTION 2: Qualifying holdings in non-financial companies**

150	Total amount of qualifying holdings	150
160	Total amount of qualifying holdings in excess of 15% of capital	160
170	Total amount of qualifying holdings in excess of 60% of capital	170
180	Total deductions from capital (also report this figure in item A180.4 on BSD3)	180

Immediately before the Supervisory Guidance Notes, insert the following:



To be used for all reports completed as at 1 December 2001 or after

# FORM SLR1 - Stock Liquidity Return



**Reporting Institution** \_\_\_\_\_

as at..... 

--	--	--

  
 (eg 12 12 2001)

**FSA Number\***

		<b>F</b>	<b>S</b>	<b>A</b>	
--	--	----------	----------	----------	--

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA. I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

\_\_\_\_\_ Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on completion**

- 1 If you have any difficulty in completing this return, please telephone your usual supervisory contact at the FSA.
- 2 For definitions, refer to the Guidance Notes
- 3 Enter amounts to nearest thousands omitting £000s.
- 4 This form should be completed as at the **SECOND WEDNESDAY OF THE MONTH**. It should also be completed for any exception within the month.
- 5 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 6 Submit the **monthly** return within **six business days** of the reporting date, clearly addressed to:

**FINANCIAL SERVICES AUTHORITY**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**

- 7 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.
- 8 Submit any **exception** reports direct to your supervisor at the Financial Services Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS.

FSA use only	Logged in	Date entered
--------------	-----------	--------------

September 2001

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

**1 STERLING STOCK:**

1.1	Cash.....	1.1	
1.2	Operational balances with Bank of England.....	1.2	
1.3	Treasury Bills.....	1.3	
1.4	Gilts.....	1.4	
1.5	Eligible bank bills.....	1.5	
1.6	Eligible local authority bills.....	1.6	
1.7	Certificates of tax deposits.....	1.7	
1.8	Other.....	1.8	
<b>1.0</b>	<b>TOTAL</b> .....		1.0
	<i>(Item 1 should be equal or greater than item 2.2)</i>		
<b>2.1</b>	<b>WHOLESALE STERLING NET OUTFLOW LIMIT</b> .....		2.1
	5 WORKING DAYS as agreed with Financial Services Authority		
<b>2.2</b>	<b>STERLING STOCK FLOOR</b> .....		2.2
	5 WORKING DAYS as agreed with Financial Services Authority		
<b>3.0</b>	<b>WHOLESALE STERLING NET OUTFLOW</b> .....		3.0
	5 WORKING DAYS		
<b>4.0</b>	<b>STERLING CERTIFICATES OF DEPOSITS HELD</b>		4.0
4.1	TOTAL.....	4.1	
4.2	Liquidity conversion factor..... <b>X</b>	4.2	
4.3	Total discounted certificates of deposit..... =	4.3	
	<i>(Equal to item 4.1 times item 4.2)</i>		
4.4	Allowable certificates of deposit.....		4.4
	<i>(Item 4.4 should not be greater than 50% of item 3.0)</i>		
4.5	Remaining certificates of deposit.....	4.5	
	<i>(Item 4.4 plus item plus 4.5 should equal 4.3)</i>		
<b>5.0</b>	<b>STERLING RETAIL DEPOSITS:</b>		
5.1	Sterling retail deposits falling due in next 5 working days.....	5.1	
5.2	Liquidity conversion factor..... <b>X</b>	5.2	
5.3	Sterling retail deposits to be covered..... =		5.3
	<i>(Equal to item 5.1 times item 5.2)</i>		
<b>6.0</b>	<b>STERLING LIQUIDITY RATIO (LQR)</b> (rounded to two decimal places and multiplied by 100, ie places input as integers).....		6.0

$$LQR = \left( \frac{A}{(B - C) + D} \right) \times 100\%$$

**CREDIT UNIONS SOURCEBOOK (AMENDMENT NO 5 AND CONSEQUENTIAL AMENDMENTS TO THE HANDBOOK) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in or under the following sections of the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making powers);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance)
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force as follows:
- (1) the amendments in Annex A come into force on 1 August 2004;
  - (2) CRED 14.10.8AG comes into force on 1 August 2004;
  - (3) CRED 10.3.6R comes into force on 31 October 2004;
  - (4) the remainder of this instrument comes into force on 1 March 2004.

**Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with Annex A to this instrument.

**Amendments to the Credit Unions sourcebook**

- E. The Credit Unions sourcebook is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Credit Unions Sourcebook (Amendment No 5 and Consequential Amendments to the Handbook) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex A

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

SUP 16 Annex 14  
Reporting requirements

16 Ann14(2) R Annual return (CY) for credit unions

...

#### Notes to accounts

...

#### Provision for members' doubtful debt

<i>General provision</i>	Balance at beginning of year		
	...		
	<del>Written off during year</del>	(—————)	16C
	...		
<i>Specific provision</i>	Balance at beginning of year		
	...		
	Written off during year	(—————)	16H
	Decrease in year	(—————)	16J
	...		
...			

#### Auditor's statement

In my opinion, the information contained in the balance sheet and revenue account of the Annual Return ~~has been completely and accurately extracted from~~ is \* / is not \*# consistent with the audited accounts published in accordance with section 3A of the Friendly and Industrial and Provident Societies Act 1968.

\* delete as appropriate

# attach a statement detailing inconsistencies

...

SUP 16 Annex 15  
Reporting requirements

16 Ann15(2) G Notes on completing the Annual Return (CY) for credit unions

...

#### General information

The Annual Return (CY) should be completed by all *credit unions* in Great Britain at the end of their financial year. The form may be updated from time to time. Credit unions should use the form in force at the end of the financial year on which they are reporting. It should be completed using the accruals-based accounting method.

...

**Revenue account**

...

**Expenditure**

4A Admin expenses This figure should include the following expenditure items as a total figure:

- ...
- 5. Legal fees
- 6. Depreciation
- 7. Other

...

**Applications**

...

9D Rate of dividend The percentage of dividend paid on members' accounts. *Credit unions* cannot pay more than 8% dividend to members in any one financial year even if several dividends are paid. **If different rates are paid on different types of accounts these different rates should be shown in the boxes provided.**

...

**Provision for members' doubtful debts**

**General Provision**

...

16C ~~Written off in year~~ ~~The total amount of loans written off from the general bad debt provision during the financial.~~

...

**FIXED ASSETS**

17A ~~Opening net book value~~ ~~cost~~ The ~~value total amount~~ of fixed assets the *credit union* had at the end of the previous financial year.

17B ~~Additions during the year~~ ~~at cost~~ The ~~value total amount~~ of fixed assets purchased during the financial year.

17C ~~Value-Original cost of~~ ~~disposals during the year~~ The ~~value total amount~~ of fixed assets sold during the financial year, included within 17A shown at original cost. It is shown as a negative, as it reduces the total amount of fixed assets held by the *credit union*.

17D Opening depreciation Total value Amount of depreciation at the end of the previous financial year.

17E	Depreciation charge in year	Total amount of depreciation charged to <u>expenditure this financial year against assets.</u>
17F	Depreciation eliminated on disposals	Total <del>value amount taken out due to disposal</del> of <u>depreciation associated with assets disposed of during the year.</u>
17G	<u>Closing n</u> Net book value	The <del>value total amount</del> of fixed assets held by the <i>credit union</i> at the end of the financial year. This figure is the sum total of boxes <b>17A+17B-17C-17D-17E-17F</b> and match that shown in the balance sheet at <b>1A</b> .
...		
32D	Total assets	This is the same as box <b>1PM</b> on the Balance Sheet.
...		

**Auditor's statement**

This statement that the information in the Annual Return (CY) is or is not consistent with ~~has been completely and accurately extracted from~~ the annual audited accounts of the *credit union* should be completed by the *credit union's* auditor (with an attached statement detailing inconsistencies if there are any). It is important to note that the *credit union* remains responsible for the completion of the Annual Return (CY).

## Annex B

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted the place where it goes is indicated and it is not underlined.

- 4.3.68 G The committee of management should consider the range of possible outcomes in relation to various risks. These risks are increased when a *credit union* provides ancillary services like issuing and administering means of payment and money transmission, which result, in particular, in higher liquidity and operational risks.
- ...
- 7.2.6 G (1) ...  
...  
(4) ...  
  
(5) CRED 9.3.7R(2) applies to loans between *credit unions* in relation to liquidity.
- 7.2.7 G Loans between *credit unions* should only be arranged after careful consideration by both parties. For example:
- (1) the borrower should consider the financial implications of relying on such borrowing in order to lend to members, or to finance share withdrawals; and
- (2) the lender should assess the risk of late and non-repayment arising from the borrower's own liquidity and credit risks, and keep the aggregate of its loans to other *credit unions* to a very modest level.
- Land holding
- 7.2.8 G A *credit union* may only hold land (and buildings) for the purpose of conducting its business on that land, and where it needs to do so as security for loans to members (section 12 of the Credit Unions Act 1979). This means that a *credit union* must not acquire as an investment land (and buildings) greatly in excess of its operating requirements, with the real purpose of letting out the excess.
- ...
- 7.3 Borrowing and Financial risk management
- Borrowing

7.3.1	R	<u>[Deleted]</u>
<u>7.3.1A</u>	R	<u>A credit union must not borrow from a natural person, except by subordinated loan qualifying as capital under CRED 8.2.1R(4).</u>
7.3.2	G	<u>[Deleted]</u>
<u>7.3.2A</u>	G	<u>Although section 10 of the Credit Unions Act 1979 now permits a credit union to borrow money without restriction, CRED 7.3.1AR imposes a limitation. Further explanation is given at CRED 7A.3.2 G.</u>
		<u>Borrowing</u>
...		
7A.3		<u>Deposits by persons too young to be members</u>
7A.3.1	R	(1) <u>A credit union must not accept deposits except:</u>  <ul style="list-style-type: none"> <li>(a) <u>as shares from its members who are natural persons qualifying in accordance with CRED Ann2 Table 1G 1;</u> <u>or</u></li> <li>(b) <u>from natural persons too young to be members under CRED 7A.3.1R(2); or</u></li> <li>(c) <u>as loans from persons under CRED 7.3.1AR – CRED 7.3.2AG.</u></li> </ul>
		(2) <u>A credit union must not accept take deposits exceeding the greater of £5,000 and 1.5 per cent of the total shareholdings in the credit union from a person who is under the age at which, under section 20 of the Industrial and Provident Societies 1965, he may become a member of the credit union.</u>
7A.3.2	G	(1) <u>The effect of the general prohibition in section 19 of the Act is that no person may carry on the regulated activity of accepting deposits, unless authorised or exempt.</u>  (2) <u>CRED 7.3.1AR and CRED 7A.3.1R are intended to ensure that the liberalisation of credit union borrowing (CRED 7.3.2AG) does not have the unintended effect of undermining the common bond concept (CRED 13 Ann1G) by allowing credit unions to operate deposit accounts for natural persons who do not qualify for membership.</u>  (3) <u>Section 20 of the Industrial and Provident Societies Act 1965 provides that a person above the age of 16 may be a member of a credit union, unless its rules provide to the contrary (see CRED 13 Ann2 Table1G3.</u>



- (4) CRED 13 Ann2G Table 1G3 gives guidance on the eligibility of natural persons too young to be members.
- (5) (a) A credit union is no longer required to:
- (i) hold such juvenile deposits in a fund apart from the general funds of the credit union; and
  - (ii) distribute all the interest earned on the fund (after deduction of expenses) to juvenile depositors.
- (b) A credit union may make a commercial judgement on the appropriate amount of interest to pay juvenile depositors.
- (c) These changes were made by amendment of section 9 of the Credit Unions Act 1979 by Order under section 428 of the Act. (The Financial Services and Markets Act 2000 (Consequential Amendments and Transitional Provisions) (Credit Unions) Order 2002 - SI 2002 No. 1501)

...

9.2.8 G ...

9.2.9 G When a credit union provides ancillary services such as issuing and administering means of payment and money transmission, it should take into account the potentially greater volatility of its funds when deciding what amount and composition of liquid assets is necessary to comply with CRED 9.2.1R.

...

- 9.3.7 R (1) For the purposes of CRED 9.3.2R – CRED 9.3.5R, only those assets shall count as liquid which can be realised for cash at short notice, and within at most eight days.
- (2) Amounts loaned by one credit union to another must not be counted as liquid by the lender.

...

10.2 General requirements concerning lending policy

...

10.2.6 G ...

- 10.2.6A R (1) A credit union must not make a loan to:
- (a) an officer, or other approved person; and

- (b) a relative of, or any person other wise connected with, anyone included in (1) above, on terms more favourable than those available to other members of the *credit union*.
- (2) "Relative" has the same meaning as in section 31 of the Credit Unions Act 1979.
- 10.2.7 G (1) To prevent conflicts of interest, a *A-credit union* should have clear arrangements for dealing with loans to ~~officers, staff and the persons specified in CRED 10.2.6A R~~ *connected persons* (for example, relatives and other close relationships) to prevent conflicts of interest.
- (2) In relation to staff, the prohibition in CRED 10.2.6A R applies only to those who are officers or *approved persons*.
- (3) "Connected" in CRED 10.2.6A R includes any close business or personal relationship.
- ...
- 10.2.10 G ...
- 10.2.11 G (1) A *credit union* may only make loans to:
- (a) its members who are natural *persons* qualifying in accordance with section 1(2) of the Credit Unions Act 1979 (see CRED 13 Ann2 Table 1G 1);
- (b) other *credit unions*.
- (2) A *credit union* may make a loan to a member for a business purpose. However, this does not mean that the *credit union* may make a loan to a member who merely intends to transmit that loan to another body that will actually carry out the purpose. A *credit union* should not make loans to members who are acting together to achieve an aggregate loan that exceeds the limits in CRED 10.3.
- 10.3 Lending limits
- 10.3.1 R Subject to CRED 10.3.6R, a *A-version 1 credit union* must not lend for a period of more than three years where unsecured and seven years where secured.
- ...
- 10.3.3 R Subject to CRED 10.3.6R, a *A-version 2 credit union* must not lend for a period of more than five years where unsecured and fifteen years where secured.

...

10.3.5 G ...

10.3.6 R *A credit union with permission for entering into a regulated mortgage contract must not enter into such a contract for a term of more than 25 years.*

...

13.1.1 G This chapter applies to:

(1) [Deleted]

(1A) *a person considering applying to the FSA for approval of the use in a name of the words "credit union" or "undeb credyd";*

(2) ...

...

After section 13.2 insert the following new section.

13.2A Use of name "credit union"

13.2A.1 G Section 3 of the Credit Unions Act 1979 (as amended) makes the following provisions about the use of the name "credit union":

(1) under section 3(1), every credit union with its registered office:

(a) in England or Scotland should have "credit union" in its name;

(b) in Wales should have "credit union" or "undeb credyd" in its name;

(2) under section 3(2), unless one is registered as a credit union, it is an offence to:

(a) refer to oneself as a "credit union" or "undeb credyd", or any related words;

(b) represent oneself as being a credit union;

subject to section 3(3) (see *CRED* 13.2AG(3));

(3) section 3(3) provides that section 3(2) (see *CRED* 13.2A.1G(2)) does not apply:

- (a) to specified overseas deposit-takers;
- (b) to a *person* who has the *FSA's* written approval;
- (c) where an officer or employee uses a title or descriptive expression indicating his office or post with:
  - (i) a credit union; or
  - (ii) an organisation in *CRED* 13.2AG(3)(a) or (b).

13.2A.2 G The effect of section 3 of the Credit Unions Act 1979 (see *CRED* 13.2A.1G) is that if one of the following organisations, for example, wishes to use the words "credit union" in its name, it will need the approval in writing of the *FSA*:

- (1) a study group working towards registration as a credit union;
- (2) a body representing or providing services to credit unions.

13.2A.3 G Approval for study groups (*CRED* 13.2A.2G(1)) will generally be limited to a period of no more than 2 years.

13.2A.4 G The organisations in *CRED* 13.2A.2G are subject to the general prohibition mentioned in *CRED* 7A.3.2G(1), which means that they cannot accept *deposits*.

...

13.4.1 G (1) For registration, applicants must demonstrate to the satisfaction of the *FSA* that the statutory conditions set out in section 1 of the Credit Unions Act 1979 will be fulfilled. *CRED* 13 Ann 1G contains a table listing these statutory conditions. The application pack contains the relevant forms for registration and explanatory notes on how to complete the forms. *CRED* 13 Ann 2G contains information about eligibility for membership of a credit union ~~*credit union*~~.

- (a) One of the conditions is that the objects of the credit union are those, and only those, of a credit union. The objects are set out in full in the table. Unless an activity is consistent with these objects, a credit union has no power to engage in it. It is important that a credit union satisfies itself that it has the necessary power before engaging in the activity. For instance, it is clear that a credit union does not have the power to run a lottery. However, a credit union is permitted to receive donations from an outside organisation, so may receive the proceeds from a lottery run by that organisation. Any such organisation will need to be independent from the credit union, with separate management and accounting.
- (b) Another condition is that admission to membership of the credit union is restricted to persons who fulfil an appropriate membership qualification ("AMQ") and that in consequence a common bond exists among the members.

- (2) The application pack contains the relevant forms for registration and explanatory notes on how to complete the forms. The notes also contain information about the appropriate membership qualifications for credit unions.
- (3) ...

...

CRED 13 Annex 1  
Requirements of Registration G

1 G Table: The requirements of registration under the Industrial and Provident Societies Act 1965, as set out in the Credit Unions Act 1979 and referred to in *CRED* 13.4.1G.

REQUIREMENT	SECTION OF THE RELEVANT ACTS
That the <del>purposes</del> <u>objects</u> of the society are those, and only those of a credit union.	Credit Unions Act 1979, s.1(2)(a)
<u>The objects of a credit union are:</u> ... the creation of sources of <del>credit</del> <u>credit</u> for the benefit of the members at a fair and reasonable rate of interest	Credit Unions Act 1979, s.1(3)

...	
the training and education of the members in the wise use of <del>money</del> <u>money</u> and in the management of their financial affairs	Credit Unions Act 1979, s.1(3)
That admission to membership of the society is restricted to individuals all of whom fulfil a specific qualification which is appropriate to a credit union ( <del>the</del> <u>and that in consequence a "common bond" exists</u> between members).	Credit Unions Act 1979, s.1(2)(b)
<u>The appropriate membership qualifications ("AMQs") for a credit union are:</u>	
following a particular occupation	Credit Unions Act 1979, s.1(4)(a)
residing in a particular locality	Credit Unions Act 1979, s.1(4)(b)
being employed in a particular locality	Credit Unions Act 1979, s.1(4)(c)
being employed by a particular employer	Credit Unions Act 1979, s.1(4)(d)
being a member of a bona fide organisation or being otherwise associated with other members of the society for a purpose other than that of forming a society to be registered as a credit union	Credit Unions Act 1979, s.1(4)(e)
residing in or being employed in a particular locality	Credit Unions Act 1979, s.1(4)(f)
<u>and such other qualifications as are for the time being approved by the FSA</u>	<u>Credit Unions Act 1979, s.1(4)</u>
<u>The following qualifications (in addition to those set out in section 1(4) of the Credit Unions Act 1979) have been approved by the FSA or its predecessor, the Registry of Friendly Societies:</u>	
...	
<del>any other qualifications as approved by the FSA</del>	

...

CRED 13 Annex 2

Eligibility for membership of a credit union G

1 Table: G

...

Persons too young to be members	
3.	A person too young to be a member (“juvenile depositor”) may make deposits with a <i>credit union</i> (section 9 of the Credit Unions Act 1979). A person too young to be a member (“juvenile depositor”) is a person who:
(1)	...
(2)	would qualify for membership (directly or indirectly) if he were old enough.
	<u>This means that in a qualification of residing in a particular locality, an eligible juvenile depositor should reside there (because indirect qualification means being a member of the same household as well as a relative of a DQM). In a qualification of being employed in a particular locality, a juvenile depositor is eligible by going to school or college there.</u>
Note:	These <i>deposits</i> are not shares and these depositors are not members.

...

Insert the following new provision after CRED 14.10.8G

14.10.8A G The form may be updated from time to time. *Credit unions* should use the form in force at the end of the financial the year on which they are reporting.

...

Insert the following new provision after CRED 14.10.12G

Controllers and close links

14.10.13 G (1) *Credit unions* are subject to the requirements of the *Act* and *SUP 11* on *controllers* and *close links*, and are bound to notify the *FSA* of changes. In practice, however, *credit unions* cannot develop such relationships, because:

(a) only individuals may be members of a *credit union* (section 5(1) of the Credit Unions Act 1979);

- (b) every member is entitled to vote and has one vote only (section 5(9) of the Credit Unions Act 1979);
- (c) the minimum number of members of a *credit union* is 21 (section 6(1) of the Credit Unions Act 1979) and its registration may be cancelled if membership falls below that number (section 16(1)(a)(i) of the Industrial and Provident Societies Act 1968 and section 20(1)(a) of the Credit Unions Act 1979);and
- (d) a *credit union* may not have a subsidiary (section 26 of the Credit Unions Act 1979).

(2) *Credit unions* are therefore exempted from the requirement to submit annual reports of *controllers* and *close links* (SUP 16.1.1R-16.1.3R, 16.4.1G(-1) and 16.5.1G(-1)).

...

## Appendix 2.1 Detailed contents of CRED

### 2.1.1 P Table

...

7	Investment and borrowing
	7.1 ...
	...
	7.3 Borrowing and Financial risk management
	7.3.3 <del>1</del> Borrowing
	...
7A	Shareholding
...	
	7A.3 <del>Deposits by persons too young to be members</del>
...	
13	Registration and Authorisation
	...
	13.2 Introduction
	<u>13.2A Use of name "credit union"</u>
	...
14	Supervision
	...
	14.10 Reporting requirements
	...
	14.10.12(G) Financial penalties for late submission of reports
	<u>14.10.13(R) Controllers and close links</u>



**DECISION MAKING MANUAL (EXTENSION OF SCOPE OF MEDIATION  
SCHEME) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power under section 157(1) (Guidance) of the Financial Services and Markets Act 2000 (“the Act”).

**Commencement**

- B. This instrument comes into force on 1 February 2004.

**Amendments to the Decision making manual and amendments to the Enforcement manual**

- C. The Decision making manual is amended in accordance with Annex A to this instrument.
- D. The Enforcement manual is amended in accordance with Annex B to this instrument.

**Citation**

- D. This instrument may be cited as the Decision Making Manual (Extension of scope of Mediation Scheme) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex A

### Amendments to the Decision making manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

DEC App 1 Settlement procedure and mediation scheme for FSA ~~disciplinary~~ enforcement cases

1.1 Introduction

1.1.1 G A *person* who is or may be subject to enforcement action may discuss the proposed action with *FSA* staff through settlement discussions. Settlement discussions may take place on an informal basis at any time during the enforcement process ~~after the *FSA* has given a warning notice.~~ Where *FSA* staff have recommended that disciplinary enforcement action be taken against a *person*, the mediation scheme will be available to those *persons* against whom action is proposed ~~after~~ where settlement discussions are, in the opinion of either party, unlikely to lead to an agreed settlement have broken down. This appendix sets out the procedure for settlement and the framework of the mediation scheme.

1.2 Settlement

1.2.1 G If a *person* who is or may be subject to enforcement action wishes to discuss the proposed action with *FSA* staff on an informal basis, he may do so at any time during the enforcement process ~~after the *FSA* has given the warning notice. The warning notice will contain details of the *person* to contact for these purposes. (There is no bar on discussions at an earlier stage, but they are likely to be less productive until the *FSA* has given the warning notice to the *person* concerned.)~~ The *FSA* and the *person* concerned should agree that discussions will take place on a "without prejudice" basis, and that neither party may subsequently rely on admissions or statements made in the context of the discussions, or documents recording the discussions.

...

1.2.3 G Having considered the terms of the proposed settlement, the *RDC* may ask to meet the relevant *FSA* staff or the *person* concerned in order to assist in its consideration of the proposed settlement. The *RDC* may:

- (1) accept the proposed settlement by issuing a , *decision notice*, second supervisory notice or (where appropriate) *notice of discontinuance* based on the terms of the settlement; or

...

### 1.3 Mediation

...

1.3.2 G As mediation will be on a "without prejudice" basis, admissions made by the parties in the course of the mediation and documents prepared for the purposes of the mediation may not be referred to in subsequent proceedings relating to the dispute if the mediation is unsuccessful. However, if the mediation results in a proposed settlement of the dispute which is approved by the *RDC*, the terms of the proposed settlement will form the basis of a *decision notice* and subsequent *final notice* or second *supervisory notice*, or (where appropriate) *notice of discontinuance* given by the *FSA*.

...

### 1.4 Scope and availability of the mediation scheme

1.4.1 G Mediation will not be available in enforcement cases where the *FSA* is contemplating bringing a criminal prosecution or cases involving disciplinary action for late submission of a report to which *ENF* 13.5 (Financial penalties for late submission of reports) applies. ~~involving disciplinary matters and market abuse subject to the exceptions set out in *DEC* App 1.4.2G.~~

1.4.2 G Mediation will be available in all other enforcement cases falling within the scope of the *RDC*. In those cases involving allegations of unfitness and impropriety based on judgements about dishonesty or lack of integrity and the exercise of the *FSA's* own initiative powers on a variation or cancellation of permission, mediation will be available subject to the *FSA's* consent. ~~not be available in:~~

- ~~(1) — cases involving allegations of a criminal offence or offences; or~~
- ~~(2) — cases involving allegations of unfitness or impropriety based on judgements about dishonesty or lack of integrity; or~~
- ~~(3) — cases involving the exercise of the *FSA's* own initiative powers on a variation of permission or~~
- ~~(4) — cases involving disciplinary action for late submission of a report as referred to in *ENF* 13.5.~~

1.4.3 G In a case falling within the scope of the scheme, In each appropriate enforcement case (see *DEC* App 1.4.1 and *DEC* App 1.4.2), the mediation scheme will be available to the person against whom a warning notice is issued. The mediation scheme will be available mediation will take place where an election to mediate is made after the *warning notice* has been issued and before the *FSA* issues a *final decision notice*  $\mp$  (the relevant *warning notice* will state the circumstances in which mediation is available for that matter under the terms of the scheme). Where an election to mediate is made before the issue of a *warning notice* or after the issue of a *decision notice*, mediation will be available subject to the *FSA's* consent.

- 1.4.4 G ~~The A person is not obliged to take part in a mediation in the course of the enforcement process submit his case for mediation.~~
- ...
- 1.6 Starting the mediation
- 1.6.1 G ~~The FSA will offer the mediation facility in all appropriate enforcement cases (see DEC App1.4.1G). If the person agrees to submit the a case is submitted to mediation, the parties will send a joint mediation notice in an agreed form to:~~
- ...
- Confidentiality
- ...
- 1.7.7 G ...
- 1.7.8 G (2) Under the mediation scheme, however, confidentiality will be limited in that:
- ...
- (b) the terms of any settlement reached will, if approved by the *RDC* be incorporated in a *decision notice* and subsequent *final notice* or second *supervisory notice*, or (where appropriate) a *notice of discontinuance* which may be made public;
- ...
- 1.10 Result of the mediation
- ...
- 1.10.2 G If no agreed proposal is reached, the mediation will be terminated and the case will return to the point it had reached in the enforcement process prior to the mediation ~~proceed to the *decision notice* or stage.~~
- 1.10.3 G If a settlement proposal is agreed, it will be considered by the *RDC*, which will decide whether to approve it. If it is approved, a *decision notice* and subsequently a *final notice*, or second *supervisory notice*, will be issued reflecting the terms of the agreement reached. If it is not approved, the parties may return to the mediation only with the *RDC's* consent. If the *RDC* does not consent, the case will return to the point it had reached in the enforcement process prior to the mediation ~~continue towards the *decision notice* stage.~~
- 1.10.4 G A person may elect to mediate only once during the course of the enforcement process.
- ...
- 1.12 Review of mediation procedure
- 1.12.1 G The use of mediation in the disciplinary context is a novel approach in the area of financial regulation, but reflects current trends in civil litigation. The

mediation provider will administer the mediation scheme and tThe *FSA* proposes to operate the mediation scheme on a pilot basis for one year and will monitor it and review its operation at the end of each year that period. The *FSA* proposes to publish core information relating to the operation of the scheme in the *FSA* 's Annual Report.

...

DEC 2 Annex 5G

...

The *FSA* operates a mediation scheme for certain *disciplinary and market abuse enforcement* cases, where settlement discussions have taken place but are, in the opinion of either party, unlikely to lead to an agreed settlement ~~broken down~~.

...

## **Annex B**

### **Amendments to the Enforcement manual**

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.3.1 G (3) the FSA will seek to ensure fair treatment when exercising its enforcement powers. For example, the FSA's decision making process for regulatory enforcement cases generally gives an opportunity for both written and oral representations to be made, and also provides a facility for mediation (where settlement discussions are unlikely to lead to an agreed settlement ~~break-down~~) in certain disciplinary cases.

**COMPLAINTS SOURCEBOOK (REMOVAL OF ANNUAL NOTICE FOR EXEMPTION) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in or under the Financial Services and Markets Act 2000 (the “Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule making powers listed above are specified for the purposes of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 February 2004.

**Amendments to the Dispute resolution: Complaints sourcebook**

- D. The Dispute resolution: Complaints sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Complaints Sourcebook (Removal of Annual Notice for Exemption) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex

### Amendments to the Dispute resolution: Complaints sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 1.1 Application and Purpose

...

#### Exemption

- 1.1.7 R (1) A *firm* which does not conduct business with *eligible complainants* and has no reasonable likelihood of doing so is exempt from *DISP* 1.2 - *DISP* 1.7, if:
- (a) it has notified~~notifies~~ the *FSA* in writing ~~of this fact and that notice remains current, that those conditions apply with effect from the date that notice is received by the *FSA*; and~~
  - (b) the conditions in fact continue to apply.
- (2) The exemption takes effect from the date on which the notice was received by the *FSA*.
- ~~(2)~~ (3) In (1), conducting business means carrying on any of the activities to which the rules in *DISP* 2.6 apply with or for *persons* who are *eligible complainants* under *DISP* 2.4.
- ...
- 1.1.8 R ~~[deleted]~~ A notice under *DISP* 1.1.7 R must be given:
- ~~(1) by 28 February 2002, in which case it will remain current until 31 March 2003; or~~
  - ~~(2) before, or as soon as practicable after, the time of the *firm's* authorisation by the *FSA*, in which case it will remain current until the end of the *financial year* in which it is given; or~~
  - ~~(3) as soon as practicable after the *firm* ceases to conduct business with *eligible complainants*, in which case it will remain current until the end of the *financial year* in which it is given; or~~
  - ~~(4) in February of each *financial year* (beginning with February 2003), in which case it will remain current until the end of the next *financial year*.~~
- 1.1.9 G ~~[deleted]~~ A notice under *DISP* 1.1.7 R will be renewable every 12 months.



## End of exemption

1.1.10 R A *firm* which is exempt under *DISP* 1.1.7 R must notify the *FSA* in writing as soon as reasonably practicable if the conditions in *DISP* 1.1.7 R no longer apply.

...

## Schedule 2 Notification Requirements

### 2 Table

Handbook reference	Matter to be Notified	Contents of notification	Trigger event	Time allowed
<i>DISP</i> 1.1.7R	<i>Firm</i> qualifies for exemption	Confirmation that a <i>firm</i> does not do business with <i>eligible complainants</i> and has no reasonable likelihood of doing so	If the <i>firm</i> wishes to take advantage of the exemption in <del><i>DISP</i> 1.1.7R</del> an annual renewal is required. See <del><i>DISP</i> 1.1.8R</del> for timing of notice <u>Conditions in <i>DISP</i> 1.1.7R apply</u>	N/A
<i>DISP</i> 1.1.10R	End of exemption	Confirmation that the conditions in <i>DISP</i> 1.1.7R no longer apply	Conditions in <i>DISP</i> 1.1.7R no longer apply	<del>Not specified</del> <u>As soon as reasonably practicable</u>

**COMPENSATION SOURCEBOOK (REMOVAL OF ANNUAL NOTICE FOR EXEMPTION) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in or under the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance);
  - (4) section 213 (The compensation scheme); and
  - (5) section 214 (General).
- B. The rule making powers listed above are specified for the purposes of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 February 2004.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Compensation Sourcebook (Removal of Annual Notice for Exemption) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex

### Amendments to the Compensation sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 13.3 Exemption

- 13.3.1 R (1) *A participant firm* which does not conduct business that could give rise to a *protected claim* by an *eligible claimant* and has no reasonable likelihood of doing so is exempt from a *specific costs levy*, or a *compensation costs levy*, or both, provided that :
- (a) it has notified~~notifies~~ the *FSCS* in writing of this fact ~~that those conditions apply~~; and
- (b) the conditions in fact continue to apply~~notice remains current~~.
- (2) The exemption takes effect from the date on which the notice was received by the *FSCS*, subject to *COMP 13.3.6R*.
- 13.3.2 R ~~[deleted] A notice under *COMP 13.3.1R* must be given:~~
- (1) ~~by 28 February 2002, in which case it will remain current until 31 March 2003; or~~
- (2) ~~as soon as practicable after the time of its authorisation by the *FSA*, in which case it will remain current until the end of the financial year of the *compensation scheme* in which it is given; or~~
- (3) ~~as soon as practicable after it ceases to conduct business that could give rise to a *protected claim* by an *eligible claimant*, in which case it will remain current until the end of the financial year of the *compensation scheme* in which it is given; or~~
- (4) ~~unless (1) applies, in February of each financial year of the *compensation scheme*, in which case the notice will remain current until the end of the next financial year.~~
- 13.3.3 G (1) ~~[deleted] A notice under *COMP 13.3.1R* will be renewable every 12 months.~~
- (2) ~~The financial year of the *compensation scheme* is the twelve months ending on 31 March.~~
- 13.3.4 R *A participant firm* which is exempt under *COMP 13.3.1R* must notify the *FSCS* in writing as soon as reasonably practicable if the conditions in *COMP 13.3.1R* no longer apply.

...

13.3.6 R If, ~~during the course of a financial year of the *compensation scheme*, a *participant firm* ceases to conduct business that could give rise to a *protected claim* by an *eligible claimant* and notifies the FSCS of this under *COMP 13.3.1R(1)13.3.2R(3)*, it will be treated as a *participant firm* to which *COMP 13.8.7R* applies until the end of the financial year of the *compensation scheme* in which the notice was given.~~

13.3.7 G The financial year of the *compensation scheme* is the twelve months ending on 31 March.

...

**Schedule 2  
Notification Requirements**

**2 Table**

<b>Handbook reference</b>	<b>Matter to be notified</b>	<b>Contents of notification</b>	<b>Trigger event</b>	<b>Time allowed</b>
...				
COMP 13.3.21R	Right to exemption for specific costs and compensation costs levy	Notice that firm does not conduct business that could give rise to a claim on the FSCS and has no reasonable likelihood of doing so	<del>In February each year or on the occasion of the firm's authorisation or when it ceases conducting</del> <u>If it does not, or if it ceases to, conduct business with persons eligible to claim on FSCS, unless it has already given such notice</u>	<del>As soon as practicable</del> <u>None specified though exemption generally only takes effect from the date of receipt of notice by FSCS</u>
COMP 13.3.4R	Loss of right to seek exemption from specific costs and compensation costs levy	Statement that firm no longer qualifies for exemption because it carries on business with persons eligible to claim on FSCS	Firm loses the right to claim the exemption	As soon as <u>reasonably</u> practicable

## THE PROFESSIONAL FIRMS (INSURANCE MEDIATION) INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance); and
  - (4) section 332(1) (Rules in relation to persons to whom the general prohibition does not apply).
- B. The provisions of the Act listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

### Commencement

- C. This instrument comes into force on 14 January 2005, except to the extent that a provision (other than in PROF 7.2) relates to a long-term care insurance contract or a regulated mortgage contract, in which case it comes into force on 31 October 2004.

### Amendments to the Professional firms sourcebook

- D. The Professional firms sourcebook is amended in accordance with the Annex to this instrument.

### Citation

- E. This instrument may be cited as the Professional Firms (Insurance Mediation) Instrument 2004.

By Order of the Board  
15 January 2004

## Annex

### Amendments to the Professional firms sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is inserted, the place where it goes is indicated and it is not underlined.

1.1.1 R This sourcebook applies as follows:

- (1) ...
- (2) ...
- (3) *PROF 6* applies to every *designated professional body* and to any *person* who requests the Treasury to make an order under section 326(1) of the Act (Designation of professional bodies); ~~and~~
- (4) *PROF 7* applies to every *designated professional body* and every *exempt professional firm* that is carrying on, or proposing to carry on, insurance mediation activity.

...

1.1.4 G This sourcebook outlines:

- (1) ...
- (2) ...
- (3) ...
- (4) ...
- (5) the implications for an *authorised professional firm* that carries on *non-mainstream regulated activities*; ~~and~~
- (6) the arrangements made by the *FSA* for complying with its obligations under the *IMD* in relation to:
  - (a) maintaining a record of *unauthorised persons*, including *exempt professional firms*, that carry on, or are proposing to carry on, insurance mediation activity; and
  - (b) *exempt professional firms* that wish to passport under the *IMD*.

...

1.1.6 G The *rules* and *guidance* in this sourcebook are intended to:

- (1) ...
- (2) promote public understanding of the *financial system* by ensuring that the *clients* of an *exempt professional firm* are made aware that the firm is not an *authorised person*; ~~and~~

- (3) enable the *FSA* to use its resources in an efficient and effective way in the collection of information relevant to its duty to keep itself informed under section 325 of the *Act* (Authority's general duty); and
- (4) explain the background to and the arrangements made by the *FSA* for:
- (a) the registration of *unauthorised persons*, including *exempt professional firms*, that carry on, or are proposing to carry on, *insurance mediation activity*; and
  - (b) *authorised professional firms* and *exempt professional firms* that wish to exercise their *EEA right* under the *IMD* to establish a *branch* or provide *cross border services* in another *EEA State*.

...

PROF 2 Ann 2

### Status of exempt professional firm G

- 1 Table: Non Exempt activities orders under section 327(6) of the Act (see *PROF* 2.1.9G)

As at ~~21 March 2002~~<sup>31 October 2004</sup>, the Treasury had made the following orders under section 327(6):

The Financial Services and Markets Act 2000 (Professions) (Non-Exempt Activities) Order 2001 (SI 2001/1227), as amended by: article 3 of the Financial Services and Markets Act 2000 (Miscellaneous Provisions) Order 2001 (SI 2001/3650); article 7 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) Order 2002 (SI 2002/682); article 3 of the Financial Services and Markets Act 2000 (Commencement of Mortgage Regulation) (Amendment) Order 2002 (SI 2002/1777); article 24 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No1) Order 2003 (SI 2003/1475), and article 16 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No2) Order 2003 (SI 2003/1476).

...

- 3.1.2 G The *FSA* keeps itself informed in a number of ways. A *designated professional body* has a duty under section 325(4) of the *Act* to cooperate with the *FSA*. Article 94 of the *Regulated Activities Order* requires each *designated professional body* to provide the *FSA* with the information it needs to maintain a public record of *persons* that are registered with the *FSA* to conduct *insurance mediation activity*. The *FSA* has made arrangements ~~envisages it will make arrangements~~

with each of the *designated professional bodies* about the information they provide to it, to include information about:

- (1) ...
- ...
- (4) supervisory activity; ~~and~~
- (5) the activities **carried on by exempt professional firms, the risks arising from them and how they are mitigated, for example by monitoring activity or training and competence arrangements;** ~~and~~  
and
- (6) the names and addresses of each of their exempt professional firms that carry on, or are proposing to carry on, insurance mediation activity, together with the details of the individuals within the management of the exempt professional firms who are responsible for the insurance mediation activity and, where relevant, the passporting information required by the FSA for the purposes of paragraph 25 of Schedule 3 to the Act (EEA Passport Rights).

...

- 3.2.1 G Section 328 of the *Act* (Directions in relation to the general prohibition) gives the *FSA* power to make a direction that the exemption under section 327 of the *Act* (see *PROF* 2.1.3 G) does not apply to the extent specified in the direction. Section 328 allows the *FSA* to make a direction in relation to different classes of *person* or different descriptions of *regulated activity*. Section 325(3) of the *Act* requires the *FSA* to keep under review the desirability of exercising its powers under Part XX of the *Act* (Provision of Financial Services by Members of the Professions), including its direction powers under section 328 of the *Act*.

...

- 3.2.5 G (1) The *FSA* may exercise its direction powers under section 328(6) of the *Act* in two situations, as set out in (2) and (3).
- (2) First, ~~the~~ *FSA* may exercise its direction power under section 328(6)(a) of the *Act* only if it is satisfied that it is desirable in order to protect the interests of *clients*. In considering whether it is satisfied, the *FSA* is required by section 328(7) of the *Act* to have regard, among other things, to the effectiveness of any arrangements made by a *designated professional body*:
- ~~(1)~~( a) for securing compliance with *rules* made under section 332(1) of the *Act* (see *PROF* 4.1.1 G);
  - ~~(2)~~( b) for dealing with complaints against its *members* in relation to the carrying on by them of *exempt regulated*



*activities* (see *PROF 4.1.4 G (2)(d)*);

in order to offer redress to *clients* who suffer, or claim

(3)(  
c) to have suffered, loss as a result of misconduct by its  
*members* in their carrying on of *exempt regulated activities* (see *PROF 4.1.4 G (2)(d)*); and

for cooperating with the *FSA* under section 325(4) of

(4)(  
d) the *Act* (see *PROF 3.1.2 G*).

(3) Second, the *FSA* may exercise its direction power under section 328(6)(b) of the *Act* if it is satisfied that it is necessary to do so in order to comply with an obligation imposed by the *IMD*. For example, the *FSA* might wish to do so if it was not receiving from a *designated professional body* the information it needs to maintain the *FSA Register* (see *PROF 7.1*).

3.2.6 G Section 330 of the *Act* (Consultation) sets out procedures which the *FSA* must follow if it wishes to make a direction under section 328(6)(a) or (b). Except as specifically provided in section 330:

...

3.2.7 G The directions the *FSA* has made under section 328(6)(a) are set out in *PROF 3 Ann 1G*. Directions made by the *FSA* under section 328(6)(b) of the *Act* are listed in *PROF 3 Ann 2 G* (The *FSA*'s duties and powers).

### **PROF 3 Ann 1 The *FSA*'s duties and powers G**

#### **PROF 1 Table: Directions made by the *FSA* under section 328(6)(a) of the *Act* (see *PROF 3.2.7G*)**

As at ~~21 June 2004~~ 31 October 2004, the *FSA* had made no directions under section 328 (6)(a) of the *Act*.

Insert the following new annex after *PROF 3 Annex 1G*

### **PROF 3 Ann 2 The *FSA*'s duties and powers G**

#### **PROF 1 Table: Directions made by the *FSA* under section 328(6)(b) of the *Act* (see *PROF 3.2.7G*)**

As at 31 October 2004, the *FSA* had made no directions under section 328(6)(b) of the *Act*.

...

4.1.1 G The effectiveness of arrangements made by a *designated professional body* for securing compliance with the *rules* in this chapter is one of the factors that the *FSA* must take into account in considering whether to exercise its powers to give a direction under section 328 of the *Act* (see *PROF* 3.2.5(2)G and (3)G).

...

4.1.3 R (1) An exempt professional firm must, before it provides a service which includes the carrying on of a regulated activity in the United Kingdom, other than an insurance mediation activity, with or for a client, disclose in writing to the client in a manner that is clear, fair and not misleading that it is not authorised under the Act.

(2) An exempt professional firm must, before it provides a service which includes the carrying on of an insurance mediation activity with or for a client, make the following statement in writing to the client in a way that is clear, fair and not misleading and no less prominent than any other information provided to the client at the same time:

“[This firm is]/[We are] not authorised by the Financial Services Authority. However, we are included on the register maintained by the Financial Services Authority so that we can carry on insurance mediation activity, which is broadly the advising on, selling and administration of insurance contracts. This part of our business, including arrangements for complaints or redress if something goes wrong, is regulated by [DPB]. The register can be accessed via the Financial Services Authority website at [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register).”

4.1.4 G (1) The *FSA* considers that material provided to satisfy *PROF* 4.1.3R(1) and (2) need not be tailored to the individual *client*. The disclosures in *PROF* 4.1.3 R(1) and (2) may be provided alongside or integrated with other material provided to a *client*. *Exempt professional firms* may therefore include the information within engagement letters or client care letters, if they wish.

(2) The *FSA* considers that it is important that *clients* understand the implications for them of receiving services from an *exempt professional firm* that is not authorised under the *Act*. It is also important that clients understand the implications of the difference between authorisation under the Act and being on the register maintained by the FSA, so that the exempt professional

firm can conduct insurance mediation activity, in relation to which activity the regulatory protections established by the Act for the benefit of consumers will not apply. The FSA therefore expects *designated professional bodies* to make rules covering the information to be provided to *clients*. These rules should require *exempt professional firms* to make a disclosure to *clients* containing the following elements:

- (a) where the exempt professional firm conducts a regulated activity other than an insurance mediation activity, a statement that the exempt professional firm is not an authorised person;
  - (b) the nature of the *regulated activities* carried on by the *exempt professional firm*, and the fact that they are limited in scope;
  - (c) a statement that the *exempt professional firm* is regulated for these *regulated activities* by the *exempt professional firm's designated professional body*, identifying the *designated professional body* concerned; ~~and~~
  - (d) the nature of the complaints and redress mechanisms available to *clients* in respect of these *regulated activities*; and
  - (e) where the regulated activity consists of insurance mediation activity, the statement contained at PROF 4.1.3 R (2).
- (3) *Exempt professional firms* should also ensure that any statement that makes reference to the FSA does not lead a *client* to suppose that the FSA has direct regulatory responsibility for the *exempt professional firm*. This could be a breach of PROF 4.1.2 R. This consideration is particularly important in relation to insurance mediation activity, where clients may well fail to appreciate the difference between authorisation under the Act and being included on the register maintained by the FSA so as to permit the exempt professional firm to carry on insurance mediation activity.

...

## 5.3 Reference to other sourcebooks and manuals

### Introduction

- 5.3.1 G The parts of the *Handbook* in which the provisions are disapplied or modified in relation to *authorised professional firms* when carrying on *non-mainstream regulated activities* include those described in PROF 5.3.1AG to PROF 5.3.79G.

...

### Insurance: Conduct of Business sourcebook

- 5.3.10 G (1) ICOB 1.2.10 R provides that ICOB does not apply to an authorised professional firm with respect to its non-mainstream regulated activities, except for:
- (a) ICOB 2.2 (Clear, fair and not misleading communication);
  - (b) ICOB 3 (Financial promotion);
  - (c) ICOB 4.2.2R in relation to the information for customers in table ICOB 4.2.8R items numbered (8), (9) and Note 4 covering complaints and compensation; and
  - (d) those sections in ICOB which implement articles 12 and 13 of the IMD, unless:
    - (i) the designated professional body of the firm has made rules which implement articles 12 and 13 of the IMD;
    - (ii) those rules have been approved by the FSA under section 332(5) of the Act; and
    - (iii) the firm is subject to the rules in the form in which they were approved.
- (2) ICOB 1.2.11 G (2) provides that the effect of ICOB 1.2.10R(4) is that if the relevant designated professional body of an authorised professional firm does not make rules implementing articles 12 and 13 of the IMD applicable to authorised professional firms those authorised professional firms will need to comply with those sections of ICOB which implement articles 12 and 13 of the IMD, namely ICOB 4.1 to 4.4 (but not 4.2.20G to 4.2.28G), and ICOB 4.8.

...

Insert the following new PROF Chapter 7

## **Professional firms**

### **Insurance mediation activity**

- 7.1 Register of persons carrying on *insurance mediation activity*  
Background
- 7.1.1 G The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No. 2) Order 2003 (SI 2003/1476) implements in part the provisions of the *IMD* and amends the *Regulated Activities Order*.  
The FSA's obligation to maintain a record
- 7.1.2 G Article 93 of the amended *Regulated Activities Order* requires the

*FSA* to maintain an up-to-date record of every *unauthorised person*, whether an *appointed representative* or an *exempt professional firm* that carries on, or is proposing to carry on, *insurance mediation activity* and to whom the *general prohibition* does not apply in relation to the carrying on of such an activity. In relation to *exempt professional firms* the *general prohibition* does not apply by virtue of section 327 of the *Act*.

- 7.1.3 G The *FSA* is not to include an *exempt professional firm* in the register relating to *unauthorised persons* if:
- (1) under a direction given by the *FSA* under section 328(1) of the *Act*, section 327(1) of the *Act* does not apply in relation to the carrying on by it of *insurance mediation activity*; or
  - (2) the *FSA* has made an order under section 329(2) of the *Act* disapplying section 327(1) of the *Act* in relation to the carrying on by the *exempt professional firm* of *insurance mediation activity*.

#### Provision of information to the *FSA*

- 7.1.4 G Article 94 of the *Regulated Activities Order* obliges a *designated professional body* to provide the *FSA* with the information it needs to maintain the record referred to in *PROF* 7.1.2G of every *unauthorised person* that carries on, or proposes to carry on, *insurance mediation activity* and keep it up to date. This information needs to include the details referred to in *PROF* 7.1.7 G. This is the responsibility of the *designated professional body* and not each *exempt professional firm*.

#### Financial Services and Markets Act 2000 (Professions) (Non-Exempt) Activities Order 2001 (SI 2001/1227)

- 7.1.5 G (1) The attention of *exempt professional firms* is drawn to the significance of The Financial Services and Markets Act 2000 (Professions) (Non-Exempt) Activities Order 2001 (SI 2001/1227), as amended by The Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No.2) Order 2003 (SI 2003/1476). The effect of these amendments is that *exempt professional firms* may not carry on certain *regulated activities* which relate to a *contract of insurance* in reliance on the *Part XX exemption* unless the *exempt professional firm* is included in the record of *unauthorised persons* carrying on *insurance mediation activity* maintained by the *FSA* under article 93 of the *Regulated Activities Order*.
- (2) Each *exempt professional firm* carrying on, or proposing to carry on, *insurance mediation activity* should ensure that at all material times the name of the firm and the requisite details are included in the record maintained by the *FSA*. Any such *exempt professional firm* carrying on, or proposing to carry on, *insurance mediation activity* whose name does not appear in the record maintained by the *FSA* is likely to be breaching the

*general prohibition* which is a criminal offence under section 23 of the *Act*.

#### FSA Register

7.1.6 G In order to comply with its obligations to maintain a record of *unauthorised persons* that carry on, or are proposing to carry on, *insurance mediation activity*, the *FSA* has established an appropriate record which forms part of the record maintained by the *FSA* under section 347 of the *Act*. The record maintained by the *FSA* under section 347 of the *Act* is known as the *FSA Register*. The *FSA Register* therefore contains a record of each *authorised* and *unauthorised person* that carries on, or proposes to carry on, *insurance mediation activity*.

7.1.7 G The information to be included on the record in relation to *exempt professional firms* will, as required by the *IMD*, include details of:

- (1) the name and address of each *exempt professional firm* that carries on, or is proposing to carry on, *insurance mediation activity*;
- (2) where the *exempt professional firm* is not an individual, the names of the individuals within the management of the *exempt professional firm* who are responsible for the *insurance mediation activity*; and
- (3) each *EEA State* in which the *exempt professional firm* under an *EEA right* derived from the *IMD*:
  - (a) has established a *branch*; or
  - (b) is providing *cross border services*.

#### FSA Website

7.1.8 G The *FSA Register* can be accessed through the *FSA* website under the link [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register).

## 7.2 Passporting under the Insurance Mediation Directive

7.2.1 G All *persons* that are on the register maintained by the *FSA* in accordance with article 3 of the *IMD*, and so permitted to conduct *insurance mediation activity*, are entitled to exercise the *EEA right* conferred upon them by article 6 of the *IMD* to establish a *branch* or provide services relating to *insurance mediation activity* in another *EEA State*. Both *authorised professional firms* and *exempt professional firms* that are so registered by the *FSA* get the benefit of these passporting rights.

7.2.2 G Any *authorised professional firm* or *exempt professional firm* that is contemplating the exercise of rights under article 6 of the *IMD* to establish a *branch* or provide services relating to *insurance mediation*

*activity* in another *EEA State* is referred to *SUP 13* (Exercise of passport rights by UK firms) for further details as to the applicable process. Note that both *authorised professional firms* and *exempt professional firms* are *UK firms* for the purposes of the *Handbook*, including *SUP 13*.

- 7.2.3 G A *UK firm* proposing to establish a *branch* in another *EEA State* for the first time under an *EEA right* derived from the *IMD* must first satisfy the conditions in paragraphs 19(2),(4) and (5) of Part III of Schedule 3 to the *Act* (EEA Passport Rights). These include the requirement that the firm must at the outset give the *FSA* a notice in the required form of its intention to establish the *branch*. *SUP 13.3.2 G* to *SUP 13.3.5 G* detail the procedure to be followed once such a notice of intention has been received by the *FSA*. *SUP 13.5.1 R* (Specified contents: notice of intention to establish a branch) and *SUP 13.6.9A G* (Firms passporting under the *IMD*) will also be relevant.
- 7.2.4 G A *UK firm* proposing to provide *cross border services* into another *EEA State* for the first time under an *EEA right* derived from the *IMD* must first satisfy the conditions in paragraph 20(1) of Part III of Schedule 3 to the *Act* (EEA Passport Rights). The *UK firm* must at the outset give the *FSA* a notice in the required form of its intention to provide the *cross border services* into another *EEA State*. In this instance, the relevant procedure to be followed is outlined in *SUP 13.4.2 G* to *SUP 13.4.5 G*. *SUP 13.5.2 R* (Specified contents: notice of intention to provide cross border services) and *SUP 13.7.11 G* will also be relevant.

**THE LISTING RULES (COMBINED CODE) (AMENDMENT) INSTRUMENT 2004**

**Powers Exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 74 (The official list); and
  - (2) section 96 (Obligations of issuers of listed securities).

**Commencement**

- B. This instrument comes into force on 1 March 2004

**Amendment of Listing Rules**

- C. The Listing Rules are amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Listing Rules (Combined Code) (Amendment) Instrument 2004

By Order of the Board  
15 January 2004



## Annex

### Amendments to Listing Rules

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### DEFINITION OF COMBINED CODE

Amend the definition of Combined Code in the Definitions as follows.

...

Combined Code

~~The principles of good governance and code of best practice prepared by the Committee on Corporate Governance, chaired by Sir Ronald Hampel, published in June 1998 and appended to, but not forming part of, the listing rules~~

The code of best practice, including the principles of good governance, which is in force in respect of the relevant annual reporting period. The Combined Code does not form part of the listing rules. The Combined Code is:

(a) (in respect of reporting periods commencing before 1 November 2003) the code and principles prepared by the Committee on Corporate Governance chaired by Sir Ronald Hampel and published in June 1998 (the 'Hampel Code'); and

(b) (in respect of reporting periods commencing on or after 1 November 2003) the 'Combined Code on Corporate Governance' published in July 2003 by the Financial Reporting Council (the '2003 FRC Code'), which is appended to the Listing Rules

...

## CHAPTER 21 INVESTMENT ENTITIES

Amend the application of the Combined Code in respect of Investment Companies as follows:

...

21.20

...

...

- (i) in the case of an investment company (including an investment trust) with no executive directors; in respect of the Combined Code:
  - (i) paragraph 12.43A(a) does not apply in respect of ~~Combined~~ the Hampel Code principles B.1 to B.3.;
  - (ii) paragraph 12.43A(b) does not apply in respect of ~~Combined~~ the Hampel Code provisions B.1.1 to B.1.10, B.2.1 to B.2.6 and B.3.1 to B.3.5; ~~and~~
  - (iii) paragraph 12.43A(c) does not apply; in respect of the Hampel Code and in respect of the 2003 FRC Code; and
  - (iv) paragraphs 12.43A(a) and (b) do not apply in respect of the 2003 FRC Code principles B.1 to B.2 and Code provisions B.1.1. to B.1.6 and B.2.1 to B.2.4 except insofar as they relate specifically to non-executive directors.

## CHAPTER 26 VENTURE CAPITAL TRUSTS

Amend the application of the Combined Code in respect of Venture Capital Trusts as follows:

...

26.9

...

...

- (d) in the case of a venture capital trust with no executive directors; in respect of the Combined Code:
  - (i) paragraph 12.43A(a) does not apply in respect of ~~Combined~~ the Hampel Code principles B.1 to B.3.;
  - (ii) paragraph 12.43A(b) does not apply in respect of ~~Combined~~ the Hampel Code provisions B.1.1 to B.1.10, B.2.1 to B.2.6 and B.3.1 to B.3.5; ~~and~~

(iii) paragraph 12.43A(c) does not apply; in respect of the Hampel Code and in respect of the 2003 FRC Code; and

(iv) paragraphs 12.43A(a) and (b) do not apply in respect of the 2003 FRC Code principles B.1 to B.2 and Code provisions B.1.1. to B.1.6 and B.2.1 to B.2.4 except insofar as they relate specifically to non-executive directors.

**THE MONEY LAUNDERING SOURCEBOOK  
(AMENDMENT NO 2) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 146 (Money laundering rules);
  - (3) section 149 (Evidential provisions);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purposes of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 March 2004.

**Amendments to the Money Laundering sourcebook**

- D. The Money Laundering sourcebook is amended in accordance with Annex A to this instrument.

**Miscellaneous amendments**

- E. SYSC, APER, CRED and the Glossary are amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Money Laundering Sourcebook (Amendment No 2) Instrument 2004.

By Order of the Board  
19 February 2004

## Annex A

### Amendments to the Money Laundering sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1.3 G The scope of this sourcebook is very wide. It includes all *firms* except those within the limited exception for *firms* concerned only with certain insurance activities and *UCITS qualifiers* (see *ML 1.1.2R*). In this respect, the chapter follows article 1 of the *Money Laundering Directive* (No 91/308/EEC as amended by No 2001/97/EEC). The scope extends to *incoming firms* (such as branches of institutions established elsewhere in the *EEA*), except those providing only *cross border services* in the *United Kingdom*. This is because the Directive is designed to apply on a “*Host State*” basis. *ML* does not apply with respect to the *unregulated activities* of a *firm*, for example *money service business*.

...

1.2.4 G This sourcebook relates to regulatory requirements, as opposed to requirements imposed by the criminal law. It is therefore, not relevant ~~regulatory or supervisory~~ guidance for the purposes of regulation 53(3) of the *Money Laundering Regulations* or section 330(8) of the *Proceeds of Crime Act 2002*.

1.2.5 G In assessing a *relevant firm’s* compliance with the requirements of this sourcebook, the *FSA* will have regard to the relevant provisions of the *Joint Money Laundering Steering Group’s Guidance Notes for the Financial Sector*.

...

3.1.3 R ...

(2A) If the *client*, or the *person* on whose behalf he is acting, engages in *money service business* and is registered with the Commissioners of the Customs and Excise, sufficient evidence of identity must include the registered number, within the meaning given by regulation 4(3) 9(2) of the *Money Laundering Regulations 2001*, of the *client* or the *person* on whose behalf he is acting.

...

3.1.4 G ~~In assessing a *relevant firm’s* compliance, with its duty to identify a *client* in accordance with *ML 3.1.3R*, the *FSA* will have regard to the *relevant firm’s* compliance with the *Joint Money Laundering Steering Group’s Guidance Notes for the Financial Sector* and with the *guidance* on financial exclusion in *ML 3.1.5G*. [deleted]~~

...

- 3.2.1 R (1) This section sets out circumstances in which:
- (a) the duty in *ML 3.1.3R(1)* (Identification of the client: the duty) need not be complied with; or
  - (b) ~~the relevant firm is entitled to regard the evidence it has as sufficient evidence.~~ the *relevant firm* is required to take reasonable steps to establish the identity of a *person* for whom the *client* is acting.

...

- 3.2.2 R The duty in *ML 3.1.3R(1)* (Identification of the client: the duty) does not apply if:

- (1) the *client* is also:
- (a) a credit institution or financial institution covered by the Money Laundering Directive; or
  - (b) an authorised professional firm; or
  - (c) is regulated by an overseas regulatory authority (see *ML 3.2.7R*) and is based or incorporated in a country (other than an *EEA State*) whose law contains comparable provisions to those contained in the *Money Laundering Directive*; or

...

- (3) with a view to carrying out a one-off *transaction*, the *client* (other than a *money service operator*) is introduced to the *relevant firm* by a *person* who has given the *relevant firm* a written assurance that in all such cases he obtains and records identification evidence, and:
- (a) the *person* who has given the written assurance is a credit institution or financial institution covered by the Money Laundering Directive, or an authorised professional firm, or an entity undertaking comparable activities in an *EEA State*; or
  - (b) ~~the person is subject to regulatory oversight exercised by a relevant overseas regulatory authority (see *ML 3.2.7R*), and to legislation at least equivalent to that required by the *Money Laundering Directive*~~ regulated by an overseas regulatory authority (see *ML 3.2.7R*) and is based or incorporated in a country (other than an *EEA State*) whose law contains comparable provisions to those contained in the *Money Laundering Directive*;  
or

...

...

~~When evidence of identity may be regarded as sufficient~~

- 3.2.4 R ~~A *relevant firm* may regard evidence as sufficient evidence for the purposes of *ML 3.1.3R* (Identification of the client: the duty) if it establishes that:~~
- ~~(1) — the relevant payment for the *transaction* was made or is to be made — from the *client's* account held at an institution which is:
    - ~~— (a) — a *relevant firm* with *permission* to accept *deposits*; or~~
    - ~~— (b) — an *incoming relevant firm* which is a *credit institution*; or~~
    - ~~— (c) — a *credit institution*;~~~~
  - ~~(2) — the payment has been or will be sent or confirmed by post or — electronically;~~
  - ~~(3) — it was or is reasonable for the payment to be sent or confirmed in that — way; and~~
  - ~~(4) — the payment is not made to open an account from which onward — payment may be made to someone other than the *client*. [deleted]~~

Where the client is acting for another person

- 3.2.5 R ~~A *relevant firm* may regard evidence as sufficient for the purposes of *ML 3.1.3 R* (Identification of the client: the duty) if it establishes that the *client* (other than a *money service operator*):~~
- ~~(1) — is bound by this sourcebook or by the *Money Laundering Regulations* or is otherwise covered by the *Money Laundering Directive*; or~~
  - ~~(2) — is acting on behalf of another *person*, and has given a written assurance that he has obtained and recorded evidence of the identity of the *person* on whose behalf he is acting, and is subject to regulatory oversight exercised by a relevant overseas regulatory authority (see *ML 3.2.7 R*) and to legislation at least equivalent to that required by *the Money Laundering Directive*. Where the *client* acts, or appears to act, other than in the circumstances covered by *ML 3.2.2R*(1) and (3) for another *person*, the *relevant firm* must take reasonable steps for the purpose of establishing the identity of that *person*.~~

- 3.2.6 G ~~A *relevant firm* is expected to take reasonable steps to determine whether or not the *client* falls within the exemption in *ML 3.2.5R*(2). [deleted]~~

...

- 4.1.1 G This section deals with the reporting to the *firm's MLRO* or a *person authorised by the Director General of NCIS* of knowledge or suspicions within the *relevant firm* about *money laundering*.

- 4.1.2 R (1) A *relevant firm* must take reasonable steps to ensure that any member of staff who handles, or is managerially responsible for handling, *transactions* which may involve *money laundering* makes a report promptly to the *MLRO* or a *person* authorised by the Director General of *NCIS*, within the same *firm* or group, if he:
- (a) knows or suspects; or
  - (b) has reasonable grounds to know or suspect;

that a *client*, or the *person* on whose behalf the *client* is acting, *person* is engaged in *money laundering*.

...

- 4.1.4 R (1) The duty in ML 4.1.2R (Internal reporting) does not apply where the *relevant firm* is a professional legal adviser and the knowledge or suspicion or the reasonable grounds for knowing or suspecting are based on information or other matter which came to it in privileged circumstances.
- (2) Information or other matter comes to a professional legal adviser in privileged circumstances if it is communicated or given to the adviser:
- (a) by (or by a representative of) its client in connection with the giving by the adviser of legal advice to the client; or
  - (b) by (or by a representative of) a *person* seeking legal advice from the adviser; or
  - (c) by a *person* in connection with legal proceedings or contemplated legal proceedings.
- (3) The privileged circumstances in (2) do not apply to information or other matter which is communicated or given with a view to furthering a criminal purpose or in contravention of a provision of the *regulatory system*.
- (4) "Professional legal adviser" includes any *person* in whose hands information or other matter may come in privileged circumstances.

...

- 4.3.2 R (1) A *relevant firm* must take reasonable steps to ensure that any report required by ML 4.1.2R(1) (Internal reporting), other than a report made to a *person* authorised by the Director General of *NCIS*, is considered by the *MLRO*, or his duly authorised delegate, and that if, having considered the report and any relevant *know your business information* to which he has sought access, the *MLRO* or his duly authorised delegate:



(1a) knows or suspects; or

(2b) has reasonable grounds to know or suspect;

that a *person* has been engaged in *money laundering*, he reports promptly to *NCIS*.

(2) In reporting to *NCIS*, an *MLRO*, or his duly authorised delegate, must have regard to any order under section 339 of the Proceeds of Crime Act 2002 prescribing the form and manner in which a disclosure must be made to *NCIS* and to any guidance issued by *NCIS* on the form and manner of reporting.

...

5.1.4 G In order to assist *relevant firms*, the Joint Money Laundering Steering Group (JMLSG) publishes government, government department, or *Financial Action Task Force* findings of the kind referred to in *ML 5.1.3R*. This information can be found on the JMLSG's website ([www.jmlsg.org.uk](http://www.jmlsg.org.uk)) or accessed indirectly via the *FSA*'s website ([www.fsa.gov.uk](http://www.fsa.gov.uk)) or, in the case of *Financial Action Task Force* findings only, via the *Financial Action Task Force's* website ([www.fatf-gafi.org](http://www.fatf-gafi.org)). ~~the *FSA* will, from time to time, publish any government, government department or *Financial Action Task Force* findings, of the kind referred to in *ML 5.1.3 R*, on the *FSA* website ([www.fsa.gov.uk](http://www.fsa.gov.uk)).~~ All *relevant firms* should check this information regularly to ensure that they keep up to date with current findings.

...

6.2.1 R A *relevant firm* must take reasonable steps to ensure that staff who handle, or are managerially responsible for the handling of, *transactions* which may involve *money laundering* are aware of:

...

(2) the identity and responsibilities of the *MLRO* or a *person* authorised by the Director General of *NCIS*;

...

(4) the potential effect, on the *relevant firm*, ~~on~~ its *employees* and its *clients*, of any breach of that law.

...

~~MLRO as "appropriate person"~~ "nominated officer" under Money Laundering Regulations

7.1.4 G If convenient, a *relevant firm* may decide that the same *person* can carry out the responsibilities of the *MLRO* and of the ~~"appropriate person"~~ "nominated officer" under the *Money Laundering Regulations*.

~~“Appropriate person” “Nominated officer”, under those Regulations, means a person appointed to handle the internal and external reporting required by the Regulations (see Regulation 14) has the meaning given by Regulation 7.~~

...

7.1.11 R A *relevant firm* must make its *MLRO* responsible for:

...

(3) making external reports to *NCIS* under ~~ML 4.2~~ 4.3 (External reporting);

...

...

7.2.1 G *SYSC 3.2.6R* (Compliance) requires a *relevant firm* to take reasonable care to establish and maintain appropriate systems and controls for compliance with its regulatory obligations and to counter the risk that it might be used to further *financial crime*. This section amplifies ~~this requirement, particular aspects of the rule in SYSC. It does not, however, limit the application of the rule, the effect of which is that, where financial crime is concerned, firms must also comply with other Handbook requirements (in particular, ML) and their legal obligations under the Money Laundering Regulations and the Proceeds of Crime Act 2002.~~

...

7.3.2 R (1) A *relevant firm* must make and retain, for the periods specified in (2), the following records:

...

(c) ~~when a relevant firm’s client has become insolvent, and it has taken steps to recover all or part of a debt owed to it by the client, a record of the grounds and those steps; [deleted]~~

...

(2) The specified periods are:

...

(b) in relation to *transactions* within (1)(b), five years from the date when the *transaction* was completed; and

(c) ~~in relation to (1)(c), five years from the date of the insolvency; and [deleted]~~

...

...

## Annex B

### Amendments to SYSC, APER, CRED and the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Senior management arrangements, Systems and Controls (SYSC)

- 3.2.7 G (3) The ~~FSA's~~ detailed requirements for systems and controls with respect to ~~money laundering~~ are set out in the ~~Money Laundering sourcebook (ML)~~. In applying SYSC 3.2.6R, where *financial crime* is concerned, *firms* must also comply with other *Handbook* requirements (in particular, *ML*) and their legal obligations under the *Money Laundering Regulations* and the *Proceeds of Crime Act 2002*.

#### Statements of Principle and Code of Practice for Approved Persons (APER)

- 4.7.9 E In the case of the *Money Laundering Reporting Officer*, failing to discharge the responsibilities imposed on him in accordance with chapter ~~8~~7 of the *Money Laundering sourcebook (ML)* falls within *APER* 4.7.2E.

#### Credit Unions sourcebook (CRED)

- 12.3.6 G *ML* 3.2 sets out a number of exceptions to the requirement upon *firms* to establish the identity of the *client*. These exceptions apply in principle to *credit unions*, ~~but the only one which is likely to be relevant to the *credit union* context is that described in *ML* 3.2.4R. That *rule* establishes that the identification requirements need not apply if the source of funding of a *transaction* is an account held by a *client* with a *firm* which itself is subject to the requirements laid down in *ML*. In the *credit union* context this, for example, would mean that funds arriving in a member's account which originated from an account held with a *bank* or *building society* need not be subject to the *customer* identification requirements set out in *ML* 3.1.3R. However, none of these exceptions applies if the *firm* has reasonable cause to know or suspects that the *client* is engaged in *money laundering*.~~

...

- 12.4.1 G *Firms* should take reasonable steps to ensure that, when any report of *money laundering* is suspected, a report is swiftly made to the *MLRO* reported to the *MLRO* is swiftly consulted. Having ~~consulted~~ considered the information available, if the *MLRO* suspects a *person* has been engaged in *money laundering*, he should report promptly to the National Criminal Intelligence Service (*NCIS*).

...

- 12.5.1 G *ML* 5.1.2R requires *relevant firms* to take reasonable steps to ensure that they obtain and make proper use of any government or *Financial Action*

*Task Force* findings. In order to assist *relevant firms*, the Joint Money Laundering Steering Group (JMLSG) publishes government, government department or *Financial Action Task Force* findings, of the kind referred to in *ML 5.1.3R*. This information can be found on the JMLSG's website ([www.jmlsg.org.uk](http://www.jmlsg.org.uk)) or accessed indirectly via the *FSA*'s website ([www.fsa.gov.uk](http://www.fsa.gov.uk)) or, in the case of *Financial Action Task Force* findings only, via the *Financial Action Task Force's* website ([www.fatf-gafi.org](http://www.fatf-gafi.org)). All *relevant firms* should check this information regularly to ensure that they keep up to date with current findings. This information will be published on the *FSA* website. *Firms* are required to access this information.

## Glossary of definitions

Amend the following definitions as shown

*money laundering*

~~an offence which involves the concealment, acquisition or use of criminal property or facilitating its concealment, acquisition or use, as defined for the time being in:~~

~~a) section 327 (Concealing etc), 328 (Arrangements) or 329 (Acquisition, use and possession) of the Proceeds of Crime Act 2002;~~

~~b) section 18 (Money laundering) of the Terrorism Act 2000.~~

any act which:

a) constitutes an offence under section 18 (Money laundering) of the Terrorism Act 2000; or

b) constitutes an offence under section 327 (Concealing etc), section 328 (Arrangements) or section 329 (Acquisition, use and possession) of the Proceeds of Crime Act 2002; or

c) constitutes an attempt, conspiracy or incitement to commit an offence specified in paragraph (b); or

d) constitutes aiding, abetting, counselling or procuring the commission of an offence specified in paragraph (b); or

e) would constitute an offence specified in paragraph (b), (c) or (d) if done in the *United Kingdom*.

*Money Laundering Directive* the Council Directive of 10 June 1991 on the prevention of the use of the financial system for the purpose of money laundering (91/308/EEC) as amended by the Council Directive of 4 December 2001 (2001/97/EEC).

*Money Laundering Regulations* the Money Laundering Regulations ~~1993 (SI 1993/1933)~~ 2003 (SI 2003/3075)  
(See *ML*).

*Money Laundering Regulations 2001* ~~the Money Laundering Regulations 2001 (SI 2001/3641)~~ [deleted]

## **WITH-PROFITS GOVERNANCE (POSTPONEMENT) INSTRUMENT 2004**

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions of the Financial Services and Markets Act 2000 (the 'Act'):
- (1) section 59 (Approval);
  - (2) section 138 (General rule-making power);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

### **Commencement**

- C. This instrument comes into force immediately.

### **Amendments to the With-Profits Governance Instrument 2003**

- D. Paragraph C of the With-Profits Governance Instrument 2003 is amended to replace "31 March 2004" with "30 April 2004".

### **Citation**

- E. This instrument may be cited as the With-Profits Governance (Postponement) Instrument 2004.

By order of the Board  
19 February 2004

**WITH-PROFITS GOVERNANCE (AMENDMENT) (POSTPONEMENT)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions of the Financial Services and Markets Act 2000 (the 'Act'):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force immediately.

**Amendments to the With-Profits Governance (Amendment) Instrument 2003**

- D. Paragraph C of the With-Profits Governance (Amendment) Instrument 2003 is amended to replace "31 March 2004" with "30 April 2004".

**Citation**

- E. This instrument may be cited as the With-Profits Governance (Amendment) (Postponement) Instrument 2004.

By order of the Board  
19 February 2004

**MORTGAGES: CONDUCT OF BUSINESS  
SOURCEBOOK (AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in or under the Financial Services and Markets Act 2000 (the “Act”):
- (1) section 138 (General rule-making power);
  - (2) section 145 (Financial promotion rules);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 31 October 2004.

**Amendments to the Mortgages: Conduct of Business sourcebook**

- D. MCOB is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Mortgages: Conduct of Business Sourcebook (Amendment) Instrument 2004.

By order of the Board  
19 February 2004



## Annex

### Amendments to MCOB

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### MCOB Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1	Every <i>rule</i> in <i>MCOB</i> unless the context otherwise requires and subject to any more specific transitional provision relating to the matter.	R	If the application of any provision in <i>MCOB</i> is dependent on the occurrence of a series of events, some of which occur before, and some of which occur <u>on or</u> after, 31 October 2004, the provision applies with respect to the events that occur <u>on or</u> after 31 October 2004.	From 31 October 2004 for six months.	31 October 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
2		G	<p>(1) For example, if a <i>customer</i> submits an application for a <i>regulated mortgage contract</i> before 31 October 2004, a <i>firm</i> responding to that application <u>on or after</u> 31 October 2004 will not be required to provide the <i>customer</i> with an <i>illustration</i> in accordance with <i>MCOB 5</i>. However, the <i>firm</i> will have to comply with the requirements in <i>MCOB</i> when taking any further action (such as issuing an offer) regarding the application <u>on or after</u> 31 October 2004.</p> <p>(2) An <i>offer document</i> may have to be issued under transitional provision 1R even though no <i>illustration</i> has been given out (because that part of the transaction occurred before 31 October 2004). In such cases the suitably adapted <i>illustration</i> required by <i>MCOB 6.4.4R</i> would need to omit:</p> <p>(a) the required text in <i>MCOB 6.4.4R</i>(<del>5</del> 4)(b); and</p> <p>...</p>		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
3		G	<p><i>MCOB</i> applies to <i>regulated mortgage contracts</i> entered into on or after 31 October 2004. Variations made <u>on or after</u> that date to mortgage contracts entered into before that date are not subject to <i>FSA regulation</i> but may be subject to the Consumer Credit Act 1974. ...</p>		
4	<i>MCOB</i> 2.2.6R	R	<p>(1) A <i>firm</i> must disclose to a <i>customer</i> :</p> <p>...</p> <p>(c) details concerning complaints and redress for services provided before 31 October 2004 and those provided <u>on or after</u> 31 October 2004.</p> <p>(2) Unless already given to the <i>customer</i> before 31 October 2004, the information required in (1) must be communicated in a <i>durable medium</i> at the time of the first contact between the <i>firm</i> and the <i>customer</i> <u>on or after</u> 31 October 2004.</p>	From 31 October 2004 for six months.	31 October 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
5	MCOB 2.2.6R		At 31 October 2004, there will be cases where a <i>firm</i> has issued documentation which satisfies the requirements of the Consumer Credit Act 1974, but where no CCA agreement has been concluded. A <i>customer</i> may even have signed a CCA agreement, which has not been executed before the onset of mortgage regulation. In such cases, a <i>firm</i> must take care to avoid giving the impression that any agreement reached <u>on or</u> after 31 October 2004 will be subject to the Consumer Credit Act 1974, ...		
6	MCOB 3.6	R	<p>(1) Providing it does not state or imply that protections under the Consumer Credit Act 1974 apply, a <i>non-real time qualifying credit promotion</i> communicated:</p> <p>(a) in a directory (or similar publication) that is updated annually;</p> <p>(b) otherwise than in (a);</p> <p><u>on or</u> after 31 October 2004 that was first communicated before that date will be in compliance with the rules in MCOB 3.6 if it satisfies the advertising requirements under the Consumer Credit Act 1974.</p> <p>...</p>	<p>(1)(a) From 31 October 2004 for one year;</p> <p>(1)(b) From 31 October 2004 for three months.</p>	31 October 2004

...

1.6.1 G *MCOB* applies to *regulated mortgage contracts* entered into on or after 31 October 2004. ...

...

## Annex 1 G

...

### 2 Table

The exclusions listed in this table are only a summary of the exclusions in the *Regulated Activities Order*. This summary is not a complete explanation of the exclusions and should not be relied on as if it were.

Type of firm	Regulated activity	Description of activity	Summary of exclusions
...			
<i>mortgage administrator</i>	<i>administering a regulated mortgage contract</i> where that contract is entered into <u>on or after</u> 31 October 2004 (article 61(2) ( <i>Regulated mortgage contracts</i> )).	...	...
<i>mortgage adviser</i>	<i>advising on regulated mortgage contracts</i> (article 53A ( <i>Advising on regulated mortgage contracts</i> )).	Giving <i>advice</i> to a <i>person</i> in his capacity as borrower or potential borrower on the merits of doing any of the following:  ...  (2) varying the terms of a <i>regulated mortgage contract</i> entered into <u>on or after</u> 31 October 2004 in such a way as to vary the borrower's obligations under the contract (see <i>AUTH</i> App 4.6 ( <i>Advising on regulated mortgage contracts</i> )).	...
...			

...

...

2 Table

Chapter	Who does the chapter apply to?
...	
MCOB 5 (Pre-application disclosure)	<p>The whole chapter applies to a <i>mortgage lender</i>; <i>mortgage administrator</i>; <i>mortgage adviser</i> and <i>mortgage arranger</i>, when it:</p> <p>(1) makes a <i>personal recommendation</i> about a particular <del>mortgage</del> <u>regulated mortgage contract</u> to a <i>customer</i>; or</p> <p>...</p>

...

Annex 4G

...

2 This table belongs to MCOB 1.4.1G

[Note: Handbook modules marked with an asterisk will be amended to take account of the introduction of mortgage regulation. The relevant amendments will take effect on 31 October 2004].

	Module	Application
...		
Business Standards	<p>Interim Prudential Sourcebooks,</p> <p>...</p> <p><del>[PRU 9.2]</del></p> <p><u>PRU 9.2 (Professional indemnity insurance requirements for insurance and mortgage mediation activities)</u></p> <p><del>[PRU 9.3]</del></p> <p><u>PRU 9.3 (Capital resources for insurance and mortgage mediation activity and mortgage lending and administration)</u></p>	<ul style="list-style-type: none"> <li>• [Applies to <u>every mortgage adviser</u> and <i>mortgage arranger</i> <del>where they are also a firm carrying on insurance mediation activities.</del>]</li> <li>▪ [Applies to <u>every mortgage adviser</u>, <i>mortgage administrator</i>, <i>mortgage arranger</i> and <i>mortgage lender</i> <del>where they are also a firm carrying on insurance mediation activities.</del>]</li> </ul>

	<p><del>PRU 9.4</del></p> <p><u>PRU 9.4 (Insurance undertakings and mortgage lenders using insurance or mortgage mediation services)</u></p>	<ul style="list-style-type: none"> <li>▪ <del>{Applies to every mortgage lender which uses, or proposes to use, the services of another person consisting of insurance mediation, or insurance mediation activity mortgage adviser and mortgage arranger where they are also a firm carrying on insurance mediation activities.}</del></li> </ul>
--	--	---

...

3.6.9 R A non-real time qualifying credit promotion must:

- (1) ...; ~~and~~
- (2) ...; and
- (3) not contain the 'key facts' logo unless it is required by a rule.

...

4.1.4 R (1) MCOB 4.4 (Initial disclosure requirements) applies only in relation to varying the terms of a *regulated mortgage contract* entered into by the *customer* in any of the following ways:

...

- (c) switching all or part of the *regulated mortgage contract* from one ~~type of~~ interest rate to another.

...

...

4.1.8 G The FSA would not view the removal of a party to the regulated mortgage contract following the death of that party (and where no other variation is proposed) as a variation for the purposes of MCOB 4.1.4R(1).

...

4.4.7 R (1) If the initial contact of a kind in MCOB 4.4.1R(1) is by telephone, then unless MCOB 4.4.1R(2)(a) applies, the following information must be given before proceeding further:

...

- (c) if the scope of the service is ~~not based on the whole market~~ MCOB 4.3.1R(1)(b), that the *customer* can request a copy of the list of *mortgage lenders* whose *regulated mortgage contracts* it offers ...

...

...

4.8.1 R (1) If a firm arranges a regulated mortgage contract or a variation to an existing regulated mortgage contract without giving a personal recommendation, it must ensure that all the questions it asks the customer about the customer's needs and circumstances are scripted in advance.

(2) In the remainder of MCOB 4.8, a reference to a firm providing information to a customer in relation to a regulated mortgage contract is to be read as including a reference to providing information in relation to varying the terms of an existing regulated mortgage contract if the context so requires.

...

Annex 1 R: Initial disclosure document (“IDD”)

...

**key facts**

**about our mortgage services** [Note 2]

**XYZ FINANCIAL SERVICES**  
[Note 3] [Note 4]

[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

---

1. ...

---

2. **Whose mortgages do we offer?** [Note 6] [Note 7]

---

- We offer mortgages from the whole market.
- We [can] [Note 8] only offer mortgages from a limited number of lenders. Ask us for a list of the lenders we offer mortgages from. [Note 9]
- We [can] [Note 8] only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender].[Note 10]  
[or]  
[Name of lender] [can] We only offer ~~its~~ our own mortgages.[Note 11]
- 

3. ...

---

4. **What will you have to pay us for this service?** [Note 6]

---

- No fee [we will be paid by commission from the lender]. [Note 12]
- A fee [of £[ ] payable at the outset and £[ ] payable when you apply for a mortgage. [We will also be paid commission from the [lender].] [Note 12] [Note 13]



You will receive a key facts illustration when considering a particular mortgage which will tell you about any fees relating to ~~a particular mortgage it~~.

---

5. ...

---

**6. Who regulates us? [Note 18]**

---

[XYZ Financial Services] [123 Any Street, Some Town ST21 7QB] [Note 19] ~~[Note 5]~~ [Note 19A] is authorised [Note 20] and regulated by the Financial Services Authority. Our FSA ~~Register~~ number is [ ].

Our permitted business is [ ]. [Note 21]

[or] [note 19B]

[Name of *appointed representative*] [Notes 3 and 4] is an appointed representative of [name of *firm*] [~~123 Any Street, Some Town ST21 7QB~~ address of *firm*] [Note 19] ~~[Note 5]~~ [Note 19A] which is authorised and regulated by the Financial Services Authority. [Name of *firm*]'s FSA ~~registration~~ Register number is [ ].

Our [Name of *firm's*] permitted business is [~~advising on and arranging mortgages.~~] [Note 21]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register/](http://www.fsa.gov.uk/register/) or by contacting the FSA on 0845 606 1234.

---

7. ...

---

...

**Note 12** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer*, it must insert a plain language explanation of this (see specimen for a plain language example).

**Note 13** – insert a plain language description of when any *fees* are payable. This description could include, for example, a cash amount, a percentage of the loan amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If the *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a fee, the text for the second box should be abbreviated to 'A fee'.

...

**Note 18** – these sections may be omitted in accordance with *MCOB* 4.4.1R(3). If this section is omitted, the other sections of the IDD must be renumbered accordingly.

...

**Note 19A** – if the *firm's* address on the *FSA Register* differs from that given on the IDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5, it should be repeated in this section.

**Note 19B** – where the information is provided by an appointed representative, the appointed representative must use this text instead.

...

...

5.4.3 R A *mortgage intermediary* must take reasonable steps to ensure that an *illustration* which it issues, or which is to be issued on its behalf, other than that provided by a *mortgage lender*:

(1) is accurate within the following tolerances:

(a) no more than one percent or £1, whichever is the greater, below the actual figures charged by the *mortgage lender* for the following:

...

(iv) the amount by which the regular instalment (or the total amount payable for loans without a term or a regular repayment plan) would increase following a one percentage point increase in interest rates in Section 7 ~~of the illustration~~;

...

(2) except in the case of conveyancing fees and insurance premiums (where estimates may be used), is ~~absolutely~~ accurate in respect of other figures quoted in the *illustration* including fees payable to the *mortgage lender* or *mortgage intermediary* in Section 8 of the *illustration* and cash examples of *early repayment charges*, calculated in accordance with the rules in MCOB 5.6.84R to MCOB 5.6.88R, in Section 10 ~~of the illustration~~.

...

5.6.18 R ...

(3) If the amount on which the *illustration* is based includes the amount that the *customer* wants to borrow plus insurance premiums (other than a *higher lending charge* or where the premium is repaid over a term of 12 months or less and no interest is charged on the premium) that have been added to the loan:

...

...

5.6.34 R The following text must be included after the text required by MCOB 5.6.31R or MCOB 5.6.32R with the relevant cost measures shown in the right-hand column of Section 5 in accordance with the layout shown in MCOB 5 Ann 1R:

...

(2) "This means you pay back £ [insert the *total amount payable* divided by the amount on which the *illustration* is based from *MCOB 5.6.6R(2)* plus all fees, charges and insurance premiums added to the loan in accordance with *MCOB 5.6.18R(2)* and *MCOB 5.6.18R(3)*] for every £1 borrowed"; and

...

5.6.35 R ...

(3) ~~Where all the interest rolls up and is repaid as a lump sum at the end of the *regulated mortgage contract*, as, for example, in the case of a secured bridging loan, the *APR* and *total amount payable* must be based on the total amount that the *customer* would owe at the end of the term. [deleted]~~

...

...

5.6.59 R Under the section heading 'Are you comfortable with the risks?':

...

(2) paragraphs (1)(g) and (1)(h) do not apply where:

(a) the interest rate is fixed throughout the term of the *regulated mortgage contract*; ~~and~~ or

(b) ...

...

5.6.65 R The following text must be included at the end of Section 7 'Are you comfortable with the risks?':

"The FSA's ~~guide~~ information sheet 'You can afford your mortgage now, but what if ...?' will help you consider the risks. ...

...

5.6.66 R Under the section heading 'What fees must you pay?' the *illustration* must:

(1) itemise all the fees that are included in the calculation of the *APR* in accordance with *MCOB 10* (Annual Percentage Rate), excluding any charges for ~~any compulsory mortgage payment protection~~ insurance set out in Section 9 in accordance with *MCOB 5.6.73R*; and

...

...

5.6.77 R The following information must be included under the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to

take out through [insert the name of the *mortgage lender*, or where relevant the name of the *mortgage intermediary*, or both]’:

...

- (3) if no insurance policies are required (other than that which is a *tied product*), the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to take out through [insert name(s) of *mortgage lender* and, where relevant the *mortgage intermediary*]' must be retained in the *illustration* ...

5.6.78 G Under the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to take out through [insert name of *mortgage lender* or where relevant the name of the *mortgage intermediary*, or both]', the *illustration* should not ...

...

5.6.93 R ...

- (3) If a *firm* provides a *customer* with supplementary information about any additional features or facilities over and above the information required under MCOB 5.6.92R to MCOB 5.6.112G, the *firm* may include a reference to that supplementary information in Section 12.

...

5.6.103 R Where any of the additional features under MCOB 5.6.99R to MCOB 5.6.102R inclusive apply, then the following must also be stated if the amount of additional borrowing that would be available to the *customer* is stated in the *illustration*:

...

- (4) (where there is a regular payment plan) the payments on this total debt based on the frequency of payments in MCOB 5.6.40R and the current interest rate(s) ~~that would apply~~ applying on the date the *illustration* is issued;

...

5.6.104 R Where more than one additional borrowing facility from MCOB 5.6.99R to MCOB 5.6.102R applies, ~~MCOB 5.6.103R(3) and (4) must each be based on the total debt and total payments due under~~ of all these linked borrowing facilities and must be included under a separate sub-section titled 'Total additional borrowing'.

...

5.6.106 R (1) Where additional features are included in accordance with MCOB 5.6.92R and these are credit facilities that do not meet the definition of a *regulated mortgage contract*, the relevant parts of Section 12 of the *illustration* must include the following text:

"This additional feature is not regulated by the ~~Financial Services Authority~~ FSA".

...

...

5.6.117 R The amount payable in *MCOB* 5.6.113R(1) or *MCOB* 5.6.114R must include, but is not limited to:

...

5.6.118 G *MCOB* 2.3.7R requires any material inducements provided by a *mortgage lender, whether directly or indirectly, to a mortgage intermediary* or third party ~~connected to the mortgage intermediary (unless the payment only reflects the cost of outsourcing work relating to the processing of mortgage applications by a firm unconnected to the mortgage intermediary), by a mortgage lender, whether directly or indirectly,~~ to be quantified in cash terms,

...

...

5.6.129 R If the *regulated mortgage contract* is a *shared appreciation mortgage*, *MCOB* 5.6 applies to the *illustration* with the following amendments:

...

(2) Section 5 'Overall cost of this mortgage' of the *illustration* must contain the following text at the end of the section:

"The APR and the total amount you must pay do not take account of the share that [insert name of *mortgage lender*] takes in any increase in the value of your property as described in Section 3 ~~4~~. ...

...

...

5.6.140 R Under the section heading 'Are you comfortable with the risks?':

...

(2) paragraph (1)(e) does not apply:

(a) where the interest rate is fixed throughout the term of the *regulated mortgage contract*; ~~and~~ or

...

...

...

5.6.145 R The following text must be included at the end of Section 7 'Are you comfortable with the risks?':

"The FSA's ~~guide~~ information sheet 'You can afford your mortgage now, but what if ...?' will help you consider the risks. ...

...

5.7.2 R A *business illustration* provided to a *customer* must:

...

- (2) include the content required by *MCOB* 5.6.3R to *MCOB* 5.6.103R (except *MCOB* 5.6.5R, *MCOB* 5.6.101R, *MCOB* 5.6.109R – to *MCOB* 5.6.112G, ~~and~~ *MCOB* 5.6.120R and *MCOB* 5.6.121R);

...

...

6.1.3 R This chapter applies with respect to an offer made by a *firm* to a *customer* with a view to the *firm*:

...

- (2) varying the terms of a *regulated mortgage contract* entered into by the *customer* in any of the following ways:

...

- (c) switching all or part of the *regulated mortgage contract* from one ~~type of~~ interest rate to another;

...

...

6.4.4 R The *illustration* provided as part of the *offer document* in accordance with *MCOB* 6.4.1R(1) must meet the requirements of *MCOB* 5.6 (Content of illustrations) with the following modifications:

...

- (8) the fees recorded in the *illustration* that is part of the *offer document* in accordance with *MCOB* 5.6.66R(1) must include any fees ~~that have been~~ paid or payable by the *customer*;

...

...

7.4.1 R (Subject to *MCOB* 7.7.5R) A *firm* that enters into a *regulated mortgage contract* with a *customer* must provide the *customer* with the following information...

...

7.5.3 R The statement required by *MCOB* 7.5.1R must contain the following:

...

- (4) information at the date the statement is issued on:

...

- (e) the cost of redeeming the *regulated mortgage contract* (this must be shown as the sum of *MCOB 7.5.3R(4)(a)* and *MCOB 7.5.3R(4)(d)* plus any linked borrowing that cannot be retained (including the outstanding balances) plus any other charges that can be quantified at the date the statement is issued); if additional charges are payable that cannot be quantified at the point that the statement is issued (for example if the *customer* is in *arrears*) a warning must be included to that effect (~~see *MCOB 7.5.7R* regarding what is included in the cost of redeeming the *regulated mortgage contract*~~); and

...

- 7.5.7 R ~~The cost of redeeming a *regulated mortgage contract* referred to in *MCOB 7.5.3R(4)(e)* includes the full amount owed by the *customer* that must be repaid on surrendering the mortgage. This means that the balances of any *linked borrowing* that cannot be retained after the mortgage has been redeemed must be included in the calculation of the cost of redeeming the *regulated mortgage contract*. [deleted]~~

...

- 7.6.18 R Before a *customer* submits an application to a *firm* to change all or part of a *regulated mortgage contract* from one ~~type of~~ interest rate to another ...

...

- 7.6.22 R (1) ~~Except where (2) applies,~~ Before a *customer* submits an application to add or remove a party to a *regulated mortgage contract*, a *firm* must provide any *customer* who will remain or become a party to the contract with an *illustration* for the whole loan that complies with the requirements of *MCOB 5* (Pre-application disclosure).

- (2) ~~A *firm* is not required to provide the *illustration* required by (1) where the removal of a party to a *regulated mortgage contract* is the result of the death of that party, and no other party is to be added to the *regulated mortgage contract*.~~

- 7.6.23 G The *FSA* would not view:

(1) a simple notification of the death of a party to the *regulated mortgage contract* as an application for the purposes of *MCOB 7.6.22R*; or

(2) a guarantor as a party to a *regulated mortgage contract*;

so *MCOB 7.6.22R(1)* does not mean that someone becoming a surviving joint borrower on or a guarantor to the *regulated mortgage contract* should receive an *illustration*.

...

- 7.6.28 R If a *customer* requests, or agrees to, a change ...

...

- (5) where the *regulated mortgage contract* will change to an *interest-only mortgage*, a prominent reminder that the *customer* should have in place arrangements to repay the capital, using the following text:

'You will still owe [insert amount borrowed or, where part of the *regulated mortgage contract* is an *interest-only mortgage*, insert the amount borrowed under the *interest-only mortgage*] at the end of the mortgage term. You will need to make separate arrangements to repay this. When comparing the new payments on this mortgage with your ~~existing mortgage~~ previous payments, remember to add any money you may need to pay into a separate savings plan to build up a lump sum to repay the amount you have borrowed.'; and

...

...

Simultaneous request for a ~~product~~ rate switch and addition or removal of a party to a contract

- 7.6.33 G Where a *customer* simultaneously requests a ~~product~~ rate switch and the addition or removal of a party to the loan, ...

...

## 7.7 Business loans

### Further advances

- 7.7.1 R ...

...

### Arrangements to repay capital

- 7.7.4 R ...

### Disclosure

- 7.7.5 R *MCOB 7.4 (Disclosure at the start of the contract) does not apply in relation to a regulated mortgage contract that is for a business purpose.*

...

- 8.1.4 R (1) *MCOB 4.4 (Initial disclosure requirements) (as modified by MCOB 8) applies only in relation to varying the terms of a regulated lifetime mortgage contract entered into by the customer in any of the following ways:*

...

- (c) switching all or part of the *regulated lifetime mortgage contract* from one ~~type of~~ interest rate to another.

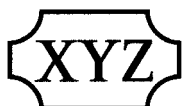


...  
Annex 1R Initial disclosure document (“IDD”)  
...

**keyfacts**

## about our lifetime mortgage [and home reversion scheme] services

[Note 2] [Note 3]



Financial Services

[Note 6]

123 Any Street

Some Town

ST21 7QB

[Note 4] [Note 5]

---

1. ...

---

2. **Whose products do we offer?** [Note 7] [Note 8]

- We offer products from the whole market.
- We [can] [Note 9] only offer products from a limited number of companies. Ask us for a list of the companies we offer products from. [Note 10]
- We [can] [Note 9] only offer [a limited range of the] [a] product[s] from [a single company] [name of single company]. [Note 11] [or] [~~Name of firm~~] [~~can~~] We only offer its our own products.[Note 12]

---

3. ...

---

4. **What will you have to pay us for this service?** [Note 7]

- No fee [we will be paid by commission from the company]. [Note 13]
- A fee of £[ ] [payable at the outset and £[ ] payable when you apply for a lifetime mortgage [or home reversion scheme]].[We will also be paid commission from the company.][Note 14]

You will receive a key facts illustration when considering a particular lifetime mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. [Note 3]

---

5. ...

---

6. **Who regulates us?** [Note 19]

[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 20] ~~[Note 6]~~ [Note 20A] is authorised [Note 21] and regulated by the Financial Services Authority. Our FSA ~~Register~~ number is [ ].

Our permitted business is [ ]. [Note 21]

[OR] [Note 20B]

[Name of *appointed representative*] [Notes 4 and 5] is an appointed representative of [name of *firm*] [~~123 Any Street, Some Town, ST21 7QB~~ address of *firm*] [Note 20] ~~[Note 6]~~ which is authorised and regulated by the Financial Services Authority. [~~Name of *firm*~~]’s FSA ~~Register~~ number is [ ].

~~Our~~ [Name of *firm*’s] permitted business is [~~advising on and arranging mortgages~~] [Note 22]

~~[Home reversion schemes are not regulated by the FSA] [Note 3]~~

You can check this on the FSA’s Register by visiting the FSA’s website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

~~[Home reversion schemes are not regulated by the FSA] [Note 3]~~

---

7. ...

...

**Note 13** – if the *firm* receives commission instead of, or in addition to, fees from the *customer*, it must insert a plain language explanation of this (see specimen for a plain language example).

**Note 14** – insert a plain language description of when any fees are payable. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If the *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

...

**Note 19** – these sections may be omitted in accordance with *MCOB* 4.4.1R(3). If this section is omitted, the other sections of the IDD must be renumbered accordingly.

...

**Note 20A** – if the *firm*’s address on the *FSA Register* differs from that given on the IDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5, it should be repeated in this section.

**Note 20B** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead.

...

...

9.3.6 R A *mortgage intermediary* must take reasonable steps to ensure that an *illustration* which it issues, or which is issued on its behalf, other than that provided by a *mortgage lender*:

...

- (2) except in the case of conveyancing fees and insurance premiums (where estimates may be used) is ~~absolutely~~ accurate in respect of other figures quoted in the *illustration*, including fees payable to the *mortgage lender* or *mortgage intermediary* in Section 11 ~~of the *illustration*~~ and cash examples of *early repayment charges*, calculated in accordance with the rules at MCOB 9.4.83R to MCOB 9.4.88R, in Section 13 ~~of the *illustration*~~.

...

9.4.21 R ...

- (4) If the amount on which the *illustration* is based includes the amount that the *customer* wants to borrow plus insurance premiums (other than a *higher lending charge* or where the premium is repaid over a term of 12 months or less and no interest is charged on the premium) that have been added to the loan or amount to be drawn down;

...

...

9.4.37 R The heading of the column on the right-hand side of ~~for~~ Section 8 of the *illustration* must state the frequency with which payments must be made by the *customer*. (For example, if payments are to be made on a monthly basis, the heading for this section must be 'What you will ~~need to pay each month owe and when~~' and the column must be headed 'Monthly payments'.

...

9.4.51 R The table showing the projection in the section headed 'Projection of roll-up of interest' should show annual details in columns under the following headings:

...

- (4) 'Interest charged at [insert percentage(s)] per year': this must be the interest charge for the year in question, calculated on the balance at the start of the year plus the amount drawn down ~~during the year~~ (if applicable) and any fees added to the loan during the year. The percentage(s) used must be as follows:

...

...

9.4.65 R Under the section heading 'What fees must you pay?' the *illustration* must:

- (1) itemise all the fees that are included in the calculation of the *APR* in accordance with *MCOB 10* (Annual Percentage Rate), excluding any

charges for ~~any compulsory mortgage payment protection~~ insurance set out in Section 12 in accordance with MCOB 9.4.72R; and

...

...

9.4.76 R The following information must be included under the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to take out through [insert name of *mortgage lender* or where relevant the name of the *mortgage intermediary*, or both]':

...

(3) if no insurance policies are required (other than that which is a *tied product*), the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to take out through [insert name(s) of *mortgage lender* and, where relevant the *mortgage intermediary*] must be retained in the *illustration* ...

9.4.77 G Under the sub-heading 'Insurance you must take out as a condition of this mortgage but that you do not have to take out through [insert name of *mortgage lender* or where relevant the name of the *mortgage intermediary* or both]', the *illustration* should not ...

...

9.4.92 R ...

(3) If a *firm* provides a *customer* with supplementary information about any additional features or facilities over and above the information required under MCOB 9.4.91R to MCOB 9.4.110R, the *firm* may include a reference to that supplementary information in Section 14.

...

9.4.103 R Where any of the additional features under MCOB 9.4.99R to MCOB 9.4.102R inclusive apply, then the following must also be stated if the amount of additional borrowing that would be available to the *customer* is stated in the *illustration*:

...

(4) the payments on this total debt based on the frequency of payments in MCOB 9.4.37R (if payments are required) and the current interest rate(s) ~~that would apply~~ applying on the date the *illustration* is issued;

...

9.4.104 R Where more than one additional borrowing facility from MCOB 9.4.99R to MCOB 9.4.102R applies, ~~MCOB 9.4.103R(3) and (4) must each be based on the total debt and total payments due (if payments are required) under~~ of all these *linked borrowing* facilities and must be included under a separate sub-section titled 'Total additional borrowing'.

...

9.4.106 R (1) Where additional features are included in accordance with *MCOB* 9.4.91R and these are credit facilities that do not meet the definition of a *regulated mortgage contract*, the relevant parts of Section 14 of the *illustration* must include the following text:

"This additional feature is not regulated by the ~~Financial Services Authority~~ FSA".

...

...

9.4.123 R The amount payable in *MCOB* 9.4.119R(1) or *MCOB* 9.4.120R must include, but is not limited to:

...

9.4.124 G *MCOB* 2.3.7R requires any material inducements provided by a mortgage lender, whether directly or indirectly, to a mortgage intermediary or third party connected to the mortgage intermediary (unless the payment only reflects the cost of outsourcing work relating to the processing of mortgage applications by a firm unconnected to the mortgage intermediary), by a mortgage lender, whether directly or indirectly, to be quantified in cash terms,

...

...

9.5.4 R The *illustration* provided as part of the *offer document* in accordance with *MCOB* 6.4.1R(1) must meet the requirements of *MCOB* 9.4, with the following modifications:

...

(7) the fees recorded in the *illustration* that is part of the *offer document* in accordance with *MCOB* 9.4.65R(1) must include any fees ~~that have been paid or payable~~ by the customer;

...

...

9.6.2 R Table of modified cross-references to other rules:

This table belongs to *MCOB* 9.6.1R.

Subject	Rule or guidance	Reference in rule or guidance	To be read as a reference to:
...			
Frequency of statements	<i>MCOB</i> 7.5.6G	<i>MCOB</i> 7.5.3R(2)	<i>MCOB</i> 9.8.1R(2)
Cost of redeeming	<del><i>MCOB</i> 7.5.7R</del>	<del><i>MCOB</i> 7.5.3R(4)(e)</del>	<del><i>MCOB</i> 9.8.1R(4)(d)</del>
...			

Addition or removal of party to contract	<i>MCOB</i> 7.6.22R <del>(4)</del>		
...			

...

9.8.1 R The statement required by *MCOB* 7.5.1R must contain the following:

...  
 (4) information at the date the statement is issued on:

...

(d) the cost of redeeming the *regulated lifetime mortgage contract* at the date that the statement is issued (this must be shown as the sum of *MCOB* 9.8.1R(4)(a) and *MCOB* 9.8.1R(4)(c) plus any linked borrowing that cannot be retained (including the outstanding balances) plus any other charges that can be quantified at the date the statement is issued). If additional charges are payable that cannot be quantified at the point that the statement is issued (for example if the *customer* is in *arrears*) a warning must be included to that effect (see *MCOB* 7.5.7R regarding what is included in the cost of redeeming the *regulated lifetime mortgage contract*); and

...

...

Notification where additional borrowing taken up

9.8.4 G ...

...

10.3.1 R ~~(4)~~—The *APR* must be calculated so that, subject to ~~(4)~~ *MCOB* 10.3.1AR(3), the *annual percentage rate* of charge is the rate for *i* which satisfies the equation set out in ~~(2)~~ *MCOB* 10.3.1AR, expressed as a percentage.

~~(2)~~

10.3.1A R Table

This table belongs to *MCOB* 10.3.1R

The equation referred to in ~~(4)~~ *MCOB* 10.3.1R is:

$$\sum_{K=1}^{K=m} \frac{A_K}{(1+i)^{t_K}} = \sum_{K'=1}^{K'=m'} \frac{A'_{K'}}{(1+i)^{t_{K'}}$$

where  
 K is the number identifying a particular advance of credit;  
 K' is the number identifying a particular instalment;  
 AK is the amount of advance K;  
 A'K' is the amount of instalment K';  
 Σ represents the sum of all the terms indicated;  
 m is the number of advances of credit;  
 m' is the total number of instalments;  
 tK is the interval, expressed in years, between the *relevant date* and the date of the second advance and those of any subsequent advances numbered three to m; and  
 tK' is the interval, expressed in years, between the *relevant date* and the dates of instalments numbered one to m'.

10.3.1B R (31) In ~~(2)~~ MCOB 10.3.1AR, references to instalments are references to...

(42) Where more than one rate is given under ~~(1)~~ MCOB 10.3.1R, the *APR* is the positive rate nearest to zero ...

...

10.3.3 R ...

(2) For the purposes of this chapter:

...

...

Annex 1 G

...

Substantively Identical Provisions	
MCOB 10	Total Charge for Credit Regulations
10.3.1R <u>and</u> 10.3.1AR	Regulation 7
10.3.3R	Regulation 2
...	

...

12.4.1 R (1) A *firm* must ensure that any *regulated mortgage contract* that it *enters into* does not impose, and cannot be used to impose, a charge for *arrears* on a *customer* except where that charge is a reasonable estimate of the cost of the ~~as a result of the individual rules above,~~ additional administration required as a result of the *customer* being in *arrears*.

**MORTGAGES: CONDUCT OF BUSINESS SOURCEBOOK  
(CONSEQUENTIAL AMENDMENTS TO THE HANDBOOK) (NO 2)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Mortgages: Conduct of Business sourcebook.
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) of the Financial Services and Markets Act 2000 (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 31 October 2004.

**Amendments to the Handbook**

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2):

(1)	(2)
GEN	Annex A
AUTH	Annex B
Glossary	Annex C

**Citation**

- E. This instrument may be cited as the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) (No 2) Instrument 2004.

By order of the Board  
19 February 2004



## Annex A

### Amendments to GEN

In this Annex, underlining indicates new text and striking through indicates deleted text. Text made but not yet in force is shown in square brackets.<sup>1</sup>

#### Transitional provisions

...

GEN

3 Table: (2) Transitional provisions applying to GEN only

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
[3]	[GEN 4.3.1R]	G	<p>[(1) ...</p> <p>(2) <del>Until 1 August 2005, a <u>A firm</u> may continue to use stationery and similar materials which refer to its membership of self-regulatory schemes superseded by FSA regulation. However, a <i>firm</i> will need to ensure that any such reference is adequately qualified so that the <i>customer</i> is not misled as to the regulatory arrangements in place.]</del></p>	[From 31 October 2004 until 15 July 2005]	[Apply in relation to <i>regulated mortgage activities</i> from 31 October 2004]

<sup>1</sup> See the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003.

...

4.2.2G There are other pre-contract information requirements outside this chapter, including:

...

[(5) for *regulated mortgage contracts*, in *MCOB 4.4* (Initial disclosure requirements), *MCOB 5.6* (Content of illustrations) and *MCOB 6.4* (Content of the offer document)-]; and

(6) for *regulated lifetime mortgage contracts*, in *MCOB 8.4* (Initial disclosure requirements), *MCOB 9.4* (Content of illustrations) and *MCOB 9.5* (Disclosure at the offer stage for lifetime mortgages).

## Annex B

### Amendments to AUTH

In this Annex, underlining indicates new text and striking through indicates deleted text. All the text being amended in this Annex is made but not yet in force.<sup>2</sup>

Appendix 4 to the Authorisation manual

- 4.4.13 G The effect of the *Regulated Activities Order* is that mortgage contracts which are varied can fall into one of the following categories:
- (1) a contract that was entered into before 31 October 2004, and that is subsequently varied on or after that date so that it satisfies the conditions set out in *AUTH* App 4.4.1G(1) to (3), will not be a *regulated mortgage contract* (because it was not a *regulated mortgage contract* at the time it was entered into);
  - (2) a contract that was originally entered into before 31 October 2004, but is subsequently changed on or after that date such that a new contract is entered into, will be a *regulated mortgage contract* (provided, of course, that it meets the definition in the *Regulated Activities Order*); and
  - (3) a *regulated mortgage contract* that was originally entered into on or after 31 October 2004, and which is subsequently varied by, for example, making a further advance, will remain a *regulated mortgage contract*.
- 4.4.14 G It is possible for more than one mortgage contract to be secured by the same (first) charge. The first contract might be entered into before 31 October 2004 (and therefore not be a *regulated mortgage contract*) and a second contract entered into on or after 31 October 2004 (and be a *regulated mortgage contract*).
- ...
- 4.5.1 G Article 25A of the *Regulated Activities Order* describes two types of *regulated activities* concerned with *arranging regulated mortgage contracts*. These are:
- (1) making arrangements for another *person* to:
    - (a) enter into a *regulated mortgage contract* as borrower; or
    - (b) vary the terms of a *regulated mortgage contract* entered into by him as borrower on or after 31 October 2004 in such a way as to vary his obligations under the contract; and
- ...

---

<sup>2</sup> See the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003.

- 4.5.18 G In addition to the exclusion in article 33A, introducers may be able to take advantage of the exclusion in article 33 of the *Regulated Activities Order* (Introducing). This excludes arrangements where:
- ...
- (3) the introduction is made with a view to the provision of independent advice or the independent exercise of discretion in relation to *investments* generally or in relation to any class of *investments* (including mortgages) to which the arrangements relate. ~~Other exclusions~~

Other exclusions

- 4.5.19 G ...

...

- 4.8.2 G The definition does not include administration of a *regulated mortgage contract* which was not entered into by way of business. ... See, however, *AUTH* App 4.4.4G and *AUTH* App 4.4.13G for a discussion of how a variation of a mortgage contract entered into before 31 October 2004 could amount to the entry into a new *regulated mortgage contract* on or after 31 October 2004.

...

- 4.11.5 G For the purposes of *regulated mortgage activities*, sections 418(2), (4), (5), (5A) and (6) are relevant, as follows:
- (1) Section 418(2) refers to a case where a *UK-based person* carries on a *regulated activity* in another *EEA State* in the exercise of rights under a *Single Market Directive*. The only *Single Market Directive* which is relevant to mortgages is the *Banking Consolidation Directive*. ~~In the FSA's view, the regulated mortgage activities of entering into or administering a regulated mortgage contract or agreeing to carry on either of those activities may be carried on by a credit institution using the passport under that directive.~~

...

...

- 4.12.5 G Where a *person* is already an *appointed representative* (in relation to any non-mortgage activities) and he proposes to carry on, with effect from 31 October 2004, any *regulated mortgage activities*, he will need to consider the following matters.
- (1) He must become *authorised* if his proposed mortgage activities include either *entering into a regulated mortgage contract* or *administering a regulated mortgage contract*. ... He will therefore need to apply for a *permission* to cover all the *regulated activities* that he proposes to carry on on or after 31 October 2004.

...

## Annex C

### Amendments to the Glossary

Amend the following definitions as shown (underlining indicates new text, striking through indicates deleted text). All the text in this Annex is made but not yet in force.<sup>3</sup>

<i>administering a regulated lifetime mortgage contract</i>	the <i>regulated activity</i> , specified in article 61(2) of the <i>Regulated Activities Order</i> , which is in summary: administering a <i>regulated mortgage contract</i> (which is a <i>lifetime mortgage</i> ) where the contract was entered into <u>on or</u> after 31 October 2004.
<i>administering a regulated mortgage contract</i>	the <i>regulated activity</i> , specified in article 61(2) of the <i>Regulated Activities Order</i> , which is in summary: administering a <i>regulated mortgage contract</i> where the contract was entered into <u>on or</u> after 31 October 2004.
<i>advising on regulated mortgage contracts</i>	the <i>regulated activity</i> , specified in article 53A of the <i>Regulated Activities Order</i> , which is in summary: advising a <i>person</i> if the advice: <ul style="list-style-type: none"><li>(a) is given to the <i>person</i> in his capacity as a borrower or potential borrower; and</li><li>(b) is advice on the merits of his:<ul style="list-style-type: none"><li>(i) entering into a particular <i>regulated mortgage contract</i>; or</li><li>(ii) varying the terms of a <i>regulated mortgage contract</i> entered into by him <u>on or</u> after 31 October 2004 in such a way as to vary his obligations under that contract.</li></ul></li></ul>
<i>arranging qualifying credit</i>	the <i>controlled activity</i> , specified in paragraph 10A of Schedule 1 to the <i>Financial Promotion Order</i> , of making arrangements: <ul style="list-style-type: none"><li>(a) for another <i>person</i> to enter as borrower into an agreement for the provision of <i>qualifying credit</i>; or</li><li>(b) for a borrower under a <i>regulated mortgage contract</i>, entered into <u>on or</u> after 31 October 2004, to vary the terms of that contract.</li></ul>
<i>arranging (bringing about) regulated mortgage contracts</i>	the <i>regulated activity</i> , specified in article 25A(1) of the <i>Regulated Activities Order</i> , which is in summary: making arrangements for another <i>person</i> to:

---

<sup>3</sup> See the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003.

- (a) enter into a *regulated mortgage contract* as borrower; or
- (b) vary the terms of a *regulated mortgage contract* entered into by him as borrower on or after 31 October 2004.

(see also *arranging* (in relation to *regulated mortgage contracts*) and *making arrangements with a view to regulated mortgage contracts*.)

*entering into a regulated mortgage contract*

the *regulated activity*, specified in article 621(1) of the *Regulated Activities Order*, which is in summary: entering into a *regulated mortgage contract* as lender.

**DECISION MAKING MANUAL (EXTENSION OF SCOPE OF MEDIATION  
SCHEME) (AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power under section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 March 2004.

**Amendments to the Decision making manual**

- C. The Decision making manual is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Decision Making Manual (Extension of Scope of Mediation Scheme) (Amendment) Instrument 2004.

By order of the Board  
19 February 2004

## Annex

### Amendments to the Decision making manual

In this Annex, striking through indicates deleted text.

#### 1.12 Review of mediation procedure

- 1.12.1 G ~~The use of mediation in the disciplinary context is a novel approach in the area of financial regulation, but reflects current trends in civil litigation.~~ The mediation provider will administer the mediation scheme and ~~t~~The *FSA* proposes to operate the ~~mediation scheme on a pilot basis for one year and will monitor it and review its operation at the end of each year that period.~~ The *FSA* proposes to publish core information relating to the operation of the scheme in the *FSA*'s Annual Report.



**CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT NO 16)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Conduct of Business sourcebook.
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) of the Financial Services and Markets Act 2000 (Rule-making instruments).

**Commencement**

- C. This instrument comes into force as follows:
  - (1) Annex A comes into force on 1 April 2004;
  - (2) Annex B comes into force on 1 May 2004.

**Amendments to the Conduct of Business sourcebook (COB)**

- D. COB is amended in accordance with Annexes A and B to this instrument.

**Citation**

- E. This instrument may be cited as the Conduct of Business Sourcebook (Amendment No 16) Instrument 2004.

By order of the Board  
18 March 2004

Amended by Addendum  
19 October 2004

## Annex A

### Amendments to the Conduct of Business sourcebook coming into force on 1 April 2004

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Table COB TR 1

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies: The COB provisions in Table COB TR 2 with the labels indicated		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1.0	Extra time provisions				
1.1	<i>ETPI</i>	R	Transitional Relief (2) ...  (g) ... and stakeholder pensions);  <u>(h) (from 1 April 2004) COB 6.1.1A R (Application of COB 6.2.26R);</u>  <u>(i) (from 1 April 2004) COB 6.2.26R (Requirement to offer a simplified prospectus for section 264 schemes); and</u>  <u>(j) (from 1 April 2004 for a mini cash ISA for the tax year 2004/2005 and later tax years) COB 6.5.42R (14) (Information requirements for cash deposit ISAs, friendly society tax-exempt policies, traded life policies and broker funds).</u>		
...					

...

COB TR5 Miscellaneous Transitional Rules applying to all firms

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
12	...				
13	<u>COB 6.2.26R</u>	<u>R</u>	<p><b><u>Simplified prospectus requirements for section 264 schemes</u></b>  <u>A firm may comply with COB 6.2.22R (Schemes) instead of COB 6.2.26R (Requirement to offer a simplified prospectus for section 264 schemes), if the EEA State in which the recognised scheme is established has not implemented the obligations of the UCITS Directive in relation to the simplified prospectus, until the earlier of:</u></p> <p><u>(1) the date that the relevant obligations of the UCITS Directive have been implemented in that EEA State; and</u></p> <p><u>(2) 30 September 2004 or, if later, the date when the relevant provisions of the UCITS Directive have been implemented in the UK.</u></p>	<u>From 1 April 2004 until 30 September 2004, or, if later, the date when the relevant provisions of the UCITS Directive have been implemented in the UK</u>	<u>1 April 2004</u>

...

6.1.1 R ...

Application of COB 6.2.26R

6.1.1A R COB 6.2.26R applies to a *firm* when it sells, *personally recommends* or arranges for the sale of a *UCITS scheme* which is a *recognised scheme* under section 264 of the *Act* (Schemes constituted in other EEA States) to a *client*.

...

...

6.2.24 R ...

Exception from the requirement to provide key features for section 264 schemes

6.2.24A R When a *firm* sells, *personally recommends* or arranges for the sale of a *UCITS scheme* which is a *recognised scheme* under section 264 of the *Act* (Schemes constituted in other EEA States), then *COB 6.2.22R* does not apply.

6.2.25 R ...

...

Requirement to offer a simplified prospectus for section 264 schemes

6.2.26 R (1) When a *firm* sells, *personally recommends* or arranges for the sale of a *UCITS scheme* which is a *recognised scheme* under section 264 of the *Act* (Schemes constituted in other EEA States) to a *client*, it must offer the *client* free of charge a copy of the *scheme's* most recent simplified prospectus before an application for the *scheme holding* is completed.

(2) The simplified prospectus must meet the requirements of the *UCITS Directive* necessary for the *scheme* to enjoy the rights conferred by the *Directive*.

(3) When the *scheme holding* is purchased on behalf of a *client* by an *investment manager* exercising discretion, the requirement in (1) will be satisfied by the *investment manager* being offered the simplified prospectus free of charge before the application form for a *scheme holding* is completed.

(4) A *firm* must not carry on any of the activities referred to in (1) in relation to a *UCITS scheme* which is a *recognised scheme* under section 264 of the *Act* unless it is satisfied on reasonable grounds that:

(a) a copy of the *scheme's* simplified prospectus has been filed with the *FSA* before any *units* in the *scheme* are marketed in the *UK*; and

(b) the information contained in the simplified prospectus is up to date and is not in need of revision;

and that any subsequent amendments thereto have been filed with the *FSA*.

...

...

6.5.42 R If COB 6.4.13R (1) applies, for a *cash deposit ISA*, the *private customer* must be given the following minimum information (in accordance with COB 6.4.13R) in place of *key features*:

.....

(14) a warning that a *mini-* and *maxi-ISA* may not be opened in the same tax year and that, by opening a mini cash *ISA*, the *customer* will be limiting the amount of ~~tax-free savings~~ savings investment in equities that he can make through ISAs, if he does not already have a mini stocks and shares or insurance *ISA* (not applicable for a TESSA-only *ISA*).

...

## Annex B

### Amendments to the Conduct of Business sourcebook coming into force on 1 May 2004

In this Annex, underlining indicates new text and striking through indicates deleted text.

Other regulations and guidelines

- 3.5.3 G *A firm communicating a financial promotion* may also be subject to other regulations and guidelines, outside the remit of the *FSA*, such as:
- (1) the codes adopted or issued from time to time by the Advertising Standards Authority, ~~the Independent Television commission and the Radio Authority~~ and Office of Communications (OFCOM);
  - ...
  - ...
  - (4) the ~~Telecommunications (Data Protection and Privacy) Regulations 1999 (SI 1999/2093)~~ Privacy and Electronic Communications (EC Directive) Regulations (SI 2003/2426).

...

- 6.5.14 G ~~A~~ The description which a *firm* is required to provide under 6.5.13R(2) might include information on the following under 'risk factors', when relevant- matters set out in the following non-exhaustive list:
- (1) ...
  - ...
  - (17) guarantees or other actual or potential liabilities, and their effect or potential effect, whether they are attributable to:
    - (a) the contractual terms and benefits of the *packaged product* which the *private customer* is or may be acquiring; or
    - (b) the contractual terms and benefits of any of the *product provider's* other products; or
    - (c) the business activities of the *product provider* or its *associates*;
- if they have or may have a material adverse effect on the returns to the *private customer* or are otherwise material to his decision to invest.

## ADDENDUM

### CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT NO 16) INSTRUMENT 2004

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex A of this instrument is amended as follows:

...

Application of COB 6.2.26R

- 6.1.12A R COB 6.2.26R applies to a *firm* when it sells, *personally recommends* or arranges for the sale of a *UCITS scheme* which is a recognised scheme under section 264 of the *Act* (Schemes constituted in other EEA States) to a *client*.

...

**CONFLICTS OF INTEREST (INVESTMENT RESEARCH)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 July 2004.

**Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Conflicts of Interest (Investment Research) Instrument 2004.

By order of the Board  
18 March 2004



## Annex A

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined. Text in square brackets is made but not yet in force<sup>1</sup>.

1.6.4 R ...

COB	Subject
...	
7.13	...
<u>7.16</u>	<u>Investment research</u>
...	

...

[2.2.4A G An offer or agreement to publish *investment research* which is, or to change a *published recommendation* so that it becomes, favourable to its subject (even if the subject is a *customer* of the *firm*), is an example of offering or accepting an inducement which is likely to conflict to a material extent with the *firm's* duties to its other *customers*. (See also *COB 5.10* in relation to inducements related to *corporate finance*] and *COB 7.16* in relation to *investment research*[.]

...

[5.10.2 G ... It also supplements other provisions in the *Handbook* (see, in particular, *COB 2.2* (Inducements and soft commission)], [~~and *COB 7.1* (Conflict of interest and material interest)~~] and *COB 7.16* (*Investment research*)[].]

...

[7.13.6A G For the purposes of *COB 7.13.6 R* (2), the *FSA* considers that an *investment analyst* is likely to be involved to a material extent in the *firm's designated investment business*.] *Firms* are reminded that there are further provisions relating to the management and activities of *investment analysts* in *COB 7.16*.

After *COB 7.15* insert the following new section:

---

<sup>1</sup> See the Conflicts of Interest (Corporate Finance and Investment Analysts) Instrument 2003, the commencement date of which was deferred from 1 February 2004 to 1 May 2004 by the Conflicts of Interest (Corporate Finance and Investment Analysts) (Postponement) Instrument 2004

- 7.16 Investment research
- Application
- 7.16.1 R This section applies to a *firm* that prepares *investment research* for publication or distribution to its *clients*, or that publishes or distributes *investment research* to its *clients*.
- Purpose
- 7.16.2 G The purpose of this section is to amplify relevant *Principles*, and set out particular steps a *firm* should take, in relation to *investment analysts* and *investment research*. The *FSA* considers that in this context *Principle 1* (Integrity), *Principle 2* (Skill, care and diligence), *Principle 3* (Management and control), *Principle 5* (Market Conduct), *Principle 6* (Customers' interests), *Principle 7* (Communication with clients) and *Principle 8* (Conflicts of interest) are particularly relevant.
- Conflicts of interest in investment research: general
- 7.16.3 G The *FSA* considers that conflicts of interest are much less likely to arise if *investment research* is solely for a *firm's* own internal use, for example to inform its decisions about managing its proprietary trading or its strategic direction. The *FSA* considers that it is inappropriate for an analyst to prepare research papers or analyses which are intended firstly for internal use for the *firm's* own advantage, and then for later publication to *clients* (in circumstances in which it might reasonably be expected to have a material influence on the *clients'* investment decisions).
- 7.16.4 G The obligations referred to in *COB 7.16.2G* apply to all types of *investment research*. A *firm's* senior management is responsible for ensuring that its systems, controls and procedures are robust and adequate to identify and manage the conflicts of interest which arise in relation to *investment research* or similar publications, and to ensure, as far as practicable, that those arrangements operate effectively. The *FSA* does not consider that these conflicts of interest can be adequately managed by disclosure alone.
- Policies for managing conflicts of interest: impartial investment research
- 7.16.5 R (1) This *rule* applies to a *firm* that publishes or distributes *investment research* and where either:
- (a) the *firm* holds it out (in whatever terms) as being an impartial assessment of the value or prospects of its subject matter; or
  - (b) it is reasonable for those to whom the *firm* has published or distributed it to rely on it as an impartial assessment of the value or prospects of its subject matter.
- (2) If this *rule* applies, a *firm* must:
- (a) establish and implement a policy, appropriate to the *firm*, for managing effectively the conflicts of interest which might affect the impartiality of *investment research* of the type described in (1);
  - (b) make a record of the policy and retain it until at least three years after it ceases to have effect;
  - (c) take reasonable steps to ensure that it and its *employees* comply with the policy;

- (d) make available to any *person* in writing, on request, a copy of the policy (for example, by including it on an appropriate website); and
  - (e) take reasonable steps to ensure that the policy remains appropriate and effective.
- (3) The policy must identify the types of *investment research* to which it applies, and must make provision for systems, controls and procedures (making clear the extent to which the *firm's* policy relies on *Chinese walls* or other information barriers within the *firm*):
- (a) to identify conflicts of interest which might affect the impartiality of the *investment research* to which the policy relates; and
  - (b) to manage effectively conflicts of interest, to the extent that they arise or might arise within the *firm*, in relation to at least the following:
    - (i) the supervision and management of *investment analysts*;
    - (ii) the remuneration structure for *investment analysts*;
    - (iii) the extent to which *investment analysts* may become involved in activities other than the preparation of *investment research*;
    - (iv) the extent to which (if at all) inducements offered by *issuers*, or others with a material interest in the subject matter of *investment research*, may be accepted by *investment analysts* or senior *employees* of the *firm*;
    - (v) who may comment on draft *investment research* before publication, and the process for taking account of their comments;
    - (vi) the timing and manner of publication and distribution of *investment research* and of the communication of its substance; and
    - (vii) what information or disclosures are appropriate to include in the *investment research* (taking due account of matters required by law).

- 7.16.6 G (1) *Investment research* may be held out as impartial in various ways, for example if it is labelled with that term or similar terms like ‘independent’ or ‘objective’. Even without this kind of labelling on the *investment research* itself, it may still be held out as impartial if, for example, the *firm's* representatives state that it is so (in writing or orally), or behave in a way that reasonably gives that impression.
- (2) The policy a *firm* makes available under COB 7.16.5R(2) is likely to be implemented by detailed procedures and operational arrangements. Those detailed procedures and operational arrangements need not be published.

Policy content: general

- 7.16.7 G *Firms* should organise the *investment research* function (including the way in which their *investment analysts* are supervised and remunerated) in a way which minimises the potential influence of the commercial interests of the *firm*, its *employees*, its *associates*, or its *clients*, on the impartiality of its *investment research*.

- 7.16.8 G A *firm's* policy under COB 7.16.5R should be appropriate for its own structure and business. The policy will therefore need to take account of the following factors (further *guidance* on what an appropriate policy might cover is set out in COB 7.16.9G to 7.16.15G, not all of which will be relevant to every *firm*):
- (1) the *firm's* size and organisational structure;
  - (2) the classification under COB 4.1 of its *clients*, to whom the *investment research* is published or distributed, and their experience and expertise;
  - (3) the nature of the *investments* in relation to which (or in relation to the *issuers* of which) the *firm* publishes or distributes *investment research*; and
  - (4) the nature of the business which it conducts with or for its *clients* and on its own account.

Policy content: supervision and remuneration of analysts

- 7.16.9 G If an individual (such as someone involved in raising capital for a corporate *client*) has responsibilities that might reasonably be considered to conflict with the interests of the *clients* to whom the *investment research* is published or distributed, it will not usually be appropriate for him to be responsible for:
- (1) the day to day supervision or control of an *investment analyst*;
  - (2) decisions on the subject matter or content of *investment research* or the timing of its publication (though it may be appropriate for him to have an opportunity to check the accuracy of the facts relied on in the *investment research*);
  - (3) determining the remuneration of an *investment analyst*.

- 7.16.10 G (1) An *investment analyst's* remuneration should be structured so as not to create (or reasonably suggest the creation of) an incentive which is inconsistent with the provision of an impartial assessment of the subject matter of *investment research* by the *analyst*.
- (2) An *investment analyst's* remuneration should not be linked to a specific transaction, or to recommendations contained in *investment research*, but it may be linked to the general profits of the *firm*.

Policy content: involvement of analysts in other activities

- 7.16.11 G (1) An *investment analyst* should not be involved in activities in a way which suggests that he is representing the interests of the *firm* or a *client* if this is likely reasonably to appear to be inconsistent with providing an impartial assessment of the value or prospects of the *relevant investments*.
- (2) A *firm's* policy may allow it to use an *investment analyst's* knowledge and information to assist it to research *corporate finance business* opportunities, to provide ideas to sales or trading staff, or to provide information and advice to the *firm's* investment *clients*.
- (3) It is likely to be inappropriate for the policy to allow the *firm* to:
- (a) use an *investment analyst* in a marketing capacity (for example in pitches to solicit or obtain *corporate finance business* from the *issuer* of a *relevant investment*), if this would give a reasonable perception of lack of impartiality in his *investment research*; or

- (b) allow an *investment analyst* to act in a way which reasonably appears to be representing the *issuer* of a *relevant investment*, for example, in roadshows relating to issues or allocations of *relevant investments*.

Policy content: avoiding inappropriate influences

- 7.16.12 G *Firms* should put in place arrangements so that *investment research* sets out impartial views about the value or prospects of the *relevant investment* or the *relevant issuer* of the *investment analyst* or *analysts* responsible for its content. For example:
- (1) the *firm* should prohibit any of its *investment analysts* or other employees, from offering or accepting an inducement to provide favourable *investment research* (*COB 2.2.3R* requires the *firm* itself to take reasonable steps to ensure that such inducements are not offered, given, solicited or accepted);
  - (2) the *firm* should not give effective editorial control to someone whose role or commercial interests might reasonably be considered to conflict with the interests of the *clients* to whom the *investment research* is to be published or distributed; accordingly, a *firm* should:
    - (a) not allow anyone other than an *investment analyst* (such as a *relevant issuer*) to approve the content of *investment research* before *publication*; and
    - (b) only allow a *person* outside the *firm* (such as a *relevant issuer*), or any *employee* other than an *investment analyst*, to view it before its *publication* for verification of factual information in the *investment research*.

Policy content: means and timing of publication

- 7.16.13 G A *firm's* policy and procedures should provide for *investment research* to be published or distributed to its *clients* in an appropriate manner. For example it will be:
- (1) appropriate for a *firm* to take reasonable steps to ensure that its *investment research* is published or distributed only through its usual channels, as set out in the policy;
  - (2) inappropriate for an *employee* (whether or not an *investment analyst*) to communicate the substance of any *investment research*, except as set out in the policy.
- 7.16.14 G A *firm* should also consider whether or not other business activities of the *firm* could create the reasonable perception that its *investment research* may not be an impartial analysis of the market in or the value or prospects of a *relevant investment*. Consequently a *firm* should consider whether its policy should contain any restrictions on the timing of the publication of *investment research*. For example, a *firm* might consider whether it should restrict publication of relevant *investment research* around the time of an investment offering.

Policy content: disclosures

- 7.16.15 G A *firm* should consider what information by way of disclosures should accompany the *investment research* it publishes or distributes.

Schedule 1  
Record keeping requirements

...

Table:

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
COB 7.13.11R(1)(d)	...	...	...	...
COB <u>7.16.5R(2)(b)</u>	<u>Policy for managing conflicts of interest arising as a result of publication or distribution of investment research</u>	<u>Details of the policy</u>	<u>When adopted</u>	<u>Until three years after the policy ceases to have effect</u>

## Annex B

### Amendments to the Glossary

In this Annex all text is new and is not underlined.

Insert the following new definitions in the Glossary in the appropriate alphabetical position:

*relevant investment* (in relation to *investment research* or a public appearance) a *designated investment* that is the subject of that research or appearance.

*relevant issuer*

- (a) (in relation to a *designated investment* that is the subject of *investment research* or a *public appearance*) the *issuer* of that *designated investment*; or
- (b) (in relation to a *related designated investment* that is the subject of *investment research* or a *public appearance*) either the *issuer* of the *related designated investment* or the *issuer* of a *designated investment* that might reasonably be expected directly to affect the value of the *related designated investment*.

**CLIENT ASSETS SOURCEBOOK (AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of:
- (1) the powers and related provisions in the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 139(1) (Miscellaneous ancillary matters).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 May 2004.

**Amendments to the Client Assets sourcebook**

- D. The Client Assets sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- G. This instrument may be cited as the Client Assets Sourcebook (Amendment) Instrument 2004.

By order of the Board  
18 March 2004



## Annex

### Amendments to the Client Assets sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 4.1.16 R *Money* need not be treated as *client money* in respect of a delivery versus payment transaction, for the purpose of settling a transaction in relation to *units* in a *regulated collective investment scheme*, if:
- (1) the ~~firm~~ authorised fund manager receives it from a *client* in relation to the ~~firm's~~ authorised fund manager's obligation to issue *units* in an AUT or to arrange for the issue of units in an ICVC, in accordance with *CIS*, unless the *price* of those *units* has not been determined by the close of business on the next *business day*:
    - (a) following the date of the receipt of the *money* from the *client*; or
    - (b) if the *money* was received by an *appointed representative* of the ~~firm~~ authorised fund manager, in accordance with *CASS 4.3.15R*, following the date of receipt at the specified business address of the ~~firm~~ authorised fund manager; or
  - (2) the *money* is held in the course of redeeming *units* where the proceeds of that redemption are paid to a *client* within the time specified in *CIS*; when a ~~firm~~ an authorised fund manager draws a cheque or other payable order within these timeframes the provisions of *CASS 4.3.101R* and *CASS 4.3.102R* will not apply.

**TRAINING AND COMPETENCE SOURCEBOOK  
(EXAMINATIONS AND MISCELLANEOUS AMENDMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 149 (Evidential provisions);
  - (3) section 150(2) (Actions for damages);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The provisions of the Act relevant to rules and listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on:
- (1) 1 May 2004 for TC 2.5.7G, TC 2.7.4G and TC 2.8.1 R (2) (miscellaneous provisions in Annex A);
  - (2) 31 October 2004 for:
    - (a) the amendments to TC 2.1.4R (relating to the activities to which TC 2 applies); and
    - (b) row 1(p) - (q) and the provision 2(g) in the table in TC 2.5.1AR (relating to the time limits for examinations in respect of mortgage business);
  - (3) 14 January 2005 for:
    - (a) row 1(r) in the table in TC 2.5.1AR (relating to the time limits for examinations in respect of insurance mediation business); and
    - (b) the words in square brackets, in both places where they occur, in TC 2.5.5R(1) which then replace “TC 2.4.5R(2)”; and
  - (4) 1 July 2004 for all other provisions (relating to examinations).

**Amendments to the Training and Competence sourcebook (TC)**

D. TC is amended in accordance with Annex A to this instrument.

**Amendments to the Supervision manual (SUP)**

E. SUP is amended in accordance with Annex B to this instrument.

**Amendments to the Glossary**

F. The Glossary is amended in accordance with Annex C to this instrument.

**Citation**

G. This instrument may be cited as the Training and Competence Sourcebook (Examinations and Miscellaneous Amendments) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendments to the Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text (unless it is in square brackets as explained in the footnotes to TC 2.4.2R and TC 2.4.5R). Where entire annexes are being deleted, they are indicated but are not reproduced.

#### 1 Table Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
4	<i>TC 2.5.1 R (1) and (2)</i>	R	(1) A <i>firm</i> which, immediately before <i>commencement</i> , was required to comply with specific training and competence requirements imposed by its <i>previous regulator</i> , may, in respect of the individuals employed before <i>commencement</i> , comply with the requirements of <i>TC 2.5.1 R (1) and (2)</i> by ensuring that those individuals pass the <del>relevant <i>approved examinations</i></del> <u>appropriate examinations</u> within the time limits imposed by its <i>previous regulator</i> .	From <i>commencement</i>	<i>Commencement</i>
...					

...

2.1.4R Table: Activities to which TC2 applies

...

	Activity	Extent of Application
1. <i>Employees</i> engaging in:	Advising (without dealing) ... (p) <i>advising a customer on a:</i>  (i) <i>regulated mortgage contract (including a <u>other than a regulated lifetime mortgage contract</u> or a regulated mortgage contract that is for a business purpose; and</i>  (ii) <i>a regulated lifetime mortgage contract.</i> <sup>1</sup> ...	

2.2.2 G The *firm* should take reasonable steps to obtain information about the knowledge and skills of the individual in *TC 2.2.1R*, including any appropriate examination ~~approved examination~~ passes, from a suitable source within a reasonable time.

...

2.4.2 R [(1)]<sup>2</sup> A *firm* which permits an *employee* to engage in an activity with or for a *private customer* under supervision must ensure that:

(1)[(1)(a)] the *employee* has first passed the relevant regulatory module of an appropriate examination ~~approved examination~~; and

<sup>1</sup> 1(p) was inserted by the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003 (FSA 2003/72) to come into force on 31 October 2004. This wording shows the changes to the wording in that instrument.

<sup>2</sup> The amendments in this rule and in *TC 2.4.5R* indicated by [ ] are the amendments contained in Annex E of the Insurance: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2004 (FSA 2004/08) which was made on 15 January 2004 and which will come into force on 14 January 2005.

(2)[(2)(b)] the *firm* has satisfied itself that the *employee* has an adequate level of knowledge and skills to act with or for *private customers* while under supervision.

[(2) (1)(a) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract*.]

...

2.4.4 R If a *firm* permits an *employee* under supervision to engage in:

(1) *advising on investments* which are, and *dealing with* ~~or~~ or for *clients* in, *securities* (other than *stakeholder pension schemes* or *broker funds*), *derivatives* or both such *securities* and *derivatives*; or

...

the *firm* must ensure that the *employee* has first passed ~~the~~ an appropriate examination ~~approved examination~~ before permitting the *employee* to engage in the relevant activity.

Assessing competence

2.4.5 R [(1)]<sup>3</sup> A *firm* must not assess an *employee* as competent to engage in or oversee an activity unless the *employee*:

(1)[(1)(a)] has been assessed as competent to apply the knowledge and skills necessary to engage in or oversee the activity without supervision; and

(2)[(2)(b)] has passed each module of ~~the~~ an appropriate ~~approved examination~~ examination ~~specified in the annexes to TC 2.~~

[(2) (1)(b) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract*.]

...

2.5 ~~Approved examinations~~ Appropriate examinations

Time limits

2.5.1 R (1) A *firm* must ensure that an *employee* under supervision passes ~~the~~ an appropriate examination ~~approved examination~~ within the time specified in ~~the annexes to TC2~~ TC 2.5.1AR, and, for this purpose, a *firm* must record the date on which the *employee* began engaging in or overseeing the relevant activity.

---

<sup>3</sup> See the footnote to TC 2.4.2R.

- (2) For the purposes of calculating the time spent by an *employee* under supervision, a *firm* must:
- (a) aggregate periods of time spent engaging in or overseeing the activity during different periods of employment; and
  - ...
- (3) A *firm* must ensure that any *employee* who does not pass an appropriate examination ~~the approved examination~~ within the specified time:
- (a) ceases to engage in or oversee the activity; and
  - (b) does not resume the activity or oversee the activity without first passing an appropriate examination ~~the approved examination~~.

2.5.1A R      The time limits to which TC 2.5.1R applies

Activity in TC 2.1.4 R	Examination must be passed:
1. (a) – (c)	<u>before starting the activity</u>
(d) – (e)	<u>within 30 months of starting the activity</u>
(f) – (g)	<u>within two years of starting the activity</u>
(h)	<u>(no examination requirement)</u>
(i) – (l)	<u>within two years of starting the activity</u>
(m) – (o)	<u>before starting the activity</u>
(p) – (q)	<u>within two years of starting the activity</u>
(r)	<u>(no examination requirement)</u>
2. (a) – (g)	<u>within two years of starting the activity</u>

- 2.5.2 G      A *firm* should, for the purposes of TC 2.8.1R (Record keeping), make and retain records of the time limits within which the appropriate examination-~~approved examination~~ has been passed.

Advising and dealing: restarting the activity

- 2.5.3 R      A *firm* must ensure that an *employee* does not recommence engaging in the activity of *advising on investments* which are, and *dealing* with or for *clients* in, *securities* (other than *stakeholder pension schemes* or *broker funds*), *derivatives* or both such *securities* and *derivatives* if:

- (1) the *employee* has not engaged in that activity for 12 ~~months~~ months; and

- (2) two years have elapsed since the *employee* passed an appropriate examination ~~approved examination~~ for that activity;

unless the *firm* can demonstrate that the *employee* has sufficient experience and has kept his technical and regulatory knowledge up to date. If the *firm* cannot do so it must require the *employee* to pass an appropriate examination ~~the appropriate approved examination~~.

...

Exemption from an appropriate examination ~~the approved examination~~

- 2.5.5 R (1) Except as described in (2) and (3), if a *firm* is satisfied that an *employee*:
- (a) has at least three years' up-to-date relevant experience in the activity in question obtained while employed outside the *United Kingdom*;
  - (b) had not previously been required to comply fully with the relevant examination requirements as stipulated in *TC* 2.4.5R(2) [*TC* 2.4.5R(1)(b)]<sup>4</sup>; and
  - (c) has passed the relevant regulatory module of an appropriate examination ~~approved examination~~;

then the requirement to have passed each module of an ~~the~~ appropriate examination ~~approved examination~~ in *TC* 2.4.5R(2) [*TC* 2.4.5R(1)(b)]<sup>4</sup> does not apply for that *employee*.

...

~~European and other overseas examinations~~

- 2.5.7 G ~~The annexes to *TC* 2 give details of the extent to which European and other overseas based examinations are appropriate for an activity. In addition, the definition of *approved examination* includes an examination which is equivalent in accordance with the *Diploma Directives*. [deleted]~~

Appropriate examinations

- 2.5.8 E (1) This rule applies for the purposes of *TC* 2.4.2R, *TC* 2.4.4R, *TC* 2.4.5R, *TC* 2.5.1R, *TC* 2.5.3R, *TC* 2.5.5R and *TC* 2.7.5R.
- (2) In ensuring that an examination is appropriate, a *firm* should select an appropriate examination from the list of examinations maintained by The Financial Services Skills Council as amended from time to time.

---

<sup>4</sup> See Commencement provisions C(3)(b) on page 1 of this instrument.



(3) Compliance with (2) may be relied on as tending to establish compliance with the *rules* referred to in (1).

...

2.7.4 G Appropriate supervision will vary according to the competence of the *employee* and is likely to be less intense once competence has been attained. If the *employee* is, for example, a *sole trader*, or the only *director* or *partner* *engaging in the activity*, the *firm* should make whatever arrangements are appropriate in the circumstances, bearing in mind that it can become difficult to be objective about one's own performance.

Supervisors of employees advising private customers on packaged products

2.7.5 R If an *employee* is engaging in the activity of giving advice on *investments* which are *packaged products* to *private customers*, the *firm* must ensure that the individual supervising that *employee*:

(1) has passed an appropriate examination~~approved examination~~; and

....

...

2.8.1 R (1) A *firm* must make appropriate records to demonstrate compliance with the *rules* in this chapter.

(2) The records in (1) must be retained by the *firm* for at least three years after ~~cessation of an *employee's* ceases to engage in or oversee an~~ activity appointment with the *firm*, except for the records of *pension transfer specialists*, which must be retained indefinitely.

Annexes 1-10 [deleted]<sup>5</sup>

Schedule 1

Record keeping requirements

...

Table: Record keeping requirements

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
TC 2.4.9G	Attaining Competence	Data on competence	On a continuing basis	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or</u> <del>Employment plus 3 years or for</del>

<sup>5</sup> Annex D of the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003 (FSA 2003/72) made on 15 October 2003 introduced Table 4 to TC 2 Ann 1R with effect from 31 October 2004. The effect of this deletion is that Table 4 will not come into effect.

				PTS indefinite
TC 2.5.1 R	<u>Appropriate examinations</u> <i>Approved examinations</i>	Examination time limits	When <i>employee</i> begins in the activity	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite
TC 2.5.2 G	<u>Appropriate examinations</u> <i>Approved examinations</i>	Examination passes and dates and other relevant data such as periods of absence	Duration of time limits for that activity	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite
TC 2.5.6 G	<u>Appropriate examinations</u> <i>Approved examinations</i> - regulatory module only	Criteria for application of TC 2.5.5 R to the <i>employee</i>	At the time of the application of the <i>rule</i>	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite
TC 2.6.4G	Maintaining Competence	Criteria for and application of assessment	On a continuing basis after competence	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite
TC 2.7.6G	Supervising and monitoring	Criteria in deciding level of supervision and how it is carried out	When the <i>employee</i> begins in the activity and on an ongoing basis	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite
TC 2.8.1 R (1)	Compliance with sourcebook	Data on competence, relevant to compliance with the sourcebook	When the <i>employee</i> begins in the activity and on a continuing basis	<u>For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or Employment plus 3 years</u> or for PTS indefinite

## Annex B

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

10.10.9 G When considering an application for *approval* in relation to this *controlled function*, the *FSA* may ask for evidence of the individual's competence. *TC 2.4.1R* provides that a *firm* must ensure that an *employee* is not allowed to engage in an activity unless the *employee* has been assessed as competent in that activity, in accordance with *TC 2.4.5R*, or is appropriately supervised. *TC 2.4.5R* provides that a *firm* must, before an *employee* can be assessed as competent, ensure that the *employee* has been assessed as able to apply the knowledge and skills necessary to engage without supervision in the relevant activity and has passed an ~~the~~ appropriate examination ~~approved examination~~.

10.10.10 G The *FSA* would expect an individual from overseas to be accompanied on a visit to a *customer*. *TC 2.5.5R(1)* provides that the *firm* will have to be satisfied that the individual has at least three years' up-to-date relevant experience obtained outside the *United Kingdom*. However, the remaining provisions of *TC 2.5.5R (1)* are disapplied in these circumstances (except for an individual who gives advice to *private customers* on *packaged products* or is a *broker fund adviser*). The effect of this is that the individual who may have previously been required to comply fully with the *United Kingdom* examination requirements, now need not pass the relevant regulatory module of an appropriate examination ~~approved examination~~ (see *TC 2.5.5R(3)* and (4)).

...

10.10.13A G The *FSA* would expect an individual from overseas to be accompanied on a visit to a *customer*. *TC 2.5.5R(1)* provides that the *firm* will have to be satisfied that the individual has at least three years' up-to-date relevant experience obtained outside the *United Kingdom*. However, the remaining provisions of *TC 2.5.5R(1)* are disapplied in these circumstances. The effect of this is that the individual, who may previously have been required to comply fully with the *United Kingdom* examination requirements, now need not pass the relevant regulatory module of an appropriate examination ~~approved examination~~ (see *TC 2.5.5R(3)* and (4)).

...

10.10.22 G The *FSA* would expect an individual from overseas to be accompanied on a visit to a *customer*. *TC 2.5.5R(1)* provides that the *firm* will have to be satisfied that the individual has at least three years' up-to-date relevant experience obtained outside the *United Kingdom*. However, the remaining provisions of *TC 2.5.5R(1)* are disapplied in these circumstances. The effect of this is that the individual, who may previously have been required to comply fully with the *United Kingdom* examination requirements, now need

not pass the relevant regulatory module of an appropriate examination  
~~approved examination~~ (see *TC 2.5.5R(3)* and (4)).

...

SUP 10 Annex 4

Approved person regime forms

Form A

Application to perform controlled functions under the approved persons regime

3.07 If the answer to 3.06 is “YES”, indicate which of the following formed part of the assessment (only tick one box):

Passing the relevant module(s) of an ~~the~~ appropriate examination ~~as specified in the annexes to TC2~~ as required by TC 2.4.5 R

OR

Complying with *TC 2.5.5R* (~~Approved examinations~~ Appropriate examinations)

OR

Complying with *TC* Transitional Provisions

## Annex C

### Amendments to the Glossary

In this Annex, striking through indicates deleted text.

*approved examination* ~~an examination listed in the annexes to *TC2*, or an examination which is equivalent in accordance with the *Diploma Directives*.~~

**APPLICATION FEES (2004/2005) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers);
  - (2) section 157(1) (Guidance); and
  - (3) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2004.

**Amendments to the Handbook**

- D. (1) The Authorisation manual (AUTH) is amended in accordance with Annex A to this instrument.
- (2) The Collective Investment Schemes sourcebook (CIS) is amended in accordance with Annex B to this instrument.
- (3) The Professional firms sourcebook (PROF) is amended in accordance with Annex C to this instrument.
- (4) The Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC) is amended in accordance with Annex D to this instrument.

**Citation**

- E. This instrument may be cited as the Application Fees (2004/2005) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendments to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

4.1.5G Most of the detail of what fees are payable by applicants and *Treaty firms* is set out in *AUTH 4 Annex 1R*, ~~the provisions of which will vary from one financial year to another. Accordingly a fresh *AUTH 4 Annex 1R* will come into force, following consultation, for each financial year.~~

Insert new AUTH 4 Ann 1R:

#### Authorisation fees payable

##### Part 1 – Authorisation fees payable

<b>Application type (see Part 2)</b>	<b>Amount payable</b>
(a) <i>Credit unions</i> – registration of common bond	£200
(b) <i>Version 1 credit unions</i> - authorisation	£300
(c) <i>Version 2 credit unions</i> - authorisation	£1,800
(d) Straightforward	£1,500
(e) Moderately complex	£5,000
(f) Complex	£25,000

##### Part 2 – Complexity Groupings

Straightforward cases

<b>Activity grouping</b>	<b>Description</b>
A.3	<i>Friendly societies</i> only
A.4	<i>Friendly societies</i> only
A.12	Advisory arrangers, dealers or brokers (holding or controlling <i>client money</i> and/or assets)
A.13	Advisory only firms and advisory arrangers, dealers or brokers (not holding or controlling <i>client money</i> and/or assets)
A.14	Corporate finance advisers

Moderately complex cases

<b>Activity grouping</b>	<b>Description</b>
A.1	<i>E-money issuers only</i>
A.5	<i>Managing agents at Lloyd's</i>
A.7	Fund managers
A.9	<i>Operators, trustees and depositaries of collective investment schemes</i>
A.10	<i>Firms dealing as principal</i>
B.	<i>Service companies</i>

Complex cases

<b>Activity grouping</b>	<b>Description</b>
A.1	<i>Deposit acceptors (excluding e-money issuers and credit unions)</i>
A.3	<i>Firms conducting insurance activities subject only to prudential regulation (excluding friendly societies)</i>
A.4	<i>Firms conducting insurance activities subject to both prudential and conduct of business regulation (excluding friendly societies)</i>

### **Part 3 – Variation of permission fees**

The fee payable under *SUP* 6.3.22R is 50% of that payable under *AUTH* 4.2.2R.

There are no circumstances specified for the purposes of *SUP* 6.3.22R(2).

### **Part 4 – Authorisation fees for Treaty firms**

If the *Treaty firm* wishes to undertake the permitted activities in question through its branch in the *United Kingdom*, the fee is 50% of the fee that would be payable under *AUTH* 4.2.2R.

If the *Treaty firm* wishes to undertake the permitted activities in question by providing services in the *United Kingdom*, the fee is 25% of the fee which would be payable under *AUTH* 4.2.2R.

### **Part 5 – Activity groupings**

The activity group definitions are set out in *SUP* 20 Ann 1R.

### **Part 6 – Application for a certificate under article 54 of the Regulated Activities Order**

The amount payable in relation to each application is £2,000.



## Annex B

### Amendments to the Collective Investment Schemes sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

18.3.1R The *person* identified in ~~Part A of CIS 18 Ann 1R~~ CIS 18 Ann 2R as the "relevant fee payer" must pay each fee applicable to any application or notification as specified in ~~part A of CIS 18 Ann 1R~~ CIS 18 Ann 2R.

18.3.2R The relevant fee payer must pay a fee identified in ~~Part A of CIS 18 Ann 1R~~ CIS 18 Ann 2R on or before the date on which the relevant application or notification is made.

...

18.3.4R A fee identified in ~~Part A of CIS 18 Ann 1R~~ CIS 18 Ann 2R must be paid by bankers draft, cheque or other payable order.

Insert new CIS 18 Ann 2R:

#### Application and notification fees payable

Table

Legislative provision	Nature and purpose of fee	Payable by	Amount of fee	Umbrella scheme factor (note 1)
Regulation 12 of the <i>OEIC Regulations</i>	On application for an order declaring a <i>scheme</i> to be an <i>ICVC</i>	An applicant (note 2)	£1,200	2
Section 242 of the <i>Act</i>	On application for an order declaring a <i>scheme</i> to be an <i>AUT</i>	An applicant (note 2)	£1,200	2
Section 264 of the <i>Act</i>	On giving notice under section 264 of the <i>Act</i>	The <i>operator</i> (note 3)	£600	2
Section 270 of the <i>Act</i>	On giving notice under section 270 of the <i>Act</i>	The <i>operator</i> (note 3)	£600	2
Section 272 of the <i>Act</i>	On application for an order declaring a <i>scheme</i> to be an individually recognised overseas <i>scheme</i>	An applicant (note 2)	£14,000	2

Notes:

1. For an *umbrella scheme* the fee is multiplied by the factor shown in the final column of the table.
2. The fee must accompany the application.
3. The fee must accompany the notice.

## Annex C

### Amendments to the Professional firms sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

6.3.1R Any *person* who requests the Treasury to make an order under section 326(1) of the *Act* (Designation of professional bodies) must pay to the *FSA* the sum specified in ~~*PROF 6 Ann 1R*~~ *PROF 6 Ann 2R* 30 days after the order is granted.

Insert new PROF 6 Ann 2R:

#### **Fees payable for an order under section 326(1) of the Financial Services and Markets Act 2000**

Table

<b>Nature and purpose of fee</b>	<b>Amount payable</b>	<b>Due date</b>
Any <i>person</i> seeking an order under section 326(1) of the <i>Act</i> (Designation of professional bodies)	£5,000	30 days after the order is granted

## Annex D

### Amendments to the Recognised Investment Exchanges and Recognised Clearing Houses sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

7.1.4G Most of the detail of the fees payable by *recognised bodies* ~~and applicants~~ is set out in *REC 7 Ann 1R*. The provisions of the annex will vary from one financial year to another. Accordingly a new annex will come into force, following consultation, for each financial year.

...

7.3.1R An application for recognition as a *UK recognised body* under section 287 or section 288 of the *Act* must pay to the *FSA* in full and without any deduction the application fee specified for that type of application in ~~part 3 of *REC 7 Ann 1R* for the year in which the application is made~~ part 1 of *REC 7 Ann 2R*.

7.3.2R An application for recognition as an *overseas recognised body* under section 287 or section 288 and section 292 of the *Act* must pay to the *FSA* in full and without any deduction the application fee specified in ~~part 4 of *REC 7 Ann 1R* for the year in which the application is made~~ part 2 of *REC 7 Ann 2R*.

Insert new *REC 7 Ann 2R*:

#### Application fees payable

##### Part 1 – Application fees for applicants for recognition as a UK recognised body

Description of applicant	Amount payable	Due date
Applicant for recognition as a <i>UK RIE</i>	£100,000	Date the application is made
Applicant for recognition as a <i>UK RCH</i>	£100,000	Date the application is made
Additional fees for applicant who proposes to:		
- act as a central counterparty	£25,000	Date the application is made
- offer safeguarding and administration services	£25,000	Date the application is made
- use substantially new and untested information technology systems in the performance of its relevant functions	£25,000	Date the application is made

**Part 2 – Application fees for applicants for recognition as an overseas recognised body**

<b>Description of applicant</b>	<b>Amount payable</b>	<b>Due date</b>
Applicant for recognition as a recognised overseas investment exchange	£50,000	Date the application is made
Applicant for recognition as a recognised overseas clearing house	£50,000	Date the application is made
Additional fees for applicant who proposes to:		
- act as a central counterparty	£25,000	Date the application is made
- offer safeguarding and administration services	£25,000	Date the application is made

## PERIODIC FEES (AMENDMENT) INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers);
  - (2) section 157(1) (Guidance); and
  - (3) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

### Commencement

- C. This instrument comes into force on 1 April 2004.

### Amendments to the Handbook

- D. (1) The Authorisation manual (AUTH) is amended in accordance with Annex A to this instrument.
- (2) The Supervision manual (SUP) is amended in accordance with Annex B to this instrument.
- (3) The Supervision manual (SUP) is further amended by inserting, as Annexes to SUP 20, the provisions in Annex C to this instrument.
- (4) The Compensation sourcebook (COMP) is amended in accordance with Annex D to this instrument.
- (5) The Collective Investment Schemes sourcebook (CIS) is amended in accordance with Annex E to this instrument.
- (6) The Credit Unions sourcebook (CRED) is amended in accordance with Annex F to this instrument.

### Citation

- E. This instrument may be cited as the Periodic Fees (Amendment) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendments to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text

7.7.2G            An annual fee of £1,000 will be charged to meet the costs of ongoing monitoring (see *SUP 20 Annex ~~4~~3R*).

...

AUTH 4 Ann 2R

...

Note: This annex specifies the application fees for applicants seeking to apply for *Part IV permission*, or to vary their existing *Part IV permission*, in order to undertake any of the activities specified in the A.2, A.18 and A.19 activity groups (see Part ~~7~~1 of *SUP 20 Ann 1R* for details of the activities).

## Annex B

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text

6.3.22R If a *firm* applies for a variation of its *Part IV permission*, it must pay the fee specified in Part 3 of *AUTH 4 Annex 1R* in either of the following cases:

(1) if the variation is granted, the business of the *firm* will fall within one or more activity groups specified in Part ~~7~~1 of *SUP 20 Annex 1R* not applicable before the grant of the variation; or

(2) ...

...

20.1.5G Most of the detail of what periodic fees are payable by *firms* is set out in *SUP 20 Annex ~~4~~2R*. The provisions of the annex will vary from one financial year to another. Accordingly a fresh *SUP 20 Annex ~~4~~2R* will come into force, following consultation, for each financial year.

...

20.1.10G Paragraph 17(2) of Schedule 1 to the *Act* prohibits the *FSA* from taking account of penalties received when setting its periodic and other fees. Accordingly each *SUP 20 Ann ~~4~~2R* will set the periodic fee without reference to the penalties received. The *FSA* will allocate the penalties by way of a permitted deduction specified in *SUP 20 Annex ~~4~~2R* for the relevant year. The *FSA* normally expects to allocate those deductions so that they apply to the fee blocks within which the *firms* paying penalties fall.

...

20.2.1R A *firm* must pay to the *FSA* an amount equal to:

(1) ...

(2) any deductions from the periodic fee specified in part ~~3~~2 of *SUP 20 Ann ~~4~~2R*.

...

20.2.3G A *firm* will be required to pay a periodic fee for every year during which it has a *permission* subject to any reductions or exemptions applicable under this chapter. The *FSA* will issue invoices to *firms* and expects to do so at least 30 days before the dates on which payments will fall due under ~~*SUP 20 Ann 4*~~ *20.2.7R*.

20.2.4R The periodic fee referred to in *SUP 20.2.1R* is (except in relation to the *Society*) calculated as follows:



(1) identify each of the tariffs set out in part ~~21~~ of SUP 20 Ann ~~42R~~ which apply to the business of the *firm* for the period specified in that annex;

(2) ...

(3) ...

(4) apply any applicable payment charge or discount specified in ~~part 1 of SUP 20 Ann 1R~~. SUP 20.2.7AR.

...

20.2.6R The periodic fee referred to in SUP 20.2.1R in relation to the *Society* is specified against its name in SUP 20 Ann ~~42R~~.

20.2.7R (1) The *firm* must pay the total amount due under SUP 20.2.1R~~;~~ using one of the payment methods specified in SUP 20.2.7AR.

~~(1) on or before the due date or dates specified in Part 1 of SUP 20 Ann 1R;~~  
~~and~~

~~(2) using one of the payment methods specified in Part 1 of SUP 20 Ann 1R.~~

(2) If the *firm's* periodic fee for the previous financial year was at least £50,000, the *firm* must pay:

(a) an amount equal to 50% of the periodic fee payable for the previous year, by 30 April in the financial year to which the sum due under SUP 20.2.1R relates; and

(b) the balance of the periodic fee due for the current financial year by 1 September in the financial year to which that sum relates.

(3) In any other case, the *firm* must pay the periodic fee due in full by 1 July in the financial year to which that sum relates.

20.2.7AR Table: specified payment methods

This table belongs to SUP 20.2.4R and SUP 20.2.7R

<u>Payment method</u>	<u>Additional amount or discount applicable</u>
<u>Direct debit</u>	<u>Discount of £20</u>
<u>Credit transfer (BACS/CHAPS)</u>	<u>Discount of £10</u>
<u>Cheque</u>	<u>None</u>
<u>Switch</u>	<u>None</u>
<u>Credit card (Visa/Mastercard only)</u>	<u>Additional 2% of sum paid</u>

...

20.3.1R A *firm* (other than the *Society*) must notify to the *FSA* the value (as at the valuation date specified in Part 23 of *SUP 20 Ann 1R*) of each element of business on which the periodic fee payable by the *firm* is to be calculated.

20.3.2R A *firm* (other than the *Society*) must send to the *FSA* in writing the information required under *SUP 20.3.1R* as soon as reasonably practicable, and in any event within two months, after the date specified as the valuation date in Part 23 of *SUP 20 Ann 1R*.

...

20.4.4R A *firm* which becomes authorised, or whose *permission* is extended, during the course of the financial year must pay a fee ~~equal to:~~ which is calculated by:

- (1) ~~the total of the sums calculated in accordance with each of the tariffs set out in Part 4 of *SUP 20 Ann 1R* for the relevant year which are only applicable to the *firm* after the *permission* is received or extended;~~ identifying each of the tariffs set out in Part 1 of *SUP 20 Ann 2R* for the relevant financial year that apply to the *firm* only after the *permission* is received or extended;
- (2) ~~modified as indicated by *SUP 20.4.6R*.~~ calculating the amount for each of those tariffs which is the higher of:
  - (a) the minimum fee specified for the tariff; and
  - (b) the result of applying the tariff to the projected valuation, for its first year (as provided to the *FSA* in the course of the *firm's* application), of the business to which the tariff relates (or, where relevant, the number of *approved persons* immediately after the *permission* is given);
- (3) adding together the amounts calculated under (2); and
- (4) modifying the result as indicated by *SUP 20.4.6R*.

...

20.4.8R For an *incoming EEA firm* or an *incoming Treaty firm*, the calculation required by *SUP 20.2.4R* is modified as follows:

- (1) the tariffs set out in Part 21 of *SUP 20 Ann 42R* are applied only to the *regulated activities* of the *firm* which are carried on in the *United Kingdom*; and
- (2) those tariffs are modified in accordance with Part 53 of *SUP 20 Ann 42R*.

...

20.5.2G The provision of this facility by the *FSA* incurs costs to it. Those costs depend upon the amount which the facility is used. Accordingly the income which the *FSA* receives from these transaction reporting fees will be set and accounted for separately from the fee block tariffs set out in *SUP 20 Ann 13R*.

20.5.3R A *firm* which reports its *reportable transactions* to the *FSA* using the *FSA's* Direct Reporting System (see *SUP 17*) must pay the fees specified in Part ~~61~~ of *SUP 20 Ann 13R*.

...

20.6.1R A person who holds a certificate under article 54 of the *Regulated Activities Order* must pay to the *FSA* each periodic fee specified in Part ~~82~~ of *SUP 20 Ann 13R* applicable to him.

...

20.6.4R If a certificate is issued to a person under article 54 of the *Regulated Activities Order* during the course of a year, the periodic fee payable under *SUP 20.6.3R* for that year is the amount specified in Part ~~82~~ of *SUP 20 Ann 13R* modified in accordance with Table *SUP 20.6.5R*.

...

20.6.7R ~~1-~~The amount due must be paid using one of the payment methods specified in Part ~~1~~ of ~~*SUP 20 Ann 1R*~~ *SUP 20.2.7AR*.

## Annex C

### Amendments to the Supervision manual

In this Annex all the text is new and is not underlined.

Insert new SUP 20 Ann 1R:

#### Activity groups, tariff bases and valuation dates applicable

##### Part 1

This table shows how the *regulated activities* for which a *firm* has permission are linked to activity groups ('fee-blocks'). A *firm* can use the table to identify which fee-blocks it falls into based on its *permission*.

Activity group	Fee-payer falls in the activity group if
<b>A.1</b> <b>Deposit acceptors</b>	its <i>permission</i> includes <i>accepting deposits</i> or <i>issuing e-money</i> ; <b>BUT DOES NOT</b> include either of the following: <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>.</li> </ul>
<b>A.2</b> <b>Mortgage lenders and administrators</b>	its <i>permission</i> includes one or more of the following: <ul style="list-style-type: none"> <li>• <i>entering into a regulated mortgage contract</i>; or</li> <li>• <i>administering a regulated mortgage contract</i>; or</li> <li>• <i>agreeing to carry on a regulated activity</i> which is within either of the above.</li> </ul>
<b>A.3</b> <b>Firms conducting insurance activities subject only to prudential regulation</b>	its <i>permission</i> includes one or more of the following: <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <b>BUT ONLY</b> in respect of <i>specified investments</i> that are: <ul style="list-style-type: none"> <li>- <i>general insurance contracts</i>; or</li> <li>- <i>long-term insurance contracts</i> other than <i>life-policies</i>.</li> </ul>
<b>A.4</b> <b>Firms conducting insurance activities subject to both prudential and conduct of business regulation</b>	its <i>permission</i> includes one or more of: <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <b>both in</b> respect of <i>specified investments</i> including <i>life policies</i> ; <ul style="list-style-type: none"> <li>• <i>entering as provider into a funeral plan contract</i>.</li> </ul>
<b>A.5</b> <b>Managing agents at Lloyd's</b>	its <i>permission</i> includes <i>managing the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's</i> .
<b>A.6</b> <b>The Society of Lloyd's</b>	it is the <i>Society of Lloyd's</i> .

<p><b>Note for authorised professional firms:</b></p> <p>Generally, for fee-blocks A.7 to A.14 below, only those <i>regulated activities</i> that are not limited to <i>non-mainstream regulated activities</i> should be taken into account in determining which fee-block(s) fee-payers belong to.</p> <p>However, in the case that all the <i>regulated activities</i> within a <i>firm's permission</i> are limited to <i>non-mainstream regulated activities</i>, then that <i>firm</i> will be allocated to fee-block A.13 alone.</p>	
<p><b>A.7 Fund managers</b></p>	<p>(1) its <i>permission</i> includes <i>managing investments</i>;</p> <p><b>OR</b></p> <p>(2) its <i>permission</i> includes <b>ONLY</b> either one or both of:</p> <ul style="list-style-type: none"> <li>• <i>safeguarding and administering of investments (without arranging)</i>; and</li> <li>• <i>arranging safeguarding and administration of assets</i>;</li> </ul> <p><b>OR</b></p> <p>(3) the <i>firm</i> is a <i>venture capital firm</i>.</p> <p><b>Class (1) firms</b> are subdivided into three classes:</p> <ul style="list-style-type: none"> <li>- <b>class (1)A</b>, where the funds managed by the <i>firm</i> belong to one or more <i>occupational pension schemes</i>;</li> <li>- <b>class (1)B</b>, where: <ul style="list-style-type: none"> <li>(a) the <i>firm</i> is not a class (1)A <i>firm</i>; and</li> <li>(b) the <i>firm's permission</i> includes <b>NEITHER</b> of the following: <ul style="list-style-type: none"> <li>• <i>safeguarding and administering of investments (without arranging)</i>;</li> <li>• <i>arranging safeguarding and administration of assets</i>; and</li> </ul> </li> <li>(c) the <i>firm</i> <b>EITHER</b>: <ul style="list-style-type: none"> <li>• has a <i>requirement</i> that prohibits the <i>firm</i> from holding or controlling <i>client money</i>, or both; <b>OR</b></li> <li>• if it does not have such a <i>requirement</i>, <b>only</b> holds or controls <i>client money</i> (or both), arising from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> </li> </ul> </li> <li>- <b>class (1)C</b>, where the <i>firm</i> is not within class (1)A or class (1)B.</li> </ul>
<p><b>A.8</b></p>	<p>Not applicable.</p>
<p><b>A.9 Operators, Trustees and Depositaries of collective investment schemes</b></p>	<p>(1) its <i>permission</i>:</p> <p>(a) includes one or more of the following:</p> <ul style="list-style-type: none"> <li>• <i>establishing, operating or winding up a regulated collective investment scheme</i>;</li> <li>• <i>establishing, operating or winding up an unregulated collective investment scheme</i>;</li> <li>• <i>acting as trustee of an authorised unit trust scheme</i>;</li> <li>• <i>acting as the depositary or sole director of an open-ended investment company</i>;</li> </ul> <p><b>AND</b></p>

	<p>(b) <b>PROVIDED</b> the <i>firm</i> is <b>NOT</b> one of the following:</p> <ul style="list-style-type: none"> <li>• a <i>corporate finance advisory firm</i>;</li> <li>• a <i>firm</i> in which the above activities are limited to carrying out <i>corporate finance business</i>;</li> <li>• a <i>venture capital firm</i>;</li> </ul> <p><b>OR</b></p> <p>(2) if the fee-payer has none of the <i>regulated activities</i> above within its <i>permission</i>, but <b>ALL</b> the remaining <i>regulated activities</i> in its <i>permission</i> are limited to carrying out trustee activities.</p>
<p><b>A.10</b> <b>Firms dealing as principal</b></p>	<p>its <i>permission</i> includes <i>dealing in investments as principal</i>; <b>BUT NOT</b> if one or more of the following apply:</p> <ul style="list-style-type: none"> <li>• the <i>firm</i> is acting exclusively as a matched principal broker;</li> <li>• the above activity is limited either to acting as an <i>operator</i> of a <i>collective investment scheme</i>, or to carrying out <i>trustee</i> activities;</li> <li>• the <i>firm</i> is a <i>corporate finance advisory firm</i>;</li> <li>• the above activity is otherwise limited to carrying out <i>corporate finance business</i>;</li> <li>• the <i>firm</i> is subject to a <i>limitation</i> to the effect that the <i>firm</i>, in carrying on this <i>regulated activity</i>, is limited to entering into transactions in a manner which, if the <i>firm</i> was an <i>unauthorised person</i>, would come within article 16 of the <i>Regulated Activities Order</i> (Dealing in contractually based investments);</li> <li>• the above activity is limited to not acting as a <i>market maker</i>;</li> <li>• the <i>firm</i> is an <i>oil market participant</i>, <i>energy market participant</i> or a <i>local</i>;</li> <li>• its <i>permission</i> includes either: <ul style="list-style-type: none"> <li>- <i>effecting contracts of insurance</i>; or</li> <li>- <i>carrying out contracts of insurance</i>.</li> </ul> </li> </ul>
<p><b>A.11</b></p>	<p>Not applicable.</p>
<p><b>A.12</b> <b>Advisory arrangers, dealers or brokers (holding or controlling client money or assets, or both)</b></p>	<p>its <i>permission</i>:</p> <p>(a) includes one or more of the following:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>;</li> <li>• <i>arranging (bringing about) deals in investments</i>;</li> <li>• <i>making arrangements with a view to transactions in investments</i>;</li> <li>• <i>dealing as principal in investments</i> where the activity is carried on as a matched principal broker, <i>oil market participant</i>, <i>energy market participant</i> or <i>local</i>;</li> <li>• <i>advising on investments (except pension transfers and pension opt-outs)</i>;</li> <li>• <i>advising on pension transfers and pension opt-outs</i>;</li> <li>• <i>advising on syndicate participation at Lloyd's</i>;</li> </ul> <p>(b) <b>BUT NONE</b> of the following:</p> <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>; or</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <p><b>AND</b></p> <p>(c) <b>CAN HAVE</b> one or more of the following:</p> <ul style="list-style-type: none"> <li>• <i>safeguarding and administering of assets</i>;</li> </ul>

	<ul style="list-style-type: none"> <li>• <i>arranging safeguarding and administration of assets</i>;</li> <li>• the ability to hold or control <i>client money</i>, or both: <ul style="list-style-type: none"> <li>- that is, there is no <i>requirement</i> which prohibits the <i>firm</i> from doing this; and</li> <li>- provided that the <i>client money</i> in question does not only arise from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> </li> </ul> <p><b>AND</b></p> <p>(d) <b>PROVIDED</b> the fee-payer is <b>NOT</b> any of the following:</p> <ul style="list-style-type: none"> <li>• a <i>corporate finance advisory firm</i>;</li> <li>• a <i>firm</i> for whom all of the applicable activities above are otherwise limited to carrying out <i>corporate finance business</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>venture capital business</i>;</li> <li>• a <i>firm</i> whose activities are limited to acting as an operator of a <i>regulated collective investment scheme</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>trustee</i> activities;</li> <li>• a <i>service company</i>.</li> </ul>
<p><b>A.13</b>  <b>Advisory arrangers, dealers or brokers (not holding or controlling client money or assets, or both)</b></p>	<p>(1) it is an <i>authorised professional firm</i> and <b>ALL</b> the <i>regulated activities</i> in its <i>permission</i> are limited to <i>non-mainstream regulated activities</i>;</p> <p><b>OR</b></p> <p>(2) its <i>permission</i>:</p> <p>(a) includes one or more of the following:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>;</li> <li>• <i>arranging (bringing about) deals in investments</i>;</li> <li>• <i>making arrangements with a view to transactions in investments</i>;</li> <li>• <i>dealing as principal in investments</i> where the activity is carried on as a matched principal broker, <i>oil market participant</i>, <i>energy market participant</i> or <i>local</i>;</li> <li>• <i>advising on investments (except pension transfers and pension opt-outs)</i>;</li> <li>• <i>advising on pension transfers and pension opt-outs</i>;</li> <li>• <i>advising on syndicate participation at Lloyd's</i>;</li> </ul> <p>(b) <b>BUT NONE</b> of the following:</p> <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> <li>• <i>safeguarding and administration of assets</i>;</li> <li>• <i>arranging safeguarding and administration of assets</i>;</li> </ul> <p><b>AND</b></p> <p>(c) <b>MUST EITHER</b>:</p> <ul style="list-style-type: none"> <li>• have a <i>requirement</i> that prohibits the <i>firm</i> from holding or controlling <i>client money</i>, or both;</li> </ul> <p><b>OR</b></p> <ul style="list-style-type: none"> <li>• if it does not have such a <i>requirement</i>, only holds or controls <i>client money</i> (or both), arising from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> <p><b>AND</b></p> <p>(d) <b>PROVIDED</b> the fee-payer is <b>NOT</b> any of the following:</p> <ul style="list-style-type: none"> <li>• a <i>corporate finance advisory firm</i>;</li> <li>• a <i>firm</i> for whom all of the applicable activities above are otherwise limited to carrying out <i>corporate finance business</i>;</li> </ul>

	<ul style="list-style-type: none"> <li>• a <i>firm</i> whose activities are limited to carrying out <i>venture capital business</i>;</li> <li>• a <i>firm</i> whose activities are limited to acting as an <i>operator</i> of a <i>regulated collective investment scheme</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>trustee</i> activities;</li> <li>• a <i>service company</i>.</li> </ul>
<b>A.14 Corporate finance advisers</b>	the <i>firm</i> is carrying on <i>corporate finance business</i> <b>PROVIDED</b> the fee-payer is <b>NOT</b> a <i>venture capital firm</i> .
<b>A.15</b>	Not applicable.
<b>A.16 Pensions review levy firms</b>	it was liable to pay the Pensions Levy to <i>PIA</i> in 2001/2002.
<b>A.17</b>	Not applicable.
<b>A.18 Mortgage lenders, advisers and arrangers</b>	its <i>permission</i> includes one or more of the following: <ul style="list-style-type: none"> <li>• <i>entering into a regulated mortgage contract</i>; or</li> <li>• <i>arranging (bringing about) regulated mortgage contracts</i>; or</li> <li>• <i>making arrangements with a view to regulated mortgage contracts</i>; or</li> <li>• <i>advising on regulated mortgage contracts</i>; or</li> <li>• <i>agreeing to carry on a regulated activity</i> which is within any of the above.</li> </ul>
<b>A.19 General insurance mediation</b>	its <i>permission</i> includes one or more of the following in relation to a <i>general insurance contract</i> or a <i>pure protection contract</i> : <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>; or</li> <li>• <i>arranging (bringing about) deals in investments</i>; or</li> <li>• <i>making arrangements with a view to transactions in investments</i>; or</li> <li>• <i>assisting in the administration and performance of a contract of insurance</i>; or</li> <li>• <i>advising on investments</i>; or</li> <li>• <i>agreeing to carry on a regulated activity</i> which is within any of the above.</li> </ul>
<b>B. Market operators</b>	<i>Firms</i> that have been prescribed as an operator of a prescribed market under the Financial Services and Markets Act 2000 (Prescribed Markets and Qualifying Investments) Order 2001 (SI 2001/996).
<b>B. Service companies</b>	it is a <i>service company</i> .

## Part 2

This table indicates the tariff base for each fee-block. The tariff base is the means by which we measure the 'amount of business' conducted by a *firm*.



Activity group	Tariff-base
A.1	<p><b>MODIFIED ELIGIBLE LIABILITIES</b></p> <p><b>For banks and e-money issuers:</b></p> <p><b>Part 1:</b></p> <p><b>Liabilities</b></p> <p>In sterling:  <math>\pounds 2 + \pounds 3 + \pounds 4 + \pounds 5A + \pounds 5B + \pounds 6B + \pounds 6C + \pounds 6D + \pounds 6E + \pounds 6F + \pounds 6G + \pounds 6H + \pounds 6J + \pounds 7B + \pounds 7C + \pounds 7D + \pounds 7E + \pounds 7F + \pounds 7G + \pounds 7H + \pounds 7J + \pounds 8 + \pounds 10 + 60\% \text{ of } \pounds 11A + \pounds 44</math>  plus  In foreign currency, one-third of:  <math>E2 + E3 + E4 + E5A + E5B + E6B + E6C + E6D + E6E + E6F + E6G + E6H + E6J + E7B + E7C + E7D + E7E + E7F + E7G + E7H + E7J + E8 + E10 + 60\% \text{ of } E11A + E44 + C2 + C3 + C4 + C5A + C5B + C6B + C6C + C6D + C6E + C6F + C6G + C6H + C6J + C7B + C7C + C7D + C7E + C7F + C7G + C7H + C7J + C8 + C10 + 60\% \text{ of } C11A</math>: less</p> <p><b>Assets</b></p> <p>In sterling:  <math>\pounds 21B + 60\% \text{ of } \pounds 22A + \pounds 23D + \pounds 23E + \pounds 23F + \pounds 30A + \pounds 30B + \pounds 31A + \pounds 31B + \pounds 32AA</math>  plus  In foreign currency, one-third of:  <math>E21B + 60\% \text{ of } E22A + E23D + E23E + E23F + E30A + E30B + E31A + E31B + E32AA + C21B + 60\% \text{ of } C22A + C23D + C23E + C23F + C30A + C30B + C31A + C31B + C32AA</math></p> <p><b>Part 2: Non-resident office offset</b></p> <p>The fee base is adjusted by deducting from the amount calculated in accordance with part 1 above, the Non-Resident Office Offset amount obtained by subtracting item 45D from item 45BA in the Form BT. The Non-Resident Office Offset amount, if it would otherwise have been a negative number, is zero.</p> <p><b>Notes:</b></p> <p>(1) All references in the above formula are to entries on Form BT (that is, the Balance Sheet Form completed to provide information required following the Banking Statistics Review 1997 and returned by <i>banks</i> to the Bank of England as required by the Bank of England Act 1998).</p> <p>(2) 'E' refers to assets and liabilities denominated in euro (as referred to in column 2 of Form BT) and 'C' refers to assets and liabilities denominated in currencies other than sterling and euro (as referred to in column 3 of Form BT). In accordance with Form BT, assets and liabilities in currencies other than sterling are to be recorded in sterling.</p> <p>(3) The figures reported on the Form BT relate to business conducted out of offices in the <i>United Kingdom</i>.</p> <p><b>For credit unions:</b></p> <p>Deposits with the <i>credit union</i> (share capital)  <b>LESS</b>  the <i>credit union's</i> bank deposits (investments + cash at bank)</p> <p><b>Note:</b></p> <p>Only <i>United Kingdom</i> business is relevant for calculating <i>credit unions'</i> MELs.</p>

	<p><b>For building societies:</b></p> <ul style="list-style-type: none"> <li>• deposit liabilities (including debt securities up to five years original maturity) (that is, the amounts in sterling (in column 1) and one-third of foreign currency referenced amounts (in columns 2 and 3) for items B1.1+B1.2+B2.0a+B2.0b+B2.10+B2.13+B2.14+B2.15+B2.16)</li> </ul> <p><b>LESS amounts in respect of:</b></p> <ul style="list-style-type: none"> <li>• <b>sterling repo liabilities with the Bank of England</b> (that is, ONLY the amounts in sterling (in column 5) for item B2.5a)</li> <li>• <b>balances held with the Bank of England</b> (excluding cash ratio deposits) (that is, the amounts in sterling (in column 1) and one-third of foreign currency referenced amounts (in columns 2 and 3) for item B6.2a, less the amounts in sterling (in column 1) and one-third of foreign currency referenced amounts (in columns 2 and 3) for item OW1.1)</li> <li>• <b>market loans to banks, building societies</b> (balances with and loans to, plus CDs, Commercial paper) (that is, the amounts in sterling (in column 1) and one-third of foreign currency referenced amounts (in columns 2 and 3) for items B6.3.a+B6.4.a+B6.4b+B6.5a+B6.5b+B6.12a)</li> <li>• <b>investments with banks and building societies</b> (bonds, notes and other debt instruments up to five years original maturity) (that is, the amounts in sterling (in column 1) and one-third of foreign currency referenced amounts (in columns 2 and 3) for items B6.6a1+B6.6a2+B6.10a1+B6.10a2)</li> </ul> <p><b>Note:</b> All references in the definition for building society MELs are to entries in the MFS1 which is submitted <i>monthly</i> by all <i>building societies</i> to the <i>FSA</i>.</p>
A.2	Not applicable. [Note: will be made to come into effect from 31 October 2004.]
A.3	<p><b>GROSS PREMIUM INCOME AND GROSS TECHNICAL LIABILITIES</b></p> <p><b>For insurers:</b> The amount of <i>premiums</i> receivable which must be included in the documents required to be deposited under <i>IPRU (INS)</i> 9.6 in relation to the financial year to which the documents relate but disregarding for this purpose such amounts as are not included in the document by reason of a <i>waiver</i> or an order under section 68 of the Insurance Companies Act 1982 carried forward as an amendment to <i>IPRU (INS)</i> under transitional provisions relating to written concessions in <i>SUP</i>; less, <i>premiums</i> relating to <i>pension fund management</i> business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk;</p> <p><b>AND</b></p> <p>the amount of gross technical liabilities (<i>IPRU (INS)</i> Appendix 9.1 – Form 15, line 19) which must be included in the documents required to be deposited under <i>IPRU (INS)</i> 9.6R in relation to the financial year to which the documents relate but disregarding for this purpose such amounts as are not included in the document by reason of a <i>waiver</i> or an order under section 68 of the Insurance Companies Act 1982 carried forward as an amendment to <i>IPRU(INS)</i> under transitional provisions relating to written concessions in <i>SUP</i>; less,</p>

	<p>the amount of gross technical liabilities relating to <i>pension fund management</i> business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk.</p> <p><b>Notes:</b></p> <p>(1) in the case of either:</p> <p>(a) a <i>pure reinsurer</i> carrying on <i>general insurance business</i> through a <i>branch</i> in the <i>United Kingdom</i>; or</p> <p>(b) an <i>insurer</i> whose head office is not in an <i>EEA State</i> carrying on <i>general insurance business</i> through a <i>branch</i> in the <i>United Kingdom</i>; or</p> <p>(c) a <i>non-EEA insurer</i> other than a <i>Swiss general insurer</i> which has <i>permission</i> to carry on <i>direct insurance business</i> and which has made a deposit in an <i>EEA state</i> other than the <i>United Kingdom</i> in accordance with <i>IPRU(INS) 8.1(2)</i>, the amount only includes <i>premiums</i> received and gross technical liabilities held in respect of its <i>United Kingdom</i> business; and</p> <p>(2) for a <i>Swiss general insurance company</i>, premiums and gross technical liabilities include those relevant to the operations of the company's <i>United Kingdom branch</i>.</p> <p><b>For friendly societies:</b></p> <p>Either:</p> <p>(a) the value of "contributions" as income under Schedule 7: Part I item 1(a) to the Friendly Societies (Accounts and Related Provisions) Regulations 1994 (SI 1994/1983) (the regulations) for a <i>non-directive friendly society</i>, included within the income and expenditure account; or</p> <p>(b) the value of "gross premiums written" under Schedule 1: Part I items I.1(a) and II.1.(a) of the regulations for a <i>directive friendly society</i> included within the income and expenditure account.</p> <p><b>Note:</b></p> <p>In both (a) and (b) above only <i>premiums</i> receivable in respect of <i>United Kingdom</i> business are relevant.</p>
<p><b>A.4</b></p>	<p><b>ADJUSTED GROSS PREMIUM INCOME AND MATHEMATICAL RESERVES</b></p> <p>Amount of new regular <i>premium</i> business (yearly <i>premiums</i> including reassurances ceded but excluding cancellations and reassurances accepted), times ten;</p> <p><b>Plus</b></p> <p>amounts of new single <i>premium</i> business (total including reassurances ceded but excluding cancellations and reassurances accepted). Group protection business (life and private health insurance) must be included;</p> <p><b>Less</b></p> <p><i>premiums</i> relating to pension fund management business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk.</p> <p>For each of the above, business transacted through independent practitioners will be divided by two in calculating the adjusted gross premium income;</p> <p><b>AND</b></p> <p>the amount of mathematical reserves (<i>IPRU (INS) Appendix 9.1R – Form 9, Line 23</i>) which must be included in the documents required to be deposited under <i>IPRU (INS) 9.6R</i> in relation to the financial year to which the documents relate but disregarding for this purpose such amounts as are not included in the document by</p>

	<p>reason of a <i>waiver</i> or an order under section 68 of the Insurance Companies Act 1982 carried forward as an amendment to <i>IPRU(INS)</i> under transitional provisions relating to written concessions in <i>SUP</i>;</p> <p><b>Less</b> mathematical reserves relating to <i>pension fund management</i> business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk.</p> <p><b>Notes:</b></p> <p>(1) Business conducted through a <i>marketing associate</i> should be excluded in reporting the <i>product provider's premium</i> income.</p> <p>(2) Only <i>premiums</i> receivable and mathematical reserves held in respect of <i>United Kingdom</i> business are relevant.</p>
<b>A.5</b>	<p><b>ACTIVE CAPACITY</b></p> <p>The capacity of the <i>syndicate(s)</i> under management in the year in question. This includes the capacity for <i>syndicate(s)</i> that are not writing new business, but have not been closed off in the year in question.</p>
<b>A.6</b>	Not applicable.
<b>A.7</b>	<p><b>FUNDS UNDER MANAGEMENT (FuM)</b></p> <p>The total value, in pounds sterling, of all assets (see note (a) below) in portfolios which the <i>firm</i> manages, on a discretionary basis (see note (b) below), in accordance with its terms of business, less:</p> <p>(a) funds covered by the exclusion contained in article 38 (Attorneys) of the <i>Regulated Activities Order</i>;</p> <p>(b) funds covered by the exclusion contained in article 66(3) (Trustees, nominees and personal representatives) of the <i>Regulated Activities Order</i>;</p> <p>(c) funds covered by the exclusion contained in article 68(6) (Sale of goods or supply of services) of the <i>Regulated Activities Order</i>;</p> <p>(d) funds covered by the exclusion contained in article 69(5) (Groups and joint enterprises) of the <i>Regulated Activities Order</i>; and</p> <p>(e) the value of those parts of the managed portfolios in respect of which the responsibility for the discretionary management has been formally delegated to another <i>firm</i> (and which <i>firm</i> will include the value of the assets in question in its own FuM total); any such deduction should identify the <i>firm</i> to which management responsibility has been delegated.</p> <p><b>Notes on FuM</b></p> <p>(a) For the purposes of calculating the value of funds under management, "assets" means all assets that consist of or include any <i>investment</i> which is a <i>designated investment</i> or those assets in respect of which the arrangements for their management are such that the assets may consist of or include such <i>investments</i>, and either the assets have at any time since 29 April 1988 done so or the arrangements have at any time (whether before or after that date) been held out as arrangements under which the assets would do so.</p> <p>(b) Assets managed on a non-discretionary basis, being assets that the <i>firm</i> has a contractual duty to keep under continuous review but in respect of which prior specific consent of the <i>client</i> must be obtained for proposed transactions, are NOT included as this activity is covered in those charged to fees in activity groups A.12 and A.13.</p> <p>(c) In respect of <i>collective investment schemes</i>, "assets" means the total value of</p>

	<p>the assets of the scheme.</p> <p>(d) For an <i>OPS firm</i>, the FuM should also be reduced by the value of the assets held as a result of a decision taken in accordance with article 4(6) of The Financial Services and Markets Act 2000 (Carrying on Regulated Activities by Way of Business) Order 2001 (investments in <i>collective investment schemes</i> or <i>bodies corporate</i> which have as their primary purpose the acquisition, directly, or indirectly, of "relevant investments", as defined in that article).</p> <p>(e) Only assets that are managed from an establishment maintained by the <i>firm</i> in the <i>United Kingdom</i> are relevant.</p>
<b>A.8</b>	Not applicable.
<b>A.9</b>	<p><b>GROSS INCOME</b></p> <p><b>For operators (including ACDs and managers of unit trusts):</b></p> <p>gross income from the activity relating to fee-block A.9 is defined as:</p> <ul style="list-style-type: none"> <li>the amount of the annual charge on funds invested in <i>regulated</i> or <i>unregulated collective investment schemes</i> received or receivable in the latest accounting period (this is calculated as a % of funds invested, typically 1% p.a.);</li> </ul> <p><b>PLUS</b></p> <ul style="list-style-type: none"> <li>the front-end or exit charge levied on sales or redemptions of <i>collective investment schemes</i> (typically 4-5% of sales/redemptions) in that same accounting period;</li> </ul> <p><b>PLUS</b></p> <ul style="list-style-type: none"> <li>any additional initial or management charges levied through a product wrapper such as a <i>PEP</i> or an <i>ISA</i>;</li> </ul> <p><b>BUT EXCLUDING</b> box management profits.</p> <p><b>For depositaries (including trustees of collective investment schemes and ICVC depositaries):</b></p> <p>The amount of the annual charge levied on funds in <i>regulated collective investment schemes</i> for which they act as <i>depository</i> (typically a % of the total funds for which they act as <i>depository</i>).</p> <p><b>Note:</b> Only the gross income corresponding to <i>United Kingdom</i> business is relevant.</p>
<b>A.10</b>	<p><b>NUMBER OF TRADERS</b></p> <p>Any <i>employee</i> or agent, who:</p> <ul style="list-style-type: none"> <li>ordinarily acts within the <i>United Kingdom</i> on behalf of an <i>authorised person</i> liable to pay fees to the <i>FSA</i> in its fee-block A.10 (firms dealing as principal); and who,</li> <li>as part of their duties in relation to those activities of the <i>authorised person</i>, commits the <i>firm</i> in market dealings or in transactions in <i>securities</i> or in other <i>specified investments</i> in the course of <i>regulated activities</i>.</li> </ul>

<b>A.11</b>	Not applicable.
<b>A.12</b>	<p><b>APPROVED PERSONS</b></p> <p>The number of <i>persons</i> approved to undertake one, or more, of the following <i>customer functions</i>:</p> <p><b>CF21</b> <i>Investment adviser function;</i>  <b>CF22</b> <i>Investment adviser (trainee) function;</i>  <b>CF24</b> <i>Pension transfer specialist function;</i>  <b>CF25</b> <i>Adviser on syndicate participation at Lloyd's function;</i> or  <b>CF26</b> <i>Customer trading function.</i></p>
<b>A.13</b>	<p><b>APPROVED PERSONS</b></p> <p>The number of <i>persons</i> approved to undertake one, or more, of the following <i>customer functions</i>:</p> <p><b>CF21</b> <i>Investment adviser function;</i>  <b>CF22</b> <i>Investment adviser (trainee) function;</i>  <b>CF24</b> <i>Pension transfer specialist function;</i>  <b>CF25</b> <i>Adviser on syndicate participation at Lloyd's function;</i> or  <b>CF26</b> <i>Customer trading function.</i></p>
<b>A.14</b>	<p><b>APPROVED PERSONS</b></p> <p>The number of <i>persons</i> approved to undertake the following <i>controlled function</i>:</p> <p><b>CF23</b> <i>Corporate finance adviser function.</i></p>
<b>A.15</b>	Not applicable.
<b>A.16</b>	Percentage share of the amount paid towards <i>PIA's</i> 2001/2002 pensions review levy by fee-payers in fee-block A.16.
<b>A.17</b>	Not applicable.
<b>A.18</b>	Not applicable. [Note: will be made to come into effect from 31 October 2004.]
<b>A.19</b>	Not applicable. [Note: will be made to come into effect from 31 October 2004.]
<b>B. Market operators</b>	Not applicable.
<b>B. Service companies</b>	Not applicable.

### Part 3

This table indicates the valuation date for each fee-block. A *firm* can calculate its tariff data by applying the tariff bases set out in Part 2 above with reference to the valuation dates shown in this table.

Activity group	Valuation date
<p>IN THIS TABLE, REFERENCES TO SPECIFIC DATES OR MONTHS ARE REFERENCES TO THE LATEST ONE OCCURRING BEFORE THE START OF THE PERIOD TO WHICH THE FEE APPLIES, UNLESS OTHERWISE SPECIFIED – E.G. FOR 2004/05 FEES (1 APRIL 2004 TO 31 MARCH 2005), A REFERENCE TO DECEMBER MEANS DECEMBER 2003</p>	
<p><b>A.1</b></p>	<p><b>For banks and e-money issuers:</b> Modified eligible liabilities (MELs), valued at:</p> <ul style="list-style-type: none"> <li>• for a <i>firm</i> which reports monthly, the average of the MELs for October, November and December;</li> <li>• for a <i>firm</i> which reports quarterly, the MELs for December.</li> </ul> <p><b>For credit unions:</b> MELs, valued at December or as disclosed by the most recent annual return made prior to that date.</p> <p><b>For building societies:</b> MELs, valued at the average of the MELs for October, November and December.</p>
<p><b>A.2</b></p>	<p>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</p>
<p><b>A.3</b></p>	<p>Annual gross <i>premium</i> income (GPI), valued at the period to which the most recent annual return relates [Note: for most <i>firms</i> this will be the 12 <i>months</i> ended 31 December].</p> <p><b>AND</b></p> <p>Gross technical liabilities (GTL) valued at the end of the period to which the most recent annual return related [Note: for most <i>firms</i> this will be the 12 <i>months</i> ended 31 December].</p>
<p><b>A.4</b></p>	<p>Adjusted annual gross <i>premium</i> income (AGPI) for the financial year ended in the calendar year ending 31 December.</p> <p><b>AND</b></p> <p>Mathematical reserves (MR) valued at the end of the financial year ended in the calendar year ending 31 December.</p>
<p><b>A.5</b></p>	<p>Active capacity (AC), in respect of the Underwriting Year (as reported to the <i>Society of Lloyd's</i>) which is current at the beginning of the period to which the fee relates.</p> <p>[Note: this is the Underwriting Year which is already in progress at the start of the fee period – e.g. for 2004/05 fees, the fee period will begin on 1 April 2004, which is in the 2004 Underwriting Year, so the AC for that Underwriting Year is the relevant measure.]</p>
<p><b>A.6</b></p>	<p>Not applicable.</p>
<p><b>A.7</b></p>	<p>Funds under management (FuM), valued at 31 December.</p>

<b>Activity group</b>	<b>Valuation date</b>
<b>A.8</b>	Not applicable.
<b>A.9</b>	Annual gross income (GI), valued at the most recent financial year ended before 31 December.
<b>A.10</b>	Number of traders as at 31 December.
<b>A.11</b>	Not applicable.
<b>A.12</b>	Relevant <i>approved persons</i> as at 31 December.
<b>A.13</b>	Relevant <i>approved persons</i> as at 31 December.
<b>A.14</b>	Relevant <i>approved persons</i> as at 31 December.
<b>A.15</b>	Not applicable.
<b>A.16</b>	Not applicable.
<b>A.17</b>	Not applicable.
<b>A.18</b>	Not applicable. [Note: will be made to come into effect from 31 October 2004.]
<b>A.19</b>	Not applicable. [Note: will be made to come into effect from 31 October 2004.]
<b>B. Market operators</b>	Not applicable.
<b>B. Service companies</b>	Not applicable.

Insert new SUP 20 Ann 2R:

**Fee tariff rates, permitted deductions and EEA/Treaty firm modifications for the period from 1 April 2004 to 31 March 2005**

**Part 1**

This table shows the tariff rates applicable to each fee-block.

(1)	For each activity group specified in the table below, the fee is the total of the sums payable for each of the tariff bands applicable to the <i>firm's</i> business, calculated as follows:
	(a) the relevant minimum fee; plus
	(b) an additional fee calculated by multiplying the <i>firm's</i> tariff base by the appropriate rates applying to each tranche of the tariff base, as indicated.
(2)	A <i>firm</i> may apply the relevant tariff bases and rates to non-UK business, as well as to its UK business, if:



	(a)	it has reasonable grounds for believing that the costs of identifying the <i>firm's</i> UK business separately from its non-UK business in the way described in Part 2 of SUP 20 Ann 1R are disproportionate to the difference in fees payable; and
	(b)	it notifies the FSA in writing at the same time as it provides the information concerned under SUP 20.3 (Information on which fees are calculated), or, if earlier, at the time it pays the fees concerned.
(3)		For a <i>firm</i> which has not complied with SUP 20.3.2R (Information on which fees are calculated) for this period:
	(a)	the fee is calculated using (where relevant) the valuation or valuations of business applicable to the previous period, multiplied by the factor of 1.10;
	(b)	an additional administrative fee of £250 is payable; and
	(c)	the minimum total fee (including the administrative fee in (b)) is £350.

Activity group	Fee payable
A.1	[to be made later]
A.2	[to be made later]
A.3	[to be made later]
A.4	[to be made later]
A.5	[to be made later]
A.6	[to be made later]
A.7	[to be made later]
A.8	This activity group does not apply for this period.
A.9	[to be made later]
A.10	[to be made later]
A.11	This activity group does not apply for this period.
A.12	[to be made later]
A.13	[to be made later]
A.14	[to be made later]
A.15	This activity group does not apply for this period.
A.16	[to be made later]
A.17	This activity group does not apply for this period.
A.18	[to be made later]
A.19	[to be made later]
B. Market operators	[to be made later]
B. Service companies	[to be made later]

## Part 2

This table shows the permitted deductions that apply:

Activity group	Nature of deduction	Amount of deduction
	[to be made later]	

### Part 3

This table shows the modifications to fee tariffs that apply to *incoming EEA firms* and *incoming Treaty firms*.

Activity group	Percentage of tariff payable under Part 1 applicable to the firm subject to a minimum amount payable of £100 (unless specified below)
A.1	20% (for a <i>firm</i> operating on cross-border services basis only, 0% and the minimum sum is not applicable)
A.3	0% and the minimum sum is not applicable
A.4	75%
A.7, A.8 and A.9	95%
A.10, A.11, A.12 and A.13	90%

Insert new SUP 20 Ann 3R:

### Transaction reporting fees and Article 54 RAO certificate fees for the period from 1 April 2004 to 31 March 2005

#### Part 1

This table shows the fees payable for transaction reporting.

Fee per transaction	Date payable	Method of payment
[to be made later]		

#### Part 2

The periodic fee payable under *SUP 20.6.1R* for a certificate issued under Article 54 of the *Regulated Activities Order* is [to be made later].

## Annex D

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text

13.5.10G Since a *firm* that becomes a *participant firm* in the course of a financial year of the *compensation scheme* will already be obtaining a discount in relation to the *base costs levy* and the *establishment costs levy* through the modified fee provisions of *SUP 20.4.34R*, no rule is necessary in *COMP* for discounts on the *base costs levy* or the *establishment costs levy*.

...

13.6.7R When calculating a *participant firm's* share of a *compensation costs levy* or *specific costs levy* allocated to:

(1) ...

(2) the investment business *sub-scheme*, the *FSCS* must (unless (3) applies) use as the *contribution groups* and tariff bases the correspondingly numbered activity groups and tariff bases set out in part 71 and part 2 of *SUP 20 Ann 1R* which are identified in *COMP 13.6.9R*;

(3) ...

...

13.6.9R Table: The contribution groups and tariff bases for the investment business sub-scheme (see *COMP 13.6.7R(2)*). (The contributions groups, legal bases for activity and tariff bases are the same as the correspondingly numbered activity groups and tariff bases set out in part 71 and part 2 of *SUP 20 Ann 1R*).

SUB-SCHEME	CONTRIBUTION GROUP (references to A7 etc are to the activity groups in part <u>71</u> of <i>SUP 20 Ann 1R</i> )	LEGAL BASIS FOR ACTIVITY (this is merely a summary of the basis in part <u>71</u> of <i>SUP 20 Ann 1R</i> ; references to articles are to articles of the <i>Regulated Activities Order</i> )	TARIFF BASE (this is merely a summary of the base in part <u>72</u> of <i>SUP 20 Ann 1R</i> )
...	...	...	...

## Annex E

### Amendments to the Collective Investment Schemes sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text

18.2.4R A periodic fee must be paid using one of the payment methods specified in ~~part 1 of SUP 20 Annex 1R~~ SUP 20.2.7AR.

## Annex F

### Amendments to the Credit Unions sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text

Schedule 3  
Fees and other required payments

...

<b>Description of fee</b>	<b>Reference</b>
...	...
Schedule of periodic fees payable	<i>SUP 20 Ann <del>12</del>R Part <u>21</u></i>
...	...

**SUPERVISION MANUAL (REPORTING AND AUDIT REQUIREMENTS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (the “Act”):
- (1) section 138 (General rule-making power);
  - (2) section 150(2) (Actions for damages);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2005, except as indicated in the table below.

<b>Handbook Provision</b>	<b>Commencement date</b>
<p>The provisions in Part 1 of Annex A that relate to mortgage lenders, mortgage intermediaries and mortgage administrators</p> <p>Transitional provision 10A in Part 2 of Annex A (in respect of mortgage mediation activities);</p> <p>Transitional provision 12F in Part 2 of Annex A.</p>	31 October 2004
<p>The provisions in Part 1 of Annex A that relate to insurance intermediaries and exempt insurance intermediaries</p> <p>Transitional provision 10A in Part 2 of Annex A (in respect of insurance mediation activities)</p> <p>The Glossary definition for ‘exempt insurance intermediary’ in Annex B</p>	14 January 2005

**Amendments to the Supervision manual (SUP)**

D. SUP is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

F. This instrument may be cited as the Supervision Manual (Reporting and Audit Requirements) Instrument 2004.

By order of the Board  
18 March 2004

Amended by Addendum  
18 March 2005

Amended by Second Addendum  
29 September 2005

**Contents of annexes to this instrument**

**ANNEX A**

**Part 1            Amendments to SUP Transitional Provisions**

**Part 2            Amendments to SUP 3**

**Part 3            Amendments to SUP 16 (excluding annexes)**

**Part 4            SUP 16 Ann 18AR**

**Part 5            SUP 16 Ann 18BG**

**Part 6            SUP 16 Ann 19AR**

**Part 7            SUP 16 Ann 19BG**

**Part 8            SUP 16 Ann 20G**

**Part 9            SUP 16 Ann 21R**

**ANNEX B        Amendments to the Glossary**



## ANNEX A

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

#### Part 1: Amendments to SUP Transitional Provisions

Insert the following new transitional provisions in the correct sequential order.

##### SUP 2 Table

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
10A	SUP 16.4 SUP 16.5	R	SUP 16.4 (Annual controllers report) and 16.5 (Annual close links report) do not apply to a <i>firm</i> with <i>permission</i> to carry on only <i>insurance mediation activity, mortgage mediation activity, or both</i> .	(1) in respect of <i>mortgage mediation activities</i> , 31 October 2004 - 31 March 2005;  (2) in respect of <i>insurance mediation activities</i> , 14 January 2005 - 31 March 2005.	1 April 2005
12B	SUP 16.7.7R; SUP 16.7.9R;  SUP 16.7.11R;  SUP 16.7.16R;  SUP 16.7.20R;  SUP 16.7.24R;  SUP 16.7.26R;  SUP 16.7.28R;  SUP 16.7.35R;	R	(1) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-yearly basis, and the <i>firm</i> has:  (a) annual income of less than £5m but more than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity and retail investment activity</i> , and  (b) an <i>accounting reference date</i> which  (i) falls between 31 December 2004 and 31 March 2005; or  (ii) falls between 30 June 2005 and 30 September 2005  this must be read as a reference to providing the first return in accordance with SUP TR 12CR.  (2) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-	From 1 April 2005	1 April 2005

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
	<p>SUP 16.7.54R;</p> <p>SUP 16.7.57R;</p> <p>SUP 16.7.62R;</p> <p>SUP 16.7.65R;</p> <p>SUP 16.7.73R;</p> <p>SUP 16.7.76R</p> <p>SUP 16.7.79R</p> <p>SUP 16.7.80R</p>		<p>yearly basis, and the <i>firm</i> has:</p> <p>(a) annual income of less than £5m but more than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity and retail investment activity</i>, and</p> <p>(b) an <i>accounting reference date</i> which is not within (1)(b);</p> <p>the first return must cover the <i>firm's</i> first full financial half-year which starts on or after 1 April 2005 and be submitted 30 <i>business days</i> after period end.</p> <p>(3) Where a <i>firm</i> is carrying on <i>regulated activities</i> before 1 April 2005 and is required under a <i>rule</i> in SUP 16.7 to submit information using the <i>MLAR</i>, the first return must cover the <i>firm's</i> first full financial quarter which starts on or after this date and be submitted 20 <i>business days</i> after period end.</p> <p>(4) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-yearly basis, and the <i>firm</i> has:</p> <p>(a) annual income of less than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity and retail investment activity</i>, and</p> <p>(b) an <i>accounting reference date</i> which falls between 1 January 2005 and 31 December 2005 the relevant <i>rule</i> must be read as requiring the first return to be provided in accordance with SUP TR 12DR.</p>		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
12C		R	If SUP TR 12B R (1) - (3) applies, the <i>firm's</i> first return must be provided as follows:					
			<i>Accounting reference date</i>	<i>Reporting period starts</i>	<i>Reporting period ends</i>	<i>Return to be provided</i>		
			Between 30 June 2005 and 30 September 2005	1 April 2005	<i>Accounting reference date</i> within 2005	30 <i>business days</i> after period end.		
			Between 31 December 2004 and 31 March 2005	1 April 2005	6 months after <i>accounting reference date</i> within 2005	30 <i>business days</i> after period end		
12D		R	(1) If SUP TR 12BR (4) applies, the <i>firm's</i> first return must be provided as follows:					
			<i>Accounting reference date</i>	<i>Reporting period starts</i>	<i>Reporting period ends</i>	<i>Return to be provided</i>		
			Between 31 December 2004 and 31 March 2005	1 April 2005	6 months after <i>Accounting reference date</i> within 2005	30 <i>business days</i> after period end (Note 1)		
			Between 1 April 2005 and 29 June 2005	the business day following <i>accounting reference date</i> within 2005	6 months after <i>Accounting reference date</i> within 2005	30 <i>business days</i> after period end. (Note 1)		
			Between 30 June 2005 and 29 September 2005	1 April 2005	<i>Accounting reference date</i> within 2005	30 <i>business days</i> after period end		
			Between 30 September 2005 and 30 December 2005	6 months preceding <i>accounting reference date</i> within 2005	<i>Accounting reference date</i> within 2005	30 <i>business days</i> after period end		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
12E		R	(2) If SUP TR 12BR (4) applies, the firm's second return must be provided as follows:					
			Between 30 June 2005 and 29 September 2005	the business day following accounting reference date within 2005	6 months after Accounting reference date within 2005	30 business days after period end  (Note 1)		
12F	SUP 16.7.77R	R	A mortgage administrator or mortgage lender must submit an annual report and audited accounts annually, 3 months after the firm's accounting reference date				31 October 2004 - 31 March 2005	1 April 2005
14A	SUP 16.11.7R	R	Until 1 July 2006, a firm will not contravene SUP 16.11.7R if it does not complete the data reporting field 'Advice at the point of sale' (see SUP 16 Ann 21R).				1 April 2005 – 30 June 2006	1 April 2005

Note 1 = The return need not provide data for sections A, B, C, D, E of the RMAR.

## Part 2: Amendments to SUP 3

### 3.1.2 R Table Applicable sections (see SUP 3.1.1R)

(1) Category of firm	(2) Sections applicable to the firm	(3) Sections applicable to its auditor
...		
(9) <u>Mortgage lender</u>	<u>SUP 3.1- SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8</u>
(10) <u>Insurance intermediary (other than an exempt insurance intermediary) to which CASS 5 (Client money and mandates) (except for CASS 5.2 (Holding money as agent)) applies (see Note 4)</u>	<u>SUP 3.1 - SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8, SUP 3.10</u>
(11) <u>Exempt insurance intermediary and insurance intermediary not subject to SUP 3.1.2R (10) which has an auditor appointed under or as a result of a statutory provision other than in the Act</u>	<u>SUP 3.1, SUP 3.2, SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8</u>
(12) <u>Mortgage intermediary or mortgage administrator which has an auditor appointed under or as a result of a statutory provision other than in the Act.</u>	<u>SUP 3.1, SUP 3.2, SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8</u>
Note 1 - ...		
Note 4	<p>The <u>client money</u> audit requirement in SUP 3.1.2R(10) therefore applies to all <u>insurance intermediaries</u> except:</p> <ul style="list-style-type: none"> <li>• <u>those which do not hold client money or other client assets in relation to insurance mediation activities; or</u></li> <li>• <u>those which only hold up to, but not exceeding, £30,000 of client money under a statutory trust arising under CASS 5.3.</u></li> </ul> <p><u>Insurance intermediaries</u> which, in relation to <u>insurance mediation activities</u>, hold no more than that amount of <u>client money</u> only on a statutory trust are <u>exempt insurance intermediaries</u>.</p>	

...

3.1.2A G If a firm falls within more than one row in column (1) of the table in SUP 3.1.2R, SUP 3.1.1R requires the firm and its external auditor to comply with

all the sections referred to in column (2) or (3). For example, a bank which carries on designated investment business which is also a mortgage lender, falls in rows (4) and (9). Therefore, the bank must comply with SUP 3.1 to SUP 3.7, and its external auditor must comply with SUP 3.1, SUP 3.2, SUP 3.8 and SUP 3.10.

3.2.4 G SUP 3.1.1R and SUP 3.1.2R limit the application of this chapter in relation to:

- (1) *authorised professional firms* to which COB 9.1 (Custody) and COB 9.3 (Client money) do not apply or which are not required by IPRU(INV) 2.1.2R to comply with chapter 3, 5, 10 or 13 of IPRU(INV);
- (2) *oil market participants, and energy market participants, to whom IPRU(INV) 3 does not apply;*
- (3) *small personal investment firms; and*
- (4) *service companies;*
- (5) *exempt insurance intermediaries;*
- (6) *insurance intermediaries not subject to SUP 3.1.2R (10);*
- (7) *mortgage intermediaries; and*
- (8) *mortgage administrators.*

~~Such a firm is~~ Such firms are not required, under this chapter, to appoint an auditor because SUP 3.3 (Appointment of auditors) does not apply. If such a firms appoints an auditor under or as a result of a statutory provision other than in the Act, for example, under the Companies Act 1985, SUP 3.7 (Notification of matters raised by auditor) and SUP 3.8 (Rights and duties of all auditors) nevertheless apply to help the FSA discharge its functions under the Act. See SUP 3.1.2R, Note 4, for further clarification concerning insurance intermediaries and those which qualify as exempt insurance intermediaries.

3.2.5 G It is the responsibility of an insurance intermediary's senior management to determine, on a continuing basis, whether the insurance intermediary is an exempt insurance intermediary for the purposes of this requirement and to appoint an auditor if management determines the firm is no longer exempt. SUP 3.7 (amplified by SUP 15) sets out what a firm should consider when deciding whether it should notify the FSA of matters raised by its auditor.

3.2.6 G The rights and duties of auditors are set out in SUP 3.8 (Rights and duties of all auditors) and SUP 3.10 (Duties of auditors: notification and report on client assets). SUP 3.8.10G includes the auditor's statutory duty to report certain matters to the FSA imposed by regulations made by the Treasury

under sections 342(5) and 343(5) of the Act (information given by auditor or actuary to the FSA). An auditor should bear these rights and duties in mind when carrying out *client* asset report work, including whether anything should be notified to the FSA immediately.

...

### 3.10.5 R Table Client assets report

Whether in the auditor's opinion	
(1)	the <i>firm</i> has maintained systems adequate to enable it to comply with the rules in <i>COB</i> 9.1 to <i>COB</i> 9.4 and <i>CASS</i> 5.1 to <i>CASS</i> 5.8 (except <i>CASS</i> 5.2) throughout the period since the last date as at which a report was made;
(2)	the <i>firm</i> was in compliance with the rules in <i>COB</i> 9.1 to <i>COB</i> 9.4 and <i>CASS</i> 5 (except <i>CASS</i> 5.2), at the date as at which the report has been made;
(3)	in the case of an <i>investment management firm</i> , <i>personal investment firm</i> a <i>UCITS management company</i> or <i>securities and futures firm</i> ...; and
(4)	if there has been a <i>secondary pooling event</i> during the period, the <i>firm</i> has complied with the rules in <i>COB</i> 9.5 and <i>CASS</i> 5.6 (Client money distribution) in relation to that pooling event.

3.10.7 R An auditor must deliver a report under *SUP* 3.10.4R to the *FSA* so as to be received within four months of the end of each period covered, unless it is the auditor of a *firm* falling within category (10) of *SUP* 3.1.2R.

...

3.10.8A R The auditor of a *firm* falling within category (10) of *SUP* 3.1.2R must deliver a report under *SUP* 3.10.4R:

(1) to the *firm* so as to be received within four months of the end of each period covered; and

(2) to the *FSA* upon request within six years of the end of the period covered.

3.10.8B G The rights and duties of auditors are set out in *SUP* 3.8 (Rights and duties of all auditors) and *SUP* 3.10 (Duties of auditors: notification and report on client assets). *SUP* 3.8.10G also refers to the auditor's statutory duty to report certain matters to the *FSA* imposed by regulations made by the

Treasury under sections 342(5) and 343(5) of the Act (information given by auditor or actuary to the FSA). An auditor should bear these rights and duties in mind when carrying out *client* asset report work, including whether anything should be notified to the FSA immediately.

3.10.8C G It is the responsibility of an *insurance intermediary's* senior management to determine, on a continuing basis, whether the *firm* is an *exempt insurance intermediary* for the purposes of this requirement and to appoint an auditor if management determines the *firm* is no longer exempt. SUP 3.7 (amplified by SUP 15) sets out what a *firm* should consider when deciding whether it should notify the FSA of matters raised by its auditor.



**Part 3: Amendments to SUP 16**

16.1.3 R

(1) Section(s)	(2) Categories of firm to which section applies	(3) Applicable rules and guidance
...		
<i>SUP 16.4</i> and <i>SUP 16.5</i>	All categories of <i>firm</i> except: ... (h) a <i>UCITS qualifier</i> ; (i) <u>a firm with permission to carry on only retail investment activities</u> ; (j) <u>a firm with permission to carry on only insurance mediation activity, mortgage mediation activity, or both</u> ; (k) <u>a firm falling within both (i) and (j)</u>	Entire sections
...		
<i>SUP 16.7</i>	...	
	<i>Personal investment firm</i>	<i>SUP 16.7.42R</i> to <i>SUP 16.7.53R</i>
...		
	<i>Insurer</i> <i>Friendly society</i>	<i>SUP 16.7.73R</i> to <i>SUP 16.7.75R</i>
	<u>A firm not subject to other reporting requirements in SUP 16.7:</u> <u>(1) with permission to carry on one or more of:</u> (a) <u>insurance mediation activity</u> ; or (b) <u>mortgage mediation activity</u> ; or (c) <u>mortgage lending</u> ; or	<i>SUP 16.7.76R</i> to <i>SUP 16.7.81G</i>

	<p><u>(d) mortgage administration; or</u></p> <p><u>(2) which is a retail investment firm</u></p>	
...		
<u>SUP 16.11</u>	<p><u>A firm, other than a managing agent, which is:</u></p> <p><u>(1) a mortgage lender; or</u></p> <p><u>(2) an insurer; or</u></p> <p><u>(3) the operator of a regulated collective investment scheme or an investment trust savings scheme; or</u></p> <p><u>(4) a person who issues or manages the relevant assets of the issuer of a structured capital-at-risk product.</u></p>	<u>Entire section</u>

...

16.3.2 G This chapter has been split into ~~six~~ eight sections, covering:

...

- (5) persistency reports (*SUP 16.8*); ~~and~~
- (6) annual appointed representatives reports (*SUP 16.9*);
- (7) confirmation of standing data (*SUP 16.10*); and
- (8) product sales data reporting (*SUP 16.11*).

...

16.3.13R ...

- (4) If the due date for submission of a report required by this chapter is a set period of time after the end of a half-year, a quarter, or a month, the dates will be determined by (a) or (b) below except where otherwise indicated:

- (a) the firm's accounting reference date;
- (b) monthly, 3 monthly or 6 months after the firm's accounting reference date, as the case may be.

- 16.7.2G (1) Financial reporting requirements for insurers, excluding friendly societies are set out in IPRU(INS). For their other reporting requirements, see SUP 16.7.73R -16.7.75R.
- (2) Financial reporting requirements for friendly societies are set out in IPRU(FSOC). For their other reporting requirements, see SUP 16.7.73R -16.7.75R.

**Purpose**

16.7.3G .....  
*Principle 4* requires firms to maintain adequate financial resources, and the Interim Prudential sourcebooks (or, in the case of firms with permission to carry on insurance mediation activity, mortgage mediation activity, or both, PRU) set out the FSA's detailed capital adequacy requirements. By submitting regular financial reports, firms enable the FSA to monitor their compliance with *Principle 4* and with the detailed requirements of the Interim Prudential sourcebooks or PRU, as the case may be. These reports also help the FSA to analyse firms' financial condition and performance and to understand their business. By means of further collation and review of the data which those reports provide, the FSA also uses the reports to identify developments across the financial services industry and its constituent sectors.

...

16.7.5G

Table Applicable rules and guidance on financial reports (see SUP 16.7.1G)

Firm category	Applicable rules and guidance
...	
<i>Personal investment firm</i>	<del>SUP 16.7.42G – SUP 16.7.53G</del>
<i>Authorised professional firm</i> (Note 2)	<del>SUP 16.7.54R – SUP 16.7.54AR</del>
...	
<i>Insurer</i> <i>Friendly society</i>	<u>SUP 16.7.73R – SUP 16.7.75R</u>

<p><u>A firm, not subject to other reporting requirements in SUP 16.7:</u></p> <p>(a) <u>with permission to carry on one or more of:</u></p> <p>(1) <u>insurance mediation activity; or</u></p> <p>(2) <u>mortgage mediation activity; or</u></p> <p>(3) <u>mortgage lending; or</u></p> <p>(4) <u>mortgage administration; or</u></p> <p>(b) <u>which is a retail investment firm.</u></p>	<p><u>SUP 16.7.76R – SUP 16.7.81G</u></p>
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...

**Compulsory electronic submission of certain reports to the FSA**

16.7.6AR A firm which is required by this section to submit an *RMAR* or an *MLAR* must provide the relevant data specified in SUP 16 Ann 18AR or 19AR respectively by electronic means made available by the *FSA*.

16.7.6BG The *RMAR* is relevant to the reporting requirements of firms carrying on insurance mediation activity, mortgage mediation activity or retail investment activity. The *MLAR* is relevant to firms carrying on mortgage lending or mortgage administration.

16.7.6CR Where reference is made in SUP 16.7 to adequate information relating to the following activities:

- (1) insurance mediation activity; or
- (2) mortgage mediation activity; or
- (3) retail investment activity;

this includes all sections of the *RMAR* in addition to those relating to financial reports, except where otherwise indicated.

16.7.6DG The *RMAR* comprises sections relating both to financial reporting and other sections (e.g. Training and Competence and *COB* data).

16.7.6EG Where SUP 16.7 requires a report containing adequate information on one or more of the following activities:

(1) insurance mediation activity;

(2) mortgage mediation activity;

(3) mortgage lending;

(4) mortgage administration;

(5) retail investment activity;

a firm should submit a report only if it carries on at least one of those activities.

...

16.7.8R

Table ~~Financial r~~Reports from a UK bank (see SUP 16.7.7R)

Content of report	Form or Return (Note 1)	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  (1) <u>insurance mediation activity;</u>  (2) <u>mortgage mediation activity;</u>  (3) <u>retail investment activity.</u>	<u>RMAR</u> (excluding sections A, B, C, D, E)	<u>Half yearly</u>	<u>30 business days after period end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u> (excluding A1, A2, B1 and C)	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1= When giving the report required, a *bank* must use the form or return indicated, if any. The content of the form has the status of *guidance* on the type of information that should be provided to meet the reporting obligation. A copy of the form is located at SUP 16 Ann 1R. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

...

16.7.10R

Table ~~Financial r~~Reports from an EEA Bank (see SUP 16.7.9R)

Content of report	Form or Return (Note 1)	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  (1) <u>insurance mediation activity;</u>  (2) <u>mortgage mediation activity;</u>  (3) <u>retail investment activity.</u>	<u>RMAR</u> (excluding <u>A, B C, D, E</u> )	<u>Half yearly</u>	<u>30 business days after period end</u>
<u>Adequate information relating to mortgage lending and mortgage administration</u>	<u>MLAR</u> (excluding <u>A1, A2, B1, C</u> )	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a *bank* must use the form or return indicated, if any. The content of the form has the status of *guidance* on the type of information that should be provided to meet the reporting obligation. A copy of the form is located at SUP 16 Ann 1R. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

...

16.7.12R

Table ~~Financial~~ Reports from a bank established outside the EEA (see SUP16.7.11R)

Content of report	Form or Return (Note 1)	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  (1) <u>insurance mediation activity;</u>  (2) <u>mortgage mediation activity;</u>  (3) <u>retail investment activity.</u>	<u>RMAR</u> (Note 3)	<u>Half yearly (quarterly for sections A to E for larger firms, subject to Note 3 exemptions)</u>  (Note 2)	<u>For half yearly report: 30 business days after period end.</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration</u>	<u>MLAR</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a *bank* must use the form or return indicated, if any. The content of the form has the status of *guidance* on the type of information that should be provided to meet the reporting obligation. A copy of the form is located at SUP 16

Ann 1R. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

Note 2 = For the purposes of RMAR reporting, a larger firm is a firm whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a firm's total revenue relating to insurance mediation activity, mortgage mediation activity and retail investment activity.

Note 3 = A firm which submits an MLAR is not required to submit sections A and B of the RMAR.

...

16.7.17R

Table ~~Financial~~ Reports from a building society (see SUP 16.7.16R)

Content of report	Form or Return (Note 1)	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  <u>(1) insurance mediation activity;</u>  <u>(2) mortgage mediation activity;</u>  <u>(3) retail investment activity.</u>	<u>RMAR</u> (excluding sections A, B, C, D, E)	<u>Half yearly</u>	<u>30 business days after period end.</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u> (excluding <u>A1, A2, B1 and C</u> )	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a *building society* must use the form or return indicated, if any. The content of the form has the status of *guidance* on the type of information that should be provided to meet the reporting obligation. A copy of the form is located at SUP 16 Ann 3R for all reports (except the “Analysis of interest rate gap” for which no form is provided). The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

...

16.7.21R

Table ~~Financial~~ Reports required from service companies (see SUP16.7.20R)

Report	Frequency	Due date
Annual audited financial statements	Annually	6 months after the <i>firm's accounting reference date</i>

...

#### 16.7.25R

Table ~~Financial~~ Reports required from a securities and futures firm which is a category A or B firm or a broad scope firm (see SUP 16.7.24R)

Report	Return	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  (1) <i>insurance mediation activity</i> ;  (2) <i>mortgage mediation activity</i> ;  (3) <i>retail investment activity</i> .	<u>RMAR</u> (excluding sections A, B, C, E) (Note 5)	<u>Half yearly</u> (quarterly for section D for larger firms)  (Note 6)	<u>For half yearly report: 30 business days after period end</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration</u>	<u>MLAR</u> (excluding A1, A2 and B1) (Note 5)	<u>Quarterly</u>	<u>20 business days after quarter end</u>

...

Note 5 = When giving the report required, a *firm* must use the return indicated. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

Note 6 = For the purposes of *RMAR* reporting, a larger *firm* is a *firm* whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a *firm's* total revenue relating to *insurance mediation activity, mortgage mediation activity and retail investment activity*.

...

#### 16.7.27R

Table ~~Financial~~ Reports required from a securities and futures firm which is a category C or D firm or an arranger or venture capital firm (see SUP16.7.26R)

Report	Return	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>	<u>RMAR</u> (excluding	<u>Half yearly</u> (quarterly for	<u>For half yearly report: 30 business</u>



<u>(1) insurance mediation activity;</u>	<u>sections A, B, C, E) (Note 5)</u>	<u>section D for larger firms)</u>	<u>days after period end</u>
<u>(2) mortgage mediation activity;</u>		<u>(Note 6)</u>	<u>For quarterly report: 30 business days after quarter end</u>
<u>(3) retail investment activity.</u>			
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR (excluding A1, A2 and B1) (Note 5)</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>

...

Note 5 = When giving the report required, a *firm* must use the return indicated. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

Note 6 = For the purposes of *RMAR* reporting, a larger *firm* is a *firm* whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a *firm's* total revenue relating to *insurance mediation activity, mortgage mediation activity and retail investment activity*.

...

#### 16.7.29R

~~Financial~~ Reports from a securities or futures firm which is an adviser, local or a traded options market maker (see SUP 16.7.28R)

Report	Return	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>	<u>RMAR (excluding sections A, B, C, E) (Note 1)</u>	<u>Half yearly (quarterly for section D for larger firms)</u>	<u>For half yearly report: 30 business days after period end</u>
<u>(1) insurance mediation activity;</u>		<u>(Note 2)</u>	<u>For quarterly report: 30 business days after quarter end</u>
<u>(2) mortgage mediation activity;</u>			
<u>(3) retail investment activity.</u>			
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR (excluding A1, A2 and B1) (Note 1)</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a firm must use the return indicated. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

Note 2 = For the purposes of RMAR reporting, a larger firm is a firm whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a firm's total revenue relating to insurance mediation activity, mortgage mediation activity and retail investment activity.

- 16.7.33R (1) Any report in SUP 16.7.23R to SUP 16.7.30R submitted to the FSA by a securities and futures firm must be signed by two authorised signatories satisfying the requirements of SUP 16.7.33R(2), except for:
- (a) the audited accounts of a subsidiary of the firm and the firm's audited annual; financial statements; and
  - (aa) reports in accordance with SUP 16 Ann 18AR or SUP 16 Ann 19AR; and
  - (b) other reports where the firm is a sole trader, when only one authorised signatory is required.

...

...

16.7.36R

Table ~~Financial~~ Reports from an investment management firm (see SUP 16.7.35R)

Report	Return	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u>  (1) <i>insurance mediation activity</i> ;  (2) <i>mortgage mediation activity</i> ;  (3) <i>retail investment activity</i> .	<u>RMAR</u> (excluding sections A, B, C, E) (Note 6)	<u>Half yearly</u> (quarterly for section D for larger firms)  (Note 7)	<u>For half yearly report: 30 business days after period end</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u> (excluding A1, A2 and B1) (Note 6)	<u>Quarterly</u>	<u>20 business days after quarter end</u>

...

Note 6 = When giving the report required, a firm must use the return indicated. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

Note 7 = For the purposes of RMAR reporting, a larger firm is a firm whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a firm's total revenue relating to insurance mediation activity, mortgage mediation activity and retail investment activity.

...

SUP 16.7.42G to SUP 16.7.53G inclusive are deleted.]

16.7.54R (1) An authorised professional firm must submit an annual questionnaire to the FSA every year in accordance with, and in the same format as, the form contained in SUP 16 Ann 9R, unless its only regulated activities are one or more of: -

(a) insurance mediation;

(b) mortgage mediation;

(c) retail investment.

...

(3) An authorised professional firm must also, where applicable, submit a report to the FSA in accordance with SUP 16.7.54AR.

#### 16.7.54AR

Table Reports from an authorised professional firm (see SUP16.7.54R)

<u>Report</u>	<u>Return (Note 1)</u>	<u>Frequency</u>	<u>Due date</u>
<u>Adequate information relating to the following activities:</u> (1) <u>insurance mediation activity;</u> (2) <u>mortgage mediation activity;</u> (3) <u>retail investment activity.</u>	<u>RMAR (Note 3)</u>	<u>Half yearly (quarterly for sections A to E for larger firms, subject to Note 3 exemptions)</u>  (Note 2)	<u>For half yearly report: 30 business days after period end</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a firm must use the return indicated. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

Note 2 = For the purposes of RMAR reporting, a larger firm is a firm whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a firm's total revenue relating to insurance mediation activity, mortgage mediation activity and retail investment activity.

Note 3 = A firm which submits an MLAR is not required to submit sections A and B of the RMAR.

...

16.7.58R

Table Financial Reports from a members' adviser (see SUP16.7.57R)

Report	Return (Note 1)	Frequency	Due date
...			
Quarterly reporting statement		Quarterly	15 business days after quarter end
<u>Adequate information relating to the following activities:</u>  (1) <u>insurance mediation activity;</u>  (2) <u>mortgage mediation activity;</u>  (3) <u>retail investment activity.</u>	<u>RMAR</u> (Note 3)	<u>Half yearly (quarterly for sections A to E for larger firms, subject to Note 3 exemptions)</u>  (Note 2)	<u>For half yearly report: 30 business days after period end</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1 = When giving the report required, a firm must use the return indicated. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

Note 2 = For the purposes of RMAR reporting, a larger firm is a firm whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a firm's total revenue relating to insurance mediation activity, mortgage mediation activity and retail investment activity.

Note 3 = A *firm* which submits an *MLAR* is not required to submit sections A and B of the *RMAR*.

...

16.7.63R

Table Financial Reports required from a credit union (see SUP16.7.62R)

Content of report	Form or Return	Frequency	Due date
Key financial data	CQ	Quarterly	One <i>month</i> after quarter end
Extended financial data	CY	Annually	Seven <i>months</i> after the financial year end
<u>Adequate information relating to the following activities:</u>  (1) <i>insurance mediation activity</i> ;  (2) <i>mortgage mediation activity</i> ;  (3) <i>retail investment activity</i> .	<u>RMAR</u> (excluding sections A, B, C, E)  (Note 1)	<u>Half yearly</u> (quarterly for section D for larger firms)  (Note 2)	<u>For half yearly report: 30 business days</u> after period end  <u>For quarterly report: 30 business days</u> after quarter end
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u> (excluding A1, A2, B1 and C)  (Note 1)	<u>Quarterly</u>	<u>20 business days</u> after quarter end

Note 1 = When giving the report required, a *firm* must use the return indicated. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

Note 2 = For the purposes of *RMAR* reporting, a larger *firm* is a *firm* whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a *firm's* total revenue relating to *insurance mediation activity*, *mortgage mediation activity* and *retail investment activity*.

16.7.63A G Guidance Notes for the completion of the reports are contained in SUP 16 Ann 15 G, SUP 16 Ann 18BG and SUP 16 Ann 19BG.

...

16.7.66R

Table Financial Reports from an ELMI (see SUP16.7.65R)

Content of report	Form or Return (Note 1)	Frequency	Due date
...			
<u>Adequate information relating to the following activities:</u> (1) <i>insurance mediation activity;</i> (2) <i>mortgage mediation activity;</i> (3) <i>retail investment activity.</i>	<u>RMAR</u> (excluding sections A, B, C, D, E)	<u>Half yearly</u>	<u>30 business days after period end</u>
<u>Adequate information relating to mortgage lending and mortgage administration</u>	<u>MLAR</u> (excluding A1, A2, B1 and C)	<u>Quarterly</u>	<u>20 business days after quarter end</u>

Note 1=When giving the report required, an *ELMI* must use the form or return indicated (if any).

A copy of forms BSD 3 and ELM-CA/LE are set out in SUP 16 Annex 1R. The RMAR and MLAR are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

...

#### Insurers and friendly societies

16.7.73R If an *insurer* or a *friendly society* is carrying on any of the activities set out in SUP 16.7.74R, it must submit a report to the *FSA* in accordance with SUP 16.7.75R.

16.7.74R The activities referred to in SUP 16.7.73R are:

- (1) *insurance mediation activity;*
- (2) *mortgage mediation activity;*
- (3) *retail investment activity;*
- (4) *mortgage lending; and*
- (5) *mortgage administration.*

16.7.75R

Table Reports from an insurer or friendly society (see SUP 16.7.73R)

<u>Report</u>	<u>Return</u> (Note 1)	<u>Frequency</u>	<u>Due date</u>
<u>Adequate information relating to the following activities:</u>  (1) <u>insurance mediation activity;</u>  (2) <u>mortgage mediation activity;</u>  (3) <u>retail investment activity.</u>	<u>RMAR</u> (excluding sections <u>A, B, C,</u> <u>D, E)</u>	<u>Half yearly</u>	<u>30 business days</u> <u>after period end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u> (excluding <u>A1, A2,</u> <u>B1 and C)</u>	<u>Quarterly</u>	<u>20 business days</u> <u>after quarter end</u>

Note 1 = When giving the report required, a *firm* must use the return indicated. The *RMAR* and *MLAR* are located at SUP 16 Ann 18AR and Ann 19AR respectively and have the status of rules.

A firm not subject to other reporting requirements in SUP 16.7

16.7.76R A firm not subject to other reporting requirements in SUP 16.7,

(a) with permission to carry on one or more of:

(1) insurance mediation activity;

(2) mortgage mediation activity;

(3) mortgage lending;

(4) mortgage administration; or

(b) which is a retail investment firm;

must submit reports to the FSA in accordance with SUP 16.7.77R.

16.7.77R

Table Reports from a firm not subject to other reporting requirements in SUP 16.7

<u>Report</u>	<u>Return</u>	<u>Frequency</u>	<u>Due date</u>
---------------	---------------	------------------	-----------------

	<u>(Note 1)</u>		
<u>Adequate information relating to the following activities:</u>  <u>(1) insurance mediation activity;</u>  <u>(2) mortgage mediation activity;</u>  <u>(3) retail investment activity.</u>	<u>RMAR</u> <u>(Note 4)</u>	<u>Half yearly (quarterly for sections A to E for larger firms)</u>  <u>(Note 2)</u>  <u>(Note 3)</u>	<u>For half yearly report: 30 business days after period end.</u>  <u>For quarterly report: 30 business days after quarter end</u>
<u>Adequate information relating to mortgage lending and mortgage administration.</u>	<u>MLAR</u>	<u>Quarterly</u>	<u>20 business days after quarter end</u>
<u>If the firm is a mortgage lender or mortgage administrator, annual report and audited accounts.</u>	<u>N/A</u>	<u>Annually</u>	<u>3 months after the firm's accounting reference date</u>

Note 1 = When giving the report required, a *firm* must use the return indicated. The *RMAR* and *MLAR* are located at *SUP* 16 Ann 18AR and Ann 19AR respectively and have the status of *rules*.

Note 2 = For the purposes of *RMAR* reporting, a larger *firm* is a *firm* whose annual regulated business revenue in its previous financial year was greater than £5m. Annual regulated business revenue for these purposes is a *firm's* total revenue relating to *insurance mediation activity, mortgage mediation activity and retail investment activity*.

Note 3 = *Firms* categorised under *IPRU(INV)* 13 as A1, A2 or A3 should submit financial information (*RMAR* sections A, B, C, D and E) in accordance with *ISD* and *CAD* requirements, as follows:

<u>Category of firm</u>	<u>Frequency</u>	<u>Due date</u>
<u>Category A1</u>	<u>Monthly</u>	<u>15 business days after month end</u>
<u>Category A2</u>	<u>Quarterly</u>	<u>30 business days from the end of the relevant period.</u>
<u>Category A3</u>	<u>half yearly (quarterly for larger firms – Note 2)</u>	<u>30 business days from the end of the relevant period.</u>

Note 4 = A *firm* which submits an *MLAR* is not required to submit sections A and B of the *RMAR*.

16.7.78R Where a mortgage lender or mortgage intermediary establishes a special purpose vehicle, it must ensure that any report which the mortgage lender or mortgage intermediary makes in accordance with SUP 16.7.76R takes account of the activities of the special purpose vehicle as if those activities were the activities of the mortgage lender itself.

16.7.79R An incoming EEA firm which in the United Kingdom carries on only cross border services and is not subject to other reporting requirements in SUP 16.7 with permission to carry on:



- (1) insurance mediation activity; or
- (2) mortgage mediation activity; or
- (3) mortgage lending; or
- (4) mortgage administration; or
- (5) retail investment activity;

is subject to the requirements of SUP 16.10 only, and no requirements in respect of the RMAR or MLAR.

16.7.80R An incoming EEA firm with a branch in the United Kingdom, not subject to other reporting requirements in SUP 16.7, with permission to carry on:

- (1) insurance mediation activity; or
- (2) retail investment activity;

is required to provide such information relating to those activities as is specified in SUP 16 Ann 18BG and SUP 16 Ann 19BG.

16.7.81G SUP 16.7.80R is relevant, for example, to an insurance broker registered in another EEA State pursuant to the IMD, which exercises its EEA right to establish a branch in the United Kingdom and is not subject to other reporting requirements in SUP 16.7.

...

## 16.11 Product Sales Data Reporting

### Application

- 16.11.1R This chapter applies to a firm which is a *mortgage lender*; or  
in respect of sales to a *private customer* or a *retail customer*:
- (1) an *insurer*; or
  - (2) the *operator* of a *regulated collective investment scheme* or an *investment trust savings scheme*; or
  - (3) a *person* who issues or manages the relevant assets of the issuer of a *structured capital-at-risk product*,
- unless the *firm* is a *managing agent*.

### Purpose

- 16.11.2G
- (1) The purpose of this chapter is to set out the requirements for *firms* in the retail mortgage, investment, and *pure protection contract* markets specified in SUP 16.11.1R to report individual product sales data to the *FSA*. This requirement applies whether the *regulated activity* has been carried out by the *firm*, or through an intermediary which has dealt directly with the *firm*.
  - (2) The purpose of collecting this data is to assist the *FSA* in the ongoing supervision of *firms* engaged in retail activities and to enable the *FSA* to gain a wider understanding of market trends in the interests of protecting *consumers*.

### Reporting requirement

- 16.11.3R
- (1) A *firm* must submit a report (the 'data report') containing the information required by SUP 16.11.5R quarterly, within 20 *business days* of the end of the quarter, unless (3) applies.
  - (2) The reporting periods are the four calendar quarters of each year beginning on 1 January.
  - (3) A *firm* need not submit a data report if no relevant sales have occurred in the quarter.
- 16.11.4G
- (1) A *firm* may submit a data report more frequently than quarterly if it wishes.

- (2) If it is easier and more practical for a *firm* to submit additional data relating to products other than those specified in *SUP* 16.11.5R, it may submit that additional data to the *FSA* in a data report.

### **Content of the report**

- 16.11.5R The data report must contain sales data in respect of the following products:
- (1) *retail investments*;
  - (2) *pure protection contracts*; and
  - (3) *regulated mortgage contracts* (but not further advances).
- 16.11.6G *Guidance* on the type of products covered by *SUP* 16.11.5R is contained in *SUP* 16 Ann 20G.
- 16.11.7R The data report must comply with the provisions of *SUP* 16 Ann 21R.
- 16.11.8R The data report must relate both to transactions undertaken by the *firm* and to transactions undertaken by an intermediary which has dealt directly with the *firm*.
- 16.11.9R A *firm* must provide the data report to the *FSA* electronically in a standard format provided by the *FSA*.
- 16.11.10G A data report will have been provided to the *FSA* in accordance with *SUP* 16.11.9R only if all mandatory data reporting fields (as set out in *SUP* 16 Ann 21R) have been completed correctly and the report has been accepted by the relevant *FSA* reporting system.

### **Use of reporting agents**

- 16.11.11R
- (1) A *firm* may appoint another *person* to provide the data report on the *firm's* behalf if the *firm* has informed the *FSA* of that appointment in writing.
  - (2) Where (1) applies, the *firm* must ensure that the data report complies with the requirements of *SUP* 16.11 and identifies the originator of the transaction.

*SUP* 16 Ann 7R is deleted.

*SUP* 16 Ann 8G is deleted.

**Part 4: SUP 16 Ann 18AR**

## **Retail Mediation Activities Return ('RMAR')**

**Illustration of reporting requirements for firms carrying on retail mediation activities**

## Sup 16 Ann 18AR

## Retail Mediation Activities Return ('RMAR')

### SECTION A: Balance sheet

#### Fixed assets

Intangible assets	BS1	
Tangible assets	BS2	
Investments	BS3	
<b>TOTAL FIXED ASSETS</b>	<b>BS4</b>	BS1 + BS2 + BS3

#### Current assets

Stocks	BS5	
Debtors	BS6	
Investments held as current assets	BS7	
Cash at bank and in hand	BS8	
<b>TOTAL CURRENT ASSETS</b>	<b>BS9</b>	BS5 + BS6 + BS7 + BS8

#### Other assets

BS10
------

#### Liabilities: amounts falling due within one year

Bank loans and overdrafts	BS11
Other liabilities falling due within one year	BS12

<b>TOTAL AMOUNTS FALLING DUE WITHIN ONE YEAR</b>	<b>BS13</b>	BS11 + BS12
--	-------------	-------------

#### Net current assets

<b>BS14</b>	BS10 less BS13
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#### Total assets less current liabilities

<b>BS15</b>	BS4 + BS10.1 + BS14
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#### Other liabilities falling due after more than one year

BS16
------

#### Provisions for liabilities and charges

BS17
------

#### Net assets

<b>BS18</b>	(BS15 less BS16) less BS17
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#### Memo: guarantees provided by firm

BS19
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#### Memo: personal net assets

BS20
------

#### Capital and reserves

##### Capital account (incorporated businesses)

Ordinary share capital	BS21	
Preference share capital	BS22	
Share premium account	BS23	
Profit and Loss account	BS24	
Other reserves	BS25	
<b>TOTAL CAPITAL AND RESERVES</b>	<b>BS26</b>	BS21 + BS22 + BS23 + BS24 + BS25

Yes / No

Was the firm's last annual accounts audit report qualified?

BS27
------

##### Capital account (unincorporated businesses)

Sole trader/Partners' capital account	BS28	
Sole trader/Partners' current account	BS29	
<b>TOTAL CAPITAL AND RESERVES</b>	<b>BS30</b>	BS28 + BS29

**SECTION B: Profit and Loss account**

**B1: Regulated Business Revenue**

	Commissions		Fees	Other income	Regulated business
	Gross	Net		(reg activities)	revenue
Regulated mortgage contracts	PL1	PL2	PL3	PL4	PL5
Non-investment insurance	PL6	PL7	PL8	PL9	PL10
Retail investments	PL11	PL12	PL13	PL14	PL15
<b>TOTAL</b>	<b>PL16</b>	<b>PL17</b>	<b>PL18</b>	<b>PL19</b>	<b>PL20</b>

**B2: Other P&L**

Other Revenue (income from non-regulated activities)	<b>PL21</b>	
<b>TOTAL REVENUE</b>	<b>PL22</b>	PL20 + PL21
<b>TOTAL EXPENDITURE</b>	<b>PL23</b>	
<b>Profit/(Loss) on ordinary activities before taxation</b>	<b>PL24</b>	PL22 less PL23
<b>Profit/(Loss) on extraordinary activities before taxation</b>	<b>PL25</b>	
<b>Taxation</b>	<b>PL26</b>	
<b>Profit/(Loss) for the period before dividends and appropriations</b>	<b>PL27</b>	(PL24 + PL25) - PL26
<b>Dividends and other appropriations</b>	<b>PL28</b>	
<b>Retained Profit</b>	<b>PL29</b>	PL27 less PL28

**SECTION C: Client money and assets**

Have any notifiable issues been raised in relation to client money or other assets, either in the firm's last client assets audit report or elsewhere, that have not previously been notified to the FSA?

Yes / No

CM1

How is your client account(s) set up (tick all that apply)?

Non-investment insurance

Retail investments

Risk Transfer	Segregated Trusts	
	Statutory	Non-statutory
CM2	CM3	CM4
	CM5	

If not risk transfer:

Client money credit total as at reporting date

Client money debit total as at reporting date

Net client money balance as at reporting date

Non-investment insurance		Retail investments
Statutory	Non-statutory	Statutory
CM6	CM7	CM8
CM9	CM10	CM11
CM12	CM13	CM14

Yes / No

If non-statutory, has auditor's confirmation of systems and controls been obtained?

CM15

Yes / No

Is any client money invested (other than on deposit)?

CM16

Yes / No

Do you hold client money for business undertaken by an AR?

CM17

Does the firm hold any client assets (other than client money)?

Mortgage	Non-investment insurance	Retail investments
CM18	CM19	CM20

**SECTION D1: Regulatory Capital**

Is the firm exempt from these capital requirements in relation to any of its retail mediation activities?

Mortgage	Non-investment insurance	Retail investments
RC1	RC2	RC3

**Mortgage and non-investment insurance**

Base requirement  
5% of annual income (firms holding client money)  
2.5% of annual income (firms not holding client money)

Client money	Non-client money
RC4 (£10000)	RC5 (£5000)
RC6	
	RC7

**Capital requirement (higher of above)**

Other FSA capital requirements (if applicable)  
Additional capital requirements for PII (if applicable)

RC8	RC9
RC10	
RC11	

**TOTAL CAPITAL REQUIREMENT**

**TOTAL CAPITAL RESOURCES**

**TOTAL CAPITAL EXCESS/DEFICIT**

RC12	(RC8 or RC9) + RC10 + RC11
RC13	See notes
RC14	RC13 less RC12

**Eligible capital (mortgage and non-investment insurance)**

**Incorporated firms**

Share capital  
Audited reserves  
Interim net profits (audited)  
Interim net profits (not audited)  
Revaluation reserves  
Eligible subordinated loans  
**less** Investments in own shares  
**less** Intangible assets  
**less** interim net losses  
TOTAL CAPITAL RESOURCES

RC27
RC28
RC29
RC30
RC31
RC32
RC33
RC34
RC35
<b>RC36</b>

RC27 + RC28 + RC29 + RC31  
+ RC32 less RC33 less RC34  
less RC35

**IPRU(INV) requirements for personal investment firms (retail investment activities only)**

Category of personal investment firm under IPRU(INV)

RC15
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**Own funds requirement**

**Own funds**

**Surplus/deficit of own funds**

Additional own funds requirement for PII (if applicable)  
Other FSA capital requirements (if applicable)

RC16	A
RC17	B
RC18	C
RC19	
RC20	

**Adjusted net current assets requirement (if applicable)**

**Adjusted net current assets (if applicable)**

**Surplus/deficit (if applicable)**

RC21 (£1)	D
RC22	E
RC23	F

**Expenditure based requirement (if applicable)**

**Adjusted Capital/liquid capital (if applicable)**

**Surplus/deficit (if applicable)**

RC24	G
RC25	H
RC26	I

**Unincorporated firms**

Capital of a sole trader or partnership  
Eligible subordinated loans  
Personal assets not needed to meet non-business liabilities  
**less** Intangible assets  
**less** interim net losses  
**less** excess of drawings over profits for a sole trader or p'ship  
TOTAL CAPITAL RESOURCES

RC37
RC38
RC39
RC40
RC41
RC42
<b>RC43</b>

RC37 + RC38 + RC39 less  
RC40 less RC41 less RC42



**SECTION D2: FINANCIAL RESOURCES - NON-ISD PERSONAL INVESTMENT FIRMS**

<b>OWN FUNDS (TEST 1)</b>		<b>ADJUSTED NET CURRENT ASSETS (TEST 1A)</b>		<b>EXPENDITURE-BASED REQUIREMENT (TEST 2)</b>	
	£		£	£	£
1 Paid up share capital (excluding preference shares redeemable by shareholders within 2 years)		18 Net current assets (from balance sheet)		25 Total assets less total liabilities (from balance sheet)	
2 Share premium account		<b>less</b>		26 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part I adjustments required against assets	
3 Audited retained profits		19 Long term assets adjustment		27 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for subordinated loans	
4 Verified interim profits		20 Connected persons adjustment		28 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for indemnity commission	
5 Revaluation reserves		21 Investments adjustments		29 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for deficiencies in subsidiaries	
6 Short term subordinated loans				30 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for contingent liabilities	
7 Debt capital				31 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for foreign exchange risk	
8 Balances on proprietors' or partners' capital accounts				32 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for redeemable preference shares	
9 Balances on proprietors' or partners' current accounts				33 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II adjustment for derivatives	
10 Personal assets				34 IPRU(INV) Table 13.12.3(1)/ 13.12.3(2) Part II other adjustments against liabilities	
11 Less intangible assets					
12 Less material current year losses					
13 Less excess of current year drawings over current year losses					
14 PASS Loan Adjustments					
<b>15 OWN FUNDS (1+2+3+4+5+6+7+8+9+10-11-12-13+14)</b>	<b>B</b>	<b>22 ADJUSTED NET CURRENT ASSETS (18-19-20-21)</b>	<b>E</b>	<b>35 ADJUSTED CAPITAL/ LIQUID CAPITAL [(25+27)-26-28-29-30-31-32-33-34]</b>	<b>H</b>
16 Own funds requirement	A - £10,000	23 Requirement	D - £1	36 Expenditure requirement per IPRU(INV) 13.12	G
17 SURPLUS/(DEFICIT) (15-16)	C	24 SURPLUS/(DEFICIT) (22-23)	F	37 SURPLUS/(DEFICIT) (35-36)	I

**SECTION D3: FINANCIAL RESOURCES - ISD PERSONAL INVESTMENT FIRMS**

<b>OWN FUNDS (TEST 1)</b>		<b>ADJUSTED NET CURRENT ASSETS (TEST 1A)</b>		<b>EXPENDITURE-BASED REQUIREMENT (TEST 2)</b>	
1 Paid up ordinary share capital		23 Net current assets (from balance sheet)		30 Total assets less total liabilities (from balance sheet)	
2 Share premium account		24 Less: long term assets adjustment		31 Illiquid asset adjustments	
3 Audited reserves (excluding revaluation reserve)		25 Less: connected persons adjustment		32 Counterparty risk adjustments	
4 Verified interim profits		26 Less: investments adjustments		33 Position risk adjustments	
5 Non-cumulative preference shares (if not redeemable by shareholders within 5 years)				34 Foreign exchange risk adjustments	
6 Balances on proprietors' or partners' capital accounts				35 Preference shares adjustments	
7 Balances on proprietors' or partners' current accounts (audited or verified)				36 Large exposure risk adjustments	
<b>8 INITIAL CAPITAL (1+2+3+4+5+6+7)</b>				37 Long term subordinated loans	
9 Less: investment in own shares				38 Short term subordinated loans	
10 Less: intangible assets				<b>39 Sub total (30-31-32-33-34-35-36+37+38)</b>	
11 Less: material current year losses				40 Preference shares (5+16+18)	
12 Less: material holdings in credit and financial institutions				41 Table 13.3.2(2) own funds restrictions	
13 Less: excess of current year drawings over current year profits.				42 Balance A (38+40+41)	
<b>14 ORIGINAL OWN FUNDS (8-9-10-11-12-13)</b>				43 Balance B (14-33)	
15 Revaluation reserves				44 Balance C (43 x 250%)	
16 Cumulative preference share capital (if not redeemable by shareholders within 5 years)				<b>45 If Balance A is greater than Balance C , enter difference</b>	
17 Long-term subordinated loans					
18 Preference share capital (if not redeemable by shareholders within 2 years) and debt capital					
<b>19 OWN FUNDS (14+15+16+17+18)</b>	<b>B</b>	<b>27 ADJUSTED NET CURRENT ASSETS (23-24-25-26)</b>	<b>E</b>	<b>46 LIQUID CAPITAL (39-45)</b>	<b>H</b>
20 Own funds requirement IPRU(INV)13.3R	<b>A</b>	28 Requirement	<b>D: £1</b>	47 Expenditure based requirement per IPRU(INV)13.5R	<b>G</b>
21 Enter exchange rate € : £					
<b>22 OWN FUNDS SURPLUS/(DEFICIT) (19-20)</b>	<b>C</b>	<b>29 SURPLUS/(DEFICIT) (27-28)</b>	<b>F</b>	<b>48 SURPLUS/ (DEFICIT) (46-47)</b>	<b>I</b>

**SECTION D4: QUARTERLY FINANCIAL RESOURCES - CAD13 - ISD PERSONAL INVESTMENT FIRMS**

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- 1. Liquid capital from last year-end return (based on audited accounts)
- 2. Less: current year losses
- 3. Subordinated loans introduced
- 4. Subordinated loans repaid
- 5. Share capital/ proprietors' capital/ partners' capital introduced since the date of the last audited figures
- 6. Share capital/ proprietors' capital/ partners' capital withdrawn since the date of the last audited figures
- 7. Total: 1 - 2 + 3 - 4 + 5 - 6**
- 8. Less: expenditure based requirement (46)
- 9. Financial resources surplus/(deficit): 7 - 8**


**SECTION D5: ISD PERSONAL INVESTMENT FIRMS - REPORTABLE LARGE EXPOSURES & CALCULATION OF ADJUSTMENT**

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Counterparty	(£) Exposure	% exempt	£ Net large exposure
LE1	LE2	LE3	LE4
<b>TOTAL LARGE EXPOSURE</b>			LE5

**SECTION E: PII Self-Certification**

Is the firm exempt from the PII requirements in respect of any regulated activities? (tick as appropriate)

Mortgage advising/arranging	Non-inv insurance advising/arranging/dealing/assisting	Retail investment advising/arranging
PI1	PI2	PI3

If not exempt, has the firm renewed its PII cover since the last reporting date?

PI4	PI5	PI6
-----	-----	-----

Have any of the data items below changed since the last reporting date (or since you last notified the FSA of any changes)?

PI7	PI8	PI9
-----	-----	-----

If any of the data items have changed, please amend the following section as appropriate, in relation to each applicable PII policy:

What activities are covered by the policy?

Mortgage advising/arranging	PI10
Non-inv insurance advising/arranging/dealing/assisting	PI11
Retail investment advising/arranging	PI12
Is the cover compliant?	PI13
Annual premium	PI14
Limit of Indemnity - single claim/aggregate	PI15
Policy excess	PI16
Increased excess(es) for specific business types	PI17
Policy exclusion(s) for specific business types	PI18
Renewal date	PI19
Insurer name	PI20

Amount of additional capital required for increased excess(es) (where applicable, total amount for all PII policies)

PI22

**Personal investment firms only:**

Total amount of additional own funds required for policy exclusion(s)

PI23

Total of additional own funds required

PI24

Total of readily realisable own funds

PI25

Excess/deficit of readily realisable own funds

PI26

Y/N

Does the firm have any other PII policies?

PI21

## SECTION F: Threshold conditions

### Adequate resources

Does the firm have adequate resources in relation to its regulated activities?

THR1

### Close links

Are you exempt from close links reporting requirements?

THR2

If not, have there been changes to your close links since the FSA was last informed?

THR3

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

THR4

### Approved persons

Have there been changes to your approved persons' details since the FSA was last informed?

THR5

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

THR6

### Controllers

Are you exempt from the controllers reporting requirements?

THR7

If not, have there been changes to your controllers since the FSA was last informed?

THR8

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

THR9

**SECTION G: Training and Competence**

Total number of all staff

Of which:

Number of staff that give advice

Number of staff that supervise others to give advice

Number of advisers that have been assessed as competent

Number of advisers that have passed approved examinations

Number of advisers that have left since the last reporting date

Number of staff that take private customers through stakeholder pension scheme decision trees

Number of staff that supervise non-advised sales of lifetime mortgages

Number of staff that design filtering questions for non-advised sales of lifetime mortgages

Mortgages		Advising on non-investment insurance (retail customers)	Retail investments		Total
advising	arranging		advising	arranging	
					TC1
TC2		TC3	TC4		TC5
TC6		TC7	TC8		TC9
TC10		TC11	TC12		TC13
TC14			TC15		TC16
TC17		TC18	TC19		TC20
				TC21	TC22
	TC23				TC24
	TC25				TC26

**SECTION H: COB Data**

**Sources of business:** please tick all that apply, or confirm here that there have been  no changes since the last reporting date  no changes  COB1

- Marketing lists
- Referrals from non-authorised introducers
- Referrals from intermediaries
- Telephone sales
- Cold calling
- Sales visits
- Postal sales
- Direct offer financial promotions
- Repeat customers
- Internet Sales
- Other

	Non-inv Mortgage	insurance	Retail investments
COB2	COB3	COB4	
COB5	COB6	COB7	
COB8	COB9	COB10	
COB11	COB12	COB13	
COB14	COB15	COB16	
COB17	COB18	COB19	
COB20	COB21	COB22	
COB23	COB24	COB25	
COB26	COB27	COB28	
COB29	COB30	COB31	
COB32	COB33	COB34	

**Advertising**  
Does your firm approve financial promotions and/or qualifying credit promotions?  COB35  COB36  COB37

**Types of advertising:** please tick all that apply, or confirm here that there have been  no changes since the last reporting date  no changes  COB38

- Newspaper
- Magazine
- T.V.
- Radio
- Internet
- Other

	Non-inv Mortgage	insurance	Retail investments
COB39	COB40	COB41	
COB42	COB43	COB44	
COB45	COB46	COB47	
COB48	COB49	COB50	
COB51	COB52	COB53	
COB54	COB55	COB56	

Do you use one or more lists or panels of preferred product providers?  y/n  COB57

If yes, indicate the applicable types of business

	Non-inv Mortgage	insurance	Retail investments
COB58	COB59	COB60	

What (if known) is the total number of providers on the panel(s)?  COB61  
How often (if known) are the panel(s) reviewed?  COB62

**General COB data**

Do regulated activities form the core business of the firm?  COB63  
If not, specify type of core business:  COB64

Do you give independent advice?  COB65

**Clawed back commission (retail investment firms only)**

Clawed back commission by: Number  COB66  
Value  COB67

**Complaints**

Does the firm have complaints handling procedures?  y/n  COB 68

**Monitoring of Appointed Representatives ('ARs')**

Number of ARs registered with the firm  COB69  
Of which, number of 'secondary' ARs  COB70  
Of which, number of introducer ARs  COB71  
Number of advisers within ARs  COB72

(Only firms that have ARs)  
Does the firm have appropriate systems and procedures to ensure that the activities of its ARs are effectively monitored and controlled?  COB73

Number of ARs that have been subject to monitoring visits by the firm during the reporting period.  COB74

Number of ARs that have been subject to file reviews by the firm during the reporting period.  COB75

Number of ARs that have been subject to financial checks by the firm during the reporting period.  COB76

Has any other monitoring of ARs by the firm taken place?  COB77



**SECTION I: supplementary product sales data**

**(i) non-investment insurance product information**

- 1 Please indicate in column **A** each product type where the firm has advised or arranged transactions for retail customers during the reporting period
- 2 Please indicate in column **B** where the firm's retail business in the product type formed more than 40% by premium of all of its retail non-investment insurance activities.

**(ii) non-investment insurance chains**

- 3 Total non-investment insurance premium derived from retail customers SU85
- 4 Of this business, please indicate in column **C** the products where retail sales were passed up a chain and in column **D** where this business is significant\*
- 5 \*significant is where premium collected from being in a chain for this product amounts to
  - 1) more than 40% of the premium collected for all non-investment insurance activities with retail customers, or
  - 2) more than 40% of premium collected for all retail business in this product
- 6 Please also indicate in column **E** where the firm has dealt directly with the retail customer within the chain

Product types:	A y/n	B y/n	C y/n	D y/n	E y/n	F y/n	G y/n
Private motor	SU1	SU2	SU3	SU4	SU5	SU6	SU7
Household	SU8	SU9	SU10	SU11	SU12	SU13	SU14
Creditor - Payment protection	SU15	SU16	SU17	SU18	SU19	SU20	SU21
Travel	SU22	SU23	SU24	SU25	SU26	SU27	SU28
Personal accident - sickness	SU29	SU30	SU31	SU32	SU33	SU34	SU35
Legal expenses	SU36	SU37	SU38	SU39	SU40	SU41	SU42
Private Medical Insurance (PMI)	SU43	SU44	SU45	SU46	SU47	SU48	SU49
Critical illness	SU50	SU51	SU52	SU53	SU54	SU55	SU56
Private Health Insurance (PHI)	SU57	SU58	SU59	SU60	SU61	SU62	SU63
Life assurance (or term assurance)	SU64	SU65	SU66	SU67	SU68	SU69	SU70
HealthCare cash plan	SU71	SU72	SU73	SU74	SU75	SU76	SU77
Extended warranty (motor only)	SU78	SU79	SU80	SU81	SU82	SU83	SU84

**(iii) dealing as agent**

If you **deal as agent** for non-investment insurance contracts:  
Please provide:

- 7 Number of sales to retail customers during the reporting period where the firm dealt as agent SU86
- 8 Premium paid by retail customers during the reporting period where the firm dealt as agent SU87
- 9 Of the total of these sales, please indicate in column **F** the products where the firm dealt as agent and in column **G** where this business is significant\*.
- 10 \*significant is where premium collected from dealing as agent in this product amounts to
  - 1) more than 40% of the premium collected for all non-investment insurance activities with retail customers, or
  - 2) more than 40% of premium collected for all retail business in this product

**(iv) claims handling**

If you **assist** in the administration and performance of contracts of insurance:  
Please provide:

- 11 Number of claims handled on behalf of customers during the reporting period SU88

**(v) Lloyd's brokers - product sales data**

	Retail	Commercial Reinsurance	Total
12 % of regulated business revenue	<span style="border: 1px solid black; padding: 2px;">SU89</span>	<span style="border: 1px solid black; padding: 2px;">SU90</span>	<span style="border: 1px solid black; padding: 2px;">SU91</span> 100%

Round to nearest 20% and ensure figures add to 100%

**SECTION J: data required for calculation of fees**

**Income for fees calculations**

	<b>FSA</b>	<b>FOS</b>	<b>FSCS</b>
Regulated mortgage contracts	F1	F2	F3
Non-investment insurance	F4	F5	F6
Retail investments	F7	F8	F9

**Part 5: SUP 16 Ann 18BG**

**NOTES FOR COMPLETION OF  
THE RETAIL MEDIATION ACTIVITIES RETURN ('RMAR')**

**Contents**

Introduction	General notes on the RMAR
Section A:	Balance Sheet
Section B:	Profit & Loss Account
Section C:	Client Money
Section D:	Regulatory Capital
Section E:	Professional Indemnity Insurance
Section F:	Threshold Conditions
Section G:	Training & Competence
Section H:	Conduct of Business
Section I:	Supplementary product sales data
Section J:	Data required for calculation of fees

## Introduction: general notes on the RMAR

1. These notes aim to assist *firms* in completing and submitting the **Retail Mediation Activities Return** ('**RMAR**').
2. The purpose of the RMAR is to provide a framework for the collection of information required by the *FSA* as a basis for its supervision activities. It also has the purpose set out in paragraph 16.7.3G of the Supervision Manual, i.e. to help the *FSA* to monitor *firms*' capital adequacy and financial soundness.

## Defined terms

3. *Handbook* terms are italicised in these notes.
4. Terms referred to in the RMAR and these notes, where defined by the Companies Act 1985 or other relevant accounting provisions, bear that meaning for these purposes. The descriptions indicated in these notes are designed simply to repeat, summarise or amplify the relevant statutory or other definitions and terminology without departing from their full meaning or effect.

## Key abbreviations

5. The following table summarises the key abbreviations that are used in these notes:

APF	<i>Authorised professional firm</i>
AR	<i>Appointed representative</i>
CAD	<i>The Capital Adequacy Directive</i>
CASS	The Client Assets sourcebook, part of the FSA Handbook
COB	The Conduct of Business sourcebook, part of the FSA Handbook
CRED	The Credit unions sourcebook, part of the FSA Handbook
DISP	Dispute resolution: the Complaints sourcebook, part of the FSA Handbook
EEA	<i>The European Economic Area</i>
ICOB	The Insurance: Conduct of Business sourcebook, part of the FSA Handbook
IMD	<i>The Insurance Mediation Directive</i>
IPRU(INV)	The Interim Prudential sourcebook for investment businesses, part of the FSA Handbook
ISD	<i>The Investment Services Directive</i>
LTCI	Long term care insurance
MCOB	The Mortgages: Conduct of Business sourcebook, part of the FSA Handbook
PII	Professional indemnity insurance
PRU	The Integrated Prudential sourcebook, part of the FSA Handbook
RMAR	Retail Mediation Activities Return, i.e. the information requirements to which these notes refer.
SUP	The Supervision Manual, part of the FSA Handbook
T&C	Training and competence, part of the FSA Handbook

## Scope

6. The following *firms* are required to complete the RMAR:

(a) *firms* with *permission* to carry on *insurance mediation activity* in relation to *non-investment insurance contracts*.

By way of example, this would include a broker advising on private motor insurance, household insurance or critical illness cover. It would not though include *advice* on a *life policy*;

(b) *firms* with *permission* to carry on *mortgage mediation activity*;

(c) *firms* (defined as *retail investment firms*) that have *private customers*, and have *permission* to carry on the following activities in relation to *retail investments*:

- *Advising on investments*;
- *Arranging (bringing about) deals in investments*;
- *Making arrangements with a view to transactions in investments*;

*Retail investments* are defined as:

- (a) a *life policy*; or
- (b) a *unit*; or
- (c) a *stakeholder pension scheme*; or
- (d) an interest in an *investment trust savings scheme*; or
- (e) a *structured capital-at-risk product*.

The practical effect of the *private customer* limitation in the definition of *retail investment firms* is to exclude from the requirements *firms* that carry on *retail investment activities* exclusively with or for *intermediate customers* or *market counterparties*.

Note also that all *long-term care insurance contracts* are defined as *life policies*, and as such are included as *retail investments*.

## Application of RMAR sections

7. Many of the *firms* conducting the above *regulated activities* also have the *permission* to carry on other *regulated activities*, including for example mortgage lending and administration, *managing investments* or *dealing in investments as agent*. These *firms* are required to complete the RMAR in addition to other data requirements.

8. However, not all *firms* are required to complete all sections of the RMAR. Certain data requirements will be duplicated because of the separate reporting requirements imposed in relation to other *regulated activities*. Broadly, a *firm* that has the *permission* to carry on other *regulated activities* will not be subject to our proposed data requirements for financial reporting (RMAR sections A, B, C, D & E) or *threshold conditions* (section F), as we would expect to be collecting similar information as part of the data requirements for these other activities. For details, see SUP 16.7.

## EEA Firms

9. In accordance with the relevant directives, *incoming EEA firms* are not subject to all reporting requirements. In broad terms, this means that *incoming EEA firms* carrying on

*insurance mediation activity* by way of *cross border services* only are not required to complete the RMAR. The same applies to *incoming EEA firms* providing *cross border services* only, pursuant to the *ISD*.

10. In broad terms, *incoming EEA firms* carrying on *regulated activities* through a branch in the *United Kingdom* are not required to complete the sections of the RMAR in the following table.

Prudential reporting requirements	Section A (balance sheet)
	Section B (profit & loss)
	Section C ( <i>client money</i> )
	Section D (capital requirements)
	Section E (professional indemnity insurance)
Threshold conditions	Section F (save in relation to questions about <i>approved persons</i> )
Training & competence	Section G

11. *Firms* that only carry on reinsurance mediation are not required to complete section C.

### **Authorised professional firms**

12. APFs that are subject to *IPRU (INV) 2.1.3R* (for their *investment activity*) or *PRU 9.3.10R* (for *insurance mediation activity* or *mortgage mediation activity*) are not required to complete sections A, B2 or D. APFs that are members of the Law Society of England and Wales, the Law Society of Scotland or the Law Society of Northern Ireland are also not required to complete section C (see below).
13. The application of the capital requirements to APFs is set out in *IPRU(INV) 2.1.2R* (for *retail investment activity*) and *PRU 9.3.10R* (for *mortgage mediation activity* and *insurance mediation activity*).
14. Where APFs are required to submit financial information (i.e. sections A to E), they should do so in relation to all of their *regulated activities*. Section F should also be completed in relation to all *regulated activities*. Other sections (G to I) need not include information in relation to *non-mainstream regulated activities*. However, APFs may complete all sections on the basis of all of their *regulated activities* if this approach is more cost effective.

### **Accounting Principles**

15. The following principles should be adhered to by *firms* in the submission of financial information (sections A to E).
- (a) Unless a rule requires otherwise, amounts to be reported within the *firm's* balance sheet and profit and loss account should be determined in accordance with:
- (i) the requirements of all relevant statutory provisions (e.g. Companies Act 1985);
  - (ii) UK generally accepted accounting practice (UK GAAP). This is set out in the Financial Reporting Standards and Statements of Standard Accounting Practice issued or adopted by the Accounting Standards Board;

- (iii) the provisions of (c) and (d) below.
- (b) If the *firm* is a *body corporate* with one or more *subsidiaries*, its financial statements should be unconsolidated.
- (c)
  - (i) All amounts should be shown in pounds sterling, unless otherwise specified in the *Handbook* (e.g. in *PRU 9.2.13R*).
  - (ii) A *firm* should translate assets and liabilities denominated in other currencies into pounds sterling using the closing mid-market rate of exchange.
  - (iii) Taxation, when reported at a quarter or half year end, should be based on an estimate of the likely effective tax rate for the year applied to the interim profit or loss arising.
  - (iv) Balances on *client bank accounts* and related client accounts must not form part of the *firm's* own balance sheet.
- (d) No netting is permitted (that is, amounts in respect of items representing assets or income may not be offset against amounts in respect of items representing liabilities or expenditure, as the case may be, or vice versa).

#### **Other**

16. You will note that some questions in the RMAR refer to the “last reporting date”. If the RMAR is being completed for the first time, you should treat the date the *firm* became authorised to carry on any of the relevant *regulated activities* as the “last reporting date”, except where otherwise indicated (e.g. in sections E & H).
17. Unless otherwise indicated, the information submitted should cover all of the *firm's* transactions in the relevant products, and all of its *customers* and *market counterparties* (where relevant).

## **NOTES FOR COMPLETION OF THE RMAR**

### **Section A: Balance sheet**

The balance sheet data should be compiled in accordance with generally accepted accounting practice. Incorporated *firms* will already be submitting this information to Companies House under Companies Act requirements, and it would normally be expected that non-incorporated *firms* would compile this data for management purposes. If further assistance is required in completing the balance sheet, professional guidance should be sought.

This information will be used by the *FSA* to monitor the *firm's* financial position and satisfy itself as to the *firm's* ongoing solvency. Aggregated data may also be used to inform our supervision activities.

The frequency of reporting for this section is determined by *SUP 16.7*.

*Firms* that have *appointed representatives* ('ARs') should note that balance sheet data should be submitted for the *firm* only, not its ARs.

### **Section B: Profit & Loss Account**

Profit & loss ('P&L') should be reported on a cumulative basis throughout the *firm's* financial year.

**Sub-section B1 – regulated business revenue:** covers the data required on the *firm's* revenue from its *regulated activities*.

**Sub-section B2 – other P&L:** incorporates the remainder of the profit & loss data requirements.

*Firms* that receive combined income in relation to both regulated and non-regulated activities (for example mortgage packagers) may have difficulties in separately identifying their regulated income from their non-regulated income. If this is the case, *firms* should, (a) in the first instance, ask the provider of the income for an indication of the regulated/non-regulated split; and (b) if this is not available, make an estimate of the income derived from each activity.

In section B1, a *firm* that has *appointed representatives* ('ARs'), including a *network*, should ensure that the figures submitted for income are calculated before deducting any commissions shared with its ARs in respect of the *regulated activities* for which the *firm* has accepted responsibility as *principal*.



## Section B: guide for completion of individual fields

Commissions (gross)	<p>This should include all commission income in respect of the relevant regulated business:</p> <ul style="list-style-type: none"> <li>• for <i>regulated mortgage contracts</i>, this includes commissions received for <i>advising on regulated mortgage contracts</i> and <i>arranging</i>, but not lending and administration;</li> <li>• for <i>non-investment insurance contracts</i>, it should include commissions received for <i>advising</i>, <i>arranging</i> and <i>dealing</i> activities;</li> <li>• for <i>retail investments</i>, only commission received in relation to the relevant activities should be recorded here.</li> </ul> <p>Gross commissions will include commission that is received and passed on to another <i>person</i>.</p> <p>Where commission is shared between two or more <i>firms</i>, the gross commission should not be double counted, i.e. each <i>firm</i> should report only the commission it has received.</p>
Commissions (net)	<p>This should be the amount of the gross commission figure that is retained by the <i>firm</i> and, where applicable, its <i>appointed representatives</i>, (i.e. not passed on to another <i>person</i>) in respect of each type of business.</p>
Fees	<p>You should record here net income received from <i>customers</i> or other sources on a fixed fee rather than commission basis, but only in respect of the relevant <i>regulated activities</i>.</p>
Other income from regulated activities	<p>You should record here any income that has derived from the relevant <i>regulated activities</i> during the reporting period, which has not been recorded under commissions or fees.</p> <p>Such income may include interest on <i>client money</i>, where the <i>firm</i> is permitted to retain this, or payments made by product providers on a basis other than fees or commissions.</p>
Regulated business revenue	<p>This is the total of the <i>firm's</i> income during the reporting period in relation to its relevant <i>regulated activities</i>.</p> <p>For an <i>insurance intermediary</i> or a <i>mortgage intermediary</i>, this should be calculated in the same way as 'annual income', as specified in PRU 9.3.44R (although in this context the period is not generally annual). This <i>rule</i> states: "For a firm which carries on <i>insurance mediation activity</i> or <i>mortgage mediation activity</i>, annual income... is the amount of all brokerage, fees, <i>commissions</i> and other related income (for example, administration charges, overrides, profit shares) due to the <i>firm</i> in respect of or in relation to those activities".</p>
Other Revenue (income from non-regulated activities)	<p>Gross revenue arising from the <i>firm's</i> non-regulated activities, if any, should be entered here.</p>

## Section C: Client Money and assets

In broad terms, *client money* includes *money* that belongs to a *client*, and is held by a *firm* in the course of carrying on *regulated activities*, for which the *firm* has responsibility for its protection. It does not include *deposits* (where the *firm* acts as deposit-taker).

The *client money rules* define further what is and is not *client money*, and set out requirements on *firms* for the proper handling of and accounting for *client money*. If a *firm* fails, there is a greater direct risk to consumers, and a greater adverse impact on market confidence, if it is a holder of *client money*.

**Note 1:** *firms* that only carry on *mortgage mediation activity* or *reinsurance mediation* are exempt from the *client money rules*, and are not therefore required to complete this section of the RMAR (unless, in the case of reinsurance mediation, the *firm* has made an election under CASS 5.1.1R(3)(a)).

**Note 2:** *authorised professional firms* regulated by The Law Society (England and Wales), The Law Society of Scotland or The Law Society of Northern Ireland must comply with the rules of their *designated professional body*, and if they do so, they will be deemed to comply with the relevant sections of CASS. These *firms* are not therefore required to complete this section of the RMAR.

### Section C: guide for completion of individual fields

Have any notifiable issues been raised in relation to client money or other assets, either in the firm's last client assets audit report or elsewhere, that have not previously been notified to the FSA?	<i>SUP</i> 3.10 sets out the requirement for auditors to report annually on the <i>firm's</i> systems and controls in relation to <i>client money or custody assets</i> .  Auditors and <i>firms</i> are required to report significant issues to the FSA (see <i>SUP</i> 3.8.10G and <i>SUP</i> 15.3). Therefore, if you answer 'yes' here, you should ensure that the relevant issues are notified to us.
Risk transfer	See CASS 5.2 – holding money as agent of <i>insurance undertaking</i>
Statutory Trust	See CASS 4.2 and 5.3
Non-statutory Trust	See CASS 5.4
Client money credit total as at reporting date	This should be the total of credits on the <i>firm's client money</i> account(s) as at the current date of return.
Client money debit total as at reporting date	This should be the total of any debits on the <i>firm's client money</i> account(s) as at the current date of return.
Net client money balance as at reporting date	This should be the aggregate balance on the <i>firm's client money</i> account(s). (The reporting of this figure should <b>not</b> be taken to mean that <i>firms</i> are permitted to offset an overdrawn client bank account against one that is in credit.)
If non-statutory, has auditor's confirmation of systems and controls been obtained?	This refers to the requirement in CASS 5.4.4R(2) that the <i>firm</i> should obtain written confirmation from its auditor that adequate systems and controls are in place.
Is any client money invested (other than on deposit)?	You should indicate 'yes' here if the <i>firm</i> has invested any <i>client money</i> other than in a bank account. See CASS 5.5.14. (Note: this is only permitted for <i>client money</i> that is held in a non-statutory trust.)
Do you hold client money for business undertaken by an AR?	If the <i>firm</i> has <i>appointed representatives</i> that receive <i>client money</i> , you should state 'yes' here. The requirements of CASS 4.3.15R (investment activities) and/or CASS 5.5.18 ( <i>insurance mediation activity</i> ) should be adhered to in these circumstances.
Does the <i>firm</i> hold any client assets (other than client money)?	If the <i>firm</i> holds client assets and is subject to the requirements of either CASS 2 or CASS 5.8, state 'yes' here.

## Section D: Regulatory Capital

### ‘Higher of’ requirements

In this section there are separate calculations of regulatory capital and capital resources requirements for the different types of business covered by the data requirements. The calculations are the same, however, for both *mortgage mediation activity* and *insurance mediation activity* relating to *non-investment insurance contracts*.

If a *firm* carries on one or both of:

- *mortgage mediation activity*, and/or
- *insurance mediation activity* relating to *non-investment insurance contracts*,

and additionally carries on

- *designated investment business* (i.e. is subject to *IPRU(INV)*);

then a ‘**higher of**’ requirement applies. This is set out in *PRU* 9.3.24R, which provides that in these circumstances, the higher of the capital resources requirements relating to the respective activities should apply.

In section **D1**, therefore, there are separate reporting requirements to establish the appropriate capital requirements for the following groups of activities and/or *firms* (the requirements have to be completed for all applicable category) :

- firms* carrying on *mortgage mediation activity*, and/or *insurance mediation activity* relating to *non-investment insurance contracts* (the capital requirements are the same for both activities, calculated in section D1);
- personal investment firms* that carry on *retail investment activities*, but no other *designated investment business*. Capital requirements are calculated in section D2 or D3 below as applicable;
- other *personal investment firms*, and *firms* that are subject to *PRU*, but are also subject to *IPRU(INV)* or *CRED* (see below). These capital requirements are not calculated as part of the RMAR.

In each case, it is the higher of the capital requirements that applies and is compared with the applicable calculation of financial resources.

Standard ‘version 1’ credit unions are exempt from the capital requirements in *PRU*, although they have capital requirements under the Credit Unions sourcebook (‘*CRED*’). For other credit unions, the capital resources requirement should be the higher of the amounts required under *PRU* or *CRED*.

**Note on the scope of Sections D2, D3, D4 & D5:** *firms* that carry on *designated investment business* and are subject to the RMAR, but do not meet the definition of *personal investment firm*, i.e. are not subject to *IPRU(INV)* Chapter 13, will **not** be subject to these sections. Such *firms*, e.g. smaller stockbrokers that advise on *retail investments* as an incidental part of their business, remain subject to the financial resources requirements associated with their principal *regulated activities*.

**Sub-sections:** this section is sub-divided as follows:

**D1:** in this sub-section, *firms* are required to complete the regulatory capital sections that are applicable for the types of business undertaken. The *personal investment firms* referred to in (ii) above are required to complete one of sections D2 or D3 to arrive at the totals required in D1.

**D2:** this section is completed by *personal investment firms* that are **not** subject to the requirements of *ISD* and the *Capital Adequacy Directive* (CAD). It is used to calculate the financial resources and financial resources requirements set out in Chapter 13.10-12 of the Interim Prudential Sourcebook for Investment Businesses (*IPRU(INV)*). This in turn will provide the totals to be submitted in the D1 fields marked A to I as applicable.

**D3:** this section is completed by *personal investment firms* that **are** subject to the requirements of *ISD* and CAD. It is used to calculate the financial resources and financial resources requirements set out in *IPRU(INV)* 13.3-5. This in turn will provide the totals to be submitted in the D1 fields marked A to I as applicable.

**D4:** this section is also completed by *personal investment firms* that are subject to the requirements of *ISD* and CAD. It is used to complete the quarterly financial resources statement that is required from these *firms* under CAD.

**D5:** this section relates to the requirements imposed by CAD on *ISD personal investment firms* in relation to *large exposures*.

### Section D1: guide for completion of individual fields

Is the firm exempt from these capital requirements in relation to any of its retail mediation activities?	<p>The <i>firm</i> should indicate here if any <i>Handbook</i> exemptions apply in relation to the capital requirements in <i>PRU</i> or <i>IPRU(INV)</i> Chapter 13. Examples of <i>firms</i> that may be subject to exemptions include</p> <ul style="list-style-type: none"> <li>• Lloyd’s <i>managing agents</i> (<i>PRU</i> 9.3.11R);</li> <li>• solo consolidated <i>subsidiaries of banks</i> or <i>building societies</i>;</li> <li>• small <i>credit unions</i> (as defined in <i>PRU</i> 9.3.8R); and</li> <li>• <i>investment firms</i> not subject to <i>IPRU(INV)</i> Chapter 13 (unless they additionally carry on <i>mortgage mediation activity</i> or <i>insurance mediation activity</i> relating to <i>non-investment insurance contracts</i>).</li> </ul>
<b>Mortgage and non-investment insurance mediation</b> (see sub paragraph (i) above)	
Base requirement	<p>The minimum capital requirements for <i>firms</i> carrying on <i>mortgage mediation activity</i> and for <i>insurance mediation activity</i> relating to <i>non-investment insurance contracts</i> are set out in <i>PRU</i> 9.3.30R.</p> <p>If the <i>firm</i> carries on <i>designated investment business</i> as well as <i>mortgage mediation activity</i>, <i>insurance mediation activity</i> or both, requirements under both <i>IPRU(INV)</i> and <i>PRU</i> need to be considered, as it is the higher of the requirements that needs to be met (see general notes above).</p>
5% of annual income (firms holding client money)	<p>For <i>firms</i> that hold <i>client money</i> or other <i>client assets</i> in relation to <i>insurance mediation activity</i> or <i>mortgage mediation activity</i>, this should be calculated as 5% of the annual income (see <i>PRU</i> 9.3.30R(2)) from the <i>firm’s insurance mediation activity</i>, <i>mortgage mediation activity</i>, or both.</p>

2.5% of annual income (firms not holding client money)	For <i>firms</i> that do not hold <i>client money</i> or other <i>client</i> assets in relation to <i>insurance mediation activity</i> or <i>mortgage mediation activity</i> , this should be calculated as 2.5% of the annual income (see <i>PRU 9.3.30R(1)</i> ) from the <i>firm's insurance mediation activity, mortgage mediation activity, or both.</i>
Capital requirements (higher of above)	The higher of the base requirement and 5% of annual income ( <i>firms</i> that hold <i>client money</i> or other <i>client</i> assets), or the higher of the base requirement and 2.5% of annual income ( <i>firms</i> that do not hold <i>client money</i> or other <i>client</i> assets)
Other <i>FSA</i> capital requirements (if applicable)	The <i>FSA</i> may from time to time impose additional requirements on individual <i>firms</i> . If this is the case for your <i>firm</i> , you should enter the relevant amount here. This excludes capital requirements in relation to PII, which are recorded below.  There may be additional capital requirements imposed on <i>firms</i> that carry on a number of different <i>regulated activities</i> . For example, <i>firms</i> that carry on the activities of mortgage lending or mortgage administration in addition to <i>mortgage mediation activity</i> and/or <i>insurance mediation activity</i> , and are not exempted under <i>PRU 9.3.4R</i> , may have an additional requirement under <i>PRU 9.3.40R(2)</i> .
Additional capital requirements for PII (if applicable)	If the <i>firm</i> has any increased excesses on its PII policies, the total of the additional capital requirements required by the tables in <i>PRU 9.2.19R</i> or <i>9.2.20R</i> should be recorded here. See also section E of the <i>RMAR</i> .
TOTAL CAPITAL REQUIREMENT	Appropriate totals from above
TOTAL CAPITAL RESOURCES	This should be the total of capital resources calculated in accordance with <i>PRU 9.3</i> in this section (D1) for incorporated or unincorporated <i>firms</i> as applicable.  For <i>firms</i> that are additionally subject to <i>IPRU(INV)</i> or <i>CRED</i> , this should be the higher of the amount calculated in this section ('total capital resources') and the financial resources determined by <i>IPRU(INV)</i> or <i>CRED</i> . See <i>PRU 9.3.51R</i> .
TOTAL CAPITAL EXCESS/DEFICIT	This should show the amount of capital resources that the <i>firm</i> has in relation to its capital requirement.
<b>IPRU(INV) requirements for personal investment firms (retail investment activities only)</b>	<i>Firms</i> that carry on <i>retail investment activities</i> , but no other <i>designated investment</i> business, are subject to this section. It is populated from section D2 or D3 as applicable (see sub paragraph (ii) above).
Category of personal investment firm under <i>IPRU(INV)</i>	If the <i>firm</i> is subject to Chapter 13 of <i>IPRU(INV)</i> , it should enter here its firm category as defined in <i>IPRU(INV)</i> Appendix 13(1), i.e. A1, A2, A3, B1, B2 or B3.
Own funds requirement	<b>See Section D2 or D3 as applicable</b> The own funds requirement ('OFR') should be calculated in accordance with Chapter 13 of the Interim Prudential Sourcebook for Investment Firms.  <i>ISD Firms</i> see section <i>IPRU (INV) 13.3</i> <i>Non-ISD Firms</i> see section <i>IPRU (INV) 13.10</i>  For a <i>low resource firm</i> , the OFR is always £10,000.

Own funds	<p><b>See Section D2 or D3 as applicable</b> This field should be filled in using the figure for own funds that is derived from the calculation in Section D2 or D3 as applicable.</p> <p>Own funds should be calculated in accordance with Chapter 13 of the Interim Prudential Sourcebook for Investment Firms.</p> <p><i>ISD Firms see IPRU (INV) 13.3</i> <i>Non-ISD Firms see IPRU (INV) 13.10</i></p> <p>Source data for the own funds calculation should be entered in the separate financial resources section for <i>ISD firms</i> or <i>non-ISD firms</i> as applicable.</p>
Surplus/deficit of own funds	<p><b>See Section D2 or D3 as applicable</b> This field should be filled in using the figure for surplus/deficit that is derived from the calculation in Section D2 or D3 as applicable.</p> <p>This should show the amount of the <i>firm's</i> own funds in relation to its own funds requirement.</p>
Additional own funds requirement for PII (if applicable)	<p>If the <i>firm</i> has any increased excesses or exclusions on its PII policies, the total of the additional capital requirements required by <i>IPRU(INV)</i> 13.1.4 should be recorded here. See also section E of the RMAR.</p>
Other <i>FSA</i> capital requirements (if applicable)	<p>The <i>FSA</i> may from time to time impose additional requirements on individual <i>firms</i>. If this is the case for your <i>firm</i>, you should enter the relevant amount here. This excludes capital requirements in relation to PII, which are recorded above.</p>
Adjusted net current assets requirement (if applicable)	<p><b>See Section D2 or D3 as applicable</b> All <i>personal investment firms</i> except <i>low resource firms</i> should at all times have adjusted net current assets of at least £1.</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p>
Adjusted net current assets (if applicable)	<p><b>See Section D2 or D3 as applicable</b> All <i>personal investment firms</i> except <i>low resource firms</i> should at all times have adjusted net current assets of at least £1.</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p> <p>This field should be filled in using the figure for adjusted net current assets that is derived from the calculation in Section D2 or D3 as applicable. Adjusted net current assets should be calculated in accordance with Chapter 13 of the Interim Prudential Sourcebook for Investment <i>Firms</i>.</p> <p><i>ISD Firms see IPRU (INV)13.4</i> <i>Non-ISD Firms see IPRU (INV)13.11</i></p>
Surplus/deficit (if applicable)	<p><b>See Section D2 or D3 as applicable</b> All <i>personal investment firms</i>, except <i>low resource firms</i>, should at all times have adjusted net current assets of at least £1.</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p> <p>This field should be filled in using the figure for surplus/deficit that is derived from the calculation in section D2 or D3 of the data requirements.</p> <p>This shows whether the <i>firm's</i> net current assets are positive.</p>

Expenditure based requirement (if applicable)	<p><b>See Section D2 or D3 as applicable</b></p> <p>All <i>personal investment firms</i>, except <i>low resource firms</i>, should calculate their expenditure based requirement ('EBR') in accordance with Chapter 13 of the Interim Prudential Sourcebook for Investment Firms.</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p> <p><i>ISD Firms</i> see <i>IPRU (INV)</i> 13.5  <i>Non-ISD Firms</i> see <i>IPRU (INV)</i> 13.12</p>
Adjusted Capital/liquid capital (if applicable)	<p><b>See Section D2 or D3 as applicable</b></p> <p>This field should be filled in using the figure for adjusted capital/liquid capital that is derived from the calculation in Section D2 or D3 as applicable.</p> <p>Adjusted/liquid capital should be calculated in accordance with Chapter 13 of the Interim Prudential Sourcebook for Investment Firms.</p> <p><i>ISD Firms</i> see <i>IPRU (INV)</i> 13.5  <i>Non-ISD Firms</i> see <i>IPRU (INV)</i> 13.12</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p>
Surplus/deficit (if applicable)	<p><b>See Section D2 or D3 as applicable</b></p> <p>This field should be filled in using the figure for surplus/deficit that is derived from the calculation in Section D2 or D3 as applicable.</p> <p>This shows the amount of the <i>firm's</i> adjusted/liquid capital in relation to its expenditure based requirement.</p> <p><i>Low resource firms</i> should enter 'n/a' here.</p>
<b>Eligible capital (mortgage and non-investment insurance)</b>	
<b>Incorporated firms</b>	
Share capital	As reported in section A
Audited reserves	<p>These are the audited accumulated profits retained by the <i>firm</i> (after deduction of tax and dividends) and other reserves created by appropriations of share premiums and similar realised appropriations. Reserves also include gifts of capital, for example, from a <i>parent undertaking</i>.</p> <p>If reserves have not been audited this field should be zero.</p>
Interim net profits (audited)	Interim net profits should be audited by the <i>firm's</i> external auditor, net of tax or anticipated dividends and other appropriations. Normally this will mean that they form a proportion of the <i>firm's</i> P&L account in field BS24, but if no audit has been undertaken during the reporting period it should be a nil return.
Interim net profits (not audited)	Other unverified profits (not included in total capital resources)
Revaluation reserves	Revaluation reserves (unrealised reserves arising from revaluation of fixed assets) can only be included here if audited.
Eligible subordinated loans	Subordinated loans should be included in capital on the basis of the provisions in <i>PRU</i> 9.3.56R and <i>PRU</i> 9.3.57R.
Less investments in own shares	Amounts recorded in the balance sheet as investments which are invested in the <i>firm's</i> own shares should be entered here for deduction.
Less intangible assets	<p>Any amounts recorded as intangible assets in section A above should be entered here for deduction.</p> <p>The balance sheet value for <b>goodwill</b> does not have to be deducted here until 14 January 2008. See <i>PRU</i> 9.3.53R</p>
Less interim net losses	Interim net losses should be calculated in relation to the period following the date as at which the capital resources are being calculated. The figures do not have to be audited to be included.

<b>Unincorporated firms</b>	
Capital of a sole trader or partnership	See <i>PRU 9.3.52R</i>
Eligible subordinated loans	Subordinated loans should be included in capital on the basis of the provisions in <i>PRU 9.3.56R</i> and <i>PRU 9.3.57R</i> .
Personal assets not needed to meet non-business liabilities	<p><i>PRU 9.3.54R</i> and <i>9.3.55G</i> state that a <i>sole trader or partner</i> <u>may</u> use personal assets to cover liabilities incurred in the <i>firm's</i> business unless:</p> <p>(1) those assets are needed to meet other liabilities arising from:  (a) personal activities; or  (b) another business activity not regulated by the <i>FSA</i>; or  (2) the <i>firm</i> holds <i>client money</i> or other <i>client</i> assets.</p> <p>This field may be left blank if the <i>firm</i> is able to satisfy the capital resources requirements without relying on personal assets.</p>
Less intangible assets	<p>Any amounts recorded as intangible assets in section A above should be entered here for deduction.</p> <p>The balance sheet value for <b>goodwill</b> does not have to be deducted here until 14 January 2008. See <i>PRU 9.3.53R</i></p>
Less interim net losses	Interim net losses should be calculated in relation to the period following the date as at which the capital resources are being calculated. The figures do not have to be audited to be included.
Less excess of drawings over profits for a sole trader or partnership	Any excess of drawings over profits should be calculated in relation to the period following the date as at which the capital resources are being calculated. The figures do not have to be audited to be included.

## **Section D2: non-*ISD* personal investment firms**

This section is for non-*ISD* personal investment firms. Its purpose is to assist in calculating the financial resources data that is required in section D1 above, based on the requirements of *IPRU(INV)* 13.10 to 13.12.

All non-*ISD* personal investment firms are required to meet the Own Funds financial resources test as follows:

### **Own Funds (test 1)**

*IPRU(INV)* requires that all non-*ISD* personal investment firms have financial resources of at least £10,000 at all times. The Own Funds test is designed to evaluate firms' adherence to this requirement.

In addition, firms that do not fall within the definition of a *low resource firm* are required to meet the following additional financial resources tests.

### **Adjusted Net Current Assets (test 1A)**

The purpose of this test is to ensure that the *firm* has adequate working capital to be able to meet its liabilities as and when they fall due. It does this by taking the *firm's* net current assets (from the balance sheet), and applying the following actions:

- (1) excluding assets which cannot be realised or recovered within twelve months;



- (2) excluding amounts receivable from *connected persons* (to the extent that they are not properly secured, except certain allowable deposits);
- (3) valuing *investments* at current market value.

The resulting balance should be at least £1.

### **Expenditure Based Requirement (test 2)**

This is a capital requirement for *personal investment firms* that are not *low resource firms*, based on a *firm's* overall audited expenditure. The Expenditure Based Requirement is calculated as a fraction of the *firm's* annual fixed costs which, for this purpose, are based upon the *firm's* annual audited expenditure and, in general terms, exclude cost items that would not be incurred were there no income. Thus staff bonuses and *partners'* profit shares (unless guaranteed) and any shared commissions are not treated as fixed costs for the purposes of the calculation.

### **Section D3: ISD personal investment firms**

This section of the data requirements is provided for *ISD personal investment firms*, to assist in calculating the financial resources data that is required in section D1 above, based on the requirements of *IPRU(INV)* 13.2-5.

All *ISD personal investment firms* are required to meet the following three financial resources tests:

#### **Own Funds (test 1)**

*IPRU(INV)* requires that *ISD personal investment firms* have appropriate financial resources in relation to their prudential category at all times. The Own Funds Requirements for these *firms* are:

for a Category A1 *firm*: €730,000;

for a Category A2 *firm*: €125,000;

for a Category A3 *firm*: €50,000.

The Own Funds test is designed to evaluate *firms'* adherence to these requirements.

#### **Adjusted Net Current Assets (test 1A)**

See Section D2 in relation to non-*ISD personal investment firms* above.

#### **Expenditure Based Requirement (test 2)**

See Section D2 in relation to non-*ISD personal investment firms* above.

### **Section D4: CAD 13 quarterly financial resources (ISD personal investment firms)**

The purpose of this section is to measure *firms'* compliance with the *Capital Adequacy Directive* ('CAD') on a quarterly basis, as required by the directive. *Firms* should use figures

taken from their most recently audited accounts, unless they relate to a change in resources of a kind specified in this section of the RMAR, e.g. the introduction of a subordinated loan.

#### **Section D5: reportable *Large Exposures (ISD personal investment firms)***

This section relates to the requirements imposed by CAD on *ISD personal investment firms* in relation to *large exposures*.

A *large exposure* exists where a *firm* is owed a debt by, or is otherwise exposed to another person, or to two or more affiliated *persons*, and that exposure equals or exceeds 10% of its own funds. Under *IPRU(INV)*, a *firm* is required to ensure that its *large exposures* do not exceed 25% of its own funds (or the aggregate of exposure to its holding company, or a subsidiary company or a group of subsidiaries of its holding company does not exceed 20% of own funds).

The detailed requirements in relation to *large exposures* are set out in *IPRU(INV)* 13.6, including the types of *exempt exposures* that may be excluded from the calculations.

*SUP* 16 requires that *large exposures* be reported to the *FSA* on a quarterly basis. This part of the data requirements fulfils that requirement, and assists *firms* in calculating the level of reportable exposure (excluding *exempt exposures*) which then feeds into the calculation of the Expenditure Based Requirement.

## Section E: Professional Indemnity Insurance

This section requires *firms* to confirm that they are in compliance with the prudential requirements in relation to professional indemnity insurance (PII).

Data is required in relation to all PII policies that a *firm* has in place, up to a limit of ten (the *firm* will be prompted to submit data on all applicable policies). If a *firm* has more than ten policies, it should report only on the ten largest policies by premium.

**Note on the scope of Section E:** *retail investment firms* that fall within the scope of these data requirements, but do not meet the definition of *personal investment firm*, i.e. are not subject to *IPRU(INV)* 13, will **not** be subject to this section.

The PII requirements for *authorised professional firms* ('APFs') that carry on *retail investment activities* are set out in *IPRU(INV)* 2.3. APFs that carry on *mortgage mediation activity* or *insurance mediation activity* are subject to the full requirements of *PRU* 9.2.

### Section E: guide for completion of individual fields

Is the firm exempt from the PII requirements in respect of any regulated activities?	<p>The conditions for exemptions from the PII requirements for <i>firms</i> carrying on <i>insurance</i> or <i>mortgage mediation</i> are set out in <i>PRU</i> 9.2.1R paragraphs (3) to (6).</p> <p><i>Personal investment firms</i> can only be exempted by individual waiver granted by the <i>FSA</i> (unless <i>IPRU(INV)</i> 13.1.5R applies in respect of comparable guarantees)</p> <p><i>Retail investment firms</i> that do not meet the definition of <i>personal investment firm</i> are not required to complete this section of the RMAR.</p>
If not exempt, has the firm renewed its PII cover since the last reporting date?	<p>The purpose of this question is to ensure that <i>firms</i> do not have to fill in the same information each time they report when the information only changes annually.</p> <p>If the <i>firm</i> is reporting for the first time, you should enter 'yes' here and complete the data fields below.</p> <p>You should only enter 'n/a' if the <i>firm</i> is exempt from the PII requirements in respect of all of <i>regulated activities</i> forming part of the RMAR.</p>
Have any of the data items below changed since the last reporting date (or since you last notified the <i>FSA</i> of any changes)?	<p>The purpose of this question is to ensure that <i>firms</i> do not have to fill in the same information for each period when the information only changes annually.</p> <p>If the <i>firm</i> is reporting for the first time, you should enter 'yes' here and complete the data fields below.</p> <p>You should only enter 'n/a' if the <i>firm</i> is exempt from the PII requirements in respect of all of the <i>regulated activities</i> within the scope of the RMAR.</p>
What activities are covered by the policy(ies)?	You should indicate which <i>regulated activities</i> are covered by the <i>firm's</i> PII policy or policies.

Is the cover compliant?	<p>The required terms for PII cover are set out in the Prudential Sourcebooks as follow:</p> <p><i>Insurance intermediaries and mortgage intermediaries – PRU 9.2</i> <i>Personal investment firms - IPRU(INV) 13.1</i></p> <p><i>Authorised professional firms</i> that carry on <i>retail investment activities</i> should note that by ticking this box they are providing confirmation that they are in compliance with <i>IPRU(INV)2.3.2E</i>, which requires them to have PII cover that is at least equivalent to the requirements of their <i>designated professional body</i>.</p>
Annual premium	This should be the annual premium that is paid by the <i>firm</i> , net of tax and any other add-ons.
Limit of Indemnity	<p>You should record here the indemnity limits on the <i>firm's</i> PII policy or policies, both in relation to single claims and in aggregate.</p> <p>For <i>insurance intermediaries</i>, see <i>PRU 9.2.13R</i>. For <i>mortgage intermediaries</i>, see <i>PRU 9.2.15R</i>. For <i>personal investment firms</i>, see <i>IPRU(INV) 13.1.4E</i>.</p> <p>If the <i>firm</i> is subject to more than one of the above limits (because of the scope of its <i>regulated activities</i>), and has one PII policy for all of its <i>regulated activities</i>, the different limits should be reflected in the policy documentation.</p>
Policy excess	<p>For <i>insurance intermediaries</i> and <i>mortgage intermediaries</i>, see <i>PRU 9.2.16-20R</i>. For <i>personal investment firms</i>, see <i>IPRU(INV) 13.1.4E</i>.</p>
Increased excess(es) for specific business types	<p>If the prescribed excess limit is exceeded in respect of a type or types of business, the amount(s) of the increased excess should be stated here. The type(s) of business to which the increased excess applies should be selected from the drop-down box.</p> <p>(Some of the business types in the drop-down box include pensions, endowments, FSAVCs, splits/zeroes, precipice bonds, income drawdown, <i>lifetime mortgages</i>, discretionary management, other)</p>
Policy exclusion(s) for specific business types	<p>If there are any exclusions in the <i>firm's</i> PII policy, the business type(s) to which they relate should be selected from the drop-down box.</p> <p>(Some of the business types in the drop-down box include pensions, endowments, FSAVCs, splits/zeroes, precipice bonds, income drawdown, <i>lifetime mortgages</i>, discretionary management, other)</p>
Renewal date	The next date by which the current cover needs to be renewed.
Insurer name	<p>The name of the <i>insurance undertaking</i> providing cover. If cover is provided by a Lloyd's syndicate, the name of the syndicate should be stated.</p> <p>If a policy is underwritten by more than one <i>insurance undertaking</i>, you should state 'multiple' along with the number of <i>insurance undertakings</i></p>
Does the <i>firm</i> have any other PII policies?	If 'Y' is entered here, the <i>firm</i> will be required to submit the information above for further policies as applicable (up to a maximum of ten).
Amount of additional capital required for increased excess(es) (where applicable, total amount for all PII policies)	This should be calculated using the tables in <i>IPRU(INV) 13.1.4(12)E</i> or <i>PRU 9.2.20-22</i> as applicable. The total of additional capital (i.e. in relation to all of the <i>firm's</i> PII policies) should have been reported under 'additional capital requirements for PII' and/or 'additional own funds for PII' in section D1.

Amount of additional own funds required for policy exclusion(s)	<i>Personal investment firms</i> only - this should be calculated in accordance with <i>IPRU(INV)</i> 13.1.4(13)R. The total of additional own funds (i.e. in relation to all of the <i>firm's</i> PII policies) should have been reported under 'additional capital requirements for PII' and/or 'additional own funds for PII' in section D1.
Total of additional own funds required	<i>Personal investment firms</i> only – this is the same figure as in section D1, representing the total of additional own funds that are required under <i>IPRU(INV)</i> 13.1.4 for all of the <i>firm's</i> PII policies.
Total of readily realisable own funds	<i>Personal investment firms</i> only - you should state here the total of the own funds reported in section D that are classed as 'readily realisable' under the terms of <i>IPRU(INV)</i> 13.1.4(4)R.
Excess/deficit of readily realisable own funds	This field will automatically calculate the excess or deficit, i.e. the 'total of additional own funds required' less the 'total of readily realisable own funds'

## Section F: the *threshold conditions*

### Sub-heading: adequate resources

This section relates to *threshold condition 4*, by virtue of which the resources of *firms* must, in the opinion of the *FSA*, be adequate in relation to the *regulated activities* that they carry on.

The scope of this requirement is set out in Chapter 2.4 of the Threshold Conditions Sourcebook (*COND* 2.4). In summary, 'resources' refers to both financial and non-financial resources, and to the means of managing those resources. Examples of matters to which the *FSA* will have regard when assessing whether a *firm* satisfies *threshold condition 4* include, among others, the following:

- whether the *firm* has access to adequate capital by reference to the *FSA's* prudential requirements;
- whether the *firm* can meet all its liabilities as they fall due; and
- whether the *firm* has taken steps to identify and measure any risks of regulatory concern, and has installed appropriate systems and controls to manage them.

### Sub-heading: close links

This section relates to *threshold condition 3*. *Firms* should consult *COND* 2.3, as well as Chapter 11 of the Supervision Manual ('*SUP*').

This section of the return replaces the *close links* annual reporting requirement in *SUP* 16.5.4R, which does not now apply to those *firms* subject only to the RMAR for the purposes of regulatory reporting. Moreover, the existing exemptions for certain other *firms* from the existing reporting requirements in *SUP* 16.5.1G are retained.

### **Sub-heading: approved persons**

The approved persons regime is one of the ways in which the *FSA* satisfies itself that *firms* are operating in accordance with *threshold conditions* 4 (adequate resources) and 5 (suitability).

An “approved person” is a *person* in relation to whom the *FSA* has given its approval under the *Act* for the performance of a *controlled function*. In broad terms, the individuals the *FSA* approves fall into the following categories:

- individuals exerting significant influence over the *firm’s regulated activities*;
- individuals dealing directly with *customers*; and
- individuals dealing with the property of *customers*.

For *retail investment firms*, all individuals undertaking *controlled functions* in relation to the above categories are subject to the *approved persons* regime.

For *firms* carrying on *mortgage mediation activity* and/or *insurance mediation activity* relating to *non-investment insurance contracts*, the ‘significant influence’ category is subject to the *approved persons* regime, but not the ‘customer functions’.

See, generally, *SUP* 10.4 for specification of *significant influence functions* and *customer functions*.

### **Sub-heading: controllers**

In very broad terms, so far as those required to fill in this part of the return are concerned, the *Handbook* requires notification of changes in a *firm’s controllers* as follows:

A *UK domestic firm* other than a *UK insurance intermediary* must notify the *FSA* of any of the following events concerning the *firm*:

- (1) a *person* acquiring *control* or ceasing to have *control*;
- (2) an existing *controller* acquiring an additional *kind of control* or ceasing to have a *kind of control*;
- (3) an existing *controller* increasing or decreasing a *kind of control* which he already has so that the percentage of shares or *voting power* concerned becomes or ceases to be equal to or greater than 20%, 33% or 50%;
- (4) an existing *controller* becoming or ceasing to be a *parent undertaking*.

An *overseas firm* must notify the *FSA* of any of the following events concerning the *firm*:

- (1) a *person* acquiring *control* or ceasing to have *control*;
- (2) an existing *controller* becoming or ceasing to be a *parent undertaking*.

A *UK insurance intermediary* must notify the *FSA* of any of the following events concerning the *firm*:

- (1) a *person* acquiring *control*;
- (2) a *controller*;

- (a) decreasing the percentage of shares held in the *firm* from 20% or more to less than 20%; or
  - (b) decreasing the percentage of shares held in a *parent undertaking* of the *firm* from 20% or more to less than 20%; or
  - (c) decreasing the percentage of voting power which it is entitled to exercise, or control the exercise of, in the *firm* from 20% or more to less than 20%; or
  - (d) decreasing the percentage of voting power which it is entitled to exercise, or control the exercise of, in a *parent undertaking* of the *firm* from 20% or more to less than 20%;
- (3) an existing *controller* becoming or ceasing to be a *parent undertaking*.

A summary of these notification requirements is provided in Annex 1G of SUP 11.

This section of the return replaces the annual *controllers* reporting requirement in SUP 16.4.5R, which does not now apply to those *firms* subject only to the RMAR for the purposes of regulatory reporting. Moreover, the exemptions for certain other *firms* from the existing reporting requirement in SUP 16.4.1G are retained.

## Section F: guide for completion of individual fields

<p><b>Adequate Resources</b> Does the firm have adequate resources in relation to its regulated activities?</p>	<p>In answering this question you should carefully consider the <i>guidance</i> in COND 2.4, which sets out the criteria that the FSA will use in determining whether a <i>firm</i> is deemed to have adequate resources.</p> <p><i>Authorised professional firms</i> should note that by ticking this box they are providing confirmation that they are in compliance with IPRU(INV)2.2, which requires them to be able to meet their liabilities as they fall due.</p>
<p><b>Close Links</b> Are you exempt from close links reporting requirements?</p>	<p>The categories of <i>firm</i> that are exempt from the reporting requirement are listed in the relevant parts of SUP 16.1.3R.</p>
<p>If not, have there been changes to your close links since the FSA was last informed?</p>	<p>For detailed <i>guidance</i> on what constitutes a <i>close link</i>, see COND 2.3.</p>
<p>If yes, on what date did these changes take effect? (if no notification has been made, please notify us separately of the changes)</p>	<p>See SUP 11.9. All <i>firms</i> should have notified the FSA immediately if they have become aware that they have become or ceased to be <i>closely linked</i> with another <i>person</i>.</p> <p>If there have been changes in <i>close links</i> that have not been notified to the FSA, you should do this now.</p>
<p><b>Approved Persons</b> Have there been changes to your approved persons' details since the FSA was last informed?</p>	<p>State yes if, for example, any of the <i>firm's</i> approved persons have joined or left during the reporting period, but the FSA was not notified in accordance with normal procedures.</p>

<p>If yes, on what date did these changes take effect? (if no notification has been made, please notify us separately of the changes)</p>	<p>Any changes in the <i>firm's approved persons</i>, e.g. joiners and leavers, should have been notified at the time to the <i>FSA</i>. Detailed requirements in relation to <i>approved persons</i> are set out in <i>SUP 10.13</i></p> <p>If the appropriate notification was <b>not</b> made at the time, you should state here the date the change took effect. If there has been more than one unnotified change, you should enter the date of the most recent change.</p> <p>If there have been changes in relation to <i>approved persons</i> that have <b>not</b> been notified to the <i>FSA</i>, you should do this now.</p>
<p><b>Controllers</b> Are you exempt from the controllers reporting requirements?</p>	<p>The categories of <i>firm</i> that are exempt from the reporting requirement are listed in the relevant parts of <i>SUP 16.1.3R</i></p>
<p>If not, have there been changes to your controllers since the <i>FSA</i> was last informed?</p>	<p>See, generally, <i>SUP 11.4</i>.</p>
<p>If yes, on what date did these changes take effect? (if no notification has been made, please notify us separately of the changes)</p>	<p>See, generally, <i>SUP 11.4</i>. If there have been changes in <i>controllers</i> that have not been notified to the <i>FSA</i>, you should do this by means of normal supervisory channels.</p>

## Section G: Training & Competence ('T&C')

Principle 3 of the *Principles for Businesses* requires *firms* to take reasonable care to organise and control their affairs responsibly and effectively, with adequate risk management systems. This includes making proper arrangements for individuals associated with a *regulated activity* carried on by a *firm* to achieve and maintain competence.

Our approach to training and competence is set out in the Training & Competence Sourcebook ('*TC*'). There are two parts to the Sourcebook:

Chapter 1 (the Commitments) consists of *guidance* that applies to those *firms* indicated in *TC 1.1.6G* (which includes all *firms* with a *Part IV permission*). It states that the *firm's* commitments to training and competence should be that employees are competent and remain competent for the work that they do, that they are appropriately supervised, that their competence is regularly reviewed, and that the level of competence is appropriate to the nature of the business.

Chapter 2 (specific requirements for particular activities) – for those *firms* indicated in *TC 2.1.1R* who are involved in specified activities, such as *advising on investments* or on *regulated mortgage contracts* (see, generally, *TC 2.1.4R*), we have set additional training and competence requirements over and above the Commitments. These extra requirements cover recruitment, training, attaining competence, (in some cases this includes a requirement for individuals to pass an examination), maintaining competence, and the supervision of individuals.

It should be noted that Chapter 2 only applies in relation to advising on *non-investment insurance contracts* where this activity is carried on with or for *retail customers*.



We will use the data we collect in this section to assess the nature of *firms'* compliance with training and competence requirements.

*Firms* that have *appointed representatives* ('ARs') should note that the information submitted in this section should include its ARs as well as the *firm* itself.

### Section G: guide for completion of individual fields

Total number of all staff	<p>This should be the total number of staff that worked for the <i>firm</i> as at the end of the reporting period.</p> <p>Therefore, employees that may have advised during the period but were not employed as at the end date should <b>not</b> be included.</p>
Of which:	
Number of staff that give advice	<p>'Advice' is given where the sale of a product is based on a recommendation given to the <i>customer</i> on the merits of a particular product.</p> <p>If staff advise in relation to more than one business type (i.e. mortgage advising, advising on <i>non-investment insurance contracts</i> or retail investment products), they should be counted in each applicable field. The 'total' in the right hand column field should be the actual number of applicable employees, however, rather than a total of the three columns.</p> <p>Note: in relation to advising on <i>non-investment insurance contracts</i>, this total should <b>not</b> include employees that do not advise <i>retail customers</i>.</p>
Number of staff that supervise others to give advice	<p>Note the requirements in the Training &amp; Competence Sourcebook (TC 2.4, 2.6 and 2.7) for employees to be appropriately supervised, and also the competencies that are required for those who supervise others.</p> <p>If any of these staff carries out supervisory activities in relation to more than one business type, they should be counted in each applicable field. The 'total' in the right hand column field should be the actual number of applicable employees, however, rather than a total of the three columns.</p>
Number of advisers that have been assessed as competent	<p>This is a subset of the total of 'number of staff that give advice' above.</p> <p>See TC 2.1.4R for the detailed training &amp; competence requirements relating to individual activities.</p> <p>If staff are competent in relation to more than one business type, they should be counted in each applicable field. The 'total' in the right hand column field should be the actual number of applicable employees, however, rather than a total of the three columns.</p>

Number of advisers that have passed <i>approved examinations</i>	<p>This is a subset of the total in ‘number of staff that give advice’ above.</p> <p>In the case of certain activities, <i>TC 2</i> imposes requirements on <i>firms</i> in relation to their <i>employees</i> and passing <i>approved examinations</i>. See, for example, requirements relating to <i>employees</i> engaged in <i>advising a customer on a regulated mortgage contract</i> other than a <i>regulated mortgage contract</i> that the firm has concluded solely for a business purpose (Table <i>TC 2.1.4R (1)(p)</i>), and requirements relating to <i>employees</i> engaged in <i>advising on investments</i> which are <i>packaged products</i> (Table <i>TC 2.1.4R (1)(f)</i>).</p> <p>If staff have qualifications in relation to more than one business type, they should be counted in each applicable field. The ‘total’ in the right hand column field should be the actual number of applicable employees, however, rather than a total of the three columns.</p>
Number of advisers that have left since the last reporting date	<p>This is the total number of advisory staff that have left the <i>firm</i> during the current reporting period.</p> <p>If any of these staff used to carry out advisory activities in relation to more than one business type, they should be counted in each applicable field. The ‘total’ in the right hand column field should be the actual number of applicable employees, however, rather than a total of the three columns.</p>
Number of staff that take private customers through stakeholder pension scheme decision trees	See <i>TC 2.1.4R Table (2)(e)</i> .
Number of staff that supervise non-advised sales of lifetime mortgages	The reason this information is required is because the detailed requirements in <i>TC 2</i> are extended to staff that supervise non-advised sales of <i>lifetime mortgages</i> where filtering questions are used, because of the higher risks associated with these products (see <i>TC 2.1.4R Table (2)(g)</i> ).
Number of staff that design filtering questions for non-advised sales of lifetime mortgages	<p>The reason this information is required is because the detailed requirements in <i>TC 2</i> are extended to staff involved in designing filtering questions for the non-advised sale of <i>lifetime mortgages</i>, because of the higher risks associated with these products (see <i>TC 2.1.4R Table (1)(q)</i>).</p> <p>Note: we would expect this total to include staff that supervise and/or sign off filtering questions as well as those that actually design them.</p>

## Section H: Conduct of Business (‘COB’) Data

In this section we are seeking data from *firms* in relation to:

- the various sources of business;
- advertising;
- commission clawback (*retail investment firms* only);
- monitoring of *appointed representatives*.

We will use the data collected in this section to establish the extent and nature of *firms’* business, and thereby assess the potential risks posed by *firms’* business activities.

*Firms* that have *appointed representatives* ('ARs') should note that the information submitted in this section should take account of the business generated by its ARs as well as the *firm* itself.

### **Sub-headings: sources of business/advertising**

This information is being requested to provide high level data on the ways in which *firms* attract business. This will assist the *FSA* in targeting its supervisory resources towards those areas of the sales process and market where risks to consumers appear to be greatest. For example, we might use supervisory resources to look at all *firms* in a certain area that advertise in print media.

### **Sub-heading: general COB data**

In this sub-section we are requesting general information on the *firm's* conduct of business.

### **Sub-heading: Clawed back commission (retail investment firms only)**

Commission is typically paid to advisers in two main ways:

- non-indemnity commission - this is where payments from providers/lenders to advisers are non-refundable should the policy lapse, cancel or be surrendered.
- indemnity commission – this is colloquially referred to as 'up-front' commission and describes the situation where a provider would pay an adviser an amount of money based on a percentage of the first year's premiums for a regular premium contract. This sum is paid immediately on commencement, on the assumption that the policy will stay in force for a number of months/years ('the earnings period'). Should the *customer* stop paying premiums within the 'earnings period' (generally between 24 & 48 months) then the provider would ask the adviser to repay the 'unearned' commission. This is known as 'clawback'.

### **Sub-heading: monitoring of *appointed representatives***

An appointed representative ('AR') is a *person* (other than an *authorised person*) who:

- (a) is a party to a contract with an *authorised person* (his *principal*) which:
  - (i) permits or requires him to carry on business of a description prescribed in the *Appointed Representatives Regulations*; and
  - (ii) complies with such requirements as are prescribed in those Regulations; and
- (b) is someone for whose activities in carrying on the whole or part of that business his *principal* has accepted responsibility in writing; and who is therefore an *exempt person* in relation to any *regulated activity* comprised in the carrying on of that business for which his *principal* has accepted responsibility.

A *firm* has significant responsibilities in relation to an AR that it has appointed, which are set

out in detail in SUP 12. In summary, the *firm* is responsible, to the same extent as if it had expressly permitted it, for anything the *appointed representative* does or omits to do, in carrying on the business for which the *firm* has accepted responsibility.

Before a *firm* appoints a *person* as an *appointed representative*, and afterwards **on a continuing basis**, it should take reasonable care to ensure that:

- (1) the appointment does not prevent the *firm* from satisfying and continuing to satisfy the *threshold conditions*;
- (2) the *person*:
  - (a) is solvent;
  - (b) is suitable to act for the *firm* in that capacity; and
  - (c) has no *close links* which would be likely to prevent the effective supervision of the *person* by the *firm*; and
- (3) the *firm* has adequate:
  - (a) controls over the *person's regulated activities* for which the *firm* has responsibility (see SYSC 3.1); and
  - (b) resources to monitor and enforce compliance by the *person* with the relevant requirements applying to the *regulated activities* for which the *firm* is responsible and with which the *person* is required to comply under its contract with the *firm*.

Accordingly, *firms* are required to monitor and oversee the activities of their ARs. It is the *firm's* responsibility to be able to demonstrate that it has adequate procedures and resources in place to monitor these activities.

By collecting the high level data required in this sub-section, we will be able to gain an understanding of the methods that *firms* are employing to remain in compliance with the monitoring requirements. This will be used to inform thematic and/or *firm-specific* work in this area.

## Section H: guide for completion of individual fields

<b>Sources of Business</b> Sources of business: please tick all that apply, or confirm here that there have been no changes since the last reporting date	The purpose of the 'no changes' checkbox is so that <i>firms</i> do not have to fill in the same information each quarter when it has not changed.  If the <i>firm</i> is reporting for the first time, you should leave this field blank and complete the data fields below.
Marketing lists	This is where a <i>firm</i> uses a commercially obtained list of potential <i>customers</i> to carry out marketing of its services.
Referrals from non-authorised introducers	A non-authorised introducer is a <i>person</i> who is neither authorised by the FSA nor an <i>appointed representative</i> , and who introduces business to <i>firms</i> or <i>appointed representatives</i> .  This would include a non-authorised professional firm that refers business to an APF.
Referrals from intermediaries	Referrals from other intermediaries, including <i>appointed representatives</i> .
Telephone sales	Sales arising solely from telephone conversations with the <i>customer</i> .

Cold calling	See <i>COB</i> 3.10, and <i>MCOB</i> 3.7.
Sales visits	Sales arising from a visit to the <i>customer</i> by the <i>firm</i> .
Postal sales	Sales arising solely by exchange of postal correspondence.
Direct offer financial promotions	See <i>Glossary</i> definition.
Repeat customers	Sales made to <i>customers</i> who had previously transacted business with the <i>firm</i> .
Internet Sales	Sales arising from the <i>customer's</i> use of the internet. This could include business originated from the <i>firm's</i> internet advertising (website or directory membership), or sales transacted online.
Other	Any other sources of business not covered in this section.
<b>Advertising</b>	
Does your firm approve financial promotions (including qualifying credit promotions)?	A financial promotion is an invitation or inducement to <i>engage in investment activity</i> . This question relates to approval of the content of the <i>financial promotion</i> for the purposes of section 21 of the <i>Act</i> .  'Qualifying credit' is defined in the <i>Glossary</i> .  See, generally, <i>AUTH</i> Appendix 1 for <i>guidance on financial promotion</i> and related activities.
Types of advertising: please tick all that apply, or confirm here that there have been no changes since the last reporting date	The purpose of this question is so that <i>firms</i> do not have to fill in the same information each quarter when it has not changed.  If the <i>firm</i> is reporting for the first time, you should leave this field blank and complete the data fields below.
Do you use one or more lists or panels of preferred product providers?  If yes, indicate the applicable types of business	You should indicate here the types of business in respect of which the <i>firm</i> uses lists or panels.
What (if known) is the total number of providers on the panel(s)?	If the <i>firm</i> compiles its own panel(s), you should state here the total number of product providers that are included as at the reporting date.  It is acceptable to leave this field blank if, for example, the <i>firm</i> uses a panel or panels compiled by a product provider or packager firm.
How often (if known) are the panel(s) reviewed?	If the <i>firm</i> compiles its own panel(s), you should state the frequency with which the panel or list is reviewed and amended as appropriate, e.g. quarterly.  If separate panels are reviewed with differing frequencies, you should state the least frequent.  It is acceptable to leave this field blank if, for example, the <i>firm</i> uses a panel or panels compiled by a product provider or packager firm.
<b>General COB data</b>	
Do regulated activities form the core business of the firm?	'Core business' for these purposes is the activity from which the largest percentage of the <i>firm's</i> gross income is derived.  Note for an <i>authorised professional firm</i> specifying that its core business is 'professional services': if the <i>firm's</i> income from <i>regulated activities</i> is 50% or more of its total income (disregarding a temporary variation of not more than 5% over the preceding year's figure), then it should have regard to <i>IPRU(INV)</i> 2.1.2R (4) and give notification to the <i>FSA</i> .

If not, specify type of core business	<p>Where applicable, the <i>firm</i> should specify its core business from the following:</p> <p><b>Motor</b> Dealer (includes commercial vehicles, motorcycles and scooters, new &amp; used vehicles) Hire/Lease of vehicles Mobility &amp; Access Equip./Vehicles Other</p> <p><b>Associations or Institutions</b> Utilities Trade Union University Housing Association &amp; Trust Trade Body Sports Club &amp; Association Other</p> <p><b>Retail - Goods</b> Electrical Appliance Retailer Furniture Retailer Mobile Telephones Sports Equipment (e.g. Fishing Tackle, Golf) Caravans &amp; Mobile Homes Other goods (e.g. Photographic, coin &amp; stamp dealers )</p> <p><b>Service sector</b> Travel (e.g. booking accommodation &amp; holidays) Supermarket Veterinary Surgeon Removals (e.g. domestic, business &amp; overseas) Property management (including overseas) Building improvements/extensions (e.g. bathroom, kitchen, conservatories) Other services (e.g. Post Offices, Hire Services)</p> <p><b>Other</b> if none of the above categories is applicable to the <i>firm's</i> business, e.g. loss assessor, professional services provided by an <i>authorised professional firm</i>.</p>
Do you give independent advice?	You should state 'yes' if the <i>firm</i> gives advice on regulated products or services that is independent of product providers or marketing groups.
<b>Clawed back commission (retail investment firms only)</b>	
Clawed back commission by:	
Number	Number of policies where cancellations have led to commissions being clawed back during the reporting period.
Value	Total value of clawed back commission during the period.
<b>Complaints</b>	
Does the firm have complaints handling procedures?	<p><i>DISP</i> 1.2 requires that all <i>firms</i> that conduct business with <i>eligible complainants</i> have in place appropriate and effective written complaint handling procedures.</p> <p>Additionally, <i>firms</i> that carry on <i>insurance mediation</i> are required to have a complaints handling procedure for all complaints, including those from non-eligible complainants (see <i>DISP</i> 1.2.1A R).</p>

<b>Monitoring of Appointed Representatives ('ARs')</b>	
Number of ARs registered with the firm	Total number of ARs for which the <i>firm</i> has regulatory responsibility, as at the reporting date.
Of which, number of 'secondary' ARs	An AR is a secondary AR if: <ul style="list-style-type: none"> <li>the activities for which it is exempt are limited to <i>insurance mediation activities</i> only; and</li> <li>its principal purpose is to carry on activities other than <i>insurance mediation activities</i>.</li> </ul>
Of which, number of introducer ARs	See <i>Glossary</i> definition
Number of advisers within ARs	This should be the total of advisory staff across all of the <i>firm's</i> appointed representatives. Advisory staff are those that advise <i>customers</i> on the merits of purchasing a particular product.  By definition this total will not include staff at introducer ARs.
Does the firm have appropriate systems and procedures in place to ensure that the activities of its ARs are effectively monitored and controlled?	A summary of the <i>firm's</i> responsibilities under SUP 12 is set out under the sub-heading "monitoring of appointed representatives" above. The <i>firm</i> should be able to demonstrate that it has been in compliance with the requirements in SUP 12 throughout the reporting period.
Number of ARs that have been subject to monitoring visits by the firm during the reporting period.	This is one of the ways in which <i>firms</i> with ARs may fulfil their responsibilities under SUP 12.
Number of ARs that have been subject to file reviews by the firm during the reporting period.	This is one of the ways in which <i>firms</i> with ARs may fulfil their responsibilities under SUP 12.
Number of ARs that have been subject to financial checks by the firm during the reporting period.	This is one of the ways in which <i>firms</i> with ARs may fulfil their responsibilities under SUP 12.
Has any other monitoring of ARs by the <i>firm</i> taken place?	If the <i>firm</i> uses other methods to fulfil its monitoring responsibilities under SUP 12, you should state 'yes' here.

## **Section I: supplementary product sales data**

Most of the product sales data ('PSD') required by the *FSA* is collected quarterly from product providers. However, this process does not include all types of *non-investment insurance contract*, and also leaves other gaps in data on sales, which we aim to fill by means of the data collected in this section.

We use this data in conjunction with PSD to identify market trends and thus inform our thematic supervision work. In addition to this, we may use the combined sales data to form a view about the state of affairs of individual *firms*, which may inform supervisory or other action.

*Firms* that have *appointed representatives* ('ARs') should note that the information submitted in this section should also take account of the business of its ARs as well as the *firm* itself.

### **Sub-heading: (i) non-investment insurance product information**

In this section *firms* are asked for aggregate data on their non-investment insurance advising and arranging activities (with *retail customers*). The information required is an indication of

the product types in which the *firm* has been active during the reporting period, and a further indication of how significant this activity is (i.e. whether it forms more than 40% by premium of all of the *firm's* retail non-investment insurance activities)

This information enables us to ascertain the importance of each product type to the *firm* and to target thematic work in this area.

### **Sub-heading: (ii) Dealing as agent for *non-investment insurance contracts***

This section captures transactions with *retail customers* by *firms* with delegated authority (e.g. where the *firm* can bind risks on behalf of the *insurance undertaking* without further reference to the *insurance undertaking*). *Firms* are required to submit aggregate volumes and value of this business, and to indicate which products they have dealt in.

*Firms* are also required to indicate whether this business is significant. 'Significant', in this context, is where the premium collected in relation to business where the *firm* dealt as agent amounts to (a) more than 40% of premium collected for all non-investment insurance business, or (b) more than 40% of premium collected for all business in a particular product).

Again, this enables us to ascertain the importance of this business to the *firm* and to target thematic work in this area.

### **Sub-heading: (iii) non-investment insurance chains**

It is common practice in the non-investment insurance market for some *firms* to pass their business to another intermediary rather than directly to the product provider, forming a 'chain'. Product Sales Data only identifies the *firm* that has submitted the business to the product provider, although this may not necessarily be the intermediary that originated the sale. This section captures data on sales that form part of chains. Collecting information on gross and net brokerage (as outlined in section B1 above) gives us some information about the extent to which a *firm* is part of a chain, and to supplement this, we are requesting the following data in this section:

- (1) the total of premium from *non-investment insurance contracts* that is derived from sales to *retail customers*;
- (2) whether transactions in the listed product types have been passed up a chain;
- (3) whether this business is significant. 'Significant', in this context, is where the premium collected in relation to business forming part of a chain amounts to (a) more than 40% of premium collected for all non-investment insurance business, or (b) more than 40% of premium collected for all retail business in a particular product; and
- (4) whether, in relation to this business, the *firm* has dealt directly with the *customer* during the reporting period (i.e. has been the first intermediary in the chain).

Note: Lloyd's brokers are exempt from the reporting requirement in this section.

### **Sub-heading: (iv) claims handling**



The activity of ‘**assisting in the administration and performance of a contract of insurance**’ encompasses claims handling on behalf of *customers*, and this section aims to capture information on claims handling that is not collected from product providers as part of PSD.

This enables us to ascertain the importance of this activity to the *firm* and to target thematic work in this area. *Firms* should note that where claims are handled on behalf of an *insurer* only, this does not constitute a *regulated activity*.

### **Sub-heading: (v) Lloyd’s brokers – product sales data**

This information is required because data on business placed through Lloyd’s is not collected as part of product sales data. To fill the gap, this section requires Lloyd’s brokers to submit data on the percentage of revenue earned through their *regulated activities* that is derived from retail, commercial and reinsurance business. This information is used alongside the product sales data to inform our thematic supervision work.

### **Section I: guide for completion of individual fields**

<b>(i) non-investment insurance product information</b>	
Please indicate in column A each product type where the firm has advised or arranged transactions for retail customers during the reporting period	You should state ‘yes’ in column A for each relevant product.
Please indicate in column B where the firm’s retail business in the product type formed more than 40% by premium of all of its non-investment insurance activities.	You should state ‘yes’ in column B for each relevant product, based on an estimate of the percentage of business. If you think the product might account for more than 40% of business but are not sure, you should state ‘yes’.
<b>(ii) non-investment insurance chains</b>	
Total non-investment insurance premium derived from retail customers	You should state here the total of premiums paid by <i>retail customers</i> during the reporting period in relation to non-investment insurance products.
Of this business, please indicate in column C the products where retail sales were passed up a chain and in column D where this business is significant (see notes above)	You should state ‘yes’ in column C for each product in which transactions have been passed up a chain.  If this business is significant (see definition above) for one or more product types, this should be indicated in column D.
Please also indicate in column E where the firm has dealt directly with the retail customer within the chain	<i>Firms</i> should also indicate in column E the product types for which they transact business in a chain, but directly with the <i>customer</i> .
<b>(iii) dealing as agent</b>	
Number of sales to retail customers during the reporting period where the firm dealt as agent	You should state here the number of sales during the reporting period where the <i>firm</i> dealt as agent of a product provider (i.e. with delegated authority).
Premium paid by retail customers during the reporting period where the firm dealt as agent	You should state here the total value of premiums from policyholders during the reporting period, where the <i>firm</i> dealt as agent of a product provider (i.e. with delegated authority).  For regular premium business, annualised figures should be used.
Of the total of these sales, please indicate in column F the products where the firm dealt as agent, and in column G where this business is significant (see notes above)	You should state ‘yes’ in column F for each product in which the <i>firm</i> has dealt as agent, and also in column G for each product type where this business is significant.

<b>(iv) claims handling</b>	
If you assist in the administration and performance of contracts of insurance: Please provide: Number of claims handled on behalf of customers during the reporting period	If you are authorised to <i>assist in the administration and performance of a contract of insurance</i> on behalf of <i>customers</i> , you should state here the number of new insurance claims that have been handled on <i>customers'</i> behalf during the reporting period.
<b>(v) Lloyd's brokers - product sales data</b>	
% of regulated business revenue	This should be a summary of the percentages of the <i>firm's</i> revenue in relation to retail, commercial and reinsurance business: <b>Retail:</b> insurance offered to individuals as opposed to commercial entities. <b>Commercial:</b> insurance taken out by a commercial entity (as opposed to an individual). <b>Reinsurance:</b> insurance protection taken out by an insurer to limit its aggregation of exposure on business written.  Figures may be rounded to the nearest 20%, but the total should be 100%.
Product types:	The product types in this table are defined in the Interim Prudential sourcebook for insurers (' <i>IPRU(INS)</i> ')

## Section J: data required for calculation of fees

This information is required so that we can calculate the fees payable by *firms* in respect of the *FSA*, Financial Ombudsman Service ('*FOS*') and the Financial Services Compensation Scheme ('*FSCS*').

The precise way in which these fees will be calculated is still under consultation. Therefore, further information on the completion of these data fields will be provided in due course.

<b>Income for fees calculations</b>	<i>Firms</i> will need to report data for the purpose of calculating <i>FSA</i> , <i>FOS</i> and <i>FSCS</i> levies. The rules to implement these measures will be subject to consultation in 2004 (see below).
FSA	The formal rules for calculating <i>FSA</i> fees will be subject to consultation in the second quarter ('Q2') of 2004, and will become final <i>handbook</i> text in Q3 2004.
FOS	<b><i>Mortgage mediation</i></b> and <b><i>insurance mediation</i></b> : the formal rules for calculating <i>FOS</i> fees will be subject to consultation in March 2004, and will become final <i>handbook</i> text in Q3 2004.  <b><i>Retail investment activities</i></b> : consultation dates to be confirmed.
FSCS	<b><i>Mortgage mediation</i></b> and <b><i>insurance mediation</i></b> : the formal rules for calculating <i>FSCS</i> fees will be subject to consultation in March 2004, and will become final <i>handbook</i> text in Q3 2004.  <b><i>Retail investment activities</i></b> : consultation dates to be confirmed.

## **Mortgage Lending and Administration Return ('MLAR')**

**Illustration of reporting requirements for firms carrying on mortgage lending and administration activities**

**Sup 16 Ann 19AR MORTGAGE LENDING & ADMINISTRATION RETURN ('MLAR')**

<b>Summary of Contents</b>	Table
Balance Sheet	A
Profit & Loss Account	B
Capital	C
Lending - Business flows & rates	D
Residential Lending to individuals - New business profile	E
Lending - Arrears analysis	F
Mortgage administration - Business profile	G
Mortgage administration - Arrears analysis	H
Fee tariff measures	J

**A BALANCE SHEET**

(£000s)

**A**

		<i>Balance at end of quarter</i>			<i>Balance at end of quarter</i>
<b>A1</b>	<b>Assets</b>			<b>A2</b>	<b>Liabilities</b>
A1.1	Fixed assets			A2.1	Shareholders' funds
A1.2	Intangible assets	_____		A2.2	Minority interests
A1.3	Tangible assets	_____		A2.3	Provisions for liabilities and charges
A1.4	Investments	_____		A2.4	Creditors
A1.5	Current assets:			A2.5	Amounts falling due within one year
A1.6	Loans to customers	_____		A2.6	Amounts falling due after more than one year
A1.7	Stocks	_____		A2.7	Other liabilities
A1.8	Debtors	_____		A2.8	TOTAL LIABILITIES
A1.9	Investments	_____			
A1.10	Cash at bank and in hand	_____			
A1.11	Other current assets	_____			
A1.12	TOTAL ASSETS				

		<u><i>Unsecured balances</i></u>			<u><i>Securitized balances</i></u>			
		<i>Gross balances</i>	<i>Provisions</i>	<i>Net balances</i>	<i>Gross balances</i>	<i>Provisions</i>	<i>Non recourse finance</i>	<i>Net balances</i>
<b>A3</b>	<b>Analysis of loans to customers</b>							
A3.1	Residential loans to individuals							
A3.2	Regulated	_____	_____	_____	_____	_____	_____	_____
A3.3	Non regulated	_____	_____	_____	_____	_____	_____	_____
A3.4	Other secured loans	_____	_____	_____	_____	_____	_____	_____
A3.5	Other loans	_____	_____	_____	_____	_____	_____	_____
A3.6	All loans to customers							

NB: A3.6[col 3] + A3.6[col 7] = A1.6

**B PROFIT AND LOSS ACCOUNT**

(£000s)

**B**

B0	Financial year -to-date is <input type="text"/> months (ie 3,6,9 or 12)	B2 Provisions analysis	<i>Provisions balance at start of financial year</i>	<i>Write offs in financial year to date</i>	<i>Provisions charge in financial year to date</i>	<i>Provisions balance at period end</i>
<b>B1 Summary Profit &amp; Loss Account</b>						
<u>Income</u>						
B1.1 Gross profit on non-financial activities	_____	B2.1 Residential loans to individuals				
B1.2 Interest receivable	_____	B2.2 Regulated	_____	_____	_____	_____
B1.3 Interest payable	_____	B2.3 Non regulated	_____	_____	_____	_____
B1.4 Net interest receivable	_____	B2.4 Other secured loans	_____	_____	_____	_____
B1.5 Fees and commissions receivable	_____	B2.5 Other loans	_____	_____	_____	_____
B1.6 Profits on dealing investments	_____	B2.6 All loans to customers	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
B1.7 Other income	_____					
B1.8 TOTAL Income	<input type="text"/>					
<u>Expenditure</u>						
B1.9 Staff costs	_____					
B1.10 Fees and commissions payable	_____					
B1.11 Occupancy	_____					
B1.12 Other operating expenses	_____					
B1.13 Other expenses	_____					
B1.14 Total Expenses	<input type="text"/>					
B1.15 OPERATING PROFIT (= B1.8 - B1.14)	<input type="text"/>					
B1.16 Provisions	_____					
B1.17 Taxation	_____					
B1.18 Minority interests	_____					
B1.19 PROFIT FOR THE FINANCIAL PERIOD (= B1.15 - B1.16 - B1.17 - B1.18)	<input type="text"/>					
B1.20 Dividends paid and proposed	_____					
B1.21 Retained profit for the financial period (= B1.19 - B1.20)	_____					

**C CAPITAL**

(£000s)

**C**

CAPITAL RESOURCES		CAPITAL REQUIREMENTS	
		<i>Balance at quarter end</i>	
<b>C1 Eligible capital</b>		<b>C4 For a lender, or an administrator with administered assets on its balance sheet.</b>	
			<i>Balance at quarter end</i>
C1.1 Reserves	_____	C4.1 Asset based measure:	
C1.2 Interim profits	_____	C4.2 Total assets	_____
C1.3 Issued capital	_____	C4.3 Undrawn commitments	_____
C1.4 General Provisions	_____	C4.4 Intangible assets	_____
C1.5 Other eligible capital	_____	C4.5 Total adjusted assets	<input type="text"/> (= C4.2 + C4.3 - C4.4)
C1.6 Total Eligible Capital	<input type="text"/>	C4.6 CAPITAL REQUIREMENT:	
		a) Minimum	_____ 100 reflecting minimum capital of £100,000
		b) 1% of C4.5	_____ using asset based measure
		c) Actual requirement	<input type="text"/> being the higher of a) and b)
<b>C2 Deductions from capital</b>		<b>C5 For an administrator not having administered assets on its balance sheet.</b>	
			<i>Latest financial year ending / /</i>
C2.1 Investments in own shares	_____		<i>Estimated current financial year ending / /</i>
C2.2 Intangible assets	_____	C5.1 Income based measure :	
C2.3 Interim net losses	_____	C5.2 Total income	_____
C2.4 Other deductions	_____	C5.3 Relevant adjustments	_____
C2.5 Total Deductions	<input type="text"/>	C5.4 Total relevant income	<input type="text"/> (= C5.2 - C5.3)
<b>C3 CAPITAL RESOURCES (= C1.6 - C2.5)</b>	<input type="text"/>	C5.5 CAPITAL REQUIREMENT:	
		a) Minimum	_____ 100 _____ 100 reflecting minimum capital of £100,000
		b) 10% of C5.4	_____ using income based measure
		c) Actual requirement	<input type="text"/> <input type="text"/> being the higher of a) and b)

**D(1) LENDING : Business flows & rates**

(£000's)

D(1)

	<i>Balance at end of previous quarter</i>	<i>Advances made in quarter</i>	<i>Repayment of principal</i>	<i>Write offs in quarter</i>	<i>Other debits/ (credits) and transfers (net)</i>	<i>Balance at end of quarter (a)</i>
<b>D1 Loans: Advances/Repayments</b>						
Residential lending to individuals :						
D1.1 Regulated						
D1.2 Non regulated						
D1.3 Other secured loans						
D1.4 TOTAL Secured loans						

a) Column 6 = Col 1 + Col 2 - Col 3 - Col 4 + Col 5

**Transactions in quarter included in D1 [column 5]**

**Balance at end quarter on loan**

	<i>Loans acquired</i>	<i>Loans sold</i>	<i>Loans securitised</i>	<i>Other</i>	<i>Total (b)</i>	<i>assets subject to non-recourse funding</i>
<b>D2 Loans: Book movements</b>						
Residential lending to individuals :						
D2.1 Regulated						
D2.2 Non regulated						
D2.3 Other secured loans						
D2.4 TOTAL Secured loans						

(b) D1 column [5] = D2[Col 1 - Col 2 - Col 3 + Col 4]

**Balances at end of quarter**

**Interest rates at end of quarter (to 2 decimal places)**

	<i>TOTAL £000s</i>	<i>Of which at :</i>		<i>Of which at :</i>			<i>Weighted average nominal annual rate on all balances</i>			
		<i>Fixed rates</i>	<i>Variable rates</i>	<i>less than 2% above BBR</i>	<i>2 &lt; 3% above BBR</i>	<i>3 &lt; 4% above BBR</i>	<i>4% or more above BBR</i>	<i>balances at fixed rates</i>	<i>balances at variable rates</i>	
		<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>%</i>	<i>%</i>	<i>%</i>
<b>D3 Loans: Interest rates</b>										
Residential loans to individuals: Regulated										
D3.1 Total book										
D3.2 Advances in quarter										
Residential loans to individuals: Non Regulated										
D3.3 Total book										
D3.4 Advances in quarter										
Other secured loans:										
D3.5 Total book										
D3.6 Advances in quarter										
All secured loans:										
D3.7 Total book										
D3.8 Advances in quarter										



**D(2) LENDING : Business flows**

(£000's)

D(2)

	<i>Commitments outstanding at end of previous quarter</i>	<i>Commitments made since end of previous quarter</i>	<i>Cancellations in quarter</i>	<i>Advances made in quarter (a)</i>	<i>Other debits/(credits) and transfers (net)</i>	<i>Commitments outstanding at end of quarter</i>
<b>D4 Loans: Advances/Repayments</b>						
Residential lending to individuals						
D4.1 Regulated						
a) House purchase	_____	_____	_____	_____	_____	_____
b) Remortgage	_____	_____	_____	_____	_____	_____
c) Other	_____	_____	_____	_____	_____	_____
d) TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.2 Non regulated						
a) House purchase	_____	_____	_____	_____	_____	_____
b) Remortgage	_____	_____	_____	_____	_____	_____
c) Other	_____	_____	_____	_____	_____	_____
d) TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.3 Other secured loans	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.4 TOTAL Secured loans	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>

a) Entries should agree with relevant items in Column 2 of D1.

		<u>Gross advances in quarter : (amount) by LTV</u>			
		<= 75 %	Over 75 <= 90 %	Over 90 <= 95 %	Over 95 %
<b>E1</b>	<b>SINGLE income multiple</b>				
	Regulated				
E1.1	Less than 2.50	_____	_____	_____	_____
E1.2	2.50 < 3.00	_____	_____	_____	_____
E1.3	3.00 < 3.50	_____	_____	_____	_____
E1.4	3.50 < 4.00	_____	_____	_____	_____
E1.5	4.00 or over	_____	_____	_____	_____
E1.6	Other	_____	_____	_____	_____
E1.7	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E1.7a	of which: Not evidenced	_____	_____	_____	_____
	Non Regulated				
E1.8	Less than 2.50	_____	_____	_____	_____
E1.9	2.50 < 3.00	_____	_____	_____	_____
E1.10	3.00 < 3.50	_____	_____	_____	_____
E1.11	3.50 < 4.00	_____	_____	_____	_____
E1.12	4.00 or over	_____	_____	_____	_____
E1.13	Other	_____	_____	_____	_____
E1.14	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E1.14a	of which: Not evidenced	_____	_____	_____	_____
	All Loans				
E1.15	Less than 2.50	_____	_____	_____	_____
E1.16	2.50 < 3.00	_____	_____	_____	_____
E1.17	3.00 < 3.50	_____	_____	_____	_____
E1.18	3.50 < 4.00	_____	_____	_____	_____
E1.19	4.00 or over	_____	_____	_____	_____
E1.20	Other	_____	_____	_____	_____
E1.21	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E1.21a	of which: Not evidenced	_____	_____	_____	_____

		<u>Gross advances in quarter : (amount) by LTV</u>			
		<= 75 %	Over 75 <= 90 %	Over 90 <= 95 %	Over 95 %
<b>E2</b>	<b>JOINT income multiple</b>				
	Regulated				
E2.1	Less than 2.00	_____	_____	_____	_____
E2.2	2.00 < 2.50	_____	_____	_____	_____
E2.3	2.50 < 2.75	_____	_____	_____	_____
E2.4	2.75 < 3.00	_____	_____	_____	_____
E2.5	3.00 or over	_____	_____	_____	_____
E2.6	Other	_____	_____	_____	_____
E2.7	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E2.7a	of which: Not evidenced	_____	_____	_____	_____
	Non Regulated				
E2.8	Less than 2.00	_____	_____	_____	_____
E2.9	2.00 < 2.50	_____	_____	_____	_____
E2.10	2.50 < 2.75	_____	_____	_____	_____
E2.11	2.75 < 3.00	_____	_____	_____	_____
E2.12	3.00 or over	_____	_____	_____	_____
E2.13	Other	_____	_____	_____	_____
E2.14	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E2.14a	of which: Not evidenced	_____	_____	_____	_____
	All Loans				
E2.15	Less than 2.00	_____	_____	_____	_____
E2.16	2.00 < 2.50	_____	_____	_____	_____
E2.17	2.50 < 2.75	_____	_____	_____	_____
E2.18	2.75 < 3.00	_____	_____	_____	_____
E2.19	3.00 or over	_____	_____	_____	_____
E2.20	Other	_____	_____	_____	_____
E2.21	TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
E2.21a	of which: Not evidenced	_____	_____	_____	_____

	<u>Regulated loans</u>				<u>Non regulated loans</u>				<u>All loans</u>			
	<u>Gross advances in quarter</u>		<u>Balances outstanding</u>		<u>Gross advances in quarter</u>		<u>Balances outstanding</u>		<u>Gross advances in quarter</u>		<u>Balances outstanding</u>	
	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>	<i>Number</i>	<i>Amount</i>
<b>E3 By credit history</b>												
E3.1 Impaired credit history												
E3.2 Other												
E3.3 TOTAL												
<b>E4 By payment type</b>												
E4.1 Repayment (capital & interest)												
E4.2 Interest only												
E4.3 Combined												
E4.4 Other												
E4.5 TOTAL												
<b>E5 By drawing facility</b>												
E5.1 Loans with extra drawing facility :												
a) Loans including unused facility												
b) Unused facility												
c) Net loans (a - b)												
E5.2 Loans with no extra drawing facility												
E5.3 TOTAL												
<b>E6 By purpose</b>												
E6.1 House Purchase:												
Owner occupation a) FTB's												
b) Other												
E6.2 Buy to let												
E6.3 Further Advance												
Remortgage:												
Own borrowers												
From other lenders												
E6.6 Lifetime Mortgage												
E6.7 Other												
E6.8 TOTAL												

**F(1) LENDING: Arrears analysis**

(£000s)

**F(1)**

Arrears categorisation by type of loan	<u>Cases entering higher (ie more serious) arrears band in quarter</u>			<u>Position on all arrears cases at end of quarter</u>			<i>Performance of current arrears cases during the quarter</i>
	<i>Number</i>	<i>Amount of arrears</i>	<i>Balance outstanding</i>	<i>Number</i>	<i>Amount of arrears</i>	<i>Balance outstanding</i>	<i>%</i>
F1 Residential loans to individuals: Regulated							
F1.1 1.5 < 2.5 %							
F1.2 2.5 < 5 %							
F1.3 5.0 < 7.5 %							
F1.4 7.5 < 10 %							
F1.5 10% or more							
F1.6 In possession							
F1.7 TOTAL							
F2 Residential loans to individuals: Non regulated							
F2.1 1.5 < 2.5 %							
F2.2 2.5 < 5 %							
F2.3 5.0 < 7.5 %							
F2.4 7.5 < 10 %							
F2.5 10% or more							
F2.6 In possession							
F2.7 TOTAL							
F3 Residential loans to individuals: All loans							
F3.1 1.5 < 2.5 %							
F3.2 2.5 < 5 %							
F3.3 5.0 < 7.5 %							
F3.4 7.5 < 10 %							
F3.5 10% or more							
F3.6 In possession							
F3.7 TOTAL							

**F(2) LENDING: Arrears analysis**

(£000s)

F(2)

Arrears categorisation by type of loan	<u>Cases entering higher (ie more serious) arrears band in quarter</u>			<u>Position on all arrears cases at end of quarter</u>			<u>Performance of current arrears cases during the quarter</u>		
	Number	Amount of arrears	Balance outstanding	Number	Amount of arrears	Balance outstanding	%		
F4 Other secured loans									
F4.1 1.5 < 2.5 %									
F4.2 2.5 < 5 %									
F4.3 5.0 < 7.5 %									
F4.4 7.5 < 10 %									
F4.5 10% or more									
F4.6 In possession									
F4.7 TOTAL									
<b>F5 Arrears management</b>	<b>Those cases no longer reported (ie not included in F1 to F4.7)</b>			<b>Arrears cases reported in F1 to F4.7 at end quarter</b>					
	<u>Possession sales during quarter</u>			<u>Capitalisation of arrears cases in quarter</u>			<u>Number of cases for which there is in place:</u>		
	Number		Balance outstanding	Number	Amount of arrears	Balance outstanding	A temporary concession	A formal arrangement	No concession arrangement
Residential loans to individuals :									
F5.1 Regulated									
F5.2 Non regulated									
F5.3 Total									
F5.4 Other secured loans									
F5.5 TOTAL									

**G0 Do you need to complete tables G and H ?**

If you have a mortgage lenders permission, and only administer your own on-balance sheet loan book, and do not have any off-balance sheet loans to administer, **then** please tick

this box ( and do not complete the rest of this section).

**Otherwise**, please complete sections G1 and G2, and table H in your capacity as a loan administrator.

		<i>Residential loans to individuals</i>		
		<i>Regulated loans</i>	<i>Non regulated loans</i>	<i>All loans</i>
<b>G1</b>	<b>Mortgage contracts administered at end of quarter</b>			
G1.1	Number of loans administered for :			
	a) Firms with a mortgage lender's permission	_____	_____	_____
	b) Other firms	_____	_____	_____
	c) SPVs	_____	_____	_____
	d) Total	<input type="text"/>	<input type="text"/>	<input type="text"/>
G1.2	Balance outstanding on loans administered for :			
	a) Firms with a mortgage lender's permission	_____	_____	_____
	b) Other firms	_____	_____	_____
	c) SPVs	_____	_____	_____
	d) Total	<input type="text"/>	<input type="text"/>	<input type="text"/>

Residential loans to individuals administered for third parties

G2 Lenders for whom mortgage administration was being carried out at end of quarter		<i>Details of lender</i>		<i>Balances outstanding at end of quarter</i>			
		<i>FSA firm reference (if available)</i>	<i>Name of firm</i>	<i>Regulated loans £000's</i>	<i>Non regulated loans £000's</i>	<i>All loans £000's</i>	
G2.1	Firms with a mortgage lenders permission : [ top 5 only]	1	_____	_____	_____	_____	
		2	_____	_____	_____	_____	
		3	_____	_____	_____	_____	_____
		4	_____	_____	_____	_____	_____
		5	_____	_____	_____	_____	_____
G2.2	Other firms : [ top 5 only]	1	_____	_____	_____	_____	
		2	_____	_____	_____	_____	
		3	_____	_____	_____	_____	_____
		4	_____	_____	_____	_____	_____
		5	_____	_____	_____	_____	_____
G2.3	SPVs: [ top 5 only]	1	_____	_____	_____	_____	
		2	_____	_____	_____	_____	
		3	_____	_____	_____	_____	_____
		4	_____	_____	_____	_____	_____
		5	_____	_____	_____	_____	_____

H(1) MORTGAGE ADMINISTRATION: Arrears analysis

(£000s)

H(1)

Arrears categorisation by type of loan	<u>Cases entering higher (ie more serious) arrears band in quarter</u>			<u>Position on all arrears cases at end of quarter</u>			<u>Performance of current arrears cases during the quarter</u>
	Number	Amount of arrears	Balance outstanding	Number	Amount of arrears	Balance outstanding	%
H1 Residential loans to individuals: Regulated							
H1.1 1.5 < 2.5 %							
H1.2 2.5 < 5 %							
H1.3 5.0 < 7.5 %							
H1.4 7.5 < 10 %							
H1.5 10% or more							
H1.6 In possession							
H1.7 TOTAL							
H2 Residential loans to individuals: Non regulated							
H2.1 1.5 < 2.5 %							
H2.2 2.5 < 5 %							
H2.3 5.0 < 7.5 %							
H2.4 7.5 < 10 %							
H2.5 10% or more							
H2.6 In possession							
H2.7 TOTAL							
H3 Residential loans to individuals: All loans							
H3.1 1.5 < 2.5 %							
H3.2 2.5 < 5 %							
H3.3 5.0 < 7.5 %							
H3.4 7.5 < 10 %							
H3.5 10% or more							
H3.6 In possession							
H3.7 TOTAL							



**Arrears categorisation  
by type of loan**

H4 [Other secured loans] [Not relevant to this analysis of arrears by Loan Administrators, but structure maintained as per table F in order to make use of the same guidance notes].

**H5 Arrears management**

Those cases no longer reported (ie not included in H1 to H3.7)

Arrears cases reported in H1 to H3.7 at end quarter

Possession sales during quarter

Capitalisation of arrears cases in quarter

Number of cases for which there is in place:

*Number*

*Balance outstanding*

*Number*

*Amount of arrears*

*Balance outstanding*

*A temporary  
concession*

*A formal  
arrangement*

*No concession  
arrangement*

Residential loans to individuals :

H5.1	Regulated								
H5.2	Non regulated								
H5.3	Total								

<b>J1</b>	<b>Fee tariff measures by regulated activity:</b>	<b>FSA measure (a)</b>	<b>FOS measure (b)</b>
J1.1	Mortgage lending activity:	<input type="text"/>	<input type="text"/>
J1.2	Mortgage administration activity:	<input type="text"/>	<input type="text"/>
J1.3	Total for these activities:	<input type="text"/>	<input type="text"/>

Notes: a), b) Details of the particular measure to be used are found in the MLAR guidance notes

It should be noted that the definitions of these measures may change from time to time, and therefore the current definitions must be established by reference to the guidance notes which provide details of where such definitions are to be found in the website version of the Handbook.

**Part 7: SUP 16 Ann 19BG**

**NOTES FOR COMPLETION OF THE MORTGAGE LENDING &  
ADMINISTRATION RETURN ('MLAR')**

**Contents**

Introduction:	General notes on the return
Section A:	Balance Sheet
Section B:	Profit & Loss Account
Section C:	Capital
Section D:	Lending: Business Flows & Rates
Section E:	Residential Lending to Individuals: New Business Profile
Section F:	Lending: Arrears Analysis
Section G:	Mortgage Administration: Business profile
Section H:	Mortgage Administration: Arrears analysis
Section J	Fee tariff measures

[Version 10 March 2004]

## INTRODUCTION: GENERAL NOTES ON THE RETURN

### 1. Introduction

This section covers a number of points that have relevance across the return generally:

- Overview
- Purpose of reporting requirements
- Regulated mortgage contracts and the wider mortgage market
- Accounting conventions
- Accuracy
- Time period
- Loans made before 31 October 2004
- Specific items:
  - (i) positions to be reported gross
  - (ii) foreign currencies

### 2. Overview of reporting requirements

The data requirements for *firms* carrying on the *regulated activities* of *mortgage lending* and *mortgage administration* consist of quarterly, half yearly and annual information. This *guidance* deals only with the quarterly requirements, however, which are referred to as the Mortgage Lending and Administration Return (*MLAR*). The remaining data requirements are applied to *firms* through existing rules within the following sections of the *Handbook*:

- the Dispute resolution: Complaints sourcebook for complaints reporting; and
- Chapter 16 of the Supervision manual for *controllers* reports (section 16.4), *close links* reports (section 16.5) and annual accounts (section 16.7).

Because the *MLAR* is activity based, it sets out the reporting requirements for a number of different *firm* types. We expect *firms* to complete the requirements as follows:

- a *firm* carrying on both *mortgage lending* and *mortgage administration* will need to complete the whole of the *MLAR*;
- a *firm* carrying on *mortgage lending* but not also *mortgage administration* will need to complete the whole of the *MLAR* except sections G and H;
- a *firm* carrying on *mortgage administration* , but not also *mortgage lending* , will need to complete sections A, B, C, G, H and J of the *MLAR*.

However, the above requirements are subject to the further details below, which are designed to avoid any duplication between *MLAR* reporting requirements and any other reporting requirements arising from the *firm's* other *regulated activities* (eg as a *bank*, *building society*, *securities and futures firm* etc). The *rules* in SUP 16 (section 16.7) provide full details of which sections of the *MLAR* do not apply for each *firm* type.

<b>Firm</b>	<b>Sections of the MLAR not required</b>
<i>Mortgage lender/administrator with no other activities (a)</i>	No duplication, so complete all sections described above this table
<i>Mortgage lender/administrator that is also subject to the RMAR (a)</i>	Duplication in RMAR, but complete all MLAR sections described above this table
<i>Securities &amp; futures firm or investment management firm</i>	A1, A2 and B1
<i>Incoming EEA firm (b)</i>	A1, A2, B1 and C
<i>UK branch of a non-EEA bank</i>	No duplication, so complete all sections described above this table
<i>Members' adviser</i>	No duplication, so complete all sections described above this table
<i>Authorised professional firm</i>	No duplication, so complete all sections described above this table
<i>Other firm types/regulated activities (except above)</i>	A1, A2, B1 and C

**Key:** **A1:** Assets **A2:** Liabilities **B1:** Profit & Loss **C:** Capital

**Note (a) :** a *firm* which is a solo-consolidated *subsidiary* of an authorised credit institution is not required to complete section C of the *MLAR*.

**Note (b) :** *Credit Institutions* passporting under *BCD* for *mortgage lending* (which also includes *mortgage administration*), or other *firms* passporting under another EU Directive for a non-mortgage activity and holding a *top-up permission* from the *FSA* for *mortgage lending* and/or *mortgage administration*. Also includes *firms* classed as "*Treaty firms*" under Schedule 4 of the *Act*. But any other *EEA firm* type should complete in full all sections of the *MLAR* described above this table, as it would not be eligible for any reduction in reporting requirements.

### **Commencement and transitional provisions**

The *MLAR* sections on **Arrears** (tables F and H) are not required to be submitted as part of a *firm's* first *MLAR* submission (in respect of the *firm's* first financial quarter starting on or after 1 April 2005). They should however be included in all subsequent quarterly submissions. A *firm* may of course submit these sections from the outset, but is not obliged to do so.

The position regarding **building society reporting** merits specific comment. Societies have previously reported a range of information on *mortgage lending* that has much in common with certain sections of the *MLAR*. Now mortgage reporting requirements have been finalised, societies' existing reporting will change from the implementation of the *MLAR* to avoid duplication. When societies begin to submit the *MLAR*, they will no longer be required to submit the following sections of the QFS1:

- QFS1 table G (1): All sections
- QFS1 table G (2): All sections
- QFS1 table J: Sections J2 and J3 only (Note (a))
- QFS1 table K (1): Sections K1 and K2 only
- QFS1 table K (2): Sections K4 and K5 only (Note (a))

**Note (a):** These sections should however continue to be completed in respect of *subsidiaries* that hold mortgages but which are not required to complete the *MLAR* (ie they are not authorised to undertake a *mortgage lending* activity).

**NB:** A society may however continue to submit these sections of the QFS1, if it so wishes (in addition to the *MLAR*). This option is intended to cater for those circumstances where a society has automated the production of its QFS1 and wishes to avoid additional work involved in cutting back on reporting as specified above.

### 3. Purpose of reporting requirements

The reasons why the *FSA* requires this data from *mortgage lenders* and *administrators* are as follows:

- to assess the probability of the failure of *firms* and the impact of failure on the ability of the *FSA* to meet its statutory objectives, including an assessment of compliance with the *threshold conditions*;
- to assist with prudential supervision of *firms*; and
- to help assess the risks in the mortgage market as a whole to inform, for example, the *FSA*'s thematic work. By this we mean that we will use some of our supervisory resources to examine issues (known as 'themes') that affect a number of *firms* rather than *firms* individually. The data collected will be considered alongside other information we receive, to identify trends and issues that inform our supervision of *firms*.

The *MLAR* requires *mortgage lenders* and *administrators* to submit four types of data:

- financial data to assist in the prudential supervision of *mortgage lenders* and *administrators*. A quarterly financial return is required, including a balance sheet and profit and loss account;
- quarterly reporting of quantitative and qualitative data by all *mortgage lenders* and *administrators* to enable monitoring of compliance with the requirements of *MCOB*;
- quarterly provision of qualitative mortgage information by all *mortgage lenders* and *administrators* to enable the *FSA* to understand developments in the mortgage markets as a whole, and to inform future policy developments and prudential supervision; and

- quarterly information on fee tariff measures.

The reporting requirements set out in the *MLAR* will enable the *FSA* to realise these information needs. In particular:

**Tables A to C:** provide the framework for the *FSA*'s financial monitoring and prudential supervision of *mortgage lenders* and *administrators*;

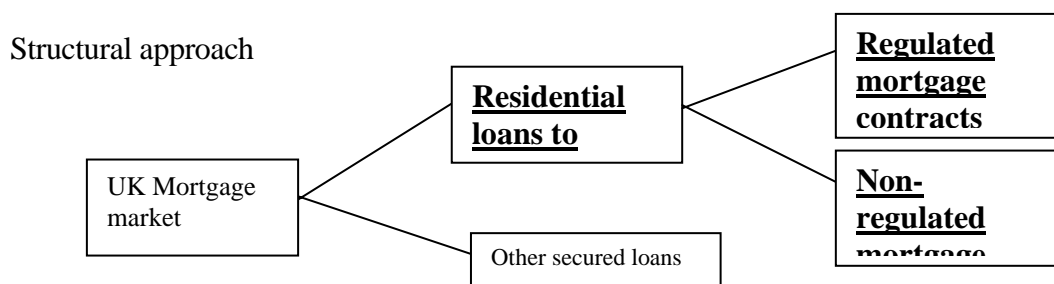
**Tables D to F:** provide the framework for the provision of qualitative mortgage information by *mortgage lenders*

**Table G, H:** provides the framework for the *FSA*'s monitoring of mortgage administration activities.

**Table J** provides information on fee tariff measures for *mortgage lenders* and *administrators*.

#### 4. Regulated mortgage contracts and the wider mortgage market

Given this background to reporting requirements, the *FSA*'s approach to obtaining information on *mortgage lending* has been structured so that ***regulated mortgage contracts*** are seen within the wider context of the **UK mortgage market as a whole**. This approach can be illustrated as follows:



Each of these key terms is explained below:

(i) **UK Mortgage market**

This refers to all lending secured on land and buildings in the United Kingdom, whether to individuals, housing associations or corporates. However, given the importance of mortgages to individuals we have chosen to look at the market in terms of two components, namely 'residential lending to individuals' and 'other secured lending'.

(ii) **Residential loans to individuals**

This is a discrete category of the mortgage market, and has characteristics (e.g. in terms of products, lending criteria and methods of credit assessments) that are often markedly different from those applying to other types of secured lending (e.g. to corporates).

It is lending to individuals secured by mortgage on land and buildings where the lender has either a first or second (or subsequent) charge, where at least 40% of the land and buildings is used for residential purposes, and where the premises are for occupation by either the borrower (or dependant), or any other third party (e.g. it includes 'buy to let' lending to individuals)

**Regulated mortgage contracts** are therefore a subset of this market category.

Examples of **non-regulated mortgage contracts** which fall under the wider category of residential loans to individuals include: buy-to-let loans and other types of loan where the property is not for use by the borrower (or qualifying dependants); residential loans to individuals where the lender does not have a first charge.

It is important, therefore, to separate this category from all other forms of secured lending.

(iii) **Other secured lending**

This covers all other forms of lending secured on land and buildings in the United Kingdom. Primarily it covers secured lending to corporate bodies (including to housing associations), but it also includes lending to individuals which, although being secured on land and buildings, is not deemed to be residential (e.g. the residential element is less than 40%).

(iv) **Regulated mortgage contract**

This is defined in the *Handbook* as follows:

- (a) (in relation to a contract) (in accordance with article 61(3) of the *Regulated Activities Order*) a contract which, at the time it was entered into, meets the following conditions:
- (i) a lender provides credit to an individual or to trustees (the 'borrower'); and
  - (ii) the obligation of the borrower to repay is secured by a first legal mortgage on land (other than timeshare accommodation) in the United Kingdom, at least 40% of which is used, or is intended to be used, as or in connection with a dwelling by the borrower or (in the case of credit provided to trustees) by an individual who is a beneficiary of the trust, or by a person who is in relation to the borrower or (in the case of credit provided to trustees) a beneficiary of the trust:
    - (A) that person's spouse; or
    - (B) a person (whether or not of the opposite sex) whose relationship with that person has the characteristics of the relationship between husband and wife; or
    - (C) that person's parent, brother, sister, child, grandparent or grandchild.



- (b) (in relation to a *specified investment*) the *investment*, specified in article 88 of the *Regulated Activities Order*, which is rights under a *regulated mortgage contract* in (a).

This means that in relation to a *regulated mortgage contract*, the following conditions must all be satisfied:

- the borrower must be an individual or trustee;
- the lender must take a first legal mortgage over *UK* property; and
- the property must be at least 40% occupied by the borrower or his immediate family.

The definition of a *regulated mortgage contract* means that many kinds of loan are caught by regulation, not just loans for house purchase. For example it includes a significant amount of short-term first charge lending. This includes lending for home improvements (including some in-store credit), lending for debt consolidation, lending to finance a business, and some specific banking products such as secured overdrafts, secured credit cards, bridging loans and loans secured by all monies charges.

## 5. Accounting conventions

Unless the contrary is stated in these guidance notes, the return should be compiled using generally accepted accounting practice.

## 6. Accuracy

It is expected that entries on the return will be actual values, or in some cases close approximations established or drawn from the *firm's* systems and prepared on the basis of being the best information in the time available for their compilation.

If such 'close approximations' are considered by the *firm* as likely to be materially different from the underlying actual values, the *firm* should advise its supervisory team of data items affected.

## 7. Time periods

Where stock figures are required (e.g. balance sheet, capital position etc) the information is required as at the *firm's accounting reference date* and the three quarter ends following this date (see SUP 16.3.13R).

Where flow figures are required, these are either for **3 months only** (i.e. the latest quarter) as in for example lending figures in tables D and E, or **cumulative in the 'year to date'**, (e.g. profit and loss in table B etc), covering the period from the *firm's accounting reference date* to the end of the reporting quarter.

## 8. Loans made before 31 October 2004

Any loans made before 31 October 2004, that otherwise satisfy the specific requirements of a *regulated mortgage contract*, should be reported as **non-regulated loans** in the various parts of the *MLAR* (since only those loans advanced after this date are required to be treated as a *regulated mortgage contract* for the purposes of *MLAR* reporting).

This reporting basis for loans made before 31 October 2004 should continue until such time, if ever, that a subsequent transaction on the loan causes it to be formally treated as a regulated contract.

## 9. Specific items

### 9(i) Positions to be reported gross

In general, liabilities and assets should be shown gross, and not netted off (unless there is a legal right of set-off). Thus an account which moves from credit to debit will move from one side of the balance sheet to the other.

A notable exception to this however concerns the reporting of loan assets which are subject to '**linked presentation**' (e.g. under FRS5). Such assets should be shown in the balance sheet net of linked funding and also on this basis in other tables where balances are reported on the same basis. Only sections A3 and D2 require the reporting of such loan assets on a 'gross' basis.

The treatment of loan assets that are being operated as part of a current account **offset mortgage** product (or similar products where *deposit* funding is offset against loan balances in arriving at a net interest cost on the account) will depend on the conditions pertaining to the mortgage product. The balance outstanding on such loans will need to be reported on the basis of the contractually defined balance according to the terms of the mortgage product. This might be the amount of loan excluding any offsetting funds, or it might be the net amount.

### 9(ii) Foreign currencies

Amounts in foreign currencies, including also any loans denominated in foreign currencies, should be translated into their equivalent sterling value using an appropriate rate of exchange at the reporting date, or where appropriate, at the rates of exchange fixed under the terms of any relevant currency hedging transaction, and that value used in the return. Thus all entries in the form represent sterling amounts. *Firms* should apply the same accounting treatment as for their published accounts.

## SECTION A: BALANCE SHEET

### Balance sheet analysis

**A1, A2** The balance sheet is intended to reflect the practices used in compiling published or other accounts (e.g. those prepared under the UK Companies Acts), although its format in the *MLAR* (with 'total assets' and 'total liabilities') will not necessarily be the same as that used by *firms* in their regular accounts. However, the differences should only be presentational.

**A1.6** **Loans to customers** may be a non-standard accounting sub-head for some *firms* whose business is not primarily mortgage related. But since this is an explicit *MLAR* data requirement, it should be split out from the sub-head under which it is routinely shown in the *firm's* other accounts.

### **A3** Analysis of loans to customers

This section recognises that some lenders may have securitised loans on their balance sheet, and hence provides for unsecuritised/securitised loans to be shown separately.

**Unsecuritised balances** are analysed in terms of three elements: gross loan balances (before deduction of any provisions); provisions balances in respect of those balances; and the net balances after deduction of such provisions.

**Securitised balances** are analysed in a similar way, except that 'gross' also means before the deduction of any linked non-recourse funding, the amount of which is also to be shown separately.

**A3.1-4** See Introduction (paragraphs 4 (i) to (iv)) for details of the coverage of these terms.

**A3.5** **Other loans** refers to any lending secured on land and buildings outside of the UK, any loan for which security is provided other than by land and buildings, together with all unsecured loans (e.g. consumer credit, personal loans, or such loans to corporates).

**A3.6** It is expected that net balances on unsecuritised loans plus net balances on securitised loans will equal the entry shown at A1.6 in the main balance sheet analysis of assets.

## SECTION B: PROFIT & LOSS ACCOUNT

### B0 Financial year to date

In terms of **reporting period**, the analysis should be compiled on a 'year to date' basis, covering successively 3, 6, 9 or 12 months from the *firm's accounting reference date*.

### B1 Profit & Loss Account

The P&L section is intended to reflect the practices used in compiling accounts prepared under the Companies Acts, although its format in the *MLAR* (with explicit focus on financial items such as interest, fees & commission etc) will not necessarily be the same as that used by *firms* in their regular accounts.

The reason for this approach is that most lenders to which this section is applicable are mortgage specialists, and as such it is considered desirable to put their P&L format onto a similar basis as that used for *banks* and *building societies*.

The analysis therefore requires the *firm's* profit & loss account to be re-structured in a way that makes a number of items explicit in the interests of achieving consistency with other reporting *firms*.

**B1.1** Focuses on **gross profit from non-financial activities**.

**B1.2-1.7** Covers a range of **income elements** which are more closely related to financial activities, including in particular those associated with mortgage lending.

**B1.9-1.13** Covers a range of **expenditure elements**, including those related to non-financial and also to financial (including mortgage related) activities.

**B1.15** **Operating Profit** is total income less total expenses.

**B1.16** **Provisions** covers write-offs and provisions charges on bad and doubtful debts, (including for example on mortgage loans); any suspended interest (i.e. any interest included in Interest Receivable which, through loan default, impairment or otherwise, is deemed unlikely to be received); and any other provisions for contingent liabilities.

### B2 Provisions analysis

This supplementary analysis draws together the key movements in provisions balances from the *firm's* accounting reference date up to the reporting quarter end.

The two 'flow items', namely **write-offs** and **provisions charges**, are those relating to the period from the *firm's* accounting reference date up to the reporting date.

The total of **provisions charges** in line B2.6 [column 3] will not necessarily be the same as the provisions charge in the Profit & Loss analysis at B1.16 (since

this latter item may include further provisions against other asset items not included in B2.6, or provisions arising from other sources).

## SECTION C: CAPITAL

### INTRODUCTION

The *threshold conditions* state that the resources of a *firm* must be adequate in the opinion of the *FSA* in relation to the *regulated activities* that the *firm* seeks to carry on or carries on. In addition, a *firm* is required to maintain 'adequate financial resources'. A *mortgage lender/administrator* should have adequate capital and funding in order to be able to meet these requirements.

In addition, the *FSA* operating framework requires us to identify the main risks to our statutory objectives. In assessing *firm*-specific risks we are required to assess the risks arising from the financial failure of a *firm* (due to business risks from the external environment, or control risks arising from the *firm* itself) which might affect both the market and individual *customers*. The specific *FSA* objectives that are potentially impacted are those relating to market confidence and consumer protection.

Details provided in this Section on Capital are drawn from the appropriate provisions of 'PRU 9.2: Capital Resources for Insurance and Mortgage Mediation Activity and Mortgage Lending and Administration'.

### C1-2

### CAPITAL RESOURCES

C1 and C2 set out first the individual components of **eligible capital** and secondly the **separate deductions** that should be made to arrive at qualifying capital.

Components of eligible capital are:

#### (1) Share capital

*Share* capital must be fully paid (i.e. the *firm* is under no obligation to repay this capital unless and until the *firm* is wound up) and may include ordinary *share* capital or preference *share* capital (excluding preference *shares* redeemable by shareholders within two years).

#### (2) Partnership or sole trader capital

*Partnership* capital is capital made up of the *partners'* capital account. The capital account is an account into which capital contributed by the *partners* is paid and from which, under the terms of the *partnership* agreement, an amount representing capital may be withdrawn by a *partner* only if he ceases to be a *partner* and an equal amount is transferred to another such account by his former *partners* or any *person* replacing him as their *partner*, or the *partnership* is otherwise dissolved or wound up.

*Sole trader* capital is the net balance on the *firm's* capital account and current account.

### **(3) Audited reserves**

Audited reserves are audited accumulated profits retained by the *firm* (after deduction of tax, dividends and proprietors' or *partners'* drawings) and other reserves created by appropriations of *share* premiums and similar realised appropriations. Reserves also include gifts of capital, for example, from a parent company. For *partnerships*, audited reserves include *partners'* current accounts according to the most recent financial statement.

### **(4) Interim net profits and partners' interim current accounts**

A *firm* is not required to take into account interim net profits. However, if it does, the profits have to be verified by the *firm's* external auditors, net of tax, anticipated dividends or proprietors' drawings and other appropriations.

In terms of the verification for inclusion, for the first, second and third financial quarters *firms* may include interim profits in their *MLAR*, on the understanding that the *firm* will obtain the required verification from its external auditors within two months of the financial quarter end. (The *FSA* may ask for a copy of the verification statement.) For the fourth quarter the *FSA* will rely on the forthcoming audited accounts as providing verification and accordingly the full year's profits should be included in the make-up of Eligible Capital under Interim Profits in the return.

### **(5) Revaluation reserve**

*Firms* should report reserves relating to the revaluation of fixed assets.

### **(6) General provisions**

*Firms* should report general provisions that are held against potential losses that have not yet been identified, but which experience indicates are present in the *firm's* portfolio of assets. Such provisions must be freely available to meet these unidentified losses wherever they arise. General provisions must be verified by external auditors and disclosed in the *firm's* annual report and accounts.

### **(7) Subordinated loans**

Subordinated debt (i.e. the amount of principal outstanding before amortisation) must not form part of the capital resources of a *firm* unless it meets the following conditions:

- (1) it has an original maturity of at least five years or is subject to five years' notice of repayment;
- (2) the claims of the subordinated creditors must rank behind those of all unsubordinated creditors;

- (3) the only events of default must be non-payment of any interest or principal under the debt agreement or the winding up of the *firm*;
- (4) the remedies available to the subordinated creditor in the event of non-payment or other default in respect of the subordinated debt must be limited to petitioning for the winding up of the *firm* or proving the debt and claiming in the liquidation of the *firm*;
- (5) the subordinated debt must not become due and payable before its stated final maturity date except on an event of default complying with (3);
- (6) the agreement and debt are governed by the law of England and Wales, or of Scotland, or of Northern Ireland;
- (7) to the fullest extent permitted under the rules of the relevant jurisdiction, creditors must waive their right to set off amounts they owe the *firm* against subordinated amounts owed to them by the *firm*;
- (8) the terms of the subordinated debt must be set out in a written agreement or instrument that contains terms that provide for the conditions set out in (1) to (7); and
- (9) the debt must be unsecured and fully paid up.

**Treatment of eligible capital items (listed above) in section C1:**

**C1.1 Reserves:** include items

- audited reserves
- revaluation reserves

**C1.2 Interim profits:** include items

- externally verified interim net profits
- externally verified *partners'* interim current accounts

**C1.3 Issued capital:** include items

- *share* capital
- *partnership* or *sole trader* capital
- subordinated loans

**C1.4 General provisions**

**C1.5 Other eligible capital:** includes

- any other item of eligible capital not required to be included in items C1.1 to C1.4.



## **C1.6 Total Eligible Capital**

This is the sum of the components listed in C1.1 to C1.5.

## **C2 Deductions from capital**

**C2.1 Investments in own shares** represents any investment in the *shares* of the company, quantified as fixed assets in the balance sheet.

**C2.2 Intangible assets** are the full balance sheet value of goodwill, capitalised development costs, brand names, trademarks and similar rights and licences. However, the balance sheet value for goodwill does not have to be deducted here until 14 January 2008. See *PRU 9.3.53R*

**C2.3 Interim net losses** refers to the cumulative amount covering the period from the *firm's accounting reference date* to the end of the current quarter. All the current year's losses should be reported. Unpublished losses from the previous accounting period should also be shown here.

**C2.4 Other deductions from capital:** include

- **Excess of drawings over profits for partnerships or sole traders:** *firms* should report the difference between the personal drawings of a *partnership or sole trader* and the profit in the period, where the drawings exceed the profit for the period.

## **C2.5 Total Deductions**

This is the sum of the components listed in C2.1 to C2.4.

## **C3 Total Capital Resources**

This is total eligible capital less total deductions (C1.6 – C2.5).

## **C4 Capital requirements**

**C4.1** The capital requirement for *mortgage lenders* or *mortgage administrators* that have the *regulated mortgage contracts* that they administer on their balance sheet is asset-based, and the information required is detailed in C4.2 to C4.4.

**C4.2 Total assets:** this is the total value of fixed and current assets.

## **C4.3 Undrawn commitments**

Undrawn commitments means the total of those amounts which a borrower has the right to draw down from the *firm* but which have not yet been drawn down.

However, undrawn commitments should not be included in the calculation of capital requirements if they have an original maturity of up to one year or if they can be unconditionally cancelled at any time by the lender.

Similarly, existing mortgage offers should not be included in the calculations of capital requirements if the offer has an original maturity of up to one year or can be unconditionally cancelled at any time by the lender.

**C4.4**                    **Intangible assets:** this is the amount shown at C2.2.

**C4.5**                    **Total adjusted assets:** this is the sum of C4.2 and C4.3, less C4.4

**C5**                    **Capital requirements**

**C5.1**                    This section sets out the income-based capital requirements applicable to *mortgage administrators* that have been appointed by *persons* that are not authorised to administer *regulated mortgage contracts* on their behalf, and which therefore do not have the assets that they administer on their balance sheet. The information requirements are detailed in C5.2 – 5.4.

**C5.2**                    **Total income**

*Firms* should report the amount of total income in their most recent audited (or other) financial statements, and an estimate of income for the current reporting year.

Total income should include both revenue and gains arising in the course of the ordinary activities of a *firm*. Revenue consists of commissions, fees, net interest income, dividends, royalties and rent. Only gains that are recorded in the profit and loss account should be included in income. What is relevant for the calculation of income is the amount of actual income generated rather than the gross cash streams of any one transaction.

**C5.3**                    **Relevant adjustments**

The following exceptional items must be deducted from the *firm's* total income:

- (1) profit on the sale or termination of an operation;
- (2) profit arising from a fundamental reorganisation or restructuring having a material effect on the nature and focus of the *firm's* operations; and
- (3) profits on the disposal of fixed assets, including *investments* held in long-term portfolio.

**C5.4**                    **Total relevant income**

Is the sum of C5.2 minus C5.3.

## SECTION D1: LENDING – BUSINESS FLOWS AND RATES

**D1-D4** For details of the terms '**Residential lending** to individuals' (and regulated/unregulated) and '**other secured loans**', see Introduction, paragraphs 4 (i) – (iv).

### **D1 Loans: Advances/Repayments – Row & Column Analysis**

For the two categories of loan assets, details are requested under various **transaction columns** that explain the transition from the previous quarter's balances to the current quarter's balances.

### **D1 Loans: Advances/Repayments – Transactions (columns)**

**Advances made in quarter** should include:

- (a) instalments released in the quarter for instalment advances;
- (b) re-advances, i.e. where previous charge cancelled;
- (c) further advances;
- (d) in the case of loans that have a facility to draw down extra amounts over and above the sum originally advanced, the total of any further amounts drawn down in the quarter;
- (e) the deduction from advances made of advance cheques cancelled;

but should exclude:

- (f) the amount of any loan books acquired in the quarter (which should be reported in 'other debits/credits etc');
- (g) retentions imposed, which should be included as they are released;
- (h) sundry debits, i.e. any items not approved and not included in commitments, e.g. insurance debits, fines, insurance guarantees, valuation fees, arrangement fees etc. (unless formally treated as part of loan).

**Repayment of principal** should include:

- (a) repayment of principal including capital repayments, full or partial redemptions and the principal element of the normal monthly payment;
- (b) mortgage receipts temporarily posted to *investment* accounts;
- (c) transfers from *investment* accounts to mortgage accounts;

but should exclude:

- d) the amount of any loan book sold during the quarter (to be reported in 'other debits/credits etc');
- (e) sundry credits to accounts, such as insurance premiums, fines, fees, etc;
- (f) advance cheques cancelled;
- (g) *investment* receipts temporarily posted to mortgage accounts.

In determining the amount shown under **repayment of principal**, it is recognised that *firms* may need to estimate the amount of interest repaid where amounts repaid include both interest and principal, and/or where the amount of interest repayable is not the same as the amount charged (e.g. annual review or deferred interest schemes, or where a loan is not being fully serviced).

### **Write offs in quarter**

This is the amount written off mortgage balances in the quarter (and off provisions charged to the income and expenditure account) and is to be on a basis consistent with amounts shown in the *firm's* published accounts as 'written off' within the analysis of changes in loss provision usually appearing as Notes to the Accounts.

The amount written off may arise for example from:

- sale of a property in possession where there is a shortfall; or
- a decision to write down the mortgage debt on a loan still on the books. This may arise where the *firm* has taken the view that it is certain that a loss will arise and that it is prudent to write down the mortgage debt rather than carry the full debt and an offsetting provision. Examples might include certain fraud cases, or where arrangements have been reached with the borrower to reduce the mortgage debt repayable.

### **Other debits/(credits) and transfers (net) include:**

- (a) interest charged to the loan account in the period;
- (b) interest repaid during the period;
- (c) amounts charged to loan accounts and amounts received from borrowers in respect of such items as insurance premiums, valuation fees, and fines etc.;
- (d) mortgage balances acquired following takeover / merger;
- (e) loan books acquired from other lenders in the quarter;

- (f) loan books sold to other lenders in the quarter;
- (g) loan books securitised during the quarter;
- (h) the transfer of any securitised assets back onto the balance sheet (e.g. following the closure of a securitised pool of loans);
- (i) transfers (net) should include any reclassified loans (e.g. where there has been a change in the use of the land on which the loan is secured to/from residential; or change in status of loan from/to regulated/non-regulated etc).

NB Balances on loan books acquired/sold/securitised should be as at the date of the relevant event.

## D2 Loans: Book movements

The '**transactions in the quarter**' columns are analyses of amounts already included within the 'other debits/(credits) and transfers (net)' column of section D1.

- (i) '**loans acquired**' represents balances on any relevant loan books acquired during the quarter from other lenders;
- (ii) '**loans sold**' represents balances on any relevant loan book (i.e. parcel of loans) sold during the quarter to another lender;
- (iii) '**loans securitised**' represents balances on any loans that the *firm* has 'securitised' in the quarter. It includes balances on loans subject to securitisation transactions qualifying either for the 'linked presentation' or 'derecognition' methods of accounting as described in FRS 5;
- (iv) '**other**' represents the net amount of other transaction amounts included in 'other debits/(credits) and transfers (net)' in D1.

NB: As a result, D2 [item (i) – item (ii) – item (iii) + item (iv)] should equal D1 [item 'other debits/(credits) and transfers (net)].

The final column '**balance at end quarter on loan assets subject to non-recourse funding**' represents all such loan assets (and not just the amount treated as transactions in the quarter), and requires the 'gross amount' of such loan assets to be reported against relevant line item categories. The 'gross amount' is the amount of any such loan that, under the 'linked presentation' method of accounting, would be shown in a *firm's* published or other balance sheet as X in the example below:

gross loan asset	=	X
less non-recourse funding	=	Y
net loan asset	=	X-Y

In the analysis here at D2, it is therefore the gross loan asset at the end of the reporting quarter that should be reported in the final column. Once securitised, it is recognised that end quarter gross balances will not necessarily remain constant (due either to borrower repayments, the possibility of any further advances, or other arrangement for 'topping up' a pool of securitised loans etc).

### D3 **Loans: Interest rates**

#### **Basis**

Interest rates in this table are **nominal annual rates** charged to the *customer* on loan accounts. They should ignore the effect of any interest rate swaps or other hedging contracts that might exist, and also ignore the effect of any offsetting deposit account (as for example in the case of an offset mortgage).

This provides an analysis of weighted average interest rates for the loan assets reported in the final column of D1 above. 'Interest rates at end of quarter' (columns 4, 5, and 6 of section D3) means rates applying at least throughout the last day of the quarter, so *firms* should not use rates which only come into operation at the beginning of the next quarter. Points to note on specific columns are:

#### (1) **Balances at end quarter**

**Accrued interest** should be included (even though it is excluded when computing the weighted average rate).

The first '**of which**' analysis is designed to obtain information on balances subject to **fixed rates** of interest and balances subject to **variable rates** of interest. (The two amounts should add to the balance in column 1). For these purposes:

**'fixed'** means the rate of interest is fixed for a stated period. It should also include any products with a 'capped rate' (i.e. subject to a guaranteed maximum rate) and any products that are 'collared loans' (i.e. subject to a minimum and a maximum rate). Annual review or stabilised payment loans should be excluded (since the purpose is merely to smooth cash flow on variable rate loans);

**'variable'** includes all other interest rate bases (i.e. other than those defined above as 'fixed') applying to particular products, including those at, or at a discount or premium to, one of the *firm's* administered lending rates; those linked to Libor (or other market rate); those linked to an index (e.g. FTSE) etc. However if any such loan products are subject to a 'capped rate', then treat as 'fixed'.

The second '**of which**' analysis is designed to obtain information on loan balances according to whether the nominal annual interest rate charged to the customer at the quarter-end is higher than the prevailing Bank of England

Base (or repo) Rate (BBR). For these purposes the BBR is that applying on the last day of the reporting quarter. The analysis is subdivided into four categories:

- (i) loan balances where the rate charged is **less than 2% above BBR**. Include here also all loan balances where the rate charged is less than BBR (as a result the sum of these four columns will equal the figure in the TOTAL column);
  - (ii) loan balances where the rate charged is **2% or up to 3% above BBR**;
  - (iii) loan balances where the rate charged is **3% or up to 4% above BBR**;
  - (iv) loan balances where the rate charged is **4% or more above BBR**.
- (2) **Weighted average nominal annual rates**
- (a) Interest rates reported in Table D3 provide a broad indication of **market rates. They should ignore the effect of any interest rate swap or hedging**. For each line item the weighted average rate should be derived as follows:
    - (i) identify the various nominal/quoted interest rates that apply to elements of this line item; then
    - (ii) for each separate nominal/quoted rate, multiply that rate by the amount of end quarter balances (excluding accrued interest) for which that rate applies; and
    - (iii) add up the results of (ii) for all the different rates for this line item; and
    - (iv) divide the total calculated in (iii) by the end quarter balance in column 1 less accrued interest (against the line item concerned).

**NB:** in the 'of which' analysis that requires separate reporting of weighted 'fixed' and 'variable' rates, **a cross check for each row** is that the weighted average nominal rate on all balances is equal to the weighted average of the reported fixed and variable rates in the subsequent two columns.

### **D3.1 –3.8 Other Points**

The interest rate to be used is the rate charged to the loan account, which in certain circumstances will differ from the interest rate 'payable' by a borrower. These circumstances include deferred interest loans, interest roll-up loans, annual review schemes or where the loan is not performing.

**Advances in quarter** refers to the same amount as covered under 'advances in quarter' in the Loans: Advances/Repayments analysis in Section D1 above.

**D4**      **Loan commitments** (columns)

**Commitments made since end of previous quarter**

should include:

- (a) the aggregate of agreed advances (whether or not the mortgage offer has been accepted by the prospective borrower), including amounts recommended for retention, all instalment elements, and further advances;

but should exclude:

- (b) commitments from previous quarters that have been cancelled in the current quarter;
- (c) retentions imposed and subsequently not released;
- (d) instalment commitments that have not been taken up;
- (e) advance cancellations that are not re-issued;
- (f) sundry debits, e.g. insurance guarantee premiums (unless additional to the loan), insurance of contents etc.

**Cancellations in quarter**

Includes (b), (c), (d) and (e) above.



## SECTION E: RESIDENTIAL LOANS TO INDIVIDUALS - Income Multiples & LTV

### E1-6 Gross advances in quarter

Covers actual advances made in the quarter. For these purposes separate advances (e.g. stage payments) made in the period on the same mortgage should count as a single advance for the 'number' column in sections E3, E4, E5 and E6.

NB: 'gross advances' should be compiled on the same basis as in section D1 above and therefore relevant totals for each section in E1 to E6 should also agree with the amount of gross advances reported in D1.

### E3-6 Balances outstanding

Covers balances at end of the quarter. Relevant sub-totals should agree with corresponding balances shown in the final columns of D1.

### E1/2 By Income Multiple and LTV (Loan to Valuation ratio)

The amount to be included in the table is the **gross advance**, but its allocation to a specific cell is determined according to income multiple and LTV which are both defined using the size of the loan (as defined below).

### E1/2 By Income Multiple and LTV

#### Income multiple based on single or joint incomes

For this analysis, '**income**' should be taken as **gross annual income** before tax or any other deductions.

The loan should first of all be categorised to 'single' or 'joint' income basis, and the income multiple calculated as described below:

- (i) **Single income basis.** This means only one person's income was taken into account when making the lending assessment/decision.

The income multiple here is the total loan amount divided by the borrower's total income (total of the borrower's main income and any other reckonable income e.g. overtime etc, to the extent that the *firm* takes such additional income into account in whole or in part).

- (ii) **Joint income basis.** This means that two or more persons' incomes were used in the lending assessment/decision.

The income multiple here is the total loan amount divided by the aggregate income of the two or more borrowers.

(iii) **Other.** This category is to be used when the loan assessment is based, only partly or not at all, on one or more persons' incomes. Thus include here:

**Under Single Income section (E1.6/E1.13)**

- **Buy to let** loans where the loan assessment is based on the rental yield of the property (but not buy to let loans based solely on one or more persons' incomes which should be shown against the relevant income multiple category);
- **Lifetime mortgages** since in most if not all instances, the concept of a supporting income is not applicable;
- **Other products** (no current examples)

#### **Under Joint Income Section (E2.6/E2.13)**

- **Business loans**, where typically the loan assessment will be based on mixed sources of business/personal income or perhaps just on the capacity of a person's business to support the loan;
- **Other products** that have similar characteristics, that is where the loan assessment is based on either mixed income sources or non-personal incomes.

(iv) **Not evidenced.** This 'of which' analysis applies to loans made on the basis of one or more persons' incomes, and therefore should exclude any loans reported in "Other" (defined in (iii) above).

It covers loans where: the lender has no independent documentary evidence to verify income (e.g. as provided by an employer's reference, a bank statement, a salary slip, a P60, or audited/certified accounts

For the purpose of **income multiples**, the multiple is of **loan** to income where **loan** is as defined below.

#### **Loan to valuation ratio LTV**

Should be based on the following:

- (i) **loan** is defined for:
  - (a) **new borrowers** - as the amount of actual advance or, in the case of loans where the amount advanced in the period is less than the total amount of the loan to which the *firm* has agreed to lend (for example loans with additional drawing facilities or loans involving instalments/stage payments/retentions), is the amount of committed advance (including any committed drawing facilities);
  - (b) **existing borrowers** - as the total amount of debt outstanding including the further advance plus any committed drawing facilities at the time of the further advance;

and will include MIG ("mortgage indemnity guarantee"), building and other insurance premiums and other sundry items **if** these are included in the amount advanced;

- (ii) **valuation** is to be taken as the most recent valuation of the property which is subject to the mortgage (the existence of additional collateral on any other property should be ignored when calculating LTV). For these purposes, "recent valuation" can either be based on an actual valuation, or an estimated valuation using indexed valuation methodology applied to an original actual valuation. In the case of staged construction or self-build schemes, valuation means 'expected final value of the property' at the time the *firm* is committed to making the loan (i.e. takes the lending decision).

### **E3 Credit History**

This seeks to categorise lending in terms of a borrower's previous credit history, as measured at the point when the new advance is made. For these purposes, it is only necessary to establish a borrower's credit history at a single point in time, i.e. at the time of making the loan. It is not intended that credit history should be reassessed after the loan has been made.

In particular the aim is to separately identify under the heading 'Impaired credit history', those loans where it appears that the borrower has some form of adverse credit history:

- (i) at the point when the new advance is made and the loan is reported under 'Gross advances';
- (ii) subsequently for reporting under 'Balances outstanding', the amount of the loan at the quarter end to such a borrower (who at the point when the present loan was advanced, was deemed to have had an adverse credit history).

#### **E3.1 Impaired credit history**

If any of the following conditions are met at the time of making the loan, the borrower should be reported as having **an impaired credit history**:

- (i) arrears on a previous (or current) mortgage or other secured loan within the last two years, where the cumulative amount overdue at any point reached three or more monthly payments;
- (ii) arrears on a previous (or current) unsecured loan within the last two years, where the cumulative amount overdue at any point reached three or more monthly payments;
- (iii) one or more county court judgements (CCJs), with a total value greater than £500, within the last three years;
- (iv) being subject to an Individual voluntary arrangement (IVA) at any time within the last three years;
- (v) being subject to a bankruptcy order at any time within the last three years;

**but** *firms* should not include technical arrears as part of the above definition. Technical arrears means circumstances where the borrower has been the victim of a banking error giving rise to late payment.

**NB** In (i) to (v), *firms* should ignore whether the borrower has subsequently paid off arrears, or has satisfied/discharged a CCJ or IVA or bankruptcy.

## **E4 Payment type**

This section analyses loans in terms of how the borrower is contractually expected to service the loan, and is split into four categories:

- repayment;
- interest only;
- combined; and
- other.

### **E4.1 Repayment (capital & interest)**

This is the traditional payment option available to borrowers. Such loans involve regular periodic payments covering interest for the period and some repayment of capital.

### **E4.2 Interest only**

This is the type of loan which requires the borrower to make regular payments of interest only (i.e. without any obligation to make periodic payments of capital). It includes 'endowment' type loans, others having an independent ultimate repayment vehicle (e.g. PEP, ISA or pension mortgages), as well as other interest only loans where there is either no specific ultimate repayment vehicle in place or where the lender does not formally require one to be in place.

### **E4.3 Combined**

This section is for loans where both of the above payment types are in place (i.e. part of the loan is 'repayment', and part is 'interest only').

### **E4.4 Other**

This category will contain loans where no regular periodic payment obligation is in place, for example secured overdraft facilities or secured credit cards, and *lifetime mortgages*.

## **E5 By drawing facility**

These are loans which include an option to draw down further amounts (i.e. where, at the outset of the loan, extra drawing rights exist over and above the original amount advanced, **but not** those arising only in relation to previous overpayments).

### **E5.1 Extra drawing facility**

These are loans which in general are structured as follows:

#### **Example structure when flexible loan contract agreed**

Amount of loan advanced	£65,000
Amount of extra drawing facility agreed to (but not advanced at outset of loan)	£15,000
Total loan facility up to	£80,000

### **E5.1 a) Loans including unused facility**

This means the total loan facility i.e. the sum of the amount of loan advanced and the amount of extra drawing facility agreed (but not advanced at the outset of the loan):

- (i) **gross advances in quarter** should detail those loans that include an extra drawing facility: show the number and amount of such loans;
- (ii) **loans outstanding** means the end quarter balances (on original advance plus any subsequent draw downs) plus the residual amount of any unused drawing facility that remains available to the borrower: show the number and amount of such loans.

### **E5.1 b) Unused facility**

This is the amount of the extra drawing facility that has not been drawn down by the borrower:

- (i) **gross advances in quarter** should detail the unused facility element of such loans: show the amount;
- (ii) **loans outstanding** means the end quarter balances of any unused extra drawing facility that remains available to the borrower: show the amount.

### **E5.1 c) Net loans**

This can be calculated by subtracting the entry in row b) from the entry in row a).

## **E5.2 Loans with no extra drawing facility**

*Firms* should report all other loans here.

## **E5.3 TOTAL**

This figure should be calculated as follows:

(i) for '**Number**' by adding E5.1(a) and E5.2, and

(ii) for '**Amount**' by adding E5.1(c) and E5.2.

## **E6 By Purpose**

This analysis is to identify the principal purpose of the loan, which should be available from the application form. A loan should therefore only be classified to one category of E6.1 – E6.7. A stage advance should be classified for the same purpose as the main advance.

### **E6.1/2 House purchase**

Loans where the borrower is purchasing a house (or flat etc). *Firms* should include stage payments on such transactions here and not in 'further advances'. A distinction is drawn between loans for house purchase where the purpose is for owner occupation, or for buying with a view to letting ('buy to let').

Loans for owner occupation are required to be sub divided into those to first time buyers (FTBs, that is where the tenure of the main borrower immediately before this advance was not owner-occupier) and those to other buyers.

### **E6.3 Further advance**

A further loan (either as a normal further advance, or as a second charge loan where the *firm* has the first charge) to an existing borrower of the *firm*, secured on the same property.

The underlying purpose of the further advance is not relevant and could include e.g. purchasing freehold interest in a currently owned leasehold property; buying a second property on the security of the first; as a consumer loan fully secured on residential property; or as a 'drawdown' on a flexible mortgage.

### **E6.4/5 Remortgage**

Loans where the borrower is not moving house but is refinancing an existing loan, either one already with the *firm* or one from another lender. The whole amount of the new advance should be classified as 'remortgage' even if it is larger than the existing loan.

### **E6.6 Lifetime mortgages**

This is a specific type of *regulated mortgage contract*, which is defined in the *Handbook* as follows:

A *regulated mortgage contract* under which:

- (a) entry into the mortgage is restricted to borrowers of a specified age; and
- (b) the *mortgage lender* does not generally specify a period at the end of which the amount borrowed (plus interest, if any, outstanding) must be repaid, and while the *customer* continues to occupy the mortgaged land as his main residence:
  - (i) no instalment repayments of the capital and no payment of interest on the capital (other than interest charged when all or part of the capital is repaid voluntarily by the *customer*), are due or capable of becoming due; or
  - (ii) although interest payments may become due, no full or partial repayment of the capital is due or capable of becoming due; or
  - (iii) although interest payments and partial repayment of the capital may become due, no full repayment of the capital is due or capable of becoming due; and
- (c) the loan made to the *customer* is repayable in one or more of the following circumstances:
  - (i) the death of the *customer*; or
  - (ii) the *customer* enters into long term care; or
  - (iii) the *customer* moves into sheltered accommodation or residential care; or
  - (iv) the *customer* acquires another dwelling for use as his main residence; or
  - (v) the *customer* chooses to repay all or part of the loan; or
  - (vi) the *mortgage lender* exercises its legal right to take possession of the mortgaged land under the terms of the contract.

#### **E6.7 Other**

Would include for example where a borrower is not moving house but takes a loan on the security of his previously unmortgaged property.

## **SECTION F: LENDING - ARREARS ANALYSIS**

## Introduction

The guidance notes in this section serve two purposes: they provide guidance for

- (i) items **F1 to F5** shown in *MLAR* table F.

For these sections, the analysis of lending refers to on-balance sheet loan assets only (ie as included in the final column of section D1 of table D)

- (ii) items **H1 to H5** shown in *MLAR* table H.

For these sections, which cover reporting of arrears by *firms* with a *mortgage administrator's* activity, the analysis should include arrears in respect of the types of residential loans to individuals set out in the guidance notes for table G. For *guidance* on items H1 to H5 see corresponding guidance against items F1 to F5. Similarly references in the *guidance* notes to any items F1 to F5, should also be read as referring to items H1 to H5 when completing table H.

### **F1 to F4**      **Arrears categorisation by type of loan**

For these sections, the analysis of lending is divided into two main types:

- (i) residential loans to individuals (split between regulated and non regulated business);
- (ii) all other secured loans.

The analysis is based on expressing **the amount of arrears** on each loan as a percentage of the **balance outstanding** on the loan, allocating cases to relevant arrears bands, providing details of cases moving up into more serious arrears bands in the quarter, and giving information on loan performance during the quarter. (In cases where there is more than one loan secured on a single property, these should be amalgamated, where possible, in reporting details of arrears cases.)

**Definitions of terms** used above, and those related to them, are given below in sections having side headings numbered 1, 2, 3, 4, 5 and 6.

**F1.6/F2.6 & F3.6/F4.6**      **In possession:** cases should be included here where the property is taken in possession (through any method e.g. voluntary surrender, court order etc). For development loans in particular, cases should also be included where the appointment of a receiver and/or a manager has been made, or where the security is being enforced in other ways (which may or may not also involve the existence of arrears e.g. building finance case with interest roll up, no arrears, but a current valuation is less than the outstanding debt).

#### **1.      Balance outstanding (columns 3 and 6)**

**1.1**      This is the amount of total debt at the reporting date, and should comprise the total amount outstanding (after deducting any write-offs but without deduction for any provisions) in respect of:



- (i) the principal of the advance (including any further advances made);
- (ii) interest accrued on the advance (but only up to the reporting date), including any interest suspended;
- (iii) any other sum which the borrower is obliged to pay the *firm* and which is due from the borrower, e.g. fees, fines, administration charges, default interest and insurance premiums;

and is intended to be consistent with the basis used for presentation of gross balances outstanding shown in the balance sheet section of the return (i.e. at A3 Column 1 for on-balance sheet or unsecuritised balances, and at A3 column 4 for securitised balances), with the addition for tables F and H of any interest suspended not included in the balance sheet.

## 2. Amount of arrears (columns 2 and 4)

2.1 Arrears will arise through the borrower failing to service any element of his debt obligation to the *firm*, including capital, interest, or fees, fines, administrative charges, default interest or insurance premiums.

2.2 At the reporting date, the **amount of arrears** is the difference between:

- (i) the accumulated total amounts of (monthly or other periodic) **payments due** to be received from the borrower; and
- (ii) the accumulated total amount of **payments actually made** by the borrower.

2.3 Only amounts which are **contractually due** at the reporting date should be included in 2.2(i) above. That is:

- (i) include accrued interest only up to the reporting date but not beyond;
- (ii) and, only include a proportion of any annual insurance premium if the *firm* permits such amounts to be paid in periodic instalments. However if the terms of the loan or the lender's practice are such as to permit insurance premiums to be added to the loan principal then do not treat such amounts as contractually due;
- (iii) similarly, where 'any other sum' has been added to the loan (see 1.1 (iii) above), only include such proportions as are contractually due (e.g. if it is the practice in particular circumstances to add the sum/charge to the loan and require repayment over the residual term of the loan);
- (iv) in assessing 'payments due' when a borrower has a **flexible loan**, it is important to apply the contractual terms of the loan: for example,

payment holidays which satisfy the terms of the loan should not be treated as giving rise to an arrears position;

(v) do not however include 'Deeds Store' loans in the arrears figures (that is, loans where the debt is de minimis e.g. £100, but the borrower still has insurance premiums to pay and perhaps some instalments are overdue).

- 2.4** In the case of **annual review schemes** the 'payment due to be received' under 2.2(i) is that calculated under the scheme. This may well differ from the amount charged to the account but should not of itself give rise to any arrears, providing the borrower is making the level of payments advised by the *firm*. The same principles apply to deferred interest products - if the borrower is making the payments that are required under the loan arrangements then he is not in arrears, even though the debt outstanding is increasing.
- 2.5** Where a *firm* makes a **temporary 'concession'** to a borrower (i.e., an agreement with the borrower whereby monthly payments are either suspended or less than they would be on a fully commercial basis) for a period, the amounts included in 2.2(i) are those contractually due (and at commercial rates of interest). Hence the borrower will continue to be in arrears and the level of arrears will in fact continue to increase until such time as he is able fully to service the debt outstanding.
- 2.6** Where the terms of the loan do not require payment of interest (or capital) until a stated date or until redemption or until certain conditions are triggered, as for example in the case of certain building finance loans, then the loan is not in arrears until such time as contractual repayments are overdue. There may be circumstances however where, even though the loan is not in arrears, it falls to be reported under F1.6, F2.6, F3.6 or F4.6. (See notes on F1.6/F2.6/F3.6/F4.6 at beginning of Section F.)
- 2.7** The reporting treatment of cases where arrears have been capitalised is dealt with in section 3 below.
- 2.8** Where a '**capitalisation**' case that has at one time been correctly removed as fully performing (see section 3) but at some later time defaults, then this should be treated as a new default and the amount of arrears taken as that arising from this new default. That is, the previously capitalised arrears should not be reinstated as current arrears.

### **3. Capitalisation of arrears and reporting criteria**

- 3.1** By '**capitalisation**' we mean a formal arrangement agreed with the borrower to add all or part of a borrower's arrears to the amount of outstanding principal (i.e. advance of principal including further advances less capital repayments received during the period of the loan) and then treating that amount of overall debt as the enlarged principal. This enlarged principal is then used as the basis for calculating future monthly payments over the remaining term of the loan. Where less than the full amount of arrears is capitalised (or indeed where none of the

arrears is capitalised) then, providing there are arrangements made for the borrower to repay the non-capitalised arrears over a shorter period ranging for example from 3 to 18 months, this type of arrangement should also be regarded as an equivalent of 'capitalisation'.

### 3.2

The decision to 'capitalise' (or treat as if capitalised) is a business decision between the *firm* and the borrower. However for the purposes of consistency in reporting arrears cases in table F (and reporting capitalisations in section F5) the following **reporting criteria** should be used where a *firm* has capitalised the loan (or treated as if capitalised) and reset the monthly payment:

- (i) such an arrears case should continue to be included in sections F1 – F4 as an arrears case until the loan has been '**fully performing**' (see (ii) below) for a period of six consecutive months (any temporary increase in arrears during this qualifying period has the effect of requiring six consecutive months of fully performing **after** such an event). Until that time it should be included in table F, and be allocated to the arrears band applicable at each reporting date as if 'capitalisation' had not taken place;
- (ii) for these purposes a loan is considered to be 'fully performing' only where the borrower has been meeting all obligations on the loan with regard to repayments of principal, interest (at a normal mortgage rate on the full balance outstanding, including as appropriate any relevant past arrears), any payment towards clearing past arrears as agreed with the *firm* and any default payments due levied in respect of previous missed repayments. That is, amounts may be either added to the principal of the loan or otherwise repaid over a shorter period than the residual term of the mortgage, as agreed between *firm* and borrower. But then this revised payment schedule must be fully maintained for a six month period before the arrears can qualify to be treated as capitalised for reporting purposes and hence removed from the arrears cases in table F;
- (iii) arrears cases qualifying as 'fully performing' under (ii) **should then be omitted from sections F1-F4**, and should then be reported in section F5 for the same reporting period during which the removal occurs.

### 4. **Cases entering higher (i.e. more serious) arrears band in quarter (columns 1 to 3)**

This refers to those cases now included in a particular arrears banding which may have been classified in a **less severe (i.e. lower numerical) band** at the end of the previous quarter, but which have deteriorated sufficiently during the quarter to move to a more severe arrears band. This would mean, for example, that cases that were previously excluded from the arrears table being less than 1.5% in arrears would now be entered in the '1.5 < 2.5%' arrears band (i.e. 1.5% or less than 2.5%) in F1.1, and F1.6 (and F2.6/F3.6/F4.6) will show details of those cases taken into possession during the quarter which were previously classified as in arrears under any of F1.1-1.5 (or F 2.1-2.5/3.1-3.5/4.1-4.5, as the case may be). Cases which have improved during the quarter and which could

now be classified in a less severe arrears band should not be included in these 3 columns.

**5. Number (of cases) (Columns 1 and 4)**

**5.1** In cases where there is more than one loan secured on a single property, these should be amalgamated, where possible, in reporting details of arrears cases.

**5.2** In cases involving, for example, arrears on loans to property developers (which would come under F4), the loan should count as a single case in the number column irrespective of the number of properties on the development itself.

**6. Performance of current arrears cases (column 7)**

**6.1** This analyses all those arrears cases included in columns 4 to 6 and gives a measure of performance covering all of the loans in a particular arrears band at the end of the quarter. The measure, which compares 'actual' with 'expected' payments, is required to be calculated for a single time period: the 3 months covered by the firm's latest financial quarter. For this time period, the performance measure should be calculated as a percentage as follows:

$$\frac{\text{total of 'payments received' from borrowers}}{\text{total of 'payments due' from borrowers}} \times 100$$

where:

- (i) 'payments due' means amounts due under normal commercial terms (and not the lesser amounts which may have been agreed as part of any temporary arrangement) fully to service the loans: that is the balances outstanding including those elements referred to in 1.1 above such as insurance, fees and fines etc. (If for some reason this is not readily available then a suitable approximation can be derived for each relevant quarter by applying one quarter of the annual interest rate to the appropriate balance outstanding, and adding in other payments due for example insurance, fees and fines etc); and
- (ii) 'payments received' should be limited to regular repayment of interest, capital and other sundry charges to the loan account, and should exclude abnormal repayments (e.g. sale proceeds of property in possession, and large lump sum repayment of part or all of the outstanding balance). The reasoning behind this is that excess payments on one or more arrears cases would otherwise have the effect of compensating for underpayment on other arrears cases and, as a result, give an overstated performance measure. Therefore, in compiling aggregate payment received figures (as part of the payment performance ratio) the contribution from an individual loan in arrears should be limited to no more than the 'payment due' amount.

**6.2** The amount to be entered on the return is a percentage to 2 decimal places.

**6.3** In calculating the performance measure on possession cases (F1.6, F2.6, F3.6 and F4.6), the following points are relevant:

- (i) 'payments received': in many cases these may be nil, but not always since the property in possession may be let out and a rental income received. In each case the payment received should be included for the purposes of calculating the performance measure;
- (ii) 'payments due': in recognition of the fact that amounts of interest will still be charged to the borrower's account, then the 'payments due' should be calculated as three months' interest at normal commercial rates of interest;
- (iii) however, in F1.6, F2.6, F3.6 and F4.6, it is likely that the performance measure will in most instances be zero;
- (iv) the relevance of the above however, is that 'payments due' on possession cases need to be computed in order to feed into the overall performance measure at F1.6, F2.6, F3.6 and F4.6.

#### **6.4**

The overall measure of performance at F1.7 (and similarly at F2.7, F3.7 and F4.7) includes possessions, and is the ratio of:

- (i) 'payments received' on all cases in F1.1 to F1.6
- (ii) 'payments due' on all cases in F1.1 to F1.6

The same approach should be used for F2.7, F3.7 and F4.7.

#### **F5**

##### **Arrears management**

##### **Number of Sales/Number of (arrears) cases**

In cases where there is more than one loan secured on a single property, these should be amalgamated where possible in reporting details of possession cases sold during the period in F5 (column 1), and details of arrears cases in F5 (columns 3 & 4).

##### **Balance outstanding**

In F5 (columns 2 and 5) this is as defined in section F/1 paragraph 1.1 (including in the case of properties sold the costs of sale where these have been debited to the borrower's account), and should be the balance at the end of the quarter.

##### **Possession sales during quarter**

*Firms* should include in F5 (columns 1 and 2) **all** properties sold in the quarter irrespective of whether losses have occurred.

##### **Capitalisation of arrears cases in quarter**

Details should be given in respect of those cases which, having previously been in the reported figures in table F on arrears, have now been capitalised

(or treated as if capitalised), have satisfied certain performance criteria for six months, and have been **removed** during the latest quarter from the arrears figures which now appear in sections F1 – F4. Sees paragraph 3 of section F of the *guidance* notes.

### **Cases involving temporary concession or arrangement**

In respect of the number of cases in arrears at the end of the quarter (i.e. reported in F1 to F4.7), details should be given of those cases for which the lender has taken steps to assist the borrower in some way.

Specifically, *firms* should state in how many cases a **temporary concession** has been made (see paragraph 2.5 in Section F), and in how many cases a formal **arrangement** to capitalise has been made (see paragraph 3.1 in section F, which also includes within the term 'arrangement' the example of a borrower making increased monthly payments to reduce some or all existing arrears). The balancing number should be shown in the next column 'No concession/arrangement'.

## SECTION G: MORTGAGE ADMINISTRATION – BUSINESS PROFILE

### Introduction

Article 61 of the Regulated Activities Order establishes *administering a regulated mortgage contract* as a *regulated activity*. This applies equally to those *firms* that are lenders, and those whose principal business is to undertake mortgage administration on behalf of third parties.

For *firms* that are authorised as *mortgage administrators* only, the information sought in this section will enable the *FSA* to establish the extent and nature of the *firm's* mortgage administration business. The *FSA* will be able to assess the potential risks posed by the *firm's* business activities and tailor its regulatory response accordingly.

A *mortgage administrator* is a *firm* with *permission* (or which ought to have *permission*) for administering a *regulated mortgage contract* and where, as defined in article 61(3)(b) of the *Regulated Activities Order*, *administering a regulated mortgage contract* consists of either or both of:

- notifying the borrower of changes in interest rates or payments due under the contract, or of other matters of which the contract requires him to be notified; and
- taking any necessary steps for the purposes of collecting or recovering payments due under the contract from the borrower;

but does not consist merely of having or exercising a right to take action to enforce the *regulated mortgage contract*, or to require that action is or is not taken.

**You should note that this section applies to *firms* with just a *mortgage administrator's* activity and those with both a *mortgage lender's* and *mortgage administrator's* activity.**

**You should also note, however, that if you have both a *mortgage lender's* activity and a *mortgage administrator's* activity to administer your own book and do not have any off-balance sheet loans to administer, then you should not complete this section of the *MLAR*.**

### G1 Mortgage contracts administered at end quarter

Collects data on mortgage contracts administered as at the end of the quarter, but only where you are formally acting as principal in exercising a *mortgage administrator's* activity. It therefore excludes the reporting of:

- any loan administration where you, being a firm without a *mortgage administrator's* activity, are merely providing an outsourced service for a third party which does have a *mortgage administrator's* activity and which is exercising it in respect of those loans; and
- any loan administration where you, a firm having a *mortgage administrator's* activity, are acting as agent and providing an outsourced

service for a third party which itself has a *mortgage administrator's* activity and which is exercising it in respect of those loans.

If you also have a *mortgage lender's* activity, then you should treat your own on and off-balance sheet loans as follows:

- (i) your *firm's* on-balance sheet loans should be excluded from G1.1 a) and G1.2 a). These items will therefore only include loans administered for third party lenders who do not themselves have a *mortgage administrator's* activity;
- ii) your *firm's* off-balance sheet loans should be included in G1.1 c) and G1.2 c). These will be the loans you have shown in section A3 "Securitised balances" under "gross balances". (These items G1.1 c) and G1.2 c) will also include loans you administer for other *special purpose vehicles* where you are formally exercising your *mortgage administrator's* activity).

### **G1.1 Number of loans**

You should detail the number of *regulated mortgage contracts* administered as at the end of the quarter for *firms* with a *mortgage lender's* activity, for other *firms* (i.e. lenders for which you administer mortgages but they themselves do not have a *mortgage lender's* activity) and for *special purpose vehicles* ('SPVs') (i.e. *firms* that fall within the *Handbook* definition of a *special purpose vehicle*).

You should also detail the number of non regulated loans administered as at the end of the quarter for *firms* with a *mortgage lender's* activity, for other firms (i.e. lenders for which you administer mortgages but they themselves do not have a *mortgage lender's* activity) and for SPVs.

The total (all loans) is the sum of *regulated mortgage contracts* and non-regulated loans.

### **G1.2 Balance outstanding on loans**

You should detail the balances outstanding on all *regulated mortgage contracts* that you administer as at the end of the quarter for *firms* with a *mortgage lender's* activity, for other firms (i.e. lenders for which you administer mortgages but they themselves do not have a *mortgage lender's* activity) and for SPVs.

You should detail the balances outstanding on all non regulated loans that you administer as at the end of the quarter for *firms* with a *mortgage lender's* activity, for other firms (i.e. lenders for which you administer mortgages but they themselves do not have a *mortgage lender's* activity) and for SPVs.

The total (all loans) is the sum of *regulated mortgage contracts* and non-regulated loans.



## **G2 Lenders for whom mortgage administration was being carried out at quarter end**

Collects data only on the top five lenders for each category by value ( i.e. the largest five *firms* by value, based on balances outstanding on regulated loans) for whom mortgage administration was being carried out at the quarter end. (Details on other lenders are not required to be shown, over and above the top five listed in each category.)

### **G2.1 Firms with a mortgage lender's activity**

Please detail the top five *firms* (by value) for whom *mortgage administration* was being carried out at the quarter end.

You should include the *firm's* FSA reference number in addition to the name of the *firm*.

You should indicate the value of *regulated mortgage contracts* and non-regulated loans for each of the top five *firms* for whom you administer such contracts.

The total (all loans) for each firm listed is the sum of *regulated mortgage contracts* and non-regulated loans.

### **G2.2 Other firms**

Please detail the top five other *firms* (by value) for whom *mortgage administration* was being carried out at the quarter end (but who themselves do not have a *mortgage lender's* activity).

You should indicate the value of *regulated mortgage contracts* and non-regulated loans for each of the top five other firms for whom you administer.

The total (all loans) for each *firm* listed is the sum of *regulated mortgage contracts* and non-regulated loans.

### **G2.3 SPVs**

Please detail the top five SPVs (by value) for whom *mortgage administration* was being carried out at the quarter end. If your *firm* has off-balance sheet loans (which it has reported in G1.1 c) and G1.2 c)) then please show your *firm* as one of these five SPVs as follows:

- group together all SPVs for which your *firm* is the originator and show the aggregated amounts on a single line (irrespective of whether the total of regulated loans for all such SPVs would rank within the top five);

- under "FSA firm reference" column, put your *firm's FSA* reference number;
- under "Name of firm" column, put your *firm's* name followed by "own SPVs" in brackets, for example XYZ firm name (own SPVs).

You should indicate the value of *regulated mortgage contracts* and non-regulated loans for each of the top five SPVs for whom you administer.

The total (all loans) for each SPV listed is the sum of *regulated mortgage contracts* and non-regulated loans.

## SECTION H: MORTGAGE ADMINISTRATION – Arrears Analysis

### Type of loans to be reported

This arrears analysis should cover only those types of loan listed below, in respect of which your *firm* is formally acting as principal in exercising a *mortgage administrator's* activity. Thus, irrespective of whether your *firm* has a *mortgage administrator's* activity, if you are merely acting as an administrator for a third party that itself has, and is exercising, a *mortgage administrator's* activity, then you should not include any such loans in this analysis.

The types of loans to be included in the analysis are:

- (i) loans administered for *firms* which do not themselves have a *mortgage lender's* activity. These are the loans reported at G1.2 b) in table G.
- (ii) loans administered for third party SPVs.
- (iii) where your *firm* has a *mortgage lender's* activity, loans that represent your firm's off-balance sheet loans and which you have reported in section A3 of table A as "gross balances" under "Securitised balances".

**NB** loans in (ii) and (iii) are all those shown in G1.2c of table G.

The information presented in table H should represent the total of all such loan types listed above, in a single version of the table.

### H1-H5 Guidance on arrears items

The *guidance* for these items is provided in section F of these guidance notes, where items H1 to H5 correspond to items F1 to F5.

## SECTION J: FEE TARIFF MEASURES

### J1 Introduction

The purpose of this section is to enable the *firm* to provide data on the current **fee tariff measures** that apply to each of the regulated activities of *mortgage lending* and *mortgage administration*.

This section also distinguishes between the fee tariff measures that apply to the *FSA* (Financial Services Authority) and *FOS* (Financial Ombudsman Service).

Since the relevant fee tariff measures may change from time to time, these *guidance* notes merely define **where** the current definitions of fee tariff measures are to be found. Accordingly the following is a reference to the relevant part of the *FSA's* website where such details can be found:

\* Refer to *SUP 20 Annex 1R of the FSA Handbook*\*

## Part 8: SUP 16 Ann 20G

### Products covered by the reporting requirement in SUP 16.11

This is the *guidance* referred to in SUP 16.11.6G.

SUP 16.11.3R requires certain *firms* to report product sales data. For reporting purposes, a reportable sale applies where the contract has been made and the premium has been paid.

In the case of mortgage transactions, the reporting requirement only applies to loans for house purchase and remortgages and not to further advances. A reportable mortgage transaction applies where the mortgage transaction has completed (i.e. funds have been transferred and have been applied for the purpose of the mortgage).

## Part 1 - Products

The following tables provide *guidance* on the products for which sales data is to be reported. These tables are not intended to be a complete list of relevant products; *firms* should report sales data on all products which would fall within the scope of *retail investments*, *pure protection contracts*, and *regulated mortgage contracts*.

### Table 1 – RETAIL INVESTMENTS

Relevant products include:

<i>Unit trust scheme /OEIC</i>
<i>Investment trust</i>
<i>ISA</i>
<i>Structured capital-at-risk product</i>
With profit bond
<i>Unit linked bond</i>
Distribution bond
Mortgage Endowment
With profit endowment
Endowment savings plan
Guaranteed income/growth/investment bond
Trustee investment bond
Life annuity
Pension annuity
Long term care insurance contract
Stakeholder pension
Personal pension
Group personal pension
<i>FSAVC</i>
<i>Individual pension transfer</i>
<i>Pension opt out</i>
Section 32 buy out
Group section 32 buy out
<i>Income drawdown</i>

Executive pension  
SSAS  
Group money purchase  
AVC final salary  
AVC group money purchase

## Table 2 - PURE PROTECTION CONTRACTS

Relevant products include:

Income protection  
Standalone critical illness  
Critical illness sold as a rider benefit to mortgage protection and mortgage term assurances

## Table 3 - MORTGAGES

Relevant mortgage types include:

Fixed rate mortgages  
Discounted variable rate mortgages  
Tracker mortgages  
Capped rate mortgages  
Standard variable rate mortgages

## Part 2: Supporting product definitions/guidance for product sales data reporting

Part 2 contains *guidance* on the terms used in part 1 and on other relevant material.

Where products have not been defined in the *Glossary*, an explanatory description is provided.

### Retail investments

<b>PRODUCT</b>	<b>Guidance</b>
<u>With profit bond</u>	<b><u>Includes all single premium policies where a lump sum is paid into a with profits fund made up of investments such as company shares, fixed interest securities, commercial property and money. Unitised with profit bonds should be reported under this category.</u></b>
<u>Unit linked bond</u>	<b><u>A contract where the premium buys, or is deemed to buy investment units in a selected fund. The value of the policyholder's fund is linked to the value of the units (see guidance relating to distribution bonds).</u></b>
<u>Distribution bond</u>	<b><u>A single premium investment policy. The funds are invested in equities and gilts and an income is paid each year to the policyholder, dependent on the performance of the investments.</u></b>  Only report as a distribution bond where over 50% of the fund allocation relates to the distribution fund. If less than a 50% allocation is made, the product should be reported as a unit linked bond.
<i>Guaranteed income/growth/investment bond</i>	This includes income and growth bonds which include guaranteed income and guaranteed equity bonds that include guarantees and pay a percentage of the movement of more one or more index.
<i>Structured capital-at-risk product</i>	<i>Defined in the Handbook Glossary.</i>
<u>Life/pension annuity</u>	An arrangement by which a life company pays someone a regular income, usually for life, in return for a lump sum premium. This would include <ul style="list-style-type: none"> <li>• deferred and immediate annuities</li> <li>• compulsory purchase annuities</li> <li>• home income plans; and</li> <li>• all other types of life annuities</li> </ul>
<u>Unit trust scheme</u>	<i>Defined in the Handbook Glossary.</i>
<b><u>Investment trust</u></b>	<i>Defined in the Handbook Glossary.</i>
<b><u>ISA</u></b>	<i>Defined in the Handbook Glossary.</i> Cash and insurance ISAs should not be reported
<b>Endowment savings plan</b>	An endowment plan with a fixed term with benefits paid on death within the term or on maturity
<b>Mortgage endowment</b>	This should include any regular premium low cost endowments plus unitised with profit endowments

<b>Long-term care insurance contract</b>	[The FSA consulted in CP 200 on the definition of long-term care insurance contract that will apply from 14 January 2005. The guidance here will cross-refer to the finalised definition.]
<b>Stakeholder Pension</b>	<i>See Handbook Glossary for definition of 'stakeholder pension scheme'.</i>
<b>Personal pension</b>	<i>See Handbook Glossary for definition of 'personal pension scheme'.</i>  For reporting purposes do not include Rebate Only Pension business.
<b><u>Group personal pension</u></b>	<i>See Handbook Glossary for definition of 'group personal pension scheme'.</i>  Phased retirement should include transfer plans that permit staggered annuities to subsequently be purchased.  Deferred transfer plans should be excluded.  Report each individual policy as a separate case.
<b><u>FSAVC</u></b>	<i>Defined in the Handbook Glossary.</i>  Do not include Rebate Only Pension business.
<b><u>Individual pension transfer</u></b>	<i>See Handbook Glossary for definition of 'pension transfer'.</i>
<b><u>Pension opt out</u></b>	<i>Defined in the Handbook Glossary.</i>
<b>Section 32 buy out/ Group section 32 buy out</b>	An arrangement where trustees accept capital from employees who have left <i>occupational pension scheme</i> service and the transfer value is reinvested in an attempt to provide better benefits when the employee retires.
<b><u>Income drawdown</u></b>	<i>See Handbook Glossary for definition of income withdrawal'.</i>  This should include transfer plans that allow income from a pension plan in advance of an annuity being purchased
<b><u>Executive pension scheme</u></b>	An arrangement where each premium paid is identifiable to an individual employee and where an employer has discretion as to whether a pension arrangement is made for a particular employee and to the level of contribution or target benefit under the policy.  Report each individual policy as a separate case.  Pension premiums should be reported gross.
<b><u>SSAS</u></b>	<i>Defined in the Handbook Glossary.</i>  Pension premiums should be reported gross.  SSAS business should not be reported if you only provide an administration service.  Report each individual policy as a separate case.
<b><u>Trustee investment bond</u></b>	A lump sum <i>investment</i> vehicle designed for use by <i>pension scheme</i> trustees. Includes SSAS Trustee Investment Bonds and SIPP Trustee Investment Bonds



<u>Group money purchase</u>	An <i>occupational pension scheme</i> which provides <i>money-purchase benefits</i> which is available to employees of the same employer or of employers within a group.
<u>AVC Final salary</u>	Pension premiums should be reported gross.
<u>AVC Group money purchase</u>	Pension premiums should be reported gross.

## Mortgages

### (a) Types of interest rate

<u>Types of interest rate</u>	<b>Description</b>
<b>Fixed rate</b>	where the interest rate is fixed for a stated period.
<b>Discounted rate</b>	where a discount is applied to the lender's standard variable rate usually for a limited period of time.
<b><u>Tracker</u></b>	where the interest rate is guaranteed to move in line with either the Bank of England Base (or repo) Rate (BBR) or another index such as LIBOR (London InterBank Offered Rate).
<b><u>Capped (and collared) rate mortgage</u></b>	where the interest rate is guaranteed not to exceed a stated maximum rate (the 'capped' rate) for specific period of time, but where the standard variable interest rate applies when the rate is lower than the capped rate. Also includes products where the interest rate is subject to a minimum rate (the 'collared' rate).
<b><u>Cashback</u></b>	a cash amount paid by a <i>mortgage lender</i> to a <i>customer</i> (typically at the beginning of a contract) as an inducement to enter into a <i>regulated mortgage contract</i> with the <i>mortgage lender</i> .
<b><u>Standard variable rate</u></b>	<u>the lender's underlying interest rate.</u>

### (b) Features

<b>Data Item</b>	<b>Description</b>
<b>Flexible mortgage</b>	<p>A mortgage where you can change the monthly payments and pay off part or all of the loan whenever you like. It is normally linked to any interest rate type.</p> <p>Details vary from one mortgage to another, but for reporting purposes, to be reported as a flexible mortgage, the mortgage should have the following features:</p> <ul style="list-style-type: none"> <li>• interest must be calculated monthly or daily; and</li> <li>• must have an overpayment facility</li> </ul>
<b>Offset mortgage – positive and/or negative offset</b>	An offset mortgage will typically have similar facilities to a flexible mortgage, but will also allow the borrower to offset positive (savings and/or current account) and/or

	negative balances (credit card and/or personal loans) against their outstanding mortgage balance.
<b>Loans where income is not evidenced</b>	This applies to loans which are based on one or more <i>persons'</i> incomes. These loans are those where the lender has no independent documentary evidence to verify income (e.g. as provided by an employer's reference, a bank statement, a salary slip, a P60, or audited/certified accounts).
<b>Total gross income</b>	This is the total of the gross annual incomes (before tax or other deductions) of each of the individual borrowers whose incomes were taken into account when the lender made the lending assessment/decision. For these purposes, each borrower's gross income is the sum of that person's main income and any other reckonable income (e.g., overtime, income from other sources etc to the extent that the lender takes such additional income into account in whole or in part). For example if borrower A has gross income of £25,000 and borrower B has gross income of £20,000 then total gross income for the loan would be £45,000

## Pure protection contracts

<b><u>Policy type</u></b>	<b>Description</b>
<b>Standalone critical illness</b>	These policies are 'pure' critical illness policies i.e. there is no life cover sold alongside them. Under these policies the <i>insurer</i> provides the sum insured to the <i>policyholder</i> in the event of diagnosis of a life threatening condition.
<b>Critical illness sold as a rider benefit to term assurance</b>	For reporting purposes, this applies where critical illness is offered as a rider benefit to either a mortgage protection policy (a <i>life policy</i> that provides by means of decreasing term assurance for a mortgage to be paid off in the event of the borrower's death) or a protection term assurance contract.
<b>Income protection</b>	Insurance contracts arranged by an individual to provide for payment of income during a period of incapacity, due to ill health or accident

**Part 9: SUP 16 Ann 21R**

**REPORTING FIELDS**

This is the annex referred to in SUP 16.11.7R.

**1 - GENERAL REPORTING FIELDS**

The following data reporting fields must be completed, where applicable, for all reportable transactions and submitted in a prescribed format. Shaded boxes represent non-compulsory data items.

<b>Data reporting field</b>	<b>Code (where applicable)</b>	<b>Notes</b>
FSA reference number of product provider	6 digit number	This field must contain the FSA reference number of the <i>firm</i> providing the data report.
FSA reference number of <i>firm</i> which sold the product	6 digit number	This field must contain the FSA reference number of the <i>firm</i> which sold the product.  For <i>firm's</i> own direct sales, enter <i>firm's</i> own FSA reference number.  For sales via an intermediary enter the intermediary's reference number.
<b>Advice at point of sale</b>	<b>Y = advised</b>  <b>N = non-advised</b>	<b>This information will not have to be reported until July 2006.</b>  <b><i>Firms</i> will however be able to report his information before then if appropriate by using the appropriate code to indicate whether the sale was advised or non-advised.</b>  <b>For reporting purposes non- advised includes execution only and direct offer transactions.</b>
FSA reference number of the intermediary's <i>principal</i> or <i>network</i>	6 digit number	This field only applies if the sale has been made by an intermediary who has a <i>principal</i> or is part of a <i>network</i> .

**2 - SPECIFIC REPORTING FIELDS**

**(a) Retail investments**

The following data reporting fields must be completed, where applicable, for all *retail investment* transactions, including *structured capital-at-risk products*:

<b>Data reporting field</b>	<b>Illustrative code (where applicable)</b>	<b>Notes</b>
Product type	Numeric	Enter relevant product code. If none of the existing codes apply report sale as 'O' for other.
Post code of customer	e.g. XY45 6XX	Applies to first named customer only.
Method of <i>premium/contribution</i> payment	S = single R = regular	Use code to indicate method of payment.
Total <i>premium/contribution</i> amount	Numeric £	Enter annualised amount rounded to nearest £
Date of birth	DD/MM/YYYY	Applies to first named customer at time of sale i.e. age obtained at proposal stage.

**(b) Pure protection contracts**

The following data reporting fields must be completed, where applicable:

<b>Data reporting field</b>	<b>Illustrative code (where applicable)</b>	<b>Notes</b>
Policy type	Numeric	Enter relevant product code. If none of the existing codes apply report sale as 'O' for other
Method of <i>premium</i> payment	S = single R = regular	Use code to indicate method of payment.
Total <i>premium</i> amount	Numeric	Enter annualised amount rounded to nearest £.

**(c) Mortgages**

**The following data reporting fields must be completed, where applicable for all regulated mortgage transactions (with the exception of further advances):**

**Note :** In the case of mixed interest rate options/combo mortgages, sales data should only be provided for the rate applying to the largest portion of the overall mortgage balance.

<b>Data reporting field</b>	<b>Illustrative code (where applicable)</b>	<b>Notes</b>
Date mortgage account opened	DD/MM/YYYY	Date of mortgage completion or draw-down of the funds.
Interest rate type	F = fixed rate C = capped rate D = discount T = tracker V = standard variable rate O = other	Enter the relevant code  If none of the existing codes apply enter sale as 'O' to denote 'other'.  Only 1 code can be entered
Mortgage characteristics	CB = cashback  FF = flexible features (allowing overpayments and underpayments)  OS = offset positive and or negative balances.  L = the loan is a <i>lifetime mortgage</i>  SAM = the loan is a <i>shared appreciation mortgage</i>	Use code to indicate additional mortgage characteristics if applicable.  Cashback should only be reported where it is linked to a variable interest rate and where the cashback is not being provided as an incentive to pay legal costs and valuation fees.  Where more than 1 code applies, report all
Post code of the mortgaged	e.g. XY45 6XX	

property		
Type of borrower	<p>F = first time buyers</p> <p>M = home movers (2<sup>nd</sup> or subsequent buyers)</p> <p>R = remortgagors</p> <p>C= council/ registered social landlord tenant exercising their right to buy</p> <p>O = other</p> <p>N = not known</p>	<p>Use code to indicate type of borrower.</p> <p>Only 1 code should be entered</p>
Method of repayment	<p>C = capital and interest</p> <p>E = interest only/ endowment</p> <p>I = interest only/ ISA</p> <p>P = interest only/ pension</p> <p>U = interest only/ unknown</p> <p>M = mix of capital and interest only</p> <p>N = not known</p>	<p>Use code to indicate method of mortgage repayment</p> <p>Only 1 code should be entered</p>
Term of mortgage	Numeric	<p>Number in whole years.</p> <p>(Optional for <i>Lifetime</i> and <i>Shared appreciation mortgages</i>)</p>
Size of loan	Numeric £	Report the original interest bearing balance at completion of the mortgage.
Value of the mortgaged property	Numeric £	<p>The value reported should be based on:</p> <ul style="list-style-type: none"> <li>the surveyors valuation (or from a valuation index) or</li> <li>from the customers estimated value as captured on the application form.</li> </ul>

		In the case of staged construction or self build schemes, value means 'expected final value of property at the time lending decision is made'.
Income Basis	S = single income J = joint income	Use code to indicate whether the income assessment has been made on a single or joint basis  (Optional for <i>Lifetime</i> and <i>Shared appreciation mortgages</i> )
Age of main borrower	DD/MM/YYYY	Report age of main borrower only.
Remortgage transactions <u>only</u>	N = no extra money raised H = extra money raised for home improvements D = extra money raised for debt consolidation M- extra money raised for home improvements and debt consolidation O = other	Use code to indicate the purpose of the remortgage.  Only 1 code can be entered
Employment status of main borrower	<b><u>F = full time employee</u></b> <b><u>S = self employed</u></b> <b><u>R = retired</u></b> <b><u>O = other</u></b>	Applies to main borrower only.  Only 1 code can be entered
Total gross income	Numeric £	The total income of all borrowers whose income was used in the credit assessment (see guidance notes for further explanation)  (Optional for <i>Lifetime</i> and <i>Shared appreciation mortgages</i> )
Income verification	Y = income evidenced N = income not evidenced	Applies to loans based on one or more persons' incomes (see guidance notes relating to 'loans where income is not evidenced')  (Optional for <i>Lifetime</i> and <i>Shared appreciation</i>

		<i>mortgages</i>
County court judgments (CCJs) Value	Numeric £	Applies where borrower/s has one or more CCJs within the <b>last 3 years</b> - either satisfied or unsatisfied - with a total value greater than £500.
Impaired credit history	A = arrears  V = IVA  Bankruptcy	Use code/s to indicate applicable credit history  A = applies to secured loans and unsecured loans where the borrower/s has arrears on a previous (or current) mortgage or other secured loan within the <b>last 2 years</b> where the cumulative amount overdue at any point reached three or more monthly payments or  V = applies where the borrower/s have been subject to an individual voluntary arrangement (IVA) at any time within the <b>last 3 years</b>  B = applies where the borrower/s have been subject to a bankruptcy order at any time within the <b>last 3 years</b>

### **3 - OPTIONAL REPORTING FIELDS**

1. The following data items are not currently mandatory reporting fields. *Firms* are not obliged to report these items within the data report if the data is not readily available.

<b>Data reporting field</b>	<b>Code (where applicable)</b>	<b>Notes</b>
Initial gross charging rate of interest	numeric	The amount of interest reported should be the initial gross nominal rate charged on the loan and should take into account any discount being provided. Where the advance is split, the interest rate applying to the largest part of the advance should be entered.
Date incentivised rate ends	DD/MM/YYYY	Only applies to fixed, capped or discounted rates where the customer is paying an incentivised rate for a set period.
Date <i>early repayment charge</i> ends	DD/MM/YYYY	If applicable, report date early repayment charge ends.



2. The following data items are not required for regulatory purposes and should only be reported by *mortgage lenders* who currently support the SML (Survey of Mortgage Lenders).

<b>Data reporting field</b>	<b>Code (where applicable)</b>	<b>Notes</b>
Purchase price of property (Purchases only)	£ numeric	Purchase price as stated on application form.
Type of dwelling	B= bungalow D= detached house S = semi – detached house T = terraced house F = flat or maisonette in converted house P= purpose built flat or maisonette O = other	Use code to indicate property type  Only 1 code can apply
Number of habitable rooms	numeric	Include kitchen but not bathroom/toilet
Number of bedrooms	numeric	
Does the property have a garage	Y=Yes N=No	The garage should be a permanent structure but does not have to stand on the main site of the property.
Is the dwelling new?	Y=Yes N=No	New refers to the period in which the main structure of the dwelling was completed and also means where a dwelling is being occupied for the first time. Does not therefore include new conversions of older dwellings.
Is mortgage payment protection insurance (MPPI) being taken out with the mortgage?	Y=Yes N=No	MPPI can be any of the following:  - full accident, sickness and unemployment insurance; or - accident and sickness only; or - unemployment only.  Report 'Yes' even where the policy was sold or provided free and irrespective of whether the premiums are collected by the lender or the insurer.

## Annex B

### Amendments to the Glossary

In this Annex, all text is new and it is not underlined.

Insert the following new definitions in the appropriate alphabetical position:

<i>exempt insurance intermediary</i>	<p>an <i>insurance intermediary</i>:</p> <ul style="list-style-type: none"><li>(a) whose <i>Part IV permission</i> is limited to or includes <i>insurance mediation activity</i>;</li><li>(b) which, in relation to <i>insurance mediation activity</i> (but disregarding money or other assets held in relation to other activities) either:<ul style="list-style-type: none"><li>(i) does not hold any <i>client money</i> or other <i>client assets</i> in any form; or</li><li>(ii) holds <i>client money</i> as trustee under a statutory trust imposed by CASS 5.3 (statutory trust) but does not otherwise hold <i>client money</i>; and</li></ul></li><li>(c) which (when aggregating the amount calculated in accordance with CASS 5.5.65R) does not in relation to <i>insurance mediation activity</i> hold <i>client money</i> in excess of £30,000 at any time during a <i>financial year</i>.</li></ul>
<i>MLAR</i>	(in <i>SUP</i> ) a Mortgage Lending and Administration Return containing data specified in <i>SUP 16 Ann 19AR</i> and relevant to the <i>firm's</i> type and <i>regulated activities</i>
<i>retail investment</i>	<ul style="list-style-type: none"><li>(a) a <i>life policy</i>; or</li><li>(b) a <i>unit</i>; or</li><li>(c) a <i>stakeholder pension scheme</i>; or</li><li>(d) an interest in an <i>investment trust savings scheme</i>; or</li><li>(e) a <i>structured capital-at-risk product</i>.</li></ul>
<i>retail investment firm</i>	a <i>firm</i> that has <i>permission</i> to carry on an activity which is a <i>retail investment activity</i> .

*retail investment activity*

- (a) *advising on investments;*
- (b) *arranging (bringing about) deals in investments;*  
*or*
- (c) *making arrangements with a view to transactions*  
*in investments,*

in relation to *retail investments*, except when carried on by a *firm* exclusively with or for *intermediate customers* or *market counterparties*.

*RMAR*

(in *SUP*) a Retail Mediation Activities Return, containing data specified in *SUP* 16 Ann 18A R and relevant to the *firm's* type and *regulated activities*

**ADDENDUM**

**SUPERVISION MANUAL (REPORTING AND AUDIT REQUIREMENTS)  
INSTRUMENT 2004**

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex A, part 4, of this instrument is amended as follows:

Sup 16 Ann 18AR Retail Mediation Activities Return ('RMAR')

Section D2

...						
<b>13</b> Less excess of current year drawings over current year <u>profits</u> <del>losses</del>						

Addendum  
18 March 2005

## **SECOND ADDENDUM**

### **SUPERVISION MANUAL (REPORTING AND AUDIT REQUIREMENTS) INSTRUMENT 2004**

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex A, part 4, of this instrument is amended as follows:

Sup 16 Ann 18AR Retail Mediation Activities Return ('RMAR')

## SECTION D1: Regulatory Capital

Is the firm exempt from these capital requirements in relation to any of its retail mediation activities?

	Non- investment insurance	Retail investments
<b>Mortgage</b>		
RR0198	RR0199	RR0200

### Mortgage and non-investment insurance

Base requirement

5% of annual income (firms holding client money)

2.5% of annual income (firms not holding client money)

Client money	Non-client money
RR0202	RR0203
RR0205	
	RR0206

### Capital requirement (higher of above)

RR0207	RR0208
--------	--------

Other FSA capital requirements (if applicable)

Additional capital requirements for PII (if applicable)

RR0210
RR0211

**TOTAL CAPITAL REQUIREMENT**

**TOTAL CAPITAL RESOURCES**

**TOTAL CAPITAL EXCESS/DEFICIT**

RR0212	See notes
RR0213	
RR0214	

### IPRU(INV) requirements for personal investment firms (retail investment activities only)

Category of personal investment firm under IPRU(INV)

RR0215a
---------

### Own funds requirement

Own funds

Surplus/deficit of own funds

Additional own funds requirement for PII (if applicable)

Other FSA capital requirements (if applicable)

RR0216	A
RR0217	B
RR0218	C
RR0219	
RR0219a	

Adjusted net current assets requirement (if applicable)

Adjusted net current assets (if applicable)

Surplus/deficit (if applicable)

RR0220	D
RR0221	E
RR0222	F

Expenditure based requirement (if applicable)

Adjusted Capital/liquid capital (if applicable)

Surplus/deficit (if applicable)

RR0223	G
RR0224	H
RR0225	I

### Eligible capital (mortgage and non-investment insurance)

#### Incorporated firms

Share capital

Audited reserves

Interim net profits (audited verified)

Interim net profits (not audited verified)

Revaluation reserves

Eligible subordinated loans

**less** Investments in own shares

**less** Intangible assets

**less** interim net losses

TOTAL CAPITAL RESOURCES

RR0228
RR0229
RR3231
RR3232
RR0233
RR0234
RR0235
RR0236
RR0237
RR0238

#### Unincorporated firms

Capital of a sole trader or partnership

Eligible subordinated loans

Personal assets not needed to meet non-business liabilities

**less** Intangible assets

**less** interim net losses

**less** excess of drawings over profits for a sole trader or p'ship

TOTAL CAPITAL RESOURCES

RR0240
RR0245
RR0246
RR0247
RR0248
RR0249
RR0250

Annex A, part 5, of this instrument is amended as follows:  
 SUP 16 Ann18B G Notes for completion of the Retail Mediation Activities Return ('*RMAR*')

...

Application of *RMAR* sections

...

8. ... will not be subject to our ~~proposed~~ data requirements for ~~financial reporting balance sheet and profit & loss account~~ in the *RMAR* (*RMAR* sections A and ~~BC, D & E~~). For details see SUP 16.7.

...

Section D1: guide for completion of individual fields

...	
<b>Eligible capital (mortgage and non-investment insurance)</b>	
...	
Interim net profits ( <del>audited</del> <u>verified</u> )	Interim net profits should be <del>audited</del> <u>verified</u> by the <i>firm's</i> external auditor, net of tax or anticipated dividends and other appropriations to be included as capital.
Interim net profits (not <del>audited</del> <u>verified</u> )	Other unverified profits (not included in total capital resources)

Second Addendum  
 29 September 2005

**ELECTRONIC REPORTING REQUIREMENTS AND  
STANDING DATA INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force:
- (1) in respect of the transitional provisions in Annex B, on the dates specified in those provisions; and
  - (2) otherwise, on 1 April 2005.

**Amendments to the Supervision manual (SUP)**

- D. SUP is amended in accordance with Annex A to this instrument.

**Amendments to the Dispute resolution: Complaints sourcebook (DISP)**

- E. DISP is amended in accordance with Annex B to this instrument.

**Amendments to the Credit Union sourcebook (CRED)**

- F. CRED is amended in accordance with Annex C to this instrument.

**Amendments to the Glossary**

- G. The Glossary is amended in accordance with Annex D to this instrument.

**Citation**

- H. This instrument may be cited as the Electronic Reporting Requirements and Standing Data Instrument 2004.

By order of the Board  
18 March 2004



## Annex A

### Amendments to the Supervision manual

In this Annex underlining indicates new text. Where an entire new section or annex is inserted, the place it goes is indicated and the text is not underlined.

#### 16.1.3 R Table: Application of different sections of SUP 16

(1) Section(s)	(2) Categories of firm to which section applies	(3) Applicable rules and guidance
...		
<i>SUP 16.9</i>	...	
<u><i>SUP 16.10</i></u>	<u>All categories of <i>firm</i> except:</u> <u>(a) an <i>ICVC</i>;</u> <u>(b) a <i>UCITS</i> <i>qualifier</i>; and</u> <u>(c) a <i>credit union</i>.</u>	<u>Entire section</u>

After SUP 16.9 (Appointed representatives annual report) insert the following new section:

#### 16.10 Confirmation of standing data

##### Application

16.10.1 G The effect of *SUP 16.1.1R* is that this section applies to every *firm* except:

(1) an *ICVC*; or

(2) a *UCITS* *qualifier*; or

(3) a *credit union*.

##### Purpose

16.10.2 G *Standing data* is used by the *FSA*:

- (1) to ensure that a *firm* is presented with the correct regulatory return when it seeks to report electronically;
- (2) in order to communicate with a *firm*;
- (3) as the basis for some sections of the *FSA Register*; and
- (4) in order to carry out thematic analysis across sectors and groups of *firms*.

16.10.3 G In view of the importance attached to *standing data*, and the consequences which may result if it is wrong, this section provides the framework for a *firm* to check and correct it.

Requirement to check the accuracy of standing data and to report to the FSA

- 16.10.4 R
- (1) Within 30 *business days* of its *accounting reference date*, a *firm* must check the accuracy of its *standing data* through the relevant section of the *FSA* website.
  - (2) If the *standing data* is correct, the *firm* must communicate that to the *FSA* using the electronic facility provided on the *FSA* website.
  - (3) If any *standing data* is incorrect, the *firm* must give the corrected *standing data* to the *firm*'s usual supervisory contact at the *FSA* by electronic mail.
- 16.10.5 G The *standing data* is made available to the *firm* when the *firm* logs into the appropriate section of the *FSA* website. The *firm* should check the *standing data* and send any corrections to the *FSA*. If there are no errors, the *firm* will be asked to signal this by pressing the appropriate button on the web page.
- 16.10.6 G A *firm* may check, and submit corrections to, its *standing data* more frequently than annually.

After SUP 16 Annex 15, insert the following new Annexes:

SUP 16 Annex 16R: Standing data (see SUP 16.10.4R)

A: Communications with a *firm*

1. Name of the *firm*
2. Trading name(s) of the *firm*
3. Country of incorporation
4. Registered office
5. Principal place of business
6. Website address
7. Telephone number
8. The name and email address of the principal compliance contact

B: Information about a firm on the *FSA Register*

9. *Regulated activities* for which a *firm* has *permission*
10. Whether the *firm* holds *client money*
11. Whether the *firm* is an “*ISD investment firm*”

C: Other information about a *firm*

12. *Firm* types
13. *Passported activities*
14. Name and address of *firm's* auditor
15. Legal status
16. *Accounting reference date*

SUP 16 Annex 17 R: List of *firm* types (see SUP 16 Annex 16R, paragraph 12)

Firm type

*alternative trading system (ATS) operator*

*authorised professional firm*

*bank*

*building society*

CIS administrator

CIS trustee

composite insurer

*corporate finance advisory firm*

*credit union*

*custodian*

*depository*

discretionary investment manager

*e-money issuer*

*energy market participant*

*friendly society*

*general insurer*

*insurance intermediary*<sup>1</sup>

*long-term insurer*

*managing agent*

*members' agent*

*members' adviser*

*market maker*

*media firm*

*mortgage administrator*<sup>2</sup>

*mortgage adviser*<sup>2</sup>

*mortgage arranger*<sup>2</sup>

*mortgage lender*<sup>2</sup>

*network*

non-discretionary investment manager

*oil market participant*

*operator*

*OPS firm*

own account trading firm

reinsurance intermediary

retail investment firm

*securities and futures firm*

*service company*

*venture capital firm*

wholesale market broker

*wholesale only bank*

...

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<sup>1</sup> Definition made by the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004

<sup>2</sup> Definition made by the Mortgage: Conduct of Business Sourcebook Instrument 2003

SUP Schedule 2 – Notification requirements

Table 2

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
<b>SUP 16.9.3R</b>	<b>Details of appointed representatives. Every firm with a <i>Part IV permission to advise on investments, arrange (bring about) deals in investments, make arrangements with a view to transactions in investments, or arrange safeguarding and administration of assets</i></b>	<b>A list of all the current <i>appointed representatives of the firm</i> as at the <i>firm's accounting reference date</i>. A report is not required if a <i>firm</i> has no <i>appointed representatives</i> as at the <i>firm's accounting reference date</i> and this is reflected in the relevant extract from the <i>FSA Register</i>.</b>	<b>Annually</b>	<b>Four months</b>
<b><u>SUP 16.10.4R</u></b>	<b><u>Confirmation of standing data items</u></b>	<b><u>Confirmation of accuracy of standing data or correction of inaccuracies</u></b>	<b><u>Accounting reference date</u></b>	<b><u>30 business days after accounting reference date</u></b>
<b>SUP 17</b>	<b>Transaction reporting</b>  <b>This applies to</b>  <b>(a) a <i>securities and futures firm</i>; or</b> <b>(b) a <i>personal investment firm</i>; or</b>	<b>The fact of intending to use one of the systems specified</b>	<b>Before using one of the reporting systems listed in <i>SUP 17.7.8 R</i>:</b>  <b>(1) CEDCOM system operated by Clearstream Banking AG, Frankfurt;</b>	<b>Before using the system specified</b>
...				

...

## Annex B

### Amendments to the Dispute resolution: Complaints Sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where the provisions of an entire section are replaced, the section is indicated and the new text is not underlined.

1 Table Transitional Provisions table

(1)	(2) <u>Material to which the transitional provision applies</u>	(3)	(4) <u>Transitional provision</u>				(5) <u>Transitional provision: dates in force</u>	(6) <u>Handbook provision: coming into force</u>
...								
10	<u>DISP 1.5.4R</u>	R	<u>DISP 1.5.4R does not apply to a firm with permission to carry on only insurance mediation activity, mortgage mediation activity, or both.</u>				(1) In respect of <u>mortgage mediation activities, 31.10.04 – 31.3.05;</u> (2) in respect of <u>insurance mediation activities, 14.1.05 – 31.3.05.</u>	
11	<u>DISP 1.5.4R</u>	R	<u>Where a firm is required under DISP 1.5.4R to submit information using a report in the format set out in DISP 1 Ann 1R on a half-yearly basis, this must be read as a reference to providing the first and second report in accordance with transitional provision 12R.</u>				<u>From 01.4.05, expiring on 31.3.06</u>	<u>1 April 2005</u>
12	<u>DISP 1.5.4R</u>	R	<u>If transitional provision 11R applies, the firm's first and second report must be provided as follows:</u>					
			<u>Accounting reference date</u>	<u>Reporting period starts</u>	<u>Reporting period ends</u>	<u>Report to be provided</u>		
			<u>Between 1 January 2005 and 31 March 2005</u>	<u>1<sup>st</sup> report:</u> <u>1 April 2005</u>	<u>6 months after accounting reference date within 2005</u>	<u>30 business days after period end</u>		
				<u>2<sup>nd</sup> report:</u> <u>6 months after the business day following the accounting reference date within 2005</u>	<u>accounting reference date within 2006</u>			

<u>Between 1 April 2005 and 30 June 2005</u>	1 <sup>st</sup> report: <u>1 April 2005</u>	<u>accounting reference date within 2005</u>	<u>30 business days after period end</u>
	2 <sup>nd</sup> report: <u>the business day following the accounting reference date within 2005</u>	<u>6 months after the accounting reference date within 2005</u>	
<u>Between 1 July 2005 and 30 September 2005</u>	1 <sup>st</sup> report: <u>1 April 2005</u>	<u>accounting reference date within 2005</u>	<u>30 business days after period end</u>
	2 <sup>nd</sup> report: <u>the business day following the accounting reference date within 2005</u>	<u>6 months after the business day following the accounting reference date within 2005</u>	
<u>Between 1 October 2005 and 31 December 2005</u>	1 <sup>st</sup> report: <u>1 April 2005</u>	<u>6 months preceding the accounting reference date within 2005</u>	<u>30 business days after period end</u>
	2 <sup>nd</sup> report: <u>6 months preceding the accounting reference date within 2005</u>	<u>accounting reference date within 2005</u>	

...

### Reporting complaints to the FSA

- 1.5.4 R A *firm* must provide the *FSA*, twice a year, with a report in the format set out in *DISP* 1 Ann 1R which contains (for the relevant reporting period) information about:

...

- (2) the total number of complaints subject to *DISP* 1.4 – *DISP* 1.6 closed by the *firm* :

...

- (c) more than eight weeks after receipt; ~~and~~
- (3) the total number of complaints subject to *DISP* 1.4 – *DISP* 1.6:
  - (a) upheld by the *firm* in the reporting period;
  - (b) that the *firm* knows have been referred to, and accepted by, the *FOS* in the reporting period; and
  - (c) outstanding at the end of the reporting period; and
- (4) the total amount of redress paid in respect of complaints subject to *DISP* 1.4 – *DISP* 1.6 during the reporting period.

1.5.5 G For the purpose of *DISP* 1.5.4R, upon completing the return, the *firm* should note that:

- (1) Where a complaint could fall into more than one category, the complaint should be recorded in the category which the *firm* considers to form the main part of the complaint.
- (2) Where a complaint has been upheld under *DISP* 1.5.4R (3)(a), a *firm* should report any complaints to which it has given a final response which accepts the complaint and, where appropriate, offers redress, even if the redress offered is disputed by the complainant. Where a complaint is upheld in part, a *firm* should treat the whole complaint as upheld for reporting purposes. Where a *firm* rejects a complaint, yet chooses to make an ex-gratia payment to the complainant, the complaint should be recorded as 'rejected'.
- (3) Where a *firm* reports on the amount of redress paid under *DISP* 1.5.4R (4), redress should be interpreted to include an amount paid, or cost borne, by the *firm*, where a cash value can be readily identified, and should include:
  - (a) amounts paid for distress and inconvenience;
  - (b) a free transfer out to another provider which transfer would normally be paid for;
  - (c) ex-gratia payments and goodwill gestures;
  - (d) interest on delayed settlements;
  - (e) waiver of an excess on an insurance policy; and
  - (f) payments to put the consumer back into the position the consumer should have been in had the act or omission not occurred.
- (4) Where a *firm* reports on the amount of redress paid under *DISP* 1.5.4R (4), such redress should not, however, include repayments or



refunds of premiums which had been taken in error (for example where a *firm* had been taking, by direct debit, twice the actual premium amount due under a policy). The refund of the overcharge would not count as redress.

1.5.6 R For the purposes of *DISP* 1.5.4R:

~~(1) the relevant reporting periods are from 1 April to 30 September and from 1 October to 31 March each year; and~~

~~(2) reports are to be submitted to the FSA within one month of the end of the relevant reporting period.~~

(1) The relevant reporting periods are:

(a) the six months immediately following a *firm's* accounting reference date; and

(b) the six months immediately preceding a *firm's* accounting reference date.

(2) Reports are to be submitted to the *FSA* within 30 business days of the end of the relevant reporting period.

...

Method of submission of reports

1.5.10 R A report under this section must be ~~given or addressed, and delivered, in the way set out in SUP 16.3.6R–SUP 16.3.16G (General provisions on reporting), except that:~~

~~(1) instead of the *firm's* usual supervisory contact, the report should be given to or addressed for the attention of the Notification, Reporting & Data Maintenance department of the *FSA*; and~~

~~(2) in addition to the methods of submission of reports in SUP 16.3.9R, a *firm* may submit a report under this section submitted through, and in the electronic format specified in, the *FSA* Complaints Reporting System or the appropriate section of the *FSA* website.~~

1.5.10A R ~~[deleted] A *firm* that has started but intends to stop submitting reports in electronic format under DISP 1.5.10R (2) must first notify the Notification, Reporting & Data Maintenance department of the *FSA* in writing of this intention.~~

Failure of electronic submission

1.5.10B R If a *firm* is unable to submit a report in electronic format because of a systems failure of any kind, the *firm* must ÷

- ~~(1) — submit its report under this section through one of the alternative methods of submission or reports in SUP 16.3.9R; and~~
- ~~(2) — notify the *FSA*, in writing and without delay, of that systems failure.~~

...

DISP 1 Annex 1

Sections 5 and 6 of the Complaints Return are replaced as follows:

Section 5: Private Individual Complaints

	Overcharging	Delays	Other admin	Misleading advice	Failure to carry out instructions	Poor customer service	Misleading advertising	Disputes over sums/amounts	Switching/churning	Breach of contract	Arrears handling	Other
FSAVC												
Personal Pension												
Stakeholder Pension												
Mortgage Endowment												
Other Endowment												
Whole of Life												
Permanent Health												
Term Assurance												
PEP/ISA												
Cash Deposit ISA												
Investment Trust												
Unit Trust/OEIC												
Investment Bond												
Share/Derivative												
Other Regulated Investments												
Current Account												
Deposit/Savings												
Credit Card												
Lifetime Mortgage												
Flexible Mortgage												
Impaired Credit Mortgage												
Self Cert Mortgage												
Other Regulated Mortgage												
Other unregulated loan secured on land												
Other loans												
Standard Annuity												
Investment based Annuity												
Income Withdrawal Product												
Income Protection												
Long Term Care												
Private Medical Insurance												
Critical Illness												
Motor												
Property												
Other GI/Pure protection												
Other												
Total												

If no private individual complaints were received during the period, tick the box and go to Section 6

## Section 6: Small Business Complaints

	Overcharging	Delays	Other admin	Misleading advice	Failure to carry out instructions	Poor customer service	Misleading advertising	Disputes over sums/amounts	Switching/churning	Breach of contract	Arrears handling	Other
FSAVC												
Personal Pension												
Stakeholder Pension												
Mortgage Endowment												
Other Endowment												
Whole of Life												
Permanent Health												
Term Assurance												
PEP/ISA												
Cash Deposit ISA												
Investment Trust												
Unit Trust/OEIC												
Investment Bond												
Share/Derivative												
Other Regulated Investments												
Current Account												
Deposit/Savings												
Credit Card												
Lifetime Mortgage												
Flexible Mortgage												
Impaired Credit Mortgage												
Self Cert Mortgage												
Other Regulated Mortgage												
Other unregulated loan secured on land												
Other loans												
Standard Annuity												
Investment based Annuity												
Income Withdrawal Product												
Income Protection												
Long Term Care												
Private Medical Insurance												
Critical Illness												
Motor												
Property												
Other GI/Pure protection												
Other												
Total												

If no small business complaints were received during the period, tick the box and go to Section 7

...

Delete Section 9 of the Complaints Return. After section 8 of the Complaints Return, insert:

Section 9: Complaints management

9.01 Number of complaints upheld by the *firm* in the period

9.02 Total amount of redress paid to *consumers* in the period

9.03 Number of complaints referred to, and accepted by, the *FOS* in the period

Section 10: Declaration

Knowingly or recklessly giving the *FSA* information which is false or misleading in a material particular may be a criminal offence (section 398 of the Financial Services and Markets Act 2000) and a breach of regulatory requirements.

In submitting this form, the *firm* acknowledges that the data supplied may be used by the *FSA* in a variety of different ways (including making it publicly available) in support of its principal functions and statutory objectives as provided for under the Financial Services and Markets Act 2000.

I confirm that I have read the notes and that the information given in this return about complaints received by the *firm* named at Section 1.02 is accurate and complete to the best of my knowledge and belief.

10.01 Name of *person* completing on behalf of the *firm*

10.02 Job title

10.03 Date

...

Notes on the completion of this return

...

Reporting period

~~The two annual reporting periods are from 1 April to 30 September, and from 1 October to 31 March (DISP 1.5.6R). Returns must be submitted within one month of the end of the relevant reporting period.~~

The two annual reporting periods are: 1) from the six months preceding the *firm's* accounting reference date to the *firm's* accounting reference date, and 2) from the *firm's* accounting reference date to the six months following the *firm's* accounting reference date (DISP 1.5.6R). Returns must be submitted within 30 business days of the end of the relevant reporting period.

...

## Section 2 – Nil Returns

If no complaints of any kind have been received during the reporting period, and no complaints were outstanding at the beginning of the period, the *firm* may submit a NIL RETURN by ticking the relevant box on the front of the form. Sections 1, 3, 4 ~~and 9, 9~~ and 10 must still be completed.

...

Delete Section 9. After section 8, insert:

## Section 9 – Complaints management

*Firms* should indicate the number of complaints that they are aware have been referred to, and accepted by, the *Financial Ombudsman Service*.

## Section 10 – Declaration

If you have any questions or need help with this return, please approach your usual supervisory contact at the *FSA*.

...

## DISP Schedule 2 – Notification requirements

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
<b>DISP 1.1.10R</b>	<b>End of exemption</b>	<b>Confirmation that the conditions in <i>DISP</i> 1.1.7R no longer apply</b>	<b>Conditions in <i>DISP</i> 1.1.7R no longer apply</b>	<b>As soon as reasonably practicable</b>
<b>DISP 1.5.4R</b>	<b>Complaints report</b>	<b>Details</b>	<b><del>– 30 September</del> <del>– 31 March</del> <b>each year</b> <b><u>- 6 months preceding the accounting reference date</u></b> <b><u>- accounting reference date</u></b></b>	<b><del>One month</del> <b><u>30 business days</u></b></b>
<b>DISP 1.5.11R</b>	<b>Single contact point</b>	<b>Details</b>	<b>At the time of authorisation or on subsequent change</b>	<b>Not specified</b>
...				

## Annex C

### Amendments to the Credit Unions sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text. Where the provisions of an entire section are replaced, the section is indicated and the new text is not underlined nor the deleted text struck through.

17.6.3 R *A credit union* must provide the *FSA*, once a year, with a report in the format set out in *CRED 17 Ann 1R* (Credit union complaints return) which contains (for the relevant reporting period) information about:

- (1) the total number of complaints received by the *credit union* (except those referred to in *CRED 17.4.1R*) broken down according to the categories and in respect of each of the generic product types described in *CRED 17 Ann 1R* (Credit union complaints return) which are relevant to the *credit union*;
- (2) the number of complaints closed by the *credit union*:
  - (a) within eight weeks of receipt; and
  - (b) more than eight weeks after receipt; -
- ~~(3) the total number of complaints outstanding at the end of the reporting period; and~~
- ~~(4) the single contact within the *credit union* for complainants.~~
- (3) the total number of complaints:
  - (a) upheld by the *credit union* in the reporting period;
  - (b) that the *credit union* knows have been referred to, and accepted by, the *FOS* during the reporting period; and
  - (c) outstanding at the end of the reporting period;
- (4) the total amount of redress paid in respect of complaints during the reporting period; and
- (5) the single contact within the *credit union* for complainants.

17.6.4 G For the purpose of *CRED 17.6.3R*, and upon completing the return, the *credit union* should note that:

- (1) Where a complaint could fall into more than one category, the complaint should be recorded in the category which the *credit union* considers to form the main part of the complaint.
- (2) Where a complaint has been upheld under CRED 17.6.3R (3)(a), a *credit union* should report any complaints to which it has given a final response which accepts the complaint and, where appropriate, offers redress, even if the redress offered is disputed by the complainant. Where a complaint is upheld in part, the *credit union* should treat the whole complaint as upheld for reporting purposes. Where a *credit union* rejects a complaint, yet chooses to make an ex-gratia payment to the complainant, the complaint should be recorded as rejected.
- (3) Where a *credit union* reports on the amount of redress paid under CRED 17.6.3R (4), redress should be interpreted to include any amount paid, or cost borne, by the *credit union*, where a cash value can be readily identified, and should include:
  - (a) amounts paid for distress and inconvenience;
  - (b) a free transfer out to another provider which transfer would normally be paid for;
  - (c) ex-gratia payments and goodwill gestures;
  - (d) interest on delayed settlements;
  - (e) waiver of an excess on an insurance policy; and
  - (f) payments to put the consumer back into the position the consumer should have been in had the act or omission not occurred.
- (4) Where a *credit union* reports on the amount of redress paid under CRED 17.6.3R (4), such redress would not, however, include repayments or refunds of premiums which had been taken in error (for example where a *credit union* had been taking, by direct debit, twice the actual premium amount due under a policy). The refund of the overcharge would not count as redress.



CRED 17 Annex 1 R

Credit Union Complaints Return

Section 5 and section 6 of the credit union complaints return are replaced as follows:

Private individual complaints

Section 5

	Overcharging	Delays	Other admin	Misleading advice	Failure to carry out instructions	Poor customer service	Misleading advertising	Disputes over sums/amounts	Switching/churning	Breach of contract	Arrears handling	Other
FSAVC												
Personal Pension												
Stakeholder Pension												
Mortgage Endowment												
Other Endowment												
Whole of Life												
Permanent Health												
Term Assurance												
PEP/ISA												
Cash Deposit ISA												
Investment Trust												
Unit Trust/OEIC												
Investment Bond												
Share/Derivative												
Other Regulated Investments												
Current Account												
Deposit/Savings												
Credit Card												
Lifetime Mortgage												
Flexible Mortgage												
Impaired Credit Mortgage												
Self Cert Mortgage												
Other Regulated Mortgage												
Other unregulated loan secured on land												
Other loans												
Standard Annuity												
Investment based Annuity												
Income Withdrawal Product												
Income Protection												
Long Term Care												
Private Medical Insurance												
Critical Illness												
Motor												
Property												
Other GI/Pure protection												
Other												
Total												

If no private individual complaints were received during the period, tick the box and go to Section 6

	Overcharging	Delays	Other admin	Misleading advice	Failure to carry out instructions	Poor customer service	Misleading advertising	Disputes over sums/amounts	Switching/churning	Breach of contract	Arrears handling	Other
FSAVC												
Personal Pension												
Stakeholder Pension												
Mortgage Endowment												
Other Endowment												
Whole of Life												
Permanent Health												
Term Assurance												
PEP/ISA												
Cash Deposit ISA												
Investment Trust												
Unit Trust/OEIC												
Investment Bond												
Share/Derivative												
Other Regulated Investments												
Current Account												
Deposit/Savings												
Credit Card												
Lifetime Mortgage												
Flexible Mortgage												
Impaired Credit Mortgage												
Self Cert Mortgage												
Other Regulated Mortgage												
Other unregulated loan secured on land												
Other loans												
Standard Annuity												
Investment based Annuity												
Income Withdrawal Product												
Income Protection												
Long Term Care												
Private Medical Insurance												
Critical Illness												
Motor												
Property												
Other GI/Pure protection												
Other												
Total												

If no small business complaints were received during the period, tick the box and go to Section 7

...

Delete Section 9 of the credit union complaints return. After section 8, insert:

Complaints management Section 9

9.01 Number of complaints upheld by the *credit union* in the period

9.02 Total amount of redress paid to *consumers* in the period

9.03 Number of complaints referred to, and accepted by, the *FOS* in the period

Declaration and signature Section 10

Knowingly or recklessly giving the *FSA* information which is false or misleading in a material particular may be a criminal offence (section 398 of the Financial Services and Markets Act 2000) and a breach of regulatory requirements.

In signing this form, the *credit union* acknowledges that the data supplied may be used by the *FSA* in a variety of different ways (including making it publicly available) in support of its principal functions and statutory objectives as provided for under the Financial Services and Markets Act 2000.

I confirm that I have read the notes and that the information given in this return about complaints received by the *credit union* named at Section 1.02 is accurate and complete to the best of my knowledge and belief.

10.01 Name of *person* completing on behalf of the *credit union*

10.02 Job title

10.03 Signature

10.04 Date

...

Notes on the completion of this return

...

Section 2 – Nil Returns

If no complaints (except those referred to in *CRED* 17.4.1R) have been received during the reporting period, and no complaints were outstanding at the beginning of the period, the *credit union* may submit a NIL RETURN by ticking the relevant box on the front of the form. Sections 1, 3, 4 ~~and 9~~, 9 and 10 must still be completed.

...

Delete Section 9. After Section 8, insert:

Section 9 – Complaints management

*Credit unions* should indicate the number of complaints that they are aware have been referred to, and accepted by, the *Financial Ombudsman Service*.

#### Section 10 – Declaration & signature

The declaration must be signed by an appropriate individual for the *credit union*.

...

## Annex D

### Amendments to the Glossary

In this Annex all text is new and is not underlined.

Insert the following new definitions in the appropriate alphabetical position:

<i>CIS administrator</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a person responsible for the administrative functions of a collective investment scheme.
<i>CIS trustee</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a person holding the property of a collective investment scheme on trust for the participants in the collective investment scheme.
<i>composite insurer</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) an insurer with permission to effect or carry out both long-term insurance contracts and general insurance.
<i>discretionary investment manager</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a person who, acting only on behalf of a client, manages designated investments in an account or portfolio on a discretionary basis under the terms of a discretionary management agreement.
<i>firm type</i>	one of a list of <i>firm types</i> set out in SUP 16 Annex 17R used for the purposes of checking and correcting standing data under SUP 16.10.4R.
<i>non-discretionary investment manager</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a person who, acting only on behalf of a client, manages designated investments in an account or portfolio on a non-discretionary basis under the terms of a non-discretionary management agreement.
<i>own account trading firm</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a firm that only deals or arranges deals in securities or contractually based investments for its own benefit, or for the benefit of an associate.
<i>standing data</i>	the information relating to a firm held by the FSA on the matters set out in SUP 16 Annex 16R.
<i>wholesale only bank</i>	(in relation to <i>firm type</i> in SUP 16.10 (Confirmation of standing data)) a bank with permission to accept deposits from wholesale depositors only.

**COMPLAINTS SOURCEBOOK  
(FINANCIAL OMBUDSMAN SERVICE GENERAL LEVY 2004/2005)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance); and
  - (4) section 234 (Funding).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2004.

**Amendment of the Complaints sourcebook**

- D. The Complaints sourcebook (DISP) is amended:
- (1) in accordance with Annex A to this instrument; and
  - (2) by inserting, as DISP 5 Ann 1R (2004/5), the provisions in Annex B to this instrument.

**Citation**

- E. This instrument may be cited as the Complaints Sourcebook (Financial Ombudsman Service General Levy 2004/2005) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendments to the Complaints sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

- 5.2.1 G The purpose of this chapter is to set out the requirements on *firms* to pay annual fees (through a *general levy* and *supplementary levy* invoiced and collected by the FSA on behalf of FOS Ltd) and case fees ~~to (invoiced and collected directly by FOS Ltd)~~ in order to fund the operation of the *Financial Ombudsman Service*.
- ...
- 5.4.6 R A *firm* must pay to ~~FOS Ltd~~ the FSA a *general levy* towards the costs of operating the *Compulsory Jurisdiction* of the *Financial Ombudsman Service*.
- 5.4.7 G Under the *standard terms*, *VJ Participants* will be required to pay to FOS Ltd an amount calculated on a similar basis towards the costs of operating the *Voluntary Jurisdiction* of the *Financial Ombudsman Service*. FOS Ltd will be responsible for invoicing and collecting this amount.
- ...
- 5.7.5 R A *firm* must pay to ~~FOS Ltd~~ the FSA a *supplementary levy* towards the costs of establishing the *Financial Ombudsman Service*.
- ...
- 5.8.1 R A *firm* must pay annually to the FSA the *general levy* and any *supplementary levy* to which it is subject ~~to FOS Ltd either:~~
- (1) ~~annually~~, on or before the later of 1 April and 30 calendar days after the date when the invoice is issued by ~~FOS Ltd~~, or the FSA.
- (2) ~~provided the amount payable exceeds the minimum levy, quarterly, at the beginning of each quarter, by direct debit agreement.~~
- ...
- 5.8.5 G ~~FOS Ltd~~ The FSA will issue invoices for the *general levy*, and any supplementary levy; FOS Ltd will issue invoices for standard case fees and special case fees. ~~The Each~~ Each invoice will be payable within 30 calendar days. Invoices will be sent to the *firm's* Compliance Officer at the principal place of business in the *United Kingdom* last notified to the *FSA*. A firm which is liable to pay under DISP 5.8.1R may do so by direct debit agreement.

...

5.8.7 G If a *firm* (or *unauthorised person*) subject to the *Compulsory Jurisdiction* fails to make payment under this chapter of standard or special case fees, after expiry of the 30 *day* period, *FOS Ltd* may:

(1) take steps to recover any money owed (including interest);

(2) refer the matter to the *FSA* so that the *FSA* may take whatever disciplinary action it considers necessary.

5.8.7A G If a *firm* (or *unauthorised person*) fails to make payment under this chapter of the *general levy* and *any supplementary levy* to which it is subject, after the expiry of the 30 *day* period, the *FSA* may take whatever action it considers appropriate including steps to recover any money owed (with interest) and commencing disciplinary proceedings.



## Annex B

### Amendments to the Complaints sourcebook (DISP)

The following Annex is inserted as DISP 5 Ann 1R.

DISP 5 Ann 1R: Annual Fees Payable in Relation to 2004/05

Introduction: annual budget

1 The *annual budget* for 2004/05 approved by the FSA is £45m.

Part 1: General levy and supplementary levy

2 The total amount expected to be raised through the *general levy* in 2004/05 will be £12.5m.

Part 2: Fee tariffs for general levy and supplementary levy

3 No *establishment costs* will be raised in 2004/05 by the *supplementary levy*.

Table: fee tariffs for industry blocks

Industry block	Tariff base	General levy payable by firm
1-Deposit acceptors, <i>mortgage lenders</i> and <i>administrators</i> (excluding <i>firms</i> in block 14)	Number of accounts relevant to the activities in <i>DISP</i> 2.6.1R	£0.0069 per relevant account, subject to a minimum levy of £200
2- <i>Firms</i> that undertake insurance activities, subject to prudential regulation only (excluding <i>firms</i> in blocks 13 & 15)	Relevant annual gross premium income	£0.081 per £1,000 of relevant annual gross premium income, subject to a minimum levy of £200
3-The <i>Society</i> (of Lloyd's)	To be allocated by the <i>Society</i>	£47,266 to be allocated by the <i>Society</i>

4-Firms that undertake insurance activities, subject to both prudential and conduct of business regulation ( <i>long-term insurers</i> )  (excluding <i>firms</i> in block 15)	Relevant adjusted annual gross premium income	£0.093 per £1,000 of relevant adjusted annual gross premium income, subject to a minimum levy of £100
5-Fund managers (including those holding <i>client money/assets</i> and not holding <i>client money/assets</i> )	Relevant funds under management	£0.00255 per £1,000 of relevant funds under management, subject to a minimum levy of £100
6-Operators, trustees and depositaries of collective investment schemes	Flat fee	Levy of £75
7-Dealers as principal	Flat fee	Levy of £75
8-Advisory arrangers, dealers or brokers holding and controlling <i>client money</i> and/or assets	Number of relevant <i>approved persons</i> ( <i>controlled functions</i> 21, 22, 24, 25, 26)	£65 per relevant <i>approved person</i> ( <i>controlled functions</i> 21, 22, 24, 25, 26), subject to a minimum levy of £75
9-Advisory arrangers, dealers or brokers not holding and controlling <i>client money</i> and/or assets	Number of relevant <i>approved persons</i> ( <i>controlled functions</i> 21, 22, 24, 25, 26)	£30 per relevant <i>approved person</i> ( <i>controlled functions</i> 21, 22, 24, 25, 26), subject to a minimum levy of £75
10-Corporate finance advisers	Flat fee	Levy of £75
11-	N/A for 2004/05	
12-	N/A for 2004/05	
13-Cash plan health providers	Flat fee	Levy of £50
14-Credit unions	Flat fee	Levy of £50
15-Friendly societies whose tax-exempt business represents 95% or more of their total relevant business	Flat fee	Levy of £50

- 5 The *industry blocks* in the table are based on the equivalent activity groups set out in Part 1 of *SUP 20 Ann 1R*.
- 6 Where the tariff base in the table is defined in similar terms as that for the equivalent activity group in Part 2 of *SUP 20 Ann 1R*, it must be calculated in the same way as that tariff base - taking into account only the *firm's relevant business*.

## COMPENSATION SOURCEBOOK (FUNDING) INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance);
  - (4) section 213 (The compensation scheme);
  - (5) section 214 (General); and
  - (6) section 223 (Management expenses).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

### Commencement

- C. This instrument comes into force on 1 April 2004.

### Amendments to the Compensation sourcebook

- D. The Compensation sourcebook is amended in accordance with Annex A to this instrument.

### Amendments to the Glossary

- E. The Glossary is amended in accordance with Annex B to this instrument.

### Citation

- F. This instrument may be cited as the Compensation Sourcebook (Funding) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text:

13.6.5 R      *A participant firm* ~~(except one exempt under COMP 13.3)~~ must pay to the FSCS a share of each *compensation costs levy* unless either the *firm* is exempt under COMP 13.3 (Exemption) or the FSCS has chosen to exercise its discretion under COMP 13.4.20R in respect of that *firm*.

...

COMP 13 Ann 1R: Management Expenses Levy Limit

- 1      This table belongs to COMP 13.5.2R
- 2      Table

Period	Limit on total of all management expenses levies attributable to that period (£)
1 December 2001 to 31 March 2002	£4,209,000
1 April 2002 to 31 March 2003	£13,228,000
1 April 2003 to 31 March 2004	£13,319,000
<u>1 April 2004 to 31 March 2005</u>	<u>£12,548,000</u>

## Annex B

### Amendments to the Glossary

In this Annex underlining indicates new text and striking through indicates deleted text. Where a new definition is inserted it is not underlined.

Insert the following definition in the appropriate alphabetical position:

*occupational pension fund management business* (in *COMP*) the business of carrying on:  
(1) *pension fund management*; or  
(2) (other than in connection with a *personal pension scheme*) pension fund management, written as *linked long term business*, for an *occupational pension scheme* or for an institution falling within article 2 of the Council Directive of 3 June 2003 on the activities and supervision of institutions for occupational retirement provision (No 2003/41/EC) but only to the extent that:  
(a) there is no transfer to the *participant firm* of:  
(i) investment, market, or credit risk;  
(ii) mortality or expense risk prior to any annuity being effected; and  
(b) any annuity options provide for the *participant firm* to change the annuity rates without prior notice.

Amend the following definition as shown:

*relevant net premium income* (1) (in relation to business which is not *occupational pension fund management business*) the premium income in respect of *protected contracts of insurance* of ~~the~~ a firm; or

(2) (in relation to *occupational pension fund management business*) the remuneration retained by a firm in relation to its carrying on *occupational pension fund management business*;

in the year preceding that in which the date for submission of the information under *COMP* ~~13.6.9R~~ 13.6.11R falls, net of any relevant rebates or refunds.

**NEW COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) 138 (General rule-making power);
    - (b) 140 (Restriction on managers of authorised unit trust schemes);
    - (c) 145 (Financial promotion rules);
    - (d) 156 (General supplementary powers);
    - (e) 157 (Guidance);
    - (f) 242 (Applications for authorisation of unit trust schemes);
    - (g) 247 (Trust scheme rules);
    - (h) 248 (Scheme particulars rules);
    - (i) 270 (Schemes authorised in designated countries or territories);
    - (j) 274 (Applications for recognition of individual schemes);
    - (k) 278 (Rules as to scheme particulars);
    - (l) 340 (Appointment); and
    - (m) paragraph 17(1) of Schedule 1 (Fees);
  - (2) regulations 6 (FSA rules) and 12 (Applications for authorisation) of the Open-Ended Investment Companies Regulations (SI 2001/1228); and
  - (3) regulation 1(6) (Citation, commencement and interpretation) of the Financial Services and Markets Act 2000 (Service of Notices) Regulations 2001 (SI 2000/1420).
- B. The provisions of or under the Act relevant to the rules and listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2004.

**Making the New Collective Investment Schemes sourcebook (COLL)**

- D. The Financial Services Authority makes the rules, gives the guidance and makes the directions and requirements in the Annex to this instrument.

### **Revocation of previous instrument**

- E. The Collective Investment Schemes Sourcebook Instrument 2001 and CIS are revoked with effect from 12 February 2007.

### **Revocation of CIS references**

- F. References in the Handbook to CIS or any provision in CIS are deleted from 12 February 2007.

### **Citation**

- G. This instrument may be cited as the New Collective Investment Schemes Sourcebook Instrument 2004.
- H. The sourcebook in the Annex to this instrument (including its Schedules) may be cited as the New Collective Investment Schemes sourcebook (or COLL) until 12 February 2007 and thereafter be cited as the Collective Investment Schemes sourcebook (or COLL).

By order of the Board  
18 March 2004



## Collective Investment Schemes

### COLL Sourcebook - Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
<b>Extra time provisions</b>					
<b>Existing schemes electing to comply with COLL</b>					
1	Each and every <i>rule</i> in <i>COLL</i>	R	The <i>rules</i> in <i>COLL</i> do not apply to any relevant party in relation to an <i>authorised fund</i> in respect of which an application for an <i>authorisation order</i> was received by the <i>FSA</i> before 1 April 2004, unless the <i>authorised fund manager</i> of the <i>scheme</i> has exercised its right of election on behalf of the <i>scheme</i> to comply with <i>COLL</i> , instead of <i>CIS</i> , in accordance with <i>CIS 1.1.1A R (Right to elect to comply with COLL)</i> .	From 1 April 2004 to 12 February 2007	1 April 2004
2	Each and every <i>rule</i> in <i>COLL</i>	G	The effect of transitional provision 1 is that the default position for the relevant parties of existing <i>authorised funds</i> (by which is meant <i>authorised funds</i> in respect of which the application for the <i>authorisation order</i> was received by the <i>FSA</i> before 1 April 2004) is that <i>CIS</i>		

			continues to apply until 12 February 2007 <u>unless</u> the relevant <i>authorised fund manager</i> has exercised its right of election in accordance with <i>CIS</i> 1.1.1A R to comply with <i>COLL</i> , instead of <i>CIS</i> .		
<b>New schemes electing to comply with CIS</b>					
<b>3</b>	<b>Each and every rule in <i>COLL</i></b>	<b>R</b>	<b>(1) The <i>authorised fund manager</i> of an <i>authorised fund</i> whose <i>authorisation order</i> application was received by the <i>FSA</i> on or after 1 April 2004 may, with the consent of each of the other relevant parties:</b>	<b>From 1 April 2004 to 12 February 2007</b>	<b>1 April 2004</b>
			<b>(a) elect to comply with <i>CIS</i>; and</b>		
			<b>(b) subsequently revoke such an election and elect to comply with <i>COLL</i>, in which case no further election is permitted for that <i>fund</i>.</b>		
			<b>(2) An election or revocation in (1) does not take effect unless the <i>authorised fund manager</i> has notified the <i>FSA</i> in writing of:</b>		

			(a) the election or revocation; and		
			(b) the date from which it is to take effect.		
			(3) While an election in (1)(a) remains in effect, <i>COLL</i> does not apply to any relevant party in respect of the <i>authorised fund</i> . Instead, each relevant party must comply with <i>CIS</i> .		
			(4) The right of election referred to in (1) only applies in relation to an <i>authorised fund</i> which is a <i>UCITS scheme</i> , a <i>money market scheme</i> , a <i>futures and options scheme</i> , a <i>geared futures and options scheme</i> , a <i>property scheme</i> , a <i>feeder fund</i> or a <i>funds of funds scheme</i> .		
			(5) The <i>authorised fund manager</i> must make a record of any election or revocation under (1), and retain it for a period of six years from the date it takes effect.		
4	Each and every <i>rule</i> in <i>COLL</i>	G	(1) It is not necessary for the <i>schemes</i> referred to in transitional provision 3(4) initially to have complied with <i>COLL</i> , before an election is made on its behalf under transitional provision 3(1)(a) to comply with <i>CIS</i> .		

			(2) Note that while the <i>FSA's</i> permission is not required for an election under paragraph 3(1)(a) or a revised election under paragraph 3(1)(b), changes to the relevant <i>instrument constituting the scheme</i> and <i>prospectus</i> to give effect to such a revised election will require the <i>FSA's</i> written permission, as explained in <i>CIS</i> 16.1.11G (Notification of proposed changes to ICVCs) and <i>CIS</i> 16.1.12G (Notification of proposed changes to AUTs).		
<b>UCITS business restrictions</b>					
5	<b>COLL 6.9.9R (2) to (6) (Restrictions of business for UCITS management companies)</b>	<b>R</b>	<b>A UCITS management company must not carry on any of the activities specified in COLL 6.9.9R (2) to (6) (inclusive) unless it is a UCITS investment firm:</b>	<b>From 1 April 2004 to 12 February 2007</b>	<b>1 April 2004</b>
			(a) <b>whose permission to carry on any such activity was given before 13 February 2004; or</b>  (b) <b>which complies with Chapter 7 of IPRU (INV).</b>		
6	<b>COLL 6.9.9R (2) to (6) (Restrictions of business for UCITS management companies)</b>	<b>G</b>	<b>A UK firm will not be able to act as such and exercise an EEA right under the UCITS Directive unless it complies with Chapter 7 of IPRU(INV).</b>		

<b>Committees and delegation</b>					
7	<b>COLL 6.6.15R(2), (4) and (5) (Committees and delegation)</b>	R	<p>(1) Subject to (2), a <i>UCITS management company</i> which became authorised before 13 February 2004 will not contravene <i>COLL 6.6.15R (2), (4) and (5) (Committees and delegation)</i> to the extent that it complies with <i>CIS 7.6.1 R (2), (4) and (5)</i> and <i>CIS 7.10.4 R (1), (5) and (6)</i> as they applied before 12 February 2004.</p> <p>(2) Paragraph (1) does not apply in relation to any <i>UK firm</i> which exercises an <i>EEA right</i> under the <i>UCITS Directive</i>.</p>	From 1 April 2004 to 12 February 2007	1 April 2004
<b>Existing dual-priced AUTs: dealing and valuation</b>					
8	<b>COLL 6.2 (dealing); COLL 6.3 (Valuation and pricing); COLL 5.2.5 (Valuation) and COLL 4.2.5R 16 (Table: contents of the prospectus)</b>	R	(1) Subject to (2), the <i>manager</i> of a <i>dual-priced AUT</i> which has exercised its entitlement under <i>CIS 1.1.1A R</i> to comply with <i>COLL</i> instead of <i>CIS</i> , will not contravene any of the provisions in column (2) to the extent that it complies with <i>CIS 15 (Dual-pricing and dealing)</i> , <i>CIS 5.2.5R (Valuation)</i> and <i>CIS 5A.2.5R (Valuation)</i> (and references in <i>COLL</i> to the <i>rules</i> in column (2) are to be construed accordingly).	From 1 April 2004 until 12 February 2007	1 April 2004

			<p>(2) Where the <i>rules</i> in <b>COLL 6.2 (Dealing), COLL 6.3 (Valuation and pricing) and COLL 5.2.5 (Valuation)</b> conflict with the relevant requirements of <b>CIS 15 (Dual-pricing and dealing), CIS 5.2.5R (Valuation) and CIS 5A.2.5R (Valuation)</b>, the <i>manager</i> must proceed on the basis that the former <i>rules</i> (<b>COLL</b>) override the latter (<b>CIS</b>) unless compliance with a relevant <i>rule</i> in <b>COLL 6.2 or COLL 6.3 or COLL 5.2.5R</b> would not be possible.</p>		
9	<p><b>COLL 6.2 (dealing); COLL 6.3 (Valuation and pricing); COLL 5.2.5 (Valuation) and COLL 4.2.5R 16 (Table: contents of the prospectus)</b></p>	G	<p>(1) A <i>dual-priced AUT</i> values on a basis that results in different <i>issue</i> and <i>cancellation prices</i> compared to a single-priced <i>scheme</i>. Furthermore, the <i>manager</i> sets <i>sale</i> and <i>redemption prices</i> within the pricing envelope of the <i>cancellation price</i> and <i>issue price</i> together with the <i>preliminary charge</i>. Transitional provision 8 allows such a system to continue to operate.</p> <p>(2) However, transitional provision 8 also requires the <b>COLL</b> provisions to override the applicable <b>CIS</b> provisions where appropriate, that is in circumstances where there is a conflict between them. So, for example, publishing <i>prices</i> should comply</p>		

			with <i>COLL</i> 6.3.11R (Publication of prices) rather than <i>CIS</i> 15.4.14R. Where complying with the relevant <i>COLL rules</i> would not be practicable or not feasible for some reason, the <i>manager</i> is advised to contact the <i>FSA</i> .		
10	COLL 10.3.1R	R	<p>(1) If the <i>authorised fund manager</i> of a <i>scheme</i> notifies the <i>FSA</i> under section 251 of the <i>Act</i> or regulation 21 of the <i>OEIC Regulations</i> in relation to a proposal to alter a <i>scheme</i> under transitional provision 1 or transitional provision 3(1)(b), the <i>authorised fund manager</i> must pay to the <i>FSA</i> a fee of £400 for each individual <i>scheme</i> and a fee of £800 for each <i>umbrella scheme</i>.</p> <p>(2) A fee payable under this provision must be paid by bankers draft, cheque or other payable order when the notification is made.</p>	1 April 2004 to 12 February 2007	1 April 2004
<b>Definition of relevant party</b>					
11	COLL	R	For the purposes of these transitional <i>rules</i> , a "relevant party" in relation to:	From 1 April 2004 until 12 February 2007	1 April 2004
			(1) any <i>AUT</i> , is its <i>manager</i> and <i>trustee</i> ; and		
			(2) any <i>ICVC</i> , is:		
			(a) the <i>ICVC</i> ;		

			<b>(b) its <i>ACD</i>;</b> <b>(c) any other <i>directors</i> of the <i>ICVC</i>; and</b> <b>(d) its <i>depository</i>.</b>		



# **1 Introduction**

## **1.1 Applications and purpose**

### **Application**

- 1.1.1 G (1) This sourcebook, except for *COLL 9* (Recognised schemes), applies to:
- (a) *investment companies with variable capital (ICVCs)*;
  - (b) *ACDs, other directors and depositaries of ICVCs*; and
  - (c) *managers and trustees of authorised unit trust schemes (AUTs)*.
- (2) *COLL 9* applies to *operators of schemes* that are *recognised schemes* and to those seeking to secure recognised status for such *schemes*.

### **Purpose**

- 1.1.2 G (1) The general purpose of this sourcebook is to contribute to the *FSA* meeting its *regulatory objective* of the protection of *consumers*. It provides a regime of product regulation for *authorised funds*, which sets appropriate standards of protection for investors by specifying a number of features of those products and how they are to be operated.
- (2) In addition, this sourcebook implements part of the requirements of the *UCITS Directive* to meet community obligations relevant to *authorised funds*, with other requirements implemented in other parts of the *Handbook*.

### **The Collective Investment Schemes Information Guide**

- 1.1.3 G The Collective Investment Schemes Information Guide *COLLG* provides some general background material on the regulatory structure surrounding *scheme* regulation in the *UK*.

## 1.2 **Types of authorised fund**

### **Types of authorised fund**

1.2.1 R An application for an *authorisation order* must propose that the *scheme* be one of the following types:

- (1) a *UCITS scheme*;
- (2) a *non-UCITS retail scheme*; or
- (3) a *qualified investor scheme*.

### **Types of authorised fund - explanation**

- 1.2.2 G
- (1) *UCITS schemes* have to comply with the conditions necessary in order to enjoy the rights available under the *UCITS Directive*. Such *schemes* must in particular comply with:
    - (a) *COLL 3.2.8R* (UCITS obligations); and
    - (b) the investment and borrowing powers rules for *UCITS schemes* set out in *COLL 5.2 to 5.5*.
  - (2) *Non-UCITS retail schemes* are schemes that do not comply with all the conditions set out in the *UCITS Directive*. Such *schemes* could become *UCITS schemes* provided they are changed, so as to comply with the conditions set out in the *UCITS Directive*.
  - (3) *Qualified investor schemes* may only be promoted to professional investors on the same terms as *unregulated collective investment schemes*. Such *schemes* could change to become *non-UCITS retail schemes* or *UCITS schemes*.
  - (4) The changes referred to in (2) and (3) require approval by the *FSA* and further information on that process is provided in *COLLG 3.1.5G* (Notification of changes to unit trusts (section 251)) and *COLLG 4.1.3G* (Notification of changes to ICVCs (Regulation 21)).

## **2 Authorised fund applications**

### **2.1 Authorised fund applications**

#### **Application**

2.1.1 R This chapter applies to any *person* seeking to arrange for the authorisation of a *scheme*.

#### **Purpose**

2.1.2 G This chapter helps in achieving the *regulatory objective* of protecting *consumers* by ensuring that any application for authorisation of a fund meets certain standards.

#### **Explanation**

2.1.3 G (1) This chapter sets out the requirements that a *person* must follow in applying for an *authorisation order* for a *scheme* under regulation 12 of the *OEIC Regulations* (Applications for authorisation) or section 242 of the *Act* (Applications for authorisation of unit trust schemes).

(2) *COLLG 3* (The FSA's responsibilities under the Act) and *COLLG 4* (The FSA's responsibilities under the OEIC Regulations) provide more information on what the *Act* and the *OEIC Regulations* require in relation to ongoing notifications to the *FSA*.

#### **Specific requirements on application**

2.1.4 D An application for an *authorisation order* in respect of an *authorised fund* must be:

- (1) in writing in the manner directed and contain the information required in the application form available from the *FSA*;
- (2) addressed for the attention of a member of *FSA* staff responsible for *collective investment scheme* authorisation matters; and
- (3) delivered to the *FSA's* address by one of the following methods:
  - (a) posting; or
  - (b) leaving it at the *FSA's* address and obtaining a time-stamped receipt; or
  - (c) delivery by hand to a member of *FSA* staff responsible for *collective investment scheme* authorisation matters.

### **3 Constitution**

#### **3.1 Introduction**

##### **Application**

3.1.1 R This chapter applies to:

- (1) an *authorised fund manager* of an *AUT* or an *ICVC*;
- (2) any other *director* of an *ICVC*;
- (3) a *depository* of an *AUT* or an *ICVC*; and
- (4) an *ICVC*,

where the *AUT* or *ICVC* is a *UCITS scheme* or a *non-UCITS retail scheme*.

##### **Purpose**

3.1.2 G This chapter assists in achieving the *regulatory objective* of protecting *consumers*. In particular:

- (1) *COLL 3.2* (The instrument constituting the scheme) contains requirements about provisions which must be included in the *instrument constituting the scheme* to give a similar degree of protection for investors in an *ICVC* or in an *AUT*; and
- (2) *COLL 3.3* (Units) provides *rules* and *guidance* which deal with the *classes* of *units* to ensure that investors in each *class* are treated equally.

## 3.2 The instrument constituting the scheme

### Application

3.2.1 R This section applies to:

- (1) an *authorised fund manager* of an *AUT* or *ICVC*;
- (2) any other *director* of an *ICVC*;
- (3) a *depository* of an *AUT* or an *ICVC*; and
- (4) an *ICVC*,

except *COLL 3.2.8R* (UCITS obligations), which applies only to an *ICVC* or to the *manager* of an *AUT* where the *ICVC* or *AUT* is a *UCITS scheme*.

### Relationship between the instrument constituting the scheme and the rules

- 3.2.2 R (1) The *instrument constituting the scheme* must not contain any provision that:
- (a) conflicts with any *rule* in this sourcebook;
  - (b) prevents *units* in the *scheme* being marketed in the *United Kingdom*; or
  - (c) is unfairly prejudicial to the interests of *unitholders* generally or to the *unitholders* of any *class* of *units*.
- (2) Any power conferred by the *rules* on the *ICVC*, the *authorised fund manager*, any other *director* of the *ICVC*, or the *depository*, whether in a sole or joint capacity, is subject to any restriction in the *instrument constituting the scheme*.

### The trust deed for AUTs

- 3.2.3 R An *AUT* must be constituted by a *trust deed* made between the *manager* and the *trustee*.

### Matters which must be included in the instrument constituting the scheme

- 3.2.4 R The statements and provisions required by *COLL 3.2.6R* (Table: contents of the instrument constituting the scheme) must be included in the *instrument constituting the scheme*, where appropriate.

### The instrument constituting the scheme: OEIC Regulations and trust law requirements

- 3.2.5 G (1) Several of the matters set out in *COLL 3.2.6R* are required to be included in the *instrument constituting the scheme* under the *OEIC Regulations* or as a consequence of relevant trust law. In addition, further statements are required if the *scheme* or the *authorised fund manager* are to take advantage of the powers under the *rules* in this sourcebook.
- (2) Additional matters which are not contained in *COLL 3.2.6R* may be required to be included in the *instrument constituting the scheme* in order to comply with the *OEIC Regulations*, (particularly Schedule 2 – Instrument of Incorporation) and for the purposes of making the *scheme* eligible under relevant tax, pensions, or charities legislation.

**Table: contents of the instrument constituting the scheme**

- 3.2.6 R This table belongs to *COLL 3.2.4R* (Matters which must be included in the instrument constituting the scheme)

**Name of scheme**

- 1 A statement of:
- (1) the name of the *authorised fund*; and
- (2) whether the *authorised fund* is a *UCITS scheme* or a *non-UCITS retail scheme*.

**Investment powers in eligible markets**

- 2 A statement that, subject to any restriction in the *rules* in this sourcebook or the *instrument constituting the scheme*, the *scheme* has the power to invest in any *eligible securities* market or *deal* on any *eligible derivatives* market to the extent that power to do so is conferred by *COLL 5* (Investment and borrowing powers).

**Unitholder's liability to pay**

- 3 A provision that a *unitholder* is not liable to make any further payment after he has paid the *price* of his *units* and that no further liability can be imposed on him in respect of the *units* which he holds.

**Base currency**

- 4 A statement of the *base currency* of the *scheme*.

### **Valuation and pricing**

- 5 A statement setting out the basis for the valuation and pricing of the *scheme*.

### **Duration of the scheme**

- 6 If the *scheme* is to be wound up after a particular period expires, a statement to that effect.

### **Object of the scheme**

- 7 A statement:
- (1) as to the object of the *scheme*, in particular the types of *investments* and assets in which it and each *sub-fund* (where applicable) may invest; and
  - (2) that the object of the *scheme* is to invest in property of that kind with the aim of spreading investment risk and giving *unitholders* the benefits of the results of the management of that property.

### **Government and public securities: investment in one issuer**

- 8 Where relevant, for a *UCITS scheme*, a statement in accordance with *COLL 5.2.12R(4)* (Spread: government and public securities) as to the individual states or bodies in which over 35% of the value of the *scheme* may be invested in *government and public securities*.

### **Classes of unit**

- 9 A statement:
- (1) specifying the *classes* of *unit* that may be issued, and for a *scheme* which is an *umbrella*, the *classes* that may be issued in respect of each *sub-fund*; and
  - (2) if the rights of any *class* of *unit* differ, a statement describing those differences in relation to the differing *classes*.

### **Authorised fund manager's charges and expenses**

- 10 A statement setting out the basis on which the *authorised fund manager* may make a charge and recover expenses out of the *scheme property*.

### **Issue or cancellation directly through the ICVC or trustee**

- 11 Where relevant, a statement authorising the *issue* or *cancellation* of *units* to take place through the *ICVC* or *trustee* directly.

**In specie issue and cancellation**

- 12 Where relevant, a statement authorising payment for the *issue* or *cancellation* of *units* to be made by the transfer of assets other than cash.

**Restrictions on sale and redemption**

- 13 Where relevant, the restrictions which will apply in relation to the *sale* and *redemption* of *units* under *COLL* 6.2.16R (Sale and redemption).

**Voting at meetings**

- 14 The manner in which votes may be given at a meeting of *unitholders* under *COLL* 4.4.8R (Voting rights).

**Certificates**

- 15 A statement:
- (1) authorising the issue of *bearer certificates* if any, and how such *holders* are to identify themselves; and
  - (2) authorising the *person* responsible for the *register* to charge for issuing any document recording, or for amending, an entry on the *register*, other than on the *issue* or *sale* of *units*.

**Income**

- 16 A statement setting out the basis for the distribution or re-investment of income.

**Income equalisation**

- 17 Where relevant, a provision for *income equalisation*.

**Redemption or cancellation of units on breach of law or rules**

- 18 A statement that where any holding of *units* by a *unitholder* is (or is reasonably considered by the *authorised fund manager* to be) an infringement of any law, governmental regulation or rule, those *units* must be redeemed or cancelled.

**ICVCs: larger and smaller denomination shares**



19 A statement of the proportion of a *larger denomination share* represented by a *smaller denomination share* for any relevant *unit class*.

**ICVCs: resolution to remove a director**

20 A statement that the *ICVC* may (without prejudice to the requirements of regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company), by a resolution passed by a simple majority of the votes validly cast for and against the resolution at a general meeting of *unitholders*, remove a *director* before his period of office expires, despite anything else in the *ICVC's instrument of incorporation* or in any agreement between the *ICVC* and that *director*.

**ICVCs: unit transfers**

21 A statement that the *person* designated for the purposes of paragraph 4 of Schedule 4 to the *OEIC Regulations* (Share transfers) is the *person* who, for the time being, is the *ACD* of the *ICVC*.

**ICVCs: Charges and expenses**

22 A statement that charges or expenses of the *ICVC* may be taken out of the *scheme property*.

**AUTs: governing law for a trust deed**

23 A statement that the *trust deed* is made under and governed by the law of England and Wales, Wales or Scotland or Northern Ireland.

**AUTs: trust deed to be binding and authoritative**

24 A statement that the *trust deed*:

- (1) is binding on each *unitholder* as if it had been a party to it and that it is bound by its provisions; and
- (2) authorises and requires the *trustee* and the *manager* to do the things required or permitted of them by its terms.

**AUTs: declaration of trust**

25 A declaration that, subject to the provisions of the *trust deed* and all *rules* made under section 247 of the *Act* (Trust scheme rules) and for the time being in force:

- (1) the *scheme property* (other than sums standing to the credit of the *distribution account*) is held by the *trustee* on trust for the *unitholders* according to the number of *units* held by each *unitholder* or, where relevant, according to the number of undivided shares in the *scheme property* represented by the *units* held by each *unitholder*; and
- (2) the sums standing to the credit of the *distribution account* are held by the *trustee* on trust to distribute or apply them in accordance with *COLL 6.8* (Income: accounting, allocation and distribution).

**AUTs: trustee's remuneration**

- 26 Where relevant, a statement authorising payments to the *trustee* by way of *remuneration* for its services to be paid (in whole or in part) out of the *scheme property*.

**AUTs: responsibility for the register**

- 27 A statement identifying the *person* responsible under the *rules* for the maintenance of the *register*.

**Umbrella scheme with only one sub-fund**

- 3.2.7 R (1) If, after the first *issue* of a *unit* in a *scheme* which is an *umbrella*, for a period of 24 consecutive *months*, *units* of less than two *sub-funds* are in *issue*, the *authorised fund manager* or, for an *ICVC*, its other *directors* must take such action as is necessary to reflect the fact the *scheme* is no longer an *umbrella* or cause *units* of more than one *sub-fund* to be in *issue*.
- (2) If (1) applies or is reasonably expected to become applicable by the *authorised fund manager* or, for an *ICVC*, its other *directors*, the *authorised fund manager* or other *directors* must notify the *unitholders* and the *FSA* of any action to comply with (1).
- (3) Paragraph (1) does not apply if before the expiry of the 24 *month* period, winding up of the *scheme* has commenced.

**UCITS obligations**

- 3.2.8 R (1) The instrument constituting a *UCITS scheme* may not be amended in such a way that it ceases to be a *UCITS scheme*.
- (2) If it is proposed to market *units* of a *UCITS scheme* in any *EEA State* other than the *United Kingdom*, the *authorised fund manager* of that *scheme* must notify the *FSA* of its proposal, specifying the *EEA State* concerned.
- (3) The *ICVC* or the *manager* must make the notification in (2) no later than the notification to the authorities in that *EEA State* of that proposal.

### 3.3 Units

#### Application

- 3.3.1 R This section applies to an *authorised fund manager*, an *ICVC* and the *trustee* of an *AUT*.

#### Classes of units

- 3.3.2 (1) The *instrument constituting the scheme* may provide for different  
G *classes of unit* to be issued in an *authorised fund* and, for a *scheme* which is an *umbrella*, provide that *classes of units* may be issued for each *sub-fund*.
- (2) In order to be satisfied that *COLL 3.2.2R* (Relationship between the instrument constituting the scheme and the rules) is complied with, the *FSA* will take into account the principles in (a) to (c) when considering proposals for *unit classes*:
- (a) a *unit class* should not provide any advantage for that *class* if that would result in prejudice to *unitholders* of any other *class*;
- (b) the nature, operation and effect of the new *unit class* should be capable of being explained clearly to prospective investors in the *prospectus*; and
- (c) the effect of the new *unit class* should not appear to be contrary to the purpose of any part of this sourcebook.

#### Currency class units

- 3.3.3 A *currency class unit* differs from other *units* mainly in that its *price*,  
G having been calculated initially in the *base currency*, will be quoted, and normally paid for, in the currency of the designation of the *class*. Income distributions will also be paid in the currency of designation of the *class*.

#### Currency class units: requirements

- 3.3.4 For a *currency class unit*:

R

- (1) the currency of the *class* concerned must not be the *base currency* (or, in the case of a *sub-fund* which, in accordance

with a statement in the *prospectus*, is to be valued in some other currency, the currency of the *class* may be in the *base currency*, but must not be in that other currency);

- (2) the *price* must be expressed in the currency of the *class* concerned;
- (3) any distribution must be paid in the currency of the *class* concerned; and
- (4) statements of amounts of *money* or values included in statements and in tax certificates must be given in the currency of the *class* concerned (whether or not also given in the *base currency*).

#### **Rights of unit classes**

- 3.3.5 R (1) If any *class* of *units* in an *authorised fund* has different rights from another *class* of *units* in that *fund*, the *instrument constituting the scheme* must provide how the proportion of the value of the *scheme property* and the proportion of income available for allocation attributable to each such *class* must be calculated.
- (2) For an *authorised fund* which is not an *umbrella*, the *instrument constituting the scheme* must not provide for any *class* of *units* in respect of which:
- (a) the extent of the rights to participate in the *capital property, income property* or *distribution account* would be determined differently from the extent of the corresponding rights for any other *class* of *units*; or
  - (b) payments or accumulation of income or capital would differ in source or form from those of any other *class* of *units*.
- (3) For a *scheme* which is an *umbrella*, the provisions in (2)(a) apply to *classes* of *units* in respect of each *sub-fund* as if each *sub-fund* were a separate *scheme*.

- (4) Paragraphs (2) and (3) do not prohibit a difference between the rights attached to one *class of units* and to another *class of units* that relates solely to:
  - (a) the accumulation of income by way of periodical credit to capital rather than distribution; or
  - (b) charges and expenses that may be taken out of the *scheme property* or payable by the *unitholders*; or
  - (c) the currency in which *prices* or values are expressed or payments made.

**Requirement: larger and smaller denomination shares in an ICVC**

- 3.3.6 R (1) This *rule* applies whenever the *instrument of incorporation* of an *ICVC* provides, in relation to any *class*, for *smaller denomination shares* and *larger denomination shares*.
- (2) Whenever a registered holding includes a number of *smaller denomination shares* that can be consolidated into a *larger denomination share* of the same *class*, the *ACD* must consolidate the relevant number of those *smaller denomination shares* into a *larger denomination share*.
- (3) The *ACD* may, to effect a transaction in *shares*, substitute for a *larger denomination share* the relevant number of *smaller denomination shares*, in which case (2) does not apply to the resulting smaller denomination shareholding or holdings until immediately after the completion of the transaction.

**Characteristics of larger and smaller denomination shares in an ICVC**

- 3.3.7 G Regulation 45 of the *OEIC Regulations (Shares)* allows the rights attached to a *share* in an *ICVC* of any *class* to be expressed in two denominations, in which case the ‘smaller’ denomination must be such proportion of the ‘larger’ denomination (a standard *share*) as is fixed by the *ICVC's instrument of incorporation* as described in *COLL* 3.2.6R19. This will enable holdings to consist of more or less than a complete number of *larger denomination shares*.

**Sub-division and consolidation of units**

- 3.3.8 (1) The *directors* of an *ICVC* or the *manager* of an *AUT* may,  
R unless expressly forbidden to do so by the *instrument constituting the scheme*, determine that:
- (a) each *unit* of any *class* is to be subdivided into two or more *units*; or
  - (b) *units* of any *class* are to be consolidated.
- (2) The *ICVC* or the *manager* must (unless it has done so before the sub-division or consolidation became effective) immediately give notice to each *unitholder* (or the first named of joint *unitholders*) of any sub-division or consolidation under (1).

#### **Guarantees and capital protection**

- 3.3.9 If there is any arrangement intended to result in a particular capital or  
R income return from a holding of *units* in an *authorised fund*, or any investment objective of giving protection to the capital value of, or income return from, such a holding:

- (1) that arrangement or protection must not be such as to cause the possibility of a conflict of interest as between:
  - (a) *unitholders* and the *authorised fund manager* or *depository*; or
  - (b) *unitholders* intended and not intended to benefit from the arrangement; and
- (2) where, in accordance with any statement required by *COLL* 4.2.5R 27(c)(iv) (Table: contents of the prospectus), action is required by the *unitholders* to obtain the benefit of any guarantee, the *authorised fund manager* must provide reasonable notice in writing to *unitholders* before such action is required.

#### **Switching rights: umbrella schemes**

- 3.3.10 (1) In accordance with section 235(4) of the *Act* (Collective  
G investment schemes), the *participants* in a *scheme* which is an *umbrella* are entitled to exchange rights in one *sub-fund* for rights in another *sub-fund* of the *umbrella*.
- (2) To satisfy (1), where any *sub-fund* in a *scheme* which is an

*umbrella* has provisions in its *prospectus* limiting the *issue* of *units* in that *sub-fund*, the *authorised fund manager* should ensure that at least two *sub-funds* are able to issue *units* at any time.



## 4 Investor Relations

### 4.1 Introduction

#### Application

4.1.1 R This chapter applies to:

- (1) an *authorised fund manager* of an *AUT* or an *ICVC*;
- (2) any other *director* of an *ICVC*;
- (3) a *depository* of an *AUT* or an *ICVC*; and
- (4) an *ICVC*,

where such *AUT* or *ICVC* is a *UCITS scheme* or a *non-UCITS retail scheme*.

#### Purpose

4.1.2 G This chapter helps in achieving the *regulatory objective* of protecting *consumers* by ensuring *consumers* have access to up-to-date detailed information about an *authorised fund* particularly before buying *units* and thereafter an appropriate level of investor involvement exists by providing a framework for them to:

- (1) participate in the decisions on key issues concerning the *authorised fund*; and
- (2) be sent regular and relevant information about the *authorised fund*.

## 4.2 Pre-sale notifications

### Application

- 4.2.1 R This section applies to an *authorised fund manager*, an *ICVC* and any other *director* of an *ICVC*.

### Publishing the prospectus

- 4.2.2 R (1) A *prospectus* must be drawn up in English and published as a *document* by the *authorised fund manager* and, for an *ICVC*, it must be approved by the *directors*.
- (2) The *authorised fund manager* must ensure that the *prospectus*:
- (a) contains the information required by *COLL 4.2.5R* (Table: contents of the prospectus);
  - (b) does not contain any provision which is unfairly prejudicial to the interests of *unitholders* generally or to the *unitholders* of any *class of units*;
  - (c) does not contain any provision that conflicts with any *rule* in this sourcebook; and
  - (d) is kept up-to-date and that revisions are made to it, whenever appropriate.

### Availability of prospectus and long report

- 4.2.3 R (1) An *ICVC* or the *manager* of an *AUT* must:
- (a) supply a copy of the *scheme's* most recent *prospectus* drawn up and published in accordance with *COLL 4.2.2R* (Publishing the prospectus) free of charge to any *person* on request; and
  - (b) file a copy of the *scheme's* original *prospectus*, together with all revisions thereto, with the *FSA*.
- (2) An *ICVC* or the *manager* of an *AUT* which in either case is a *UCITS scheme* intending to *market units* in the territory of another *EEA State* must:
- (a) ensure that the following *documents* are drawn up in the, or one of the, official languages of the *EEA State* or a language approved by the *Host State regulator*:
    - (i) the *prospectus*;
    - (ii) the *instrument constituting the scheme*; and

- (iii) the latest annual and half-yearly long reports of the *scheme*;
  - (b) supply copies of the most recent version of the *documents* in (a) to any purchaser of *units* free of charge on request, and
  - (c) file copies of the most recent version of the *documents* in (a) with the *competent authority* of each such *Host State*, provided in the, or one of the, languages of that *State* or a language approved by the *competent authority* of that *State*.
- (3) An *authorised fund manager* must, upon the request of a *unitholder* in a *UCITS scheme* that it manages, provide information supplementary to the *prospectus* of that *scheme* relating to:
- (a) the quantitative limits applying to the risk management of that *scheme*;
  - (b) the methods used in relation to (a); and
  - (c) any recent development of the risk and yields of the main categories of *investment*.

#### **False or misleading prospectus**

- 4.2.4 R (1) The *authorised fund manager*:
- (a) must ensure that the *prospectus* of the *authorised fund* does not contain any untrue or misleading statement or omit any matter required by the *rules* in this sourcebook to be included in it; and
  - (b) is liable to pay compensation to any *person* who has acquired any *units* in the *authorised fund* and suffered loss in respect of them as a result of such statement or omission; this is in addition to any liability incurred apart from under this *rule*.
- (2) The *authorised fund manager* is not in breach of (1)(a) and is not liable to pay compensation under (1)(b) if, at the time when the *prospectus* was made available to the public, it had taken reasonable care to determine that the statement was true and not misleading, or that the omission was appropriate, and that:
- (a) it continued to take such reasonable care until the time of the relevant acquisition of *units* in the *scheme*; or

- (b) the acquisition took place before it was reasonably practicable to bring a correction to the attention of potential purchasers; or
  - (c) it had already taken all reasonable steps to ensure that a correction was brought to the attention of potential purchasers; or
  - (d) the *person* who acquired the *units* was not materially influenced or affected by that statement or omission in making the decision to invest.
- (3) The *authorised fund manager* is also not in breach of (1)(a) and is not liable to pay compensation under (1)(b) if:
- (a) before the acquisition a correction had been published in a manner calculated to bring it to the attention of *persons* likely to acquire the *units* in question; or
  - (b) it took all reasonable steps to secure such publication and had reasonable grounds to conclude that publication had taken place before the *units* were acquired.
- (4) The *authorised fund manager* is not liable to pay compensation under (1)(b) if the *person* who acquired the *units* knew at the time of the acquisition that the statement was untrue or misleading or knew of the omission.
- (5) For the purposes of this *rule* a revised *prospectus* will be treated as a different *prospectus* from the original one.
- (6) References in this *rule* to the acquisition of *units* include references to contracting to acquire them.

**Table: contents of the prospectus**

4.2.5 R This table belongs to *COLL* 4.2.2R (Publishing the prospectus).

**Document status**

- 1 A statement that the *document* is the *prospectus* of the *authorised fund* valid as at a particular date (which shall be the date of the *document*).

**Authorised fund**

- 2 A description of the *authorised fund* including:
- (a) its name;
  - (b) whether it is an *ICVC* or an *AUT* and that:
    - (i) *unitholders* are not liable for the debts of the

*authorised fund*;

- (ii) for an *ICVC*, a statement that the *sub-funds* of a *scheme* which is an *umbrella* are not 'ring fenced' and in the event of the *umbrella* being unable to meet liabilities attributable to any particular *sub-fund* out of the assets attributable to that *sub-fund*, that the remaining liabilities may have to be met out of the assets attributable to other *sub-funds*;
- (c) for an *ICVC*, the address of its head office and the address of the place in the *United Kingdom* for service on the *ICVC* of notices or other documents required or authorised to be served on it;
- (d) the effective date of the *authorisation order* made by the *FSA* and relevant details of termination, if the duration of the *authorised fund* is limited;
- (e) its *base currency*;
- (f) for an *ICVC*, the maximum and minimum sizes of its capital; and
- (g) the circumstances in which it may be wound up under the *rules* and a summary of the procedure for, and the rights of *unitholders* under, such a winding up.

#### **Investment objectives and policy**

3 The following particulars of the investment objectives and policy of the *authorised fund*:

- (a) the investment objectives, including its financial objectives;
- (b) the *authorised fund's* investment policy for achieving those investment objectives, including the general nature of the portfolio and, if appropriate, any intended specialisation;
- (c) an indication of any limitations on that investment policy;
- (d) the description of assets which the *capital property* may consist of;
- (e) the proportion of the *capital property* which may consist of an asset of any description;
- (f) the description of transactions which may be effected on behalf

- of the *authorised fund* and an indication of any techniques and instruments or borrowing powers which may be used in the management of the *authorised fund*;
- (g) a list of the *eligible* markets through which the *authorised fund* may invest or *deal* in accordance with *COLL 5.2.10R(2)(b)* (Eligible markets: requirements);
  - (h) for an *ICVC*, a statement as to whether it is intended that the *scheme* will have an interest in any immovable property or movable property ((in accordance with *COLL 5.6.4R(2)* (Investment powers: general) or *COLL 5.2.8R(2)* (UCITS schemes: general)) for the direct pursuit of the *ICVC*'s business;
  - (i) where *COLL 5.2.12R(3)* (Spread: government and public securities) applies, a prominent statement as to the fact that more than 35% of the *scheme property* is or may be invested in *government and public securities* and the names of the individual states, local authorities or public international bodies in whose *securities* the *authorised fund* may invest more than 35% of the *scheme property*;
  - (j) the policy in relation to the exercise of borrowing powers by the *authorised fund*;
  - (k) for an *authorised fund* which may invest in other *schemes*, the extent to which the *scheme property* may be invested in the *units* of *schemes* which are managed by the *authorised fund manager* or by its *associate*;
  - (l) where a *scheme* invests principally in *scheme units*, *deposits* or *derivatives*, or replicates an index in accordance with *COLL 5.2.31R* or *COLL 5.6.23* (Schemes replicating an index), a prominent statement regarding this investment policy;
  - (m) where *derivatives* transactions may be used in a *scheme*, a prominent statement as to whether these transactions are for the purposes of hedging or meeting the investment objectives or both and the possible outcome of the use of *derivatives* on the risk profile of the *scheme*;
  - (n) information concerning the profile of the typical investor for

- whom the *scheme* is designed;
- (o) information concerning the historical performance of the *scheme* presented in accordance with *COB* 3.8.11R (Specific non-real time financial promotions: past performance);
  - (p) for a *non-UCITS retail scheme* which invests in immovables, a statement of the countries or territories of situation of land or buildings in which the *authorised fund* may invest;
  - (q) for a *UCITS scheme* which invests a substantial portion of its assets in other *schemes*, a statement of the maximum level of management fees that may be charged to that *UCITS scheme* and to the *schemes* in which it invests;
  - (r) where the net asset value of a *UCITS scheme* is likely to have high volatility owing to its portfolio composition or the portfolio management techniques that may be used, a prominent statement to that effect; and
  - (s) for a *UCITS scheme*, a statement that any *unitholder* may obtain on request the types of information (which must be listed) referred to in *COLL* 4.2.3 R(3) (Availability of prospectus and long report).

#### **Reporting, distributions and accounting dates**

- 4 Relevant details of the reporting, accounting and distribution information which includes:
- (a) the accounting and distribution dates;
  - (b) procedures for:
    - (i) determining and applying income (including how any distributable income is paid);
    - (ii) unclaimed distributions; and
    - (iii) if relevant, calculating, paying and accounting for *income equalisation*;
  - (c) the *accounting reference date* and when the long report will be published in accordance with *COLL* 4.5.14R (Publication and availability of annual and half-yearly long report); and
  - (d) when the short report will be sent to *unitholders* in accordance with *COLL* 4.5.13R (Provision of short report).

#### **Characteristics of the units**

- 5 Information as to:
- (a) where there is more than one *class of unit* in *issue* or available for *issue*, the name of each such *class* and the rights attached to each *class* in so far as they vary from the rights attached to other *classes*;
  - (b) where the *instrument constituting the scheme* provides for the *issue of bearer certificates*, that fact and what procedures will operate for them;
  - (c) how *unitholders* may exercise their voting rights and what these amount to;
  - (d) where a mandatory *redemption, cancellation* or conversion of *units* from one *class* to another may be required, in what circumstances it may be required; and
  - (e) for an *AUT*, the fact that the nature of the right represented by *units* is that of a beneficial interest under a trust.

**Authorised fund manager**

- 6 The following particulars of the *authorised fund manager*:
- (a) its name;
  - (b) the nature of its corporate form;
  - (c) the date of its incorporation;
  - (d) the address of its registered office;
  - (e) the address of its head office, if that is different from the address of its registered office;
  - (f) if neither its registered office nor its head office is in the *United Kingdom*, the address of its principal place of business in the *United Kingdom*;
  - (g) if the duration of its corporate status is limited, when that status will or may cease; and
  - (h) the amount of its issued share capital and how much of it is paid up.

**Directors of an ICVC, other than the ACD**

- 7 Other than for the *ACD*:
- (a) the names and positions in the *ICVC* of any other *directors* (if



any); and

- (b) the manner, amount and calculation of the *remuneration* of such *directors*.

### **Depositary**

8 The following particulars of the *depositary*:

- (a) its name;
- (b) the nature of its corporate form;
- (c) the address of its registered office;
- (d) the address of its head office, if that is different from the address of its registered office;
- (e) if neither its registered office nor its head office is in the *United Kingdom*, the address of its principal place of business in the *United Kingdom*; and
- (f) a description of its principal business activity.

### **Investment adviser**

9 If an *investment adviser* is retained in connection with the business of an *authorised fund*:

- (a) its name; and
- (b) where it carries on a significant activity other than providing services to the *authorised fund* as an *investment adviser*, what that significant activity is.

### **Auditor**

10 The name of the auditor of the *authorised fund*.

### **Contracts and other relationships with parties**

11 The following relevant details:

- (a) for an *ICVC*:
  - (i) a summary of the material provisions of the contract between the *ICVC* and the *authorised fund manager* which may be relevant to *unitholders* including provisions (if any) relating to remuneration, termination, compensation on termination and indemnity;
  - (ii) the main business activities of each of the *directors*

- (other than those connected with the business of the *ICVC*) where these are of significance to the *ICVC*'s business;
- (iii) if any *director* is a *body corporate* in a *group* of which any other corporate *director* of the *ICVC* is a member, a statement of that fact; and
  - (iv) the main terms of each contract of service between the *ICVC* and a *director* in summary form;
- (b) the names of the *directors* of the *authorised fund manager* and the main business activities of each of the *directors* (other than those connected with the business of the *authorised fund*) where these are of significance to the *authorised fund's* business;
  - (c) a summary of the material provisions of the contract between the *ICVC* or the *manager* of the *AUT* and the *depository* which may be relevant to *unitholders*, including provisions relating to the *remuneration* of the *depository*;
  - (d) if an *investment adviser* retained in connection with the business of the *authorised fund* is a *body corporate* in a *group* of which any *director* of the *ICVC* or the *manager* of the *AUT* is a member, that fact;
  - (e) a summary of the material provisions of any contract between the *authorised fund manager* or the *ICVC* and any *investment adviser* which may be relevant to *unitholders*;
  - (f) if an *investment adviser* retained in connection with the business of the *authorised fund* has the authority of the *authorised fund manager* or the *ICVC* to make decisions on behalf of the *authorised fund manager* or the *ICVC*, that fact and a description of the matters in relation to which it has that authority;
  - (g) what functions (if any) the *authorised fund manager* has delegated and to whom; and
  - (h) in what capacity (if any), the *authorised fund manager* acts in relation to any other *collective investment schemes* and the

name of such *schemes*.

### **Register of unitholders**

12 Details of:

- (a) the address in the *United Kingdom* where the *register of unitholders*, and where relevant the *plan register* is kept and can be inspected by *unitholders*; and
- (b) the *registrar's* name and address.

### **Payments out of scheme property**

13 In relation to each type of payment from the *scheme property*, details of:

- (a) who the payment is made to;
- (b) what the payment is for;
- (c) the rate or amount where available;
- (d) how it will be calculated and accrued;
- (e) when it will be paid; and
- (f) where a performance fee is taken, examples of its operation in plain English and the maximum it can amount to.

### **Allocation of payments**

14 If, in accordance with *COLL 6.7.10R* (Allocation of payments to income or capital), the *authorised fund manager* and the *depository* have agreed that all or part of any income expense payments may be treated as a capital expense:

- (a) that fact;
- (b) the policy for allocation of these payments; and
- (c) a statement that this policy may result in capital erosion or constrain capital growth.

### **Moveable and immovable property (ICVC only)**

15 An estimate of any expenses likely to be incurred by the *ICVC* in respect of movable and immovable property in which the *ICVC* has an interest.

### **Valuation and pricing of scheme property**

16 In relation to the valuation and *pricing of scheme property*:

- (a) a provision that there must be only a single *price* for any *unit* as determined from time to time by reference to a particular *valuation point*;
- (b) details of:
  - (i) how the value of the *scheme property* is to be determined in relation to each purpose for which the *scheme property* must be valued;
  - (ii) how frequently and at what time or times of the *day* the *scheme property* will be regularly valued for *dealing* purposes and a description of any circumstance in which the *scheme property* may be specially valued;
  - (iii) where relevant, how the *price* of *units* of each *class* will be determined for *dealing* purposes; and
  - (iv) where and at what frequency the most recent *prices* will be published; and
- (c) if provisions in (a) and (b) do not take effect when the *instrument constituting the scheme* or (where appropriate) supplemental *trust deed* takes effect, a statement of the time from which those provisions are to take effect or how it will be determined.

## **Dealing**

17 The following particulars:

- (a) the procedures, the dealing periods and the circumstances in which the *authorised fund manager* will effect:
  - (i) the *sale* and *redemption* of *units* and the settlement of transactions (including the minimum number or value of *units* which one *person* may hold or which may be subject to any transaction of *sale* or *redemption*) for each *class* of *unit* in the *authorised fund*; and
  - (ii) any direct *issue* or *cancellation* of *units* by an *ICVC* or by the *trustee* (as appropriate) through the *authorised fund manager* in accordance with *COLL 6.2.7R(2)* (Issue and cancellation of units through an

- authorised fund manager);
- (b) the circumstances in which the *redemption* of *units* may be suspended;
  - (c) whether certificates will be issued in respect of registered *units*;
  - (d) the circumstances in which the *authorised fund manager* may arrange for, and the procedure for the *issue* or *cancellation* of *units* in specie;
  - (e) the investment exchanges (if any) on which *units* in the *scheme* are listed or dealt;
  - (f) the circumstances and conditions for issuing *units* in an *authorised fund* which limit the *issue* of any *class of units* in accordance with *COLL* 6.2.18R (Limited issue);
  - (g) the circumstances and procedures for the limitation or deferral of *redemptions* in accordance with *COLL* 6.2.19R (Limited redemption) or *COLL* 6.2.21R (Deferred redemption); and
  - (h) in a *prospectus* available during the period of any *initial offer*:
    - (i) the length of the *initial offer* period;
    - (ii) the initial *price* of a *unit*, which must be in the *base currency*;
    - (iii) the arrangements for issuing *units* during the *initial offer*, including the *authorised fund manager's* intentions on investing the subscriptions received during the *initial offer*;
    - (iv) the circumstances when the *initial offer* will end;
    - (v) whether *units* will be *sold* or *issued* in any other currency; and
    - (vi) any other relevant details of the *initial offer*.

### **Dilution**

18 Details of what is meant by *dilution* including:

- (a) a statement explaining:
  - (i) that it is not possible to predict accurately whether *dilution* is likely to occur; and
  - (ii) which of the policies the *authorised fund manager* is

- adopting under *COLL* 6.3.8R(1) (Dilution) together with an explanation of how this policy may affect the future growth of the *authorised fund*; and
- (b) if the *authorised fund manager* may require a *dilution levy* or make a *dilution adjustment*, a statement of:
- (i) the *authorised fund manager's* policy in deciding when to require a *dilution levy*, including the *authorised fund manager's* policy on *large deals*, or when to make a *dilution adjustment*;
- (ii) the estimated rate or amount of any *dilution levy* or *dilution adjustment* based either on historical data or future projections; and
- (iii) the likelihood that the *authorised fund manager* may require a *dilution levy* or make a *dilution adjustment* and the basis (historical or projected) on which the statement is made.

#### **SDRT provision**

- 19 An explanation of:
- (a) what is meant by stamp duty reserve tax, *SDRT provision* and *large deals*; and
- (b) the *authorised fund manager's* policy on imposing an *SDRT provision* including its policy on *large deals*, and the occasions, and the likely frequency of the occasions, in which an *SDRT provision* may be imposed and the maximum rate of it (a usual rate may also be stated).

#### **Forward and historic pricing**

- 20 The *authorised fund manager's* normal basis of pricing under *COLL* 6.3.9R (Forward and historic pricing).

#### **Preliminary charge**

- 21 Where relevant, a statement authorising the *authorised fund manager* to make a *preliminary charge* and specifying the basis for and current amount or rate of that charge.

#### **Redemption charge**

22 Where relevant, a statement authorising the *authorised fund manager* to deduct a *redemption charge* out of the proceeds of *redemption*; and if the *authorised fund manager* makes a *redemption charge*:

- (a) the current amount of that charge or if it is variable, the rate or method of calculating it;
- (b) if the amount, rate or method has been changed, that details of any previous amount, rate or method may be obtained from the *authorised fund manager* on request; and
- (c) how the order in which *units* acquired at different times by a *unitholder* is to be determined so far as necessary for the purposes of the imposition of the *redemption charge*.

### **General information**

23 Details of:

- (a) the address at which copies of the *instrument constituting the scheme*, any amending instrument and the most recent annual and half-yearly long reports may be inspected and from which copies may be obtained;
- (b) the manner in which any notice or *document* will be served on *unitholders*;
- (c) the extent to which and the circumstances in which:
  - (i) the *scheme* is liable to pay or suffer tax on any appreciation in the value of the *scheme property* or on the income derived from the *scheme property*; and
  - (ii) deductions by way of withholding tax may be made from distributions of income to *unitholders* and payments made to *unitholders* on the *redemption* of *units*; and
- (d) for a *UCITS scheme*, any possible fees or expenses not described in paragraphs 13 to 22, distinguishing between those to be paid by a *unitholder* and those to be paid out of *scheme property*.

### **Information on the umbrella**

24 In the case of a *scheme* which is an *umbrella*, the following information:

- (a) that a *unitholder* is entitled to exchange *units* in one *sub-fund* for *units* in any other *sub-fund* (other than a *sub-fund* which has limited the *issue* of *units*);
- (b) that an exchange of *units* in one *sub-fund* for *units* in any other *sub-fund* is treated as a *redemption* and *sale* and will, for *persons* subject to *United Kingdom* taxation, be a realisation for the purposes of capital gains taxation;
- (c) that in no circumstances will a *unitholder* who exchanges *units* in one *sub-fund* for *units* in any other *sub-fund* be given a right by law to withdraw from or cancel the transaction;
- (d) the policy for allocating between *sub-funds* any assets of, or costs, charges and expenses payable out of, the *scheme property* which are not attributable to any particular *sub-fund*;
- (e) what charges, if any, may be made on exchanging *units* in one *sub-fund* for *units* in any other *sub-fund*;
- (f) for each *sub-fund*, the currency in which the *scheme property* allocated to it will be valued and the *price* of *units* calculated and payments made, if this currency is not the *base currency* of the *scheme* which is an *umbrella*; and
- (g) if there are *units* for less than two *sub-funds* in issue, the effect of *COLL 3.2.7R* (Umbrella scheme with only one sub-fund).

#### **Application of the prospectus contents to an umbrella**

25 For a *scheme* which is an *umbrella*, information required must be stated:

- (a) in relation to each *sub-fund* where the information for any *sub-fund* differs from that for any other; and
- (b) for the *umbrella* as a whole, but only where the information is relevant to the *umbrella* as a whole.

#### **Marketing in another EEA state**

26 A *prospectus* of a *UCITS scheme* which is prepared for the purpose of marketing units in a *EEA State* other than the *United Kingdom*, must give details as to:

- (a) what special arrangements have been made :



- (i) for paying in that *EEA State* amounts distributable to *unitholders* resident in that *EEA State*;
  - (ii) for *redeeming* in that *EEA State* the *units* of *unitholders* resident in that *EEA State*;
  - (iii) for inspecting and obtaining copies in that *EEA State* of the *instrument constituting the scheme* and amendments to it, the *prospectus* and the annual and half-yearly long report; and
  - (iv) for making public the *price* of *units* of each *class*; and
- (b) how the *ICVC* or the *manager* of an *AUT* will publish in that *EEA State* notice:
- (i) that the annual and half-yearly long report are available for inspection;
  - (ii) that a distribution has been declared;
  - (iii) of the calling of a meeting of *unitholders*; and
  - (iv) of the termination of the *authorised fund* or the revocation of its authorisation.

**Additional information**

27 Any other material information which is within the knowledge of the *directors* of an *ICVC* or the *manager* of an *AUT*, or which the *directors* or *manager* would have obtained by making reasonable enquiries, including but not confined to, the following matters:

- (a) information which investors and their professional advisers would reasonably require, and reasonably expect to find in the *prospectus*, for the purpose of making an informed judgement about the merits of investing in the *authorised fund* and the extent and characteristics of the risks accepted by so participating;
- (b) a clear and easily understandable explanation of any risks which investment in the *authorised fund* may reasonably be regarded as presenting for reasonably prudent investors of moderate means;

- (c) if there is any arrangement intended to result in a particular capital or income return from a holding of *units* in the *authorised fund* or any investment objective of giving protection to the capital value of, or income return from, such a holding:
  - (i) details of that arrangement or protection;
  - (ii) for any related guarantee, sufficient details about the guarantor and the guarantee to enable a fair assessment of the value of the guarantee;
  - (iii) a description of the risks that could affect achievement of that return or protection; and
  - (iv) details of the arrangements by which the *authorised fund manager* will notify *unitholders* of any action required by the *unitholders* to obtain the benefit of the guarantee; and
- (d) whether any notice has been given to *unitholders* of the *authorised fund manager's* intention to propose a change to the *scheme* and if so, its particulars.

#### **Guidance on contents of the prospectus**

- 4.2.6 G (1) In relation to *COLL* 4.2.5R 3(b) the *prospectus* might include:
- (a) a description of the extent (if any) to which that policy does not envisage the *authorised fund* remaining fully invested at all times;
  - (b) for a *non-UCITS retail scheme* which may invest in immovable property:
    - (i) the maximum extent to which the *scheme property* may be invested in immovables; and
    - (ii) a statement of the policy of the *authorised fund manager* in relation to insurance and immovables forming part of the *scheme property*; and

- (c) a description of any restrictions in the assets in which investment may be made, including restrictions in the extent to which the *authorised fund* may invest in any category of asset, indicating (if appropriate) where the restrictions are more onerous than those imposed by *COLL 5* (Investment and borrowing powers).
- (2) In relation to *COLL 4.2.5R 13*, the type of payments are likely to include management fees (such as periodic and performance fees), *depository* fees, custodian fees, transaction fees, registrar fees, audit fees and FSA fees. Expenses which represent properly incurred costs of the *scheme* may also be treated as a type of payment for this purpose.
- (3) In relation to *COLL 4.2.5R 27*, the *prospectus* might include a prominent statement of non-accountability referred to in *COLL 6.7.16G* (Exemptions from liability to account for profits).

### 4.3 Approvals and notifications

#### Application

4.3.1 R This section applies to an *authorised fund manager*.

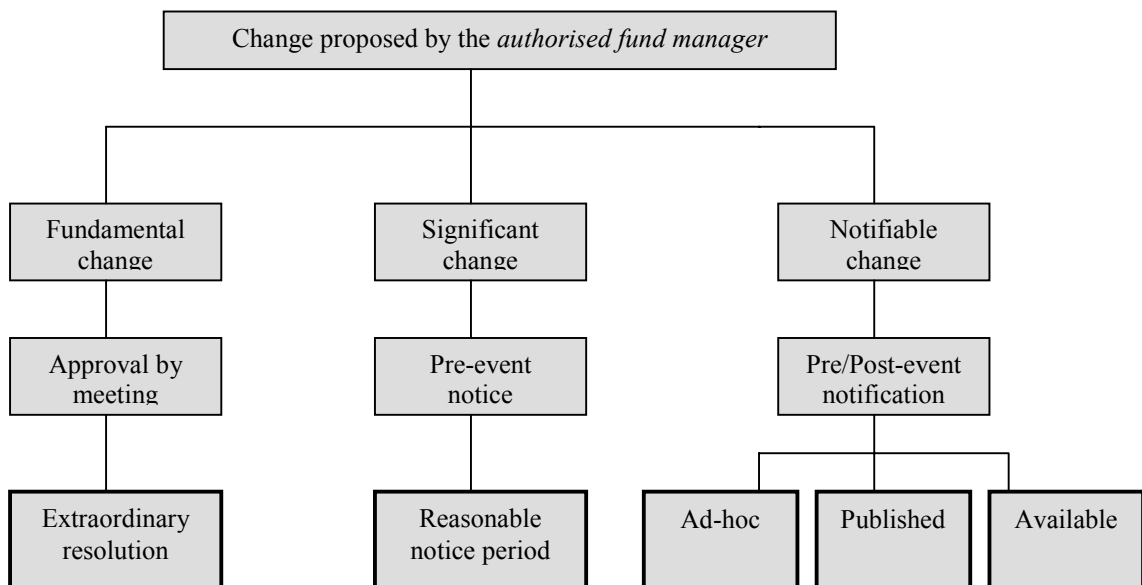
#### Explanation

4.3.2 G (1) The diagram in *COLL 4.3.3G* explains how an *authorised fund manager* should treat changes it is proposing to a *scheme* and provides an overview of the *rules* and *guidance* in this section.

(2) Regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company) and section 251 of the *Act* (Alteration of schemes and changes of manager or trustee) require the prior approval of the *FSA* for certain proposed changes to an *authorised fund*, including a change of the *authorised fund manager* or *depository* or a change to the *instrument constituting the scheme*. This should be kept in mind when considering any proposed change.

#### Diagram: Change event

4.3.3 G This diagram belongs to *COLL 4.3.2G*.



#### Fundamental change requiring prior approval by meeting

4.3.4 R (1) The *authorised fund manager*, must, by way of an *extraordinary resolution*, obtain prior approval from the *unitholders* for any proposed change to the *scheme* which, in accordance with (2), is a fundamental change.

- (2) A fundamental change is a change or event which:
  - (a) changes the purposes or nature of the *scheme*; or
  - (b) may materially prejudice a *unitholder*; or
  - (c) alters the risk profile of the *scheme*; or
  - (d) introduces any new type of payment out of *scheme property*.

### **Guidance on fundamental changes**

- 4.3.5 G (1) Any change may be fundamental depending on its degree of materiality and effect on the *scheme* and its *unitholders*. Consequently an *authorised fund manager* will need to determine whether in each case a particular change is fundamental in nature or not.
- (2) For the purpose of *COLL* 4.3.4R(2)(a) to (c), a fundamental change to a *scheme* is likely to include:
- (a) any proposal for a *scheme of arrangement* referred to in *COLL* 7.6.2R (Schemes of arrangement: requirements);
  - (b) a change in the investment policy to achieve capital growth from investment in one country rather than another;
  - (c) a change in the investment objective or policy to achieve capital growth through investment in fixed interest rather than equity *investments*;
  - (d) a change in the investment policy to allow the *authorised fund* to invest in *derivatives* as an investment strategy which increases its volatility;
  - (e) a change to the characteristics of a *scheme* to distribute income annually rather than *monthly*; or
  - (f) the introduction of *limited redemption arrangements*.

### **Significant change requiring pre-event notification**

- 4.3.6 R (1) The *authorised fund manager* must give prior written notice to *unitholders*, in respect of any proposed change to the operation of a *scheme* that, in accordance with (2), constitutes a significant change.
- (2) A significant change is a change or event which is not fundamental in accordance with *COLL* 4.3.4R but which:
- (a) affects a *unitholder's* ability to exercise his rights in relation to

- his investment; or
  - (b) would reasonably be expected to cause the *unitholder* to reconsider his participation in the *scheme*; or
  - (c) results in any increased payments out of the *scheme property* to an *authorised fund manager* or any other *director* of an *ICVC* or an *associate* of either; or
  - (d) materially increases other types of payment out of *scheme property*.
- (3) The notice period in (1) must be of a reasonable length (and must not be less than 60 *days*).

#### **Guidance on significant changes**

- 4.3.7 G (1) Changes may be significant depending in each case on their degree of materiality and effect on the *scheme* and its *unitholders*. Consequently the *authorised fund manager* will need to determine whether in each case a particular change is significant in nature or not.
- (2) For the purpose of *COLL* 4.3.6R a significant change is likely to include:
- (a) a change in the method of *price* publication;
  - (b) a change in any operational policy such as dilution policy or allocation of payments policy; or
  - (c) an increase in the *preliminary charge* where *units* are purchased through a *group savings plan*.

#### **Notifiable changes**

- 4.3.8 R (1) The *authorised fund manager* must inform *unitholders* in an appropriate manner and timescale of any notifiable changes that are reasonably likely to affect, or have affected, the operation of the *scheme*.
- (2) A notifiable change is a change or event, other than a fundamental change under *COLL* 4.3.4R or a significant change under *COLL* 4.3.6R, which a *unitholder* must be made aware of unless the *authorised fund manager* concludes that the change is insignificant.

#### **Guidance on notifiable changes**

- 4.3.9 G (1) The circumstances causing a notifiable change may or may not be within the control of the *authorised fund manager*.
- (2) For the purpose of COLL 4.3.8R (Notifiable changes) a notifiable change might include:
- (a) a change of named *investment manager* where the *authorised fund* has been marketed on the basis of that individual's involvement;
  - (b) a significant political event which impacts on the *authorised fund* or its operation;
  - (c) a change to the time of the *valuation point*;
  - (d) the introduction of limited issue arrangements; or
  - (e) a change of the *depository* or a change in the name of the *authorised fund*.
- (3) The appropriate manner and timescale of notification would depend on the nature of the change or event. Consequently the *authorised fund manager* will need to assess each change or event individually.
- (4) An appropriate manner of notification could include:
- (a) sending an immediate notification to the *unitholder*;
  - (b) publishing the information on a website; or
  - (c) the information being included in the next long report of the *scheme*.

## 4.4 Meetings of unitholders and service of notices

### Application

- 4.4.1 R This section applies to an *authorised fund manager*, a *depository* and any other *director* of an *ICVC*.

### General meetings

- 4.4.2 R (1) The *authorised fund manager*, the *depository* or the other *directors* of an *ICVC* may convene a general meeting of *unitholders* at any time.
- (2) The *unitholders* may request the convening of a general meeting by a requisition which must:
- (a) state the objects of the meeting;
  - (b) be dated;
  - (c) be signed by *unitholders* who, at that date, are registered as the *unitholders* of *units* representing not less than one-tenth in value (or such lower proportion stated in the *instrument constituting the scheme*) of all of the *units* then in *issue*; and
  - (d) be deposited at the head office of the *ICVC* or with the *trustee*.
- (3) The *authorised fund manager*, the *depository* or the other *directors* of an *ICVC* must on receipt of a requisition that complies with (2), immediately convene a general meeting of the *authorised fund* for a date no later than eight weeks after receipt of the requisition.

### Class meetings

- 4.4.3 R This section applies, unless the context otherwise requires, to *class meetings* by reference to the *units* of the *class* concerned and the *unitholders* and *prices* of such *units*.

### Special meaning of unitholder in COLL 4.4

- 4.4.4 R (1) Unless a *unit* in the *authorised fund* is a *participating security*, in this section "*unitholders*" means *unitholders* as at a cut-off date selected by the *authorised fund manager* which is a reasonable time before notices of the relevant meeting are sent out.
- (2) If any *unit* in the *authorised fund* is a *participating security*, a registered *unitholder* of such a *unit* is entitled to receive a notice of a meeting or a notice of an adjourned meeting under *COLL 4.4.5R*



(Notice of general meetings), if entered on the *register* at the close of business on a *day* to be determined by the *authorised fund manager*, which must not be more than 21 *days* before the notices of the meeting are sent out.

- (3) For the purposes of (2), in *COLL* 4.4.6R (Quorum) to 4.4.11R (Chairman, adjournments and minutes) “*unitholders*” in relation to those *units* means:
- (a) the *persons* entered on the *register* at a time to be determined by the *authorised fund manager* and stated in the notice of the meeting, which must not be more than 48 hours before the time fixed for the meeting; or
  - (b) in the case of bearer *units*, *unitholders* of bearer *units* which were in *issue* at the time applicable under (a).

#### **Notice of general meetings**

- 4.4.5 R (1) Where the *authorised fund manager*, the *depository* or the other *directors* of an *ICVC* decide to convene a general meeting of *unitholders*:
- (a) each *unitholder* must be given at least 14 *days* written notice, inclusive of the date on which the notice is first served and the day of the meeting; and
  - (b) the notice must specify the place, day and hour of the meeting and the terms of the resolutions to be proposed and a copy of the notice must be sent to the *depository*.
- (2) The accidental omission to give notice to, or the non-receipt of notice by, any *unitholder* does not invalidate the proceedings at any meeting.
- (3) Notice of an adjourned meeting of *unitholders* must be given to each *unitholder*, stating that while two *unitholders* present in person or proxy are required to constitute a quorum at the adjourned meeting, this may be reduced to one in accordance with *COLL* 4.4.6R(3), should two such *unitholders* not be present after a reasonable time of convening of the meeting.
- (4) Paragraph (1)(a) does not apply to the notice of an adjourned meeting.

#### **Quorum**

- 4.4.6 R (1) The quorum required to conduct business at a meeting of *unitholders* is two *unitholders*, present in person or by proxy.
- (2) If after a reasonable time from the time for the start of the meeting, a quorum is not present, the meeting:
- (a) if convened on the requisition of *unitholders*, must be dissolved; and
- (b) in any other case, must stand adjourned to:
- (i) a day and time which is seven or more *days* after the day and time of the meeting; and
- (ii) a place to be appointed by the chairman.
- (3) If, at an adjourned meeting under (2)(b), a quorum is not present after a reasonable time from the time for the meeting, one *person* entitled to be counted in a quorum present at the meeting shall constitute a quorum.

### **Resolutions**

- 4.4.7 R (1) Except where an *extraordinary resolution* is specifically required or permitted, any resolution of *unitholders* is passed by a simple majority of the votes validly cast at a general meeting of *unitholders*.
- (2) In the case of an equality of, or an absence of, votes cast, the chairman is entitled to a casting vote.

### **Voting rights**

- 4.4.8 R (1) On a show of hands every *unitholder* who is present in person has one vote.
- (2) On a poll:
- (a) votes may be given either personally or by proxy or in another manner permitted by the *instrument constituting the scheme*;
- (b) the voting rights for each *unit* must be the proportion of the voting rights attached to all of the units in *issue* that the *price* of the *unit* bears to the aggregate *price* or *prices* of all of the *units* in *issue*:
- (i) if any *unit* is a *participating security*, at the time determined under *COLL* 4.4.4R(2) (Special meaning of unitholder in *COLL* 4.4);

- (ii) otherwise at the date specified in *COLL 4.4.4R(1)*; and
  - (c) a *unitholder* need not use all his votes or cast all his votes in the same way.
- (3) For joint *unitholders* of a *unit*, only the vote of the first named in the *register of unitholders* can be taken.
  - (4) No *director* of the *ICVC* or the *manager* can be counted in the quorum of, and no such *director* or the *manager* nor any of their *associates* may vote at, any meeting of the *authorised fund*.
  - (5) The prohibition in (4) does not apply to any *units* held on behalf of, or jointly with, a *person* who, if himself the registered *unitholder*, would be entitled to vote and from whom the *director*, the *manager* or its *associate* have received voting instructions.
  - (6) For the purpose of this section, *units* held, or treated as held, by the *authorised fund manager* or any other *director* of the *ICVC*, must not, except as mentioned in (5), be regarded as being in *issue*.

#### **Right to demand a poll**

- 4.4.9 R (1) A resolution put to the vote of a general meeting must be determined on a show of hands unless a poll is (before or on the declaration of the result of the show of hands) demanded by:
- (a) the chairman;
  - (b) at least two *unitholders*; or
  - (c) the *depository*.
- (2) Unless a poll is demanded in accordance with (1), a declaration by the chairman as to the result of a resolution is conclusive evidence of the fact.

#### **Proxies**

- 4.4.10 R (1) A *unitholder* may appoint another *person* to attend a general meeting and vote in his place.
- (2) Unless the *instrument constituting the scheme* provides otherwise, a *unitholder* may appoint more than one proxy to attend on the same occasion but a proxy may vote only on a poll.
- (3) Every notice calling a meeting of a *scheme* must contain a reasonably prominent statement that a *unitholder* entitled to attend and vote may

appoint a proxy.

- (4) For the appointment to be effective, any *document* relating to the appointment of a proxy must not be required to be received by the *ICVC* or any other *person* more than 48 hours before the meeting or adjourned meeting

#### **Chairman, adjournment and minutes**

- 4.4.11 R (1) A meeting of *unitholders* must have a chairman, nominated by the *depository*.
- (2) If the chairman is not present after a reasonable time from the time for the meeting, the *unitholders* present must choose one of them to be chairman.
  - (3) The chairman:
    - (a) may, with the consent of any meeting of *unitholders* at which a quorum is present; and
    - (b) must, if so directed by the meeting;  
adjourn the meeting from time to time and from place to place.
  - (4) Business must not be transacted at any adjourned meeting, except business which might have lawfully been transacted at the original meeting.
  - (5) The *authorised fund manager* must ensure that:
    - (a) minutes of all resolutions and proceedings at every meeting of *unitholders* are made and kept; and
    - (b) any minute made in (a) is signed by the chairman of the meeting of *unitholders*.
  - (6) Any minute referred to in (5)(b) is conclusive evidence of the matters stated in it.

#### **Notices to unitholders**

- 4.4.12 R (1) Where this sourcebook requires any notice or *document* to be served upon a *unitholder*, it is duly served :
- (a) for *units* held by a registered *unitholder*, if it is:
    - (i) delivered to the *unitholder's* address as appearing in the *register*; or

- (ii) delivered by using an electronic medium in accordance with *COLL 4.4.13R* (Other notices); or
- (b) for *units* represented by *bearer certificates*, if given in the manner provided for in the *prospectus*.
- (2) Any notice or *document* served by post is deemed to have been served on the second *business day* following the *day* on which it is posted.
- (3) Any *document* left at a registered address or delivered other than by post is deemed to have been served on that *day*.

#### **Other notices**

- 4.4.13 R (1) Any *document* or notice to be served on or information to be given to, any *person*, including the *FSA*, must be in legible form.
- (2) For the purposes of this *rule*, any form is legible form which:
- (a) is consistent with the *ICVC's*, the *directors'*, the *authorised fund manager's* or the *depository's* knowledge of how the recipient of the *document* wishes or expects to receive the *document*;
  - (b) is capable of being provided in hard copy by the *authorised fund manager*, the *depository* or any other director of the *ICVC*;
  - (c) enables the recipient to know or record the time of receipt; and
  - (d) is reasonable in the context.
- (3) In this sourcebook, any requirement that a *document* be signed may be satisfied by an electronic signature or electronic evidence of assent.

#### **References to writing and electronic documents**

- 4.4.14 G In this sourcebook references to writing and the use of electronic media should be construed in accordance with *GEN 2.2.14R* (References to writing) and its related *guidance* provisions.

#### **Service of notice Regulations**

- 4.4.15 G The provisions in this section relating to the service and delivery of notices and *documents* both to *unitholders* and to the *FSA*, disapply the provisions of The Financial Services and Markets Act 2000 (Service of Notices) Regulations 2001 (SI 2001/1420) under the power in Regulation 1(6) of those Regulations.

## 4.5 Reports and accounts

### Application

- 4.5.1 R The *rules* and *guidance* in this section apply to an *authorised fund manager*, a *depository* and any other *director* of an *ICVC*.

### Explanation

- 4.5.2 G In order to provide the *unitholders* with regular and relevant information about the progress of the *authorised fund*, the *authorised fund manager* must:
- (1) prepare a short report and a long report half-yearly and annually;
  - (2) send the short report to all *unitholders*; and
  - (3) make the long report available to *unitholders* on request.

### Preparation of long and short reports

- 4.5.3 R
- (1) The *authorised fund manager* must for each *annual accounting period* and *half-yearly accounting period*, prepare a short report and a long report for a *scheme*.
  - (2) For a *scheme* which is an *umbrella*, the *authorised fund manager* must prepare a short report for each *sub-fund* but this is not necessary for the *umbrella* as a whole.
  - (3) Where the first *annual accounting period* of a *scheme* is less than 12 *months*, a half-yearly report need not be prepared.
  - (4) The first *annual accounting period* of a *scheme* must begin:
    - (a) on the first *day* of any period of *initial offer*; or
    - (b) in any other case, on the date of the relevant *authorisation order*.

### ICVC requirements

- 4.5.4 G
- (1) The *OEIC Regulations* contain requirements for the preparation of annual and half-yearly reports and make the *directors* of an *ICVC* responsible for the preparation of annual and half-yearly reports on the *ICVC*.
  - (2) Regulations 66 (Reports: preparation), 67 (Reports: accounts) and 68 (Reports: voluntary revision) of the *OEIC Regulations* also contain a

number of other requirements relating to reports and accounts of an *ICVC*.

### **Contents of a short report**

- 4.5.5 R (1) The short report for an *authorised fund*, or for a *scheme* which is an *umbrella*, its *sub-fund*, must contain for the relevant period:
- (a) the name of the *scheme* or *sub-fund*, its stated investment objectives and policy for achieving those objectives, a brief assessment of its risk profile and the name and address of the *authorised fund manager*;
  - (b) a review of the *scheme* or *sub-fund's* investment activities and investment performance during the period;
  - (c) a performance record consistent with *COLL 4.5.10R(1)* (Comparative table) so as to enable a *unitholder* to put into context the results of the investment activities of the *scheme* during the period;
  - (d) sufficient information to enable *unitholders* to form a view on where the portfolio is invested at the end of the period and the extent to which that has changed over the period;
  - (e) any other significant information which would reasonably enable *unitholders* to make an informed judgement on the activities of the *scheme* or *sub-fund* during the period and the results of those activities at the end of the period; and
  - (f) a statement that the latest long report is available on request.
- (2) The *authorised fund manager* must take reasonable steps to ensure that the short report is structured and written in such a way that it can be easily understood by the average investor.
- (3) The short report must form a separate stand-alone *document* which must not include any extraneous material.
- (4) The inclusion in a single *document* of the short reports of more than one of an *authorised fund manager's schemes* with the same accounting periods, or of more than one *sub-fund* in an *umbrella*, is not a contravention of (3) if each such report is discrete and easily identifiable.

- (5) The *authorised fund manager* must ensure that the information given in the short report is consistent with the long report for the relevant accounting period prepared under *COLL 4.5.7R* (Contents of the annual long report) or *COLL 4.5.8R* (Contents of the half-yearly long report).

#### **Significant information to be contained in the short report**

- 4.5.6 G For the purpose of *COLL 4.5.5R*(1)(d) and (e) the *authorised fund manager* should consider including the following as sufficient and significant information:
- (1) particulars of any fundamental change to the *scheme* which required *unitholder* approval by meeting during the period;
  - (2) particulars of any significant change to the operation of the *scheme* requiring pre-notification, but this need only be given if the change impacts on the *unitholders*' ability to make an informed judgement on the activities of the *scheme*;
  - (3) particulars of any other developments in relation to the investment policy of the *scheme* or the instruments used by it during the period;
  - (4) the total expense ratio at the end of the period;
  - (5) particulars of any qualification of the reports of the auditor and *depository*; and
  - (6) particulars of any income or distribution relating to the period.

#### **Contents of the annual long report**

- 4.5.7 R (1) An annual long report on an *authorised fund*, other than a *scheme* which is an *umbrella*, must contain:
- (a) the full accounts for the *annual accounting period* which must be prepared in accordance with the requirements of the *IMA SORP*;
  - (b) the report of the *authorised fund manager* in accordance with *COLL 4.5.9R* (Authorised fund manager's report);
  - (c) the comparative table in accordance with *COLL 4.5.10R* (Comparative table);



- (d) the report of the *depository* in accordance with *COLL 4.5.11R* (Report of the depository); and
  - (e) the report of the auditor in accordance with *COLL 4.5.12R* (Report of the auditor).
- (2) An annual long report on a *scheme* which is an *umbrella* must contain:
- (a) for each *sub-fund*:
    - (i) the full accounts for the *annual accounting period* which must be prepared in accordance with the requirements of the *IMA SORP*;
    - (ii) the report of the *authorised fund manager* in accordance with *COLL 4.5.9R*; and
    - (iii) the comparative table in accordance with *COLL 4.5.10R*;
  - (b) the aggregation of the accounts required by (a)(i) for each *sub-fund*;
  - (c) the report of the *depository* in accordance with *COLL 4.5.11R*; and
  - (d) the report of the auditor in accordance with *COLL 4.5.12R*.
- (3) The *directors* of an *ICVC* or the *manager* of an *AUT* must ensure that the accounts referred to in (1)(a) and (2)(a) give a true and fair view of the net income and the net gains and the losses on the *scheme property* of the *authorised fund*, or, in the case of (2)(a), the *sub-fund*, for the *annual accounting period* in question and the financial position of the *authorised fund* or *sub-fund* as at the end of that period.

### **Contents of the half-yearly long report**

- 4.5.8 R (1) A half-yearly long report on an *authorised fund*, other than for a *scheme* which is an *umbrella*, must contain:
- (a) the full accounts for the *half-yearly accounting period* which must be prepared in accordance with the requirements of the *IMA SORP*; and
  - (b) the report of the *authorised fund manager* in accordance with *COLL 4.5.9R* (Authorised fund manager's report).

- (2) A half-yearly long report on a *scheme* which is an *umbrella* must contain:
- (a) for each *sub-fund*:
    - (i) full accounts for the *annual accounting period* which must be prepared in accordance with the requirements of the *IMA SORP*; and
    - (ii) the report of the *authorised fund manager* in accordance with *COLL 4.5.9R*; and
  - (b) the aggregation of the accounts in (a)(i) for each *sub-fund*.

#### **Authorised fund manager's report**

4.5.9 R The matters set out in (1) to (12) must be included in any *authorised fund manager's* report, except where otherwise indicated:

- (1) the names and addresses of :
  - (a) the *authorised fund manager*;
  - (b) the *depository*;
  - (c) the *registrar*;
  - (d) any *investment adviser*;
  - (e) the auditor; and
  - (f) for a *scheme* which invests in immovables, the *standing independent valuer*;
- (2) (for an *ICVC*), the names of any *directors* other than the *ACD*;
- (3) a statement of the authorised status of the *scheme*;
- (4) (for an *ICVC*) a statement that the *unitholders* of the *ICVC* are not liable for the debts of the *ICVC*;
- (5) the investment objectives of the *authorised fund*;
- (6) the policy for achieving those objectives;
- (7) a review of the investment activities during the period to which the report relates;
- (8) particulars of any fundamental changes in accordance with *COLL 4.3.4R* (Fundamental change requiring prior approval by meeting) made since the date of the last report;

- (9) particulars of any significant changes which have occurred in accordance with *COLL* 4.3.6R (Significant change requiring pre-event notification) since the date of the last report;
- (10) any other information which would enable *unitholders* to make an informed judgement on the development of the activities of the *authorised fund* during this period and the results of those activities as at the end of that period;
- (11) for a report on an *umbrella* prepared in accordance with *COLL* 4.5.7R or *COLL* 4.5.8R:
  - (a) a statement to the effect that, as a *sub-fund* is not a legal entity, if the assets attributable to any *sub-fund* were insufficient to meet the liabilities attributable to it, the shortfall might have to be met out of the assets attributable to one or more other *sub-funds* of the *ICVC*; and
  - (b) information required by (1) to (10) must be given for each *sub-fund*, if it would vary from that given in respect of the *umbrella* as a whole; and
- (12) for a *UCITS scheme* which invests a substantial proportion of its assets in other *schemes*, a statement as to the maximum proportion of management fees charged to the *scheme* itself and to other *schemes* in which that *scheme* invests.

### **Comparative table**

- 4.5.10 R The comparative table required by *COLL* 4.5.7R(1)(c) (Contents of the annual long report) must set out:
- (1) a performance record over the last five calendar years, or if the *authorised fund* has not been in existence during the whole of that period, over the whole period in which it has been in existence, showing:
    - (a) the highest and the lowest *price* of a *unit* of each *class* in issue during each of those years; and
    - (b) the net income distributed (or, for *accumulation units*, allocated) for a *unit* of each *class* in issue during each of those years, taking account of any sub-division or consolidation of *units* that

- occurred during that period;
- (2) as at the end of each of the last three *annual accounting periods* (or all of the *authorised fund's annual accounting periods*, if less than three):
    - (a) the total net asset value of the *scheme property* at the end of each of those years;
    - (b) the net asset value per *unit* of each *class*; and
    - (c) (i) (for a report of the *directors* of an *ICVC*) the number of *units* of each *class* in issue; or
      - (ii) (for a report of the *manager* of an *AUT*) the number of *units* of each *class* in existence or treated as in existence; and
  - (3) if, in the period covered by the table:
    - (a) the *authorised fund* has been the subject of any event (such as a *scheme of arrangement*) having a material effect on the size of the *authorised fund*, but excluding any *issue* or *cancellation* of *units* for cash; or
    - (b) there have been changes in the investment objectives of the *authorised fund*;

an indication, related in the body of the table to the relevant year in the table, of the date of the event or change in the investment objectives and a brief description of its nature.

### **Report of the depositary**

- 4.5.11 R (1) The *depositary* must make an annual report to *unitholders* which must be included in the annual report.
- (2) The annual report must contain:
- (a) a description, which may be in summary form, of the duties of the *depositary* under *COLL 6.6.4R* (General duties of the depositary) and in respect of the safekeeping of the *scheme property*; and
  - (b) a statement whether, in any material respect:
    - (i) the *issue*, *sale*, *redemption* and *cancellation*, and calculation of the *price* of the *units* and the application of the *authorised fund's* income, have not been carried out in

accordance with the *rules* in this sourcebook and, where applicable, the *OEIC Regulations* and the *instrument constituting the scheme*; and

- (ii) the investment and borrowing powers and restrictions applicable to the *authorised fund* have been exceeded.

### **Report of the auditor**

4.5.12 R The *authorised fund manager* must ensure that the report of the auditor to the *unitholders* must include a statement:

- (1) whether, in the auditor's opinion, the accounts have been properly prepared in accordance with the *IMA SORP*, the *rules* in this sourcebook, and the *instrument constituting the scheme*;
- (2) whether, in the auditor's opinion, the accounts give a true and fair view of the net income and the net gains or losses of the *scheme property* of the *authorised fund* (or, as the case may be, the *scheme property* attributable to the *sub-fund*) for the *annual accounting period* in question and the financial position of the *authorised fund* or *sub-fund* as at the end of that period;
- (3) whether the auditor is of the opinion that proper accounting records for the *authorised fund* (or, as the case may be, *sub-fund*) have not been kept or whether the accounts are not in agreement with those records;
- (4) whether the auditor has been given all the information and explanations which, to the best of his knowledge and belief, are necessary for the purposes of his audit; and
- (5) whether the auditor is of the opinion that the information given in the report of the *directors* or in the report of the *authorised fund manager* for that period is consistent with the accounts.

### **Provision of short report**

- 4.5.13 R (1) The *authorised fund manager* must, within four *months* after the end of each *annual accounting period* and within two *months* after the end of each *half-yearly accounting period*, respectively provide free of charge the short report in accordance with (2).
- (2) The *authorised fund manager* must send a copy of the report :

- (a) to each *unitholder* (or to the first named of joint *unitholders*) entered in or entitled to be entered in the *register* at the close of business on the last *day* of the relevant accounting period; and
- (b) to each *unitholder* of bearer *units* at his request.

- =
- (3) *Unitholders* in a *scheme* which is an *umbrella* must be provided with a report relating to the particular *sub-fund* in which they hold *units* subject to providing the long report on the *umbrella* on request in accordance with *COLL* 4.5.14R(2)(a).

#### **Publication and availability of annual and half-yearly long report**

- 4.5.14 R (1) The *authorised fund manager* must, within four *months* after the end of each *annual accounting period* and two *months* after the end of each *half-yearly accounting period* respectively, make available and publish the long report prepared in accordance with *COLL* 4.5.7R (Contents of the annual long report) or *COLL* 4.5.8R (Contents of the half-yearly long report).
- (2) The reports referred to in (1) must:
- (a) be supplied free of charge to *unitholders* who request it;
  - (b) be available in English, for inspection by the public free of charge during ordinary office hours at a place specified;
  - (c) for a *UCITS scheme*, be available for inspection by the public at a place designated by the *authorised fund manager* in each *EEA State* other than the *United Kingdom* in which *units* in the *authorised fund* are marketed, in English and in at least one of that other *EEA State's* official languages; and
  - (d) be sent to the *FSA*.

## 5 Investment and borrowing powers

### 5.1 Introduction

#### Application

- 5.1.1 R (1) *COLL 5.1 to COLL 5.5 apply to the authorised fund manager and the depositary of an authorised fund, and to an ICVC, which is or ever has been a UCITS scheme.*
- (2) *COLL 5.1, COLL 5.4 and COLL 5.6 apply to the authorised fund manager and depositary of an authorised fund, and to an ICVC, which is a non-UCITS retail scheme.*
- (3) Paragraph (2) ceases to apply if a *non-UCITS retail scheme* converts to be authorised as a *UCITS scheme*.

#### Purpose

- 5.1.2 G (1) This chapter helps in achieving the *regulatory objective* of protecting *consumers* by laying down minimum standards for the investments that may be held by an *authorised fund*. In particular:
- (a) the proportion of *transferable securities* and *derivatives* that may be held by an *authorised fund* is restricted if those *transferable securities* and *derivatives* are not listed on an *eligible market*; the intention of this is to restrict investment in *transferable securities* or *derivatives* that cannot be accurately valued and readily disposed of; and
- (b) *authorised funds* are required to comply with a number of investment *rules* that require the spreading of risk.
- (2) Table 5.1.4G gives an overview of the permissible investments and maximum investment limits for *UCITS schemes* and *non-UCITS retail schemes*.

#### Treatment of obligations

- 5.1.3 R (1) Where a *rule* in this chapter allows a transaction to be entered into or an investment to be retained only if possible obligations arising out of the transaction or out of the retention would not cause the breach of any limits in this chapter, it must be assumed that the maximum possible liability of the *authorised fund* under any other of those *rules* has also to be provided for.
- (2) Where a *rule* in this chapter permits a transaction to be entered into or an investment to be retained only if that transaction, or the retention, or other similar transactions, are covered:
- (a) it must be assumed that in applying any of those *rules*, the *authorised fund* must also simultaneously satisfy any other obligation relating to cover; and
- (b) no element of cover must be used more than once.

**Indicative overview of investment and borrowing powers**

5.1.4 G This table belongs to *COLL 5.1.2G (2)*.

<i>Scheme investments and investment techniques</i>	<i>Limits for UCITS schemes</i>		<i>Limits for non-UCITS retail schemes</i>	
	<u>Permissible investment</u>	<u>Maximum limit</u>	<u>Permissible investment</u>	<u>Maximum limit</u>
<i>Approved securities</i>	Yes	None	Yes	None
<i>Transferable securities that are not approved securities</i>	Yes	10%	Yes	20%
<i>Government and public securities</i>	Yes	None	Yes	None
<i>Regulated schemes</i>	Yes	None	Yes	None
<i>Unregulated schemes</i>	No	N/A	Yes	20%
<i>Warrants</i>	Yes	None	Yes	None
<i>Investment trusts</i>	Yes	None	Yes	None
<i>Deposits</i>	Yes	None	Yes	None
<i>Derivatives</i>	Yes	None	Yes	None
<i>Immovables (i.e real property)</i>	No	N/A	Yes	None
<i>Gold</i>	No	N/A	Yes	10%
<i>Hedging</i>	Yes	None	Yes	None
<i>Stock lending</i>	Yes	None	Yes	None
<i>Underwriting</i>	Yes	None	Yes	None



Borrowing	Yes	10% (T)	Yes	10%
Cash and <i>near cash</i>	Yes	None	Yes	None
Note:	Meaning of terms used:			
A percentage	an upper limit (though there may be limits of other kinds).			
"(T)"	temporary only- see <i>COLL 5.5.4R(4)</i>			
"N/A"	Not applicable			

## 5.2 General investment powers and limits for UCITS schemes

### Application

- 5.2.1 R This section applies to an *ICVC*, an *ACD*, a *manager* of an *AUT*, a *depository* of an *ICVC* and a *trustee* of an *AUT*, where such *ICVC* or *AUT* is a *UCITS scheme*, in accordance with *COLL 5.2.2R* (Table of application).

### Table of application

- 5.2.2 R This table belongs to *COLL 5.2.1R*.

Rule	<i>ICVC</i>	<i>ACD</i>	<i>Manager of an AUT</i>	<i>Depository of an ICVC</i>	<i>Trustee of an AUT</i>
5.2.3R to 5.2.9R		x	x		
5.2.10R(1)		x	x		
5.2.10R(2)(a)&(b)		x	x		
5.2.10R(2)(c)				x	x
5.2.10R(3)		x	x		
5.2.11R to 5.2.21R		x	x		
5.2.22R	x		x		
5.2.23R(1)	x	x	x		
5.2.23R(2)	x	x	x	x	x
5.2.23R(3)	x	x	x	x	x
5.2.24R		x	x		
5.2.25G		x	x	x	x
5.2.26R		x	x		
5.2.27R	x				
5.2.28R			x		
5.2.29R to 5.2.33R	x	x	x		
Note: x means "applies"					

### Prudent spread of risk

- 5.2.3 R (1) An *authorised fund manager* must ensure that, taking account of the investment objectives and policy of the *UCITS scheme* as stated in the most recently published *prospectus*, the *scheme property* of the *UCITS scheme* aims to provide a prudent spread of risk.
- (2) The *rules* in this section relating to spread of investments do not apply until the expiry of a period of six *months* after the date of which the *authorisation order*, in respect of the *UCITS scheme*,

takes effect or on which the *initial offer* commenced, if later, provided that (1) is complied with during such period.

**Investment powers: general**

- 5.2.4 R The *scheme property* of each *UCITS scheme* must be invested only in accordance with the relevant provisions in sections *COLL 5.2* to *COLL 5.5* that are applicable to that *UCITS scheme* and up to any maximum limit so stated, but, the *instrument constituting the scheme* may further restrict:
- (1) the kind of property in which the *scheme property* may be invested;
  - (2) the proportion of the *capital property* of the *UCITS scheme* be invested in assets of any description;
  - (3) the descriptions of transactions permitted; and
  - (4) the borrowing powers of the *UCITS scheme*.

**Valuation**

- 5.2.5 R (1) In this chapter, the value of the *scheme property* of a *UCITS scheme* means the net value determined in accordance with *COLL 6.3* (Valuation and pricing), after deducting any outstanding borrowings, whether immediately due to be repaid or not.
- (2) When valuing the *scheme property* for the purposes of this chapter:
- (a) the time as at which the valuation is being carried out ("the relevant time") is treated as if it were a *valuation point*, but the valuation and the relevant time do not count as a valuation or a *valuation point* for the purposes of *COLL 6.3* (Valuation and pricing);
  - (b) *initial outlay* is to be regarded as remaining part of the *scheme property*; and
  - (c) if the *authorised fund manager*, having taken reasonable care, determines that the *UCITS scheme* will become entitled to any unrealised profit which has been made on account of a transaction in *derivatives*, that prospective entitlement is to be regarded as part of the *scheme property*.

**Valuation guidance**

- 5.2.6 G It should be noted that for the purpose of *COLL 5.2.5R*, *COLL 6.3* may

be affected by specific provisions in this chapter such as, for example, *COLL* 5.4.6R (Treatment of collateral).

**Transferable securities**

- 5.2.7 R (1) A *transferable security* is an *investment* which is any of the following:
- (a) a *share*;
  - (b) a *debenture*;
  - (c) a *government and public security*;
  - (d) a *warrant*; or
  - (e) a *certificate representing certain securities*.
- (2) An *investment* is not a *transferable security* if the title to it cannot be transferred, or can be transferred only with the consent of a third party.
- (3) In applying (2) to an *investment* which is issued by a *body corporate*, and which is a *share* or a *debenture*, the need for any consent on the part of the *body corporate* or any members or *debenture* holders of it may be ignored.
- (4) An *investment* is not a *transferable security* unless the liability of the holder of it to contribute to the debts of the issuer is limited to any amount for the time being unpaid by the holder of it in respect of the *investment*.

**UCITS schemes: general**

- 5.2.8 R (1) The *scheme property* of a *UCITS scheme* must, except where otherwise provided in the *rules* in this chapter, consist only of any or all of:
- (a) *transferable securities*;
  - (b) *units* in *collective investment schemes* permitted under *COLL* 5.2.13R (Investment in collective investment schemes);
  - (c) approved money-market instruments permitted under *COLL* 5.2.18R (Investment in money-market instruments);
  - (d) *derivatives* and forward transactions permitted under *COLL* 5.2.20R (Permitted transactions (derivatives and forwards));
- and

- (e) *deposits* permitted under *COLL 5.2.26R* (Investment in deposits).
- (2) For an *ICVC* the *scheme property* may also include movable and immovable property that is necessary for the direct pursuit of the *ICVC's* business.
- (3) *Transferable securities* and money-market instruments held within a *UCITS scheme* must be;
  - (a) admitted to or *dealt* in on an *eligible* market within *COLL 5.2.10R(1)(a)* (Eligible markets: requirements); or
  - (b) *dealt* in on an *eligible* market within *COLL 5.2.10R(1)(b)*; or
  - (c) admitted to or *dealt* in on an *eligible* market within *COLL 5.2.10R(2)*; or
  - (d) for a money-market instrument, within *COLL 5.2.18R(2)*.
- (4) Not more than 10% in value of the *scheme property* of a *UCITS scheme* is to consist of *transferable securities*, which do not fall within (3) or of money-market instruments, which do not fall within *COLL 5.2.18R(2)*.

**Eligible markets regime: purpose**

- 5.2.9 G (1) This section specifies criteria based on those in article 19 of the *UCITS Directive*, as to the nature of the markets in which the property of a *UCITS scheme* may be invested.
- (2) Where a market ceases to be *eligible*, *investments* on that market cease to be *approved securities*. The 10% restriction in *COLL 5.2.8R(4)* applies, and exceeding this limit because a market ceases to be *eligible* will generally be regarded as a breach beyond the control of the *authorised fund manager*.

**Eligible markets: requirements**

- 5.2.10 R (1) A market is *eligible* for the purposes of the *rules* in this sourcebook if it is:
- (a) a *regulated market*;
  - (b) a market in an *EEA State* which is regulated, operates regularly and is open to the public; or
  - (c) any market within (2).

- (2) A market not falling within (1)(a) and (b) is *eligible* for the purposes of the *rules* in this sourcebook if:
  - (a) the *authorised fund manager*, after consultation with and notification to the *depository* (and in the case of an *ICVC*, any other *directors*), decides that market is appropriate for investment of, or *dealing in*, the *scheme property*;
  - (b) the market is included in a list in the *prospectus*; and
  - (c) the *depository* has taken reasonable care to determine that:
    - (i) adequate custody arrangements can be provided for the *investment dealt in* on that market; and
    - (ii) all reasonable steps have been taken by the *authorised fund manager* in deciding whether that market is *eligible*.
- (3) In (2)(a), a market must not be considered appropriate unless it:
  - (a) is regulated;
  - (b) operates regularly;
  - (c) is recognised as a market or exchange or as a self-regulating organisation by an *overseas regulator*;
  - (d) is open to the public;
  - (e) is adequately liquid; and
  - (f) has adequate arrangements for unimpeded transmission of income and capital to or to the order of investors.

**Spread: general**

- 5.2.11 R (1) This *rule* does not apply to *government and public securities*.
- (2) For the purposes of this *rule* companies included in the same group for the purposes of consolidated accounts as defined in accordance with the Seventh Council Directive 83/349/EEC of 13 June 1983 based on Article 54(3)(g) of the Treaty on consolidated accounts or, in the same group in accordance with international accounting standards, are regarded as a single body.
- (3) Not more than 20% in value of the *scheme property* is to consist of *deposits* with a single body.
- (4) Not more than 5% in value of the *scheme property* is to consist of

*transferable securities* or money-market instruments issued by any single body.

- (5) The limit of 5% in (4) is raised to 10% in respect of up to 40% in value of the *scheme property*.
- (6) In applying (4) and (5), *certificates representing certain securities* are to be treated as equivalent to the underlying *security*.
- (7) The exposure to any one counterparty in an *OTC derivative* transaction must not exceed 5% in value of the *scheme property*; this limit being raised to 10% where the counterparty is an *approved bank*.
- (8) Not more than 20% in value of the *scheme property* is to consist of *transferable securities* and money-market instruments issued by the same group (as referred to in (2)).
- (9) Not more than 20% in value of the *scheme* is to consist of the *units* of any one *collective investment scheme*.
- (10) In applying the limits in (3),(4),(5), (6) and (7), not more than 20% in value of the *scheme property* is to consist of any combination of two or more of the following:
  - (a) *transferable securities* or money-market instruments issued by; or
  - (b) *deposits* made with; or
  - (c) exposures from *OTC derivatives* transactions made with; a single body.

**Spread: government and public securities**

- 5.2.12 R (1) This *rule* applies to *government and public securities* (“such *securities*”).
- (2) Where no more than 35% in value of the *scheme property* is invested in such *securities* issued by any one body, there is no limit on the amount which may be invested in such *securities* or in any one issue.
  - (3) An *authorised fund* may invest more than 35% in value of the *scheme property* in such *securities* issued by any one body provided that:

- (a) the *authorised fund manager* has before any such investment is made consulted with the *depository* and as a result considers that the issuer of such *securities* is one which is appropriate in accordance with the investment objectives of the *authorised fund*;
  - (b) no more than 30% in value of the *scheme property* consists of such *securities* of any one issue;
  - (c) the *scheme property* includes such *securities* issued by that or another issuer, of at least six different issues; and
  - (d) the disclosures in (4) have been made.
- (4) Where it is intended that (3) may apply, the *instrument constituting the scheme*, and the most recently published *prospectus*, must prominently state:
- (a) the fact that more than 35% of the *scheme property* is or may be invested in such *securities* issued by one issuer; and
  - (b) the names of the individual states, the local authorities or public international bodies issuing such *securities* in which the *authorised fund* may invest over 35% of its assets.
- (5) In this *rule* in relation to such *securities*:
- (a) issue, issued and issuer include guarantee, guaranteed and guarantor; and
  - (b) an issue differs from another if there is a difference as to repayment date, rate of interest, guarantor or other material terms of the issue.

#### **Investment in collective investment schemes**

- 5.2.13 R A *UCITS scheme* must not invest in *units* in a *collective investment scheme* (“second *scheme*”) unless the second *scheme* satisfies all of the following conditions, and provided that no more than 30% of the value of the *UCITS scheme* is invested in second *schemes* within(1)(b) to (d):
- (1) the second *scheme* must:
    - (a) satisfy the conditions necessary for it to enjoy the rights conferred by the *UCITS Directive*; or



- (b) be recognised under the provisions of section 270 of the *Act* (Schemes authorised in designated countries or territories); or
  - (c) be authorised as a *non-UCITS retail scheme* (provided the requirements of article 19(1)(e) of the *UCITS Directive* are met); or
  - (d) be authorised in another *EEA State* (provided the requirements of article 19(1)(e) of the *UCITS Directive* are met);
- (2) the second *scheme* must comply, where relevant, with *COLL* 5.2.15R (Investment in associated collective investment schemes) and *COLL* 5.2.16R (Investment in other group schemes); and
  - (3) the second *scheme* must have terms which prohibit more than 10% in value of the *scheme property* consisting of *units* in *collective investment schemes*.

**Qualifying non-UCITS collective investment schemes**

- 5.2.14 G (1) *COLL* 9.3 gives further detail as to the recognition of a *scheme* under section 270 of the *Act*.
- (2) Article 19 of the *UCITS Directive* sets out the general investment limits. So, a *non-UCITS retail scheme*, or its equivalent *EEA scheme* which has the power to invest in gold or immovables would not meet the criteria set in *COLL* 5.2.13R(1)(c) and (d).

**Investment in associated collective investment schemes**

- 5.2.15 R A *UCITS scheme* must not invest in or dispose of *units* in another *collective investment scheme* (the second *scheme*) if the second *scheme* is managed or operated by (or, for an *ICVC*, whose *ACD* is) the *authorised fund manager* of the investing *UCITS scheme* or an *associate* of that *authorised fund manager*, unless:
- (1) the *prospectus* of the investing *UCITS scheme* clearly states that the property of that investing *scheme* may include such *units*; and
  - (2) *COLL* 5.2.16R (Investment in other group schemes) is complied with.

**Investment in other group schemes**

- 5.2.16 R (1) Where:

- (a) an investment or disposal is made under *COLL* 5.2.15R; and
  - (b) there is a charge in respect of such investment or disposal;
- the *authorised fund manager* of the *UCITS scheme* making the investment or disposal must pay the *UCITS scheme* the amounts referred to in (2) or (3) within four *business days* following the date of the agreement to invest or dispose.
- (2) When an investment is made, the amount referred to in (1)(a) is either:
    - (a) any amount by which the consideration paid by the *UCITS scheme* for the *units* in the second *scheme* exceeds the price that would have been paid for the benefit of the second *scheme* had the *units* been newly issued or sold by it; or
    - (b) if such price cannot be ascertained by the *authorised fund manager* of the *authorised fund*, the maximum amount of any charge permitted to be made by the seller of *units* in the second *scheme*.
  - (3) When a disposal is made, the amount referred to in (1)(a) is any charge made for the account of the *authorised fund manager* or *operator* of the second *scheme* or an *associate* of any of them in respect of the disposal.
  - (4) In this *rule*:
    - (a) any addition to or deduction from the consideration paid on the acquisition or disposal of *units* in the second *scheme*, which is applied for the benefit of the second *scheme* and is, or is like, a *dilution levy* made in accordance with *COLL* 6.3.8R (Dilution) or *SDRT provision* made in accordance with *COLL* 6.3.7 (SDRT provision) is to be treated as part of the *price* of the *units* and not as part of any charge; and
    - (b) any charge made in respect of an exchange of *units* in one *sub-fund* or separate part of the second *scheme* for *units* in another *sub-fund* or separate part of that *scheme* is to be included as part of the consideration paid for the *units*.

**Investment in warrants and nil and partly paid securities**

- 5.2.17 R (1) Where a *UCITS scheme* invests in a *warrant*, the exposure created by the exercise of the right conferred by that *warrant* must not exceed the limits in *COLL 5.2.11R* (Spread: general) and *COLL 5.2.12R* (Spread: government and public securities).
- (2) A *transferable security* or a money-market instrument on which any sum is unpaid falls within a power of investment only if it is reasonably foreseeable that the amount of any existing and potential call for any sum unpaid could be paid by the *UCITS scheme*, at the time when payment is required, without contravening the *rules* in this chapter.

**Investment in money-market instruments**

- 5.2.18 R A *UCITS scheme* may invest in money-market instruments which are normally dealt in on the money market, are liquid and whose value can be accurately determined at any time, provided the money-market instrument is:
- (1) within *COLL 5.2.8R(3)*(UCITS schemes: general); or
- (2) a money-market instrument issued or guaranteed by:
- (a) a central, regional or local authority or central bank of an *EEA State*, the European Central Bank, the European Union or the European Investment Bank, a non-*EEA State* or, in the case of a federal state, by one of the members making up the federation, or by a public international body to which one or more *EEA States* belong; or
- (b) an establishment subject to prudential supervision in accordance with criteria defined by Community law or an establishment which is subject to and complies with prudential rules considered by the *FSA* to be at least as stringent as those laid down by Community law; or
- (3) issued by a body, any *securities* of which are *dealt* in on an *eligible* market.

**Derivatives: general**

- 5.2.19 R (1) A transaction in *derivatives* or a forward transaction must not be effected for a *UCITS scheme* unless:

- (a) the transaction is of a kind specified in *COLL 5.2.20R* (Permitted transactions (derivatives and forwards)); and
  - (b) the transaction is covered, as required by *COLL 5.3.3R* (Cover for transactions in derivatives and forward transactions).
- (2) Where a *UCITS scheme* invests in *derivatives*, the exposure to the underlying assets must not exceed the limits in *COLL 5.2.11R* (Spread: general) and *COLL 5.2.12R* (Spread: government and public securities) save as provided in (4).
  - (3) Where a *transferable security* or money-market instrument embeds a *derivative*, this must be taken into account for the purposes of complying with this section.
  - (4) Where a *scheme* invests in an index based *derivative*, provided the relevant index falls within *COLL 5.2.33R* (Relevant indices) the underlying constituents of the index do not have to be taken into account for the purposes of *COLL 5.2.11R* and *COLL 5.2.12R*.
  - (5) The relaxation in (4) is subject to the *authorised fund manager* taking account of *COLL 5.2.3R* (Prudent spread of risk).

**Permitted transactions (derivatives and forwards)**

- 5.2.20 R (1) A transaction in a *derivative* must:
- (a) be in an *approved derivative*; or
  - (b) be one which complies with *COLL 5.2.23R* (OTC transactions in derivatives).
- (2) The underlying of a transaction in a *derivative* must consist of any one or more of the following to which the *scheme* is *dedicated*:
- (a) *transferable securities*;
  - (b) money-market instruments permitted under *COLL 5.2.18R* (Investment in money-market instruments);
  - (c) *deposits* permitted under *COLL 5.2.26R* (Investment in deposits);
  - (d) *derivatives* permitted under this *rule*;
  - (e) *collective investment scheme units* permitted under *COLL 5.2.13R* (Investment in collective investment

- schemes);
  - (f) financial indices;
  - (g) interest rates;
  - (h) foreign exchange rates; and
  - (i) currencies.
- (3) A transaction in an *approved derivative* must be effected on or under the rules of an *eligible derivatives* market.
  - (4) A transaction in a *derivative* must not cause a *scheme* to diverge from its investment objectives as stated in the *instrument constituting the scheme* and the most recently published *prospectus*.
  - (5) A transaction in a *derivative* must not be entered into if the intended effect is to create the potential for an uncovered sale of one or more *transferable securities*, money-market instruments, *units* in *collective investment schemes* or *derivatives*.
  - (6) Any forward transaction must be made with an *eligible institution* or an *approved bank*.

#### **Transactions for the purchase of property**

- 5.2.21 R A *derivative* or forward transaction which will or could lead to the delivery of property for the account of the *UCITS scheme* may be entered into only if:
- (1) that property can be held for the account of the *UCITS scheme*;
  - and
  - (2) the *authorised fund manager* having taken reasonable care determines that delivery of the property under the transaction will not occur or will not lead to a breach of the *rules* in this sourcebook.

#### **Requirement to cover sales**

- 5.2.22 R (1) No agreement by or on behalf of a *UCITS scheme* to dispose of property or rights may be made unless:

- (a) the obligation to make the disposal and any other similar obligation could immediately be honoured by the *UCITS scheme* by delivery of property or the assignment (or, in Scotland, assignation) of rights; and
  - (b) the property and rights at (a) are owned by the *UCITS scheme* at the time of the agreement.
- (2) Paragraph (1) does not apply to a *deposit*.

**OTC transactions in derivatives**

5.2.23 R A transaction in an *OTC derivative* under *COLL 5.2.20R(1)(b)* must be:

- (1) with an approved counterparty; a counterparty to a transaction in *derivatives* is approved only if the counterparty is:
  - (a) an *eligible institution* or an *approved bank*; or
  - (b) a *person* whose *permission* (including any *requirements* or *limitations*), as published in the *FSA Register*, or whose *Home State authorisation*, permits it to enter into the transaction as *principal off-exchange*;
- (2) on approved terms; the terms of the transaction in *derivatives* are approved only if, before the transaction is entered into, the *depository* is satisfied that the counterparty has agreed with the *ICVC* or the *authorised fund manager*:
  - (a) to provide a reliable and verifiable valuation in respect of that transaction at least daily and at any other time at the request of the *ICVC* or *authorised fund manager*; and
  - (b) that it will, at the request of the *ICVC* or *authorised fund manager*, enter into a further transaction to *close out* that transaction at any time, at a fair value arrived at under the pricing model or other reliable basis agreed under (3); and
- (3) capable of valuation; a transaction in *derivatives* is capable of valuation only if the *authorised fund manager* having taken reasonable care determines that, throughout the life of the *derivative* (if the transaction is entered into), it will be able to value the *investment* concerned with reasonable accuracy:

- (a) on the basis of the pricing model which has been agreed between the *authorised fund manager* and the *depository*; or
- (b) on some other reliable basis reflecting an up-to-date market value which has been so agreed.

**Risk management: derivatives**

- 5.2.24 R (1) An *authorised fund manager* must use a risk management process enabling it to monitor and measure as frequently as appropriate the risk of a *scheme's derivatives* and forwards positions and their contribution to the overall risk profile of the *scheme*.
- (2) The following details of the risk management process must be notified by the *authorised fund manager* to the *FSA* in advance of the use of the process as required by (1):
- (a) the methods for estimating risks in *derivative* and forward transactions; and
  - (b) the types of *derivatives* and forwards to be used within the *scheme* together with their underlying risks and any relevant quantitative limits.
- (3) The *authorised fund manager* must notify the *FSA* in advance of any material alteration to the details in (2)(a) or (b).

**Risk management process**

- 5.2.25 G (1) The risk management process should take account of the investment objectives and policy of the *scheme* as stated in the most recent *prospectus*.
- (2) The *depository* should take reasonable care to review the appropriateness of the risk management process in line with its duties under *COLL* 6.6.14R (Duties of the depository and authorised fund manager: investment and borrowing powers), as appropriate.

- (3) An *authorised fund manager* is expected to demonstrate more sophistication in its risk management process for a *scheme* with a complex risk profile than for one with a simple risk profile. In particular, the risk management process should take account of any characteristic of non-linear dependence in the value of a position to its underlying.
- (4) An *authorised fund manager* should take reasonable care to establish and maintain such systems and controls as are appropriate to its business as required by SYSC 3.1 (Systems and controls).
- (5) The risk management process should enable the analysis required by COLL 5.2.24R to be undertaken at least daily or at each *valuation point* whichever is the more frequent.

#### **Investment in deposits**

5.2.26 R A *UCITS scheme* may invest in *deposits* only if it:

- (1) is with an *approved bank*;
- (2) is:
  - (a) repayable on demand; or
  - (b) has the right to be withdrawn; and
- (3) matures in no more than 12 *months*.

#### **Significant influence for ICVCs**

- 5.2.27 R (1) An *ICVC* must not acquire *transferable securities* issued by a *body corporate* and carrying rights to vote (whether or not on substantially all matters) at a general meeting of that *body corporate* if:
- (a) immediately before the acquisition, the aggregate of any such *securities* held by the *ICVC* gives the *ICVC* power to influence significantly the conduct of business of that *body corporate*; or
  - (b) the acquisition gives the *ICVC* that power.



- (2) For the purpose of (1), an *ICVC* is to be taken to have power significantly to influence the conduct of business of a *body corporate* if it can, because of the *transferable securities* held by it, exercise or control the exercise of 20% or more of the voting rights in that *body corporate* (disregarding for this purpose any temporary suspension of voting rights in respect of the *transferable securities* of that *body corporate*).

#### **Significant influence for managers of AUTs**

- 5.2.28 R (1) A *manager* must not acquire, or cause to be acquired for an *AUT* of which it is the *manager*, *transferable securities* issued by a *body corporate* and carrying rights to vote (whether or not on substantially all matters) at a general meeting of the *body corporate* if:
- (a) immediately before the acquisition, the aggregate of any such *securities* held for that *AUT*, taken together with any such *securities* already held for other *AUTs* of which it is also the *manager*, gives the *manager* power significantly to influence the conduct of business of that *body corporate*; or
  - (b) the acquisition gives the *manager* that power.
- (2) For the purpose of (1), a *manager* is to be taken to have power significantly to influence the conduct of business of a *body corporate* if it can, because of the *transferable securities* held for all the *AUTs* of which it is the *manager*, exercise or control the exercise of 20% or more of the voting rights in that *body corporate* (disregarding for this purpose any temporary suspension of voting rights in respect of the *transferable securities* of that *body corporate*).

#### **Concentration**

- 5.2.29 R A *UCITS scheme*:
- (1) must not acquire *transferable securities* (other than *debt securities*) which:
    - (a) do not carry a right to vote on any matter at a general meeting of the *body corporate* that issued them; and

- (b) represent more than 10% of those *securities* issued by that *body corporate*;
- (2) must not acquire more than 10% of the *debt securities* issued by any single body;
- (3) must not acquire more than 25% of the *units* in a *collective investment scheme*;
- (4) must not acquire more than 10% of the money-market instruments issued by any single body; and
- (5) need not comply with the limits in (2), (3) and (4) if, at the time of acquisition, the net amount in issue of the relevant *investment* cannot be calculated.

#### **UCITS schemes that are umbrellas**

- 5.2.30 R (1) In relation to a *UCITS scheme* which is an *umbrella*, the provisions in *COLL 5.2* to *COLL 5.5* apply to each *sub-fund* as they would for an *authorised fund*, except the following *rules* which apply at the level of the *umbrella* only:
- (a) *COLL 5.2.27R* (Significant influence for ICVCs);
  - (b) *COLL 5.2.28R* (Significant influence for managers of AUTs); and
  - (c) *COLL 5.2.29R* (Concentration).
- (2) A *sub-fund* must not invest in another *sub-fund* of the same *umbrella*.

#### **Schemes replicating an index**

- 5.2.31 R (1) A *UCITS scheme* may invest up to 20% in value of the *scheme property* in *shares* and *debentures* which are issued by the same body where the investment policy of that *scheme* as stated in the most recently published *prospectus* is to replicate the composition of a relevant index which satisfies the criteria specified in *COLL 5.2.33R* (Relevant indices).
- (2) The limit in (1) can be raised for a particular *UCITS scheme* up to 35% in value of the *scheme property*, but only in respect of one body and where justified by exceptional market conditions.

#### **Index replication**

- 5.2.32 G In the case of a *UCITS scheme* replicating an index under *COLL 5.2.31R* (Schemes replicating an index) the *scheme property* need not consist of the exact composition and weighting of the underlying in the relevant index where deviation from this is expedient for reasons of poor liquidity or excessive cost to the *scheme* in trading in an underlying *investment*.

**Relevant indices**

- 5.2.33 R The indices referred to in *COLL 5.2.31R* are those which satisfy the following criteria:
- (1) the composition is sufficiently diversified;
  - (2) the index is a representative benchmark for the market to which it refers; and
  - (3) the index is published in an appropriate manner.

## **Derivative exposure**

### **Application**

- 5.3.1 R This section applies to an *authorised fund manager* of a *UCITS scheme* and to an *ICVC* which is a *UCITS scheme*.

### **Introduction**

- 5.3.2 G (1) A *scheme* may invest in *derivatives* and forward transactions as long as the exposure to which the *scheme* is committed by that transaction itself is suitably covered from within its *scheme property*. Exposure will include any *initial outlay* in respect of that transaction.
- (2) Cover ensures that a *scheme* is not exposed to the risk of loss of property, including *money*, to an extent greater than the net value of the *scheme property*. Therefore, a *scheme* is required to hold *scheme property* sufficient in value or amount to match the exposure arising from a *derivative* obligation to which the *scheme* is committed. *COLL 5.3.3R* (Cover for transactions in derivatives and forward transactions) sets out detailed requirements for cover of a *scheme*.
- (3) In accordance with *COLL 5.1.3R(2)(b)* (Treatment of obligations), cover used in respect of one transaction in *derivatives* or forward transaction should not be used for cover in respect of another transaction in *derivatives* or a forward transaction.

### **Cover for transactions in derivatives and forward transactions**

- 5.3.3 R (1) A transaction in *derivatives* or forward transaction may be entered into only if the maximum exposure, in terms of the *principal* or *notional principal* created by the transaction to which the *scheme* is or may be committed by another *person*, is covered globally under (2).
- (2) Exposure is covered globally if adequate cover from within the *scheme property* is available to meet the *scheme's* total exposure, taking into account the value of the underlying assets, any reasonably foreseeable market movement,

counterparty risk, and the time available to liquidate any positions.

- (3) Cash not yet received into the *scheme property* but due to be received within one *month* is available as cover for the purposes of (2).
- (4) Property the subject of a transaction under *COLL* 5.4 (Stock lending) is only available for cover if the *authorised fund manager* has taken reasonable care to determine that it is obtainable (by return or re-acquisition) in time to meet the obligation for which cover is required.
- (5) The total exposure relating to *derivatives* held in a *UCITS scheme* may not exceed the net value of the *scheme property*.

#### **Guidance on cover**

- 5.3.4 G An *authorised fund manager* should note that the scope of *COLL* 5.3.3R is extended in relation to underwriting commitments by *COLL* 5.5.8R(4) (General power to accept or underwrite placings).

#### **Borrowing**

- 5.3.5 R (1) Cash obtained from borrowing, and borrowing which the *authorised fund manager* reasonably regards an *eligible institution* or an *approved bank* to be committed to provide, is not available for cover under *COLL* 5.3.3R (Cover for transactions in derivatives and forward transactions), except if (2) applies.
- (2) Where, for the purposes of this section, the *ICVC* or the *trustee* for the account of the *AUT* on the instructions of the *manager*:
- (a) borrows an amount of currency from an *eligible institution* or an *approved bank*; and
  - (b) keeps an amount in another currency, at least equal to the borrowing for the time being in (a), on *deposit* with the lender (or his agent or nominee);
- then this section applies as if the borrowed currency, and not the deposited currency, were part of the *scheme property*.

#### **Continuing nature of limits and requirements**

- 5.3.6 R (1) An *authorised fund manager* must, (as frequently as necessary), re-calculate the amount of cover required in respect of *derivatives* and forward positions already in existence under this section.
- (2) *Derivatives* and rights under forward transactions may be retained in the *scheme property* only so long as they remain covered globally under *COLL 5.3.3R*.

## 5.4 Stock lending

### Application

- 5.4.1 R (1) This section applies to a *depository* of an *authorised fund* which is a *UCITS scheme* or a *non-UCITS retail scheme*.
- (2) *COLL 5.4.3R* (Stock lending: general) also applies to:
- (a) an *ICVC* which is a *UCITS scheme* or a *non-UCITS retail scheme*; and
  - (b) a *manager* of an *AUT* which is a *UCITS scheme* or a *non-UCITS retail scheme*.
- (3) *COLL 5.4.4R* (Stock lending: requirements) also applies to an *ICVC* which is a *UCITS scheme* or a *non-UCITS retail scheme*.

### Permitted stock lending

- 5.4.2 G (1) This section permits the generation of additional income for the benefit of the *authorised fund*, and hence for its investors, by entry into *stock lending* transactions for the account of the *authorised fund*.
- (2) The specific method of *stock lending* permitted in this section is in fact not a transaction which is a loan in the normal sense. Rather it is an arrangement of the kind described in section 263B of the Taxation of Chargeable Gains Act 1992, under which the lender transfers *securities* to the borrower otherwise than by way of *sale* and the borrower is to transfer those *securities*, or *securities* of the same type and amount, back to the lender at a later date. In accordance with good market practice, a separate transaction by way of transfer of assets is also involved for the purpose of providing *collateral* to the "lender" to cover him against the risk that the future transfer back of the *securities* may not be satisfactorily completed.

### Stock lending: general

- 5.4.3 R The *stock lending* permitted by this section may be exercised by an *authorised fund* when it reasonably appears to the *ICVC* or to the *manager* to be appropriate to do so with a view to generating additional income for the *authorised fund* with an acceptable degree of risk.

**Stock lending: requirements**

- 5.4.4 R (1) An *ICVC*, or the *depository* at the request of the *ICVC*, or the *trustee* at the request of the *manager*, may enter into a *stock lending* arrangement of the kind described in section 263B of the Taxation of Chargeable Gains Act 1992 (without extension by section 263C), but only if:
- (a) all the terms of the agreement under which *securities* are to be reacquired by the *depository* for the account of the *ICVC* or by the *trustee*, are in a form which is acceptable to the *depository* or to the *trustee* and are in accordance with good market practice;
  - (b) the counterparty is an *authorised person* or a *person* authorised by a *Home State regulator*; and
  - (c) *collateral* is obtained to secure the obligation of the counterparty under the terms referred to in (a) and the *collateral* is:
    - (i) acceptable to the *depository*;
    - (ii) adequate within *COLL 5.4.6R(1)*; and
    - (iii) sufficiently immediate within *COLL 5.4.6R(2)*.
- (2) The counterparty for the purpose of (1) is the *person* who is obliged under the agreement referred to in (1)(a) to transfer to the *depository* the *securities* transferred by the *depository* under the *stock lending* arrangement or *securities* of the same kind.

**Stock lending: treatment of collateral**

- 5.4.5 G Where a *stock lending* arrangement is entered into, the *scheme property* remains unchanged in terms of value. The *securities* transferred cease to be part of the *scheme property*, but there is



obtained in return an obligation on the part of the counterparty to transfer back equivalent *securities*. The *depository* will also receive *collateral* to set against the risk of default in transfer, and that *collateral* is equally irrelevant to the valuation of the *scheme property* (because it is transferred against an obligation of equivalent value by way of re-transfer). *COLL 5.4.6R* accordingly makes provision for the treatment of the *collateral* in that context.

#### **Treatment of collateral**

- 5.4.6 R (1) *Collateral* is adequate for the purposes of this section only if it is:
- (a) transferred to the *depository* or its agent;
  - (b) at least equal in value, at the time of the transfer to the *depository*, to the value of the *securities* transferred by the *depository*; and
  - (c) in the form of one or more of:
    - (i) cash; or
    - (ii) *government and public securities*; or
    - (iii) a certificate of *deposit*; or
    - (iv) a letter of *credit*; or
    - (v) a *readily realisable security*.
- (2) *Collateral* is sufficiently immediate for the purposes of this section if:
- (a) it is transferred before or at the time of the transfer of the *securities* by the *depository*; or
  - (b) the *depository* takes reasonable care to determine at the time referred to in (a) that it will be transferred at the latest by the close of business on the *day* of the transfer.
- (3) The *depository* must ensure that the value of the *collateral* at all times is at least equal to the value of the *securities* transferred by the *depository*.
- (4) The duty in (3) may be regarded as satisfied in respect of *collateral* the validity of which is about to expire or has expired where the *depository* takes reasonable care to

determine that sufficient *collateral* will again be transferred at the latest by the close of business on the *day* of expiry.

- (5) Any agreement for transfer at a future date of *securities* or of *collateral* (or of the equivalent of either) under this section may be regarded, for the purposes of valuation under *COLL* 6.3 (Valuation and pricing) or this chapter, as an unconditional agreement for the *sale* or transfer of property, whether or not the property is part of the property of the *authorised fund*.
- (6) *Collateral* transferred to the *depository* is part of the *scheme property* for the purposes of the *rules* in this sourcebook, except in the following respects:
  - (a) it does not fall to be included in any valuation for the purposes of *COLL* 6.3 or this chapter, because it is offset under (5) by an obligation to transfer; and
  - (b) it does not count as *scheme property* for any purpose of this chapter other than this section.
- (7) Paragraph (5) and (6)(a) do not apply to any valuation of *collateral* itself for the purposes of this section.

**Limitation by value**

- 5.4.7 R There is no limit on the value of the *scheme property* which may be the subject of *stock lending* transactions within this section.

## 5.5 Cash, borrowing, lending and other provisions

### Application

- 5.5.1 R This section applies to an *ICVC*, an *ACD*, a *manager* of an *AUT*, a *depository* of an *ICVC* and a *trustee* of an *AUT*, where such *ICVC* or *AUT* is a *UCITS scheme* as set out in *COLL 5.5.2R* (Table of application).

### Table of application

- 5.5.2 R This table belongs to *COLL 5.5.1R*.

Rule	<i>ICVC</i>	<i>ACD</i>	<i>Manager of an AUT</i>	<i>Depository of an ICVC</i>	<i>Trustee of an AUT</i>
5.5.3R		x	x		
5.5.4R(1) to (3)	x				x
5.5.4R(4)&(5)		x	x		
5.5.4R(6)				x	x
5.5.4R(7)	x	x	x	x	x
5.5.4R(8)	x				
5.5.5R(1) to (3)		x	x		
5.5.5R(4)	x	x			
5.5.6R(1)&(2)	x		x		x
5.5.6R(3)	x				
5.5.7R(1)-(3)	x		x		x
5.5.7R(4)	x			x	x
5.5.8R	x	x	x		
5.5.9R	x			x	x
5.5.10G	x	x	x	x	x
Note: x means "applies"					

### Cash and near cash

- 5.5.3 R (1) Cash and *near cash* must not be retained in the *scheme property* except to the extent that this may reasonably be regarded as necessary in order to enable:
- (a) the pursuit of the *scheme's* investment objectives; or
  - (b) *redemption* of *units*; or
  - (c) efficient management of the *authorised fund* in accordance with its investment objectives; or

- (d) other purposes which may reasonably be regarded as ancillary to the investment objectives of the *authorised fund*.
- (2) During the period of the *initial offer* the *scheme property* may consist of cash and *near cash* without limitation.

**General power to borrow**

- 5.5.4 R (1) The *ICVC* or *trustee* (on the instructions of the *manager*) may, in accordance with this *rule* and *COLL 5.5.5R* (Borrowing limits), borrow *money* for the use of the *authorised fund* on terms that the borrowing is to be repayable out of the *scheme property*.
- (2) Paragraph (1) is subject to the obligation of the *authorised fund* to comply with any restriction in the *instrument constituting the scheme*.
  - (3) The *ICVC* or *trustee* may borrow under (1) only from an *eligible institution* or an *approved bank*.
  - (4) The *authorised fund manager* must ensure that any borrowing is on a temporary basis and that borrowings are not persistent, and for this purpose the *authorised fund manager* must have regard in particular to:
    - (a) the duration of any period of borrowing; and
    - (b) the number of occasions on which resort is had to borrowing in any period.
  - (5) In addition to complying with (4), the *authorised fund manager* must ensure that no period of borrowing exceeds three *months*, whether in respect of any specific sum or at all, without the prior consent of the *depository*.
  - (6) The *depository* may only give its consent as required under (5) on such conditions as appear to the *depository* appropriate to ensure that the borrowing does not cease to be on a temporary basis only.
  - (7) This *rule* does not apply to "back to back" borrowing under

*COLL 5.3.5R(2)* (Borrowing).

- (8) An *ICVC* must not issue any *debenture* unless it acknowledges or creates a borrowing that complies with (1) to (6)

**Borrowing limits**

- 5.5.5 R (1) The *authorised fund manager* must ensure that the *authorised fund's* borrowing does not, on any *day*, exceed 10% of the value of the *scheme property*.
- (2) This *rule* does not apply to "back to back" borrowing under *COLL 5.3.5R(2)*(Borrowing).
- (3) In this *rule*, borrowing includes, as well as borrowing in a conventional manner, any other arrangement (including a combination of *derivatives*) designed to achieve a temporary injection of *money* into the *scheme property* in the expectation that the sum will be repaid.
- (4) For an *ICVC*, borrowing does not include any arrangement for the *ICVC* to pay to a third party (including the *ACD*) any costs which the *ICVC* is entitled to amortise under the *rules* in this sourcebook and which were paid on behalf of the *ICVC* by the third party.

**Restrictions on lending of money**

- 5.5.6 R (1) None of the *money* in the *scheme property* of an *authorised fund* may be lent and, for the purposes of this prohibition, *money* is lent by an *authorised fund* if it is paid to a *person* ("the payee") on the basis that it should be repaid, whether or not by the payee.
- (2) Acquiring a *debenture* is not lending for the purposes of (1); nor is the placing of *money* on deposit or in a current account.
- (3) Paragraph (1) does not prevent an *ICVC* from providing an *officer* of the *ICVC* with funds to meet expenditure to be incurred by him for the purposes of the *ICVC* (or for the purposes of enabling him properly to perform his duties as an *officer* of the *ICVC*) or from doing anything to enable an *officer* to avoid incurring such expenditure.

### **Restrictions on lending of property other than money**

- 5.5.7 R (1) The *scheme property* of an *authorised fund* other than *money* must not be lent by way of deposit or otherwise.
- (2) Transactions permitted by *COLL 5.4* (Stock lending) are not to be regarded as lending for the purposes of (1).
- (3) The *scheme property* must not be mortgaged.
- (4) Nothing in this *rule* prevents the *ICVC* or the *depository* at the request of the *ICVC*, or the *trustee* at the request of the *manager*, from lending, depositing, pledging or charging *scheme property* for *margin* requirements where transactions in *derivatives* or forward transactions are used for the account of the *authorised fund* in accordance with any other of the *rules* in this chapter.

### **General power to accept or underwrite placings**

- 5.5.8 R (1) Any power in this chapter to invest in *transferable securities* may be used for the purpose of entering into transactions to which this *rule* applies, subject to compliance with any restriction in the *instrument constituting the scheme*.
- (2) This *rule* applies to any agreement or understanding which:
- (a) is an underwriting or sub-underwriting agreement; or
  - (b) contemplates that *securities* will or may be issued or subscribed for or acquired for the account of the *authorised fund*.
- (3) Paragraph (2) does not apply to:
- (a) an *option*; or
  - (b) a purchase of a *transferable security* which confers a right to:
    - (i) subscribe for or acquire a *transferable security*; or
    - (ii) convert one *transferable security* into another.
- (4) The exposure of an *authorised fund* to agreements and understandings within (2) must, on any *day*, be:
- (a) covered under *COLL 5.3.3R* (Cover for transactions in derivatives and forward transactions); and

- (b) such that, if all possible obligations arising under them had immediately to be met in full, there would be no breach of any limit in this chapter.

**Guarantees and indemnities**

- 5.5.9 R (1) An *ICVC* or a *depository* for the account of an *authorised fund* must not provide any guarantee or indemnity in respect of the obligation of any *person*.
- (2) None of the *scheme property* of an *authorised fund* may be used to discharge any obligation arising under a guarantee or indemnity with respect to the obligation of any *person*.
- (3) Paragraphs (1) and (2) do not apply to:
- (a) any indemnity or guarantee given for *margin* requirements where the *derivatives* or forward transactions are being used in accordance with the *rules* in this chapter; and
  - (b) for an *ICVC*:
    - (i) an indemnity falling within the provisions of regulation 62(3) of the *OEIC Regulations* (Exemptions from liability to be void);
    - (ii) an indemnity (other than any provision in it which is void under regulation 62 of the *OEIC Regulations*) given to the *depository* against any liability incurred by it as a consequence of the safekeeping of any of the *scheme property* by it or by anyone retained by it to assist it to perform its function of the safekeeping of the *scheme property*; and
    - (iii) an indemnity given to a *person* winding up a *scheme* if the indemnity is given for the purposes of arrangements by which the whole or part of the property of that *scheme* becomes the first property of the *ICVC* and the *holders* of *units* in that *scheme* become the first *unitholders* in the *ICVC*; and
  - (c) for an *AUT*, an indemnity given to a *person* winding up a body corporate or other *scheme* in circumstances where

those assets are becoming part of the *scheme property* by way of a *unitisation*.

**Guidance on restricting payments**

- 5.5.10 G *COLL* 6.7.15R (Payment of liabilities on transfer of assets) and *COLL* 6.7.4R (Payments out of scheme property) contain provisions restricting payments out of *scheme property*.



## 5.6 Investment powers and borrowing limits for non – UCITS retail schemes

### Application

- 5.6.1 R (1) This section applies to the *authorised fund manager* and the *depository* of a *non-UCITS retail scheme* and to an *ICVC* which is a *non-UCITS retail scheme*.
- (2) Where this section contains a reference to a *rule* in any of *COLL 5.1* to *COLL 5.5*, these *rules* and any *rules* to which they refer or any relevant *guidance* should be read as if any reference to a *UCITS scheme* is to a *non-UCITS retail scheme*.

### Explanation of COLL 5.6

- 5.6.2 G (1) This section contains *rules* on the types of permitted investments and any relevant limits with which *non-UCITS retail schemes* must comply. These *rules* allow for the relaxation of certain investment and borrowing powers from the requirements of the *UCITS Directive*. Consequently, a *scheme* authorised as a *non-UCITS retail scheme* will not qualify for the cross border passporting rights conferred by the *UCITS Directive* on a *UCITS scheme*.
- (2) Some examples of the different investment and borrowing powers under the *rules* in this section for *non-UCITS retail schemes* are the power to:
- (a) invest not more than 10% of the value of *scheme property* in *transferable securities* or money-market instruments issued by any single body;
  - (b) invest in up to 20% in aggregate of the value of the *scheme property* in *transferable securities* which are not *approved securities* and unregulated *schemes*;
  - (c) invest in a wider range of *schemes* which do not comply with the requirements of the *UCITS Directive*;
  - (d) include gold in the *scheme property* (up to a limit of 10% of the value of the *scheme property*);
  - (e) include immovables in the *scheme property*; and

- (f) borrow on a non-temporary basis without any specific time limit as to repayment of the borrowing.

**Prudent spread of risk**

- 5.6.3 R (1) An *authorised fund manager* must ensure that, taking account of the investment objectives and policy of the *non-UCITS retail scheme* as stated in its most recently published *prospectus*, the *scheme property* of the *non-UCITS retail scheme* aims to provide a prudent spread of risk
- (2) The *rules* in this section relating to spread of investments do not apply during any period in which it is not reasonably practical to comply, provided that (1) is complied with during such period.

**Investment powers: general**

- 5.6.4 R (1) The *scheme property* of a *non-UCITS retail scheme* may, subject to the *rules* in this section, comprise any assets or *investments* to which it is *dedicated*.
- (2) For an *ICVC*, the *scheme property* may also include movable or immovable property that is necessary for the direct pursuit of the *ICVC's* business of investing in those assets or investments.
- (3) The *scheme property* must be invested only in accordance with the relevant provisions in this section that are applicable to that *non-UCITS retail scheme* and within any upper limit specified in this section.
- (4) The *instrument constituting the scheme* may restrict the investment powers of a *scheme* further than the relevant restrictions in this section.
- (5) The *scheme property* may only, except where otherwise provided in the *rules* in this section, consist of any one or more of:
- (a) *transferable securities*;
  - (b) money-market instruments;

- (c) *units in collective investment schemes* permitted under *COLL 5.6.10R* (Investment in collective investment schemes);
- (d) *derivatives* and forward transactions permitted under *COLL 5.6.13R* (Permitted transactions (derivatives and forwards));
- (e) *deposits* permitted under *COLL 5.2.26R* (Investment in deposits);
- (f) immovables permitted under *COLL 5.6.18R* (Investment in property) and *COLL 5.6.19R* (Investment limits for immovables); and
- (g) gold up to a limit of 10% in value of the *scheme property*.

**Transferable securities and money-market instruments**

5.6.5 R *Transferable securities* and money-market instruments held within a *non-UCITS retail scheme* must:

- (1) be admitted to or *dealt* in on an *eligible* market within *COLL 5.2.10R*(Eligible markets: requirements); and
- (2) subject to a limit of 20% in value of the *scheme property* be:
  - (a) *transferable securities* which are not *approved securities*;
  - or
  - (b) money-market instruments which are liquid and have a value which can be determined accurately at any time.

**Valuation**

5.6.6 R In this section the value of the *scheme property* means the value of the *scheme property* determined in accordance with *COLL 5.2.5R* (Valuation).

**Spread: general**

- 5.6.7 R (1) This *rule* does not apply in respect of *government and public securities*.
- (2) Not more than 20% in value of the *scheme property* is to consist of *deposits* with a single body.

- (3) Not more than 10% in value of the *scheme property* is to consist of *transferable securities* or money-market instruments issued by any single body subject to *COLL 5.6.23R* (Schemes replicating an index).
- (4) In applying (3) *certificates representing certain securities* are to be treated as equivalent to the underlying *security*.
- (5) The exposure to any one counterparty in an *OTC derivative* transaction must not exceed 10% in value of the *scheme*.
- (6) Except for a *feeder fund*, not more than 35% in value of the *scheme* is to consist of the *units* of any one *scheme*.

**Spread: government and public securities**

- 5.6.8 R (1) This *rule* applies in respect of *government and public securities*.
- (2) The requirements in *COLL 5.2.12R* (Spread: government and public securities) apply to investment in *government and public securities* by a *non-UCITS retail scheme*.

**Investment in warrants and nil and partly paid securities**

- 5.6.9 R A *non-UCITS retail scheme* must not invest in *warrants*, and nil and partly paid *securities* unless the investment complies with the conditions in *COLL 5.2.17R* (Investment in warrants and nil and partly paid securities).

**Investment in collective investment schemes**

- 5.6.10 R A *non-UCITS retail scheme* must not invest in *units* in a *collective investment scheme* (second *scheme*) unless the second *scheme* meets each of the requirements at (1) to (4):
- (1) the second *scheme*:
    - (a) satisfies the conditions necessary for it to enjoy the rights conferred by the *UCITS Directive*; or
    - (b) is a *non-UCITS retail scheme*; or
    - (c) is a *recognised scheme*; or
    - (d) is constituted outside the *United Kingdom* and the investment and borrowing powers of which are the same or more restrictive than those of a *non-UCITS retail scheme*; or

- (e) is a *scheme* not falling within (a) to (d) and in respect of which no more than 20% in value of the *scheme property* (including any *transferable securities* which are not *approved securities*) is invested;
- (2) the second *scheme* operates on the principle of the prudent spread of risk;
- (3) the second *scheme* is prohibited from having more than 15% in value of the property of that *scheme* consisting of *units* in *collective investment schemes*; and
- (4) the *participants* in the second *scheme* must be entitled to have their *units* redeemed in accordance with the *scheme* at a *price*:
  - (a) related to the net value of the property to which the *units* relate; and
  - (b) determined in accordance with the *scheme*.

**Investment in associated collective investment schemes**

- 5.6.11 R *Units* in a *scheme* do not fall within COLL 5.6.10R if that *scheme* is managed or operated by (or, if it is an *ICVC*, has as its *ACD*) the *authorised fund manager* of the investing *non-UCITS retail scheme* or by an *associate* of that *authorised fund manager*, unless:
- (1) the *prospectus* of the investing *authorised fund* clearly states that the property of that investing fund may include such *units*; and
  - (2) the conditions in COLL 5.2.16R (Investment in other group schemes) are complied with.

**Derivatives: general**

- 5.6.12 R (1) A transaction in *derivatives* or a forward transaction must not be effected for a *non-UCITS retail scheme* unless the transaction is:
- (a) of a kind specified in COLL 5.2.20R (Permitted transactions (derivatives and forwards)); and
  - (b) covered, as required by COLL 5.3.3R (Cover for transactions in derivatives and forward transactions).

- (2) Where a *scheme* invests in *derivatives*, the exposure to the underlying assets must not exceed the limits in *COLL 5.6.7R* (Spread: general) and *COLL 5.6.8R* (Spread: government and public securities) except as provided in (4).
- (3) Where a *transferable security* or money-market instrument embeds a *derivative*, this must be taken into account for the purposes of calculating any limit in this section.
- (4) Where a *scheme* invests in an index-based *derivative*, provided the relevant index falls within *COLL 5.6.23R* (Schemes replicating an index) the underlying constituents of the index do not have to be taken into account for the purposes of *COLL 5.6.7R* and *COLL 5.6.8R*.
- (5) The relaxation in (4) is subject to the *authorised fund manager* taking account of *COLL 5.6.3R* (Prudent spread of risk).

**Permitted transactions (derivatives and forwards)**

- 5.6.13 R (1) A transaction in a *derivative* must be within *COLL 5.2.20R(1)* (Permitted transactions (derivatives and forwards)) and:
- (a) the underlying must be within *COLL 5.2.20R(2)* or *COLL 5.6.4R(5)* (Investment powers: general); and
  - (b) the exposure to the underlying must not exceed the limits in *COLL 5.6.7R* (Spread: general) and *COLL 5.6.8R* (Spread: government and public securities).
- (2) A transaction in an *approved derivative* must be effected on or under the rules of an *eligible derivatives* market.
  - (3) A transaction in a *derivative* must not cause a *scheme* to diverge from its investment objectives as stated in the *instrument constituting the scheme* and the most recently published *prospectus*.
  - (4) A transaction in a *derivative* must not be effected if the intended effect is to create the potential for an uncovered sale of:
    - (a) *transferable securities*;
    - (b) money-market instruments;

- (c) *units in collective investment schemes*; or
  - (d) *derivatives*.
- (5) Any forward transaction must be made with an *eligible institution* or an *approved bank*.
- (6) The *authorised fund manager* must ensure compliance with *COLL 5.3.6R* (Continuing nature of limits and requirements).

**Transactions for the purchase or disposal of property**

- 5.6.14 R The requirements of *COLL 5.2.21R* (Transactions for the purchase of property) and *COLL 5.2.22R* (Requirement to cover sales) apply to *non-UCITS retail schemes* in the same manner as to *UCITS schemes*.

**OTC transactions in derivatives**

- 5.6.15 R Any transaction in an *OTC derivative* under *COLL 5.6.13R* (Permitted transactions (derivatives and forwards)) must comply with the requirements of *COLL 5.2.23R* (OTC transactions in derivatives).

**Risk management: derivatives and forwards**

- 5.6.16 R An *authorised fund manager* must use a risk management process enabling it to monitor and measure as frequently as appropriate the risk associated with a *non-UCITS retail scheme's derivatives* and forwards positions and their contribution to the overall risk profile of the *scheme*.

**Risk management process**

- 5.6.17 G (1) The risk management process should take account of the investment objectives and policy of the *non-UCITS retail scheme* as stated in its most recent *prospectus*.
- (2) The *depository* should take reasonable care to review the appropriateness of the risk management process in line with its duties under *COLL 6.6* (Powers and duties of the scheme, the authorised fund manager and the depository), as appropriate.

- (3) An *authorised fund manager* is expected to demonstrate more sophistication in its risk management process for a *non-UCITS retail scheme* with a complex risk profile than for one with a simple risk profile. In particular, the risk management process should take account of any characteristic of non-linear dependence in the value of a position to its underlying.
- (4) An *authorised fund manager* should take reasonable care to establish and maintain such systems and controls as are appropriate to its business as required by SYSC 3.1 (Systems and controls).
- (5) The risk management process should enable the analysis required by COLL 5.6.16R (Risk management: derivatives and forwards) to be undertaken at least daily or at each *valuation point* whichever is the more frequent.

#### **Investment in property**

- 5.6.18 R (1) Any investment in land or a building held within the *scheme property* of a *non-UCITS retail scheme* must be an immovable within (2) to (5).
- (2) An immovable must:
    - (a) be situated in a country or territory identified in the *prospectus* for the purpose of this *rule*; and
    - (b) if situated in:
      - (i) England and Wales or Northern Ireland, be a freehold or leasehold interest; or
      - (ii) Scotland, be any interest or estate in or over land or heritable right including a long lease; or
    - (c) if not situated in the jurisdictions referred to in (b)(i) or (ii), be equivalent to any of the interests in (b)(i) or (ii).
  - (3) The *authorised fund manager* must have taken reasonable care to determine that the title to the immovable is a good marketable title.
  - (4) The *manager* or the *ICVC* must:
    - (a) have received a report from an *appropriate valuer* which:



- (i) contains a valuation of the immovable (with and without any relevant subsisting mortgage); and
    - (ii) states that in the *appropriate valuer's* opinion the immovable would, if acquired by the *scheme*, be capable of being disposed of reasonably quickly at that valuation; or
  - (b) have received a report from an *appropriate valuer* as required by (4)(a)(i) and stating that:
    - (i) the immovable is adjacent to or in the vicinity of another immovable included in the *scheme property* or is another legal interest as defined in (2)(b) or (c) in an immovable which is already included in the *scheme property*; and
    - (ii) in the opinion of the *appropriate valuer*, the total value of both immovables would at least equal the sum of the price payable for the immovable and the existing value of the other immovable.
- (5) An immovable must:
- (a) be bought or be agreed by enforceable contract to be bought within six *months* after receipt of the report of the *appropriate valuer* under (4);
  - (b) not be bought, if it is apparent to the *authorised fund manager* that the report in (a) could no longer reasonably be relied upon; and
  - (c) not be bought at more than 105% of the valuation for the relevant immovable in the report in (4).
- (6) Any furniture, fittings or other contents of any building may be regarded as part of the relevant immovable.
- (7) An *appropriate valuer* must be a *person* who:
- (a) has knowledge of and experience in the valuation of immovables of the relevant kind in the relevant area;
  - (b) is qualified to be a *standing independent valuer* of a *non-UCITS retail scheme* or is considered by the *scheme's*

*standing independent valuer* to hold an equivalent qualification;

- (c) is independent of the *ICVC*, the *depository* and each of the *directors* of the *ICVC* or of the *manager* and *trustee* of the *AUT*; and
- (d) has not engaged himself or any of his *associates* in relation to the finding of the immovable for the *scheme* or the finding of the *scheme* for the immovable.

#### **Investment limits for immovables**

5.6.19 R The following limits apply in respect of immovables held as part of *scheme property* of a *scheme*:

- (1) not more than 15% in value of the *scheme property* is to consist of any one immovable;
- (2) in (1), immovables within *COLL 5.6.18R (4)(b)*(Investment in property) must be regarded as one immovable;
- (3) the figure of 15% in (1) may be increased to 25% once the immovable has been included in the *scheme property* in compliance with (1);
- (4) the income receivable from any one *group* in any accounting period must not be attributable to immovables comprising:
  - (a) more than 25%; or
  - (b) in the case of a government or public body more than 35%;of the value of the *scheme property*;
- (5) not more than 20% in value of the *scheme property* is to consist of mortgaged immovables and any mortgage must not secure more than 100% of the value in *COLL 5.6.18R(4)* (on the assumption the immovable is not mortgaged);
- (6) an immovable may be mortgaged up to 100% of the value in (4) provided that no more than 20% of the value of the *scheme property* consists of such immovables and any *transferable securities* which are not *approved securities*;
- (7) not more than 50% in value of the *scheme property* is to

consist of *immovables* which are unoccupied and non-income producing or in the course of substantial development, redevelopment or refurbishment; and

- (8) no option may be granted to a third party to buy any immovable comprised in the *scheme property* unless the value of the relevant immovable does not exceed 20% of the value of the *scheme property* together with, where appropriate, the value of investments in:
  - (a) *unregulated collective investment schemes*; and
  - (b) any *transferable securities* which are not *approved securities*.

### **Standing independent valuer and valuation**

- 5.6.20 R (1) The following requirements apply in relation to the appointment of a valuer:
- (a) the *authorised fund manager* must ensure that any immovables in the *scheme property* are valued by an *appropriate valuer (standing independent valuer)* appointed by the *authorised fund manager*; and
  - (b) the appointment must be made with the approval of the *trustee* or *depository* at the outset and upon any vacancy.
- (2) The *standing independent valuer* in (1) must be:
- (a) for an *AUT*, independent of the *manager* and *trustee*; and
  - (b) for an *ICVC*, independent of the *ICVC*, the *directors* and the *depository*.
- (3) The following requirements apply in relation to the functions of the *standing independent valuer*:
- (a) the *authorised fund manager* must ensure that the *standing independent valuer* values all the immovables held within the *scheme property*, on the basis of a full valuation with physical inspection (including, where the immovable is or includes a building, internal inspection), at least once a year;
  - (b) for the purposes of (a) any inspection in relation to

- adjacent properties of a similar nature may be limited to that of only one such representative property;
- (c) the *authorised fund manager* must ensure that the *standing independent valuer* values the immovables, on the basis of a review of the last full valuation, at least once a *month*;
  - (d) if either the *authorised fund manager* or the *depository* becomes aware of any matters that appear likely to:
    - (i) affect the outcome of a valuation of an immovable;
    - or
    - (ii) cause the valuer to decide to value under (a) instead of under (c);it must immediately inform the *standing independent valuer* of that matter;
  - (e) the *authorised fund manager* must use its best endeavours to ensure that any other *affected person* reports to the *standing independent valuer* immediately upon that *person* becoming aware of any matter within (d); and
  - (f) any valuation by the *standing independent valuer* must be on the basis of an 'Open Market value' as defined in Practice Statement 3 in the Royal Institute of Chartered Surveyors' Appraisal and Valuation Manual (first edition published September 1995) but subject to *COLL* 6.3 (Valuation and pricing).
- (4) In relation to an immovable:
- (a) any valuation under *COLL* 6.3 (Valuation and pricing) has effect, until the next valuation under that *rule*, for the purposes of the value of immovables; and
  - (b) an agreement to transfer an immovable or an interest in an immovable is to be disregarded for the purpose of the valuation of the *scheme property* unless it reasonably appears to the *authorised fund manager* to be legally

enforceable.

**Stock lending**

- 5.6.21 R A *non-UCITS retail scheme* may undertake *stock lending* in accordance with *COLL 5.4* (Stock lending).

**Cash, borrowing, lending and other provisions**

- 5.6.22 R The following *rules* in Chapter 5 apply to a *non-UCITS retail scheme*:

- (1) *COLL 5.2.7R* (Transferable securities);
- (2) *COLL 5.5.1R*(Application);
- (3) *COLL 5.5.3R* (Cash and near cash);
- (4) *COLL 5.5.4R*(1),(2),(3) and (8) (General power to borrow);
- (5) *COLL 5.5.5R* (1),(2) and (4) (Borrowing limits);
- (6) *COLL 5.5.6R* (Restrictions on lending of money) ;
- (7) *COLL 5.5.7R*(1)and (2)(Restrictions on lending of property other than money);
- (8) *COLL 5.5.8R* (General power to accept or underwrite placings); and
- (9) *COLL 5.5.9R* (Guarantees and indemnities).

**Schemes replicating an index**

- 5.6.23 R (1) A *non-UCITS retail scheme* may invest up to 20% in value of the *scheme property* in *shares* and *debentures* which are issued by the same body where the aim of the investment policy of that *scheme* as stated in its most recently published *prospectus* is to replicate the performance or composition of an index within (2).
- (2) The index must:
- (a) have a sufficiently diversified composition;
  - (b) be a representative benchmark for the market to which it refers; and
  - (c) be published in an appropriate manner.

- (3) The limit in (1) may be raised for a particular *scheme* up to 35% in value of the *scheme property*, but only in respect of one body and where justified by exceptional market conditions.

**Non-UCITS retail schemes that are umbrellas**

- 5.6.24 R (1) In relation to a *scheme* which is an *umbrella*, the provisions in this section apply to each *sub-fund* as they would for a *non-UCITS retail scheme*.
- (2) A *sub-fund* must not invest in another *sub-fund* of the same *umbrella*.

## 6 Operating duties and responsibilities

### 6.1 Introduction and Application

#### Application

6.1.1 R This chapter applies to:

- (1) an *authorised fund manager* of an *AUT* or an *ICVC*;
- (2) any other *director* of an *ICVC*;
- (3) a *depository* of an *AUT* or an *ICVC*; and
- (4) an *ICVC*,

where such *AUT* or *ICVC* is a *UCITS scheme* or a *non-UCITS retail scheme*.

#### Purpose

6.1.2 G This chapter helps in achieving the *regulatory objective* of protecting *consumers*. It provides the operating framework within which the *authorised fund* must be operated on a day-to-day basis to ensure that *clients* are treated fairly when they become, remain or as they cease to be *unitholders*.

#### Explanation of this chapter

- 6.1.3 G (1) The *authorised fund manager* operates the *scheme* on a day-to-day basis. Its operation is determined by the *rules* in this chapter, which require appropriate powers in the *instrument constituting the scheme* or refer to the need to state the relevant operating procedures in the *prospectus* of the *scheme*.
- (2) The *authorised fund manager* does not necessarily have to carry out all the activities it is responsible for and may delegate functions to other *persons*. The *rules* in this chapter set out the parameters of such delegation.
- (3) The *depository's* duty is, generally speaking, to ensure the safe custody of *scheme property* and to oversee certain functions of the *authorised fund manager* (most notably the pricing and dealing function and investment powers). The oversight responsibilities for a *trustee* of an *AUT* are similar to, but not the same as, the oversight responsibilities of the *depository* of an *ICVC*. These differences result from the different legal structure of the *authorised funds* and the *trustee's* obligations under trust law.

## 6.2 Dealing

### Application

- 6.2.1 R This section applies to an *authorised fund manager*, a *depository*, an *ICVC* and any other *directors* of an *ICVC*.

### Purpose

- 6.2.2 G (1) This section helps in achieving the *regulatory objective* of securing an appropriate degree of protection for *consumers*. In accordance with *Principle 6*, this section is also concerned with ensuring the *authorised fund manager* pays due regard to its *clients'* interests and treats them fairly.
- (2) An *authorised fund manager* is responsible for arranging for the *issue* and the *cancellation* of *units* for the *authorised fund*, and is permitted to *sell* and *redeem units* for its own account. The *rules* in this section are intended to ensure that the *authorised fund manager* treats the *authorised fund* fairly when arranging for the *issue* or *cancellation* of *units*, and treats *clients* fairly when they purchase or *sell units*.
- (3) This section also sets out common standards for how the amounts in relation to *unit* transactions are to be paid. These arrangements include the *initial offer* of *units*, the exchange of *units* for *scheme property* and *issues* and *cancellations* of *units* by an *ICVC*, or by the *trustee* of an *AUT*, carried out directly with the *unitholder*.
- (4) This section also sets out *rules* and *guidance* relating to the *authorised fund manager's* controls over the *issue* and *cancellation* of *units* including any box holdings.
- (5) The requirements in this section are to be applied separately to each *sub-fund* of a *scheme* which is an *umbrella*, and, if appropriate, the currency of a *sub-fund* may be used instead of the *base currency* of the *umbrella*.

### Initial offers



- 6.2.3 R (1) During the *initial offer* period, *units* may only be issued at the *initial price*.
- (2) The length of any *initial offer* should not be unreasonable when considered alongside the characteristics of the *authorised fund*.
- (3) The *authorised fund manager* must, as soon as practicable after receiving the *initial price* from the purchaser and no later than the fourth *business day* following the end of the *initial offer*, pay the *depository* the *initial price* of any *unit* it has agreed to *sell* during the period of the *initial offer*.
- (4) The period of the *initial offer* comes to an end if the *authorised fund manager* reasonably believes the *price* that would reflect the current value of the *scheme property* would vary by more than 2% from the *initial price*.

**Initial offer: guidance**

- 6.2.4 G (1) Details of any *initial offer* period must be provided in the relevant *prospectus* as described in *COLL* 4.2.5R 17(h) (Table: contents of the prospectus).
- (2) It may be appropriate that the *initial offer* for a *scheme* operating limited *issue* or *limited redemption arrangements*, or intending to invest in illiquid assets, is longer than one for a *scheme* which does not have these features.

**Issue and cancellation of units by an ICVC**

- 6.2.5 R (1) *Units* in an *ICVC* are *issued* or *cancelled* by the *ACD* making a record of the *issue* or *cancellation* and of the number of the *units* of each *class* concerned, and cannot be *issued* or *cancelled* in any other manner, unless *COLL* 3.2.6R 11 (Table: contents of the instrument constituting the scheme) applies.
- (2) The time of the *issue* or *cancellation* under (1) is the time when the record is made.

**Issue and cancellation of units in an AUT**

- 6.2.6 R (1) The *trustee* must *issue* or *cancel units* in an *AUT* when instructed by the *manager*.

- (2) Any instructions given by the *manager* must state, for each *class* of *unit* to be *issued* or *cancelled*, the number to be *issued* or *cancelled*, expressed either as a number of *units* or as an amount in value (or as a combination of the two).
- (3) If the *trustee* is of the opinion that it is not in the interests of *unitholders* that any *units* should be *issued* or *cancelled* or that to do so would not be in accordance with the *trust deed* or *prospectus*, it must notify the *manager* of that fact and it is then relieved of the obligation to *issue* or *cancel* those *units*.

**Issue and cancellation of units through an authorised fund manager**

- 6.2.7 R (1) The *authorised fund manager* may require, on agreement with the *depository*, or may permit, on the request of the investor, direct *issues* and *cancellations* of *units* by an *ICVC* or by the *trustee* of an *AUT*.
- (2) If (1) applies:
- (a) *the instrument constituting the scheme* must provide for this; and
  - (b) *the prospectus* must provide details of the procedure to be followed which must be consistent with the *rules* in this section.

**Controls over the issue and cancellation of units**

- 6.2.8 R (1) An *authorised fund manager* must ensure that at each *valuation point* there are at least as many *units* in *issue* of any *class* as there are *units* registered to *unitholders* for that *class*.
- (2) An *authorised fund manager* must not:
- (a) for an *AUT*, when giving instructions to the *depository* for the *issue* or *cancellation* of *units*; or
  - (b) for an *ICVC*, when arranging for the *issue* or *cancellation* of *units*;
- do, or omit to do, anything which would, or might, confer on himself or an *associate* a benefit or advantage at the expense of a *unitholder* or a potential *unitholder*.

- (3) For the purpose of (1), the *authorised fund manager* may take into account instructions to *redeem units* at the following *valuation point* received before any time agreed with the *depository* for such purpose.

**Controls over the issue and cancellation of units – guidance**

- 6.2.9 G (1) As the *authorised fund manager* normally controls the *issue, cancellation, sale* and *redemption* of an *authorised fund's units*, it occupies a position that could, without appropriate systems and controls, involve a conflict of interest between itself and its *clients*.
- (2) SYSC 3.1.1 (Systems and controls) requires that a *firm* take reasonable care to establish and maintain such systems and controls as are appropriate to its business and *Principle 8* requires a *firm* to manage conflicts of interest between itself and a *customer* fairly.
  - (3) To manage the conflict of interest that arises, when an *authorised fund manager* gives an instruction to *issue* or *cancel units*, the *price* of the *units* should be calculated at the valuation point before or after the instruction has been given, in accordance with (4).
  - (4) An *authorised fund manager* should agree a period of time with the *depository* during which it will give instructions to *issue* or *cancel units*. Where the *authorised fund manager* operates a box with the principal aim of making a profit, this period will be short (for example, two hours); otherwise a longer period (for example, up to the next *valuation point* but in all cases within 24 hours) may be acceptable, provided the principles in (2) are followed.
  - (5) The last *valuation point* should be used for the pricing of *units* where instructions are given before the expiry of the period of time agreed in (4); otherwise the next *valuation point* should be used.

- (6) Where an in specie *issue* or *cancellation* occurs it should be undertaken using the next *valuation point's price*.

**Modification to number of units issued or cancelled**

- 6.2.10 R (1) Any instruction for the *issue* or *cancellation* of *units* under *COLL* 6.2.5R (Issue and cancellation of units by an ICVC) or *COLL* 6.2.6R (Issue and cancellation of units in an AUT) may be modified but only if the *depository* agrees and has taken reasonable care to determine that:
- (a) the modification corrects an error in the instruction; and
  - (b) the error is an isolated one.
- (2) Any error in (1) must be corrected within the payment period applicable under *COLL* 6.2.13R (Payment for units issued) or *COLL* 6.2.14R (Payment for cancelled units).

**Compensation for box management errors**

- 6.2.11 R (1) Where the *authorised fund manager* has not complied with *COLL* 6.2.8R(1) (Controls over the issue and cancellation of units), it must correct the error as soon as possible and must reimburse the *authorised fund* any costs it may have incurred in correcting the position.
- (2) The *authorised fund manager* need not reimburse the *authorised fund* when:
- (a) the amount under (1) is not, in the *depository's* opinion, material to the *authorised fund*;
  - (b) the *authorised fund manager* can demonstrate that it has effective controls in place over box management, including all of the areas that affect the figures which are included in the box management calculations; and
  - (c) the requirements of *COLL* 6.2.10R (Modification to number of units issued or cancelled) are complied with.

**Box management errors guidance**

- 6.2.12 G Explanatory table: This table belongs to *COLL* 6.2.2G(4) (Purpose).

<b>Correction of box management errors</b>	
<b>1</b>	<b>Controls by authorised fund managers</b>
	An <i>authorised fund manager</i> needs to be able to demonstrate that it has effective controls over:
(1)	its calculations of what <i>units</i> are owned by it (its 'box'); and
(2)	compliance with <i>COLL</i> 6.2.8R which is intended to prevent a negative box.
<b>2</b>	<b>Controls by depositaries</b>
(1)	Under <i>COLL</i> 6.6.4 (General duties of the depositary), a <i>depositary</i> should take reasonable care to ensure that a scheme is managed in accordance with <i>COLL</i> 6.2 (Dealing) and 6.3 (Pricing and valuation).
(2)	A <i>depositary</i> should therefore make a regular assessment of the <i>authorised fund manager's</i> box management procedures (including supporting systems) and controls. This should include reviewing the <i>authorised fund manager's</i> controls and procedures when the <i>depositary</i> assumes office, on any significant change and on a regular basis, to ensure that a series of otherwise minor changes do not have a cumulative and a significant effect on the accuracy of the controls and procedures.
<b>3</b>	<b>Recording and reporting of box management errors</b>
(1)	An <i>authorised fund manager</i> should record all errors which result in a breach of <i>COLL</i> 6.2.8R (Controls over the issue and cancellation of units) and as soon as an error is discovered, the <i>authorised fund manager</i> should report the fact to the <i>depositary</i> , together with details of the action taken, or to be taken, to avoid repetition of the error.
(2)	A <i>depositary</i> should report material box management errors to the <i>FSA</i> immediately. Materiality should be determined by taking into account a number of factors including: <ul style="list-style-type: none"> <li>(a) the implications of the error for the sufficiency of controls put into place by the <i>authorised fund manager</i>;</li> <li>(b) the significance of any breakdown in the <i>authorised fund manager's</i> management controls or other checking procedures;</li> <li>(c) the significance of any failure of systems or back-up arrangements;</li> <li>(d) the duration of an error; and</li> <li>(e) the level of compensation due to the <i>scheme</i>, and an <i>authorised fund manager's</i> ability (or otherwise) to meet claims for compensation in full.</li> </ul>
(3)	A <i>depositary</i> should also make a return to the <i>FSA</i> (in the manner <i>SUP</i> 16.6.8R) on a quarterly basis.

### **Payment for units issued**

- 6.2.13 R (1) The *authorised fund manager* must, by the close of business on the fourth *business day* following the *issue* of any *units* arrange for payment of the value of the *units issued* and any payment required under *COLL* 6.3.7R (SDRT provision) and *COLL* 6.3.8R (Dilution) to the *trustee* or the *ICVC*.
- (2) The *authorised fund manager* must make the payment referred to in (1) in cash or cleared funds unless *COLL* 6.2.15R (In specie issue and cancellation) applies.

- (3) Where the *authorised fund manager* has not complied with (1), it must reimburse the *authorised fund* for any lost interest unless the amount involved is not, in the *depository's* opinion, material to the *authorised fund*.

#### **Payment for cancelled units**

- 6.2.14 R (1) On *cancelling units* the *authorised fund manager* must, before the expiry of the fourth *business day* following the *cancellation* of the *units* or, if later, as soon as practicable after delivery to the *trustee* or the *ICVC* of such evidence of title to the *units* as it may reasonably require, require the *depository* to pay the *price* of the *units* (less any deduction required under *COLL 6.3.7R* and *COLL 6.3.8R*) to the *authorised fund manager* or, where relevant, the *unitholder* or, for a *relevant pension scheme*, in accordance with the relevant provisions of the *trust deed*.
- (2) If the *authorised fund manager* has not ensured that the *scheme property* includes or will include sufficient cash in the appropriate currency (or a sufficient facility to borrow without infringing any restriction in *COLL 5* (Investment and borrowing powers)) within the period in (1), that period is extended, for any relevant currency, until the shortage is rectified.
- (3) If (2) applies, the *authorised fund manager* must take reasonable steps to rectify the currency shortage as quickly as possible.
- (4) This *rule* does not apply where *COLL 6.2.15R* is in operation.
- (5) Nothing in this section requires an *ICVC*, a *depository* or an *authorised fund manager* to part with *money* or to transfer *scheme property* for a *cancellation* or *redemption* of *units* where any *money* due on the earlier *issue* or *sale* of those *units* has not been received.

#### **In specie issue and cancellation**

- 6.2.15 R The *depository* may take into or pay out of *scheme property* assets other than *cash* as payment for the *issue* or *cancellation* of units but only if:
- (1) it has taken reasonable care to ensure that the property concerned would not be likely to result in any material prejudice to the interests of *unitholders*; and
  - (2) the *instrument constituting the scheme* so provides.

#### **Sale and redemption**

- 6.2.16 R (1) In accordance with *COLL* 4.2.5R 17 (Table: contents of the prospectus), the *authorised fund manager* must describe the arrangements for the *sale* and *redemption* of *units* in the *prospectus*.
- (2) The *authorised fund manager* must, at all times during the *dealing day*, be willing to effect the *sale* of *units* in the *authorised fund*, in accordance with the conditions in the *instrument constituting the scheme* and the *prospectus* unless:
- (a) it has reasonable grounds to refuse such *sale*; or
  - (b) the issue of units is prevented under *COLL* 6.2.18R (Limited issue).
- (3) Subject to *COLL* 6.2.19R (Limited redemption) and *COLL* 6.2.21R (Deferred redemption), the *authorised fund manager* must, at all times during the *dealing day*, on request of any qualifying *unitholder*, effect the *redemption* of *units* in accordance with the conditions in the *instrument constituting the scheme* and the *prospectus* unless it has reasonable grounds to refuse such *redemption*.
- (4) On agreeing to a *redemption* of *units* in (3), the *authorised fund manager* must pay the *unitholder* the appropriate proceeds of *redemption* within the period specified in (5) unless the *authorised fund manager* has reasonable grounds for withholding all or any part of the proceeds.
- (5) The period in (4) expires at the close of business on the fourth *business day* following the later of:

- (a) the *valuation point* at which the *price* for the *redemption* was determined; or
  - (b) the time when the *authorised fund manager* has all the duly executed instruments and authorisations to effect (or enable the *authorised fund manager* to effect) the transfer of title to the *units*.
- (6) Except where (7) applies, and subject to *COLL 6.2.21R* (Deferred redemption), the *authorised fund manager* must *sell* or *redeem units* at a *price* determined no later than the end of the *business day* immediately following the receipt and acceptance of an instruction to do so, or at the next *valuation point* for the purposes of buying or selling *units* if later (or, for a *sale* or *redemption* at an *historic price*, at the *price* determined at the last *valuation point*).
- (7) Where the *authorised fund* operates *limited redemption arrangements*, the *authorised fund manager* must *sell* or *redeem units* at a price determined no later than the expiry of a period of 185 *days* from the date of the receipt and acceptance of the instruction to *sell* or *redeem*.
- (8) The *authorised fund manager* must not *sell* a *unit* for more than the *price* of a *unit* of the relevant *class* at the relevant *valuation point*, to which may be added any *preliminary charge* permitted and any payment required under *COLL 6.3.7R* and *COLL 6.3.8R*.
- (9) The *authorised fund manager* must not redeem a *unit* for less than the *price* of a *unit* of the relevant *class* at the relevant *valuation point*, less any *redemption charge* permitted and any deduction under *COLL 6.3.7R* and *COLL 6.3.8R*.
- (10) Paragraphs (4), (5) and (9) do not apply where the *authorised fund manager* is buying units as *principal* on an investment exchange (for an *AUT* in accordance with a power in the *trust deed*) and settlement will be made in accordance with the rules of that exchange.



### **Sale and redemption: guidance**

- 6.2.17 G (1) The *prospectus* of an *authorised fund* that does not operate on the basis of *historic prices* may allow the *authorised fund manager* to identify a point in time in advance of a *valuation point* (a cut-off point) after which it will not accept instructions to *sell* or *redeem* units at that *valuation point*. In order to protect *customers'* interests, the cut-off point should be no earlier than the close of business on the *business day* before the *valuation point* it relates to. If there is more than one *valuation point* in a *day* the cut-off should not be before any previous *valuation point*.
- (2) Where the *authorised fund* operates *limited redemption arrangements*, the cut-off point may reflect the expected length of time required to undertake transactions in the underlying investments provided the 185 *day* limit in *COLL* 6.2.16R(7) (Sale and redemption) is complied with.
- (3) Where (1) applies, different cut-off points may be used to differentiate between the methods of submitting instructions to *sell* or *redeem* to the *authorised fund manager* but not to differentiate between *unitholders* or potential *unitholders*.

### **Limited Issue**

- 6.2.18 R (1) If an *authorised fund* limits the *issue* of any *class* of *unit*, the *prospectus* of an *authorised fund* must provide for the circumstances and conditions when *units* will be issued.
- (2) Where (1) applies, the *authorised fund manager* may not provide for the further *issue* of *units* unless, at the time of the issue, he is satisfied on reasonable grounds that the proceeds of that subsequent *issue* can be invested without compromising the *scheme's* investment objective or materially prejudicing existing *unitholders*.
- (3) Within a *scheme*, *unit classes* may operate different arrangements for the *issue* of *units* provided there is no prejudice to the interests of any *unitholder*.

### **Limited redemption**

- 6.2.19 R (1) The *instrument constituting the scheme* and the *prospectus* of a *non-UCITS retail fund* that invests substantially in *approved immovables*, or whose investment objective is to provide a specified level of return, may provide for *limited redemption arrangements* appropriate to its aims and objectives.
- (2) Where (1) applies, the *scheme* must provide for *redemptions* at least once in every six *months*.
- (3) Within a *scheme*, *unit classes* may operate different arrangements for *redemption* of *units* provided there is no prejudice to the interests of any *unitholder*.

### **Limited redemption: guidance**

- 6.2.20 G The conditions for *limited redemption arrangements* in COLL 6.2.19R should be considered, for *AUTs* as well as for *ICVCs*, in conjunction with *AUTH* Appendix 2 (Meaning of an open-ended investment company) and *AUTH* Appendix 2.8 (The investment condition: the ‘expectation test’ (section 236(3)(a) of the *Act*)).

### **Deferred redemption**

- 6.2.21 R (1) The *instrument constituting the scheme* and the *prospectus* of an *authorised fund* which has at least one *valuation point* on each *business day*, may permit deferral of *redemptions* at a *valuation point* to the next *valuation point* where the requested *redemptions* exceed 10%, or some other reasonable proportion disclosed in the *prospectus*, of the *authorised fund’s* value.
- (2) Any deferral of *redemptions* under (1) must be undertaken in accordance with the procedures explained in the *prospectus* which must ensure:
- (a) the consistent treatment of all *unitholders* who have sought to redeem *units* at any *valuation point* at which redemptions are deferred; and
  - (b) that all *deals* relating to an earlier *valuation point* are completed before those relating to a later *valuation point* are considered.

### **Deferred redemption: guidance**

- 6.2.22 G In times of high levels of *redemption*, deferred *redemption* will enable the *authorised fund manager* to protect the interests of continuing *unitholders* by allowing it to match the sale of *scheme property* to the level of *redemptions*. This should reduce the impact of *dilution* on the *scheme*.

### 6.3 Valuation and pricing

#### Application

- 6.3.1 R This section applies to an *authorised fund manager*, a *depository*, an *ICVC* and any other *director* of an *ICVC*.

#### Purpose

- 6.3.2 G (1) In accordance with *Principle 6*, this section is intended to ensure that the *authorised fund manager* pays due regard to its *clients'* interests and treats them fairly.
- (2) An *authorised fund manager* is responsible for valuing the *scheme property* of the *authorised fund* it manages and for calculating the *price of units* in the *authorised fund*. This section protects *clients* by:
- (a) setting out *rules* and guidance to ensure the *price of units* in an *authorised fund* is calculated fairly and regularly;
  - (b) allowing for the *authorised fund manager* to mitigate the effects of any *dilution* (reduction) in the value of the *scheme property* by:
    - (i) payment of stamp duty reserve tax (SDRT) in relation to certain *unit* transactions; and
    - (ii) buying and selling underlying investments as a result of the *issue* or *cancellation of units*;
  - (c) making appropriate provision to ensure *clients* are treated fairly where *units* are being dealt with at a known (historic) *price*; and
  - (d) ensuring that the *price* is made public in an appropriate manner.
- (3) The requirements in this section are to be applied separately to each *sub-fund* of a *scheme* which is an *umbrella*, and, if appropriate, the currency of a *sub-fund* may be used instead of the *base currency* of the *umbrella*.

#### Valuation

- 6.3.3 R To determine the *price of units* the *authorised fund manager* must carry out a fair and accurate valuation of all the *scheme property*.

**Valuation points**

- 6.3.4 R (1) An *authorised fund* must not have fewer than two regular *valuation points* in any *month* and if there are only two *valuation points* in any *month*, the regular *valuation points* must be at least two weeks apart.
- (2) The *prospectus* of a *scheme* must contain information about its regular *valuation points* for the purposes of *dealing in units* in accordance with COLL 4.2.5R 16 (Table: contents of the prospectus).
- (3) Where a *scheme* operates *limited redemption arrangements*, (1) does not apply and the *valuation points* must be stated in the *prospectus* but must not be set more than six *months* apart.
- (4) Where a *scheme* operates *limited redemption arrangements*, it must be valued and *prices* published in the manner set out in COLL 6.3.11R (Publication of prices) at least once in every *month*.
- (5) In (4), a *valuation point* for the purpose of publishing *prices* only, does not make it a *valuation point* for the purpose of (2) unless it is disclosed as such in the *prospectus*.
- (6) *Higher volatility funds* must have at least one *valuation point* every *business day*.
- (7) No *valuation points* are required during the period of any *initial offer*.
- (8) The *authorised fund manager* may determine to have an additional *valuation point* for an *authorised fund* as a result of market movement under COLL 6.3.9 (Forward and historic pricing) or otherwise, in which case he must inform the *depository*.

**Price of a unit**

- 6.3.5 R (1) The *price* of a *unit* of any *class* must be calculated by reference to the net value of *scheme property* and must be calculated in accordance with the provisions of the *prospectus*.

- (2) Any *unit price* calculated in accordance with (1) must be expressed in a form that is accurate to at least four significant figures.

### Valuation and pricing guidance

6.3.6 G Table: This table belongs to *COLL 6.3.2G(2)(a)*.

Valuation and pricing	
1	<b>The valuation of scheme property</b>
(1)	Where possible, <i>investments</i> should be valued using a reputable source. The reliability of the source of prices should be kept under regular review.
(2)	An <i>investment</i> for which different <i>prices</i> are quoted according to whether it is being bought or sold should be valued at its mid-market price. The <i>instrument constituting the scheme</i> should set out the valuation method that will apply where a single price for buying and selling a <i>security</i> is quoted.
(3)	Any part of the <i>scheme property</i> of an <i>authorised fund</i> that is not an <i>investment</i> should be valued at a fair value, but for immovables this is subject to <i>COLL 5.6.20R(3)(f)</i> (Standing independent valuer and valuation).
(4)	For the purposes of (2) and (3), any fiscal charges, commissions, professional fees or other charges that were paid, or would be payable on acquiring or disposing of the <i>investment</i> or other part of the <i>scheme property</i> should be excluded from the value of an <i>investment</i> or other part of the <i>scheme property</i> .
(5)	Where the <i>authorised fund manager</i> has reasonable grounds to believe that: <ul style="list-style-type: none"> <li>(a) no reliable price exists for a <i>security</i> at a <i>valuation point</i>; or</li> <li>(b) the most recent price available does not reflect the <i>authorised fund manager's</i> best estimate of the value of a <i>security</i> at the <i>valuation point</i>;</li> </ul> it should value an <i>investment</i> at a price which, in its opinion, reflects a fair and reasonable price for that <i>investment</i> (the fair value price).
(6)	The circumstances which may give rise to a fair value price being used include: <ul style="list-style-type: none"> <li>(a) no recent trade in the <i>security</i> concerned; or</li> <li>(b) the occurrence of a significant event since the most recent closure of the market where the price of the <i>security</i> is taken.</li> </ul> In (b), a significant event is one that means the most recent price of a <i>security</i> or a basket of <i>securities</i> is materially different to the price that it is reasonably believed would exist at the <i>valuation point</i> had the relevant market been open.
(7)	In determining whether to use such a fair value price, the <i>authorised fund manager</i> should include in his consideration: <ul style="list-style-type: none"> <li>(a) the type of <i>authorised fund</i> concerned;</li> <li>(b) the <i>securities</i> involved;</li> <li>(c) the basis and reliability of the alternative <i>price</i> used; and</li> <li>(d) the <i>authorised fund manager's</i> policy on the valuation of <i>scheme property</i> as disclosed in the <i>prospectus</i>.</li> </ul>

	(8)	The <i>authorised fund manager</i> should document the basis of valuation (including any fair value pricing policy) and, where appropriate, the basis of any methodology and ensure that the procedures are applied consistently and fairly.
	(9)	Where a <i>unit price</i> is determined using properly applied fair value prices in accordance with policies in (8), subsequent information that indicates the <i>price</i> should have been different from that calculated will not normally give rise to an instance of incorrect pricing.
<b>2</b>	<b>The pricing controls of the authorised fund manager</b>	
	(1)	An <i>authorised fund manager</i> needs to be able to demonstrate that it has effective controls over its calculations of <i>unit prices</i> .
	(2)	The controls referred to in (1) should ensure that: <ul style="list-style-type: none"> <li>(a) asset prices are accurate and up to date;</li> <li>(b) <i>investment</i> transactions are accurately and promptly reflected in valuations;</li> <li>(c) the components of the valuation (including stock, cash, and <i>units</i> in issue), are regularly reconciled to their source or prime records and any reconciling items resolved promptly and debtors reviewed for recoverability;</li> <li>(d) the sources of prices not obtained from the main pricing source are recorded and regularly reviewed;</li> <li>(e) compliance with the investment and borrowing powers is regularly reviewed;</li> <li>(f) dividends are accounted for as soon as stocks are quoted ex-dividend (unless it is prudent to account for them on receipt);</li> <li>(g) fixed interest dividends, interest and expenses are accrued at each valuation point,</li> <li>(h) tax positions are regularly reviewed and adjusted, if necessary;</li> <li>(i) reasonable tolerances are set for movements in the key elements of a valuation and movements outside these tolerances are investigated; and</li> <li>(j) the fund manager regularly reviews the portfolio valuation for accuracy.</li> </ul>
	(3)	In exercising its pricing controls, the <i>authorised fund manager</i> may exercise reasonable discretion in determining the appropriate frequency of the operation of the controls and may choose a longer interval, if appropriate, given the level of activity on the fund or the materiality of any effect on the <i>price</i> .
	(4)	Evidence of the exercise of the pricing controls should be retained.
	(5)	Evidence of persistent or repetitive errors in relation to these matters, and in particular any evidence of a pattern of errors working in an <i>authorised fund manager's</i> favour, will make demonstrating effective controls more difficult.
	(6)	Where the pricing function is delegated to a third party, COLL 6.6.15R (Committees and delegation) will apply.
<b>3</b>	<b>The depositary's review of the authorised fund manager's systems and controls</b>	

	(1)	This section provides details of the types of checks a <i>depository</i> should carry out to be satisfied that the <i>authorised fund manager</i> adopts systems and controls which are appropriate to ensure that <i>prices</i> of <i>units</i> are calculated in accordance with this section and to ensure that the likelihood of incorrect <i>prices</i> will be minimised. These checks also apply where an <i>authorised fund manager</i> has delegated all or some of its pricing functions to a third party.
	(2)	A <i>depository</i> should thoroughly review an <i>authorised fund manager's</i> systems and controls to confirm that they are satisfactory. The <i>depository's</i> review should include an analysis of the controls in place to determine the extent to which reliance can be placed on them.
	(3)	A review should be performed when the <i>depository</i> is appointed and thereafter as it feels appropriate given its knowledge of the robustness and the stability of the systems and controls and their operation.
	(4)	A review should be carried out more frequently where a <i>depository</i> knows or suspects that an <i>authorised fund manager's</i> systems and controls are weak or are otherwise unsatisfactory.
	(5)	Additionally, a <i>depository</i> should from time to time review other aspects of the valuation of the <i>scheme property</i> of each <i>authorised fund</i> for which it is responsible, verifying, on a sample basis, if necessary, the assets, liabilities, accruals, <i>units</i> in issue, <i>securities</i> prices (and in particular the prices of unapproved <i>securities</i> and the basis for the valuation of unquoted <i>securities</i> ) and any other relevant matters, for example an accumulation factor or a currency conversion factor.
	(6)	A <i>depository</i> should ensure that any issues, which are identified in any such review, are properly followed up and resolved.
<b>4</b>	<b>The recording and reporting of instances of incorrect pricing</b>	
	(1)	An <i>authorised fund manager</i> should record each instance where the <i>price</i> of a <i>unit</i> is incorrect as soon as the error is discovered, and report the fact to the <i>depository</i> together with details of the action taken, or to be taken, to avoid repetition as soon as practicable.
	(2)	In accordance with COLL 6.6.11G (Duty to inform the FSA), the <i>depository</i> should report any breach of the rules in COLL 6.3 immediately to the FSA. However, notification should relate to instances which the <i>depository</i> considers material only.
	(3)	A <i>depository</i> should also report to the FSA immediately any instance of incorrect pricing where the error is 0.5% or more of the <i>price</i> of a <i>unit</i> , where a <i>depository</i> believes that reimbursement or payment is inappropriate and should not be paid by an <i>authorised fund manager</i> .
	(4)	In accordance with SUP 16.6.8R, a <i>depository</i> should also make a return to the FSA on a quarterly basis which summarises the number of instances of incorrect pricing during a particular period.



5	The rectification of pricing breaches	
	(1)	COLL 6.6.3R (Functions of the authorised fund manager) places a duty on the <i>authorised fund manager</i> to take action to reimburse affected <i>unitholders</i> , former <i>unitholders</i> , and the <i>scheme</i> itself, for instances of incorrect pricing, except if it appears to the <i>depository</i> that the breach is of minimal significance.
	(2)	A <i>depository</i> may consider that the instance of incorrect pricing is of minimal significance if: <ul style="list-style-type: none"> <li data-bbox="421 539 1310 613">(a) the <i>authorised fund manager</i> and <i>depository</i> meet the standards of control set out in Section 2 and Section 3 of this Table; and</li> <li data-bbox="421 629 1310 663">(b) the error in pricing of a <i>unit</i> is less than 0.5% of the correct <i>price</i>.</li> </ul>
	(3)	In determining (2), if the instance of incorrect pricing is due to one or more factors or exists over a period of time, each <i>price</i> should be considered separately.
	(4)	If a <i>depository</i> deems it appropriate, it may, in spite of the circumstances outlined in (2), require a payment from the <i>authorised fund manager</i> or from the <i>authorised fund</i> to the <i>unitholders</i> , former <i>unitholders</i> , the <i>authorised fund</i> or the <i>authorised fund manager</i> (where appropriate).
	(5)	The <i>depository</i> should satisfy itself that any payments required following an instance of incorrect pricing are accurately and promptly calculated and paid.
	(6)	If a <i>depository</i> considers that reimbursement or payment is inappropriate, it should report the matter to the <i>FSA</i> , together with its recommendation and justification. The <i>depository</i> should take into account the need to avoid prejudice to the rights of <i>unitholders</i> , or the rights of <i>unitholders</i> in a <i>class</i> of <i>units</i> .
	(7)	It may not be practicable, or in some cases legally permissible, for the <i>authorised fund manager</i> to obtain reimbursement from <i>unitholders</i> , where the <i>unitholders</i> have benefited from the incorrect <i>price</i> .
	(8)	In all cases where reimbursement or payment is required, amounts due to be reimbursed to <i>unitholders</i> for individual sums which are reasonably considered by the <i>authorised fund manager</i> and <i>depository</i> to be immaterial, need not normally be paid.

### SDRT Provision

- 6.3.7 R (1) The *authorised fund manager* may, in accordance with the *prospectus*, require the payment of an *SDRT provision* for the *issue* or *sale* of *units* or any *class* of *units* or the deduction of an *SDRT provision* for the *redemption* or *cancellation* of *units* or any *class* of *units*.

- (2) Any such payment or deduction becomes due at the same time as payment or transfer of property becomes due for the *issue, sale, redemption* or *cancellation*.
- (3) Any payment referred to in (1) must be paid to the *depository* to become part of *scheme property* as soon as practicable after receipt.
- (4) As soon as practicable after each *valuation point*, the *authorised fund manager* must notify the *depository* of the transactions, or types of transactions for which an *SDRT provision* is applied and the amounts or rates of those *SDRT provisions*.

### **Dilution**

- 6.3.8 R (1) When arranging to *sell, redeem, issue* or *cancel units*, or when *units* are *issued* or *cancelled* under COLL 6.2.7R (Issues and cancellations through an authorised fund manager), an *authorised fund manager* is permitted to:
- (a) require the payment of a *dilution levy*; or
  - (b) make a *dilution adjustment*; or
  - (c) neither require a *dilution levy* nor make a *dilution adjustment*;
- in accordance with its statements in the *prospectus* required by COLL 4.2.5R 18 (Table: contents of the prospectus).
- (2) An *authorised fund manager* operating either a *dilution levy* or a *dilution adjustment*, must operate that measure in a fair manner to reduce *dilution* and solely for that purpose.
  - (3) A *dilution levy* becomes due at the same time as payment or transfer of property becomes due for the *issue, sale, redemption* or *cancellation* and any such payment in respect of a *dilution levy* must be paid to the *depository* to become part of *scheme property* as soon as practicable after receipt.

- (4) A *dilution adjustment* may be made as part of the calculation of the *unit price* for the purpose of reducing *dilution* in the *scheme* or to recover any amount which it had already paid or reasonably expects to pay in the future in relation to the *issue* or *cancellation* of *units*.
- (5) Where the *authorised fund manager* decides to make or not to make a *dilution adjustment*, it must not do so for the purpose of creating a profit or avoiding a loss for the account of an *affected person*.
- (6) As soon as practicable after a *valuation point*, the *authorised fund manager* must provide the *depository* with the amount or rate of any *dilution adjustment* made to the *price* or any *dilution levy* applied.

#### **Forward and historic pricing**

- 6.3.9 R (1) For the *sale* and *redemption* of *units*, the *authorised fund manager* must, in accordance with the *prospectus* of an *authorised fund*, operate on the basis of *forward price* only or *historic prices*.
- (2) If *forward prices* only are to be used, all deals must be at a *forward price*.
- (3) *Forward prices* for the *sale* and *redemption* of *units* must be used:
- (a) for a *higher volatility fund*;
  - (b) where the regular *valuation points* are more than one *day* apart;
  - (c) if the request to deal reaches the *authorised fund manager* through the post or by any similar form of non-interactive communication;
  - (d) for an *issue* or *cancellation* under COLL 6.2.7 (Issue and cancellation of units through an authorised fund manager);
  - (e) if the applicant for the *sale* or *redemption* so requests; or

- (f) where the *authorised fund manager* has reason to believe at any time that the *price* that would reflect the current value of the *scheme property* would vary by more than 2% from the last calculated *price*, unless the *authorised fund manager* has decided to carry out an additional valuation.
- (4) If an *authorised fund manager* operates *historic prices*, the *prospectus* must detail the circumstances under which *deals* in the *authorised fund*, individually or otherwise, will nevertheless be carried out on a *forward price* basis or when the *authorised fund* will elect to move to *forward prices* or declare an additional *valuation point*.
- (5) Where the *authorised fund* elects to move to *forward prices* temporarily in accordance with (4), such election will only apply until the next *valuation point*.
- (6) All *sub-funds* of a *scheme* which is an *umbrella* must adopt the same pricing basis, but this does not apply merely because of a requirement to price on a *forward price* basis temporarily under this *rule*.

**Historic pricing: guidance**

- 6.3.10 G The *authorised fund manager* should advise the *depository* of the date and time of any decision to use *forward prices*.

**Publication of prices**

- 6.3.11 R Where the *authorised fund manager* is prepared to deal in *units*, or is willing to *issue* or cancel *units*, under *COLL* 6.2.7, it must make the dealing *prices* public in an appropriate manner.

**Manner of price publication**

- 6.3.12 G (1) In determining the appropriate manner of making *prices* public, the *authorised fund manager* should ensure that:
- (a) a *unitholder* or potential *unitholder* can obtain the *prices* at a reasonable cost;
  - (b) *prices* are available at reasonable times;

- (c) publication is consistent with the manner and frequency at which the *units* are sold;
  - (d) the manner of publication is disclosed in the *prospectus*;  
and
  - (e) *prices* are published in a consistent manner.
- (2) Examples of what might be deemed appropriate include:
- (a) publication in a national newspaper;
  - (b) supply through an advertised local rate or freephone telephone number;
  - (c) publication on the internet;
  - (d) inclusion in a database of *prices* which is publicly available; or
  - (e) communication to all existing *unitholders*.
- (3) The *authorised fund manager* should make previous *prices* available to any *unitholder* or potential *unitholder*.

## 6.4 Title and registers

### Application

- 6.4.1 R (1) This section applies to a *manager* and a *trustee* of an *AUT*.  
(2) *COLL* 6.4.9 (Plan registers) also applies to the *ACD*, any other *director* and the *depository* of an *ICVC*.

### Purpose

- 6.4.2 G The aim of this section is to protect *consumers*, by setting out the requirements for a *register* of *unitholders* for an *AUT* and for a *plan register* for an *authorised fund*, so a proper record of ownership of *units* is maintained, whether held directly or indirectly through a *group plan*.

### Explanation of this section

- 6.4.3 G (1) This section deals with matters relating to the *register* of *unitholders* of *units* in an *AUT* including its establishment and contents. The *manager* or *trustee* may be responsible for the *register*. In any event, the *person* responsible for the *register* must be stated in the *trust deed* and this section details what his duties are. The provisions relating to *documents evidencing title to units*, including the issue of *bearer certificates* are dependent on the provisions in the *trust deed* and their operation should be set out in the *prospectus*.  
(2) For an *ICVC*, requirements as to the *register* of *holders* and transfer of *units* are contained in Schedule 3 of the *OEIC Regulations* (Register of shareholders).  
(3) *COLL* 6.4.9R makes provision to ensure that if the cost of the *plan register* is borne by the *scheme*, *plan investors* have the same rights in respect of notice and disclosure as *unitholders* on the main *register*.

### Register: general requirements and contents

- 6.4.4 R (1) Either the *manager* or the *trustee* (as nominated in the *trust deed*) must establish and maintain a *register* of *unitholders* as a *document* in accordance with this section.

- (2) The *manager* or *trustee* in accordance with their duties under (1) must exercise all due diligence and take all reasonable steps to ensure the information contained on the *register* is at all times complete and up to date.
- (3) The *register* must contain:
  - (a) the name and address of each *unitholder* (for joint *unitholders*, no more than four need to be registered) other than *units* represented by *bearer certificates*;
  - (b) the number of *units* of each *class* held by each *unitholder* (other than *units* represented by *bearer certificates*);
  - (c) the date on which the *unitholder* was registered for *units* standing in his name (other than *units* represented by *bearer certificates*); and
  - (d) the number of *units* of each *class* currently in *issue*, including *bearer certificates* and the number of *units* of those *bearer certificates*.
- (4) No notice of any trust, express, implied or constructive which may be entered in the *register* is binding on the *manager* or *trustee*, but this does not affect their obligations under *COLL* 6.4.9R (Plan registers).
- (5) The *register* is conclusive evidence of the *persons* entitled to the *units* entered in it.
- (6) The *person* responsible for the *register* in (1) must:
  - (a) take reasonable steps to alter the *register* on receiving written notice of a change of name or address of any *unitholder*;
  - (b) in relation to a change of name in (a) where a certificate has been issued, either endorse the existing certificate or issue a new one;

- (c) make the *register* available for inspection free of charge in the *United Kingdom* by or on behalf of any *unitholder* (including the *manager*), during office hours, but it may be closed for periods not exceeding 30 *business days* in any one year;
- (d) supply free of charge to any *unitholder* or his authorised representative a copy of the entries on the *register* relating to that *unitholder* on request;
- (e) where a *unitholder* defaults on paying for the *issue* or sale of *units*, make an alteration or deletion in the *register* to compensate for the default after which the *manager* becomes entitled to those *units* (until those *units* are either cancelled or re-sold and paid for); and
- (f) carry out any conversion of *units* allowed for by *COLL* 6.4.8R (Conversion of units) after consultation with the *manager* or *trustee*, as appropriate.

**The manager as unitholder**

- 6.4.5 R (1) If no *person* is entered in the *register* as the *unitholder* of a *unit*, the *manager* must be treated as the *unitholder* of each such *unit* which is in *issue* (other than a *unit* which is represented by a *bearer certificate*).
- (2) Where *units* are transferred to the *manager*, they need not be *cancelled* and the *manager* need not be entered on the *register* as the new *unitholder*.

**Transfer of units by act of parties**

- 6.4.6 R (1) Every *unitholder* is entitled to transfer *units* held on the *register* by an instrument of transfer in any form that the *person* responsible for the *register* may approve, but that *person* is under no duty to accept a transfer unless:
- (a) it is permitted by the *trust deed* or *prospectus*; and



- (b) the transfer is excluded by Schedule 19 of the Finance Act 1999 from a charge to stamp duty reserve tax, or there has been paid to the *trustee*, for the account of the *AUT*, an amount agreed between the *trustee* and the *manager* not exceeding the amount that would be derived by applying the rate of stamp duty reserve tax to the market value of the *units* being transferred.
- (2) Every instrument of transfer of *units* must be signed by, or on behalf of, the *unitholder* transferring the *units* (or, for a *body corporate*, sealed by that *body corporate* or signed by one of its *officers* (or in Scotland, two of its *officers*)) authorised to sign it and, unless the transferee is the *manager*, the transferor must be treated as the *unitholder* until the name of the transferee has been entered in the *register*.
- (3) Every instrument of transfer (stamped as necessary) must be left for registration, with the *person* responsible for the *register*, accompanied by:
  - (a) any necessary documents that may be required by legislation; and
  - (b) any other evidence reasonably required by the *person* responsible for the *register*.
- (4) The details of instruments of transfer must be kept for a period of six years from the date of its registration.
- (5) On registration of an instrument of transfer, a record of the transferor and the transferee and the date of transfer must be made on the *register*.

**Certificates (including bearer certificates)**

- 6.4.7 R (1) Following the *sale* of *units* or as a result of *COLL* 6.4.6R (Transfer of units by act of parties) a document recording title to those *units* may be issued in such a form as the *trust deed* permits.

- (2) The person responsible for the *register* must issue any document in (1) or provide relevant information in a timely manner where the procedures for redeeming *units* require the *unitholder* to surrender that document.
- (3) *Bearer certificates* may only be issued if they are permitted by the *instrument constituting the scheme*.

**Conversion of units**

- 6.4.8 R Where there is more than one *class* of *units* offered for *issue* or *sale*, the *unitholder* has a right to convert from one to the other, provided that doing so would not contravene any provision in the *prospectus*.

**Plan registers**

- 6.4.9 R (1) The *ACD* and any other *directors* of an *ICVC* or the *person* responsible for the *register* of an *AUT* may arrange for a *plan register* to be established and maintained.
- (2) Where payments are made out of *scheme property* to establish and maintain a *plan register*, *plan investors* must be treated as *unitholders* for the purposes of *COLL* 4.3 to 4.5 and *COLL* 6.4.4R (Register: general requirements and contents).

## 6.5 Appointment and replacement of the authorised fund manager and the depositary

### Application

6.5.1 R This section applies in accordance with *COLL 6.5.2R* (Table of application).

6.5.2 R Table of application  
This table belongs to *COLL 6.5.1R*.

<i>Rule</i>	<i>ICVC</i>	<i>ACD</i>	<i>Any other director of an ICVC</i>	<i>Depositary of an ICVC</i>	<i>Manager of an AUT</i>	<i>Trustee of an AUT</i>
6.5.1R	x	x	x	x	x	x
6.5.3R	x	x	x	x		
6.5.4R		x	x	x		
6.5.5R		x	x			
6.5.6R	x			x		
6.5.7R					x	x
6.5.8R					x	x
6.5.9R					x	x
6.5.10R		x		x	x	x
Note: "x" means "applies", but not every paragraph in every <i>rule</i> will necessarily apply.						

### Appointment of an ACD

- 6.5.3 R (1) The *directors* (or *director*) of an *ICVC* must take all practicable steps to ensure the *ICVC* has at all times as its *ACD* a *person* who is qualified to act as *ACD*.
- (2) If the *ICVC* ceases to have any *director*, the *depositary* must exercise its powers, under the *OEIC Regulations*, to appoint a *person* to be an *ACD* of the *ICVC*.
- (3) The appointment of an *ACD* (other than the first *ACD*), under (1) or (2), must terminate at the close of the next annual general meeting following the date of the appointment or (if later) upon the expiration of 12 *months* from the date the appointment takes

effect, unless the appointment has been approved by a resolution of the *unitholders* before the close of that annual general meeting or expiration of that 12 *month* period (as the case may be).

- (4) An *ACD* must not voluntarily terminate its appointment as *ACD* unless the termination is effective at the same time as the commencement of the appointment of a successor *ACD*.
- (5) (a) In the event of:
  - (i) any *person* becoming or ceasing to be a *director*;
  - (ii) the appointment of an *ACD* being terminated;
  - (iii) a new *ACD* being appointed; or
  - (iv) a corporate *director* (including the *ACD*) becoming aware of any change of its *controller*;the *FSA* must immediately be notified in accordance with (b).
- (b) In the case of:
  - (i) (a)(i), by the *ACD*;
  - (ii) (a)(ii), by the *ACD* whose appointment is being terminated;
  - (iii) (a)(iii), by the new *ACD*; and
  - (iv) (a)(iv), by the corporate *director* concerned.

#### **Termination of appointment of an ACD**

- 6.5.4 R (1) The appointment of an *ACD* terminates immediately upon it ceasing to be a *director*.
- (2) The appointment of an *ACD* terminates if a notice of termination of that appointment, the terms of which have been approved by a resolution of the board of *directors* of the *ICVC*, is given to the *ACD*.
- (3) If there is no *director* other than the *ACD*, the appointment of the *ACD* terminates if a notice of termination of that appointment is given by the *depository* to the *ACD* and to the *ICVC*, following any of the following events:
- (a) the calling of a meeting to consider a resolution for winding up the *ACD*;

- (b) an application being made to dissolve the *ACD* or to strike it off the Register of Companies;
  - (c) the presentation of a petition for the winding up of the *ACD*;
  - (d) the making of, or any proposals for the making of, a composition or arrangement with any one or more of the *ACD's* creditors;
  - (e) the appointment of a receiver to the *ACD* (whether an administrative receiver or a receiver appointed over particular property);
  - (f) anything equivalent to (a) to (e) above occurring in respect of the *ACD* in a jurisdiction outside the *United Kingdom*.
- (4) Any termination under (2) or (3) takes effect when the notice is given, or on any subsequent time for its effect stated in the notice, or, if later, the time at which the termination is permitted to take effect under regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company).
- (5) The *depository* must (unless the termination takes effect at the same time as the appointment of a successor *ACD*) ensure that the unitholders are informed of the termination of the appointment of an *ACD*.
- (6) The *depository* is entitled to be reimbursed out of the *scheme property* for its out of pocket expenses in complying with (5).

**Other directors**

- 6.5.5 R (1) Any *directors* of an *ICVC* other than the *ACD* must exercise reasonable care to ensure that the *ACD* undertakes the responsibilities allocated under *COLL 6.6.3R* (Functions of the authorised fund manager) in a competent manner and the *ACD* must give those *directors* the information and explanations they consider necessary for this purpose.
- (2) A *director* of an *ICVC* must not appoint an alternate *director*.

- (3) When there is no *person* acting as *ACD*, the *directors* of an *ICVC* have the functions of an *ACD* under *COLL* 6.6.3R, but this does not affect the powers of the *directors* under *COLL* 6.6.15R (Committees and delegation).
- (4) When (3) applies, the *directors* must retain the services of one or more *authorised persons* to assist them in performing the functions referred to in *COLL* 6.6.3R (1) and (2).

#### **ICVC without a director**

- 6.5.6 R If the *ICVC* ceases to have any *directors*, the *depository* may:
- (1) retain the services of an *authorised person* to carry out the functions referred to in *COLL* 6.6.3R(3)(a) and(b); or
  - (2) manage the *scheme property* itself on behalf of the *ICVC* until a *director* is appointed or the winding up of the *ICVC* is commenced provided it is not prohibited from doing so by any law or *rule*.

#### **Replacement of a manager**

- 6.5.7 R (1) The *manager* of an *AUT* is subject to removal by written notice by the *trustee* upon any of the following events:
- (a) the calling of a meeting to consider a resolution for winding up the *manager*;
  - (b) an application being made to dissolve the *manager* or to strike it off the Register of Companies;
  - (c) the presentation of a petition for the winding up of the *manager*;
  - (d) the making of, or any proposals for the making of, a composition or arrangement with any one or more of the *manager's* creditors;
  - (e) the appointment of a receiver to the *manager* (whether an administrative receiver or a receiver appointed over particular property);
  - (f) anything equivalent to (a) to (e) above occurring in respect of the *manager* in a jurisdiction outside the *United Kingdom*;

- (g) the *trustee* forming the reasonable opinion, and stating in writing, that a change of *manager* is desirable in the interest of *unitholders*;
  - (h) a resolution of *unitholders* being passed to remove the *manager*; or
  - (i) the *unitholders* of three quarters in value of the *units in existence* (excluding *units* held or treated as held by the *manager* or by any *associate* of the *manager*) making a request in writing to the *trustee* that the *manager* should be removed.
- (2) On receipt of a notice by the *trustee* under (1), the *manager* of the *AUT* ceases to be the *manager*; and the *trustee* must by deed appoint another *person* eligible under the *Act* to be the *manager* of the *AUT* upon and subject to that other entering into such deed or deeds as the *trustee* may require.
- (3) If the name of the *AUT* contains a reference to the name of the former *manager*, the former *manager* is entitled to require the new *manager* and the *trustee* immediately on receipt of a notice under (1) to propose a change in the name of the *AUT*.

#### **Retirement of a manager of an AUT**

- 6.5.8 R (1) The *manager* of an *AUT* has the right to retire in favour of another *person* eligible under the *Act* and approved in writing by the *trustee* upon:
- (a) the retiring *manager* appointing that *person* by deed as *manager* in its place and assigning to that *person* all its rights and duties as such a *manager*; and
  - (b) the new *manager* entering into such deeds as the *trustee* reasonably considers necessary or desirable to be entered into by that *person* in order to secure the due performance of its duties as the *manager* of the *AUT*.
- (2) Upon retirement, the retiring *manager*:
- (a) subject to (3), is released from all further obligations under the *rules* in this sourcebook and under the *trust*

*deed*; and

- (b) may retain any consideration paid to it in connection with the change without having to account for it to any *unitholder*.
- (3) Sub-paragraph (2)(a) does not affect the rights of the *trustee* or any other *person* in respect of any act or omission on the part of the retiring *manager* before his retirement.

**Consequences of removal or retirement of a manager of an AUT**

- 6.5.9 R (1) Upon the removal or retirement of the *manager*, the removed or retiring *manager*:
- (a) is entitled to be recorded in the *register* for those *units* continued to be held or treated as held by it; and
  - (b) may require the *trustee* to issue to it a certificate for those *units* (if not previously issued).
- (2) Paragraph (1) is subject to any restriction in the *prospectus* relating to the permitted categories of *unitholders*.

**Retirement of the depositary**

- 6.5.10 R (1) The *depositary* of an *authorised fund* may not retire voluntarily except upon the appointment of a new *depositary*.
- (2) The *depositary* of an *authorised fund* must not retire voluntarily unless, before its retirement, it has ensured that the new *depositary* has been informed of any circumstance of which the retiring *depositary* has informed the *FSA*.
- (3) When the *depositary* of an *authorised fund* wishes to retire or ceases to be an *authorised person*, the *authorised fund manager* may, subject to section 251 of the *Act* (Alteration of schemes and changes of manager or trustee) or regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company) appoint another *person* eligible to be the *depositary* in its place.



**6.6 Powers and duties of the scheme, the authorised fund manager, and the depositary**

**Application**

6.6.1 R This section applies in accordance with *COLL 6.6.2R* (Table of application).

**Table of application**

6.6.2 R This table belongs to *COLL 6.6.1R*.

<i>Rule</i>	<i>ICVC</i>	<i>ACD</i>	Any other <i>directors of</i> an <i>ICVC</i>	<i>Depositary of</i> an <i>ICVC</i>	<i>Manager</i> of an <i>AUT</i>	<i>Trustee</i> of an <i>AUT</i>
6.6.1R	x	x	x	x	x	x
6.6.3R	x	x		x	x	x
6.6.4R				x		x
6.6.5R		x	x	x	x	x
6.6.6R		x			x	
6.6.7R	x	x				
6.6.8R					x	x
6.6.9R					x	x
6.6.10R		x		x	x	x
6.6.11G				x		x
6.6.12R				x		x
6.6.13R		x	x	x	x	x
6.6.14R		x		x	x	x
6.6.15R	x	x	x	x	x	x
6.6.16G		x		x	x	x
6.6.17R		x	x	x	x	x
6.6.18G		x	x	x	x	x
Note: "x" means "applies", but not every paragraph in every <i>rule</i> will necessarily apply.						

### Functions of the authorised fund manager

- 6.6.3 R (1) The *authorised fund manager* must manage the *scheme* in accordance with:
- (a) the *instrument constituting the scheme*;
  - (b) the *rules* in this sourcebook;
  - (c) the most recently published *prospectus*; and
  - (d) for an *ICVC*, the *OEIC Regulations*.
- (2) The *authorised fund manager* must take such steps as necessary to ensure compliance with the *rules* in this sourcebook that impose obligations upon the *ICVC*.
- (3) The *authorised fund manager* must:
- (a) make decisions as to the constituents of the *scheme property* in accordance with the investment objectives and policy of the *scheme*;
  - (b) instruct the *depository* in writing how rights attaching to the ownership of the *scheme property* are to be exercised, but not where *COLL* 6.6.13R(2) (Exercise of rights in respect of the scheme property) applies; and
  - (c) take action immediately to rectify any breach of *COLL* 6.3 and, where the breach relates to the incorrect pricing of *units* or to the late payment in respect of the *issue* of *units*, the rectification must, (unless the *depository* otherwise directs under (4)), extend to the reimbursement or payment, or arranging the reimbursement or payment, of *money*:
    - (i) by the *authorised fund manager* to *unitholders* and former *unitholders*;
    - (ii) by the *ACD* to the *ICVC*;
    - (iii) by the *ICVC* to the *ACD*;
    - (iv) by the *manager* to the *trustee*; or
    - (v) by the *trustee* (for the account of the *AUT*) to the *manager*.

- (4) Rectification under (3)(c) need not, unless the *depository* so directs, extend to any such reimbursement or payment where it appears to the *depository* such breach, is of minimal significance.

#### **General duties of the depository**

- 6.6.4 R (1) The *depository* of an *authorised fund* must take reasonable care to ensure that the *scheme* is managed by the *authorised fund manager* in accordance with:
- (a) *COLL 5* (Investment and borrowing powers);
  - (b) *COLL 6.2* (Dealing);
  - (c) *COLL 6.3* (Valuation and pricing);
  - (d) *COLL 6.8* (Income: accounting, allocation and distribution); and
  - (e) any provision of the *instrument constituting the scheme* or *prospectus* that relates to the provisions referred to in (a) to (d).
- (2) The *depository* must, in so far as not required under (1)(c), take reasonable care to ensure on a continuing basis that:
- (a) the *authorised fund manager* is adopting appropriate procedures to ensure that the *price* of a *unit* is calculated for each *valuation point* in accordance with *COLL 6.3*; and
  - (b) the *authorised fund manager* has maintained sufficient records to show compliance with *COLL 6.3*.
- (3) The *depository*, when acting in its capacity as *depository*, must act solely in the interests of the *unitholders*.
- (4) The *depository*:
- (a) must also take reasonable care to ensure that;
    - (i) the *authorised fund manager* considers whether or not to exercise the power provided by *COLL 6.3.7R* (SDRT provision) or *COLL 6.3.8R* (Dilution) (as the case may be) and, if applicable, the rate or amount of any *SDRT provision*, *dilution levy* or

- dilution adjustment* that is imposed;
  - (ii) the *authorised fund manager* has in relation to (i), taken account of all factors that are material and relevant to the *authorised fund manager's* decision; and
  - (iii) when the *authorised fund manager* considers whether or not to exercise the power under *COLL 6.3.8R*, the *authorised fund manager* has acted in accordance with the restrictions imposed by that *rule*; and
- (b) has no duty in respect of the *authorised fund manager's* exercise of the discretion referred to in (a).

**Duties of the authorised fund manager and the depositary under the general law**

- 6.6.5 R (1) The duties and powers of the *authorised fund manager*, the *directors* of an *ICVC* and the *depositary* under the *rules* in this sourcebook and under the *instrument constituting the scheme* are in addition to the powers and duties under the general law.
- (2) Paragraph (1) applies only in so far as the relevant general law is not qualified by the *rules* in this sourcebook or the *instrument constituting the scheme* or the *OEIC Regulations*.

**Maintenance of records**

- 6.6.6 R (1) The *authorised fund manager* must make and retain for six years such records as enable:
- (a) the *scheme* and the *authorised fund manager* to comply with the *rules* in this sourcebook and the *OEIC Regulations*; and
  - (b) it to demonstrate at any time that such compliance has been achieved.
- (2) The *authorised fund manager* must make and retain for six years a daily record of the *units* in the *scheme* held, acquired or disposed of by the *authorised fund manager*, including the

*classes* of such *units*, and of the balance of any acquisitions and disposals.

- (3) Where relevant, an *authorised fund manager* must make and retain for a period of six years a daily record of:
  - (a) how it calculates and estimates *dilution*; and
  - (b) its policy and method for determining the amount of any *dilution levy* or *dilution adjustment*.
- (4) The *authorised fund manager* must on the request of the *depository* immediately supply it with such information concerning the management and administration of the *authorised fund* as the *depository* may reasonably require.

**Maintenance of capital: notification**

- 6.6.7 R The *ACD* must immediately notify the *FSA* in writing if the *ICVC's* capital falls below the minimum or exceeds the maximum stated in the *instrument of incorporation*.

**Auditor: AUTs**

- 6.6.8 R (1) The *manager* of an *AUT* must, upon any vacancy for the position of auditor for an *AUT*, with the approval of the *trustee*, appoint as auditor for the *AUT* a *person* qualified for appointment as auditor of an *authorised person*.
- (2) The audit fees of the auditor are determined by the *manager* with the approval of the *trustee*.
- (3) The *manager* of an *AUT* may, with the approval of the *trustee*, at any time, remove the auditor of an *AUT*; this power exists notwithstanding anything in any agreement between the *persons* concerned.

**Returns: AUTs**

- 6.6.9 R The *manager* of an *AUT* must prepare and supply to the *trustee* the returns required to be submitted by the *trustee* to the Board of Inland Revenue.

**Dealings in scheme property**

- 6.6.10 R (1) The *authorised fund manager* may give instructions to deal in the property of the *scheme*.

- (2) The *authorised fund manager* must obtain the consent of the *depository* for the acquisition or disposal of immovable property.
- (3) Where the *depository* is of the opinion that a deal in property is not within the *rules* in this sourcebook and the *instrument constituting the scheme*, the *depository* may require the *authorised fund manager* to cancel the transaction or make a corresponding disposal or acquisition to secure restoration of the previous situation and to meet any resulting loss or expense.
- (4) Where the *depository* is of the opinion that:
  - (a) an acquisition of property necessarily involves documents evidencing title being kept in the custody of a *person* other than the *depository*; and
  - (b) the *depository* cannot reasonably be expected to accept the responsibility which would otherwise be placed upon it if it were to permit custody by that other *person*;
 the *authorised fund manager* must, if the *depository* so requests, either cancel the transaction or make a corresponding disposal.

**Duty to inform the FSA**

- 6.6.11 G *SUP* 15.3 (General notification requirements) contains *rules* and *guidance* on matters that should be notified to the *FSA*. Such matters include, but are not limited to, any circumstance that the *depository* becomes aware of whilst undertaking its functions or duties in *COLL* 6.6.4 (General duties of the depository) that the *FSA* would reasonably view as significant.

**Control by the depository over the scheme property**

- 6.6.12 R (1) The *depository* of an *authorised fund* is responsible for the safekeeping of all of the *scheme property* (other than tangible movable property) entrusted to it and must:
- (a) take all steps and complete all documents needed to ensure completion of transactions properly entered into for the account of the *scheme*;

- (b) ensure that *scheme property* in registered form is, as soon as practicable, registered in the name of the *depository*, its nominee or a *person* retained by it under COLL 6.6.15R (Committees and delegation);
  - (c) take into its *custody* or under its control documents of title to the *scheme property* other than for transactions in *derivatives* or forward transactions; and
  - (d) ensure that any transaction in *derivatives* or a forward transaction is entered into so as to ensure that any resulting benefit is received by the *depository*.
- (2) The *depository* is responsible for the collection of income due to be paid for the account of the *authorised fund*.
  - (3) The *depository* must keep for six years such records as are necessary:
    - (a) to enable it to comply with the *rules* in this sourcebook; and
    - (b) to demonstrate that it has achieved such compliance.

**Exercise of rights in respect of the scheme property**

- 6.6.13 R (1) The *depository* must take all necessary steps to ensure that instructions given to it by the *authorised fund manager* for the exercise of rights attaching to the ownership of *scheme property* are carried out.
- (2) Where the *scheme property* of an *authorised fund* contains *units* in any other *scheme* managed or otherwise operated by the *manager* of the *AUT* or, as the case may be, by any *director* of the *ICVC* or by any *associate* of either, the *depository* must exercise any voting rights associated with those *units* in accordance with what he reasonably believes to be the interests of the *unitholders* in the *authorised fund*.

**Duties of the depository and the authorised fund manager: investment and borrowing powers**

- 6.6.14 R (1) The *authorised fund manager* must avoid the *scheme property* being used or invested contrary to *COLL 5*, or any provision in the *instrument constituting the scheme* or the *prospectus* as referred to in *COLL 5.2.4R* (Investment powers:general), except to the extent permitted by (3)(b).
- (2) The *authorised fund manager* must, immediately upon becoming aware of any breach of a provision listed in (1), take action, at its own expense, to rectify that breach, unless the breach occurred as the result of any of the circumstances within (3).
- (3) The *authorised fund manager* must restore compliance with *COLL 5* as soon as reasonably practicable having regard to the interests of the *unitholders* and, in any event, within the period specified in (5) or, when applicable, (6) where:
- (a) the *scheme property* is:
- (i) used or invested contrary to *COLL 5* (other than a provision excusing a failure to comply on a temporary basis); and
  - (ii) the contravention is beyond the control of both the *authorised fund manager* and the *depository*; or
- (b) there is a transaction (“subsequent transaction”) deriving from a right (such as the right to convert stock or subscribe to a rights issue) attributable to an *investment* (‘original *investment*’) of the scheme if:
- (i) the subsequent transaction, but for this *rule* would constitute a breach of *COLL 5*; and
  - (ii) at the time of the acquisition of the original *investment*, it was reasonable for the *authorised fund manager*, to expect that a breach would not be caused by the subsequent transaction; and
- in this rule the reference to the exercise of a right includes the taking effect of a right without any action by or on behalf of the *depository* or the *authorised fund manager*.



- (4) Immediately upon the *depository* becoming aware of any breach of any provision listed in (1), it must ensure that the *authorised fund manager* complies with (2).
- (5) The maximum period for restoration of compliance under (3) starts at the date of discovery of the relevant circumstance and lasts, subject to any extension under (6):
  - (a) for six *months*; or
  - (b) where the transaction in question was a transaction in *derivatives* or a forward transaction under *COLL 5.2.20R* (Permitted transactions (derivatives and forwards)) or *COLL 5.6.13R* (Permitted transactions (derivatives and forwards)), until the close of business five *business days* later; or
  - (c) where the transaction relates to an immovable, for two years.
- (6) The period specified at (5)(b) is extended where:
  - (a) the transaction involved a delivery of a *commodity*, from five to twenty *business days*;
  - (b) the reason for the contravention in (3)(a) is the inability of the *authorised fund manager* to *close out* a transaction because of a limit in the number or value of transactions imposed by an *eligible derivatives* market, until five *business days* after:
    - (i) the inability resulting from any such limit is removed; or
    - (ii) it becomes, to the knowledge of the *authorised fund manager*, reasonably practicable and reasonably prudent for the transaction to be *closed out* in some other way.

#### **Committees and delegation**

- 6.6.15 R (1) The *directors* of an *ICVC* may delegate to any one or more of their number any of the *directors'* powers or duties but remain responsible for the acts or omissions of any such *directors*.

- (2) The *authorised fund manager* of a *scheme* and the *directors* of an *ICVC* have the power to retain the services of anyone to assist in the performance of their respective functions, provided that:
- (a) a mandate in relation to *managing investments* of the *scheme property* is not given to:
    - (i) the *depository*; or
    - (ii) any other *person* whose interests may conflict with those of the *authorised fund manager* or the *unitholders*; or
    - (iii) any other *person* who is not both:
      - (A) authorised or registered for *managing of investments*; and
      - (B) subject to prudential supervision; unless there is an agreement in place between the *FSA* and the *overseas regulator* of the delegate ensuring adequate co-operation;
  - (b) the *authorised fund manager* ensures that at all times it can monitor effectively the relevant activities of any *person* so retained;
  - (c) the mandate permits the *authorised fund manager* to:
    - (i) give further relevant instructions to the *person* so retained; and
    - (ii) withdraw the mandate with immediate effect when this is in the interests of the *unitholders*; and
  - (d) the mandate does not prevent effective supervision of the *authorised fund manager* and it must not prevent the *authorised fund manager* from acting, or the *scheme* from being managed in the best interests of the *unitholders*.
- (3) Subject to the provisions of the *OEIC Regulations* and to (1), where services are retained under (2), the responsibility which the *authorised fund manager* had in respect of such services prior to that retention of services will remain unaffected.

- (4) The *depository of a scheme* may delegate any function to any *person* save:
- (a) the *ICVC* or any *director* of the *ICVC* or the *authorised fund manager* of a *scheme*, to assist the *depository* to perform:
    - (i) any function of oversight in respect of the *scheme*, its *directors* or the *authorised fund manager* as the case may be; or
    - (ii) any function of *custody* or control of the *scheme property*;
  - (b) an *associate* of the *ICVC* or of any of the *directors* of the *ICVC* or of the *authorised fund manager* of the *scheme* (as the case may be) to assist the *depository* to perform any function in (a)(i); or
  - (c) a *nominee company* or anyone else to assist it to perform the function of being a *custodian* of *documents* evidencing title to *scheme property* of the *scheme* unless the arrangements with the *custodian* prohibit the *custodian* from releasing the *documents* into the possession of a third party without the consent of the *depository*.
- (5) Where a *depository* retains services under (4):
- (a) if it retains the services of a *director* of the *ICVC*, or an *associate* or such a *director* or its own *associate*, then its liability for those services shall remain unaffected; and
  - (b) in any other case, it will not be held responsible by virtue of the *rules* in *COLL* for any act or omission of the *person* so retained if it can show that:
    - (i) it was reasonable for it to obtain assistance to perform the function in question;
    - (ii) the *person* retained was and remained competent to provide assistance in the performance of the function in question; and

- (iii) it had taken reasonable care to ensure that the assistance in question was provided by the *person* retained in a competent manner.
- (6) Where *COLL* 6.5.5R(4) (Other directors) applies, the *directors* have, in respect of the functions of the *ACD* under *COLL* 6.6.3R (Functions of the authorised fund manager), the same rights and responsibilities as for an *ACD* under this *rule*.

**Delegation: guidance**

- 6.6.16 G (1) *SYSC* 3.2 (Areas covered by systems and controls) contains *guidance* relating to delegation, including external delegation. *SYSC* 3.2.4G(1) states that a *firm* cannot contract out of its regulatory obligations.
- (2) *SUP* 15.8.6R (Delegation by UCITS management companies) requires an *authorised fund manager* of a *UCITS scheme* to inform the *FSA* where one of its duties is delegated to another *person*.

**Conflicts of interest**

- 6.6.17 R (1) The *authorised fund manager*, any other *director* of an *ICVC* and the *depository* must take reasonable care to ensure that a transaction within (a) to (f) is not carried out on behalf of the *scheme*:
- (a) putting cash on *deposit* with an *affected person* unless that *person* is an *eligible institution* or an *approved bank* and the arm's length requirement in (2) is satisfied;
  - (b) lending *money* by an *affected person* to, or for the account of, the *scheme*, unless the *affected person* is an *eligible institution* or an *approved bank*, and the arm's length requirement in (2) is satisfied;
  - (c) the dealing in property by an *affected person*, to, or with, the *scheme* (or the *depository* for the account of the *scheme*), unless (3) applies;
  - (d) the vesting of property (other than cash) by an *affected person* in the *scheme* or the *depository* for the account of

the *scheme* against the *issue* of *units* in the *scheme*,  
unless:

- (i) (3) applies; or
  - (ii) the purpose of the vesting is that the whole or part of the property of a *body corporate* or a *collective investment scheme* becomes the first property of the *scheme* and the *unitholders* of *shares* or *units* in the *body corporate* or *collective investment scheme* become the first *unitholders* in the *scheme*;
- (e) the *acquisition* of *scheme property* by an *affected person* from the *scheme* (or the *depository* acting for the account of the *scheme*), unless *COLL 6.2.15R* (In specie issue and cancellation) applies, or unless (3) applies; and
- (f) transactions within *COLL 5.4* (Stock lending) by an *affected person* with, or in relation to, the *scheme* unless the arm's length requirement in (2) is satisfied.
- (2) Any transaction in (1)(a),(b) or (f) must be at least as favourable to the *scheme* as any comparable arrangement on normal commercial terms negotiated at arm's length between the *affected person* and an independent party.
- (3) There is no breach of (1)(c), (d) or (e) if the transaction meets the requirements of (4) (best execution *on-exchange*), (5) (independent valuation) or (6) (arm's length transaction).
- (4) There is best execution *on-exchange* for the purposes of (3) if:
- (a) the property is an *approved security* or an *approved derivative*;
  - (b) the transaction is effected under the rules of the relevant exchange with or through a *person* who is bound by those rules;
  - (c) there is evidence in writing of the effecting of the transaction and of its terms; and
  - (d) the *authorised fund manager* has taken all reasonable steps to ensure that the transaction is effected on the terms

which are the best available for the *scheme*.

- (5) There is independent valuation for the purposes of (3) if:
  - (a) the value of the property is certified in writing for the purpose of the transaction by a *person* approved by the *depository* as:
    - (i) independent of any *affected person*; and
    - (ii) qualified to value property of the relevant kind; and
  - (b) the *depository* is of the opinion that the terms of the transaction are not likely to result in any material prejudice to *unitholders*.
- (6) There is an arm's length transaction for the purposes of (3) if:
  - (a) paragraph (4)(a) is not satisfied;
  - (b) it is not reasonably practicable to obtain an independent valuation under (5); and
  - (c) the *depository* has reliable evidence that the transaction is or will be on terms which satisfy the arm's length requirement in (2).

**Conflicts of interest: guidance**

- 6.6.18 G (1) *COB 7.1* (Conflict of interest and material interest) applies for *scheme management activity* and contains *rules* on the fair treatment of *customers* where a *firm* has a conflict of interest in relation to a transaction. *COLL 6.6.17R* provides *rules* for specific circumstances where *COB 7.1* would not be appropriate for an *authorised fund*.
- (2) Regulation 44 of the *OEIC Regulations* (Invalidity of certain transactions involving directors) is relevant to the application of *COLL 6.6.17R*.

## 6.7 Payments

### Application

6.7.1 R This section applies in accordance with *COLL 6.7.2R* (Table of application).

### Table of application

6.7.2 R Table of Application. This table belongs to *COLL 6.7.1R*.

<i>Rule</i>	<i>ICVC</i>	<i>ACD</i>	<i>Depository of an ICVC</i>	<i>Manager of an AUT</i>	<i>Trustee of an AUT</i>
6.7.1R to 6.7.5G	x	x	x	x	x
6.7.6G	x	x		x	
6.7.7R		x		x	
6.7.8G		x		x	
6.7.9R		x		x	
6.7.10R		x	x	x	x
6.7.11G		x	x	x	x
6.7.12R	x	x		x	
6.7.13G	x	x		x	
6.7.14R	x				
6.7.15R	x	x	x	x	x
6.7.16G		x	x	x	x
6.7.17R	x	x		x	

Note: "x" means "applies", but not every paragraph in every *rule* will necessarily apply.

### Purpose

- 6.7.3 G (1) This section assists in securing the *regulatory objective* of protecting *consumers* through requirements which govern the payments out of *scheme property* and charges imposed on investors when buying or selling *units*.
- (2) The requirements clarify the nature of permitted charges and payments and ensure the disclosure for *unitholders* of any increases in charges and payments to the *authorised fund manager*.
- (3) The *prospectus* should make adequate provision for payments from an *authorised fund*. This section:
- (a) prohibits, or stipulates the conditions on which, the payments out of the *scheme property* can be made;

- (b) requires certain payments to be conditional on disclosure in the *prospectus*; and
- (c) governs the allocation of payments between capital and income.

**Payments out of scheme property**

- 6.7.4 R (1) The only payments which may be recovered from the *scheme property* of an *authorised fund* are those in respect of:
- (a) remunerating the parties operating the *authorised fund*;
  - (b) the administration of the *authorised fund*; or
  - (c) the investment or safekeeping of the *scheme property*.
- (2) No payment under this *rule* can be made from *scheme property* if it is unfair to (or materially prejudices the interests of) any class of *unitholders* or potential *unitholders*.
- (3) Paragraphs (1) and (2) do not apply to any payments in relation to any taxation payable by the *authorised fund*.

**Payments out of scheme property: guidance**

- 6.7.5 G (1) Details of permissible types of payments out of *scheme property* are to be set out in full in the *prospectus* in accordance with *COLL* 4.2.5R 13 and 14 (Table: contents of the prospectus).
- (2) An *authorised fund manager* should consider *COB* 5.6.3R (Charges to a private customer) in determining whether a payment to an *affected person* is unfair because of its amount or because it confers a disproportionate benefit on the *affected person*.
- (3) *COLL* 6.7.4R(2) (Payments out of scheme property) does not invalidate a payment that gives rise to a difference between the rights of separate *classes* of *unit* that relates solely to the payments that may be taken out of *scheme property*.

**Performance fees**



- 6.7.6 G (1) For the *authorised fund manager's* periodic charge or for payments out of *scheme property* to the *investment adviser*, the *prospectus* may permit a payment based on a comparison of one or more aspects of the *scheme property* or *price* in comparison with fluctuations in the value or *price* of property of any description or index or other factor designated for the purpose (a "performance fee").
- (2) Any performance fee should be specified in the appropriate manner in the *prospectus* and should be consistent with *COLL 6.7.4R*. In determining whether the performance fee is consistent the *authorised fund manager* should have regard to factors such as:
- (a) it should be calculated and paid after consideration of all other payments;
  - (b) where it is made on the basis of performance of the *authorised fund* against any index or any other factor, that benchmark must be reasonable given the investment objectives of the *authorised fund* and must be consistently applied;
  - (c) it may be based on performance above a defined positive rate of return (the "hurdle rate"), which may be fixed or variable;
  - (d) where (b) or (c) applies, the benchmark or hurdle rate may be carried forward to future accrual periods;
  - (e) the period over which it accrues and the frequency with which it crystallises should be reasonable; and
  - (f) except where allowed by *COLL 6.7.4R*, there are to be no arrangements to adjust the *price* or value of *sale* or repurchase transactions in respect of performance fees accrued or paid if the transactions occur within the accrual period of the charge.

- (3) In accordance with *COLL* 4.2.5R 13 (Table: contents of prospectus) the *prospectus* should contain the maximum amount or percentage of *scheme property* that the performance fee might represent in an *annual accounting period*. This disclosure should be given in plain language together with examples of the operation of the performance fee.

#### **Charges on buying and selling units**

- 6.7.7 R (1) No *person* other than the *authorised fund manager* may impose charges on *unitholders* or potential *unitholders* when they buy or sell *units*.
- (2) An *authorised fund manager* must not make any charge or levy in connection with:
- (a) the *issue* or *sale* of *units* except where a *preliminary charge* is made in accordance with the *prospectus* of the *scheme* which must be either a fixed amount or calculated as a percentage of the *price* of a *unit*; or
  - (b) the *redemption* or *cancellation* of *units*, except a *redemption charge* made in accordance with the *prospectus* current at the time the relevant *units* were purchased by the *unitholder*.
- (3) This rule is subject to *COLL* 6.3.7R (SDRT provision) and *COLL* 6.3.8R (Dilution).

#### **Charges on buying and selling units: guidance**

- 6.7.8 G (1) To introduce a new charge for the *sale* or *redemption* of *units*, or any new category of remuneration for its services or increase the rate stated in the *prospectus*, the *authorised fund manager* will need to comply with *COLL* 4.2.5R (Table: contents of prospectus) and *COLL* 4.3 (Approvals and notifications).

- (2) A *redemption charge* may be expressed in terms of amount or percentage. It may also be expressed as diminishing over the time during which the *unitholder* has held the *units* or be calculated on the basis of the *unit price* performance of the *units*. However any *redemption charge* should not be such that it could be reasonably regarded as restricting any right of *redemption*.
- (3) The *prospectus* should contain a statement as to the determination of the order in which *units* which have been acquired at different times by a *unitholder* are to be taken to be *redeemed* or *cancelled* for the purpose of the imposition of the *redemption charge*.

#### **Charges for the exchange of units in an umbrella**

- 6.7.9 R For a *scheme* which is an *umbrella*, an *authorised fund manager* must not make a charge on an exchange of *units* in one *sub-fund* for *units* in another *sub-fund* unless the amount of the charge is not more than the amount stated in the current *prospectus*.

#### **Allocation of payments to income or capital**

- 6.7.10 R (1) The *authorised fund manager* must determine whether a payment is to be made from the *income property* or *capital property* of an *authorised fund*, and in doing so the *authorised fund manager* must:
- (a) pay due regard to whether the nature of the cost is income related or capital related and the objective of the *scheme*; and
  - (b) agree the treatment of any payment with the *depository*.
- (2) Where, for any *annual accounting period*, the amount of the *income property* is less than the income distributed, the shortfall must, as from the end of that period, be charged to the *capital account* and must not subsequently be transferred to the *income account*.

### **Allocation of payments to income or capital: guidance**

- 6.7.11 G (1) Any payment as a result of effecting transactions for the *authorised fund* should be made from the *capital property* of the *scheme*.
- (2) Other than the payments in (1), all other payments should be made from *income property* in the first instance but may be transferred to the *capital account* in accordance with *COLL* 6.7.10R (Allocation of payments to income or capital).
- (3) For payments transferred to the *capital property* of the *scheme* in accordance with (2), the *prospectus* should disclose the matters in *COLL* 4.2.5R 14.
- (4) If the *authorised fund manager* wishes to make a change in relation to the allocation of payments, the procedures in *COLL* 4.3 (Approvals and notifications) will be relevant.

### **Prohibition on promotional payments**

- 6.7.12 R No payment may be made from *scheme property* to any *person*, other than a payment to the *authorised fund manager* permitted by the *rules* in *COLL*, for the acquisition or promotion of the *sale* of *units* in an *authorised fund*.

### **Prohibition on promotional payments: guidance**

- 6.7.13 G Examples of payments which are not permitted by *COLL* 6.7.12R include:
- (1) *commission* payable to intermediaries (such payments should normally be borne by the *authorised fund manager*);
- (2) payments or costs in relation to the preparation or dissemination of *financial promotions* (other than the preparation of *key features*); and
- (3) payments to third parties, for maintaining details of beneficial *unitholders*.

### **Movable or immovable property**

- 6.7.14 R An *ICVC* must not incur any expense for the use by it of any movable or immovable property except to the extent that such property is necessary for the direct pursuit of its business or held in accordance with its investment objectives.

**Payment of liabilities on transfer of assets**

- 6.7.15 R (1) Where the property of an *authorised fund* is transferred to a second *authorised fund* (or to the *depository* for the account of the *authorised fund*) in consideration of the *issue* of *units* in the second *authorised fund* to *unitholders* in the first *scheme*, (2) applies.
- (2) The *ICVC*, its *depository* or the *trustee* of the *AUT* as the successor in title to the property transferred, may pay out of the *scheme property* any liability arising after the transfer which, had it arisen before the transfer, could properly have been paid out of the property transferred, but only if:
- (a) there is nothing in the *instrument constituting the scheme* of the *authorised fund* expressly forbidding the payment; and
  - (b) the *authorised fund manager* is of the opinion that proper provision was made for meeting such liabilities as were known or could reasonably have been anticipated at the time of the transfer.

**Exemptions from liability to account for profits**

- 6.7.16 G An *affected person* is not liable to account to another *affected person* or to the *unitholders* of any *scheme* for any profits or benefits it makes or receives that are made or derived from or in connection with:
- (1) *dealings* in the *units* of a *scheme*; or
  - (2) any transaction in *scheme property*; or
  - (3) the supply of services to the *scheme*;
- where disclosure of the non-accountability has been made in the *prospectus* of the *scheme*.

**Allocation of scheme property**

6.7.17 R For a *scheme* which is an *umbrella*, any assets to be received into, or any payments out of, the *scheme property* which are not attributable to one *sub-fund* only, must be allocated by the *authorised fund manager* between the *sub-funds* in a manner which is fair to the *unitholders* of the *umbrella* generally.

## 6.8 **Income: accounting, allocation and distribution**

### **Application**

- 6.8.1 R (1) This section applies to an *authorised fund manager*.
- (2) *COLL* 6.8.4 (Unclaimed, de minimis and joint unitholder distributions) also applies to the *depository* of an *authorised fund*.
- (3) Except in the case of *COLL* 6.8.2R (Accounting periods) and *COLL* 6.8.3R(1) (Income allocation and distribution), *COLL* 6.8 applies as if each *sub-fund* were a separate *authorised fund*.

### **Accounting periods**

- 6.8.2 R (1) An *authorised fund* must have:
- (a) an *annual accounting period*;
- (b) a *half-yearly accounting period*; and
- (c) an *accounting reference date*.
- (2) A *half-yearly accounting period* begins with the first *day* of an *annual accounting period* and ends on the *day* which is six *months* later or ends on some other reasonable date as set out in the *prospectus* of the *scheme*.

### **Income allocation and distribution**

- 6.8.3 R (1) An *authorised fund* must have an *annual income allocation date*, which must be within four *months* of the *accounting reference date*.
- (2) An *authorised fund* may have an *interim income allocation date* and *interim accounting periods* and, if it does, the *interim income allocation date* must be within four *months* of the end of the relevant *interim accounting period*.
- (3) An *authorised fund* must have a *distribution account* to which the *income property* is transferred at the end of the relevant accounting period.
- (4) If income is allocated and distributed during an accounting period:

- (a) with effect from the end of the relevant *accounting period*, the amount of income allocated to *unit classes* that accumulate income becomes part of the *capital property* and requires an adjustment to the proportion of the value of the *scheme property* to which they relate if other *classes of units* are in *issue* during the period;
- (b) the adjustment in (a) must ensure the *price of units* remains unchanged despite the transfer of income; and
- (c) the amount of any interim distribution may not be more than the amount which, in the opinion of the *authorised fund manager*, would be available for allocation if the *interim accounting period* and all previous *interim accounting periods* in the same *annual accounting period*, taken together, were an *annual accounting period*.

**Unclaimed, de minimis and joint unitholder distributions**

- 6.8.4 R (1) Any distribution remaining unclaimed after a period of six years, or such longer time specified by the *prospectus*, must become part of the *capital property*.
- (2) The *authorised fund manager* and the *depository* may agree a de minimis amount in respect of which a distribution of income is not required, and how any such amounts are to be treated.
- (3) Distributions made to the first named joint *unitholder* on the *register* will be as effective a discharge to the *trustee and manager*, as if the first named joint *unitholder* had been a sole *unitholder*.

**Guidance: contents of the prospectus**



6.8.5 G *COLL* 4.2.5R (Table: contents of prospectus) requires the details of *COLL* 6.8.2R, *COLL* 6.8.3R(1) and (2) and *COLL* 6.8.4R(1) and (2) to be contained in the *prospectus* as well as when, and how, the distribution will be paid (e.g. by cheque or BACS) and also how any unclaimed distributions are to be processed.

## 6.9 Independence, names and UCITS business restrictions

### Application

- 6.9.1 R This section applies to the *authorised fund manager* and the *depository* of an *authorised fund*.

### Independence of depositories and scheme operators

- 6.9.2 G (1) Regulation 15(8)(f) of the *OEIC Regulations* (Requirements for authorisation) requires independence between the *depository*, the *ICVC* and the *ICVC's directors*, as does section 243(4) of the *Act* (Authorisation orders) for the *trustee* and *manager* of an *AUT*. *COLL 6.9.3G* to *COLL 6.9.5G* give *FSA's* view of the meaning of independence of these relationships. An *ICVC*, its *directors and depository* or a *manager* and a *trustee* of an *AUT* are referred to as "relevant parties" in this *guidance*.
- (2) There are at least three possible kinds of links between the relevant parties:
- (a) *directors* in common;
  - (b) cross-shareholdings; and
  - (c) contractual commitments.
- (3) If any of these links exist between the relevant parties, the *FSA* will have regard to *COLL 6.9.3G* to *COLL 6.9.5G* in determining whether there is independence.

### Independence: influence by directors

- 6.9.3 G (1) Independence is likely to be lost if, by means of executive power, either relevant party could control the action of the other.
- (2) The board of one relevant party should not be able to exercise effective control of the board of another relevant party. Arrangements which might indicate this situation include quorum provisions and reservations of decision-making capacity of certain *directors*.

- (3) For an *AUT*, the *FSA* would interpret the concept of *directors* in common to include any *directors* of associates of one relevant party who are simultaneously *directors* of the other relevant party.
- (4) For an *ICVC*, independence would not be met if:
  - (a) a *director* of the *ICVC* or any *associate* of the *director* is a *director*, an employee, or both of the *depository*; or
  - (b) a *director* of an *ICVC*:
    - (i) has a direct or indirect shareholding for investment purposes of more than 0.5% of the votes at a general meeting or a meeting of *holders* of the class of *share* concerned of the *depository* of that *ICVC*; or
    - (ii) has any other relationship with the *depository* which might reasonably be expected to give rise to a potential conflict of interest.

**Independence: influence by shareholding**

- 6.9.4 G Independence is likely to be lost if either of the relevant parties could control the actions of the other by means of shareholders' votes. The *FSA* considers this would happen if any shareholding by one relevant party and their respective *associates* in the other exceeds 15% of the voting *share* capital, either in a single *share* class or several *share* classes. The *FSA* would be willing, however, to look at cross-shareholdings exceeding 15% on a case-by-case basis to consider if there were exceptional grounds for concluding that independence was safeguarded by other means.

**Independence: contractual commitments**

- 6.9.5 G The *FSA* would encourage relevant parties to consult it in advance about its view on the consequences of any intended contractual commitment or relationship which could affect independence, whether directly or indirectly.

**Undesirable or misleading names**

- 6.9.6 G (1) Regulation 15(9) of the *OEIC Regulations* and section 243(8) of the *Act* require that an *authorised fund's* name must not be

undesirable or misleading. This section contains *guidance* on some specific matters the *FSA* will consider in determining whether the name of an *authorised fund* is undesirable or misleading. It is in addition to the requirements of regulation 19 of the *OEIC Regulations* (Prohibition on certain names).

- (2) The *FSA* will take into account whether the name of the *scheme*:
  - (a) is substantially similar to the name of another *authorised fund*;
  - (b) implies that the *authorised fund* has merits which are not, or might not be, justified;
  - (c) implies that the *authorised fund manager* has particular qualities, which may not be justified;
  - (d) is inconsistent with the *authorised fund's* investment objectives or policy;
  - (e) implies that the *authorised fund* is not an *authorised fund* (for example, describing the *authorised fund* as a “plan” or “account” are unlikely to be acceptable); and
  - (f) might mislead investors into thinking that *persons* other than the *authorised fund manager* are responsible for the *authorised fund*.
- (3) The *FSA* is unlikely to approve a name of an *authorised fund* that includes the word "guaranteed" unless:
  - (a) the guarantee is given by:
    - (i) an *authorised person*;
    - (ii) a *person* authorised by a *Home State regulator*; or
    - (iii) a *person* subject to prudential supervision in accordance with criteria defined by Community law or prudential rules at least as stringent as those laid down by Community law;other than the *authorised fund manager* or the *depository*.
  - (b) the *authorised fund manager* can demonstrate that the guarantor has the authority and resources to honour the terms of the guarantee;

- (c) the guarantee covers all *unitholders* within the *authorised fund* and is legally enforceable by each *unitholder* who is intended to benefit from it or by a *person* acting on that *unitholder's* behalf;
  - (d) the guarantee relates to the total amount paid for a *unit* which includes any charge or other costs of buying or selling *units* in the *authorised fund*;
  - (e) the guarantee provides for payment at a specified date or dates and is unconditional although reasonable commercial exclusions such as force majeure may be included; and
  - (f) where the guarantee applies to different *classes* of *unit*, it is identical in its application to all *classes* except for the differences attributable to income already received or charges already suffered by the different *classes* of *unit*.
- (4) The name of an *authorised fund* may indicate a guaranteed capital return or income return or both but only if the total amount paid for a *unit* is guaranteed in accordance with (3).
- (5) The *FSA* is unlikely to approve a name of an *authorised fund* that includes words implying a degree of capital security (such as "capital protected" or anything with a similar meaning) unless the degree of capital security is apparent from the name and clearly stated in the *prospectus*, and:
- (a) the principles in (3) are satisfied except that, for the purposes of (3)(d), the guarantee may relate to an amount not materially less than the total amount paid for a *unit*; or
  - (b) the investment objective and investment policy for the *authorised fund* are such as to show a clear intention to provide a material degree of security in respect of the total amount paid for a *unit*.
- (6) When determining whether (5) is complied with, the *FSA* will take into account whether the degree of capital security implied by the name fairly reflects the nature of the arrangements for providing that security. This assessment will take place on a

case-by-case basis.

**Undesirable or misleading names: umbrellas**

- 6.9.7 R The *authorised fund manager* must ensure that the name of a *sub-fund* or of a *class of unit* is not undesirable or misleading.

**Undesirable or misleading names: umbrellas – guidance**

- 6.9.8 G When deciding whether *COLL 6.9.7R* is complied with, the *FSA* will take into account *COLL 6.9.6G*. *COLL 6.9.7R* applies generally and not just to the names that include the words "guaranteed" or "capital protected".

**Restrictions of business for UCITS management companies**

- 6.9.9 R A *UCITS management company* must not engage in any activities other than:
- (1) acting as:
    - (a) an *authorised fund manager* of an *authorised fund*; or
    - (b) an *operator* of any other *collective investment scheme* for which the *firm* is subject to prudential supervision;
  - (2) activities for the purposes of or in connection with those in (1);
  - (3) collective portfolio management, including without limitation:
    - (a) investment management;
    - (b) administration:
      - (i) legal and fund management accounting services;
      - (ii) *customer* enquiries;
      - (iii) valuation and pricing (including tax returns);
      - (iv) regulatory compliance monitoring;
      - (v) maintenance of *unitholder register*;
      - (vi) distribution of income;
      - (vii) *unit issues* and *redemptions*;
      - (viii) contract settlements (including certificate dispatch);
      - and
      - (ix) record keeping; and
    - (c) marketing;

- (4) *managing investments* where the relevant portfolio includes one or more *ISD instruments*;
- (5) *advising on investments* where:
  - (a) the *firm* has a *permission* for the activity in (4); and
  - (b) each of the instruments are *ISD instruments*; and
- (6) safeguarding and administration of *collective investment scheme units* where the *firm* has a *permission* for the activity in (4).

**Connected activities: guidance**

- 6.9.10 G (1) Examples of the connected activities referred to in *COLL* 6.9.9R(2) include management of *group plans*, as long as they are dedicated to *investments* in *unit trust schemes* and *OEICs* for which the *firm* acts as an *authorised fund manager*.
- (2) The restrictions of business imposed by *COLL* 6.9.9R reflect the position under Article 5 of the *UCITS Directive*. In accordance with recital (7) of the amending UCITS Management Directive (2001/107/EC) the activities referred to at *COLL* 6.9.9R (3)(a) to (c) may be performed on behalf of *EEA UCITS management companies*.

**Notification to the FSA in its role as registrar of ICVCs**

- 6.9.11 R An *ICVC* must notify the *FSA* within 14 *days* of the occurrence of any of the following:
- (1) any amendment to the *instrument of incorporation*;
  - (2) any change in the address of the head office of the *ICVC*;
  - (3) any change of *director*;
  - (4) any change of *depository*;
  - (5) in respect of any *director* or *depository*, any change in the information mentioned in regulation 12(1)(b) or (c) of the *OEIC Regulations (Applications for authorisation)*;
  - (6) any change of the auditor of the *ICVC*;
  - (7) any order in respect of the *ICVC* made by virtue of regulation 70 of the *OEIC Regulations (Mergers and divisions)*.

## 7 Suspension of dealings and termination of authorised funds

### 7.1 Introduction

#### Application

- 7.1.1 R This chapter applies to an *ICVC*, an *ACD*, any other *director* of a *ICVC*, a *depository* of an *ICVC*, a *manager* of an *AUT* and a *trustee* of an *AUT*, where such *AUT* or *ICVC* is a *UCITS scheme* or a *non-UCITS retail scheme* in accordance with *COLL 7.1.2R* (Table of application).

#### Table of application

- 7.1.2 R This table belongs to *COLL 7.1.1R*.

<i>Rule</i>	<i>ICVC</i>	<i>ACD</i>	<i>Any other directors of an ICVC</i>	<i>Depository of an ICVC</i>	<i>Manager</i>	<i>Trustee</i>
7.1.1	x	x	x	x	x	x
7.1.3	x	x	x	x	x	x
7.2.1	x	x		x	x	x
7.3.1	x	x	x	x		
7.3.2	x	x	x	x		
7.3.3	x	x	x			
7.3.4	x	x	x			
7.3.5		x	x			
7.3.6	x	x	x			
7.3.7	x	x	x	x		
7.3.8		x	x			
7.3.9		x				
7.3.10	x	x	x	x		
7.3.11		x				
7.3.12	x	x				
7.3.13 (1)		x	x			
7.3.13 (2)			x	x		
7.4					x	x
7.5		x	x	x	x	x
7.6		x	x	x	x	x
Note: x means "applies"						



## Purpose

- 7.1.3 G (1) This chapter helps to achieve the *regulatory objective* of protecting investors by ensuring they do not buy or *redeem units* at a *price* that cannot be calculated accurately. For instance, due to unforeseen circumstances, it may be impossible to value, or to dispose of and obtain payment for, all or some of the *scheme property* of an *authorised fund* or *sub-fund*. *COLL 7.2.1R* (Requirement) sets out the circumstances in which an *authorised fund manager* must or may suspend dealings in *units* and the manner in which a suspension takes effect.
- (2) This chapter also helps with the *regulatory objective* of protecting *consumers*, by providing a cost effective and fair means of winding up *authorised funds* and terminating *sub-funds* of *ICVCs* and *AUTs*. *ENF 16* (Collective investment schemes) deals with the *FSA's* powers to revoke the authorisation of *authorised funds* otherwise than by consent.

## 7.2 Suspension and restart of dealings

### Requirement

- 7.2.1 R (1) The *authorised fund manager* may, with the prior agreement of the *depository*, and must without delay, if the *depository* so requires, suspend the *issue, cancellation, sale and redemption of units* in an *authorised fund* (referred to in this chapter as "*dealings in units*"), where due to exceptional circumstances it is in the interest of all the *unitholders* in the *authorised fund*.
- (2) On suspension, the *authorised fund manager*, or the *depository* if it has required the *authorised fund manager* to suspend *dealings in units*, must:
- (a) immediately inform the *FSA*, stating the reason for its action; and
  - (b) as soon as practicable give written confirmation of the suspension and the reasons for it to:
    - (i) the *FSA*; and
    - (ii) the *Home State regulator* in each *EEA State* in which the *authorised fund manager* holds itself out as willing to *sell* or redeem *units* of the *authorised fund* concerned.
- (3) During a suspension, none of the obligations in *COLL 6.2* (Dealing) and *COLL 6.3* (Valuation and pricing) apply.
- (4) The suspension of *dealings in units* must cease as soon as practicable after the exceptional circumstances referred to in (1) have ceased and, in any event, within 28 *days* of the commencement of the suspension.
- (5) The *authorised fund manager* must inform the *FSA* of the proposed restart of *dealings in units* and immediately after the restart must confirm this by giving notice to the *FSA* and the authorities mentioned in (2)(b)(ii).
- (6) The *authorised fund manager* may agree, during the suspension, to *deal in units* at a *price* calculated by reference to the first *valuation point* after restart of *dealings in units*, subject

- to (8).
- (7) This *rule* applies to a *sub-fund* as it applies to an *authorised fund*, and:
- (a) references to the *units* of the *class* or *classes* relate to that *sub-fund* and to the *scheme property* attributable to the *sub-fund*; and
  - (b) this *rule* can only apply to one or more *classes* of *units* without being applied to other *classes*, if it is in the interest of all the *unitholders*.
- (8) If an *authorised fund* operates *limited redemption arrangements*, and the event in (1) has affected a *valuation point*, the *authorised fund manager* must declare an additional *valuation point* as soon as possible after the restart of *dealings* in *units*.

### **7.3 Winding up a solvent ICVC and terminating a sub-fund of an ICVC**

#### **Explanation of COLL 7.3**

- 7.3.1 G (1) The winding up of an *ICVC* may be carried out under this section instead of by the court provided the *ICVC* is solvent and the steps required under regulation 21 the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company) are fulfilled. This section lays down the procedures to be followed and the obligations of the *ACD* and any other *directors* of the *ICVC*.
- (2) The termination of a *sub-fund* under this section will be subject to the conditions set out in regulation 21 of the *OEIC Regulations*. Termination can only commence once the proposed alterations to the *ICVC's instrument of incorporation* and *prospectus* have been notified to the *FSA* and permitted to take effect. On termination, the assets of the *sub-fund* will normally be realised, and the *unitholders* in the *sub-fund* will receive their respective share of the proceeds net of liabilities and the expenses of the termination.
- (3) A *sub-fund* or *ICVC* may also be terminated or wound up in connection with a *scheme of arrangement*. *Unitholders* will become entitled to receive *units* in another *regulated collective investment scheme* in exchange for their *units*.

#### **Special meanings for termination of a sub-fund of an ICVC**

- 7.3.2 R In this section, where a *sub-fund* of an *ICVC* is being terminated, references to:
- (1) *units*, are references to *units* of the *class* or *classes* related to the *sub-fund* to be terminated;
  - (2) a resolution, or *extraordinary resolution*, are references to such a resolution passed at a meeting of *unitholders* of *units* of the *class* or *classes* referred to in (1);
  - (3) *scheme property*, are references to the *scheme property* allocated or attributable to the *sub-fund* to be terminated; and
  - (4) liabilities, are references to liabilities of the *ICVC* allocated or

attributable to the *sub-fund* to be terminated.

**Guidance on winding up or termination**

7.3.3 G This table belongs to *COLL 7.3.3G*.

<p>Summary of the main steps in winding up a solvent <i>ICVC</i> or terminating a <i>sub-fund</i> under <i>FSA rules</i>, assuming <i>FSA</i> approval.</p> <p>Notes: N = Notice to be given to the <i>FSA</i> under regulation 21 of <i>OEIC Regulations</i></p> <p>E = commencement of winding up or termination</p> <p>W/U = winding up</p> <p>FAP = final accounting period (<i>COLL 7.3.8R(4)</i>)</p>			
Step number	Explanation	When	<i>COLL rule</i> (unless stated otherwise)
1	Commence preparation of solvency statement	N-28 <i>days</i>	7.3.5 (2)
2	Send audited solvency statement to the <i>FSA</i> with copy to <i>depository</i>	By N + 21 <i>days</i>	7.3.5 (4) and (5)
3	Receive the <i>FSA</i> approval	N + one <i>month</i>	Regulation 21 of <i>OEIC Regulations</i>
4	Normal business ceases; publish notices	E	7.3.6
5	Realise proceeds, wind up, instruct <i>depository</i> accordingly	ASAP after E	7.3.7
6	Prepare final account or termination account & have account audited	On completion of W/U or termination	7.3.8

7	Send final account or termination account and auditor's report to the <i>FSA &amp; unitholders</i>	Within 2 <i>months</i> of FAP	7.3.8(6)
8	Request <i>FSA</i> to revoke relevant <i>authorisation order</i>	On completion of W/U	7.3.7(9)

**When an ICVC is to be wound up or a sub-fund terminated**

- 7.3.4 R (1) An *ICVC* must not be wound up except under this section or as an unregistered company under Part V of the Insolvency Act 1986.
- (2) An *ICVC* must not be wound up under this section if there is a vacancy in the position of *ACD*.
- (3) An *ICVC* must not be wound up or a *sub-fund* terminated under this section:
- (a) unless and until effect may be given, under regulation 21 of the *OEIC Regulations*, to proposals to wind up the affairs of the *ICVC* or to proposals to make the alterations to the *ICVC's instrument of incorporation* and *prospectus* that will be required if a *sub-fund* is terminated; and
- (b) unless a statement has been prepared and sent or delivered to the *FSA* under *COLL 7.3.5R* (Solvency statement) and received by the *FSA* prior to satisfaction of the condition in (a).
- (4) Subject to (3) and the subsequent provisions of this section, the appropriate steps to wind up an *ICVC* or terminate a *sub-fund* under this section must be taken:
- (a) if an *extraordinary resolution* to that effect is passed; or
- (b) when the period (if any) fixed for the duration of the *ICVC* or the *sub-fund* by the *instrument of incorporation* expires or any event occurs, for which the *instrument of incorporation* provides that the *ICVC* or the *sub-fund* is to

- be wound up; or
- (c) on the date stated in any agreement by the *FSA* in response to a request from the *directors* for the winding up of the *ICVC* or a request for the termination of the *sub-fund*.

### **Solvency statement**

- 7.3.5 R (1) Before notice is given to the *FSA* under regulation 21 of the *OEIC Regulations* of the proposals referred to in *COLL 7.3.4R* (3), the *directors* must make a full enquiry into the *ICVC's* affairs to determine whether the *ICVC* will be able to meet all its liabilities.
- (2) The *ACD* must then, based on the results of this enquiry, prepare a statement either:
- (a) confirming that the *ICVC* will be able to meet all its liabilities within twelve *months* of the date of the statement; or
- (b) stating that such confirmation cannot be given.
- (3) This solvency statement must:
- (a) relate to the *ICVC's* affairs at a date no more than 28 *days* before the date on which notice is given to the *FSA*;
- (b) if there is more than one *director*, be approved by the board of *directors* and signed on their behalf by the *ACD*; and
- (c) if it contains the confirmation under (2)(a), be signed by at least one other *director* or, if there is no *director* other than the *ACD*, be signed by the *ACD*.
- (4) A statement which contains the confirmation under (2)(a) must annex a statement signed by the auditor appointed under Schedule 5 to the *OEIC Regulations* (Auditors) to the effect that, in his opinion, the enquiry required by (1) has been properly made and is fairly reflected by the confirmation.
- (5) The solvency statement must be sent or delivered to the *FSA* and the *depository* no later than 21 *days* after notice is given to

the *FSA* in accordance with regulation 21 of the *OEIC Regulations*.

**Consequences of commencement of winding up or termination**

- 7.3.6 R (1) Winding up or termination must commence once the conditions referred to in *COLL 7.3.4 R (3)* are both satisfied or, if later, once the events in *COLL 7.3.4R(4)* have occurred.
- (2) Once winding up or termination has commenced:
- (a) *COLL 6.2 (Dealing)*, *COLL 6.3 (Valuation and pricing)* and *COLL 5 (Investment and borrowing powers)* cease to apply to the *ICVC* or to the *units* and *scheme property* in the case of a *sub-fund*;
  - (b) the *ICVC* must cease to *issue* and cancel *units*;
  - (c) the *ACD* must cease to *sell* or redeem *units* or to arrange for the *issue* or *cancellation* of units;
  - (d) no transfer of a *unit* may be registered and no other change to the *register* of *unitholders* may be made without the sanction of the *directors*;
  - (e) where winding up an *ICVC*, the *ICVC* must cease to carry on its business, except for its beneficial winding up; and
  - (f) the corporate status and corporate powers of the *ICVC* and (subject to the preceding provisions of this *rule*) the powers of the *directors* continue until the *ICVC* is dissolved.
- (3) The *ACD* must as soon as practicable after winding up or termination has commenced:
- (a) if the *ACD* has not previously notified *unitholders* of the proposal to wind up the *ICVC* or terminate the *sub-fund*, give written notice of the commencement of the winding up or termination to the *unitholders*; and
  - (b) if winding up an *ICVC*, publish notice of the commencement of the winding up (if the head office of the *ICVC* is situated in England and Wales or Wales) in the *London Gazette*, or (if the head office of the *ICVC* is



situated in Scotland) in the Edinburgh Gazette.

**Manner of winding up or termination**

- 7.3.7 R (1) Paragraphs (2) to (9) of this *rule* apply to winding up an *ICVC* and termination of a *sub-fund*, paragraph (10) only applies to the winding up of an *ICVC* and paragraphs (11) to (15) only apply to the termination of a *sub-fund* of an *ICVC*.
- (2) The *ACD* must, as soon as practicable after winding up or termination has commenced, cause the *scheme property* to be realised and the liabilities of the *ICVC* or the *sub-fund* to be met out of the proceeds.
- (3) The *ACD* must instruct the *depository* how such proceeds (until utilised to meet liabilities or make distributions to *unitholders*) must be held and those instructions must be prepared with a view to the prudent protection of creditors and *unitholders* against loss.
- (4) Where sufficient liquid funds are available after making adequate provision for the expenses of the winding up or termination and the discharge of the *ICVC's* or the *sub-fund's* remaining liabilities, the *ACD* may arrange for the *depository* to make one or more interim distributions to the *unitholders* proportionately to the right of their respective *units* to participate in *scheme property* at the commencement of the winding up or termination.
- (5) On or before the date on which the final account is sent to *unitholders* in accordance with *COLL 7.3.8R* (Final account and termination account), the *ACD* must arrange for the *depository* to make a final distribution to the *unitholders*, in the same proportions as provided by (4), of the balance remaining (net of a provision for any further expenses of the *ICVC* or *sub-fund*).
- (6) Paragraphs (2) to (5) are subject to the terms of any *scheme of arrangement* sanctioned by an *extraordinary resolution* passed on or before the commencement of the winding up or

termination.

- (7) Where the *ICVC* and one or more *unitholders* (other than the *ACD*) agree, the requirement in (2) to realise the *scheme property* does not apply to that part of the *scheme property* which is proportionate to the right to participate in *scheme property* of that or those *unitholders*.
- (8) In the case of (7), the *ACD* must cause the *ICVC* to distribute that part of the *scheme property* in specie to that or those *unitholders* in proportion to their respective rights to participate, this distribution being effected after making adjustments and retaining such provision as appears to the *ACD* appropriate to ensure that those *unitholders* bear the proportion of the liabilities and the expenses of the distribution attributable to their *units*.
- (9) The *depository* must notify the *FSA* once the winding up of the *ICVC* or the termination of a *sub-fund* (including compliance with *COLL 7.3.8R*) is complete and at the same time the *ACD* or the *depository* must request the *FSA* to revoke the relevant *authorisation order*.
- (10) Where any sum of *money* stands to the account of the *ICVC* at the date of its dissolution, the *ACD* must arrange for the *depository* to pay or lodge that sum within one *month* after that date in accordance with regulation 33(4) or (5) of the *OEIC Regulations* (Dissolution in other circumstances).
- (11) Where any sums (including unclaimed distributions) remain standing to the account of the *scheme property* following tender of payment (whether to a creditor or a *unitholder*), the *ACD* must instruct the *depository* to retain the sums ('tendered sums') in an account ('unclaimed payments account') separate from any other part of the *scheme property*.
- (12) The *depository* must, if instructed by the *ACD*, make a payment out of the unclaimed payments account for the purpose of settling a claim for a tendered sum.

- (13) Any costs and reasonable expenses of the *ACD* for investigating a claim and any costs and expenses incurred by the *depository* in making a payment out of the unclaimed payments account may be reimbursed from the payment.
- (14) The *person* entitled to any tendered sum is not entitled to any interest in respect of the unclaimed payments account and any interest arising in respect of the unclaimed payments account must be allocated between the continuing *sub-funds* of the *ICVC* in a manner which is fair to the *unitholders* of the *ICVC* generally.
- (15) Amounts standing to the credit of an unclaimed payments account must be excluded from the value of the *scheme property* and must not be subject to any distribution under this *rule*, but upon a dissolution of the *ICVC* under regulation 33 of the *OEIC Regulations*, the *depository* must cease to hold those amounts as part of that account and they will become subject to the provisions of (10).

**Final account and termination account**

- 7.3.8 R (1) Once the *ICVC's* affairs are fully wound up or termination of the *sub-fund* has been completed (including distribution or provision for distribution in accordance with *COLL 7.3.7 R(5)*), the *ACD* must prepare an account of the winding up or termination showing:
- (a) how it has been conducted; and
  - (b) how the *scheme property* has been disposed of.
- (2) The account in (1) must be, if there is:
- (a) more than one *director*, approved by the board of *directors* and be signed on their behalf by the *ACD* and at least one other *director*; or
  - (b) no *director* other than the *ACD*, signed by the *ACD*.
- (3) Once signed, this account is the "final account" for the purposes of the winding up of an *ICVC* and the "termination account" for the purposes of the termination of a *sub-fund*.

- (4) The final account must state the date on which the *ICVC's* affairs were fully wound up and the date stated must be regarded as the final *day* of the accounting period of the *ICVC* then running ('final accounting period').
- (5) The *ACD* must ensure that the *ICVC's* auditor makes a report in respect of the final account or termination account, which states the auditor's opinion whether the final account or termination account has been properly prepared for the purpose of (1).
- (6) Within two *months* of the date of the completion of the winding up of the *ICVC* or termination of the *sub-fund*, the *ACD* must send a copy of the final account or termination account and the auditor's report on it to the *FSA* and to each *person* who was a *unitholder* (or the first named of joint *unitholders*) immediately before its end.

**Duty to ascertain liabilities**

- 7.3.9 R (1) The *ACD* must use all reasonable endeavours to ensure that all the liabilities of the *ICVC* are discharged before the completion of the winding up or termination.
- (2) The duty in (1) relates to all liabilities of which the *ACD*:
- (a) is, or becomes, aware before the completion of the winding up or termination; or
  - (b) would have become aware before the completion of the winding up or termination had it used all reasonable endeavours to ascertain the liabilities.
- (3) If the *ACD* rejects any claim against the *ICVC* in whole or part or against the *ICVC* in respect of a liability in whole or part, the *ACD* must immediately send to the claimant written notice of its reasons for doing so.

**Reports and accounts**

- 7.3.10 R (1) The *ACD* need not (as would be required under *COLL* 4.5.13R (Provision of short report)) send to each *unitholder* a copy of any short report relating to an *annual accounting period* or *half-yearly accounting period* which began after

commencement of winding up or termination, if the *directors* of the *ICVC*, after consulting the *FSA*, have reasonably determined that this is not required in the interest of *unitholders*.

- (2) Where (1) applies, a copy of the short or long report must be supplied free of charge to any *unitholder* upon request.

#### **Liabilities of the ACD**

- 7.3.11 R (1) Except to the extent that the *ACD* can show that it has complied with *COLL 7.3.9R* (Duty to ascertain liabilities), the *ACD*:
- (a) is personally liable to meet any liability of an *ICVC*, of which it is the *ACD*, wound up under this section (whether or not the *ICVC* has been dissolved); and
  - (b) must keep the *ICVC* indemnified against any liability allocated or attributable to a *sub-fund* that has been terminated under these *rules*;
- that was not discharged before the completion of the winding up or termination.
- (2) Where winding up an *ICVC*, if the proceeds of the realisation of the assets attributable, or allocated to a particular *sub-fund* of an *umbrella ICVC* are insufficient to meet the liabilities attributable or allocated to that *sub-fund*, the *ACD* must pay to the *ICVC*, for the account of that *sub-fund* the amount of the deficit, unless and to the extent that the *ACD* can show that the deficit did not arise as a result of any failure by the *ACD* to comply with the *rules* in *COLL*.
- (3) The liabilities of the *ACD* under this *rule* create a debt (in England and Wales in the nature of a specialty) accruing due from it on the completion of the winding up or termination and payable upon the demand of the creditor in question (including the *ICVC* in the circumstances described in (2)).
- (4) The obligations of the *ACD* under this *rule* do not affect any other obligation of the *ACD* under these *rules* or the general law.

### **Additional provisions applicable to umbrella companies**

- 7.3.12 R (1) Liabilities of an *ICVC* which is an *umbrella* attributable, or allocated, to a particular *sub-fund* must be met first out of the *scheme property* attributable or allocated to such *sub-fund*.
- (2) If the liabilities to be met out of a particular *sub-fund* of an *umbrella ICVC* are greater than the proceeds of the realisation of the *scheme property* attributable or allocated to that *sub-fund*, the deficit must be met out of the *scheme property* attributable or allocated to the solvent *sub-funds* of that *umbrella ICVC* in which the proceeds of realisation exceed liabilities and divided between those *sub-funds* in a manner that is fair to the *unitholders* in those solvent *sub-funds*.
- (3) Paragraph (2) applies in respect of any deficit arising as a result of additional liabilities accruing to a *sub-fund* through the operation of (2).
- (4) In calculating the amount of liabilities for the purpose of (2), account must be taken of any payments received or to be received from the *ACD* under *COLL 7.3.11R* (Liabilities of the *ACD*).

### **Miscellaneous**

- 7.3.13 R (1) If:
- (a) during the course, or as a result, of the enquiry referred to in *COLL 7.3.5R(1)* (Solvency statement), the *directors* become of the opinion that it will not be possible to provide the confirmation referred to in (2)(a) of that *rule*;  
or
- (b) after winding up or termination has commenced, the *ACD* becomes of the opinion that the *ICVC* will be unable to meet all its liabilities within twelve *months* of the date of the statement provided under (a) of *COLL 7.3.5R(2)*;  
the *directors* must immediately present a petition or cause the *ICVC* to present a petition for the winding up of the *ICVC* as an unregistered *ICVC* under Part V of the Insolvency Act 1986.

- (2) If, after the commencement of a winding up under this chapter and before notice of completion of the winding up has been sent to the *FSA*, there is a vacancy in the position of *ACD*, the *directors* of the *ICVC* must immediately present or cause the *ICVC* to present or, if there are no *directors*, the *depository* must immediately present, a petition for the winding up of the *ICVC* as an unregistered *ICVC* under Part V of the Insolvency Act 1986.

## 7.4 Winding up an AUT and terminating a sub-fund of an AUT

### Explanation of COLL 7.4

- 7.4.1 G (1) This section deals with the circumstances and manner in which an *AUT* is to be wound up or a *sub-fund* of an *AUT* is to be terminated. Under section 256 of the *Act* (Requests for revocation of authorisation order), the *manager* or *trustee* of an *AUT* may request the *FSA* to revoke the *authorisation order* in respect of that *AUT*. Section 257 of the *Act* (Directions) gives the *FSA* the power to make certain directions.
- (2) The termination of a *sub-fund* under this section will be subject to section 251 of the *Act* (Alteration of schemes and changes of manager or trustee). Termination can only commence once the proposed alterations to the *trust deed* and *prospectus* have been notified to the *FSA* in writing and permitted to take effect. On termination, the assets of the *sub-fund* will normally be realised, and the *unitholders* in the *sub-fund* will receive their respective share of the proceeds net of liabilities and the expenses of the termination.
- (3) An *AUT* or a *sub-fund* of an *AUT* may also be wound up or terminated in connection with a *scheme of arrangement*. *Unitholders* will become entitled to receive *units* in another *regulated collective investment scheme* in exchange for their *units*.

### Special meanings for termination of a sub-fund of an AUT

- 7.4.2 R In this section, where a *sub-fund* of an *AUT* is being terminated, references to:
- (1) *units*, are references to *units* of the *class* or *classes* related to the *sub-fund* to be terminated;
- (2) a resolution or *extraordinary resolution*, are references to such a resolution passed at a meeting of *unitholders* of *units* of the *class* or *classes* referred to in (1);
- (3) *scheme property*, are references to the *scheme property* allocated or attributable to the *sub-fund* to be terminated; and



- (4) liabilities, are references to liabilities of the *AUT* allocated or attributable to the *sub-fund* to be terminated.

**When an *AUT* is to be wound up or a sub-fund terminated**

- 7.4.3 R (1) Upon the happening of any of the events or dates referred to in paragraph (2) and not otherwise:
- (a) *COLL 6.2* (Dealing), *COLL 6.3* (Valuation and pricing) and *COLL 5* (Investment and borrowing powers) cease to apply to the *AUT*;
  - (b) the *trustee* must cease to *issue* and cancel *units*;
  - (c) the *manager* must cease to *sell* and redeem *units*;
  - (d) the *manager* must cease to arrange the *issue* or *cancellation* of *units* under *COLL 6.2.7R* (Issue and cancellation of units through an authorised fund manager); and
  - (e) the *trustee* must proceed to wind up the *AUT* or terminate the *sub-fund* in accordance with *COLL 7.4.4.R*.
- (2) The events referred to in (1) are:
- (a) the *authorisation order* of the *AUT* is revoked;
  - (b) alterations to the *AUT's trust deed* and *prospectus* that will be required if the *sub-fund* is terminated taking effect in accordance with section 251 of the *Act*;
  - (c) the passing of an *extraordinary resolution* winding up the *AUT* or terminating the *sub-fund*, provided *FSA's* prior consent to the resolution has been obtained by the *manager* or *trustee*;
  - (d) in response to a request to the *FSA* by the *manager* or the *trustee* for the revocation of the *authorisation order*, the *FSA* has agreed, subject to there being no material change in any relevant factor, that, on the conclusion of the winding up of the *AUT*, the *FSA* will agree to that request;
  - (e) the expiration of any period specified in the *trust deed* as the period at the end of which the *AUT* is to be wound up

- or the *sub-fund* is to terminate;
  - (f) the effective date of a duly approved *scheme of arrangement*, which is to result in the *AUT* or *sub-fund* that is subject to the *scheme of arrangement* being left with no property; or
  - (g) the date on which a *relevant pension scheme* is notified in writing by the Occupational Pensions Schemes Regulatory Authority that the *scheme* is no longer registered under the Welfare and Pensions Reform Act 1999 as a *stakeholder pension scheme*.
- (3) This *rule* is without prejudice to *COLL 7.2.1R* (Requirement) and to any order or direction made under section 257 or 258 of the *Act*.

**Manner of winding up or termination**

- 7.4.4 R (1) Where *COLL 7.4.3R* (2)(f) applies, the *trustee* must wind up the *AUT* or terminate the *sub-fund* in accordance with the approved *scheme of arrangement*.
- (2) In any other case falling within *COLL 7.4.3R*:
- (a) once the *AUT* falls to be wound up or *sub-fund* terminated, the *trustee* must realise the *scheme property*;
  - (b) after paying out or retaining adequate provision for all liabilities payable and for the costs of the winding up or termination, the *trustee* must distribute the proceeds of that realisation to the *unitholders* and the *manager* proportionately to their respective interests in the *AUT* or *sub-fund* as at the date, or the date of the relevant event referred to in *COLL 7.4.3R*; and
  - (c) any unclaimed net proceeds or other cash (including unclaimed distribution payments) held by the *trustee* after one year from the date on which they became payable must be paid by the *trustee* into court (or, in Scotland, as the court may direct), subject to the *trustee* having a right to retain any expenses properly incurred by him relating

to that payment.

- (3) For an *AUT* which is a *relevant pension scheme*, payments must not be made to *unitholders* in the *AUT*, the realisation proceeds having to be paid by the *trustee* in accordance with the *trust deed*.
- (4) Where the *trustee* and one or more *unitholders* agree, the requirement in (2) to realise the *scheme property* does not apply to that part of the property proportionate to the entitlement of that or those *unitholders*.
- (5) The *trustee* may distribute the part of the *scheme property* referred to in (4) in the form of property, after making adjustments or retaining provisions as appears appropriate to the *trustee* for ensuring that, that or those *unitholders* bear a proportional share of the liabilities and costs.
- (6) On completion of the winding up in respect of the events referred to in *COLL 7.4.3R* (2)(c), (d) or (e), the *trustee* must notify the *FSA* in writing and at the same time the *manager* or *trustee* must request the *FSA* to revoke the relevant *authorisation order*.

#### **Accounting and reports during winding up or termination**

- 7.4.5 R (1) For any *annual* or *half-yearly accounting period* which began after commencement of the winding up or termination, the *trustee* (after consulting the *manager* (if appropriate) and the *FSA*) may direct that *COLL 4.5.13R* (Provision of short report) may be dispensed with, provided that it has taken reasonable care to determine that the report is not required in the interests of the *unitholders*.
- (2) Where (1) applies, a copy of the short and long report must be supplied free of charge to any *unitholder* upon request.
  - (3) The period in question in (2) must be reported on together with the following period in the next report prepared for the purposes of this *rule*.
  - (4) At the conclusion of the winding up or termination, the

accounting period then running is regarded as the final *annual accounting period*.

- (5) Within two *months* after the end of the final *annual accounting period* or the termination of the *sub-fund*, the annual reports of the *manager* and *trustee* must be published and sent to the *FSA* and to each *person* who was a *unitholder* or the first named of joint *unitholders* immediately before its end.

## 7.5 Schemes or sub-funds that are not commercially viable

### Explanation of this section

- 7.5.1 G (1) The *FSA* expects that the majority of requests it will receive for the winding up of an *authorised fund* (under regulation 21(1) of the *OEIC Regulations* or under section 256 of the *Act*) or termination of a *sub-fund* will be from *authorised fund managers* and *depositories* who consider that the *AUT*, *ICVC* or *sub-fund* in question is no longer commercially viable.
- (2) It is in *consumers'* interests to minimise, as far as possible, the period between which the *FSA* receives such requests and responds to them. To assist the *FSA* in arriving at a quick decision, based on all the relevant factors, it would be helpful for the *FSA* to receive the information listed at *COLL 7.5.2G*. Further information, however, may be requested by the *FSA* after receipt of the information, depending on the individual circumstances of the case.

### Information to be provided to the FSA

- 7.5.2 G The information referred to in *COLL 7.5.1G* is listed below:
- (1) the name of the *authorised fund* or *sub-fund*;
  - (2) the size of the *authorised fund* or *sub-fund*;
  - (3) the number of *unitholders*;
  - (4) whether dealing in *units* has been suspended;
  - (5) why the request is being made;
  - (6) what consideration has been given to the *authorised fund* or *sub-fund* entering into a *scheme of arrangement* with another *regulated collective investment scheme* and the reasons why a *scheme of arrangement* is not feasible;
  - (7)
    - (a) whether *unitholders* have been informed of the intention to seek termination, winding up or revocation; and
    - (b) if not, when they will be informed;
  - (8) details of any proposed preferential switching rights offered or to be offered to *unitholders*;
  - (9) details of any proposed rebate of charges to be made to

- unitholders* who recently purchased *units*;
- (10) where the costs of winding up or termination will fall;
  - (11) the *depository's*:
    - (a) statement whether having taken reasonable care it is certain that a *scheme of arrangement* is not feasible and explaining what steps have been considered that would result in the *authorised fund* or *sub-fund* not needing to wind up or terminate (for example, appointing a replacement *authorised fund manager*); and
    - (b) confirmation that it will not or does not expect to qualify a report made in accordance with *COLL 4.5.11R* (Report of the depository);
  - (12) the preferred date for the *FSA's* determination to revoke authorisation or the date for the commencement of the winding up or termination; and
  - (13) any additional information or material considered to be relevant to the *FSA's* decision under sections 251 and 256 of the *Act* or regulation 21 of the *OEIC Regulations* (as appropriate).

## 7.6 Schemes of arrangement

### Schemes of arrangement: explanation

- 7.6.1 G (1) A proposal that an *authorised fund* should be involved in a *scheme of arrangement* is subject to written notice to and approval by the *FSA* under section 251 of the *Act* (Alteration of schemes and changes of manager or trustee) or regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company). Effect cannot be given to such a change except in accordance with that section or regulation.
- (2) The *issue* of *units* in exchange for assets as part of an approved *scheme of arrangement* is subject to:
- (a) *COLL 6.2.5R* and *COLL 6.2.6R* (Issue and cancellation of units);
  - (b) *COLL 6.2.15R* (In specie issue and redemption); and
  - (c) *COLL 7.6.2R* (Scheme of arrangement: requirements).

### Schemes of arrangement: requirements

- 7.6.2 R (1) If a *scheme of arrangement* is entered into in relation to an *authorised fund* ("transferor fund") or a *sub-fund* of a *scheme* which is an *umbrella* ("transferor *sub-fund*"), an *authorised fund manager* must ensure that the *unitholders* of the transferor fund or *sub-fund* do not become *unitholders* of *units* in a *collective investment scheme* other than a *regulated collective investment scheme*.
- (2) For a *UCITS scheme* or a *sub-fund* of a *UCITS scheme*, (1) applies as if the reference to a *regulated collective investment scheme* also excludes any *recognised scheme* other than a *scheme* recognised under section 264 of the *Act* (Schemes constituted in other EEA States).
- (3) Where, for the purpose of a *scheme of arrangement*, it is proposed that *scheme property* of an *authorised fund* should become the property of another *regulated collective investment scheme* or *sub-fund* of a *regulated collective investment*

*scheme*, the proposal must not be implemented without the sanction of an *extraordinary resolution* of the *unitholders* in the *authorised fund*, unless (4) applies.

- (4) Where, for the purposes of a *scheme of arrangement*, it is proposed that *scheme property* attributable to a *sub-fund* of an *umbrella* should become the property of another *regulated collective investment scheme* or of another *sub-fund* of a *regulated collective investment scheme* (whether or not of that *umbrella*), the proposal must not be implemented without the sanction of:
  - (a) an *extraordinary resolution* of the *unitholders* in the *sub-fund* of that *umbrella*; and
  - (b) (unless implementation of the *scheme of arrangement* is not likely to result in any material prejudice to the interests of the *unitholders* in any other *sub-fund* of that *umbrella*) an *extraordinary resolution* of the *unitholders* of *units* in that *umbrella*.
- (5) If it is proposed that an *authorised fund* or *sub-fund* of an *umbrella* should receive property (other than its first property) as a result of a *scheme of arrangement* (or an arrangement equivalent to a *scheme of arrangement*) which is entered into by some other *collective investment scheme* or *sub-fund*, or by a *body corporate*, the proposal must not be implemented without the sanction of an *extraordinary resolution* of the *unitholders* in the *authorised fund* or (as the case may be) of the *class* or *classes* of *units* related to the *sub-fund* unless (6) applies.
- (6) This paragraph (6) applies if the *directors* of the *ICVC* or the *manager* and *trustee* of the *AUT* agree that the receipt of the property concerned for the account of the *ICVC* or *AUT*:
  - (a) is not likely to result in any material prejudice to the interests of the *unitholders* of the *authorised fund*;
  - (b) is consistent with the objectives of the *authorised fund* or *sub-fund*; and



- (c) could be effected without any breach of a *rule* in *COLL 5*  
(Investment and borrowing powers).

## 8 Qualified investor schemes

### 8.1 Introduction

#### Application

8.1.1 R (1) This chapter applies to:

- (a) an *authorised fund manager* of an *AUT* or an *ICVC*;
- (b) any other *director* of an *ICVC*;
- (c) a *depository* of an *AUT* or an *ICVC*; and
- (d) an *ICVC*,

which is a *qualified investor scheme*.

- (2) Where this chapter refers to *rules* in any other chapter of this sourcebook, those *rules* and any relevant *guidance* should be applied as if they referred to *qualified investor schemes*.

#### Purpose

8.1.2 G (1) This chapter assists in achieving the *regulatory objective* of protecting *consumers* by providing an appropriate degree of protection in respect of *authorised funds* that are only intended for investors that are, in general, prepared to accept a higher degree of risk in their investments or have a higher degree of experience and expertise than investors in *retail schemes*.

- (2) This section ceases to apply where a *qualified investor scheme* has converted to be authorised as a *UCITS scheme* or a *non-UCITS retail scheme*.

#### Qualified investor schemes: eligible investors

8.1.3 R (1) The *authorised fund manager* of a *qualified investor scheme* must take reasonable care to ensure that ownership of *units* in that *scheme* is only recorded in the *register* for the categories of *person* to whom it can be promoted under *COB 3 ANN5* (Permitted promotion of unregulated collective investment schemes and qualified investor schemes).

- (2) The *authorised fund manager* will be regarded as complying with (1) to the extent that it can show that it was reasonable for it to rely on relevant information provided by another *person*.

#### Qualified investor schemes – explanation

- 8.1.4 G (1) *Qualified investor schemes* are *authorised funds* which may only be sold or marketed to sophisticated investors. Therefore, the *authorised fund manager* must take reasonable care to ensure that subscription in relation to the *units* of this type of *scheme* should only be in relation to the *client* types set out in COB 3 ANN5. COB 3.11.6R (Promotion of qualified investor schemes) also restricts promotion of *qualified investor schemes* to the categories of *person* set out in COB 3 ANN5.
- (2) Accordingly, *qualified investor schemes* have a more relaxed set of *rules* governing their operation and in particular their investment powers than for retail *schemes*. A *qualified investor scheme* is essentially a mixed asset type of *scheme* where different types of permitted asset may be included as part of the *scheme property*, depending on the investment objectives and policy of that *scheme* and within any restrictions in the *rules*.

#### **Application and notification procedures**

- 8.1.5 G Details of the application procedures in respect of *qualified investor schemes* are contained in COLL 2.1 (Authorised fund applications). COLLG provides details on how notifications may be made to the FSA.

## 8.2 Constitution

### Application

- 8.2.1 R This section applies to an *authorised fund manager* in respect of a *qualified investor scheme*.

### Classes of unit

- 8.2.2 R A *qualified investor scheme* may issue such *classes of unit* as are set out in the *instrument constituting the scheme*, provided the rights of any *class* are not unfairly prejudicial as against the interests of the *unitholders* of any other *class of units* in that *scheme*.

### Names of schemes, sub-funds, and classes of units

- 8.2.3 R The *authorised fund manager* must ensure that the name of the *scheme*, a *sub-fund* or a *class of unit* is not undesirable or misleading.

### Undesirable and misleading names

- 8.2.4 G *COLL 6.9.6G* (Undesirable or misleading names) contains *guidance* as to names which may be undesirable or misleading.

### Instrument constituting the scheme

- 8.2.5 R The statements and provisions required by *COLL 8.2.6R* must be included in the *instrument constituting the scheme* of a *qualified investor scheme*.

### Table: contents of the instrument constituting the scheme.

- 8.2.6 R This table belongs to *COLL 8.2.5R*.

#### 1 Description of the authorised fund

Information detailing:

- (1) the name of the *authorised fund*;
- (2) that the *authorised fund* is a *qualified investor scheme*; and
- (3) in the case of an *ICVC*, whether the head office of the *company* is situated in England and Wales or Wales or Scotland or Northern Ireland.

#### 2 Constitution

The following statements:

- (1) the *scheme property* of the *scheme* is entrusted to a *depository* for safekeeping (subject to any exception permitted by the *rules*);

- (2) if relevant, the duration of the *scheme* is limited and, if so, for how long;
- (3) charges and expenses of the *scheme* may be taken out of *scheme property*;
- (4) for an *ICVC*:
  - (a) what the maximum and minimum sizes of the *scheme's* capital are; and
  - (b) the *unitholders* are not liable for the debts of the *company*; and
- (5) for an *AUT*:
  - (a) the *trust deed*:
    - (i) is made under and governed by the law of England and Wales, or the law of Scotland or the law of Northern Ireland;
    - (ii) is binding on each *unitholder* as if he had been a party to it and that he is bound by its provisions; and
    - (iii) authorises and requires the *trustee* and the *manager* to do the things required or permitted of them by its terms;
  - (b) subject to the provisions of the *trust deed* and all the *rules* made under section 247 of the *Act* (Trust scheme rules):
    - (i) the *scheme property* (other than sums held to the credit of the distribution account) is held by the *trustee* on trust for the *unitholders* according to the number of *units* held by each *unitholder* or, where relevant, according to the number of individual shares in the *scheme property* represented by the *units* held by each *unitholder*; and
    - (ii) the sums standing to the credit of any *distribution account* are held by the *trustee* on trust to distribute or apply in accordance with *COLL 8.5.15R*(Income);
  - (c) a *unitholder* is not liable to make any further payment after he has paid the *price* of his *units* and that no further liability can be imposed on him in respect of the *units* he holds; and
  - (d) payments to the *trustee* by way of *remuneration* are authorised to be paid (in whole or in part) out of the *scheme property*.

### 3 **Investment objectives**

A statement of the object of the *scheme*, in particular the types of *investments* and assets in which it and each *sub-fund* (where applicable) may invest and that the object of the *scheme* is to invest in property of that kind with the aim of spreading investment risk.

### 4 **Units in the scheme**

A statement of:

- (1) the *classes* of *units* which the *scheme* may issue, indicating, for a *scheme* which is an *umbrella*, which *class* or *classes* may be issued in respect of each *sub-fund*; and
- (2) the rights attaching to *units* of each *class* (including any provisions for the expression in two denominations of such rights).

### 5 **Limitation on issue of and redemption of units**

Details as to:

- (1) the provisions relating to any restrictions on the right to redeem *units* in any *class*; and
- (2) the circumstances in which the issue of the *units* of any particular *class* may be limited.

### 6 **Income and distribution**

Details of the *person* responsible for the calculation, transfer, allocation and distribution of income for any *class* of *unit* in *issue* during the accounting period.

### 7 **Base currency**

A statement of the *base currency* of the *scheme*.

### 8 **Meetings**

Details of the procedures for the convening of meetings and the procedures relating to resolutions, voting and the voting rights for *unitholders*.

### 9 **Powers and duties of the authorised fund manager and depositary**

Where relevant, details of any function to be undertaken by the *authorised fund manager* and *depository* which the *rules* in *COLL* require to be stated in the *instrument constituting the scheme*.

#### 10 **Termination and suspension**

Details of:

- (1) the grounds under which the *authorised fund manager* may initiate a suspension of the *scheme* and any associated procedures; and
- (2) the methodology for determining the rights of *unitholders* to participate in the *scheme property* on winding up.

#### 11 **Other relevant matters**

Details of those matters which enable the *scheme*, *authorised fund manager* or *depository* to obtain any privilege or power conferred by the *rules* in *COLL* which is not otherwise provided for in the *instrument constituting the scheme*.

#### **Limited issue**

- 8.2.7 *Units* whose *issue* may be limited can only be issued if permitted by the *instrument*
- R *constituting the scheme*, under the conditions set out in the *prospectus* and provided that this will not materially prejudice any existing *unitholders* in the *scheme*.

### 8.3 Investor relations

#### Application

- 8.3.1 R This section applies to an *ICVC* which is a *qualified investor scheme* and the *authorised fund manager* of a *qualified investor scheme*.

#### Drawing up and availability of prospectus

- 8.3.2 R (1) An *authorised fund manager* must ensure that a *prospectus* of a *qualified investor scheme* is drawn up which contains the information, specified in *COLL 8.3.4R* (Table: contents of qualified investor scheme prospectus), and the *authorised fund manager* must:
- (a) revise the *prospectus* immediately upon the occurrence of any materially significant change in the information required to be stated within it;
  - (b) include the date of any revision in a prominent manner in the revised *prospectus*, and
  - (c) send a copy of the original and any revised *prospectus* to the *FSA*.
- (2) The *prospectus* must not contain any provision which is unfairly prejudicial to the interests of *unitholders* generally or to the *unitholders* of any *class* of *units*.
- (3) An *ICVC* or the *manager* of an *AUT* must offer a copy of the *scheme's* most recent *prospectus* free of charge to any *person* eligible to invest in a *qualified investor scheme* prior to the purchase of any *units*.

#### False or misleading prospectus

- 8.3.3 R The *authorised fund manager* must ensure that the *prospectus* does not contain any untrue or misleading statement or omit any matter required by the *rules* in this sourcebook to be included in it.

#### Table: contents of qualified investor scheme prospectus

- 8.3.4 R This table belongs to *COLL 8.3.2R*.

##### 1 Document status

A statement that this document is the *prospectus* of the *authorised fund* valid as at a particular date which shall be the date of the *document*.

##### 2 Description of the authorised fund

Information detailing:

- (1) the name of the *authorised fund*;
- (2) that the *authorised fund* is either an *ICVC* or an *AUT*;



- (3) that the *scheme* is a *qualified investor scheme*;
- (4) where relevant, that the *unitholders* in an *ICVC* are not liable for the debts of the *authorised fund*;
- (5) where relevant, the address of the *ICVC's* head office and the address in the *United Kingdom* for service on the *ICVC* of documents required or authorised to be served on it;
- (6) the effective date of the *authorisation order* made by the *FSA* and, if the duration of the *authorised fund* is not unlimited, when it will or may terminate;
- (7) the *base currency* for the *authorised fund*;
- (8) where relevant, the maximum and minimum sizes of the *ICVC's* capital; and
- (9) the circumstances in which the *authorised fund* may be wound up under the *rules* in *COLL* and a summary of the procedure for, and the rights of *unitholders* under, such a winding up.

### 3 **Investment objectives and policy**

- (1) Sufficient information to enable a *unitholder* to ascertain:
  - (a) the investment objectives of the *authorised fund*;
  - (b) the *authorised fund's* investment policy for achieving those investment objectives, including:
    - (i) the general nature of the portfolio and any intended specialisation;
    - (ii) the policy for the spreading of risk in the *scheme property*; and
    - (iii) the policy in relation to the exercise of borrowing powers;
  - (c) a description of any restrictions in the assets in which investment may be made; and
  - (d) the extent (if any) to which that investment policy does not envisage remaining fully invested at all times.
- (2) For investment in immovables :
  - (a) the countries or territories of immovables in which the *authorised fund* may invest;
  - (b) the policy of the *authorised fund manager* in relation to insurance of immovables forming part of the *scheme property*; and

(c) the policy of the *authorised fund manager* in relation to the granting of options over immovables in the *scheme property* and the purchase of options on immovables.

(3) If intended, whether the *scheme property* may consist of *units* in *collective investment schemes* ("second *schemes*") which are managed by or operated by the *authorised fund manager* or by one of its *associates* and a statement as:

(a) to the basis of the maximum amount of the charges in respect of transactions in a second *scheme*; and

(b) the extent to which any such charges will be reimbursed to the *scheme*.

(4) If intended, whether the *scheme* may enter into *stock lending* transactions and, if so, what procedures will operate and what *collateral* will be required.

#### 4 **Distributions and accounting dates**

Relevant details of accounting and distribution dates and a description of the procedures:

(1) for determining and applying income (including how any distributable income is paid); and

(2) relating to unclaimed distributions.

#### 5 **The characteristics of units in the authorised fund**

Information as to:

(1) the names of the *classes* of *units* in issue or available for *issue* and the rights attached to them in so far as they vary from the rights attached to other *classes*;

(2) how *unitholders* may exercise their voting rights and what these are; and

(3) the circumstances where a mandatory *redemption*, *cancellation* or conversion of *units* from one *class* to another may be required.

#### 6 **The authorised fund manager**

The following particulars of the *authorised fund manager*:

(1) its name and the nature of its corporate form;

(2) the country or territory of its incorporation;

(3) the date of its incorporation and if the duration of its corporate status is limited, when that status will or may cease;

- (4) if it is a *subsidiary*, the name of its ultimate *holding company* and the country or territory in which that *holding company* is incorporated;
- (5) the address of its registered office, its head office, and, if different, the address of its principal place of business in the *United Kingdom*;
- (6) the amount of its issued share capital and how much of it is paid up;
- (7) for an *ICVC*, a summary of the material provisions of the contract between the *ICVC* and the *authorised fund manager* which may be relevant to *unitholders* including provisions (if any) relating to termination, compensation on termination and indemnity; and
- (8) for an *AUT*, the names of the *directors* of the *manager*.

#### 7 **Directors of an ICVC, other than the ACD**

Other than for the *ACD*:

- (1) the names and positions in the *ICVC* of the *directors*; and
- (2) the manner, amount and calculation of the *remuneration* of the *directors*.

#### 8 **The depositary**

The following particulars of the *depositary*:

- (1) its name and the nature of its corporate form;
- (2) the country or territory of its incorporation;
- (3) the address of its registered office and the address of its head office if that is different from the address of its registered office; and
- (4) if neither its registered office nor its head office is in the *United Kingdom*, the address of its principal place of business in the *United Kingdom*.

#### 9 **The investment adviser**

If an *investment adviser* is retained in connection with the business of the *authorised fund*, its name and whether or not it is authorised by the *FSA*.

#### 10 **The auditor**

The name of the auditor of the *authorised fund*.

#### 11 **The register of unitholders**

Details of the address in the *United Kingdom* where the *register* of *unitholders* is kept and can be inspected by *unitholders*.

#### 12 **Payments out of the scheme property**

The payments that may be made out of the *scheme property* to any *person* whether by way of *remuneration* for services, or reimbursement of expense and for each category of *remuneration* or expense, the following should be specified:

- (1) the current rates or amounts of such *remuneration*;
- (2) how the *remuneration* will be calculated and accrue and when it will be paid;
- (3) if notice has been given to *unitholders* of the *authorised fund manager's* intention to:
  - (a) introduce a new category of *remuneration* for its services; or
  - (b) increase the basis of any current charge; or
  - (c) change the basis of the treatment of a payment from the *capital property* set out in *COLL 8.5.13R(2)(Payments)*;  
particulars of that introduction or increase and when it will take place;
- (4) the types of any other charges and expenses that may be taken out of the *scheme property*; and
- (5) if, in accordance with *COLL 8.5.13R(2)*, all or part of the *remuneration* or expense are to be treated as a capital charge:
  - (a) that fact; and
  - (b) the basis of the charge which may be so treated.

### 13 **Dealing**

Details of:

- (1) the *dealing days* and times in the *dealing day* on which the *authorised fund manager* will receive requests for the *sale* and *redemption* of *units*;
- (2) the procedures for effecting:
  - (a) the *issue* and *cancellation* of *units*;
  - (b) the *sale* and *redemption* of *units*; and
  - (c) the settlement of transactions;
- (3) the steps required to be taken by a *unitholder* in redeeming *units* before he can receive the proceeds including any relevant notice periods and the circumstances and periods where a deferral of payment as provided in *COLL 8.5.11R(3)* (Sale and redemption) may be applied;
- (4) the circumstances in which the *redemption* of *units* may be suspended;

- (5) the *days* and times in the *day* on which recalculation of the *price* will commence;
- (6) details of the minimum number or value of each type of *unit* in the *authorised fund* which:
  - (a) any one *person* may hold; and
  - (b) may be the subject of any one transaction of *sale* or *redemption*;
- (7) the circumstances in which the *authorised fund manager* may arrange for, and the procedure for, a *redemption* of *units* in specie;
- (8) the circumstances in which the further *issue* of *units* in any particular *class* may be limited and the procedures relating to this; and
- (9) the circumstances in which direct *issue* or *cancellation* of *units* by the *ICVC* or the *trustee* (as appropriate) may occur and the relevant procedures for such *issues* and *cancellations*.

#### 14 **Valuation of scheme property**

Details as to:

- (1) how frequently and at what times of the *day* the *scheme property* will be regularly valued to determine the *price* at which *units* in the *scheme* may be purchased from or redeemed by the *authorised fund manager* and a description of any circumstance where the *scheme property* may be specially valued;
- (2) in relation to each purpose for which the *scheme property* must be valued, the basis on which it will be valued; and
- (3) how the *price* of *units* of each *class* will be determined, including whether a forward or *historic price* basis is to be applied.

#### 15 **Sale and redemption charges**

If the *authorised fund manager* makes any charges on *sale* or *redemption* of *units*, details of the charging structure and how notice will be provided to *unitholders* of any increase.

#### 16 **General information**

Details as to:

- (1) when annual and half- yearly reports will be published; and

- (2) the address at which copies of the *instrument constituting the scheme*, any amending instrument and the most recent annual reports may be inspected and from which copies may be obtained.

#### 17 **Information on the umbrella**

In the case of a *scheme* which is an *umbrella*, the following information:

- (1) that a *unitholder* may exchange *units* in one *sub-fund* for *units* in another *sub-fund* and that such an exchange is treated as a *redemption and sale*;
- (2) what charges may be made on exchanging *units* in one *sub-fund* for *units* in other *sub-funds*;
- (3) the policy for allocating between *sub-funds* any assets of, or costs, charges and expenses payable out of, the *scheme property* which are not attributable to any particular *sub-fund*;
- (4) in respect of each *sub-fund*, the currency in which the *scheme property* allocated to it will be valued and the *price* of *units* calculated and payments made, if this currency is not the *base currency* of the *umbrella*; and
- (5) for an *ICVC*, that the *sub-funds* are not “ring fenced” and in the event of an *umbrella* being unable to meet liabilities attributable to any particular *sub-fund* out of the assets attributable to that *sub-fund*, the remaining liabilities may have to be met out of the assets attributable to other *sub-funds*.

#### 18 **Application of the prospectus contents to an umbrella**

For a *scheme* which is an *umbrella*, information required must be stated:

- (1) in relation to each *sub-fund* where the information for any *sub-fund* differs from that for any other; and
- (2) for the *umbrella* as a whole, but only where the information is relevant to the *umbrella* as a whole.

#### 19 **Additional information**

Any other material information which is within the knowledge of the *directors* of an *ICVC* or the *manager* of an *AUT*, or which the *directors* or *manager* would have obtained by the making of reasonable enquiries which investors and their professional advisers would reasonably require, and reasonably expect to find in the *prospectus*, for the purpose of making an informed judgement about the merits of investing in the *authorised fund* and the extent and characteristics of the risks accepted by so participating.

### **Report and accounts**

- 8.3.5 (1) The *authorised fund manager* must prepare a report in respect of each *annual*  
R *accounting period* and *half-yearly accounting period*.
- (2) The first *annual accounting period* must begin:
- (a) on the first *day* of any period of *initial offer*; or
  - (b) in any other case, on the date of the relevant *authorisation order*.
- (3) The *authorised fund manager* must within a reasonable time after the end of each relevant accounting period, publish the annual report and half-yearly report and provide a copy free of charge on request to any *unitholder*.
- (4) The *authorised fund manager* must comply with the requirements of the *IMA SORP*.
- (5) The *authorised fund manager* must provide free of charge on the request of a purchaser of *units* a copy of the latest annual or half-yearly report before the conclusion of that sale.
- (6) The *authorised fund manager* must provide a copy of each annual and half-yearly report to the *FSA*.

### **Alterations to the scheme and notices to unitholders**

- 8.3.6 (1) Any proposed change which would be reasonably considered to be a  
R fundamental change to the *scheme* requires the prior sanction of an ordinary resolution of the *unitholders*.
- (2) Any proposed change to the *scheme* which is not within (1) but which would be reasonably considered to be significant, requires the giving of reasonable notice to *unitholders* to become effective.
- (3) Alterations affecting only a particular *sub-fund* or *class* of *units* may be approved in accordance with (1) or (2) for the particular *sub-fund* or *class* of *units*, with the consent of, or, as the case may be, notice to, the relevant *unitholders*.
- (4) This *rule* and *COLL* 8.3.8R (Meetings) will apply (unless the context requires otherwise) to alterations concerning *unitholders* of a particular *sub-fund* or *class* of *units* rather than the *scheme* or *sub-fund* as a whole.

### **Alterations to the scheme and notices to unitholders: guidance**

8.3.7 Although account should be taken of the *guidance* on fundamental changes (*COLL*  
G 4.3.5G (Guidance on fundamental changes)) and significant changes (*COLL* 4.3.7G  
(Guidance on significant changes)) the impact of any change to the *scheme* should be  
assessed individually based on the nature of the *scheme* and its investor profile.

**Meetings**

- 8.3.8 (1) Details of the procedures for the convening and conducting of meetings and  
R resolutions must be set out in the *instrument constituting the scheme* and be  
reasonable and fair as between all relevant parties.
- (2) The *authorised fund manager* must record and keep minutes for six years of all  
proceedings to which *COLL* 8.3.6R (Alterations to the scheme and notices to  
unitholders) and this *rule* are relevant.
- (3) The provisions in *COLL* 4.4.12R (Notices to unitholders), *COLL* 4.4.13R  
(Other notices) and *COLL* 4.4.14G (References to writing and electronic  
documents) apply in relation to *qualified investor schemes*.



## 8.4 Investment and borrowing powers

### Application

- 8.4.1 This section applies to an *ICVC* which is a *qualified investor scheme* and an  
R *authorised fund manager* and a *depository* of a *qualified investor scheme*.

### Spread of risk

- 8.4.2 An *authorised fund manager* must take reasonable steps to ensure that the *scheme*  
R *property* of a *qualified investor scheme* provides a spread of risk, taking into  
account the investment objectives and policy of the *scheme* as stated in the most  
recently published *prospectus*, and in particular, any investment objective as regards  
return to the *unitholders* (whether through capital appreciation or income or both).

### Investment powers: general

- 8.4.3 (1) The *scheme property* of a *qualified investor scheme* may, subject to the *rules*  
R in this chapter, comprise any assets or *investments* to which it is *dedicated*.
- (2) The *instrument constituting the scheme* and the *prospectus* may further  
restrict:
- (a) the kinds of assets in which the *scheme property* may be invested;
  - (b) the types of transactions permitted and any relevant limits; and
  - (c) the borrowing powers of the *scheme*.

### Qualified investor schemes: general

- 8.4.4 The *scheme property* of a *qualified investor scheme* must, except where otherwise  
R provided by the *rules* in this chapter, consist only of one or more of the following to  
which it is *dedicated*:
- (1) any *specified investment*:
    - (a) within articles 74 to 86 of the *Regulated Activities Order*; and
    - (b) within article 89 (Rights to or interests in investments) of the *Regulated Activities Order* where the right or interest relates to a *specified investment* within (a);
  - (2) an interest in an *approved immovable* under *COLL* 8.4.11R (Investment in property), provided the country or territory in which the land or building is situated is identified in the *prospectus*;

- (3) *precious metals*; or
- (4) a *commodity* contract traded on an *RIE* or a *recognised overseas investment exchange*.

**Investment in collective investment schemes**

8.4.5 A *qualified investor scheme* may invest in *units* in a *scheme* (a second *scheme*) only  
 R if the second *scheme* is:

- (1) a *regulated collective investment scheme*; or
- (2) a *scheme* not within (1) where the *authorised fund manager* has taken reasonable care to determine that:
  - (a) it is the subject of an independent annual audit conducted in accordance with international accounting standards;
  - (b) it has its value verified by a *person* independent from its *operator* in relation to each *day* on which dealing in that *scheme's units* may take place;
  - (c) there are mechanisms in place to enable *unitholders* to redeem their *units* within a reasonable time;
  - (d) it is prohibited from having more than 15% of its value in *units* of *schemes*; and
  - (e) it operates in accordance with the principle of risk spreading.

**Delivery of property under a transaction in derivatives or a commodities contract**

8.4.6 (1) An *authorised fund manager* must take reasonable care to determine the  
 R following when entering into any transaction in *derivatives* or any *commodity* contract which may result in any asset becoming part of the *scheme property*:

- (a) if it is an asset in which the *scheme property* could be invested, that the transaction:
  - (i) can be readily closed out; or
  - (ii) would at the expected time of delivery relate to an asset which could be included in the *scheme property* under the *rules* in this chapter; or
- (b) in any other case that the transaction can be readily closed out.

- (2) An *authorised fund manager* may acquire an asset within (1) if its determination has proved incorrect and if it determines that acquisition is in the interests of the *unitholders*, provided it has the consent of the *depository*.
- (3) Any asset within (1) acquired in accordance with (2) may form part of the *scheme property* despite any other *rule* in this chapter until the position can be rectified.

#### **Cover for transactions in derivatives and forward transactions**

- 8.4.7 (1) A transaction in *derivatives* or a forward transaction may be entered into only  
R if the maximum exposure, in terms of the *principal* or *notional principal* created by the transaction to which the *scheme* is or may be committed by another *person*, is covered globally under (2).
- (2) Exposure is globally covered if adequate cover from within the *scheme property* is available to meet the *scheme's* total exposure taking into account any reasonably foreseeable market movement.
  - (3) The total exposure relating to *derivatives* held in a *qualified investor scheme* may not exceed the net value of the *scheme property*.
  - (4) No element of cover may be used more than once.

#### **Continuing nature of limits and requirements**

- 8.4.8 (1) An *authorised fund manager* must, as frequently as necessary to ensure  
R compliance with *COLL* 8.4.7R(2) and (4), re-calculate the amount of cover required in respect of *derivatives* and forwards positions in existence under this chapter.
- (2) *Derivatives* and forwards positions may be retained in the *scheme property* only so long as they remain covered globally under *COLL* 8.4.7R.
  - (3) An *authorised fund manager* must use a risk management process enabling it to monitor and measure as frequently as appropriate the risk of a *scheme's derivatives* positions and their contribution to the overall risk profile of the *scheme*.

#### **Permitted stock lending**

- 8.4.9 (1) The *ICVC*, or the *depository* at the request of the *ICVC*, or the *trustee* at the  
R request of the *manager*, may enter into a *stock lending* arrangement within section 263B of the Taxation of Chargeable Gains Act 1992 (without extension by section 263C).

- (2) The *depository* must ensure that the value of any *collateral*, for the *stock lending* arrangement is at all times at least equal to the value of the securities transferred by the *depository*.
- (3) In the case of the expiry of validity of any *collateral*, the duty in (2) is satisfied if the *depository* or the *authorised fund manager*, as appropriate, takes reasonable care to determine that sufficient *collateral* will be transferred by close of business on the *day* of expiry.

**General power to borrow**

- 8.4.10 R (1) The *ICVC* or *trustee* (on the instructions of the *manager*) may borrow money for the use of the *authorised fund* on terms that the borrowing is to be repayable out of the *scheme property*.
- (2) The *authorised fund manager* must ensure that the *authorised fund's* borrowing does not, on any *day*, exceed 100 % of the net value of the *scheme property* and must take reasonable care to ensure that arrangements are in place that will enable borrowings to be closed out to ensure such compliance.
- (3) In this rule "borrowing" also includes any arrangement (including a combination of *derivatives*) designed to achieve a temporary injection of money into the *scheme property* in the expectation that the sum will be repaid.
- (4) Where the limit in (2) is breached, the *authorised fund manager* must take action in accordance with the principles set out in *COLL* 8.5.3R(3) to (5) (Duties of the authorised fund manager: investment and borrowing powers) to deal with that breach.

**Investment in property**

- 8.4.11 R (1) Any investment in land or a building held within the *scheme property* of a *qualified investor scheme* must be in an immovable within (2).
- (2) For an immovable :
- (a) it must be situated in a country or territory identified in the *prospectus*;
  - (b) the *authorised fund manager* must have taken reasonable care to determine that the title to the interest in the immovable is a good marketable title; and
  - (c) the *manager* or the *ICVC* must have received a report from the *appropriate valuer* that:

- (i) contains a valuation of the interest in the immovable (with and without any relevant existing mortgage); and
  - (ii) states that in the *appropriate valuer's* opinion the interest in the immovable would if acquired by the *scheme*, be capable of being disposed of reasonably expeditiously at that valuation;
- (d) unless (c) is satisfied, the *manager* or the *ICVC* must have received a report from an *appropriate valuer* valuing the interest in the immovable and stating that:
- (i) the immovable is adjacent to or in the vicinity of another immovable included in the *scheme property*; and
  - (ii) in the opinion of the *appropriate valuer*, the total value of the interests in both immovables would at least equal the sum of the price payable for the interest in the immovable and the existing value of the interest in the other immovable; and
- (e) it must not be bought:
- (i) if it becomes apparent to the *authorised fund manager* that the report in either (c) or (d) could no longer reasonably be relied upon; or
  - (ii) at a price more than 105% of the valuation relevant to the interest for that immovable in the report in either (c) or (d).
- (3) Any contents of any building may be regarded as part of the relevant immovable.
- (4) An *appropriate valuer* must be a *person* who:
- (a) has knowledge of and experience in the valuation of immovables of the relevant kind in the relevant area;
  - (b) is qualified to be a *standing independent valuer* of an *authorised fund* or is considered by the *scheme's standing independent valuer* to hold an equivalent qualification;
  - (c) is independent of the *ICVC*, the *depository* and each of the *directors* of the *ICVC* or of the *manager* and *trustee* of the *AUT*; and
  - (d) has not engaged himself or any of his *associates* in relation to the finding of the immovable for the *scheme* or the finding of the *scheme* for the immovable.

### **Investment limits for immovables**

8.4.12 The following limits apply in respect of immovables held as part of the *scheme*  
R *property*:

- (1) the amount secured by mortgages over any immovable must not exceed 100% of the latest valuation by an *appropriate valuer* under *COLL* 8.4.11(2)(c) or (d) or *COLL* 8.4.13R, as appropriate;
- (2) no option may be granted to a *person* to buy or obtain an interest in any immovable comprised in the *scheme property* if this might unduly prejudice the ability to provide *redemption*. and
- (3) the total of all premiums paid for options to purchase immovables must not exceed 10% of the *scheme* value in any 12 *month* period, calculated at the date of the granting of the option.

### **Standing independent valuer and valuation**

8.4.13 (1) In relation to the appointment of a valuer the *authorised fund manager* must:  
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- (a) at the outset appoint the *standing independent valuer* with the approval of the *depository* and likewise upon any vacancy; and
  - (b) ensure that any immovables in the *scheme property* are valued by an *appropriate valuer (standing independent valuer)* appointed by the *authorised fund manager*.
- (2) The following apply in relation to the functions of the *standing independent valuer*:
- (a) the *authorised fund manager* must ensure that the *standing independent valuer* appointed under (1), procures the valuation of all the immovables held within the *scheme property*, on the basis of a full valuation with physical inspection (including, where the immovable is or includes a building, internal inspection) at least once a year;
  - (b) for the purposes of (a), any inspection in relation to adjacent properties of a similar nature and value may be limited to that of only one such representative property;
  - (c) the *authorised fund manager* must ensure that the *standing independent*

- valuer* values the immovables, on the basis of a review of the last full valuation, at least once a *month*;
- (d) if either the *authorised fund manager* or the *depository* becomes aware of any matter which appears likely to:
    - (i) affect the outcome of a valuation of an immovable; or
    - (ii) cause the valuer to decide to value under (a), instead of under (c), it must immediately inform the *standing independent valuer* of that matter;
  - (e) the *authorised fund manager* must use its best endeavours to ensure that any other *affected person* reports to the *standing independent valuer* immediately upon that *person* becoming aware of any matter within (d); and
  - (f) any valuation by the *standing independent valuer* must be on the basis of an 'Open Market value' as defined in the Royal Institute of Chartered Surveyors' Appraisal and Valuation Standards (Fifth Edition) ("Red Book") but is subject to any provisions of the *instrument constituting the scheme*.
- (3) In relation to immovables:
- (a) any valuation under this *rule* has effect, until the next valuation under this *rule*, for the purposes of the value of immovables; and
  - (b) an agreement to transfer an immovable or an interest in an immovable is to be disregarded for the purpose of the valuation of the *scheme property* unless it reasonably appears to the *authorised fund manager* to be legally enforceable.

## 8.5 Powers and responsibilities

### Application

- 8.5.1 This section applies to an *ICVC* which is a *qualified investor scheme* and the  
R *authorised fund manager*, any other *directors* of an *ICVC* and the *depository* of a *qualified investor scheme*.

### Functions of the authorised fund manager

- 8.5.2 (1) The *authorised fund manager* must manage the *scheme* in accordance with:  
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- (a) the *instrument constituting the scheme*;
  - (b) the *rules* in this sourcebook;
  - (c) the most recently published *prospectus*; and
  - (d) for an *ICVC*, the *OEIC Regulations*.
- (2) The *authorised fund manager* must carry out such functions as are necessary to ensure compliance with the *rules* in this sourcebook that impose obligations on the *authorised fund manager* or *ICVC*, as appropriate.
- (3) The *authorised fund manager* must:
- (a) make decisions as to the constituents of the *scheme property* in accordance with the investment objectives and policy of the *scheme*;
  - (b) instruct the *depository* how rights attaching to the ownership of *scheme property* are to be exercised;
  - (c) take action immediately to rectify any breach of the pricing methodology set out in the *prospectus*, which must (unless the *authorised fund manager* determines on reasonable grounds that the breach is of minimal significance) extend to payment of money:
    - (i) by the *authorised fund manager* to *unitholders* and former *unitholders*;
    - (ii) by the *ACD* to the *ICVC*;
    - (iii) by the *ICVC* to the *ACD*;
    - (iv) by the *manager* to the *trustee*; or
    - (v) by the *trustee* (for the account of the *AUT*) to the *manager*;
  - (d) ensure where relevant that the *ICVC* complies with the relevant



obligations imposed by, and when appropriate, exercises the relevant powers provided under, the *OEIC Regulations*;

- (e) maintain such records as are necessary to enable the *authorised fund manager* or the *ICVC*, as appropriate, to comply with and demonstrate compliance with the *rules* in this sourcebook and also in the case of an *ICVC*, the *OEIC Regulations*; and
- (f) maintain for a period of six years a daily record of the *units* held, acquired or disposed of by the *authorised fund manager* including the *classes* of such *units*, and of the balance of any acquisitions and disposals.

#### **Duties of the authorised fund manager: investment and borrowing powers**

8.5.3 (1) An *authorised fund manager* may give instructions to deal in the *scheme*  
R *property*.

- (2) An *authorised fund manager* must avoid the *scheme property* being used or invested contrary to any provision in *COLL 8.4* (Investment and borrowing powers).
- (3) An *authorised fund manager* must immediately on becoming aware of any breach of *COLL 8.4* take action, at its own expense, to rectify that breach.
- (4) An *authorised fund manager* must take the action in (3) immediately, except in circumstances where doing so would not be in the best interests of *unitholders*, in which case the action must be taken as soon as such circumstances cease to apply.
- (5) An *authorised fund manager* must not postpone taking action in accordance with (3) unless the *depository* has given its consent.

#### **Duties of the depository**

8.5.4 (1) The *depository* is responsible for the safekeeping of all the *scheme property*.  
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- (2) The *depository* must:
  - (a) take all steps to ensure that transactions properly entered into for the account of the *scheme* are completed;
  - (b) take all steps to ensure that instructions properly given by the *authorised fund manager* in respect of the exercise of rights related to *scheme*

- property* are carried out;
- (c) ensure that any *scheme property* in registered form is as soon as reasonably practicable registered in its name or that of its nominee or delegate, as appropriate;
  - (d) take into its custody or control all documents of title of the *scheme property* other than in respect of *derivatives* or forward transactions;
  - (e) ensure that any resulting benefit of a *derivatives* or forward transaction is received by itself in respect of the *scheme*;
  - (f) hold and deal with any income received in respect of *scheme property* in accordance with *COLL* 8.5.15R (Income);
  - (g) take reasonable care to ensure that the *scheme* is managed by the *authorised fund manager* in accordance with:
    - (i) *COLL* 8.4 (Investment and borrowing powers);
    - (ii) *COLL* 8.5.9R (Valuation, pricing and dealing); and
    - (iii) *COLL* 8.5.15R (Income);
  - (h) keep records so as to comply with the *rules* in this sourcebook and so as to demonstrate such compliance; and
  - (i) be responsible for any other duties as set out in the *instrument constituting the scheme*.
- (3) If a relevant *ICVC* ceases to have any *directors*, the *depository* may act in accordance with *COLL* 6.5.6R (*ICVC* without a director).

### **Delegation**

- 8.5.5 (1) The *authorised fund manager* (or in addition any other *director* in the case of R an *ICVC*) may delegate any function to any *person*.
- (2) The *depository* has the power to delegate any function to anyone, including in the case of an *ICVC* a *director*, to assist the *depository* to perform its functions, save that it must not retain the services of the *authorised fund manager* or, in the case of an *ICVC*, any other *director* to perform any part of its functions of safe custody of the *scheme property*.
- (3) Subject to any provisions of the *OEIC Regulations*, the delegator in (1) and (2) will not be responsible under the *rules* in *COLL* for any act or omission of the delegate provided that the delegator can show:

- (a) that it was reasonable for the delegator to obtain assistance to perform the function in question;
- (b) that the delegate was and remained competent to provide that assistance; and
- (c) that the delegator took reasonable care to ensure that the assistance was provided in a competent manner.

### **Delegation and responsibility for regulatory obligations**

8.5.6 SYSC 3.2 contains *guidance* relating to delegation including external delegation, and G SYSC 3.2.4(1) G states that a *firm* cannot contract out of its regulatory obligations.

### **Conflicts of interest**

- 8.5.7 (1) The *authorised fund manager and the depositary* must ensure that any transaction in respect of the *scheme property* undertaken with an *affected person* is on terms at least as favourable to the *scheme* as any comparable arrangement on normal commercial terms negotiated at arm's length with an independent third party.
- R (2) Paragraph (1) is subject to any provision in the *instrument constituting the scheme* and the *prospectus* imposing a prohibition in relation to any type of transaction.

### **The register of unitholders: AUTs**

- 8.5.8 (1) The *manager* or the *trustee* (in accordance with their responsibilities as set out in the *instrument constituting the scheme*) must maintain a *register* of *unitholders* as a *document* in accordance with this *rule*.
- R (2) The *register* must contain:
- (a) the name and address of each *unitholder* (for joint *unitholders* no more than four need to be registered);
  - (b) the number of *units* (including fractions of a *unit*) of each *class* held by each *unitholder*; and
  - (c) the date on which the *unitholder* was registered in the *register* for the *units* standing in his name.
- (3) The *manager* or the *trustee* (as appropriate) must take all reasonable steps and exercise all due diligence to ensure the *register* is kept complete and up to date.

- (4) Where relevant, the *manager* must immediately notify the *trustee* of any information he receives which may affect the accuracy of any entry in the *register*.

### **Valuation, pricing and dealing**

- 8.5.9 R
- (1) The value of the *scheme property* is the net value of the *scheme property* after deducting any outstanding borrowings (including any capital outstanding on a mortgage of an immovable).
  - (2) Any part of the *scheme property* which is not an *investment* (save an immovable) must be valued at fair value.
  - (3) For the purposes of (2), any charges that were paid, or would be payable, on acquiring or disposing of the asset must be excluded from the value of that asset.
  - (4) The value of the *scheme property* of an *authorised fund* must, save as otherwise provided in this section, be determined in accordance with the provisions of the *instrument constituting the scheme* and the *prospectus*, as appropriate.
  - (5) The *scheme* must have a *valuation point* on each *dealing day*.
  - (6) The *authorised fund manager* must prepare a valuation in accordance with (4) for each relevant type of *unit* at each relevant *valuation point*.
  - (7) The price of a *unit* must be calculated on the basis of the valuation in (6) in a manner that is fair and reasonable as between *unitholders*.
  - (8) Immediately after completing a valuation under (6), the *authorised fund manager* must notify the *depository* of:
    - (a) the price in the relevant currency of each type of *unit* as determined for the relevant *valuation point*; and
    - (b) the basis of any adjustment applied in relation to that *valuation point*.
  - (9) The *authorised fund manager* must publish in an appropriate manner the price of any type of *unit* based on the notification to the *depository* in (8)(a).
  - (10) The *authorised fund manager* must also provide on request to any *unitholder* at any time an estimated price for any type of *unit* in the *scheme*.
  - (11) The period of any *initial offer* and how it should end must be set out in the *prospectus* and must not be of unreasonable length.

### **Issues and cancellations of units**

8.5.10 (1) The *authorised fund manager* must:

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- (a) ensure that at each *valuation point* there are at least as many *units* in issue of any *class* as there are *units* registered to *unitholders* of that *class*; and
  - (b) not do, or omit anything that would, or might confer on itself a benefit or advantage at the expense of a *unitholder* or potential *unitholder*.
- (2) For the purposes of (1) the *authorised fund manager* may take into account *sales* and *redemptions* after the *valuation point*, provided it has systems and controls to ensure compliance with (1).
- (3) The *authorised fund manager* must arrange for the *issue* and *cancellation* of *units* and pay money or assets to or from the *depository* for the account of the *scheme* as required by the *prospectus*.
- (4) The *authorised fund manager* must keep a record of *issues* and *cancellations* made under this *rule*.
- (5) The *authorised fund manager* may arrange for the *ICVC*, or instruct the *trustee* to *issue* or *cancel units* where the *authorised fund manager* would otherwise be obliged to *sell* or *redeem* the *units* in the manner set out in the *prospectus*.
- (6) Where the *authorised fund manager* has not complied with (1), it must correct the error as soon as possible and must reimburse the *scheme* any costs it may have incurred in correcting the position, subject to any reasonable minimum level for such reimbursement as set out in the *prospectus*.

### **Sale and redemption**

8.5.11 (1) The *authorised fund manager* must, at all times during the *dealing day*, be willing to effect the *sale* of *units* to any eligible investor (within any conditions in the *instrument constituting the scheme* and the *prospectus* which must be fair and reasonable as between all *unitholders* and potential *unitholders*) for whom the *authorised fund manager* does not have reasonable grounds to refuse such *sale*.

- (2) The *authorised fund manager* must, at all times during the *dealing day*, effect a *redemption* on the request of any eligible *unitholder* (within any conditions in the *instrument constituting the scheme* and the *prospectus*) of *units* owned by that *unitholder*, unless the *authorised fund manager* has reasonable grounds to refuse such *redemption*.
- (3) On agreeing to a *redemption* of *units* within (2), the *authorised fund manager* must pay the full proceeds of the *redemption* to the *unitholder* within any reasonable period specified in the *instrument constituting the scheme* or the *prospectus*, unless it has reasonable grounds for withholding payment.
- (4) Payment of proceeds on *redemption* must be made by the *authorised fund manager* in any manner provided for in the *prospectus* which must be fair and reasonable as between redeeming *unitholders* and continuing *unitholders*.

#### **Limited redemption periods**

- 8.5.12 The maximum period between *dealing days* for a *qualified investor scheme* will  
 G depend on the reasonable expectations of the target investor group and the particular investment objectives and policy of the *scheme*. For instance, for a *scheme* aiming to invest in large property developments, the expectation would be that it is reasonable to have a much longer period between *dealing days* for liquidity reasons than for a *scheme* investing predominantly in listed *securities*.

#### **Payments**

- 8.5.13 (1) An *ICVC* must not incur any expense in respect of the use of any movable or  
 R immovable property unless the *scheme* is *dedicated* to such investment or such property is necessary for the direct pursuit of its business.
- (2) Payments out of the *scheme property* may be made from *capital property* rather than from income, provided the basis for this is set out in the *prospectus*.

#### **Exemption from liability to account for profits**

- 8.5.14 An *affected person* is not liable to account to another *affected person* or to the  
 G *unitholders* of the *scheme* for any profits or benefits it makes or receives that are made or derived from or in connection with:
- (1) *dealings* in the *units* of a *scheme*; or
  - (2) any transaction in *scheme property*; or
  - (3) the supply of services to the *scheme*;

where disclosure of the non-accountability has been made in the *prospectus* of the *scheme*.

### **Income**

8.5.15 (1) A *qualified investor scheme* must have:

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- (a) an *annual accounting period*;
- (b) a *half-yearly accounting period*; and
- (c) an *accounting reference date*;

the details of which must be set out in the *prospectus*.

- (2) A *qualified investor scheme* must have an *annual income allocation date*, which must be within four months of the *accounting reference date*.
- (3) A *qualified investor scheme* may have an *interim income allocation date* and *interim accounting periods* and if it does, the *interim income allocation date* must be within a reasonable period of the end of the relevant *interim accounting period* as set out in the *prospectus*.
- (4) A *qualified investor scheme* must have a *distribution account* where the *income property* is transferred at the end of the relevant accounting period.
- (5) If income is allocated and distributed during an accounting period:
  - (a) with effect from the end of the relevant accounting period, the amount of income allocated to *unit classes* that accumulate income becomes part of the *capital property* and requires an adjustment to the proportion of the value of the *scheme property* to which they relate if other *classes units* are in *issue* during the period;
  - (b) the adjustment in (a) must ensure the *price* remains unchanged despite the transfer of income; and
  - (c) the amount of any interim distribution may not be more than the amount which, in the opinion of the *authorised fund manager*, would be available for allocation if the *interim accounting period* and all previous *interim accounting periods* in the same *annual accounting period*, taken together, were an *annual accounting period*.

## 8.6 Termination, suspension, and schemes of arrangement

### Application

8.6.1 This section applies to:

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- (1) an *authorised fund manager*, the *directors*, and the *depository* of a *qualified investor scheme*; and
- (2) an *ICVC* which is a *qualified investor scheme*.

### Termination

8.6.2 For a *qualified investor scheme* the provisions in *COLL 7.3* to *COLL 7.5* will apply

R as appropriate as if *COLL 7* applied to *qualified investor schemes*.

### Suspension

- 8.6.3
- R
- (1) The *authorised fund manager* may within any parameters which are fair and reasonable in respect of all the *unitholders* in the *scheme* and which are set out in the *prospectus*, suspend *dealings* in *units* of the *scheme*, a *sub-fund* or a *class*.
  - (2) Any suspension within (1) must only be where the *authorised fund manager* has determined on reasonable grounds that there is good and sufficient reason in the interests of *unitholders* or potential *unitholders* and the *authorised fund manager* must have regard to the interests of all the *unitholders* in the *scheme* in reaching such an opinion.
  - (3) At the commencement of suspension under (1), the *authorised fund manager* must immediately inform the *FSA* of the suspension and the reasons for it.
  - (4) The suspension of *dealings* in *units* must cease within 28 *days* of its commencement or, if earlier, as soon as (2) no longer applies.
  - (5) The *authorised fund manager* must inform the *FSA* immediately of the resumption of *dealings*.

### Suspension

8.6.4 Under section 257 of the *Act* (Directions) the *FSA* may at its option extend the  
G suspension of *dealings* in *units* beyond 28 *days* of the commencement of suspension.

### Schemes of arrangement



8.6.5 In relation to an *ICVC* or an *AUT* which is a *qualified investor scheme*, the  
R provisions in *COLL 7.6* (Schemes of arrangement) will apply as appropriate to the  
*authorised fund manager*, any other *directors* of the *ICVC* and the *depository* as if  
*COLL 7.6* applied to a *qualified investor scheme* and did not exclude *unitholders*  
becoming *unitholders* in another *qualified investor scheme*.

## **9 Recognised schemes**

### **9.1 Application and general information**

#### **Application**

- 9.1.1 R This chapter applies to *operators of recognised schemes* and to *operators of schemes* making a notification in respect of them under Chapter V of Part XVII of the *Act* (Recognised overseas schemes).

#### **Purpose**

- 9.1.2 G This chapter enables potential *operators of recognised schemes* to know what information and *documents* the *FSA* wish to receive to enable it to consider whether to recognise the *scheme* under the *Act* for *marketing* in the *United Kingdom*.

#### **General information**

- 9.1.3 G Further information about notifications for recognition is contained in *COLLG*.

## 9.2 Section 264 recognised schemes

### Information and documents to be supplied with a section 264 notification

- 9.2.1 G (1) If the *operator* of a *collective investment scheme* constituted in a *EEA State* gives notice to the *FSA* under section 264 of the *Act*, it should include the information described in paragraphs (2) to (4) below (see the *Financial Services and Markets Act 2000 (Collective Investment Schemes Constituted in Other EEA States) Regulations 2001(SI 2001/2383)*, as amended).
- (2) The *documents* must be in English, or accompanied by a translation in English.
- (3) The *documents* should be certified by the *operator* to be true copies of the original.
- (4) The *FSA* will need the following information and documentation in connection with the notification:
- (a) the name of the *scheme*;
  - (b) the legal form of the *scheme*;
  - (c) the name and address of the *operator*;
  - (d) the address of the place in the *United Kingdom* for the service on the *operator* of notices or other *documents*;
  - (e) the name and address of any supervisory authority or authorities to which the *operator* is subject in the *EEA State* in which it is established;
  - (f) whether the *operator* intends to market the *scheme* in the *United Kingdom* in a manner which will involve it carrying on a *regulated activity* in the *United Kingdom*;
  - (g) the name and address of the *depository*;
  - (h) the address in the *United Kingdom* where the *scheme* facilities (see *COLL 9.4*) will be maintained;
  - (i) details of the arrangements for the *marketing* of *units* in the *United Kingdom*, namely:
    - (i) the proposed commencement date;
    - (ii) whether the *units* will be sold by or through any employed sales force, *authorised persons*, or unsolicited calls;

- (j) the attestation or certificate from the authorities of the *EEA State* in which the *scheme* is authorised which demonstrates that the *scheme* complies with the *UCITS Directive*;
- (k) a copy of the *instrument constituting the scheme*;
- (l) a copy of the *prospectus* and the simplified prospectus of the *scheme*; and
- (m) a copy of the latest annual report and any subsequent half-yearly report.

### 9.3 Section 270 and 272 recognised schemes

#### Information and documents to be supplied for a section 270 notification or section 272 application

- 9.3.1 D (1) If the *operator* of a *scheme* gives notice to the *FSA* under section 270 of the *Act* (Schemes authorised in designated countries or territories) or makes an application under section 272 of the *Act* (Individually recognised overseas schemes), the notice or application must include the information in paragraph (4).
- (2) The *documents* must be in English or accompanied by a translation in English.
- (3) The *documents* must be certified by the *operator* to be true copies of the originals.
- (4) The *operator* of the *scheme* must provide the following information and *documents* with the notification or application:
- (a) the name of the *scheme*;
  - (b) the legal form of the *scheme*;
  - (c) the name and address of the *operator*;
  - (d) the address of the place in the *United Kingdom* for service on the *operator* of notices or other *documents*;
  - (e) whether the *operator* intends to market the *scheme* in the *United Kingdom* in a manner which will involve it carrying on a *regulated activity* in the *United Kingdom*;
  - (f) the name and address of any *person* to whom the property subject to the *scheme* is entrusted for safekeeping;
  - (g) the address of the place in the *United Kingdom* where *scheme* facilities (see *COLL* 9.4) will be maintained;
  - (h) details of the arrangements for the *marketing* of *units* in the *United Kingdom*, namely:
    - (i) the proposed commencement date;
    - (ii) whether the *units* will be sold by or through any

employed sales force, *authorised persons*, or unsolicited calls;

- (i) a copy of the *instrument constituting the scheme*;
- (j) a copy of the *prospectus* or any similar document giving details of the *scheme*;
- (k) a copy of the latest annual report and any subsequent half-yearly report;
- (l) a copy of any other *document* affecting the rights of *participants* in the *scheme*; and
- (m) for notifications under section 270 only, a copy of the authorisation document issued by the authority in the designated territory confirming that the *scheme* is of a class covered by the designation order.

**Additional information required in the prospectus for an application under section 272**

- 9.3.2 R An *operator* of a *scheme* recognised under section 272 of the *Act* must ensure the *prospectus*:
- (1) contains a statement that “Complaints about the operation of the *scheme* may be made to the *FSA*.”; and
  - (2) states whether or not investors in the *scheme* would be covered by the *compensation scheme*, and if so, it must state how they are covered and who they would need to contact for further information.

**Preparation and maintenance of prospectus**

- 9.3.3 R (1) An *operator* of a *scheme* which is a *recognised scheme* by virtue of section 270 or 272 of the *Act* must comply, subject to paragraph (2) below, with the requirements set out in *COLL* 4.2 (Pre-sale notifications).
- (2) Where a *scheme* recognised under section 270 of the *Act* is managed and authorised in Guernsey, Jersey, or the Isle of Man, the *prospectus* need not comply with the requirements of *COLL* 4.2.5R (Table: contents of prospectus), providing it contains corresponding matter required under the law in its

home territory.

## 9.4 Facilities in the United Kingdom

### General

- 9.4.1 R (1) The *operator* of a *recognised scheme* under section 264, section 270 or section 272 of the *Act* must maintain facilities in the *United Kingdom* in order to satisfy the requirements of *COLL 9.4.2R* to *COLL 9.4.6R*.
- (2) In this section, a facility is a place of business that complies with *COLL 9.4.6R* (Place of facilities).

### Documents

- 9.4.2 R (1) The *operator* of a *recognised scheme* must maintain facilities in the *United Kingdom* for any *person*, for inspection (free of charge) and for the obtaining (free of charge, in the case of the *documents* at (c) and (d), and otherwise at no more than a reasonable charge) of copies in English of:
- (a) the *instrument constituting the scheme*;
  - (b) any instrument amending the *instrument constituting the scheme*;
  - (c) the latest *prospectus* (which must include the address where the facilities are maintained and details of those facilities);
  - (d) for a section 264 *recognised scheme*, the simplified prospectus; and
  - (e) the latest annual and half-yearly reports.
- (2) In relation to notices and *documents* sent by *operators* and *depositories* to and from the *United Kingdom*, *COLL 4.4.12R* (Notice to unitholders) and *COLL 4.4.13R* (Other notices) apply.

### Price and redemption

- 9.4.3 R (1) The *operator* must maintain facilities in the *United Kingdom* for any *person* where:
- (a) information in English can be obtained about prices of *units* in the *scheme*; and
  - (b) a *participant* may *redeem* or arrange for *redemption* of



*units* in the *scheme* and obtain payment.

- (2) An *operator* is treated as complying with paragraph (1) if it ensures *participants* may sell their *units* on an investment exchange at a price not significantly different from net asset value; and if so, must inform *participants* of the investment exchange.

#### **Bearer certificates and characteristics of units in the scheme**

- 9.4.4 R (1) The *operator* must maintain facilities in the *United Kingdom* at which the *unitholder* of a *bearer certificate* may obtain free of charge:
- (a) payment of dividends; and
  - (b) details or copies of any notices which have been given or sent to *participants* in the *scheme*.
- (2) The *operator* must state
- (a) the nature of the right represented by the *units* in the *scheme*; and
  - (b) whether *persons* other than *unitholders* can vote at meetings of *unitholders* and, if so, who those *persons* are.

#### **Complaints**

- 9.4.5 R The *operator* must maintain facilities in the *United Kingdom*, at which any *person* who has a complaint to make about the operation of the *scheme* can submit his complaint for transmission to the *operator*.

#### **Place of facilities**

- 9.4.6 R (1) The address of the facilities maintained by the *operator* in accordance with this section and the details of the facilities so maintained must be stated in the *prospectus* of the *scheme*.
- (2) The address of the facilities referred to in (1) must be the address of the *operator's* principal place of business in the *United Kingdom*, or, if there is no such address, the alternative address in paragraph (3).
- (3) The alternative address is such convenient address as the *operator* determines, except that, in the case of a *scheme*

recognised under section 272 of the *Act* where the *operator* is not an *authorised person*, the alternative address is to be the principal place of business in the *United Kingdom* of the *authorised person* who is the representative of the *operator*.

## **10 Fees**

### **10.1 Introduction**

#### **Application**

- 10.1.1 R This chapter applies to:
- (1) every *person* seeking an *authorisation order* for, or recognition of, a *collective investment scheme*;
  - (2) every *manager* of an *authorised unit trust*;
  - (3) every *ACD* of an *ICVC*; and
  - (4) every *person* who, under the constitution or founding arrangements of a *recognised scheme*, is responsible for the management of the property held for or within the *scheme*.

#### **Purpose**

- 10.1.2 G The purpose of this chapter is to set out the requirements for the payment of fees relating to *collective investment schemes*.

#### **Background**

- 10.1.3 G *GEN 3* (FSA Fees – General Provisions) applies to fees required by this chapter and explains how the *FSA* sets fees.
- 10.1.4 G Most of the detail of the fees payable in relation to a *collective investment scheme* is set out in *COLL 10 Annex 1R*. The provisions of the Annex may vary from one financial year to another. Accordingly a fresh *COLL 10 Annex 1R* will come into force, following consultation, for each financial year.
- 10.1.5 G The fees for *collective investment schemes* reflect the estimated costs to the *FSA* of assessing applications and notifications, considering proposals to change *regulated collective investment schemes*, maintaining up to date records about them, and related policy work.
- 10.1.6 G The level of fees payable in respect of an application or notification will vary depending upon the provision of the *Act* under which it is made, as well as the type of *scheme* concerned. This fee is adjusted when the *scheme* concerned is an *umbrella scheme*.

## 10.2 Obligation to pay periodic fees

### General

- 10.2.1 R A *person* identified in COLL 10 Annex 1R as the relevant fee payer for a *regulated collective investment scheme* must pay each periodic fee applicable to it in full and without deduction.
- 10.2.2 G A relevant fee payer will be required to pay a periodic fee for every year during which a *regulated collective investment scheme* has that status. If that *person* is the relevant fee payer for more than one *regulated collective investment scheme*, he will be required to pay a fee in relation to each.

### Due date

- 10.2.3 R The relevant fee payer must pay the amount due on or before 30 April.

### Method of payment

- 10.2.4 R A periodic fee must be paid using one of the payment methods specified in SUP 20.2.7AR.

### Modifications for newly authorised or recognised schemes

- 10.2.5 R If an *authorisation order* is made in relation to a *scheme*, or a *scheme* becomes a *recognised collective investment scheme* during the course of a financial year to which a COLL 10 Annex 1R fee applies:
- (1) the periodic fee required under COLL 10.2 is modified in accordance with the table at COLL 10.2.6R; and
  - (2) the due date for payment is 30 *days* after:
    - (a) the making of the *authorisation order* for the *scheme*; or
    - (b) the *scheme* becomes *recognised*.
- 10.2.6 R Table. Modified fees for newly authorised or recognised schemes  
This table belongs to COLL 10.2.5R

Period in which authorisation or recognition is granted	Proportion of periodic fee payable
1 April to 30 June inclusive	100%
1 July to 30 September inclusive	75%
1 October to 31 December inclusive	50%
1 January to 31 March inclusive	25%

### **10.3 Obligation to pay notification and application fees**

#### **General**

- 10.3.1 R The *person* identified in *COLL 10 Annex 2R* as the relevant fee payer must pay each fee applicable to any application or notification as specified in *COLL 10 Annex 2R*.

#### **Due date**

- 10.3.2 R The relevant fee payer must pay a fee identified in *COLL 10 Annex 2R* on or before the date on which the relevant application or notification is made.
- 10.3.3 G Any application or notification, for which a fee is payable under this section, will be treated as incomplete until that fee is paid.

#### **Method of payment**

- 10.3.4 R A fee identified in *COLL 10 Annex 2R* must be paid by bankers draft, cheque or other payable order.

## Collective Investment Schemes

### COLL 10 Annex 2R

#### Application and notification fees payable

Table.

Legislative provision	Nature and purpose of fee	Payable by	Amount of fee	Umbrella scheme factor (note 1)
Regulation 12 of the <i>OEIC Regulations</i>	On application for an order declaring a <i>scheme</i> to be an <i>ICVC</i> , where the <i>scheme</i> is: - <i>UCITS scheme</i> - <i>non-UCITS retail scheme</i> - <i>qualified investor scheme</i>	An applicant (Note 2)	£1,200 £1,500 £2,400	2
Section 242 of the <i>Act</i>	On application for an order declaring a <i>scheme</i> to be an <i>AUT</i> , where the <i>scheme</i> is: - <i>UCITS scheme</i> - <i>non-UCITS retail scheme</i> - <i>qualified investor scheme</i>	An applicant (Note 2)	£1,200 £1,500 £2,400	2
Section 264 of the <i>Act</i>	On giving notice under section 264 of the <i>Act</i>	The <i>operator</i> (Note 3)	£600	2
Section 270 of the <i>Act</i>	On giving notice under section 270 of the <i>Act</i>	The <i>operator</i> (Note 3)	£600	2
Section 272 of the <i>Act</i>	On application for an order declaring a <i>scheme</i> to be an individually recognised overseas <i>scheme</i> .	An applicant (Note 2)	£14,000	2

Notes:

1. For an *umbrella scheme* the fee is multiplied by the factor shown in final column of the table.

2. The fee must accompany the application.
3. The fee must accompany the notice.

- 1 COLL Sourcebook - Record keeping requirements  
 G  
 1 Record keeping requirements

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
<i>COLL</i> Transitional Provision 3	Election or revocation to comply with <i>CIS</i>	Details	At election or revocation	6 years
<i>COLL</i> 4.4.11R(5)	Minutes of meetings ( <i>AFM</i> )	Full details	As implicit from the rules in <i>COLL</i>	As implicit from the rules in <i>COLL</i>
<i>COLL</i> 6.2.5R(1)	<i>Issues and cancellations of units (AFM)</i>	Full details	As implicit from the rules in <i>COLL</i>	As implicit from the rules in <i>COLL</i>
<i>COLL</i> 6.4.6R(4)	Instruments of Transfer ( <i>person</i> responsible for the register)	Full details	From registration	6 years
<i>COLL</i> 6.6.6R(1)	General record-keeping obligations ( <i>AFM</i> )	Such as to demonstrate compliance with the rules in <i>COLL</i> .	As implicit from the rules in <i>COLL</i>	6 years
<i>COLL</i> 6.6.6R(2)	<i>Units held, acquired or disposed of (AFM)</i>	Daily record of <i>units</i> held, acquired or disposed of by the <i>AFM</i>	As implicit in rules in <i>COLL</i>	6 years
<i>COLL</i> 6.6.6R(3)	Dilution record-keeping obligations ( <i>AFM</i> )	How the <i>AFM</i> calculates and estimates <i>dilution</i> and its policy and method for determining the amount of any <i>dilution levy</i> or <i>dilution adjustment</i>	As implicit from the rules in <i>COLL</i>	6 years



<i>COLL</i> 6.6.12R(3)	General record-keeping obligations ( <i>depository</i> )	Such as to demonstrate compliance with the <i>rules</i> in <i>COLL</i> .	As implicit from the <i>rules</i> in <i>COLL</i>	6 years
<i>COLL</i> 8.3.8R(2)	Minutes of meetings ( <i>AFM</i> )	Full details	As implicit from the <i>rules</i> in <i>COLL</i>	6 years
<i>COLL</i> 8.5.2R(3)(e)	General record keeping obligations ( <i>AFM</i> )	Full details	As implicit from the <i>rules</i> in <i>COLL</i>	As implicit from the <i>rules</i> in <i>COLL</i>
8.5.2R(3)(f)	<i>Units</i> held, acquired or disposed of ( <i>AFM</i> )	Daily record of <i>units</i> held, acquired or disposed of by the <i>AFM</i>	As implicit from the <i>rules</i> in <i>COLL</i>	6 years
<i>COLL</i> 8.5.4R(2)(h)	General record keeping obligation ( <i>depository</i> )	Full details	As implicit from the <i>rules</i> in <i>COLL</i>	As implicit from the <i>rules</i> in <i>COLL</i>
<i>COLL</i> 8.5.10R(4)	<i>Issues</i> and <i>cancellations</i> of <i>units</i> ( <i>AFM</i> )	Full details	As implicit from the <i>rules</i> in <i>COLL</i>	As implicit from the <i>rules</i> in <i>COLL</i>

2 COLL Sourcebook - Notification requirements  
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This schedule sets out the notification requirements detailed in *COLL* in respect only of notifications to be provided to the *FSA*. These notification requirements, it should be noted, are in addition to the notifications which must be made to the *FSA* under section 251 of the *Act* (Alteration of schemes and changes of manager or trustee) and under regulation 21 of the *OEIC Regulations* (The Authority's approval for certain changes in respect of a company).

1 Notification requirements

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
<i>COLL</i> Transitional provision 3	Election or revocation to comply with CIS	Details and the date from which it is to take effect	At election or revocation	Immediate
<i>COLL</i> 3.2.7R(2)	<i>ICVC</i> with only one <i>sub-fund</i>	Action to rectify situation	<i>Umbrella</i> has only one <i>sub-fund</i>	24 months
<i>COLL</i> 3.2.8R(2)	Marketing of <i>UCITS</i> scheme in another <i>EEA State</i>	Details, including <i>EEA state</i> concerned	Intention to market	Immediate
<i>COLL</i> 4.2.3R(1)(b)	<i>Prospectus</i> and any revisions thereto	Copy provided	<i>Marketing scheme</i>	Before marketing begins
<i>COLL</i> 4.5.14R(2)(d)	Annual and half yearly reports	Copy of report	End of annual or <i>half-yearly accounting period</i>	Immediately on publication
<i>COLL</i> 5.2.24R(2)&(3)	Risk management process and any material alteration to it	Methods of estimating risk, types of <i>derivative</i> their underlying risk and any quantitative limits	Intention to use derivatives in the management of a <i>scheme</i> or any subsequent proposed material alteration to the risk management process	Before policy is implemented

<b>Handbook reference</b>	<b>Matter to be notified</b>	<b>Contents of notification</b>	<b>Trigger event</b>	<b>Time allowed</b>
<i>COLL</i> 6.5.3R(5)	Change of <i>ACD</i> , <i>directors</i> or <i>controller</i> of <i>ACD</i> or a corporate <i>director</i>	Details	Occurrence	Immediate
<i>COLL</i> 6.6.7R	Capital of <i>ICVC</i>	Details if capital: (a) falls below minimum or (b) exceeds maximum	Occurrence	Immediate
<i>COLL</i> 6.9.11R	Change to <i>ICVC</i> or to one of its officers	Details	Occurrence	14 days
<i>COLL</i> 7.2.1R(2)&(5)	Suspension or resumption of <i>dealing</i>	Details including reason for suspension	Occurrence	Immediate
<i>COLL</i> 7.3.5R(5)	Winding up a solvent <i>ICVC</i> or terminating a solvent <i>ICVC sub-fund (Directors)</i>	Solvency statement	Winding up a solvent <i>ICVC</i> or <i>ICVC sub-fund</i>	Within 21 days of notice given under regulation 21 of <i>OEIC Regulations</i>
<i>COLL</i> 7.3.7R(9)	Winding up a solvent <i>ICVC</i> or <i>sub-fund</i> of an <i>ICVC (Depositary)</i>	Completion of winding up or termination of a <i>sub-fund</i>	Winding up a solvent <i>ICVC</i> or <i>ICVC sub-fund</i>	As soon as reasonably practical after winding up completed
<i>COLL</i> 7.3.8R(6)	Winding up a solvent <i>ICVC (ACD)</i>	Final accounts	Completion of winding up	Two months
<i>COLL</i> 7.3.8R(6)	Winding up a solvent <i>ICVC sub-fund (ACD)</i>	Termination account and auditor's report	Termination of <i>sub-fund</i>	Two months
<i>COLL</i> 7.4.4R(6)	Winding up of an <i>AUT</i> or an <i>AUT sub-fund (Trustee)</i>	Completion of winding up	Winding up of an <i>AUT</i>	Immediate
<i>COLL</i> 7.4.5R(5)	Winding up an <i>AUT</i> or <i>AUT sub-fund</i>	Annual reports of the <i>manager</i> and <i>trustee</i>	End of final accounting period	Two months
<i>COLL</i> 8.3.2R	<i>Prospectus</i> and revisions	Full documents	Before marketing commences	Immediate

<b>Handbook reference</b>	<b>Matter to be notified</b>	<b>Contents of notification</b>	<b>Trigger event</b>	<b>Time allowed</b>
<i>COLL</i> 8.3.5R(6)	Annual and half yearly reports	Copy of report	End of <i>annual</i> or <i>half yearly accounting period</i>	Immediately on publication
<i>COLL</i> 8.6.3R(3)&(5)	Suspension or resumption of <i>dealing (AFM)</i>	Details including reason for suspension	Occurrence	Immediate
<i>COLL</i> 9.3.1D	Notification of a <i>scheme</i> constituted in a <i>designated territory</i>	Prescribed details	Intention to market <i>scheme</i> in <i>UK</i>	As implicit from <i>rules</i> in <i>COLL</i>
<i>COLL</i> 9.3.1D	Application under S272 of the <i>Act</i>	Details	Intention to market <i>scheme</i> in the <i>UK</i>	Up to 6 months before commencing marketing

3 Fees and other required payments  
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1.	The aim of the <i>guidance</i> in the following table is to give the reader a quick overview of the relevant requirements for paying fees.
2.	It is not a complete statement of those requirements and should not be relied on as if it were.

2

Type of fee	Trigger event	Date/Time for payment	Amount/rate	Handbook reference
Periodic fee	-	On or before 30 April in each year, or 30 days after the <i>scheme</i> is <i>recognised</i> or the <i>scheme's</i> <i>authorisation order</i> is made	See <i>COLL</i> 10 Ann 1R	<i>COLL</i> 10.2
Application/notification fee	See <i>COLL</i> 10 Ann 2R	On or before making the relevant application or notification	See <i>COLL</i> 10 Ann 2R	<i>COLL</i> 10.3
Conversion fee	See <i>COLL</i> Transitional Provision 10	On making the relevant notification	£400 for an individual <i>scheme</i> ; £800 for an <i>umbrella</i>	<i>COLL</i> Transitional Provision 10

4 COLL - Sourcebook – Powers Exercised  
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The following powers and related provisions in or under the *Act* have been exercised by the *FSA* to make the *rules* in *COLL*:

1. Section 138 (General rule-making power)
2. Section 140 (Restriction on managers of authorised unit trust schemes)
3. Section 145 (Financial Promotion rules)
4. Section 156 (General supplementary powers)
5. Section 242 (Applications for authorisation of unit trust schemes)
6. Section 247 (Trust scheme rules)
7. Section 248 (Scheme particulars rules)
8. Section 278 (Rules as to scheme particulars)
9. Section 340 (Appointment)
10. Paragraph 17(1) of Schedule 1 (fees)
11. Regulation 6 (FSA rules) of the *OEIC regulations*

The following powers in the *Act* have been exercised by the *FSA* to give the *guidance* in *COLL*:

12. Section 157(1) (Guidance)

The following powers in the *Act* have been exercised by the *FSA* in *COLL* to specify and direct:

13. Section 270(6)(b)
14. Section 274(2), (4) and (5)

5 COLL Sourcebook - Rights of action for damages

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The table below sets out the rules in *COLL* contravention of which by an authorised person may be actionable under section 150 of the Act (Actions for damages) by a person who suffers loss as a result of the contravention.

If a Yes appears in the column headed For private person, the rule may be actionable by a private person under section 150 unless a Yes appears in the column headed Removed. A Yes in the column headed Removed indicates that the *FSA* has removed the right of action under section 150(2) of the Act. If so, a reference to the rule in which it is removed is also given.

In accordance with The Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001/2256), a private person is:

- (1) any individual, except when acting in the course of carrying on a regulated activity; and
- (2) any person who is not an individual, except when acting in the course of carrying on business of any kind;

but does not include a government, a local authority or an international organisation.

The column headed For other person indicates whether the rule is actionable by a person other than a private person, in accordance with those Regulations. If so, an indication of the type of person by whom the rule is actionable is given.

1 Actions for damages: the New Collective Investment Schemes Sourcebook

Chapter/ Appendix	Section/ Annex	Paragraph	Right of action under section 150			
			For private person?		For other person?	
			Yes	Removed?	No	
All rules in <i>COLL</i>			Yes	No	No	

6 COLL Sourcebook – Rules that can be waived

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1. The rules in *COLL* can be *waived* by the *FSA* under sections 148 or 250 of the *Act* (Modification or waiver of rules) or regulation 7 of the *OEIC Regulations* (Modification or waiver of *FSA* rules), except *COLL* 3.2.8R (UCITS obligations) and *COLL* 6.9.9 (Restrictions of business for UCITS management companies).
2. Although the *FSA* has the formal power of *waiver* under the *Act* in relation to these *rules*, much of *COLL* implements the requirements of the *UCITS Directive* by ensuring that relevant *authorised funds* comply with such requirements. Accordingly, while formal power may exist to waive such *UCITS Directive* derived rules, the *FSA*'s ability to do so is severely constrained.
3. No *rules* in *COLL* 10 (Fees) and *COLL* Transitional Provision 10 can be waived by the *FSA*.



**NEW COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK  
(CONSEQUENTIAL AMENDMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions:
- (1) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) 138 (General rule-making power);
    - (b) 140 (Restriction on managers of authorised unit trust schemes);
    - (c) 156 (General supplementary powers);
    - (d) 157 (Guidance);
    - (e) 242 (Applications for authorisation of unit trust schemes);
    - (f) 247 (Trust scheme rules); and
    - (g) 248 (Scheme particulars rules); and
  - (2) regulations 6 (FSA rules) and 12 (Applications for authorisation) of the Open-Ended Investment Companies Regulations (SI 2001/1228).
- B. The provisions of or under the Act relevant to the rules and listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2004.

**Amendments to the Collective Investment Schemes sourcebook (CIS)**

- D. CIS is amended in accordance with Annex A of this instrument.

**Amendments to other FSA manuals and sourcebooks and the Glossary**

- E. The modules of the FSA Handbook of Rules and Guidance listed in column (1) below are amended in accordance with the relevant annex listed in column 2.

(1)	(2)
SYSC	Annex B
GEN	Annex C
IPRU (INS)	Annex D
IPRU INV)	Annex E
COB	Annex F
ICOB	Annex G
AUTH	Annex H
SUP	Annex I
ENF	Annex J
DEC	Annex K
CRED	Annex L
ELM	Annex M
Glossary	Annex N

### **Citation**

- F. This instrument may be cited as the New Collective Investment Schemes Sourcebook (Consequential Amendments) Instrument 2004.

By order of the Board  
18 March 2004

## Annex A

### Amendment to the CIS Sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

#### Transitional provisions for CIS

(1)	(2) Material to which the transitional provision applies	(3)	(4)  Transitional provision	(5)  Transitional provision: dates in force	(6)  Handbook provision: coming into force
22	<p>...</p> <p><i>CIS</i> 7.6.1R(2), (4) and (5)</p> <p><i>CIS</i> 7.10.4R(1) ,(5) and (6)</p> <p>...</p>	R	<p>(1) Subject to (2), in relation to a <i>UCITS management company</i> which became authorised before 13 February 2004, <i>CIS</i> 7.6.1R(2),(4) and (5) and <i>CIS</i> 7.10.4R(1),(5) and (6) have effect as they applied before 12 February 2004.</p>	<p>From 13 February 2004 to 12 February 2007</p>	<p>13 February 2004</p>

...

#### 1.1 Application

##### Right to elect to comply with COLL

- 1.1.1A R (1) *CIS* does not apply to any relevant party in relation to an *authorised fund* if the *authorised fund manager* of such *fund* with the consent of each of the other relevant parties has elected on behalf of the *fund* to comply with the *rules* in *COLL* instead of *CIS*, provided the *authorised fund manager* notifies the *FSA* in writing of such election and of the date from which such election is to take effect.
- (2) For the purposes of (1) a relevant party in relation to:

- (a) any AUT, is its manager and trustee; and
- (b) any ICVC, is :
  - (i) the ICVC;
  - (ii) its ACD;
  - (iii) any other directors of the ICVC; and
  - (iv) its depositary.

Operators of recognised schemes

1.1.1B R CIS 16 (Application and notification) and CIS 17 (Recognised schemes) do not have any effect in relation to an operator of a recognised scheme or to any person seeking recognition in the United Kingdom for such a scheme after 1 April 2004.

...  
3.5.2 R Table: Contents of the prospectus

...  
3  
(15) In the case of a *UCITS scheme*, information concerning the historical performance of the scheme presented in accordance with COB 3.8.11R (specific non real time financial promotions: past performance).

...  
R 23 ...  
(1A) if the authorised fund manager determined that short form reports are to be prepared for the purposes of CIS 10.5.2R (2A)(2), a statement when the short report will be sent to the unit holders.

...  
4.4.3 R (2) ...  
(d) ~~if it has reasonable grounds, relating to the circumstances of the person concerned,~~ for refusing to *sell units* to ~~him~~ the person concerned; and

...

- 4.8.4 G (4) ~~Where there has been no recent trade in the *security* concerned, or where no reliable price exists, an investment should be valued at a price which, in the *authorised fund manager's* opinion, reflects a fair and reasonable price for that investment. In such cases, the *authorised fund manager* should document the reasons for its decision and should be prepared to justify any assumptions made.~~ Where the *authorised fund manager* has reasonable grounds to believe that:
- (a) no reliable price exists for a security at a *valuation point*; or
  - (b) the most recent price available does not reflect the *authorised fund manager's* best estimate of the value of a *security* at the *valuation point*;
- he should value the *investment* at a price which, in his opinion, reflects a fair and reasonable price for that *investment* (the fair value price).
- (5) The circumstances which may give rise to a fair value price being used include:
- (a) no recent trade in the *security* concerned; or
  - (b) the occurrence of a significant event since the most recent closure of the market where the price of the *security* is taken.
- In (b), a significant event is one that means the most recent price of a *security* or a basket of *securities* is materially different to the price that it is reasonably believed would exist at the *valuation point* had the relevant market been open.
- (6) In determining whether to use such a fair value price, the *authorised fund manager* should include in his consideration:
- (a) the type of *authorised fund* concerned;
  - (b) the *securities* involved;
  - (c) the basis and reliability of the alternative *price* used; and
  - (d) the *authorised fund manager's* policy on the valuation of *scheme property* as disclosed in the *prospectus*.

(7) The authorised fund manager should document the basis of valuation (including any fair value pricing policy) and, where appropriate, the basis of any methodology and ensure that the procedures are applied consistently and fairly.

(8) Where a unit price is determined using properly applied fair value prices in accordance with policies in (7), subsequent information that indicates the price should have been different from that calculated will not normally give rise to an instance of incorrect pricing.

...

Spread: general

...

5.2.13 R (7) The exposure to any one ~~counterparty~~ counterparty in an *OTC derivative* transaction must not exceed 5% in value of the *scheme property*. This limit is raised to 10% where the ~~counterparty~~ counterparty is an *approved bank*.

(8) Not more than 20% in value of the *scheme property* is to consist of *transferable securities* ~~or~~ and money market instruments issued by the same group (as referred to in (2)).

...

(11) ~~In applying the limit in (3),(4),(5),(6),(7) and (10), not more than 35% in value of the *scheme property* is to consist of any combination of two or more of the following:~~

(a) ~~*transferable securities* or money market instruments issued by; or~~

(b) ~~*deposits made with; or*~~

(c) ~~exposures from *derivatives* transactions made with a single body.~~

Spread: government and public securities

5.2.14 R (1) This *rule* (CIS 5.2.14) applies to *government and public securities* ("such securities").

...

Investment in collective investment schemes

- 5.2.15 R A *scheme* may invest in *units* in a *collective investment scheme* provided that no more than 30% of the value of that investing scheme is in *collective investment schemes* which are not *UCITS schemes* and only if the second *scheme* is permitted under (1) - (4):
- (1) it is a *scheme* which:
    - (a) complies with the conditions necessary for it to enjoy the rights conferred by the *UCITS Directive*; or
    - (b) is recognised under the provisions of section 270 of the *Act* (Schemes authorised in designated countries or territories); or
    - (c) is authorised as a *non-UCITS retail scheme* (provided the requirements of article 19(1)(e) of the *UCITS Directive* are met); or
    - (d) is authorised in another *EEA State* (provided the requirements of article 19(1)(e) of the *UCITS Directive* are met);
  - (2) ~~it is a the second *scheme* which ~~complies~~ must comply~~ where relevant with *CIS* 5.2.18R (Investment in other group schemes);
  - (3) ~~it is a the second *scheme* which ~~has~~ must have~~ terms which prohibit more than 10% in value of the *scheme property* consisting of *units* in *collective investment schemes*; and
  - (4) for the purposes of this *rule* (*CIS* 5.2.15R) and (*CIS* 5.2. 13R (Spread: general) each *sub-fund* of an *umbrella scheme* is to be treated as if it were a separate *scheme* but no *sub-fund* of an *umbrella scheme* may invest in another *sub-fund* of that *umbrella scheme*.

Qualifying non-UCITS collective investment schemes

- 5.2.16 G (1) *CIS* 17.3 gives further detail as to the recognition of a *scheme* under section 270 of the *Act*.
- (2) Article 19 of the *UCITS Directive* sets out the general investment limits. So, a *non-UCITS retail scheme*, or its equivalent *EEA scheme* which has the power to invest in gold or immovables would not meet the criteria set in *CIS* 5.2.15R (1) (c) and (d).

...

Investment in warrants and nil and partly paid securities

- 5.2.19 R (1) Where a UCITS scheme invests in a warrant, the exposure created by the exercise of the right conferred by the warrant must not exceed the limits in CIS 5.2.13R (Spread: general) and CIS 5.2.14R (Spread: government and public securities). ~~A warrant ("the proposed warrant") falls within any power of investment only if, on the assumptions that:~~
- ~~(a) there is no change to the scheme property between the acquisition of the proposed warrant and its exercise; and~~
  - ~~(b) the right conferred by the proposed warrant and all other warrants forming part of the scheme property at the time of the acquisition of the proposed warrant will be exercised (whether or not it is intended that they will be);~~
- ~~it is reasonably foreseeable that the right conferred by the proposed warrant could be exercised by the authorised fund without contravening the rules in this chapter.~~
- (2) ...
- (3) ~~A warrant which is an investment falling within article 80 of the Regulated Activities Order (Certificates representing certain securities) and which is akin to an investment falling within article 79 (Instruments giving entitlement to investments) of the Regulated Activities Order may not be included in the scheme property unless it is listed on an eligible securities market.~~

Investment in money market instruments

- 5.2.20 R A UCITS scheme may invest in money market instruments which are normally dealt in on the money market, are liquid and whose value can be accurately determined at any time, provided:

...

- 5.2.22 R (6) Any forward transaction must be with an approved counterparty under CIS 5.2.25R(2) (OTC transactions in derivatives).

...



Risk management: derivatives

- 5.2.26 R (1) An *authorised fund manager* must use a risk management process enabling it to monitor and measure as frequently as appropriate the risk of a *scheme's derivatives and forwards* positions and their contribution to the overall risk profile of the *scheme*.
- (2) The following details of the risk management process must be notified by the *authorised fund manager* to the *FSA* in advance of the use of the process as required by (1) along with advance notification of any material alteration to such details:
- (a) the methods for estimating risks in *derivative and forward* transactions; and
  - (b) the types of ~~derivatives~~ *derivatives and forwards* to be used within the *scheme* together with their underlying risks and any relevant quantitative limits.

- ...
- 5.3.3.. R (5) The ~~global total~~ exposure relating to *derivatives* held in a *UCITS scheme* may not exceed the net value of the *scheme property*.

...

Permitted stock lending

- 5.4.4 R (1) An ICVC, or the depositary at the request of the ICVC, or a the trustee at the request of the manager, may enter into a stock lending arrangement of the kind described in section 263B of the Taxation of Chargeable Gains Act 1992 (without extension by section 263C), but only if:
- (a) all the terms of the agreement under which securities are to be reacquired by the depositary for the account of the ICVC or by the trustee, are in a form which is acceptable to the depositary or to the trustee and are in accordance with good market practice;
  - (b) the ~~counterparty~~ *counterparty* is an authorised person or a person authorised by a Home State regulator; and
  - (c) collateral is obtained to secure the obligation of the ~~counterparty~~ *counterparty* under the terms referred to in (a) and the collateral is:

...

- (2) The ~~counterparty~~ counterparty for the purpose of (1) is the person who is obliged under the agreement referred to in (1)(a) to transfer to the depositary the securities transferred by the depositary under the stock lending arrangement or securities of the same kind.

Stock lending: treatment of collateral

- 5.4.5 G Where a stock lending arrangement is entered into, the scheme property remains unchanged in terms of value: the securities transferred cease to be part of the scheme property, but there is obtained in return an obligation on the part of the ~~counterparty~~ counterparty to transfer back equivalent securities. The depositary will also receive collateral to set against the risk of default in transfer, and that collateral is equally irrelevant to the valuation of the scheme property (because it is transferred against an obligation of equivalent value by way of re-transfer). CIS 5.4.6R accordingly makes provision for the treatment of the collateral in that context.

...

Publication of reports

- 10.5.2 R ...
- (2) (a) The *authorised fund manager* must, subject to (2A) and (3) provide free of charge:
- (i) a copy of each annual report and each half-yearly report to each *holder* (or to the first named of joint *holders*) entered in or entitled to be entered in the *register* at the close of business on the last *day* of the relevant accounting period or *half-yearly accounting period*; and
- (ii) a copy of the report to each *holder* of bearer *units* at his request.
- (b) A report relating to an *umbrella scheme* to be provided under (a)(i) or (ii) need not contain an aggregation of the accounts relating to each *sub-fund*, but such information must be sent, free of charge, to any *holder* who requests it

- (2A) (1) Notwithstanding (2), the *authorised fund manager* may comply with *COLL* 4.5.13R (Provision of short report) instead of (2), provided that any short report prepared by the *authorised fund manager* for this purpose:
- (a) meets the requirements of *COLL* 4.5.3R (1) and (2) (Preparation of long and short reports); and
  - (b) contains the information required by *COLL* 4.5.5R (Contents of a short report).
- (2) In preparing a short report for the purposes of (1), the *authorised fund manager* should construe references to a long report in *COLL* 4.5.5 R(1)(f) and (5) and in *COLL* 4.5.13R (3) as the annual report referred to in *CIS* 10.3.3R (Annual reports) or, as the case may be, the half-yearly report in *CIS* 10.3.4 (Half-yearly reports).

...

Guidance on short report contents

10.5.2A G *COLL* 4.5.6G which provides *guidance* on sufficient and significant information which should be contained in short reports, applies in relation to short reports prepared for the purposes of *CIS* 10.5.2R (2A). References in that *guidance* to a fundamental change should be regarded as a change requiring *unitholder* approval by meeting during the period. Similarly, references to a significant change should be regarded as a change in respect of which prior written notice of the change should be given to *unitholders* by the *authorised fund manager*.

(3) ...

...

15.4.3 R (2) ...

(d) ~~if it has reasonable grounds, relating to the circumstances of the person concerned, for refusing to sell units to him the person concerned;~~ and

...

- 15.8.5 G (4) Circumstances may arise where the chosen method may not provide a reliable basis for valuation. Guidance on such instances is provided at CIS 4.8.4G(4) – (8). ~~This could happen, for example, where there has been no recent trade in the *security* concerned or where no reliable price exists. In such cases, the *manager* should exercise judgement to estimate a reasonable price at which the *security* could be bought or sold in the most appropriate market, and should document the reasons for its decision. Additionally, W~~where the *manager* imputes a ‘spread’ in order to arrive at an estimated *buying* or *selling* price – for example, in circumstances where there are no buy or *sell* orders on the order book, it should be able to justify any assumptions made.

...

Restrictions of business of managers of UCITS schemes for UCITS management companies

- 16.5.1 R ~~A firm which is the *authorised fund manager* of a *UCITS scheme*~~ UCITS management company must not engage in any activity other than:
- (1) acting as ~~*manager*~~ of:
    - (a) *authorised fund manager* of an *authorised fund*; or
    - (b) an *operator* of any other *collective investment scheme* for which the firm is subject to prudential supervision ~~and under which the contributions of the *participants* and the profits or income out of which payments are to be made to them are pooled; or~~
  - (2) acting as the ~~director~~ of an ICVC; or
  - (3) activities for the purposes of or in connection with those in (1) ~~or~~ (2);
  - (2) (2);
  - (3) collective portfolio management, including without limitation:
    - (a) investment management;
    - (b) administration:
      - (i) legal and fund management accounting services;
      - (ii) customer enquiries;
      - (iii) valuation and pricing (including tax returns);
      - (iv) regulatory compliance monitoring;

- (v) maintenance of *unitholder register*;
  - (vi) distribution of income;
  - (vii) *unit issues and redemptions*;
  - (viii) contract settlements (including certificate dispatch);  
and
  - (ix) record keeping; and
  - (c) marketing;
  - (4) *managing investments* where the relevant portfolio includes one or more *ISD instruments*;
  - (5) *advising on investments* where ~~the firm has permission in respect of~~ (4);
    - (a) the *firm* has a *permission* for the activity in (4); and
    - (b) each of the instruments is an *ISD instrument*; and
  - (6) safekeeping and administration of *collective investment scheme units* where the *firm* has a *permission* for the activity in respect of (4).
- 16.5.2 G (1) Examples of the connected activities referred to in *CIS 16.5.1R*~~(3)~~(2) include management of *group plans* *PEPs*, *ISAs* and stakeholder pensions, as....
- (2) The restrictions of business imposed by *CIS 16.5.1R* reflect the position under Article 5 of the *UCITS Directive*. In accordance with recital (7) of the amending *UCITS Management Directive* (2001/107/EC) the activities referred to at *CIS 16.5.1R* (3)(a) to (c) may be performed on behalf of *EEA UCITS management companies*.

...

**CIS Sourcebook**  
**Schedule 2- Notification requirements**

<b>Handbook reference</b>	<b>Matters to be notified</b>	<b>Contents of notification</b>	<b>Trigger event</b>	<b>Time allowed</b>
<u>CIS 1.1.1A</u>	<u>Election to comply with <i>COLL</i></u>	<u>Details and date of occurrence</u>	<u>When election takes effect</u>	<u>Before election takes effect</u>

...

## Annex B

### Amendment to the Senior Management Arrangements, Systems and Controls (SYSC)

In this Annex underlining indicates new text and striking through indicates deleted text.

3.2.8 R (2) In SYSC 3.2.8 R (1) "compliance" means compliance with the rules in:

- (a) ...
- (b) COLL (New Collective Investment Schemes) and CIS  
(~~Collective Investment Schemes~~); and
- ...

## Annex C

### Amendment to the General Provisions (GEN)

In this Annex underlining indicates new text and striking through indicates deleted text.

1.1.1 R (2) For a *UCITS qualifier*, this chapter applies only with respect to the *communication* and *approval of financial promotions* to which *COB 3* (Financial promotion) applies and to the maintenance of facilities to which *COLL 9.4 (Facilities in the United Kingdom)* and *CIS 17.5* (Facilities in the United Kingdom) ~~applies~~ apply.

...

3.1.2 R *GEN 3.2.1 R* and *GEN 3.3.1 R* do not apply in respect of any fee payable under *AUTH 4* (Authorisation fees), *REC 7* (Recognised bodies fees), *SUP 6.3.22 R* (Application fee for variation of permission), ~~*COLL 10 (Fees)*~~ or *CIS 18* (Collective investment schemes fees) on the making of an application or a notification.

...

## **Annex D**

### **Amendment to the Interim Prudential sourcebook for Insurers IPRU(INS)**

In this Annex underlining indicates new text and striking through indicates deleted text.

#### **GUIDANCE NOTE 4.4 LINKED CONTRACTS**

5.7 ~~All~~ Most authorised or recognised unit trusts fall under one or other of the criteria of paragraph 5.5 above.



## Annex E

### Amendment to the Interim Prudential sourcebook for Investment Businesses IPRU(INV)

In this Annex underlining indicates new text and striking through indicates deleted text.

#### APPENDIX 1 (INTERPRETATION)

##### GLOSSARY OF TERMS FOR CHAPTER 5 (FORMER IMRO FIRMS)

*authorised corporate director* means the *director* of an *ICVC* who is the authorised corporate director of the *ICVC* in accordance with COLL 6.5.3R (Appointment of an ACD) or, as the case may be, CIS 7.2.1R (The directors).

...

#### APPENDIX 13 (1)

##### Defined terms for Chapter 13

*authorised corporate director* the *director* of an *ICVC* who is the authorised corporate director of the *ICVC* in accordance with COLL 6.5.~~4G(ICVCs)~~3R (Appointment of an ACD) or, as the case may be, CIS 7.2.1R(The directors).

...

- ...
- (c) (except in COLL and CIS) (in relation to any other *investment*) issuing or creating the *investment* or granting the rights or interests of which it consists.

## Annex F

### Amendments to the Conduct of Business sourcebook (COB)

In this Annex underlining indicates new text and striking through indicates deleted text.

#### 3.11 **Unregulated collective investment schemes and qualified investor schemes**

#### 3.11 **~~Introduction~~ Unregulated collective investment schemes**

##### **Promotion of qualified investor schemes**

3.11.6 R A firm may communicate or approve an invitation or inducement to participate in a qualified investor scheme only if:

(a) the communication falls within COB 3 Ann 5; or

(b) the communication is exempt under the Financial Promotion Order (see COB 3 Ann1).

3.11.7 G COLL 8 provides for a type of authorised fund (qualified investor scheme) which is intended for particular non-retail investors. COB 3.11.6R restricts the promotion of such schemes.

COB 3 Ann 5 Permitted promotion of *unregulated collective investment schemes* and qualified investor schemes.(R)

#### 1 Table

1. This annex forms part of *COB 3.11.2R* and *COB 3.11.6R*.

...

#### 2 Table **Permitted promotion of unregulated collective investment schemes and qualified investor schemes**

Promotion to:	Promotion of an unregulated collective investment scheme <u>or qualified investor scheme</u> which is:
Category 1 person:	
(1) a person who is already a participant in an <i>unregulated collective investment scheme</i> <u>or a qualified investor scheme</u> ;	.....
(2) a person who has been, in the last 30 months, a participant in an <i>unregulated collective investment scheme</i> <u>or a qualified investor scheme</u> .	

## Annex G

### Amendments to the Insurance: Conduct of Business sourcebook (ICOB)

In this Annex underlining indicates new text and striking through indicates deleted text.

#### ICOB 1: Application and purpose

#### Annex 2G

#### Summary of Handbook provisions for insurance intermediaries

...

3 Table

	<b>Module</b>	<b>Application</b>
...		
<b>Specialist sourcebooks</b>		
...		
	Collective Investment Schemes sourcebooks, <u>COLL</u> and <u>CIS</u>	<del>Applies</del> <u>Apply</u> to an <i>insurance intermediary</i> doing (1) or (2) where it is also an <i>operator</i> or a <i>depository</i> of an <i>AUT</i> , <i>ICVC</i> or certain other <i>collective investment schemes</i> .
...		

## Annex H

### Amendments to the Authorisation manual (AUTH)

In this Annex underlining indicates new text and striking through indicates deleted text.

- 2.7.12 G The *regulated activities* carried on in relation to a *collective investment scheme* generally are the *establishing, operating or winding up a collective investment scheme*. Acting as the *depository* and acting as sole director of an *open-ended investment company* are also separate *regulated activities*. In all these cases, the activities are regulated where the schemes themselves are authorised schemes for the purposes of the *UK* product regulation regime under Part XVII of the *Act* (Collective investment schemes) as well as where the schemes are unregulated schemes. The process for applying for authorisation of a *collective investment scheme* is described in COLL 2 (Authorised fund applications) and *CIS 16* (Application and notification).
- ...
- 3.17.1 G An applicant seeking to *establish a collective investment scheme* should consult COLL and *CIS* for detailed requirements and *guidance*. Applicants should note that until 12 February 2007 they may elect to comply with COLL or CIS, although qualified investor schemes have to comply with COLL.
- 3.17.2 G Applicants seeking to establish a *collective investment scheme* or to act as *manager* of a *regulated collective investment scheme* should note the rules in COLL 6.4.9 (Plan registers) and CIS 6.5 (Plan registers), which implements article 6 of the *UCITS Directive* and restrict the activities of a manager of an authorised unit trust which is a *UCITS scheme*.
- 3.17.3 G An applicant which wishes to act as ~~*manager of an authorised unit trust which is a UCITS scheme*~~ a *UCITS management company* should note the restriction on the activities it may engage in (see COLL 6.9.9 R (Restrictions of business of UCITS management companies) and *CIS 16.5 (Restrictions of business of ~~managers of UCITS schemes~~ UCITS management companies)*).
- 3.17.4 G A *firm* which is subject to the rule in COLL 6.9.9R or *CIS 6.5* may, however, carry on 'connected activities' referred to in COLL 6.9.10G and *CIS 6.5*,
- ...
- 3.20.3 G (2) COLLG 2 and *CIS 2.3.4G* gives *guidance* when an operator of a *UCITS* scheme wishes to market its *scheme* in another *EEA State*.
- ...

3.22.3 G The limited *partnership* may be set up to invest the funds of the *partners*, for example, in the way of a venture capital fund. If so, it will usually be a *collective investment scheme*. The partnership will not require authorisation simply for being a *collective investment scheme* as this is not a *regulated activity*. It will also often be the case that the partnership, in investing its assets, will be excluded from the *regulated activity* of dealing in investments as *principal* (see AUTH 2.8.4G (Dealing in investments as principal)). However, it is likely that the general *partner* will require *permission* from the FSA to *establish, operate or wind up a collective investment scheme* (see AUTH 3.17 (Specific obligations: applicants seeking to establish a collective investment scheme or to act as manager of a regulated collective investment scheme) and *COLL and CIS*). If the general *partner* delegates responsibility for operating a limited *partnership* that is a *collective investment scheme* to another *person* on behalf of the *partnership*, that other *person* will require *authorisation* from the *FSA* (whether or not the general *partner* also requires *authorisation*).

5.3.16 G A *UCITS qualifier* should refer to *COLLG* or to the following sections of *COLL and CIS* for requirements for recognised schemes:

- (1) *COLL 9.2.1G and CIS 16.1.8G* for *guidance* on notifications;
- (2) *COLL 9.2.1G and CIS 17.2* for *guidance* on information and documentation requirements; and
- (3) *COLL 9.4 and CIS 17.4* which includes *guidance* on what facilities need to be maintained.

...

## **AUTH 5: Qualifying for authorisation under the Act**

...

2 Table G

(1) Module of Handbook	(2) ...	(3) ...
<u><i>COLL and CIS</i></u>	<u><i>COLL and CIS</i></u> applies if a firm	As column (2)
	(a)	
	(b)	
	(c)	
	(d)	

...

- ...
- 2.1.4 G The only kind of *body corporate* of an open-ended kind that may currently be formed under the law of the *United Kingdom* is one that is authorised by the FSA. A *person* intending to form an open-ended *body corporate* that has its head office in Great Britain should refer to the Open-ended Investment Companies Regulations 2001 (SI 2001/1228). *Bodies corporate* formed under these Regulations are referred to in the *Handbook* as *investment companies with variable capital* (or 'ICVCs'). *COLL 2 (Authorised fund applications)* and *CIS 16 (Application and notification)* contains *rules* and *guidance* on forming such *bodies corporate*. The Northern Ireland Assembly was in September 2002 considering a Bill to enable the establishment of open-ended *bodies corporate* whose head office is in Northern Ireland.
- 2.1.5 G *Open-ended investment companies* constituted in other *EEA States* which are seeking to exercise rights conferred by the *UCITS Directive* should refer to *COLL 9 (Recognised schemes)* and *CIS 17 (Recognised Schemes)* for *guidance* on the requirements of section 264 of the *Act* (Schemes constituted in other *EEA States*).
- ...
- 2.10.4 G (3) *collective investment schemes* that are *recognised schemes* (see *COLL 9 (Recognised schemes)* and *CIS 17 (Recognised schemes)*).

## Annex I

### Amendments to the Supervision manual (SUP)

In this Annex underlining indicates new text and striking through indicates deleted text.

1.2.2 For a *firm* which undertakes business internationally (or is part of a *group* which does), the *FSA* will have regard to the context in which it operates, including the nature and scope of the regulation to which it is subject in jurisdictions other than the *United Kingdom*. For a *firm* with its head office outside the *United Kingdom*, the regulation in the jurisdiction where the head office is located will be particularly relevant. As part of its supervision of such a *firm*, the *FSA* will usually seek to cooperate with relevant *overseas regulators*, including exchanging information on the *firm*. Different arrangements apply for an incoming *EEA firm*, an incoming *Treaty firm* and a *UCITS qualifier*. The arrangements applying for an incoming *EEA firm* and an incoming *Treaty firm* are addressed in *SYSC App1*. For *UCITS qualifiers* see also *COLLG*, and *CIS 2.3*, *CIS 16*, and *CIS 17*.

...  
6.1.2 If appropriate, a *firm* which is the manager of a *collective investment scheme* should also refer to *COLL 7* and *CIS 14* for guidance on the termination of *ICVCs* and *AUTs* and on winding up schemes that are not commercially viable.

...  
8.1.1 (2) *person*, as respects a particular *AUT* or *ICVC*, who wishes to apply for, or consent to, or has been given a modification of or waiver of the *rules* in *COLL* or, as the case may be, *CIS*.

...  
8.2.3 Section 250 of the *Act* and regulation 7 of the *OEIC Regulations* allow the *FSA* to waive the application of certain *rules* in *COLL* and *CIS* to:

...  
8.2.7 Table Rules which can be waived (see SUP 8.2.6G)

Rules	Section of the Act or other Provision under which rules are made	Chapters of the Handbook where such rules appear (Note 1)
... <i>Authorised unit trust scheme rules</i>	Section 247	<u><i>COLL</i></u> and <i>CIS</i>
<i>Authorised unit trust scheme particulars rules</i>	Section 248	<u><i>COLL</i></u> and <i>CIS</i>
<i>Investment company with variable capital rules</i>	Regulation 6 of the <i>OEIC Regulations</i>	<u><i>COLL</i></u> and <i>CIS</i>

- ...
- 8.6.4 G In making *waiver* applications under section 250 of the *Act* or regulation 7 of the *OEIC Regulations*, SUP 8.6.2G(2) should be read in application to *rules* in *COLL* or *CIS* as if the word "commercial" were omitted.
- ...
- 10.7.10 G Compliance in *SYSC* 3.2.8R means compliance with the rules in *COB* and *COLL* or *CIS*. The *FSA* anticipates that some *firms* will include oversight of compliance with *PRIN*, *MAR*, and other requirements and standards, within its compliance function. These other responsibilities would not, however, be brought within the *compliance oversight function* (see also *SUP* 10.4.3G).
- ...
- 13.1.3 G (4) the marketing of a *UCITS* scheme by its operator in another *EEA State* under the *UCITS Directive* (see *COLLG* 2.1.8 and *CIS* 2.3.4G).
- ...
- 14.1.2 G (2) a *UCITS qualifier* that is an *authorised person* under Schedule 5 to the *Act*; a *UCITS qualifier* should, however, refer to *COLL* 9.2.1G and *CIS* for full details of applicable *rules* and *guidance*.
- ...
- 14.6.11 G Section 36 of the *Act* states that a *UCITS qualifier* may ask the *FSA* to give a direction cancelling its *authorisation* under paragraph 1(1) of Schedule 5 to the *Act*. *UCITS qualifiers* should also refer to *COLLG* 3.1.11 and *CIS* 17.4.8G (Revocation of recognition: schemes recognised under section 264 of the *Act*).
- ...
- 15.8.7 G A *UCITS management company* which delegates any of its functions to a third party must, as well as complying with *SUP* 15.8.6R, comply with the requirements in *COLL* 6.6.15R(2), *CIS* 7.6.1R(2) or *CIS* 7.10.4R(1) as appropriate.
- ...
- 16.6.8 R (1) (a) (ii) was not corrected in accordance with the *FSA's guidance* as set out in *COLL* 6.2.12G or *CIS* App as the case may be;
- (b) price *units* in the *AUT* in accordance with *COLL* 6.2 or *CIS* 4 as the case may be for single-priced *AUTs* and *CIS* 15 for dual-priced *AUTs*, where the pricing error was:
- ...
- (2) (a) (ii) was not corrected in accordance with the *FSA's guidance* as set out in *COLL* 6.2.12G or *CIS* App as the case may be;
- (b) price *shares* in the *ICVC* in accordance with the provisions of *COLL* 6.3 or *CIS* 4 for *ICVCs* as the case may be, where the pricing error was:
- ...

**SUP 16 Ann 12G: Reports from trustees of AUTs and depositaries of ICVCs (see SUP 16.6.9G)**



- 1 Table
1. ...
- ...
- (4) A firm should refer to COLL 6, and CIS 4, 7, 15 and Appendix CIS or COLL 6.2.12G(Box management errors guidance) before completing this report.
2. ...
- ...
- (4) A firm should refer to COLL 6 and CIS 4, 7 and Appendix CIS or COLL 6.2.12G before completing this report.

SUP Appendix 1

Prudential categories and sub-categories

- 1.3.1 G Table Prudential categories and sub-categories used in the Interim Prudential sourcebooks and the Supervision manual

<i>Prudential categories</i> (Note 1)	Applicable prudential requirements (Note 2)	Prudential sub sub-categories
... <i>ICVC*</i>	None, but see <u>COLL and CIS</u>	

**Schedule 2**  
**Notification requirements**

...

- 2 Table

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
<i>SUP</i> 16.6.6R	Reporting – compliance reports – trustee of an <i>AUT</i>	... (a)... (i)... (ii) was not corrected in accordance with the <i>FSA's guidance</i> as set out in <u>COLL 6.2.12G and CIS App</u> ; (b) <i>price units</i> in the <i>AUT</i> in accordance with <u>COLL 6 and CIS 4</u> for	...	...

<p><i>SUP</i> 16.6.6R</p>	<p>Reporting – compliance reports – <i>depository</i> of an <i>ICVC</i></p>	<p><i>single-priced AUTs and CIS 15 for dual-priced AUTs, where the pricing error was:</i></p> <p>...</p> <p>(a)...</p> <p>(i)...</p> <p>(ii) was not corrected in accordance with the <i>FSAs guidance</i> as set out in <u><i>COLL 6.2.12G</i></u> and <u><i>CIS App</i></u>;</p> <p>(b) price <i>shares</i> in the <i>ICVC</i> in accordance with <u><i>COLL 6</i></u> and <u><i>CIS 4</i></u> for <i>ICVCs</i>, for where the pricing error was:</p> <p>...</p>		
-------------------------------	---	---	--	--

## Annex J

### Amendments to the Enforcement manual (ENF)

In this Annex underlining indicates new text and striking through indicates deleted text.

- 17.3.2 ...  
G
- (1) the duties imposed by *rules* made under *section 340(3)* of the *Act* (Appointment) contained in *SUP 3* (Auditors) and *SUP 4* (Actuaries) and, in the case of *firms* which are *ICVCs*, contained in *COLL 4* (Investor relations), ~~*COLL 7* (Suspension of dealings and termination of authorised funds)~~, *CIS 10* (Report and accounts) and *CIS 14* (Termination of authorised funds);
- ...  
17.3.3 G Under section 249 of the *Act* (Disqualification of auditor for breach of trust scheme rules) if it appears to the *FSA* that an auditor has failed to comply with the duties imposed on him by *trust scheme rules* it may disqualify him from being the auditor for any *AUT* or *ICVC*. These duties are set out in *COLL 4* (Investor relations), *COLL 7* (Suspension of dealings and termination of authorised funds), *CIS 10* (Report and accounts), and *CIS 14* (Termination of authorised funds).
- ...  
17.4.4 G ...
- (1) the nature and seriousness of any breach of *rules* and the effect of that breach: the *rules* are set out in *SUP 3* (Auditors) and *SUP 4* (Actuaries), and in the case of *firms* which are *ICVCs*, in *COLL 4* (Investor relations), *COLL 7* (Suspension of dealings and termination of authorised funds), *CIS 10* (Report and accounts), and *CIS 14* (Termination of authorised funds). The *FSA* will regard as particularly serious any breach of *rules* which has resulted in, or is likely to result in, loss to *consumers* or has resulted in, or is likely to result in, damage to confidence in the financial markets;
- ...  
17.4.5 G ...
- (1) the effect of the auditor's breach of a duty imposed by *trust scheme rules*: the *FSA* will regard as particularly serious a breach of a duty imposed by *trust scheme rules* (set out in *COLL 4* (Investor relations), *COLL 7* (Suspension of dealings and termination of authorised funds), *CIS 10* (Report and accounts), and *CIS 14* (Termination of authorised funds)) which has resulted in, or is likely to result in, loss to *consumers* or has resulted in, or is likely to result in, damage to the integrity of the financial markets;



## Annex K

### Amendments to the Decision Making manual (DEC)

In this Annex underlining indicates new text and striking through indicates deleted text.

- 1.2.5 Events leading to the giving of a *statutory notice* are covered in *AUTH*, *SUP*,  
 G *ENF* and *COLL* or *CIS*. *DEC 2Ann1G* and *DEC 3Ann1G* list the relevant references.

#### DEC 2: Statutory notice procedure: Warning notice and decision notice procedure

Annex 1

- 1 Table List of warning notices and decision notices under the Act (other than Part VI) and certain other enactments

Section of the Act	Description	Handbook reference	Decision maker
...			
245(1)/(2)	when the <i>FSA</i> is proposing/deciding to refuse an application for an <i>authorisation</i> order declaring a <i>unit trust scheme</i> to be an <i>AUT</i>	<u><i>COLL 2</i></u> and <i>CIS 16</i>	<i>RDC/ executive procedures</i> (Note 2)
252(1)/(4)	when the <i>FSA</i> is proposing/deciding to refuse approval of a proposal to replace the <i>trustee</i> or <i>manager</i> of an <i>AUT</i>	<u><i>COLL 2</i></u> and <i>CIS 16</i>	<i>Executive procedures</i>
...			
264(2)/265(4) (Note 3)	when the <i>FSA</i> is notifying/deciding not to withdraw a notice, to the operator and relevant <i>EEA State</i> authorities, that the way in which a <i>collective investment scheme</i> constituted in another <i>EEA State</i> intends to invite <i>persons</i> in the <i>United Kingdom</i> to participate in the <i>scheme</i> does not comply with <i>UK</i> law	<u><i>COLL 9</i></u> and <i>CIS 16</i>	<i>Executive procedures</i>
...			
271(1)/(3)	when the <i>FSA</i> is proposing/deciding to refuse approval of a collective investment scheme as an authorised scheme under section 270	<u><i>COLL 9</i></u> and <i>CIS 16</i>	<i>Executive procedures</i>
276(1)/(2)	when the <i>FSA</i> is proposing/deciding to refuse an application for an order declaring a <i>collective investment scheme</i> to be an <i>authorised scheme</i> under section 272	<u><i>COLL 9</i></u> and <i>CIS 16</i>	<i>Executive procedures</i>

...			
OEIC Regulations reference	Description	Handbook reference	Decision maker
Regulation 16(1)/(2)	when the <i>FSA</i> is proposing/deciding to refuse an application for an <i>authorisation order</i> in respect of a proposed <i>ICVC</i>	<u><i>COLL 2</i></u> <u>and</u> <i>CIS 16</i>	<i>RDC / executive procedures</i>
Regulation 22(1)/(2)/(4)/(5)	when the <i>FSA</i> is proposing/deciding to refuse approval of (or, having given <i>a warning notice</i> , deciding to approve (Note 4)) a proposal to replace the <i>depository</i> or director of an <i>ICVC</i> , or any other proposal/decision falling within regulation 21	<u><i>COLL 2</i></u> <u>and</u> <i>CIS 16</i>	Executive procedures

## Annex L

### Amendments to the Credit Unions sourcebook (CRED)

In this Annex underlining indicates new text and striking through indicates deleted text.

CRED Appendix 1

Contents of the Handbook

1.1.1 Table

	<b>Sourcebook or manual</b>	<b>Reference code</b>
...		
<b>Specialist sourcebook</b>	Collective investment schemes <u>New Collective Investment Scheme sourcebook</u>	<i>CIS</i> <u><i>COLL</i></u>
...		

## Annex M

### Amendments to the Electronic Money sourcebook (ELM)

In this Annex underlining indicates new text and striking through indicates deleted text.

#### 1.5.2 G Table Application of other parts of the Handbook to ELMIs

Block	Module	Application
...		
Block 5 (Specialist sourcebooks other than <i>ELM</i> )	Credit unions ( <i>CRED</i> ), Professional firms, ( <i>PROF</i> ), Lloyd's ( <i>LLD</i> ), Collective Investment Schemes ( <i>CIS</i> ) or <u><i>COLL</i></u> and Recognised Clearing Houses ( <i>REC</i> )	These sourcebooks do not apply to an <i>ELMI</i> .



## Annex N

### Changes to the Glossary of definitions

In this Annex underlining indicates new text and striking through indicates deleted text.

<i>accounting reference date</i>	(1) (except in <u>COLL and CIS</u> ): ... (2) (in <u>COLL and CIS</u> ): <del>the date stated in the most recently published prospectus as the date on which the annual accounting period of the authorised fund is to end in each year.</del> <u>the date on which the annual accounting period of an authorised fund ends.</u>
<i>accrual interval</i>	(in <u>COLL and CIS</u> ) (in relation to an <u>authorised fund manager's</u> periodic charge) the interval specified in the <del>trust deed</del> <u>instrument constituting the scheme</u> over which the periodic charge accrues. ...
<i>affected person</i>	(in <u>COLL and CIS</u> ) (a) ..... (vi) <u>the auditor of the scheme</u> ; (b)..... (iv) any associate of any <i>person</i> in (b)(i), (ii) or (iii); (v) <u>the auditor of the scheme</u> . ...
<i>annual accounting period</i>	(in <u>CIS</u> ) a period determined in accordance with <u>CIS 9.2.1R</u> (Accounting period); (in <u>COLL</u> ) <u>the 12 month period stipulated in the prospectus which ends on the accounting reference date.</u> ...

<i>appropriate valuer</i>	(in <u>COLL and CIS</u> ) a person who complies with the requirements of <u>COLL 5.6.18R(7) (Investment in property)</u> , <u>COLL 8.4.11R(4) (Investment in property)</u> or, as the case may be, <u>CIS 5A.8.5R(7) (Approved immovables)</u> . ...
<i>approved bank</i>	(except in <u>COLL and CIS</u> ) (in relation to a <i>bank</i> account opened by a firm): (a) ... (b) ... (c) ... (d) ... (in <u>COLL and CIS</u> ) any person falling within (a-c) ...
<i>approved derivative</i>	(in <u>COLL and CIS</u> ) a derivative which is traded or <i>dealt</i> in on an eligible derivatives <i>market</i> . ...
<i>approved mortgage</i>	(in <u>COLL and CIS</u> ) a mortgage:...
<i>approved security</i>	(1) (in <u>COLL and CIS</u> ) ...
<i>authorised corporate director</i>	the director of an ICVC who is the <i>authorised corporate</i> director of the ICVC in accordance with <u>COLL 6.5.3R (Appointment of an ACD)</u> or, as the case may be, <u>CIS 7.2.1R (The directors)</u> . ...
<i>base currency</i>	(1) (in <u>COLL and CIS</u> ) ...
<i>bearer certificate</i>	(in <u>COLL and CIS</u> ) ... ...
<i>cancellation</i>	(in <u>COLL and CIS</u> ) .... ...
<i>capital account</i>	(in <u>COLL and CIS</u> ) ... ...

<i>capital property</i>	(in <u>COLL</u> and CIS) ...
	...
<i>class</i>	(2) (in <u>COLL</u> and CIS)
	...
<i>class meeting</i>	(in <u>COLL</u> and CIS) ...
	...
<i>close out</i>	(in <u>COLL</u> , CIS and COB)
<u>COLL</u>	<u>the New Collective Investment Schemes sourcebook</u>
<i>collateral</i>	(1) (in <u>COLL</u> and CIS)...
	...
<u>COLLG</u>	<u>the Collective Investment Scheme Information Guide</u>
	...
<i>currency class share</i>	CIS 2.4.5R(1) ( <u>Currency class shares: requirements</u> )
	...
<u>currency class unit</u>	<u>(in COLL) a class of unit denominated in a currency that is not the base currency of the authorised fund, or, if permitted, by COLL 3.3.4R(1) (Currency class units: requirements).</u>
	...
<u>dealing day</u>	<del>(in CIS) the period in each business day (or in each other day when the ACD or operator is open for business) during which the ACD or operator keeps its premises or any of them open to the public or otherwise publicly available for business of any kind.</del> <u>(in COLL and CIS) the period in a business day (in accordance with the provisions of the prospectus) during which the ACD or the operator is open for business.</u>
	...
<i>dealing period</i>	(in <u>COLL</u> and CIS) ...
	...

<i>dilution</i>	(in <u>COLL</u> and <u>CIS</u> ) ...
<i>dilution adjustment</i>	an adjustment to the price of a <i>unit</i> determined by the <i>ACD</i> , or the <i>manager</i> of a <i>single-priced AUT</i> , under <u>COLL 6.3.8R (Dilution)</u> or, as the case may be, <u>CIS 4.6.4R (Dilution adjustment)</u> for the purpose of reducing <i>dilution</i> .
	...
<i>director</i>	(1) (except in <u>COLL</u> and <u>CIS</u> ) ...
	...
	(2) (in <u>COLL</u> and <u>CIS</u> ) ....
	...
<i>distribution account</i>	(in <u>COLL</u> and <u>CIS</u> ) the account to which the income property of an authorised fund must be transferred as at the end of each annual accounting period under <u>COLL 6.8.3R (Income allocation and distribution)</u> , <u>COLL 8.5.15R (Income)</u> or, as the case may be, <u>CIS 9.2.3R (Annual allocation of income)</u> .
	...
<i>eligible</i>	(in <u>COLL</u> and <u>CIS</u> ) (in relation to a <i>securities</i> or a <i>derivatives</i> market) a market that satisfies the requirements in <u>COLL 5.2.10R (Eligible markets: requirements)</u> , <u>CIS 5.2.12R</u> or <u>CIS 5A.3.3R (Eligible markets: requirements)</u> in relation to schemes falling under <u>COLL 5</u> , <u>CIS 5</u> or <u>CIS 5A</u> respectively.
	...
<i>eligible institution</i>	(in <u>COLL</u> and <u>CIS</u> ) ...
	...
<i>extraordinary resolution</i>	(in <u>COLL</u> and <u>CIS</u> ) ...
	...
<i>geared scheme</i>	a <i>regulated collective investment scheme</i> where the policies which the <i>operator</i> adopts or proposes to adopt mean that as a result of investment in <i>warrants</i> or <i>derivatives</i> , <u>or through borrowing that is not temporary in nature</u> , movements in prices of <i>units</i> are likely to be amplified significantly.

	...
<i>half-yearly accounting period</i>	(in <u>COLL and CIS</u> ) a period determined in accordance with <i>CIS</i> 9.2.1R(6) (Accounting period) <u>or, as the case may be COLL 6.8.2R(2) (Accounting periods).</u>
	...
<i>income account</i>	(in <u>COLL and CIS</u> ) ...
	...
<i>initial margin</i>	(1) (in <u>COLL and CIS</u> ) ...
	...
<i>initial offer</i>	(in <u>COLL and CIS</u> ) an offer for sale of units in an authorised fund or in a sub-fund (otherwise than in accordance with <i>arrangements</i> of the type described in <u>COLL 5.5.9R(3)(b)(iii) (Guarantees and indemnities)</u> or, as the case may be, <i>CIS</i> 5.15.8R(3)(b)(iii) or (c) (Guarantees and indemnities)), where all or part of the consideration paid for the account of the authorised fund for the units is to be used to acquire the initial scheme property of the authorised fund or the initial scheme property attributable to the sub-fund.
	...
<i>initial price</i>	(in <u>COLL and CIS</u> ) (a) (in relation to a share of an ICVC or a unit in a single-priced AUT) the price to be paid for a <i>unit</i> of any class during the period of the initial offer under <u>COLL 6.2.3R (Initial offers)</u> or, as the case may be, <i>CIS</i> 4.2.4R(1) ( <i>Issue of units: initial offer</i> );
	...
<i>interim accounting period</i>	(in <u>COLL and CIS</u> ) ...
	...
<u>ISD instrument</u>	(in accordance with Schedule B of the Annex to the ISD) <u>any of the following investments:</u> (a) <u>transferable securities;</u> (b) <u>units in collective investment undertakings;</u> (c) <u>money-market instruments;</u>

- (d) financial-futures contracts, including equivalent cash-settled instruments;
- (e) forward interest-rate agreements
- (f) interest-rate, currency and equity swaps; and
- (g) options to acquire or dispose of any instruments falling within (a) to (f), including equivalent cash-settled instruments and options on currency and on interest rates.

...

*large deal*

(in *CIS*) ...;

(in *COLL*) a transaction (or series of transactions) in one dealing period by any person to buy, sell or exchange units in an authorised fund, of any value as set out in the prospectus, for the purposes of:

- (a) an SDRT provision;
- (b) a dilution levy; or
- (c) a dilution adjustment.

...

limited redemption arrangements

the arrangements operated by an authorised fund manager for the redemption of units in an authorised fund where the authorised fund manager holds himself out to redeem units in that scheme less frequently than twice in a calendar month in accordance with COLL 6.2.19R (Limited redemption).

...

*margin*

(in *COLL* and *CIS*) ...

...

*marginised contract*

(in *COLL* and *CIS*) ...

...

*marketing*

(in *COLL* and *CIS*) ...

...

non-UCITS retail scheme

an authorised fund which is neither a UCITS scheme or a qualified investor scheme.

...

<i>plan investor</i>	a person entered in the plan register under <u>COLL 6.4.9R (Plan registers)</u> or, as the case may be, <u>CIS 6.5.4R(7) (Requirement)</u> . ...
<i>plan register</i>	(1) ... (2) (in relation to an AUT) a sub- <i>register</i> to the register, which sub- <i>register</i> records persons who subscribe to a group plan and for whom units in the AUT are held for the purposes of the plan by the plan manager or a nominee (other than any sub- <i>register</i> that has not been established and maintained in accordance with <u>COLL 6.4.4R (Register: general requirements and contents)</u> or, as the case may be, <u>CIS 6.5.4R (Requirement)</u> or for the establishment of which no payments are to be made out of the scheme property). ...
<i>precious metals</i>	<u>(in COLL) gold, silver or platinum.</u> ...
<i>price</i>	(in relation to a unit in an ICVC or a single-priced AUT) the <i>price</i> of the unit calculated in accordance with <u>COLL 6.3 (Valuation and pricing)</u> or, as the case may be, <u>CIS 4 (Single pricing and dealing)</u> . ...
<i>prospectus</i>	(in relation to a collective investment scheme) a document containing information about the scheme and complying with the <i>requirements</i> in <u>COLL 4.2.5R (Table: contents of the prospectus)</u> , <u>COLL 8.3.4R (Table: contents of qualified investor scheme prospectus)</u> ; <u>COLL 9.3.2R (Additional information required in the prospectus for an application under section 272)</u> or, as the case may be, <u>CIS 3 or CIS 17</u> applicable to a <i>prospectus</i> of a scheme of the type concerned. ...

<i>qualified investor scheme</i>	<p><u>an authorised fund whose instrument constituting the scheme contains the statement in COLL 8.2.6R1(2) (Table: contents of the instrument constituting the scheme) that it is a <i>qualified investor scheme</i>.</u></p> <p>...</p>
<i>redemption charge</i>	<p>an amount levied by the operator of a scheme upon the redemption of units, in the case of an authorised fund under:</p> <p>(a) <u>COLL 6.7.7R (Charges on buying and selling units); or</u>  <del>(a)</del> CIS 8.2.7R (Redemption charge: ICVCs); or  <b>(b)</b>  <del>(b)</del> CIS 8.5.2R (Redemption charge: single-priced AUTs); or  <b>(c)</b>  <del>(c)</del> CIS 15.4.10R (Redemption charge).  <b>(d)</b></p> <p>...</p>
<i>register</i>	<p>...</p> <p><u>(in COLL) the register of unitholders kept under Schedule 3 to the OEIC Regulations or COLL 6.4.4R (Register: general requirements and contents) , or COLL 8.5.8R (The register of unitholders: AUTs) as appropriate or, in relation to a <i>collective investment scheme that is not an authorised fund</i>, a record of the holders (other than of <i>bearer certificates</i>) of units in it.</u></p> <p>...</p>
<i>sale</i>	<p>(in <u>COLL and CIS</u>) ...</p> <p>...</p>
<i>scheme of arrangement</i>	<p>(in <u>COLL and CIS</u>) an <i>arrangement</i> relating to an authorised fund ("transferor fund") or to a sub-fund of <del>an umbrella</del> <u>a scheme that is an <i>umbrella</i></u> ("transferor <i>sub-fund</i>") under which:</p> <p>...</p>



<i>standing independent valuer</i>	the person appointed as such under <u>COLL 5.6.20R (Standing independent valuer and valuation)</u> and <u>COLL 8.4.13R(1) (Standing independent valuer and valuation)</u> or, as the case may be, CIS 12.3.1R ( <i>Standing independent valuer</i> ).
	...
<i>transferable security</i>	(in <u>COLL</u> and CIS) an <u>investment</u> within <u>COLL 5.2.7R (Transferable securities)</u> , CIS 5.2.9R ( <i>Transferable securities</i> ) or, as the case may be, CIS 5A.2.9R ( <i>Transferable securities</i> ) in relation to <i>schemes</i> falling under <u>COLL 5</u> , CIS 5 or CIS 5A respectively.
	...
<i>trust deed</i>	(in <u>COLL</u> and CIS) the deed referred to in <u>COLL 3.2.3R (The trust deed for AUTs)</u> or, as the case may be, CIS 2.2.5R ( <i>The trust deed for AUTs</i> ), together with any deed expressed to be supplemental to it, made between the manager and the trustee (or, in the case of a recognised scheme that is a unit trust scheme, the instrument constituting the scheme as amended from time to time).
	...
<i>trust scheme rules</i>	rules in <u>COLL</u> and CIS made by the FSA under section 247(1) of the Act ( <i>Trust scheme rules</i> ) in relation to:
	...
<i>UCITS scheme</i>	<del>an authorised fund which complies with the conditions necessary for it to enjoy the rights conferred by the UCITS Directive.</del> <u>an authorised fund whose instrument constituting the scheme contains the statement in COLL 3.2.6R1(2) (Table: contents of the instrument constituting the scheme) that it is a UCITS scheme; unless:</u> (a) <u>the scheme raises capital without promoting the sale of its units to the public within the EEA or any part of it; or</u>

(b) the scheme's units, under its trust deed or its instrument constituting the scheme, may be sold only to the public in non-EEA States.

...

*umbrella*

(in COLL and CIS) ...

...

*umbrella scheme*

~~(in CIS) an authorised fund that is an umbrella.~~

(in CIS) an authorised fund that is an umbrella except in CIS 2.1 and CIS 5A where such a reference is to a scheme authorised as the type of scheme under CIS 2.1.4R(10) (Types of authorised fund).

...

*unitholder*

(in CIS).....

(in COLL)

(a) (in relation to an ICVC or an AUT as appropriate, and subject to COLL 4.4.4R (Special meaning of unitholder in COLL 4.4)):

(i) ( in relation to a unit which is represented by a bearer certificate) the person who holds that certificate; or

(ii) (in a relation a unit that is not represented by a bearer certificate) the person whose name is entered on the register in relation to that unit; or

(b) (in relation to a unit in a collective investment scheme not within (a)):

(i) the holder of a bearer certificate representing that unit; or

(ii) the person who is entered on the register of the scheme as the holder of that unit.

...

*valuation point*

(in COLL and CIS) a *valuation point* fixed by the authorised fund manager for the purpose of COLL 6.3.4R (Valuation points), COLL 8.5.9R (Valuation, pricing and dealing), CIS 4.8.5R (Regular *valuation points*), CIS 4.8.6R (Additional *valuation points*) or CIS 15.8.3(1) or (2)R (Frequency of valuation).

...

**LISTING RULES (TREASURY SHARES) (AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act (“the Act”):
- (1) section 74 (The official list);
  - (2) section 96 (Obligations of issuers of listed securities); and
  - (3) section 101 (Listing rules: general provisions).

**Commencement**

- B. This instrument comes into force on 1 May 2004.

**Amendments to the Listing Rules**

- C. The Listing Rules are amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Listing Rules (Treasury Shares) (Amendment) Instrument 2004.

By order of the Board  
18 March 2004

## Annex

### Amendments to the Listing Rules

In this Annex underlining indicates new text and striking through indicates deleted text.

12.43 The following items must, unless the UK Listing Authority otherwise agrees, be included in the annual report and accounts:

(n) ...

- (iii) in the case of sales of treasury shares for cash made otherwise than through the market, or in connection with an employees' share scheme, or otherwise than pursuant to an opportunity which (so far as was practicable) was made available to all holders of the company's securities (or to all holders of a relevant class of its securities) on the same terms, particulars of the names of purchasers of such shares sold, or proposed to be sold, by the company during the period under review;

...

...

15.23 The limit on discounts of more than 10% to the middle market price of securities set out in paragraphs 4.8, 4.26 and 4.30(b) will apply where a company is selling treasury shares for cash by way of a placing, open offer or vendor consideration placing. ~~Subject to paragraph 15.24 and 15.25, a company must not sell treasury shares for cash at a discount of more than 10% to the middle market price of those shares at the time of the sale otherwise than pursuant to an opportunity which is made available on the same terms to all holders of the company's shares (or to all holders of the relevant class of its shares).~~

15.24 ~~A company may sell treasury shares for cash otherwise than as contemplated in paragraph 15.23 where the UK Listing Authority is satisfied that the issuer is in severe financial difficulties or that there are other exceptional circumstances. Further the limit on the discount to middle market price in paragraph 15.23 shall not apply to a sale of treasury shares for cash if the sale is either:~~

- (a) ~~to a small number of persons who are specifically approved by shareholders in general meeting and who have been named in the circular for the general meeting; or~~
- (b) ~~pursuant to a general disapplication of section 89 of the Companies Act 1985 approved by shareholders in general meeting. Paragraph deleted – May 2004~~

15.25 ~~The prohibition in paragraph 15.23 will not apply to transfers of treasury shares for cash by a company to an employee share scheme under which participation is offered on similar terms to all or substantially all employees of the issuer and its subsidiaries. Paragraph deleted – May 2004~~

**APPLICATION FEES (UNAUTHORISED MUTUAL SOCIETIES REGISTRATION)  
(2004/2005) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers);
  - (2) section 157(1) (Guidance); and
  - (3) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 April 2004.

**Amendments to the Unauthorised mutuals registration fees rules**

- D. The Unauthorised mutuals registration fees rules are amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Application Fees (Unauthorised Mutual Societies Registration) (2004/2005) Instrument 2004.

By order of the Board  
18 March 2004

## Annex

### Amendments to the Unauthorised mutuals registration fees rules

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

- 3.1R A *person* who submits to the *FSA* a proposal for the registration of a society must pay to the *FSA*, in full and without deduction, the fee specified for the type of application under Annex 1AR ~~for the year in which the fee is paid~~.
- 3.2R A *sponsoring body* wishing a set of rules to become *model rules* for the first time must pay to the *FSA*, in full and without deduction, the application fee specified in Annex 1AR ~~for the year in which the fee is paid~~.
- 3.3R Application fees must be paid by the method specified in Annex 1AR.

Insert new Annex 1AR after Annex 1R:

#### Application fees payable

##### Part 1 – Application fees payable to register a new society other than a credit union

Transaction	Amount payable (£)
Application using <i>model rules</i> without any amendment to the model	40
Application using <i>model rules</i> with between 1 and 6 amendments to the model	120
Application using <i>model rules</i> with between 7 and 10 amendments to the model	350
Application using <i>model rules</i> with 11 or more amendments to the model, or using free draft rules	950

##### Part 2 – Application fees payable by sponsoring bodies

This fee is not payable by sponsoring bodies in respect of the model rules of credit unions

Transaction	Amount payable (£)
Application for a new set of <i>model rules</i>	950

##### Part 3 – Method of payment of application fees

Payment method	Additional amount or discount applicable
Cheque	None

**INSOLVENCY PROVISIONS (COND AND FIT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 June 2004.

**Amendment to Threshold Conditions (COND)**

- C. COND is amended in accordance with Annex A to this instrument.

**Amendment to The Fit and Proper test for Approved Persons (FIT)**

- D. FIT is amended in accordance with Annex B to this instrument.

**Citation**

- E. This instrument may be cited as the Insolvency Provisions (COND and FIT) Instrument 2004.

By order of the Board  
15 April 2004



## Annex A

### Amendments to the Threshold Conditions

In this Annex underlining indicates new text and striking through indicates deleted text:

2.4.4 G (2) Relevant matters may include but are not limited to:

...

- (c) whether there are any implications for the adequacy of the *firm's* resources arising from the history of the *firm*; for example, whether the *firm* has:

...

- (iii) been the subject of a receiving order or ~~administration order~~ been in administration; or
- (iv) had a bankruptcy or winding-up petition served on it, been the subject of a bankruptcy restrictions order (including an interim bankruptcy restrictions order) or offered a bankruptcy restrictions undertaking; or

## Annex B

### Amendments to The Fit and Proper test for Approved Persons

In this Annex underlining indicates new text:

2.3.1 G In determining a *person's* financial soundness, the *FSA* will have regard to any factors including, but not limited to:

...

- (2) whether, in the *United Kingdom* or elsewhere, the *person* has made any arrangements with his creditors, filed for bankruptcy, had a bankruptcy petition served on him, been adjudged bankrupt, been the subject of a bankruptcy restrictions order (including an interim bankruptcy restrictions order), offered a bankruptcy restrictions undertaking, had assets sequestrated, or been involved in proceedings relating to any of these.

**INTERIM PRUDENTIAL SOURCEBOOK FOR FRIENDLY SOCIETIES  
(AMENDMENT OF FORM 12) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 150(2) (Actions for damages); and
  - (3) section 156 (General supplementary powers).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 May 2004 and, insofar as it applies to friendly societies' FSC1 or FSC3 return, only applies in respect of financial years ending on or after 31 December 2004.

**Amendment to the Interim Prudential sourcebook for friendly societies  
(IPRU(FSOC))**

- D. IPRU(FSOC) is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Friendly Societies (Amendment of Form 12) Instrument 2004.

By order of the Board  
15 April 2004

## Annex

### Amendments to the Interim Prudential sourcebook for friendly societies

In this Annex, underlining indicates new text and striking through indicates deleted text.

5.1 ...

- (5) A *friendly society* that submits an FSC1 return in respect of the *financial year* ending on 31 December 2003 must also send to its normal supervisory contact at the *FSA*, by 30 June 2004, Form 60 and associated Forms 11 and 12 as amended by the Interim Prudential Sourcebook for Friendly Societies (Solvency I Directive) Instrument 2003 and the Interim Prudential Sourcebook for Friendly Societies (Amendment of Form 12) Instrument 2004.

...

5.2 ...

- (10) A *friendly society* that submits an FSC3 return in respect of the *financial year* ending on 31 December 2003 must also send to its normal supervisory contact at the *FSA*, by 30 June 2004:
- (a) Forms 11 and 12 as amended by the Interim Prudential Sourcebook for Friendly Societies (Solvency I Directive) Instrument 2003 and the Interim Prudential Sourcebook for Friendly Societies (Amendment of Form 12) Instrument 2004; and
- (b) the amounts at line 12 of amended Form 15 and line 61 of amended Form 13, if these lines contain amounts different from the amounts at the same lines of the un-amended forms.

In Appendix 10 (Prudential reporting forms), FSC 3 – Form 12 is amended as follows:

## FSC 3 – FORM 12

### Returns under the Friendly Societies Prudential Rules

General insurance business: Calculation of required margin of solvency – second method, and statement of required minimum margin

Name of Society

Period ended 31 December

	Reg No	Units £/£000
<input style="width: 80%; height: 30px;" type="text"/>	<input style="width: 80%; height: 30px;" type="text"/>	<input style="width: 80%; height: 30px;" type="text"/>

Name of Fund/Summary

1 Last 12 months of this period

2 Last 12 months of the previous period

Reference period (means the three last preceding financial years) (Note 1)	11				
Claims paid in reference period	21				
Claims outstanding carried forward at the end of the period	23				
Claims outstanding brought forward at the beginning of the period	25				
Sub-total E (21 + 23 – 25)	29				
Sub-total F: Conversion of Sub-total E to annual figure (multiply by 12 and divide by the number of months in the reference period)	31				
Division of Sub-total AF	Other than health insurance	Up to and including sterling equivalent of 35M Euro x 26/100 (note 3)	32		
		Excess (if any) over 35M Euro x 23/100 (note 3)	33		
	Health insurance	Up to and including sterling equivalent of 35M Euro x 26/300 (note 3)	34		
		Excess (if any) over 35M Euro x 23/300 (note 3)	35		
Sub-total FG (32 to 35)	39				
Second result Sub-total FG x Sub-total D Sub-total C (or, if 0.5 is greater, x 0.5)	41				
Higher of first result and brought forward amount (Note 2)	42				
Required margin of solvency (the higher of lines 41 and 42)	43				
Minimum guarantee fund	44				
Required minimum margin (the higher of lines 43 and 44)	49				

#### NOTES

1. If the society has not been in existence long enough to acquire a reference period, this must be stated and lines 11 to 41 ignored.
2. The entry at line 42 must be equal to the entry at line 52 on Form 11.
3. Entries in column 2, lines 32-35 must be the corresponding entries in column 1 of the Form for the previous year, even if the amount of Euro in the description of the line has changed.

**DISTANCE MARKETING DIRECTIVE INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000("the Act"):
- (1)
    - (a) section 118(8) (Market abuse);
    - (b) section 138 (General rule-making power);
    - (c) section 139(1) and (4) (Miscellaneous ancillary matters);
    - (d) section 145 (Financial promotion rules);
    - (e) section 147 (Control of information rules);
    - (f) section 149 (Evidential provisions);
    - (g) section 156 (General supplementary powers);
    - (h) section 157(1) (Guidance);
    - (i) section 247 (Trust scheme rules); and
  - (2)
    - (a) regulation 6(1) of The Open-Ended Investment Companies Regulations 2001 (SI 2001/1228);
    - (b) regulation 3 of the Electronic Commerce Directive (Financial Services and Markets Act 2000) Regulations 2002 (SI 2002/1775); and
    - (c) regulation 2 of the Financial Services and Markets Act 2000 (Fourth Motor Insurance Directive) Regulations 2002 (SI 2002/2706).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments)of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) Annex B (Amendments to the Insurance: Conduct of Business sourcebook) comes into force on 14 January 2005;
  - (2) Annex C (Amendments to the Mortgages: Conduct of Business sourcebook) comes into force on 31 October 2004; and
  - (3) the remainder of this instrument comes into force on 9 October 2004.

**Amendments to the Handbook**

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Conduct of Business sourcebook (COB)	Annex A
Insurance: Conduct of Business sourcebook (ICOB)	Annex B
Mortgages: Conduct of Business sourcebook (MCOB)	Annex C
Market Conduct of Business sourcebook (MAR)	Annex D
Authorisation manual (AUTH)	Annex E
Credit unions sourcebook (CRED)	Annex F

Electronic Commerce Directive sourcebook (ECO)	Annex G
Professional firms sourcebook (PROF)	Annex H
Electronic Money sourcebook (ELM)	Annex I
Glossary of definitions	Annex J

### **Citation**

E. This instrument may be cited as the Distance Marketing Directive Instrument 2004.

By order of the Board  
15 April 2004

## Annex A

### Amendment to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

Transitional provisions

...

COB TR1

(1)	(2) Material to which the transitional provision applies: The COB provisions in Table COB TR 2 with the labels indicated	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1.0	Extra time provisions				
1.1	<i>ETPI</i>	R	Transitional Relief		
			<p>...</p> <p>(2) Paragraph (1) does not apply to the following:</p> <p>...</p> <p>(j) ...</p> <p><u>(k) (from 9 October 2004) any rule in COB inserted or amended by the Distance Marketing Directive Instrument 2004 and, in the case of an amendment, to the extent of such amendment.</u></p>	...	...
	...				

...



After the miscellaneous transitional rules table, insert the following new table:

COB 5

Table: Distance Marketing Directive transitional rules (applicable to all firms)

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1	<i>COB</i>	R	<p>Delayed amendment of COB for non-distance contracts</p> <p>The amendments to <i>COB</i> made by the Distance Marketing Directive Instrument 2004 on 9 October 2004 do not apply in relation to business which does not involve the conclusion of a <i>distance contract</i> with a <i>retail customer</i>, provided that the <i>firm</i> complies with the requirements of <i>COB</i> in force immediately before 9 October 2004, taking account of any amendments which come into force after that date.</p>	From 9 October 2004 for 12 months	Already in force

2	COB 6.2.21R(1)(a) and COB 6.2.24R(1)	R	<p>Exception for provision of key features to EEA customers</p> <p>(1) There is no requirement for <i>key features</i> to be provided for a new <i>life policy</i>, variation to a <i>life policy</i> or in respect of a <i>scheme</i> if, at the time he signs the application, the <i>customer</i>:</p> <p>(a) (in the case of a <i>life policy</i>) is <i>habitually resident</i> in an <i>EEA State</i> other than the <i>United Kingdom</i>; or</p> <p>(b) (in the case of a <i>scheme</i>) is not present in the <i>United Kingdom</i>;</p> <p>provided that the conditions in (2) are satisfied.</p> <p>(2) The conditions referred to in (1) are that:</p> <p>(a) the <i>EEA State</i> in which the <i>private customer</i> is (as applicable) <i>habitually resident</i> or present imposes requirements on the communication of pre-contract information (beyond the minimum required by Community legislation) when doing the <i>designated investment business</i> concerned from an establishment in the <i>United Kingdom</i>; and</p> <p>(b) the <i>firm</i> complies with COB 6.4.25R, in respect of the <i>packaged product</i>, as if references to “<i>accepting deposits</i>” and “<i>deposits</i>” were references to “<i>designated investment business</i>” and “<i>packaged products</i>” respectively.</p>	From 9 October 2004, indefinitely	Already in force
---	---	---	---	-----------------------------------	------------------

3		<p>R</p> <p>Non-investment insurance contracts: compliance with DMD Regulations or ICOB</p> <p>When an <i>insurer effects or carries out a non-investment insurance contract which is a distance contract, then either:</i></p> <p>(1) <i>the Distance Marketing Regulations (other than regulation 2(3)) apply as if the insurer was an unauthorised person; or</i></p> <p>(2) <i>(if the insurer has elected) the rules in ICOB which implement the DMD apply.</i></p> <p>An election under (2) is irrevocable and applies in relation to all such contracts. The <i>insurer</i> must make a record of the election and retain it for 6 years from 14 January 2005.</p> <p>In this transitional provision:</p> <p>“<i>ICOB</i>” means the Insurance: Conduct of Business sourcebook; and</p> <p>“<i>non-investment insurance contract</i>” means a <i>contract of insurance</i> which is a <i>general insurance contract</i> or a <i>pure protection contract</i> but which is not a <i>long-term care insurance contract</i>.</p>	<p>From 9 October 2004 until 14 January 2005</p>	
---	--	--	--	--

...

Chapter 1 (title)      General aApplication and general provisions

...

1.2.1 R      *COB* applies to every *firm*, except that:

- ...
- (4)      *COB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for:

...

- (c) the following provisions of *COB* 4.2 (Terms of business and client agreements with customers); ~~*COB* 4.2.1R to *COB* 4.2.6G, *COB* 4.2.9R to *COB* 4.2.11E and *COB* 4.2.15E(26) *COB* 4.2.12AE and *COB* 4 Ann 2E(25).~~

...

1.2.5 G *Authorised professional firms* should be aware of the following:

- (1) ~~*PROF* 5.2 (Nature of nNon-mainstream regulated activities);~~

...

...

1.3.2 G (2) Most of *COB* applies in relation to *regulated activities*, conducted by *firms*, which fall within the definition of *designated investment business*. In relation to *deposits*, *COB* has limited application, as described in *COB* 1.11 (Application of *COB* in relation to deposits). In relation to pure protection contracts and general insurance contracts, *COB* has only limited application.

Application for private customers, intermediate customers, ~~and~~ market counterparties and retail customers

1.3.3 G ...

- (3) Some rules in *COB* (mainly those relating to *distance contracts*) use the term “*retail customer*” rather than “*customer*”, “*private customer*” or “*intermediate customer*”. A *retail customer* is an individual who is acting for purposes which are outside his trade, business or profession.

...

1.3.5 G *Firms* are reminded that the definition of *inter-professional business* does not include:

...

- (3) ... ;
- (4) concluding a *distance contract* with a *retail customer*.

...

1.4.3 R This sourcebook applies in relation to activities not within *COB* 1.4.2R (UK establishments: general) carried on with or for a *client* in the *United Kingdom*, ~~unless (if the office from which the activity is carried on were a separate person) the activity~~ except in any of the following cases:

- (1) this sourcebook does not apply in relation to an activity carried on from an office outside the *United Kingdom* which, if that office were a separate person, if the activity would fall within the overseas persons

exclusions in article 72 of the *Regulated Activities Order*; or ~~(2)~~ would not be regarded as carried on in the *United Kingdom*; ~~or~~

(2) COB 4.2 (Terms of business and client agreements with customers), COB 5 (Advising and selling) and COB 6 (Product disclosure and the customer's right to cancel or withdraw) do not apply to a firm with respect to an activity exclusively concerning a distance contract with a retail customer, if the following conditions are satisfied:

(a) the firm carries on the activity from an establishment maintained by the firm in an EEA State other than the United Kingdom;

(b) either that EEA State:

(i) has implemented the DMD; or

(ii) has obligations in its domestic law corresponding to those provided for by the DMD;

and, in either case, with the result that the obligations provided for by the DMD (or corresponding obligations) are applied by that State when the firm carries on that activity; and

(c) the firm is a national of an EEA State or a company or firm mentioned in article 48 of the Treaty.

...

1.4.7 R In addition to the situations in *COB 1.4.2R* and *COB 1.4.3R*, *COB 6* (Product disclosure and the customer's right to cancel or withdraw) applies in relation to long term insurance business if the habitual residence of the client is in the United Kingdom, other than except:

(1) *COB 6.3* (Post-sale confirmation: life policies) ~~and~~;

(2) *COB 6.9* (With-profits guides); and

(3) (in relation to the conclusion of a distance contract with a retail customer and if the conditions in *COB 1.4.3R(2)* are satisfied) *COB 6.7* (Cancellation and withdrawal) and any provision of *COB 6* which requires the provision of information prior to the conclusion of the contract.

~~applies in relation to long term insurance business if the habitual residence of the client is in the United Kingdom.~~

General insurance business

1.4.8 R In addition to the situations in *COB 1.4.2R* and *COB 1.4.3R*, *COB 6.8* (Insurance contracts: life and general) applies in relation to general insurance business if the State of the risk is the United Kingdom (except, in relation to

the conclusion of a *distance contract* and if the conditions in *COB 1.4.3R(2)* are satisfied, any provision of *COB 6.8* which requires the provision of information prior to the conclusion of the contract).

...

1.6.2 R Table Provisions of COB applied to sStock lending activity  
This table belongs to COB 1.6.1R

COB	Subject
...	
<u>6.7</u>	<u>Cancellation and withdrawal, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i></u>

...

1.6.4 R Table Provisions of COB applied to cCorporate finance business  
This table belongs to COB 1.6.3R

COB	Subject
...	
<u>6.7</u>	<u>Cancellation and withdrawal, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i></u>
...	

...

1.6.5A G *COB 6.7 (Cancellation and withdrawal) has limited application for corporate finance business. Distance contracts concluded with retail customers in the course of corporate finance business are exempt from COB 6.7 if the price of the financial service is dependent on fluctuations in the financial market outside the firm's control (COB 6.7.17R, row 2, case 15(a)).*

...

The Distance Marketing Directive

1.9.3 G The *Distance Marketing Directive* is also relevant for *electronic commerce activities* and *communications*. The *E-Commerce Directive* applies in relation to any commercial transaction entered into over the Internet; the *Distance Marketing Directive* applies only in relation to contracts for financial services concluded exclusively by any means of *distance communication* such as telephone, fax or mail as well as electronic communications. *COB 1.10 (Application of the Distance Marketing Directive and the Distance Marketing Regulations)* provides *guidance* on the *Distance Marketing Directive*.

After *COB 1.9* insert the following new sections:

1.10 Application of the Distance Marketing Directive and the Distance Marketing Regulations

1.10.1 G This section provides *guidance* on certain expressions used in *COB* that are derived from the *Distance Marketing Directive* and on the application of the *Distance Marketing Regulations*.

Initial service agreement and successive operations

1.10.2 G This sourcebook adopts the concepts of "initial service agreement" and "successive operations" from the *DMD*.

(1) A *firm's* contract with a *customer* may take the form of an initial service agreement under which successive operations or a series of separate operations of the same nature are performed over time. Where this is the case, the *DMD* disclosure and cancellation requirements apply in relation to the initial service agreement only and not to the successive or separate operations. However, if new elements are added to the initial service agreement, the addition of those new elements is treated as a new contract to which the *DMD* disclosure and cancellation requirements apply. In accordance with recital 17 of the *Distance Marketing Directive*, examples are:

- (a) the opening of a bank account, which would be an initial service agreement, and the deposit or withdrawal of funds from that account which would be a successive or series of separate operations under that initial agreement; however, adding a debit card to the account would be the addition of a new element involving a separate contract; and
- (b) concluding an *investment management* agreement would be an initial service agreement, and carrying on discretionary or advisory transactions under that agreement would be a successive or a series of separate operations under it.

Other examples are, in the *FSA's* view:

- (c) opening a brokerage account for the purposes of trading securities, and transactions under that account;
- (d) establishing a facility to enable a *customer* to subscribe to an *ISA* for the present and future tax years, and successive subscriptions under that agreement;
- (e) subscribing to an *investment trust savings scheme*, and successive purchases or sales of *shares* under that scheme; and
- (f) concluding a *life policy*, *pension contract* or *stakeholder pension scheme* that includes a pre-selected option providing for future increases or decreases in regular *premiums* or payments, and subsequent *index-linked* changes to those

premiums or increases or decreases to pension contributions following fluctuations in salary.

- (2) Even if a *firm* has not entered into an initial service agreement with a *retail customer*, but simply performs successive operations or a series of separate operations of the same nature for a *retail customer* over time, the *DMD* disclosure requirements will not apply to the successive or separate operations, provided there has been an operation of the same nature within the past year. But if it has been longer than a year, the next operation will be treated as the first in a new series of operations and the *DMD* disclosure requirements will apply. In accordance with recital 17 of the *Distance Marketing Directive*, an example of “successive operations” is the subscription to *units* of the same *collective investment scheme*.

#### Retail customer

- 1.10.3 G (1) The *Distance Marketing Directive* provides protections for ‘any natural person who, in distance contracts ... is acting for purposes which are outside his trade, business or profession’, for which the *FSA* uses the term ‘*retail customer*’. In practice, private individuals may act in a number of capacities. In the *FSA*’s view *retail customer* does not include an individual acting, for example:
- (a) as trustee of a trust such as a housing or NHS trust; or
  - (b) as member of the governing body of a club or other unincorporated association such as a trade body or a student union; or
  - (c) as a pension trustee (but see *COB* 6.4.19R and *COB* 6.7.8R regarding the information and cancellation rights of such trustees).
- (2) Examples of *retail customers* are:
- (a) personal representatives, including executors, unless they are acting in a professional capacity, for example, a solicitor acting as executor; or
  - (b) private individuals acting in personal or other family circumstances for example, as trustee of a family trust.

1.10.4 not used

#### Use of intermediaries

- 1.10.5 G The mere fact that an intermediary (acting for the supplier or for the *retail customer*) is involved, does not make the sale of a financial product or service a *distance contract*. The same principles apply as in the case of contact between the supplier and a *retail customer*. For example, if the intermediary and *retail customer* are simultaneously physically present at some stage in the



course of the offer, negotiation and conclusion of a contract, the contract will not be a *distance contract*.

#### Distance contracts for intermediation services

- 1.10.6 G Some of the services which some intermediaries provide will themselves fall within the scope of the *DMD*. The *FSA* expects this to apply in only a small minority of cases, for example where the intermediary agrees to provide continuing advisory, broking or portfolio management services for a *retail customer*. The *DMD* is only relevant if:
- (1) there is a contract between the intermediary and the *retail customer* in respect of the intermediary's mediation services; an intermediary may in its *terms of business* make clear that it does not, in providing its mediation services, act contractually on behalf of, or for, its *retail customer* and then proceed on the basis that no contract for its mediation services will arise;
  - (2) the contract is a *distance contract*; and
  - (3) the contract is concluded other than merely as a stage in the provision of another service by the intermediary or another *person* (see *COB 4 Ann 1R(13)* and *COB 6.7.17*, Row 1, case D(a)).

#### Application of parts of the Distance Marketing Regulations

- 1.10.7 G *COB* implements most of the *Distance Marketing Directive* for *distance contracts* concluded by *firms*, the making or performance of which constitutes, or is part of, *designated investment business* or *accepting deposits*. However, certain aspects of the *Distance Marketing Directive* are implemented by provisions of the *Distance Marketing Regulations*, which apply in addition to *COB*, in particular:
- (1) regulation 11 (Automatic cancellation of an attached distance contract) on which there is guidance in *COB 6.7.51A*; and
  - (2) regulation 13 (Payment cards).

#### 1.11 Application of COB in relation to deposits

##### 1.11.1 G Table: Application of rules in COB in relation to deposits

COB	Subject matter	Application for cash deposit ISAs	Application for other deposits
2.5.3R	Exclusion of liability	√ *	√*
2.6	General provisions related to distance contracts	√ *	√ *
3.5.5R to 3.5.7R 3.8.4R to 3.8.5E	Financial promotions	√	√
3.9.6R(1) and 3.9.8R	Direct offer financial promotions	√ *	X

6.1.4R, 6.1.5R, 6.2.2R, 6.4.13R, 6.5.2R(2), 6.5.3R, 6.5.42R	Key features	√ *	X
6.4.27R	Provision of key features or other information in relation to a telephone call	√ *	√ *
6.4.25R	Pre-contract information when entering into a <i>distance contract</i> for <i>accepting deposits</i>	X	√ *
6.7.7R(1) 6.7.7R(3)	Cancellable contracts	X √ *	√ * X
6.7.10R(2), 6.7.10AR, 6.7.11R, 6.7.28R	Cancellation period	√ *	√ *
6.7.51R	Effects of cancellation	√ *	√ *
6.7.42R, 6.7.44R	Exercising the right to cancel	√ *	√ *
6.7.52R	Obligations on cancellation	√ *	√ *
<p>Note:</p> <p>(1) Those <i>rules</i> marked with "X" do not apply; those marked with √ do apply. Those marked * will not apply to a <i>firm</i> which subscribes to the edition of the Guidance for subscribers to the Banking Code [in force on 9 October 2004]. Instead, the <i>firm</i> must comply with certain provisions of the Banking Code Guidance (<i>COB 1.11.2R</i>).</p> <p>(2) This Table lists rules imposing obligations. It does not list all application <i>rules</i>, exemptions, transitional <i>rules</i> or <i>guidance</i>.</p>			

#### Exemption for firms which follow the Banking Code Guidance

- 1.11.2 R (1) The *rules* in *COB 1.11.3R* do not apply in relation to *accepting deposits*, to a *firm* which subscribes to the “Guidance for subscribers” to the Banking Code (the 'Banking Code Guidance') issued by the British Banker’s Association, the Building Societies Association and the Association for Payment Clearing Services [edition in force on 9 October 2004].
- (2) In relation to a *firm* in (1) the provisions of the Banking Code Guidance in *COB 1.11.3R* apply as if they were *rules*.

1.11.3 R Table: This table belongs to *COB 1.11.2R(2)*

(1) COB rules which do not apply	(2) Equivalent provisions of the Banking Code Guidance
<i>COB 2.5</i> (Exclusion of liability)	[references in the Code which correspond to relevant COB rules to be added when settled]
<i>COB 2.6</i> (General provisions related to distance contracts)	
<i>COB 3.9.6R(2)</i> and <i>3.9.8R</i> (Direct offer financial promotions: cash deposit ISAs)	
<i>COB 6.1 to 6.5</i> (Key features)	
<i>COB 6.7</i> (Cancellation and withdrawal)	

...

Chapter 2 ~~General r~~ Rules which apply to all firms conducting designated investment business  
(title)

...

- 2.5.1 R (1) This section (other than *COB 2.5.5R*) applies to a firm that ~~makes any written or oral communication to a *customer* in the course of, or in connection with,~~ its conducts *designated investment business*.
- (2) This section (other than *COB 2.5.3R* and *COB 2.5.4R*) applies to a *firm* which enters into a *distance contract* to accept deposits with a *retail customer*.

Purpose

- 2.5.2 G This section amplifies *Principle 6* (Customers' interests) which requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly. ~~A *firm* may not exclude the duties it owes or the liabilities it has to a *customer* under the *Act* or the *regulatory system*. It may exclude the other duties and liabilities only if it is reasonable for it to do so.~~

Limits on the exclusion of liability: designated investment business

- 2.5.3 R A *firm* must not in any written or oral communication, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability it may have to a *customer* (which for these purposes includes a *retail customer*) under the *regulatory system*.

...

Limits on the exclusion of liability: distance contracts to accept deposits

- 2.5.5 R A firm must not, in any written or oral communication to a retail customer in connection with a distance contract to accept deposits with a retail customer, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability it may have to a retail customer under COB (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)).

After COB 2.5 (Exclusion of liability), insert the following new section:

2.6 General provisions related to distance contracts

Application

- 2.6.1 R This section applies to a *firm* which:

- (1) conducts *designated investment business* with or for a *retail customer* in relation to a *distance contract*; or
- (2) enters into a *distance contract to accept deposits* with a *retail customer* (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)).

Pre-contract information about contractual obligations to be in conformity with contract

- 2.6.2 R A *firm* must ensure that information provided to a *retail customer* before the conclusion of a *distance contract* about his contractual obligations under that contract conforms with the contractual obligations that would be imposed on him under the law applying if the contract were concluded.

Unsolicited services

- 2.6.3 R Subject to COB 2.6.4R, a *firm* must not:

- (1) *advise on, arrange, enter into* or conduct any *designated investment business* in relation to a *distance contract* with a *retail customer* without a prior request on his part, when the supply of such service includes a request for immediate or deferred payment; or
- (2) enforce any obligations against a *retail customer* in the event of unsolicited supplies of such services, the absence of reply not constituting consent.

- 2.6.4 R COB 2.6.3R does not apply for a tacit renewal of a *distance contract*.

Paper copy of contractual terms and conditions

- 2.6.5 R During the course of a *distance contract* with a *firm*, if a *retail customer* requests a paper copy of his contractual terms and conditions, the *firm* must provide it without additional charge and without delay.

Change in means of distance communication

2.6.6 R During the course of a *distance contract*, a *firm* must comply with a *retail customer's* request to change the *means of distance communication* used, unless this is incompatible with the *distance contract* concluded or the service being provided by the *firm*.

...

3.3.1 R This chapter applies to a *firm* only in relation to:

...

(3) ...

subject to *COB 3.3.3R* (Exceptions to territorial scope: rules without territorial limitation) and *COB 3.3.4AR* (Exceptions to territorial scope: distance contracts).

...

Exceptions to territorial scope: rules without territorial limitation

3.3.3 R The following parts of this chapter apply without any territorial limitation, subject to *COB 3.3.4AR*:

...

...

Exceptions to territorial scope: distance contracts

3.3.4A R (1) Notwithstanding *COB 3.3.1R* and *COB 3.3.3R*, this chapter, other than the rules in (3), does not apply to a *firm* when it *communicates a financial promotion*, if the conditions in (2) are satisfied:

(2) The conditions are that:

(a) the *firm* communicates the *financial promotion* from an establishment maintained by the *firm* in an *EEA State* other than the *United Kingdom*, and not from an establishment maintained by the *firm* in the *United Kingdom* or outside the *EEA*;

(b) either that *EEA State*:

(i) has implemented the *DMD*; or

(ii) has obligations in its domestic law corresponding to those provided for by the *DMD*;

(c) the *financial promotion* relates, exclusively, to a *distance contract*, for the conclusion of which the obligations provided for by the *DMD* (or corresponding obligations) are applied by that State; and

(d) the *firm* is a national of an *EEA State* or a company or firm mentioned in article 48 of the *Treaty*.

(3) The *rules* which continue to apply, notwithstanding this *rule*, are:

(a) *COB 3.8.4R* (Non-real time financial promotions: clear, fair and not misleading; comparisons; restriction of information on compensation);

(b) *COB 3.8.22R(1)* and (2) (Real time financial promotions);

(c) *COB 3.9.5R* (Prohibited types of direct offer financial promotion);

(d) *COB 3.10* (Unsolicited real time financial promotions);

(e) *COB 3.11* (Unregulated collective investment schemes and qualified investor schemes); and

(f) *COB 3.13.1R* (Additional requirements for financial promotions for an overseas long-term insurer).

...

3.9.6 R (1) A direct offer financial promotion must be in a *durable medium* and contain sufficient information to enable a *person* to make an informed assessment of the *investment* or service to which it relates.

(2) In particular, a *direct offer financial promotion* must contain:

(a) the information set out in ~~*COB 3.9.7R-App 1*~~ (the information in *COB App 1.1.1R(1)* and (4) must be provided in relation to the *person* offering the *investment* or service and, if different, the *firm communicating* or *approving the financial promotion*);

(b) a prominent statement that, if the *person* has any doubt about the suitability of the agreement which is the subject of the *financial promotion*, he should contact the *firm* which has *communicated* or *approved the financial promotion* for advice (or an independent financial adviser if the *firm* does not offer *advice*);

(c) if the *financial promotion* is *communicated* by a *firm* whose *permission* includes a *requirement* that it must not hold *client money*, the name of the *person* to whom payment (if any) should be made;

(d) details of the basis or amount of any *commission* or *remuneration* which might be payable by the *person* who is offering the *investment* or service to another *person*.

- 3.9.7 R ~~[deleted] Direct offer financial promotions: particular information required~~  
~~This table belongs to COB 3.9.6R(2)~~

Delete the table "Direct offer financial promotions: particular information required".

Contractual terms and conditions for distance contracts

- 3.9.7A R (1) A firm must ensure that a retail customer is provided with all the contractual terms and conditions on which its service will be provided in a durable medium in good time before the retail customer is bound to the firm by a distance contract or offer resulting from a direct offer financial promotion, unless an exemption in (2), (3) or (4) applies:

- (2) Exemption: means of distance communication

This exemption applies if the contract is concluded at the retail customer's request using a means of distance communication which does not enable provision of the contractual terms and conditions in a durable medium in accordance with (1). In that case, the firm must provide the retail customer with the information in a durable medium immediately after conclusion of the distance contract.

- (3) Exemption: successive or separate operations under an initial service agreement

This exemption applies if the firm has an initial service agreement with the retail customer and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see COB 1.10.2G(1)).

- (4) Exemption: other successive or separate operations

This exemption applies if:

- (a) the firm has no initial service agreement with the retail customer;
- (b) the firm has performed an operation with the retail customer within the last year; and
- (c) the contract is in relation to a successive operation or separate operation of the same nature (see COB 1.10.2G(2)).

Cash deposit ISAs

3.9.8 R ~~(1) A direct offer financial promotion relating to a cash deposit ISA must contain the information required by COB 6.5.42R (1) to (8) (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)).~~

~~(2) Paragraph (1) does not apply to a bank or building society which subscribes to, and includes in the direct offer financial promotion the information relating to a cash deposit ISA that is suggested in the January 2001 edition of the Banking Code the "Guidance for subscribers" to the Banking Code issued by the British Bankers' Association, the Building Societies Association and the Association for Payment Clearing Services.~~

...

3.9.10 R A direct offer financial promotion relating to a packaged product must contain the information required by COB 6.5.2R(1), (3) and (5) as applicable (Contents of key features).

...

Cancellation rights EIS or non-packaged product, ISA or PEP with no right of withdrawal

3.9.21 R ~~(1) A direct offer financial promotion which relates to an investment which is subject to cancellation or withdrawal rights must describe those rights and explain:~~

~~(a) The length of the cancellation or withdrawal period, and when it will begin;~~

~~(b) Whether cancellation or withdrawal is a legal right or voluntarily conferred;~~

~~(c) (if it is the case) that there might be a shortfall, or, if applicable, a significant shortfall, on cancellation.~~

~~(2) A direct offer financial promotion which relates to an EIS or non-packaged product, ISA or PEP for which no right to withdraw is given under case 8 of column row 2, COB 6.7.17R, must include the statement required by that provision.~~

~~3.9.22 G [deleted]The description 'significant shortfall' is appropriate for higher volatility funds where a large proportion of the investment may be lost during the cancellation period.~~

...

4.2.1 R This section applies to a firm intending to conduct or conducting designated investment business with or for a specific customer, unless the designated business relates to the type of transaction or firm in



column A of COB 4.2.9R and is limited to the type of business specified in the same row in column B. \_

#### Meaning of 'private customer'

- 4.2.2 ~~G~~  
R In this section, COB 4.2, references to a 'private customer' include, in relation to the conclusion of a distance contract, a retail customer, and references to 'customer' are to be interpreted accordingly.  
~~This section does not apply to transactions relating to a cash deposit ISA held on deposit with a deposit-taking firm, since it is not a designated investment.~~

#### Authorised professional firms

- 4.2.3 G If an authorised professional firm conducts a non-mainstream regulated activity for a customer (whether with or without any other regulated activity for the customer) then, subject to COB 4.2.8G, the effect of COB 1.2.1R(4) and PROF 5.4 is that:

- (1) terms of business must be provided in accordance with COB 4.2.5R; but
- (2) with respect to the non-mainstream regulated activity the terms of business should satisfy COB 4.2 as to content if it contains ~~the effect of~~ the disclosure in ~~COB 4.2.15E(26)~~ COB 4 Ann 2E(25); and
- (3) the Distance Marketing Regulations may apply and require the provision of pre-contractual information in certain circumstances.

#### Purpose

- 4.2.4 G COB 4.2 amplifies Principle 6 (Customers' interests) and Principle 7 (Communications with clients). These requires a firm to pay due regard to the interests of its customers and to their information needs, of its customers, to treat them fairly and to communicate information to them which is clear, fair and not misleading. A customer needs to know on what basis a firm intends to do business with him. Terms of business or a client agreement set this out. the basis on which a firm conducts any designated investment business with or for the customer.

#### Requirement to provide terms of business to a customer

- 4.2.5 R (4) Unless any of the exemptions in COB 4 Ann 1R applies, a customer A firm must, in good time before designated investment business is conducted, provide a customer be provided with its a firm's terms of business, setting out the basis on which the designated investment business is to be conducted with or for the customer within the period specified in (2) or

(3).

- (2) ~~A firm must, before conducting any designated investment business with or for a specific private customer, provide him with its terms of business, unless the customer has made an oral offer to enter into an investment agreement relating to an ISA, or a stakeholder pension scheme, that relates to a designated investment, in which case the terms of business must be provided to him within five business days of the offer.~~
- (3) ~~If the customer is an intermediate customer, the firm must provide its terms of business within a reasonable period of the firm beginning to conduct designated investment business with or for the customer.~~

4.2.6 G ~~[deleted]-COB 4.2.5R(2) does not require a firm to provide information that, by its nature, is unavailable at the time the terms of business are issued. For example, a firm will not necessarily know a private customer's investment objectives before providing terms of business, since it may not be possible to determine the private customer's requirements without undertaking know your customer checks, as required by COB 5.2. In these circumstances, the firm should notify the private customer of any relevant information set out in COB 4.2.15E and COB 4.2.16E as soon as practicable after it becomes available.~~

- 4.2.6 G (1) Terms of business will be provided in 'good time' for the purposes of COB 4.2.5R if provided in sufficient time to enable the customer to consider properly the service or investment on offer before he is bound.
- (2) COB 4.2.5R does not require the same information to be provided again if the customer already has it (for example through a direct offer financial promotion).

...

4.2.9 R ~~[deleted]-Designated investment business to which the terms of business and client agreement requirements in this section do not apply.  
This table belongs to COB 4.2.1R~~

Delete the table "Designated investment business to which the terms of business and client agreement requirements in this section do not apply".

Contents of terms of business Adequate detail

4.2.10 R A firm must ensure that its terms of business (including a client agreement with a customer) provided in accordance with this section, COB 4.2:

- (1) set out in adequate detail the basis on which it will conduct

designated investment business with the customer; and

(2) (in respect of distance contracts with retail customers) include all contractual terms and conditions and the information set out in COB App 1. ~~designated investment business is to be conducted~~

4.2.11 E (1) A firm should, in order to provide adequate detail, include in its *terms of business* provided to a customer:

(a) a provision about each item set out in COB 4 Ann 2E and COB 4 Ann 3E ~~COB 4.2.15E and COB 4.2.16E~~, except those the customer has requested not to be included; and

(b) any further or alternative provisions that the customer has asked for and on his own initiative agreed with the firm;

to the extent that each such provision is relevant in the circumstances and that it is practicable to provide it.

(2) Compliance with (1) may be relied on as tending to establish compliance with COB 4.2.10R (1).

(3) Contravention of (1) may be relied on as tending to establish contravention of COB 4.2.10R (1).

#### Information not available at time of issue of terms of business

4.2.11AR A firm is not required to provide information under COB 4.2.10R that, by its nature, is unavailable at the time the terms of business are issued. In such circumstances, the firm must notify the customer of any relevant information as soon as practicable after it becomes available and, in the case of a distance contract with a retail customer, in good time before the contract is concluded.

4.2.11BG COB 4.2.11AR will apply, for example, where a firm does not know a private customer's investment objectives before providing terms of business, as it cannot determine the private customer's requirements without undertaking know-your-customer checks, as required by COB 5.2.

#### Terms of business provided in more than one document

4.2.12 R A firm's *terms of business* provided to a customer may comprise more than one document, provided that it is clear that collectively they constitute the *terms of business*, and provided the use of several documents does not materially diminish the significance of any information the firm is required to give the customer, or the ease with which this can be understood.

#### Contents of terms of business: non-mainstream regulated activities of an authorised professional firm

- 4.2.12A E (1) An authorised professional firm should include, in its terms of business, the information in COB 4 Ann 2E (25).
- (2) For an authorised professional firm, with respect to its non-mainstream regulated activities and as to the content only of its terms of business:
- (a) compliance with (1) may be relied on as tending to establish compliance with COB 4.2.5R; and
- (b) contravention of (1) may be relied on as tending to establish contravention with COB 4.2.5R.

...

#### Records

4.2.14 R ...

Delete in their entirety the tables at *COB 4.2.15E* and *COB 4.2.16E* which are replaced by the new Annexes *COB 4 Ann 2E* and *COB 4 Ann 3E*.

At the end of *COB 4*, insert the following new Annexes:

1 Table: Circumstances in which the terms of business requirement in COB 4.2.5R does not apply and conditions for using the exemption (R)

This table belongs to COB 4.2.5R

	<b>Exempted type of firm or transaction or event:</b>	<b>Conditions for using the exemption:</b>
(1)	Voice telephony communications	(a) At the beginning of the telephone conversation, the <i>firm</i> must provide the <i>customer</i> with the name of the <i>firm</i> and (if the call is initiated by or on behalf of the <i>firm</i> ) the commercial purpose of the call;  (b) if the <i>customer</i> gives his explicit consent to receiving only limited information about the <i>terms of business</i> , the <i>firm</i> must in good time before the <i>retail customer</i> is bound by a contract or offer on the telephone, provide the <i>customer</i> with the following information:
		(i) the name of the person in contact with the <i>customer</i> and his link with the <i>firm</i> ;
		(ii) a description of the main characteristics of the service;
		(iii) the total price to be paid by the <i>customer</i> to the <i>firm</i> for the services, including all related fees, charges and expenses, and all taxes paid through the <i>firm</i> or, where an exact price cannot be indicated, the basis for the calculation of the price enabling the <i>customer</i> to verify it; and notice of the possibility that other taxes or costs may exist that are not paid through the <i>firm</i> or imposed by it;

		(iv) the existence or absence of a right to cancel under <i>COB 6.7</i> and, where there is such a right, its duration and the conditions for exercising it, including information on the amount which the <i>customer</i> may be required to pay in accordance with <i>COB 6.7.52R(1)(b)</i> , as well as the consequences of not exercising it; and
		(v) that other information is available on request and the nature of that information;
		<p>(c) if the <i>customer</i> does not give his explicit consent to receiving only the limited information in (b), and the parties wish to proceed by telephone, the <i>firm</i> must in good time before the <i>retail customer</i> is bound by a contract or offer on the telephone, provide all of the information required by <i>COB App 1</i> orally to the <i>customer</i>; and</p> <p>(d) in the case of either (b) or (c), the <i>firm</i> must immediately after conclusion of the contract, send the <i>customer</i> a full <i>terms of business</i>.</p> <p>(See also <i>COB 3.8.21G</i> (Real time financial promotions) and <i>COB 3.10</i> (Unsolicited real time financial promotions)).</p>
(2)	The service is being provided exclusively by <i>means of distance communication</i> (other than telephone) which does not enable a <i>terms of business</i> to be provided before a contract is concluded	<p>(a) The service is provided in this way at the <i>customer's</i> request; and</p> <p>(b) the <i>firm</i> must send the <i>terms of business</i> to the <i>customer</i> immediately after conclusion of the contract.</p>

(3)	The <i>firm</i> has an initial service agreement with the <i>customer</i>	The <i>designated investment business</i> to be conducted is a successive operation or separate operation of the same nature to be performed for the <i>customer</i> under that initial agreement (see <i>COB</i> 1.10.2G(1)).
(4)	The <i>firm</i> has no initial service agreement with the <i>customer</i> but the <i>designated investment business</i> to be conducted is a successive operation or separate operation of the same nature for the <i>customer</i> (see <i>COB</i> 1.10.2G(2))	The <i>firm</i> has performed an operation of the same nature for the <i>customer</i> within the last year.
(5)	<i>Life insurer</i>	The <i>firm</i> is <i>effecting</i> a <i>life policy</i> issued or to be issued by it as <i>principal</i> .
(6)	<i>Operator of a collective investment scheme</i>	The <i>firm</i> is: (a) conducting any <i>designated business</i> as part of <i>scheme management activity</i> ; or (b) providing any service to the <i>trustee</i> or <i>depository</i> of the <i>scheme</i> which is not part of the <i>operator's scheme management activity</i> ; or (c) selling or purchasing as <i>principal units</i> in a <i>scheme</i> except a sale or purchase of <i>units</i> in an <i>unregulated collective investment scheme</i> under a <i>distance contract</i> with a <i>retail customer</i> .
(7)	<i>Trustee or depository</i>	The <i>firm</i> is acting as a <i>trustee</i> of a <i>unit trust</i> or <i>depository</i> of an <i>ICVC</i> .

(8)	<i>Operator of investment trust savings scheme</i>	The <i>firm</i> is: (a) bringing about a transaction in the <i>shares</i> of any <i>investment trust</i> that is the subject of the <i>scheme</i> ; or (b) conducting any <i>designated investment business</i> as part of its activities as such (except a <i>distance contract</i> not within (a) with a <i>retail customer</i> ).
(9)	<i>Supplier of a published recommendation</i>	The <i>firm</i> is supplying a <i>published recommendation</i> .
(10)	<i>OPS firms</i> who are <i>trustees</i> of an <i>OPS</i>	The <i>firm</i> is carrying on any <i>designated investment business</i> as part of its <i>OPS activity</i> in relation to an <i>occupational pension scheme</i> of which it is <i>trustee</i> .
(11)	Advising during preparation of <i>terms of business</i>	The <i>advice</i> on <i>investments</i> or information is provided solely for the purpose of preparing <i>terms of business</i> or entering into a <i>client agreement</i> .
(12)	<i>Designated investment business</i> performed after termination of <i>terms of business</i>	The <i>firm</i> is acting for the purposes only of fulfilling any obligations still outstanding under the <i>terms of business</i> .



(13)	<i>Execution-only transactions</i>	<p>The <i>firm</i> is entering into or bringing about any <i>execution-only transaction</i> except:</p> <p>(a) a transaction in a <i>contingent liability investment</i> with or for a <i>private customer</i>; or</p> <p>(b) where the <i>firm</i> is entering into a <i>distance contract</i> with a <i>retail customer</i>, unless the contract:</p> <p>(i) relates solely to <i>dealing as agent, advising</i> or <i>arranging</i> by the <i>firm</i>; and</p> <p>(ii) is concluded merely as a stage in the provision of another service by the <i>firm</i> or another <i>person</i> (see <i>COB 1.10.6G</i>).</p>
(14)	<i>Direct offer financial promotion</i>	<p>The <i>firm</i> is concluding a contract with a <i>customer</i> as a result of a <i>direct offer financial promotion</i> to which <i>COB 3.9</i> (Direct offer financial promotions) applies. (<i>COB 4.2.5R</i> (Requirement to provide terms of business to a customer) may therefore apply for a contract concluded as a result of a <i>direct offer financial promotion</i> communicated to a <i>person</i> outside the <i>United Kingdom</i>.)</p>
(15)	The <i>customer</i> is an <i>intermediate customer</i> and not a <i>retail customer</i>	<p>The <i>firm</i> must provide <i>terms of business</i> within a reasonable period of the <i>firm</i> beginning to conduct business with or for the <i>customer</i>.</p>

## 1 Table Content of terms of business provided to a customer: general requirements

This table belongs to COB 4.2.11E

A <i>firm's terms of business</i> (including a <i>client agreement</i> ) provided to a <i>customer</i> should, where relevant, include some provision about:	
(1)	Commencement of the terms of business When and how the <i>terms of business</i> are to come into force.
(2)	Regulator The <i>firm's</i> statutory status (in accordance with GEN 4 Ann 1R (Statutory Status Disclosure)).
(3)	Investment objectives The <i>customer's</i> investment objectives.
(4)	Restrictions (a) Any restrictions on: (i) the types of <i>designated investment</i> in which the <i>customer</i> wishes to invest; and (ii) the markets on which the <i>customer</i> wishes transactions to be <i>executed</i> ; or (b) that there are no such restrictions.
(5)	Services The services the <i>firm</i> will provide.
(6)	Payments for services Details of any payment for services payable by the <i>customer</i> to the <i>firm</i> , including where appropriate: (a) the basis of calculation; (b) how it is to be paid and collected; and (c) how frequently it is to be paid; whether or not any other payment is receivable by the <i>firm</i> (or to its knowledge by any of its <i>associates</i> ) in connection with any transaction <i>executed</i> by the firm, with or for the customer, in addition to or in lieu of any <i>fees</i> .
(7)	Investment manager If the <i>firm</i> is to act as an <i>investment manager</i> :
	(a) the arrangements for giving instructions to the firm and acknowledging those instructions;
	(b) the initial value of the managed portfolio;
	(c) the initial composition of the managed portfolio; and

	(d)	the period of account for which statements of the portfolio are to be provided in accordance with <i>COB 8.2.4R</i> (Requirement for a periodic statement) (where <i>periodic statements</i> are required).
(8)	Accounting	The arrangements for accounting to the <i>customer</i> for any transaction <i>executed</i> on his behalf.
(9)	Cancellation and withdrawal	<p>(a) In the case of a <i>non-packaged product ISA</i> or <i>PEP</i>, an explanation of any right to withdraw (see <i>COB 6.7</i> (Cancellation and withdrawal)) or, if it is the case, a statement that such rights will not apply.</p> <p>(b) (In the case of <i>ISAs</i>), information about:</p> <p>(i) the options available on cancellation;</p> <p>(ii) how cancellation will operate in circumstances where the account forms part of, for example, a <i>maxi-ISA</i> which contains other components; and</p> <p>(iii) a statement that the effect of cancelling the last component has the effect of cancelling the entire <i>ISA</i> agreement and may also (where it is the case) delay the <i>customer</i> from entering into another <i>ISA</i> agreement until the next tax year.</p>
(10)	Unsolicited real time financial promotion	In the case of a <i>private customer</i> , the circumstances, if any, in which the <i>firm</i> or its <i>representative</i> or <i>employees</i> may <i>communicate</i> an <i>unsolicited real time financial promotion</i> to the <i>private customer</i> .
(11)	Acting as principal	That the <i>firm</i> may act as <i>principal</i> in a transaction with the <i>customer</i> , if this is the case.
(12)	Conflict of interest and material interest	When a <i>material interest</i> or conflict of interest may or does arise, the manner in which the <i>firm</i> will ensure fair treatment of the <i>customer</i> as required by <i>COB 7.1.3R</i> (Fair treatment).
(13)	Broker fund adviser	If the <i>firm</i> acts as a <i>broker fund adviser</i> for a <i>private customer</i> , a statement explaining the nature of the <i>firm's</i> dual role as adviser to the <i>customer</i> and adviser to the <i>life office</i> or <i>operator</i> in question.

(14)	<p>Use of soft commission agreements</p> <p>If the <i>firm</i> is to be authorised under the <i>terms of business</i> to undertake transactions with or through the agency of another <i>person</i> with whom the <i>firm</i> has a <i>soft commission agreement</i>, the prior disclosure required by COB 2.2.16R (Prior disclosure).</p>
(15)	<p><i>Customer's</i> understanding of risk</p> <p>When a <i>firm</i> chooses to fulfil its obligations under COB 5.4.3R (Requirement for risk warnings) in the <i>terms of business</i> in relation to any of the following:</p>
	(a) <i>warrants</i> or <i>derivatives</i> ;
	(b) <i>non-readily realisable investments</i> ;
	(c) <i>penny shares</i> ;
	(d) <i>securities</i> which may be subject to stabilisation;
	(e) <i>stock lending activity</i> ;
	the relevant risk warning.
(16)	<p>Unregulated collective investment scheme</p> <p>That the services to be provided by the <i>firm</i> will or may include <i>advice on investments</i> relating to, or <i>executing</i> transactions in <i>units</i> in <i>unregulated collective investment schemes</i>, if this is the case.</p>
(17)	<p>Underwriting</p> <p>That the <i>firm</i> may enter into transactions for the <i>customer</i>, either generally or subject to specified limitations, when the <i>customer</i> will incur obligations as an underwriter or sub-underwriter, if this is the case.</p>
(18)	<p>Stock lending</p> <p>In the case of a <i>private customer</i>, that the <i>firm</i> may undertake <i>stock lending activity</i> with or for the <i>private customer</i> (if this is the case), specifying the assets to be lent, the type and value of <i>relevant collateral</i> from the borrower and the method and amount of payment due to the <i>private customer</i> in respect of the lending.</p>
(19)	<p>Right to realise a private customer's assets</p> <p>The information required by COB 7.8.3R (Contractual rights to realise a private customer's assets), if applicable.</p>
(20)	<p>Complaints procedure</p> <p>How to complain to the <i>firm</i>, and a statement, if relevant, that the <i>customer</i> may subsequently complain directly to the <i>Financial Ombudsman Service</i>.</p>

(21)	<p>Compensation</p> <p>Whether or not compensation may be available from the <i>compensation scheme</i>, should the <i>firm</i> be unable to meet its liabilities, and information about any other applicable named compensation scheme; and, for each applicable scheme, the extent and level of cover and how further information can be obtained. (See the example in COB 5.5.11G (Investment firms: compensation information)).</p>	
(22)	<p>Termination method</p> <p>How the <i>terms of business</i> may be terminated, including a statement:</p>	
	(a)	<p>That termination will be without prejudice to the completion of transactions already initiated, if this is the case;</p>
	(b)	<p>That the <i>customer</i> may terminate the <i>terms of business</i> by written notice to the <i>firm</i> and when this may take effect;</p>
	(c)	<p>That if the <i>firm</i> has the right to terminate the <i>terms of business</i>, it may do so by notice given to the <i>customer</i>, and specifying the minimum notice period, if any; and</p>
	(d)	<p>of any agreed time after which, or any agreed event on which, the <i>terms of business</i> will terminate.</p>
(23)	<p>Termination consequences</p> <p>The way in which transactions in progress are to be dealt with upon termination.</p>	
(24)	<p>Contracting out of best execution</p> <p>When the obligation to provide best execution can be and is to be waived, a statement:</p>	
	(a)	<p>that the firm does not owe a duty of best execution; or</p>
	(b)	<p>the circumstances in which it does not owe such a duty.</p>
(25)	<p>Authorised professional firms</p> <p>If the <i>firm</i> is an <i>authorised professional firm</i> and may conduct a <i>non-mainstream regulated activity</i> with or for the <i>customer</i> (whether with or without any other <i>regulated activity</i> for the same <i>customer</i>), an explanation, with respect to that activity, of:</p>	
	(a)	<p>how to complain to the <i>firm</i>, where the <i>customer</i> may subsequently complain and the mechanisms that operate in respect of such a subsequent complaint; and</p>
	(b)	<p>what, if any, compensation arrangements are available to the <i>customer</i> if the <i>firm</i> is unable to meet any of its liabilities, or the availability of an explanation describing those arrangements.</p>

- 1 Table Content of terms of business provided to a customer: managing investments on a discretionary basis

This table belongs to COB 4.2.11E.

<b>Managing investments on a discretionary basis</b>	
Additional contents in respect of discretionary management	
In respect of discretionary management, <i>terms of business</i> (including a <i>client agreement</i> ) provided to a <i>customer</i> should, in addition, include some provision about each of:	
(1)	Extent of discretion
(a)	The extent of the discretion to be exercised by the <i>firm</i> , including any restrictions on:
(i)	the value of any one <i>investment</i> ; and
(ii)	the proportion of the portfolio which any one <i>investment</i> or any particular kind of <i>investment</i> may constitute; or
(b)	That there are no such restrictions.
(2)	Periodic statements
(a)	The frequency of any <i>periodic statements</i> , except when a <i>periodic statement</i> is not required by COB 8.2.7R (Promptness, suitable intervals and adequate information); and
(b)	whether those statements will include some measure of performance, and if so, what the basis of that measurement will be.
(3)	Valuation The basis on which assets comprised in the portfolio are to be valued.
(4)	Borrowings That the <i>firm</i> may commit the <i>customer</i> to supplement the funds in the portfolio, including borrowing on his behalf, if this is the case, and, if it may:
(a)	the circumstances in which the <i>firm</i> may do so;
(b)	whether there are any limits on the extent to which the <i>firm</i> may do so and, if so, what those limits are; and
(c)	any circumstances in which such limits may be exceeded.

(5)	Underwriting commitments If it is the case, that the <i>firm</i> may commit the <i>customer</i> to any obligation to underwrite or sub-underwrite any issue or offer for sale of <i>securities</i> , and:
(a)	whether there are any restrictions on the categories of <i>securities</i> which may be underwritten and, if so, what these restrictions are; and
(b)	whether there are any financial limits on the extent of the underwriting and, if so, what these limits are.

...

5.3.18 R The *firm* must provide the letter required by COB 5.3.14R to the *customer*:

- (1) in the case of a *life policy*, *pension contract* or *stakeholder pension scheme* where the *cancellation rules* require notification of the right to cancel, no later than the ~~issue of the post-sale notice of the customer's right to cancel~~ fourteenth day after the contract is concluded; or

...

...

ISD investment firms: compensation information

5.5.9 R An *ISD investment firm* providing or offering to provide a *core investment service* or *custody* must make available to every *client*, who has used or intends to use those services, information on whether or not compensation may be available from the *compensation scheme* or a compensation scheme established in another EEA State in accordance with the Investor Compensation Directive should the *firm* be unable to meet its liabilities, and ~~about any other applicable named compensation scheme; for each applicable scheme, the firm must describe~~ the extent and level of cover and how further information can be obtained.

...

6 Product disclosure and the customer's right to cancel or withdraw

6.1 ~~Packaged p~~Product and ISA disclosure

Application

6.1.1 R COB 6.1 to COB 6.5 apply to a *firm*:

...

(6) ...

- (e) (where an *open market option* is available under the contract terms) a *pension buy-out contract*; or

(7) which enters into a distance contract with a retail customer to accept deposits.

6.1.1A R In COB 6.1 to COB 6.5, references to a *private customer* include, in relation to the conclusion of a *distance contract*, a *retail customer*.

...

6.1.3 G *COB 6.1 to COB 6.5 amplify Principle 7 (Communications with clients), which requires a firm to pay due regard to the information needs of its customers. In the case of packaged products there is a special need to ensure that private customers are supplied with information which will highlight particular packaged product features. This also needs to be achieved in a way which will optimise the private customer's ability to make a comparative analysis of different packaged products. These rules also address a similar information need in relation to cash deposit ISAs and when a firm enters into a distance contract to accept deposits with a retail customer.*

Requirement to produce key features

6.1.4 R ...

~~(3) A firm must produce key features in printed hard copy format and may in addition produce key features in an electronic format, unless the firm intends to conduct the activities in COB 6.1.1R solely through electronic media, in which case there is no requirement for a printed hard copy.~~

...

General Medium for provision of key features

6.2.2 R The key features or information which the rules in COB 6.1, COB 6.2 and COB 6.4 require a firm to provide to a *private customer* must be provided by the firm in a durable medium ~~writing~~.

...

6.2.4 G *Firms are reminded that any key features or other information required by COB 6.4 to COB 6.5 is a form of financial promotion and therefore the financial promotion rules contained in COB 3 apply (subject to the application provisions in COB 3.1 to COB 3.3). The same is true for a document relating to a cash deposit ISA produced by a bank or building society under the Banking Code in place of that required under COB 6.5.42R (see COB 6.4.13R(2)).*

...



6.2.5A G Where this chapter requires *key features* or other information to be given, it does not require the same information to be provided again if the *private customer* already has it.

...

6.2.7 R When a *firm* sells, *personally recommends* or arranges the sale of a *life policy* to a *private customer*, ~~the *firm* must provide the *private customer* must be provided~~ with appropriate *key features* before the *private customer* completes an application for the *policy*, subject to COB 6.2.9R (Sales through intermediaries) and COB 6.4.27R (telephone sales) unless COB 6.2.9R(2) applies.

...

#### Exception for life policies: sales through intermediaries

6.2.9 R (4) ~~COB 6.2.7R does not apply to a *product provider* when its *life policy* is sold on the *personal recommendation* of, or arranged to be sold by, an *independent intermediary* or *marketing group associate* another *person*, provided that other *person*:~~

(1) is a *firm* (or *appointed representative*) operating from an establishment maintained by the *firm* (or *appointed representative*) in the *United Kingdom*; or

(2) is operating from an establishment in an *EEA State* whose law imposes an obligation on the *person* to provide information about the *life policy* in accordance with articles 3 and 5(1) and (2) of the *Distance Marketing Directive*.

(2) ~~COB 6.2.7R does not apply to a *firm* where the *private customer* is to acquire a *life policy* without making a written application, but the *firm* must instead ensure that it gives an adequate oral explanation of the main features of the *policy*, and must give or send the *private customer* appropriate *key features* within five *business days* of the date on which the sale, recommendation or arrangement was made.~~

6.2.10 G ~~[deleted] In most cases, *life policies* will be sold through written applications or proposal forms. COB 6.2.9R(2) in particular allows personal pensions to be effected or varied quickly at the end of the tax year, when speed might be essential and the transaction is effected by telephone. A 'written' application includes an application by electronic means.~~

6.2.11 G ~~[deleted] An adequate oral explanation of the information required by COB 6.2.9R(2) should include the following:~~

- (1) ~~The *policy type*, brand name and issuing *company*;~~
- (2) ~~the *policy aims*, the *private customer's* commitment and the risk factors;~~
- (3) ~~a summary of the reasons for any recommendation;~~
- (4) ~~where it is the case, the fact that *commission* or *remuneration*~~

- ~~will be paid to the adviser or representative; and~~  
(5) ~~that key features will be sent within five business days.~~

-

#### Life policies: pre-completion variations

- 6.2.12 R (1) Where *key features* have already been provided by a *firm* to a *private customer* in accordance with COB 6.2.7R and the terms for the proposed *life policy* are subsequently altered before the *private customer* completes an application form, the *firm* must ensure that the *private customer* is provided with revised *key features*, unless the alteration is one or more of the following:
- (1) (a) the amount of the *premium* is changed;
  - (2) (b) the amount of any *commission* or *remuneration* payable is reduced;
  - (3) (c) a rider benefit is added, removed or amended.
- (2) If (1)(a) to (c) apply, then, subject to COB 6.4.27R (telephone sales), if the contract is to be a *distance contract* with a *retail customer*, the *retail customer* must be provided with details of such changes in a *durable medium* in good time before the contract is concluded.

-

...

- 6.2.14 R Where *key features* have already been provided to a *private customer* by a *firm*, and the terms of the proposed *life policy* are materially altered after the *private customer* completes an application form, the ~~*firm* must ensure that the *private customer* must be~~ is provided with ~~written~~ details of the change in a *durable medium* as soon as practicable and offered revised *key features*.
- 6.2.15 G What constitutes a ~~'material change'~~ 'materially altered' requires consideration of the facts in the circumstances of each case. Changes which lead to an increase in the proposed *premium* of 25 per cent or less can be regarded as not material and can be ignored, so long as the underlying *policy* terms and conditions are the same. Other changes to the terms of the proposed contract, such as an increase in the rate or basis of *commission*, a different charges structure or an extension of the *policy* term should be regarded as material.

#### Variations to existing life policies

- 6.2.16 R When a policyholder applies to vary a *life policy* issued on or after 1 January 1995 (or is recommended to do so) and the variation of the *policy* gives rise to a right to cancel under COB 6.7.7R, ~~a document containing at least~~ the policyholder must be provided with:
- (1) the information required by COB 6.5.15R to COB 6.5.19R, COB 6.5.23R to COB 6.5.25R, COB 6.5.27R to COB 6.5.28R

and *COB* 6.5.38R; and

- (2) in the case of a variation which results in a new *distance contract*, all the contractual terms and conditions and the information in *COB* App 1;

~~must be provided to the policyholder~~ in a *durable medium* by the *firm* personally recommending, arranging or effecting the variation in good time before it is put into effect, unless *COB* 6.2.19R (sales through intermediaries) or *COB* 6.4.27R (telephone sales) applies.

- 6.2.17 G ~~*Key features* were introduced for new *policies* sold from 1 January 1995. *Firms can meet* One way of meeting the requirements of *COB* 6.2.16R is by providing a complete set of new *key features* to the policyholder. If a full *key features* is not provided, then as a minimum the information to be supplied must include the details required by *COB* 6.5.15R to *COB* 6.5.19R (An Example), *COB* 6.5.23R to *COB* 6.5.25R (Tables), *COB* 6.5.19R to *COB* 6.5.28R (Deductions Summary) and *COB* 6.5.38R (Commission/Remuneration). The illustrative figures in the *key features* could relate to just the increase in *premiums* and benefits, or could illustrate a 'before and after' situation.~~
- 6.2.18 R When a policyholder applies to vary a *policy* issued before 1 January 1995 (or is *personally recommended* to do so) and the variation of the *policy* gives rise to a right to cancel under *COB* 6.7.7R, information must be given to the policyholder by the *firm* that is *personally recommending*, arranging or effecting the variation before it is put into effect, unless *COB* 6.2.19R or *COB* 6.4.27R (telephone sales) applies. The *firm* must:
- (1) believe on reasonable grounds that the information given is sufficient to enable the policyholder to understand the consequences of the variation; and
- (2) in the case of a variation which results in a new *distance contract*, in good time before the variation is put into effect, provide all the contractual terms and conditions and the information in *COB* App 1.
- 6.2.19 R (+) ~~*COB* 6.2.16R and *COB* 6.2.18R do not apply to a *product provider* when the variation to its *life policy* is effected on the *personal recommendation* of or arranged by an *independent intermediary* or *marketing group associate* another person, provided that other person:~~
- (1) is a *firm* (or *appointed* representative) operating from an establishment maintained by the *firm* (or *appointed representative*) in the *United Kingdom*; or
- (2) is operating from an establishment in an *EEA State* whose law imposes an obligation on the *person* to

provide information about the variation to the *life policy* in accordance with articles 3 and 5(1) and (2) of the *Distance Marketing Directive*.

- (2) ~~COB 6.2.16R and COB 6.2.18R do not apply to a *firm* where the *private customer* is to vary a *life policy* without making a written application, but the firm must instead ensure that it gives an adequate oral explanation of the variation, and must give or send the *private customer* the information required by whichever of COB 6.2.16R or COB 6.2.18R is applicable within five *business days* of the variation being effected.~~

- 6.2.20 G ~~[deleted] The *guidance* in COB 6.2.10G and COB 6.2.11G is also relevant to top-ups to existing *policies* when speed might be essential and the transaction is effected by telephone.~~

~~Exception from the requirement to provide key features for life policies: non-UK customers~~

- 6.2.21 R (1) ~~There is no requirement for *key features* to be provided for a new *life policy* or a variation to an existing *policy* if, at the time that the *private customer* signs the application, he is *habitually resident*:~~

~~(except for *distance contracts with retail customers*) in an~~

~~(a) *EEA State* other than the *United Kingdom*; or~~

~~1)~~

~~Outside the *EEA* and he is not present in the *United*~~

~~(b) *Kingdom*.~~

~~2)~~

- ~~(2) Paragraph (1)(a) does not apply to a *firm* acting as an *outgoing ECA provider*.~~

~~Schemes~~

- 6.2.22 R ~~When a *firm* sells, *personally recommends* or arranges for the sale of a *scheme* to a *private customer*: (1) the *firm* must, unless COB 6.2.24R (exceptions) or COB 6.2.25R or COB 6.4.27R (telephone sales) applies, provide the *private customer* must be provided with *key features* for the *scheme* before the *private customer* completes an application for the *scheme holding*.~~

- ~~(2) the *firm* may delay the provision of *key features* where a *private customer* is to acquire the *scheme* without making a written application, provided that it gives an adequate oral explanation of the main features of the *scheme holding* to the *private customer* and the *key features* are sent to him within five *business days* of the date on which the sale, recommendation or arrangement was made.~~

- 6.2.23 G (1) ~~COB 6.2.22R applies not just to new purchases but also to any recommendation or application to transfer the value of a~~

particular fund holding within a *scheme* to a different fund within the same *scheme*.

- (2) Where a *private customer* has responded to a *direct offer financial promotion*, the mailing package or *direct offer financial promotion* should have included example-based *key features* – there is no requirement to provide a further set of *key features* to such a *private customer* in respect of the same transaction.
- (3) ~~An adequate oral explanation of the information required by COB 6.2.22R should include the following:~~
  - ~~(a) The name of the *scheme*;~~
  - ~~(b) the *scheme's* aims, the amount to be invested and the risk factors;~~
  - ~~(c) the charges that the *customer* will or may bear and their effect on his *investment*;~~
  - ~~(d) a summary of the reasons for any recommendation;~~
  - ~~(e) Where it is the case, that *commission* or *remuneration* will be paid to the *adviser* or *representative*; and~~
  - ~~(f) That *key features* will be sent within five *business days*.~~

Exceptions from the requirement to provide key features for schemes

6.2.24 R A firm need not provide *key features* to a *private customer* in respect of a *scheme* if:

- (1) ~~It is a *UK firm* and the obligation arises from business carried on in another *EEA State* under an *EEA right* the firm is a *product provider* and the *scheme holding* is sold on the *personal recommendation* of, or arranged to be sold by another *person*, provided that other *person*:~~
  - ~~(a) is a firm (or appointed representative) operating from an establishment maintained by the firm (or appointed representative) in the United Kingdom; or~~
  - ~~(b) is operating from an establishment in an EEA State whose law imposes obligations on the person to provide information about the scheme holding in accordance with articles 3 and 5(1) and (2) of the Distance Marketing Directive; or~~
- (2) at the time the *private customer* signs the application, the *private customer* is *habitually resident* outside the *EEA* and is not present in the *United Kingdom*; or

- (3) (except for distance contracts with retail customers) the *scheme holding* is purchased by a *private customer* on an execution-only basis; or
- (4) the *scheme holding* is purchased on behalf of a *private customer* by an *investment manager* exercising discretion; or
- (5) the sale of the *scheme holding* is arranged or recommended by an *investment manager* who is not exercising discretion and the *private customer* has agreed, either in relation to that specific holding or generally, that *key features* need not be provided; or
- (6) a *private customer* is making a purchase of a *scheme holding* in a fund in which he already has a *scheme holding* and has already been provided with appropriate key features covering the purchase:
  - (a) ~~where the terms and conditions, including all charges, are the same as applied at the time of the previous purchase of a scheme holding in that fund; and~~
  - (b) ~~key features outlining those terms and conditions were issued to the private customer in respect of that previous purchase; or~~
- (7) a *private customer* is transferring from *accumulation units* to *income units* of the same *scheme* (or vice versa) and has already been supplied with *key features* ~~for that scheme, which cover the transfer; or-~~
- (8) the scheme is a UCITS scheme recognised under section 264 of the Act (Schemes constituted in other EEA States); however, if the sale is by way of a distance contract, the firm must provide all the contractual terms and conditions and the information in COB App 1 instead of key features.

- 6.2.24A R ~~[deleted] When a firm sells, personally recommends or arranges for the sale of a UCITS scheme recognised under section 264 of the Act (Schemes constituted in other EEA States), then COB 6.2.22R does not apply.~~
- 6.2.25 R ~~[deleted] COB 6.2.22R does not apply to a product provider when the scheme holding is sold on the personal recommendation of, or arranged to be sold by, an independent intermediary or marketing group associate.~~
- ...
- 6.3.5 R The post-sale confirmation required by COB 6.3.3R must be sent or given to the *private customer* ~~no later than the issue of any post-sale notice under the cancellation rules or, if no such notice is required, as~~

soon as reasonably practicable after the contract is effected.

...

- 6.4.1 R *COB 6.4 applies to a firm in accordance with COB 6.1.1R, in respect of occupational pension schemes, self invested personal pensions, income withdrawals, cash deposit ISAs, traded life policies, and stakeholder pension schemes, packaged products and other deposits.*
- 6.4.2 G *Firms are reminded that, under COB 6.2.2R, the key features required to be provided to a private customer under COB 6.4 must be provided by the firm in a durable medium writing. See also COB 6.2.3G to COB 6.2.5G.*
- ...
- 6.4.7 G *Investments within a self-invested personal pension scheme (a "SIPP") are effected by the trustees on behalf of scheme members. Key features should be given to the trustees and to members of SIPPs when packaged products (whether life policies or schemes) are recommended by a firm to scheme members or effected by SIPP trustees. Notice of the right to cancel Cancellation notices should also be copied to SIPP members in these circumstances, in accordance with COB 6.7.31R.*

#### Income withdrawals

- 6.4.8 R *When a firm personally recommends, arranges or effects income withdrawals to or for a private customer, the firm customer must be provided with key features to the customer in good time before the customer signs any form of application or authority electing to make those withdrawals, whether that election is made with advice on investments or on an execution-only basis, unless COB 6.4.10R to COB 6.4.12R apply.*
- ...

#### Cash deposit ISAs

- 6.4.13 R ~~(1) When a firm that manages, personally recommends or sells a cash deposit ISA to a private customer must ensure, in relation to that cash deposit ISA, that the private customer must be provided with the information specified in COB 6.5.42R instead of key features in good time before the customer is bound by the transaction is entered into, unless COB 6.4.27R (telephone sales) applies (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)).~~
- (2) ~~Paragraph (1) does not apply to a firm if it is a bank or building society which subscribes to the Banking Code issued by the British Bankers' Association, the Building Societies Association and the Association for Payment Clearing Services.~~

#### Traded life policies

6.4.14 R When a *firm* personally recommends that a *private customer* should purchase a *traded life policy*, the *customer* need not be provided with key features, if the *firm* instead supplies the information outlined in COB 6.5.44R writing to the *private customer* in good time before the *customer* he is asked to complete any form of application or authority giving effect to the purchase of the *traded life policy*.

...

6.4.18 R COB 6.4.15R does not apply to a *stakeholder pension scheme* operator when its *stakeholder pension scheme* is sold on the *personal* recommendation of, or arranged to be sold by, another ~~*firm*~~ *person*, provided that other *person*:

- (1) is a *firm* (or an *appointed representative*) operating from an establishment maintained by the *firm* (or *appointed representative*) in the *United Kingdom*; or
- (2) is operating from an establishment in an *EEA State* whose law imposes an obligation on the *person* to provide information about the *stakeholder pension scheme* in accordance with articles 3 and 5(1) and (2) of the *Distance Marketing Directive*.

6.4.19 R ...

- (2) In COB 6.2 to COB 6.5, for the purposes of (1), the *firm* must treat trustees and ~~managers~~ operators as *private customers*.

...

6.4.22 R A written notice required by COB 6.4.21R must be provided by the *firm* no later than 8 *business days* after the *cancellation period* commences ~~the issue of the post-sale notice of the *private customer's* right to cancel under the cancellation rules.~~

...

#### Entering into a distance contract for accepting deposits

6.4.25 R (1) A *retail customer* must be provided with all the contractual terms and conditions and the information in COB App 1 in a *durable medium* in good time before he is bound by a *distance contract* or offer under which the *firm* will *accept deposits*, unless an exemption in (2), (3), (4) or (5) applies.

(2) Exemption: telephone sales

The exemption in COB 6.4.27R applies in the case of *voice telephony communications* (references to a '*customer*' in that rule should be read as references to a '*retail customer*').



(3) Exemption: certain other means of distance communication

This exemption applies, if the contract is concluded at the *retail customer's* request using a *means of distance communication* (other than telephone) which does not enable provision of the contractual terms and conditions and the information in accordance with (1). In that case, the *firm* must provide it to the *retail customer* in a *durable medium* immediately after the conclusion of the *distance contract*.

(4) Exemption: successive or separate operations under an initial service agreement

This exemption applies if the *firm* has an initial service agreement with the *retail customer* and the contract is in relation to a successive operation or a separate operation of the same nature under that agreement (see *COB 1.10.2G (1)*).

(5) Exemption: other successive or separate operations

This exemption applies if:

- (a) the *firm* has no initial service agreement with the *retail customer*;
- (b) the *firm* has performed an operation with the *retail customer* within the last year; and
- (c) the contract is in relation to a successive operation or separate operation of the same nature (see *COB 1.10.2G (2)*).

6.4.26 G There is a further exemption for those *firms* which subscribe to the Banking Code Guidance (see *COB 1.11.2R*).

...

Provision of key features or other information in relation to a telephone call

- 6.4.27 R (1) Where this chapter requires *key features* or other information to be provided, in the case of voice telephony communications, a *firm*:
- (a) must provide the *customer* at the beginning of the telephone conversation with the name of the *firm* and (if the call is initiated by the *firm*) the commercial purpose of the call; and
  - (b) provided the *customer* gives his explicit consent to receiving only limited information, may proceed on the basis of the following oral information only:
    - (i) the name of the person in contact with the *customer* and his link with the *firm*;
    - (ii) a description of the main characteristics of the service;
    - (iii) the total price to be paid by the *customer* to the *firm* for the service, including all related fees, charges and expenses, and all taxes paid through the *firm* together with a statement, where relevant, that commission or remuneration will be paid to the *adviser* or *representative*, or, where an exact price cannot be indicated, the basis for the calculation of the price enabling the *customer* to verify it;
    - (iv) where relevant, notice of the possibility that other taxes or costs may exist that are not paid through the *firm* or imposed by it;
    - (v) the existence or absence of a right to cancel the service under COB 6.7 and, where there is such a right, its duration and the conditions for exercising it, including information on the amount which the *customer* may be required to pay if the contract is terminated early or unilaterally under its terms, as well as the consequences of not exercising it; and
    - (vi) that other information is available on request, and the nature of that information.
- (2) If the *customer* does not give his explicit consent to receiving only the limited information in (1)(b), and the parties wish to proceed by telephone, the *firm* must prior to the conclusion of the contract provide all of the information required by COB App 1 orally to the *customer*.

- (3) In the case of either (1) or (2), the *firm* must send the *private customer* immediately after the contract is concluded, the required *key features* or other information (as applicable) in a *durable medium*.
- (4) If the service relates to a *tax-exempt policy* issued by a *friendly society*, the *firm* may send an abbreviated *key features* in accordance with COB 6.5.43R (Friendly Society tax-exempt policies).

6.4.28 G Firms are reminded of the requirements in COB 3.8.21G (Real time financial promotions) and COB 3.10 (Unsolicited real time financial promotions) in relation to telephone calls that may fall within the definition of a *financial promotion*.

General

6.5.2 R A *firm* must ensure, unless COB 6.5.3R applies, that:

- (4) ...; and
- (5) ...; and
- (6) all *key features* it produces in relation to a *distance contract* with a *retail customer* include all the contractual terms and conditions and the information in COB App 1 except to the extent that they are separately provided to the *retail customer* in a *durable medium* at the same time.

6.5.3 R A *firm* may adapt the prescribed content and format requirements in COB 6.5 only when it can demonstrate that this is necessary to reflect the terms and nature of a particular product and that, in relation to a *distance contract* with a *retail customer*, in doing so it does not omit the contractual terms and conditions and information in COB App 1.

...

Information requirements for *cash deposit ISAs*, friendly Society tax-exempt policies, traded life policies and broker funds

6.5.41 G COB 6.5.42R does not apply to a *cash deposit ISA* offered by a *bank* or *building society* which subscribes to the Banking Code Guidance (see COB 1.11.2R 6.4.13R(2)).

6.5.42 R If COB 6.4.13R(1) applies, for a *cash deposit ISA*, the *private customer* must be given the following ~~minimum~~ information (in accordance with COB 6.4.13R) and, in relation to a *distance contract with a retail customer*, all the contractual terms and conditions and the information in COB App 1 in place of *key features*:

...

- (8) the arrangements for the application of the right to cancel, including the following:
- (a) the options available on cancellation (a firm must either assist the private customer in switching accounts or refund all monies deposited together with interest);
  - (b) information about how cancellation will operate in circumstances where the account forms part of a maxi-ISA which contains other components;
  - (c) a statement that the effect of cancelling the last component has the effect of cancelling the entire ISA agreement and may also (where it is the case) delay the customer from entering into another ISA agreement until the next tax year; and
  - (d) a statement that a private customer who exercises a right to cancel will not incur any additional charges or be affected by any notice period;

...

#### Friendly Society tax exempt policies

- 6.5.43 R Where a *private customer* buys a *tax-exempt policy* issued by a *friendly society*, or agrees to make additional contributions to such a *policy*, the *firm* may, where there is a right to cancel under COB 6.7 (Cancellation and withdrawal), issue an abbreviated form of *key features* containing ~~only~~ the following details of and, in relation to a distance contract with a retail customer, all the contractual terms and conditions and the information required under COB App 1:

...

#### Traded life policies

- 6.5.44 R When *personally recommending* the purchase of a *traded life policy*, a *firm* may provide a *private customer* with the information in ~~at~~ COB 6.5.49R and, in relation to a distance contract with a retail customer, all the contractual terms and conditions and the information in COB App 1 in place of *key features* (in accordance with COB 6.4.14R).

...

- 6.7.1 R COB 6.7 applies to:

...

- (5) the operator of a *stakeholder pension scheme*;

(6) a firm which enters into distance contracts with retail customers, the making or performance of which constitutes, or is part of:

(a) dealing as agent, advising or arranging in relation to designated investments, unless the distance contract is concluded merely as a stage in the provision of another service by the firm or another person (see COB 1.10.6G);

(b) any other designated investment business; or

(c) accepting deposits;

but not including a distance contract entered into by an appointed representative as principal.

6.7.2 G The firms in COB 6.7.1R (except those in COB 6.7.1R(3)) are product providers, insurers, deposit-taking firms or stakeholder pension scheme operators, that is, the firms responsible for issuing life policies, selling units, issuing long-term insurance contracts, accepting deposits for ISAs, or acting as operators of stakeholder pension schemes.

COB 6.7 (Cancellation and withdrawal) does not act to cancel distance contracts entered into by an appointed representative as principal to provide intermediation services to a retail customer. Regulations 8 (Right to cancel) to 12 (Payment for services provided before cancellation) of the Distance Marketing Regulations may apply instead (see regulation 4(5)).

6.7.3 G ~~[deleted] (1) COB 6.7 specifies the rights which customers have either to cancel agreements into which they have entered, or to withdraw any offer before an agreement has commenced.~~

~~(2) COB 6.7.12R specifies those agreements for a stakeholder pension scheme which customers have a right to cancel.~~

~~(3) COB 6.7.14R(1) specifies those agreements for an EIS, ISA or PEP from which customers have a right to withdraw.~~

~~(4) COB 6.7.15R specifies those long-term insurance contracts which customers have a right to cancel and those which they do not.~~

~~(5) A firm has the option to replace a post-sale right to cancel certain pension annuities referred to as "cancellation substitute" (see COB 6.7.14R(2)). This option is also available for pension transfers. If a firm chooses not to offer the cancellation substitute, it has to offer cancellation. The cancellation substitute is available as it is very difficult for post-sale cancellation to work effectively in the case of pension~~

~~transfers, because of the difficulty of putting the customer back in his original position.~~

- (6) ~~COB 6.7.17R specifies those non-life agreements for a pension contract, appropriate personal pension or units in an AUT or ICVC which customers have a right to cancel and those which they do not. It also allows firms, for units within an ISA or PEP, to replace cancellation with a pre-sale right to withdraw.~~
- (7) ~~COB 6.7.20R specifies the cancellation procedure which applies to cash deposit ISAs.~~
- (8) ~~COB 6.7.23R specifies certain variations to existing agreements which customers have a right to cancel or right to withdraw.~~
- (9) ~~COB 6.7.54R to COB 6.7.58R contain rules and guidance on investment agreements subject to shortfall and describe how to calculate shortfall.~~

6.7.4 G COB 6.7.5G summarises the applicable cancellation and withdrawal rights and the maximum period of reflection. Firms should have regard to the detailed rules and guidance in all cases, particularly for the detailed exemptions.

6.7.5 G Cancellable investment agreements.  
This table belongs to COB 6.7.4G

Delete the existing table and replace with the following:

<b>Cancellable investment agreements</b>			
	Post-sale right to cancel?	Pre-sale right to withdraw ?	Maximum period of reflection (but see COB 6.7.11R)
<b>A. Contracts where the right arises regardless of means of sale.</b>			
<i>Appropriate personal pension (APP)</i>	Yes	No	30 days
<i>Cash deposit ISA</i>	Yes	No	14 days
<i>Life policy (including pension policy, pension annuity or within ISA)</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>

<b>Cancellable investment agreements</b>			
<i>Personal pension contract</i>	Yes <sup>1</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<i>Stakeholder pension scheme (SHP)</i>	Yes <sup>1</sup>	No <sup>1</sup>	30 days <sup>2</sup>
Certain variations of existing <i>life policies, pension contracts</i> and <i>SHPs</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<b>B. Contracts where the right arises only if advice is given or if sold by distance contract.</b>			
<i>Units in an AUT, recognised scheme or ICVC (within an ISA or PEP)</i> (1) if sold by <i>distance contract</i> ; (2) if sold otherwise with advice	No Yes <sup>4</sup>	No No <sup>4</sup>	14 days
<i>ISA or PEP not mentioned in any other row</i>  (1) if sold by <i>distance contract</i> (2) if sold otherwise with advice	Yes <sup>5,6</sup> No	No Yes <sup>3</sup>	14 days 7 days
<i>Units in an AUT, recognised scheme or ICVC (outside an ISA or PEP)</i>  (1) if sold by <i>distance contract</i> (2) if sold otherwise with advice	No Yes	No No	14 days
<i>EIS</i>  (1) if sold by <i>distance contract</i> (2) if sold otherwise with advice	Yes <sup>5,6</sup> No	No Yes <sup>3</sup>	14 days 7 days
<b>C. Contracts where the right arises for distance contracts only</b>			
<i>Distance contract to accept deposits</i>	Yes <sup>5,6</sup>	No	14 days

### Cancellable investment agreements

<i>Distance contract</i> not mentioned in another row the making or performance of which constitutes, or is part of, <i>designated investment business</i>	Yes <sup>5,6,7</sup>	No	14 days
Notes:			
1. For a <i>pension annuity</i> or <i>pension transfer</i> (and a relevant variation), the <i>firm</i> can, in certain circumstances, choose to operate a pre-sale right to withdraw in <i>COB 6.7.19R</i> instead of a post-sale right to cancel (see <i>COB 6.7.14R(2)</i> ). A <i>firm</i> may offer a pre-sale right to withdraw, even where there is no right to cancel.			
2. The period is at least 14 days if the option of pre-sale withdrawal is offered.			
3. There is no right to withdraw for a second or subsequent <i>EIS</i> or <i>ISA</i> , or (for an <i>EIS</i> or non-packaged product <i>ISA</i> or <i>PEP</i> ) where the <i>firm</i> has previously disclosed to the <i>customer</i> that no such rights will apply.			
4. For <i>units</i> in an <i>AUT</i> , <i>recognised scheme</i> or <i>ICVC</i> (within an <i>ISA</i> or <i>PEP</i> ), the <i>firm</i> can choose to offer a seven-day pre-sale right to withdraw rather than a post-sale right to cancel (see <i>COB 6.7.14R(1)</i> ). There is no right to cancel or withdraw for a second or subsequent <i>ISA</i> .			
5. There is no post-sale right to cancel for a <i>distance contract</i> where the price depends on fluctuations in the financial market place outside the <i>firm's</i> control which may occur during the cancellation period.			
6. There is no post-sale right to cancel for a <i>distance contract</i> : <div style="margin-left: 20px;"> <p>(a) where the performance of the <i>distance contract</i> has been fully completed by both parties at the <i>customer's</i> express request before the <i>customer</i> exercises his right to cancel; or</p> <p>(b) where the <i>firm</i> has an initial service agreement with the <i>customer</i> and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see <i>COB 1.10.2G</i>).</p> </div>			
7. For a <i>distance contract</i> to give advice, arrange deals, or deal as agent see <i>COB 1.10.6G</i> (Distance contracts for intermediation services).			

...

#### Post-sale rRight to cancel

- 6.7.7 R A retail customer, ~~who is an individual~~, has a right to cancel:
- (1) a contract ~~an investment agreement~~ specified in column row 1 of *COB 6.7.15R* or *COB 6.7.17R*, unless the right to cancel is disapplied or replaced by anything in column row 2 of *COB 6.7.15R* or *COB 6.7.17R*;
  - (2) a contract ~~n investment agreement~~ for a *stakeholder pension scheme* for which a right to cancel applies under *COB 6.7.12R*;



- (3) ~~a contract~~ an investment agreement for a *cash deposit ISA* ~~in accordance with COB 6.7.20R (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance))~~);
- (4) a variation of a *life policy, pension contract* or *stakeholder pension* scheme for which a right to cancel applies under COB 6.7.23R.

6.7.8 R The trustees of an *occupational pension scheme* or the trustees and managers of a *stakeholder pension scheme* must be treated so far as necessary as an ~~individual~~ retail customer for the purposes of the *cancellation rules*, and acquire the same right to cancel as an ~~individual~~ retail customer.

- 6.7.9 G (1) ...
- (2) A *product provider* or operator of a *stakeholder pension scheme* (see COB 6.7.2G) may be unsure whether any of the situations in ~~column~~ row 2 of COB 6.7.17R applies to the ~~agreement~~ contract in question. In such circumstances the *product provider* or operator of a *stakeholder pension scheme* may find it convenient to contract with an intermediary for the provision of documentary evidence needed to confirm the status of *customers*. However, the responsibility for ensuring compliance with the *cancellation rules* remains with the *product provider* or operator of a *stakeholder pension scheme*.

#### Cancellation period

6.7.10 R When a retail customer has a right to cancel under COB 6.7.7R(1), (2) ~~or (4)~~, that right must (unless COB 6.7.11R applies) be exercised:

- (1) (in the case of a *life policy, personal pension policy, personal pension contract* or *stakeholder pension scheme*) within ~~the shorter of:~~
  - (a) ~~30 days~~ days; or
  - (b) ~~the period (of 14 days or more) specified by the firm;~~  
 from the date when the *customer* received a *post sale notice* from the *firm*.
- (2) (in any other case) within 14 ~~days~~ days ~~from the date when the customer received a post sale notice from the firm.~~

6.7.10A R The cancellation period begins on:

- (1) (other than for distance contracts and cash deposit ISAs) the date the customer receives the reminder notice of his right to

cancel in accordance with COB 6.7.30R;

- (2) (for distance contracts and cash deposit ISAs the later of:
- (a) (for a life policy) the day the retail customer is informed that the contract has been concluded; or
  - (b) (for any other contract) the day of the conclusion of the contract; or
  - (c) the day on which the retail customer receives the contractual terms and conditions and other information required by COB 3.9, 4.2 or 6, as applicable.

6.7.11 R Where the terms of the *firm's* contract give the *retail customer* a longer period to cancel (that is, in excess of the 14 or 30 days specified), the *firm* must disclose in the information about the right to cancel ~~post-sale notice~~ the differences between the *retail customer's* rights under COB 6.7.10R and the terms of the contract, which operate independently.

Right to cancel a stakeholder pension scheme

- 6.7.12 R (1) A *retail customer*, ~~who is an individual, and~~ who has entered into an ~~investment agreement~~ contract for a *stakeholder pension scheme* has a right to cancel.
- (2) When the *retail customer* has entered into an ~~investment agreement~~ contract for a *stakeholder pension scheme* involving recurring contributions to that *stakeholder pension scheme*, only the first contribution will attract a right to cancel provided that:
- (a) the intention or option to make regular contributions has been disclosed in advance of the *retail customer* entering into the *investment agreement*; and
  - (b) the *retail customer's* intention to make regular contributions is evidenced.

6.7.13 G For the purposes of COB 6.7.12R(2)(a), disclosure of the option to make regular contributions may, for example, take place in the *key features*. For the purposes of COB 6.7.12R(2)(b), ~~an individual~~ *retail customer's* intention to make regular contributions could, for example, be demonstrated by the establishment of a direct debit mandate or instructions to an employer to deduct regular contributions from salary.

Pre-sale rRight to withdraw

- 6.7.14 R A retail customer, ~~who is an individual~~, has a right to withdraw an offer to enter into:
- (1) (unless a right to cancel is offered for an *ISA* or *PEP* under COB 6.7.7R(3), COB 6.7.15R or, COB 6.7.17R or ~~COB 6.7.20R~~ and subject to cases 8 and 9 of ~~column~~ row 2 COB 6.7.17R) an *EIS*, *ISA* or *PEP*, following *advice on investments*; the right to withdraw procedures are that the offer made by the *customer* to enter into the agreement contract cannot be accepted by the *firm* until at least seven days after the offer is made; or
  - (2) a *pension annuity* or a *pension transfer* (or a relevant variation), if a right to cancel has been replaced by a right to withdraw under case 4(a) or 7(a) of ~~column~~ row 2, COB 6.7.15R, case 12 of ~~column~~ row 2, COB 6.7.17R, COB 6.7.23R (3), or COB 6.7.26AR (2); the right to withdraw procedures are set out in COB 6.7.19R.

6.7.15 R Cancellable investment agreements contracts and exceptions – life  
This table belongs to COB 6.7.7R(1).

Delete the existing table and replace with the following (in this table, the existing columns (1) and (2) have been changed to rows (1) and (2). This change is not indicated but, otherwise, changes are indicated by using underlining and striking-through in the usual way):

<b><u>Cancellable investment agreements contracts and exceptions</u> – life</b>	
<del>Investment agreements for a</del> <u>Long-term insurance contracts</u> for which an <del>individual</del> a <u>retail customer</u> has a right to cancel under <u>COB 6.7.7R(1)</u> (subject to row 2):	
Row 1	<p>A. <u>Life policy</u> (whether or not held within an <i>ISA</i> – see notes 1, 2 and 3 in <u>COB 6.7.16R</u>) (see <u>COB 6.7.23R</u> regarding variation of an existing <i>life policy</i>);</p> <p>B. <u>Appropriate personal pension</u> which is a <i>pension policy</i>;</p> <p>C. <u>Pure protection contract</u>.</p>

**Cancellable ~~investment agreements~~ contracts and exceptions – life**

~~Investment agreements for a~~ Long-term insurance contracts for which an individual a retail customer has a right to cancel under *COB* 6.7.7R(1) (subject to row 2):

Row 2	<p><u>There is</u> no right to cancel where any one or more of the following cases applies:</p> <ol style="list-style-type: none"> <li>1. <del>P</del><u>pension fund management</u> policy (<u>but see note 5 in COB 6.7.16R</u>);</li> <li>2. <del>L</del><u>ife</u> policy that relates to or is associated with securing benefits under a <i>defined benefits pension scheme</i> (<u>but see note 5 in COB 6.7.16R</u>);</li> <li>3. <del>A</del><u>ny</u> life policy for a term of six months or less (unless note 3 in <i>COB</i> 6.7.16R applies) (<u>see also note 5 in COB 6.7.16R</u>);</li> <li>4. <del>P</del><u>pension</u> policy or <i>stakeholder pension scheme</i> funded (wholly or in part) from payments derived from:             <ol style="list-style-type: none"> <li>(a) a <i>pension transfer</i>, for which the right to cancel is replaced by the right to withdraw (see <i>COB</i> 6.7.14R(2)), using the cancellation substitute in <i>COB</i> 6.7.19R; or</li> </ol> </li> </ol>
	(b) compensation or redress paid by a <i>firm</i> following a review undertaken in relation to a complaint;
	5. <del>T</del> <u>raded</u> life policy;
	6. <del>L</del> <u>ife</u> policy effected by the trustees of an <i>occupational pension scheme</i> or the employer, or the manager or trustees of a <i>stakeholder pension scheme</i> that represents a:
	(a) <i>pension buy-out contract</i> ; or
	(b) purchase of a without-profits deferred <i>pension annuity</i> ; or
	(c) <i>defined benefits pension scheme</i> or a single <i>premium</i> payment to any <i>occupational pension scheme</i> with a pooled fund (that is, underlying <i>investments</i> are not earmarked for individual scheme members); or
	(d) purchase made to insure and secure members' pension benefits under a <i>money-purchase occupational scheme</i> or <i>stakeholder pension scheme</i> (unless it is the master, first or only <i>policy</i> );
	7. <del>P</del> <u>pension annuity</u> that is:
	(a) due to commence within a year and a day of the contract, for which the right to cancel is replaced by the right to withdraw (see <i>COB</i> 6.7.14R(2)), using the cancellation substitute in <i>COB</i> 6.7.19R; or

**Cancellable investment agreements contracts and exceptions – life**

~~Investment agreements for a~~ Long-term insurance contracts ~~for which an individual a~~ retail customer has a right to cancel under *COB 6.7.7R(1)* (subject to row 2):

	(b) funded (wholly or in part) from compensation or redress paid by a <i>firm</i> following a review undertaken in relation to a complaint;
	8. <del>The</del> <u>retail customer</u> , other than an <i>EEA ECA recipient</i> , at the time he signs the application, is <i>habitually resident</i> :
	(a) in an <i>EEA State</i> other than the <i>United Kingdom</i> ( <u>but see note 4 and note 5 in COB 6.7.16R</u> ); or
	(b) outside the <i>EEA</i> and is not present in the <i>United Kingdom</i> ;
	9. <del>P</del> <u>pure protection contract</u> effected by the trustees of an <i>occupational pension scheme</i> , an employer or a <i>partnership</i> to secure benefits for employees or the <i>partners</i> in the <i>partnership</i> ;
	<u>10. life policy which is a distance contract where the price depends on fluctuations in the financial market place outside the firm's control which may occur during the cancellation period;</u>
	11. the contract is a <u>distance contract</u> where: (a) the performance of the <i>distance contract</i> has been <u>fully completed by both parties at the retail customer's express request before the retail customer exercises his right to cancel</u> ; or (b) the <i>firm</i> has an initial service agreement with the <u>retail customer</u> and the contract is in relation to a <u>successive operation or separate operations of the same nature under that agreement (see COB 1.10.2G)</u> .

6.7.16 R Notes to cancellable ~~investment agreements~~ contracts and exceptions – life

This table belongs to *COB 6.7.15R*

**Notes to COB 6.7.15R:**

- |  |
|--|
| <p>1. Recurring single <i>premium life policy</i>: Under certain conditions, only the first <i>premium</i> in what might be a series of <i>premiums</i> (for example, in the case of a <i>mini-ISA insurance component</i>) attracts cancellation rights under <i>COB 6.7.7R(1)</i>. The conditions are:</p>   |
| <p>(a) the option to make a series of single <i>premium</i> payments is disclosed at outset (for example, in the <i>key features</i>); and</p> <p>(b) the intention is evidenced (for example, by the <i>retail customer</i> establishing a direct-debit mandate).</p>   |
| <p>2. Multiple contracts: Where a <i>retail customer</i> enters into a set of <u>contracts</u> <del><i>investment agreements</i></del> at the same time (for example, the different components held within a <i>maxi-ISA</i>) and with the same <i>firm</i> (or another <i>person</i> in the same <i>marketing group</i> as that <i>firm</i>), and that set is being purchased to fulfil one investment objective of the <i>retail customer</i>, the <i>firm</i> may treat the multiple <del><i>agreements</i></del> <u>contracts</u> as being one <del><i>agreement</i></del> <u>contract</u> for the purposes of <i>COB 6.7</i>. But if it does so, the <i>firm</i> must ensure that the <i>customer</i> retains a right to cancel each <u>contract</u> <del><i>investment agreement</i></del> separately. See also <del><i>COB 6.7.37R in relation to a maxi-ISA</i></del>. This note applies also to a group of <i>contracts of insurance</i>, for example, <i>term assurance</i> contracts which have been established as part of a specific marketing arrangement. Such an arrangement may not have an investment objective.</p> |
| <p>3. A purchaser of a single <i>premium pension policy</i> has a right to cancel where the designated retirement date is within six months of the date of the <i>policy</i>, unless the <i>policy</i> falls within case 1, 4 or 7(b) of <del>column</del> <u>row 2</u>.</p>   |
| <p>4. For a <i>customer</i>, other than an <i>EEA ECA recipient, habitually resident</i> in an <i>EEA State</i> other than the <i>United Kingdom</i>, <i>firms</i> are reminded that they may need to apply cancellation in accordance with the requirements in that <i>EEA State</i>.</p>   |
| <p>5. <u>This exemption from giving a right to cancel does not apply for distance contracts.</u></p>   |

6.7.17 R Cancellable ~~investment agreements~~ contracts and exceptions – non-life  
This table belongs to *COB 6.7.7R (1)* and *COB 6.7.14R (1)*

Delete the existing table and replace with the following (in this table, the existing columns (1) and (2) have been changed to rows (1) and (2). This change is not indicated but, otherwise, changes are indicated by using underlining and striking-through in the usual way):

**Cancellable investment agreements contracts and exceptions – non-life**

Investment agreements Contracts for which an individual a retail customer has a right to cancel under COB 6.7.7R(1) (subject to column row 2):-

Row 1	<p>A. <del>P</del><u>pension contract</u> (see notes 1, 2 and 4 in COB 6.7.18R):-</p> <p>B. <del>A</del><u>appropriate personal pension</u> which is a <i>pension contract</i> (see note 4 in COB 6.7.18R):-</p> <p>C. <del>S</del><u>subscriptions</u> (but see notes 1, <del>and 2</del> and 5 in COB 6.7.18R) which can be invested only in <i>units</i> (whether or not held within an <i>ISA</i>, <i>PEP</i> or <i>pension contract</i>) in an <i>AUT</i>, <i>recognised scheme</i> or <i>ICVC</i> purchased from:</p> <p>(a) the <i>operator</i>; or</p> <p>(b) its <i>marketing group associate</i> acting as an <i>ISA manager</i> or <i>plan manager</i>:-</p> <p>D. <u>distance contracts</u> (other than for a <i>life policy</i>, <i>stakeholder pension scheme</i>, <i>cash deposit ISA</i> or a contract in A, B or C) the making or performance of which by the <i>firm</i> constitutes or is part of:</p> <p>(a) <u>dealing as agent, advising or arranging in relation to designated investments</u>, unless the <i>distance contract</i> is concluded merely as a stage in the provision of another service by the <i>firm</i> or another <i>person</i> (see COB 1.10.6G); or</p> <p>(b) any other <i>designated investment business</i>; or</p> <p>(c) <u>accepting deposits</u>.</p>
Row 2	<p><u>There is</u> no right to cancel where any one or more of the following cases applies:</p> <p>1. <del>T</del><u>he customer</u> is not a <i>private customer</i> (but see note 5 in COB 6.7.18R):-</p>
	<p>2. <del>T</del><u>he agreement-contract</u> is entered into with the <i>firm</i> (and where relevant with any <i>independent intermediary</i>) as an <i>execution-only transaction</i> (unless note 4 or note 5 in COB 6.7.18R applies):-</p> <p>3. <del>T</del><u>he agreement-contract</u> is entered into through a <i>direct offer financial promotion</i> (unless note 4 or note 5 in COB 6.7.18R applies):-</p> <p>4. <del>T</del><u>he agreement-contract</u> represents an exchange of <i>units</i> between <i>sub-funds</i>:-</p>

**Cancellable investment agreements contracts and exceptions – non-life**

Investment agreements Contracts for which an individual a *retail customer* has a right to cancel under COB 6.7.7R(1) (subject to column row 2):-

	<p>5. <del>The agreement contract</del> represents a <i>defined benefits pension scheme</i> (but see note 5 in COB 6.7.18R):-</p> <p>6. <del>The agreement contract</del> is entered into under a <i>customer agreement</i> or during negotiations (which are not <i>ISA</i> or <i>PEP</i> related) intended to lead to a <i>client agreement</i> (unless note 4 or note 5 in COB 6.7.18R applies):-</p>
	<p>7. <del>The agreement contract</del> relates to an <i>ISA</i> or <i>PEP</i> for which the right to cancel is replaced by the right to withdraw (but see COB 6.7.14R(1) and note 5 in COB 6.7.18R):-</p>
	<p>8. <del>The agreement contract</del> relates to an <i>EIS</i> or non-packaged product <i>ISA</i> or <i>PEP</i> and is entered into, following <i>advice on investments</i>, and following an explanation <u>that neither of the rights specified in case 7 will apply</u>, given to the <i>customer</i> in accordance with COB 3.9.21R(2) (<del>Direct offer financial promotions: Cancellation rights</del>) or COB 4 Ann 2E(9)(a) 4.2.15E(10) (<del>Terms of business and client agreements with customers</del>) in a <i>direct offer financial promotion, terms of business</i>, or given in <i>EIS particulars</i>, <del>that neither of the rights specified in case 7 will apply</del> (but see note 5 in COB 6.7.18R):-</p>
	<p>9. <del>The agreement contract</del> entered into is a second or subsequent <i>ISA</i> (or <i>EIS</i>) on substantially the same terms (see note 3 in COB 6.7.18R) as an <i>ISA</i> (or <i>EIS</i>) purchased from the same <i>ISA manager</i> (or <i>EIS manager</i>) in the previous tax year (but see note 5 in COB 6.7.18R):-</p>
	<p>10. <del>The agreement contract</del> relates to a change from <i>accumulation units</i> to <i>income units</i> or vice versa, in the same <i>scheme</i>:-</p>
	<p>11. <del>Pension contract</del> funded (wholly or in part) from payments derived from compensation or redress paid by a <i>firm</i> following a review undertaken in relation to a complaint:-</p>
	<p>12. <del>Pension contract</del> or <i>stakeholder pension scheme</i> funded (wholly or in part) from payments derived from a <i>pension transfer</i> for which a right to cancel is replaced by a right to withdraw (see COB 6.7.14R(2)R) using the cancellation substitute in COB 6.7.19R:-</p>
	<p>13. <del>The agreement contract</del> relates to a <i>recognised scheme</i> and is with an <i>operator</i> who is not:</p>



**Cancellable investment agreements contracts and exceptions – non-life**

Investment agreements Contracts for which an individual a retail customer has a right to cancel under COB 6.7.7R(1) (subject to ~~column~~ row 2):-

	<p>(a) an <i>authorised person</i>; or</p> <p>(b) carrying on business in the <i>United Kingdom</i>:-</p>
	<p>14. <del>The agreement contract</del> relates or would relate to exported products, that is to say:</p>
	<p>(a) where the <i>customer</i> is not <i>habitually resident</i> in the <i>United Kingdom</i> (or, for a <i>distance contract</i>, <i>EEA</i>) at the date of the offer of the <del>agreement contract</del>; or</p>
	<p>(b) the <i>firm</i> has reasonable grounds for assuming that no <i>advice on investments</i> about the <del>agreement contract</del> was provided by anyone carrying on <i>designated investment business</i> in the <i>United Kingdom</i> (but see note 5 in COB 6.7.18R):-</p> <p>15. <u>for distance contracts</u>:</p> <p>(a) <u>the price depends on fluctuations in the financial market outside the <i>firm</i>'s control which may occur during the cancellation period, such as contracts related to:</u></p> <p>(i) <u>foreign exchange</u>; or</p> <p>(ii) <u>money market instruments</u>; or</p> <p>(iii) <u>transferable securities</u>; or</p> <p>(iv) <u>units in collective investment undertakings</u>; or</p> <p>(v) <u>financial-futures contracts, including equivalent cash-settled instruments</u>; or</p> <p>(vi) <u>forward interest-rate agreements</u>; or</p> <p>(vii) <u>interest-rate, currency and equity swaps</u>; or</p> <p>(viii) <u>options to acquire or dispose of any instruments in (i) to (vii), including cash-settled instruments and options on currency and on interest rates</u>; or</p> <p>(b) <u>the performance of the <i>distance contract</i> has been fully completed by both parties at the <i>customer</i>'s express request before the <i>customer</i> exercises his right to cancel</u>; or</p> <p>(c) <u>the <i>firm</i> has an initial service agreement with the <i>customer</i> and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see COB 1.10.2G).</u></p>

6.7.18 R Notes to cancellable ~~investment agreements~~ contracts and exceptions - non-life

This table belongs to COB 6.7.17R

Notes to COB 6.7.17R:	
1.	Recurring single payment <i>pension contracts</i> and <i>unit savings plans</i> . Under certain conditions, only the first payment in what might be a series of payments attracts cancellation rights under COB 6.7.7R (1). The conditions are:
	(a) the intention or option to make a series of single payments is disclosed at outset (for example, in the <i>key features</i> ); and
	(b) the intention is evidenced (for example, by the <i>customer</i> establishing a direct debit mandate).
2.	Multiple <del>agreements</del> <u>contracts</u> . Where a <i>customer</i> enters into a set of <del>investment agreements</del> <u>contracts</u> at the same time (for example, regarding different components held within a <i>maxi-ISA</i> ) and with the same <i>firm</i> (or another <i>person</i> in the same <i>marketing group</i> as that <i>firm</i> ) and that set is being purchased to fulfil one investment objective of the <i>customer</i> , the <i>firm</i> may treat the <del>agreements</del> <u>contracts</u> as being one <u>agreement contract</u> for the purposes of COB 6.7. But if it does so, the <i>firm</i> must ensure that the <i>customer</i> has a right to cancel each <u>contract investment agreement</u> separately ( <del>see also COB 6.7.37R in relation to maxi-ISA</del> ).
3.	For example, <i>mini-</i> to <i>mini-ISA</i> or <i>maxi-</i> to <i>maxi-ISA</i> would be regarded in this context as ‘on substantially the same terms’.
4.	A <i>customer</i> has a right to cancel an <i>appropriate personal pension or pension contract</i> at the outset and on any subsequent agreement for a variation of a <i>pension contract</i> (see COB 6.7.23R regarding variation of an existing contract).
5.	<u>This exemption from giving a right to cancel does not apply for distance contracts.</u>

6.7.19 R Cancellation substitute

This table belongs to COB 6.7.14R(2), cases 4(a) and 7(a) of ~~column~~ row 2 to COB 6.7.15R and case 12 of ~~column~~ row 2 to COB 6.7.17R.

Cancellation substitute	
The <i>retail customer's</i> right to cancel under COB 6.7.7R(1) or (4) is replaced by the right to withdraw only if:	
1.	the <i>firm</i> has supplied (or has reasonably relied upon another <i>firm</i> to supply) to the <i>retail customer</i> , at least <u>30 days in the case of a life policy and 14 days in any other case</u> before the contract is concluded, a written notice (see note 1) which prominently states:

<b>Cancellation substitute</b>	
	(a) that the <i>retail customer</i> has a <u>that</u> period of at least 14 days within which to consider his pension options;
	(b) the dates at which the period begins and ends (which must be, in the case of a <i>pension transfer</i> , before the transfer has been irrevocably effected);
	(c) the pension options available (for example, the <i>open-market option</i> in relation to a <i>pension annuity</i> );
	(d) the steps the <i>retail customer</i> must take in order to exercise a particular pension option;
	(e) that the <i>retail customer</i> is entitled to <i>key features</i> and is advised to check with the <i>firm</i> if it has not been received;
	(f) the cost of any advice given to the <i>retail customer</i> in relation to the transaction; and
2.	the <i>firm</i> has taken sufficient steps (or has reasonably relied upon the same <i>firm</i> as in 1. to take those steps) to ensure that the <i>customer</i> has been informed and made fully aware of the potential advantages and disadvantages of proceeding and has had an opportunity to consider all other possible alternatives.
Note:	
1. The notice must be issued separately or feature prominently as part of the application form; <u>or suitability letter</u> <del>or key features</del> supplied to the <i>customer</i> .	

6.7.20 R ~~[deleted]~~ Cancellation— cash deposit ISA

This table belongs to *COB 6.7.7R(3)*

<b><del>Cancellation— cash deposit ISA</del></b>	
<del>The <i>firm</i> must supply (or may reasonably rely upon another <i>firm</i> to supply) to the <i>retail customer</i> before the account is opened, a written notice (see note 1) which prominently states:-</del>	
<del>A.</del>	<del>That the <i>retail customer</i> has a 14 day period within which to consider whether or not to keep the account open;</del>
<del>B.</del>	<del>The dates at which the 14 day period begins and ends (see note 2);</del>
<del>C.</del>	<del>The options available (see note 3);</del>
<del>D.</del>	<del>How cancellation will operate in circumstances where the account forms part of a <i>maxi ISA</i> which contains other components (see <i>COB 6.7.37R</i>);</del>
<del>E.</del>	<del>the steps the <i>retail customer</i> must take to communicate any decision not to proceed with the account (see <i>COB 6.7.42R</i> to <i>6.7.46G</i>); and</del>

## Cancellation—cash deposit ISA

F. That a *retail customer* who exercises a right to cancel will not incur any additional charges or be affected by any notice period.

Notes:

1. The notice must be issued separately or feature prominently as part of the minimum information supplied to the *retail customer*.
2. Unless the *firm* has specified a longer period to the *retail customer*, the minimum expiry date is the end of the fifteenth day from the date the account was opened.
3. A *firm* must either assist the *retail customer* in switching accounts or refund all monies deposited together with interest.

### Voluntary provisions

- 6.7.21 R If anything in column row 2 of either COB 6.7.15R or COB 6.7.17R removes the right to cancel a contract investment agreement, but a *firm* voluntarily gives the *retail customer* a right to cancel in any event, the *firm* must treat the agreement contract as if it were cancellable under COB 6.7.7R(1).
- 6.7.22 G (1) If the *firm* has any doubt whether a contract the investment agreement or the circumstances of its purchase bring the case within any part of COB 6.7.7R(1), it should treat the agreement contract as if it were cancellable.
- (2) A *firm* that informs a retail customer that he has sends a pre-sale notice or post-sale notice notice of a right to cancel where it is not obliged to give a right to cancel do so under COB 6.7.30R will be taken to have voluntarily granted the *retail customer* a right to cancel (unless, for the purposes of COB 6.7.17R, there is a relevant *client agreement* between the *firm* and the *retail customer*).

### Variations

- 6.7.23 R (1) After an increase in regular or single *premiums* or payments (including a *pension transfer*) to a *life policy*, *pension contract* or *stakeholder pension scheme*, a *retail customer*, ~~who is an individual~~, has a right to cancel (see COB 6.7.7R(4)) in the following circumstances unless (2) applies:
- (a) any variation, other than a ‘pre-selected option’ (see COB 6.7.26G), providing for substantial increases in *premium* or payment where the increase:
- (i) is being paid by way of varying the existing agreement contract; or
  - (ii) will result in a new agreement contract established

on the same terms as the original agreement contract;

and, in each case, represents an increase on the original *premium* or payments (or the previous highest agreed *premium* or payment) of more than 25% (see *COB 6.7.25G*); or

- (b) any variation, other than a 'pre-selected option' (see *COB 6.7.26G*), that results in a new agreement contract which involves fresh contract terms or imposes additional obligations on the *retail customer* due to a change in the terms of the original agreement contract;
- (c) any variation where the increase represents the proceeds of a *pension transfer*.

(2) Paragraph (1) does not apply if:

- (a) there would have been no right to cancel the original contract investment agreement under *COB 6.7.7R(1)* had that agreement been entered into on the date of the variation; or
- (b) the variation arises out of the settlement of a claim for damages or compensation connected with a previous contract investment agreement.

(3) A *firm* may use the cancellation substitute in *COB 6.7.19R* in relation to a variation of a contract investment agreement in any case where that substitute would have been available to it had the contract agreement been entered into on the date of the variation.

...

Electronic communication relating to cancellation and withdrawal

6.7.27 G For electronic transactions (for example, facsimile, e-mail or Internet) *firms* are referred to the *guidance* in *COB 1.8*. The *rules* in *COB* permit the *firm* to issue the *pre-sale or post-sale notices information about a right to cancel* and other communications, and to accept notice from *customers* who are exercising the right to cancel or withdraw, by electronic means. However, a *firm* should be able to demonstrate that the *customer* wishes to communicate electronically.

Time deadlines relating to cancellation and withdrawal

6.7.28 R ~~[deleted] (1) The deadlines in *COB 6.7.10R*, item 1 of *COB 6.7.19R*, item A and note 2 of *COB 6.7.20R*, *COB 6.7.34R(2)* and *COB 6.7.48R* are based on calendar days (excluding public holidays) and must be calculated by reference to the day after the date on which the agreement is concluded.~~

(2) In the event of any contingency beyond the *firm* or *customer's* control which prevents delivery or service of the cancellation notice, the period in question must be counted as public holidays and therefore will not count for the purposes of the time delay.

6.7.29 G ~~[deleted]~~ For an example of the operation of COB 6.7.28R(1), in the case of the eight-day deadline, the *post-sale notice* for an agreement concluded on Wednesday would need to be sent by the *firm* no later than Thursday of the following week.

Giving Reminding the customer notice of the right to cancel – contracts other than distance contracts and cash deposit ISAs

6.7.30 R Other than for distance contracts and cash deposit ISAs, wWhere there is a right to cancel, under COB 6.7.7R(1), (2) or (4), the *firm* which enters into the agreement contract with the *customer* (also see COB 6.7.31R) must send give the *customer*, in writing, a clear and prominent reminder notice of this right:

(1) (for any contract specified in Part II of COB 6.7.57R to which shortfall applies), no later than the end of the eighth day; and

(2) (in any other case specified in COB 7.7.7R) no later than the end of the fourteenth day;

after the contract is concluded.

(1) before the agreement is concluded (a 'pre-sale notice'); and  
(2) after the agreement has been concluded (a 'post-sale notice').

6.7.31 R When the *customer* is a trustee who is reasonably believed by the *firm* to be expected to act on the instructions of the individual beneficiary or purchaser of the *policy* or contract, the *firm* must send a copy of the notice of the right to cancel in COB 6.7.30R *post-sale notice* to:

...

Pre-sale notices

6.7.32 R ~~[deleted]~~ A *pre-sale notice* must contain at least a summary of the information required in a *post-sale notice*.

6.7.33 G ~~[deleted]~~ The following is an example of the type of summary statement which *firms* could use: 'You will be able to cancel your [investment]/ [contract] during a two-week period after concluding the agreement and receive a refund [in full / less a deduction for shortfall to reflect any fall in the markets in the interim]. You will be told of this right in more detail (including when it begins and ends, and how to exercise it) in documents that we will send you at the

relevant time.‘

Post-sale notices: general

6.7.34 R ~~[deleted]~~ A *post-sale notice* must be:

- (1) ~~In writing;~~
- (2) ~~given to the customer:~~
  - 
  - (a) ~~(for any investment agreement specified in Part II of COB 6.7.57R to which *shortfall* applies), no later than the end of the eighth day; and~~
  - (b) ~~(in any other case specified in COB 6.7.7R), no later than the end of the fourteenth day;~~

~~After the agreement is concluded;~~

- (3) ~~sufficiently clear, prominent (see COB 6.7.39R) and informative to enable the customer to exercise the right to cancel; and~~
  -
- (4) ~~accompanied by a slip or form (or an electronic equivalent) to enable the customer to exercise a right to cancel.~~

Post-sale notices: method of sending

6.7.35 R ~~[deleted]~~ A *post-sale notice* must be sent by *post*, or electronically, except in the case of an *industrial assurance policy*, when it may, instead, be given to the *customer* by hand.

Post-sale notices: content

6.7.36 R ~~[deleted]~~ A *post-sale notice* must state:

- (1) ~~That there is an agreement between the customer and the firm;~~
- (2) ~~That there is a right to cancel the agreement;~~
- (3) ~~the duration of the right to cancel and the date at which the right begins and ends;~~
- (4) ~~the steps the customer must take to cancel the agreement;~~
- (5) ~~the consequences of cancelling the agreement, including a prominent statement of any *shortfall* (see COB 6.7.54R) which the customer will have to bear;~~
- (6) ~~(as a prominent reminder) that the customer is entitled to key features and is advised to check with the firm if the key features have not been received (except in the case of *pure protection*~~

*contracts*); and

- (7) That the *customer's* right to cancel will remain unaffected if any contingency beyond the *customer's* control arises which makes it impracticable for the *customer* to communicate his wish to cancel (see *COB 6.7.28R*).

Post sale notices: ISAs

- 6.7.37 R ~~[deleted] In the case of ISAs, a firm must ensure that the slip or form in COB 6.7.34R(4) (1) will enable the customer to indicate whether the entire ISA agreement is to be cancelled or just a particular component or product.~~
- 6.7.38 G ~~[deleted] For example, in the case of a maxi-ISA, the customer:~~
- (1) has to be able to cancel at the component (or underlying product) level and is not compelled to cancel other components (or products);
- (2) needs to know that the effect of cancelling the last component has the effect of cancelling the entire ISA agreement and may also (where it is the case) delay the customer from entering into another ISA agreement until the next tax year.

Prominence of post-sale notice

- 6.7.39 R ~~[deleted] To comply with COB 6.7.34R(3), where the post-sale notice forms part of another document or is one of a number of documents sent to the customer at the same time, a firm must ensure that the presence of the post-sale notice is drawn to the customer's attention (see COB 6.7.40G).~~
- 6.7.40 G ~~[deleted] Where the post-sale notice forms part of a brochure or is included in a pack of documents, the front of the brochure or pack should prominently feature words such as: 'IMPORTANT: information about your right to cancel this agreement is enclosed'.~~

Failure to send post-sale notice give information on cancellation rights

- 6.7.41 R G If a firm does not send a *post-sale notice* when required by these rules give a retail customer information about his cancellation rights in accordance with COB App 1.1.1R(17), the contract remains cancellable and the retail customer can cancel the agreement at any time within two years of the agreement and will not be liable for any shortfall (see COB 6.7.56R(31)).

Exercising the right to cancel

- 6.7.42 R A retail customer who has a right to cancel under *COB 6.7.7R* may, without giving any reason, cancel the agreement contract by serving



notice upon the *firm*, before expiry of the relevant cancellation period either:

- (1) by post to the *firm*'s last known address; or
- (2) in accordance with any other practical instructions for exercising that right provided to the *customer* in accordance with COB App 1.1.1R (17)(b).

6.7.43 R ~~[deleted] Notice of cancellation is valid if sent by post or in any other manner that the *firm* has told the *customer* is acceptable.~~

#### ~~Valid notice of cancellation~~

- 6.7.44 R (1) ~~A notice of cancellation given by a *retail customer* is valid when it is served on, or otherwise sent by post to the *firm*'s last known address, addressed to the *firm*, its *appointed representative* or on any agent of the *firm* with authority to accept notice on the *firm*'s behalf.~~
- (2) ~~A *firm* must treat any notice of cancellation sent by prepaid post, or otherwise sent, and valid in accordance with COB 6.7.43R and COB 6.7.44R(1), as being served on the date it was posted or sent. Where the notice of cancellation is in a  durable medium  and served in accordance with COB 6.7.42R, it must be treated as being served on the *firm* on the date it is despatched by the *retail customer*.~~

...

6.7.46 G In the event of any dispute, unless there is clear written evidence to the contrary, the *firm* should treat the date cited by the *customer* as being the date when the notice was given, posted or otherwise sent.

...

6.7.48 R If a *firm* has provided information on cancellation rights in accordance with COB App 1.1.1R(17), ~~sent a *post sale notice*~~, it need not (unless COB 6.7.11R applies) accept a notice of cancellation if it is served later than the period specified for that agreement contract in COB 6.7.10R.

...

#### Effects of cancellation

6.7.51 R By exercising a right to cancel under COB 6.7.7R(1), (2) or (4), the *retail customer* withdraws from the investment agreement contract and:

- (1) the entire agreement contract; or
- (2) the particular ISA component (~~see COB 6.7.37R~~); or

(3) the variation alone (see *COB* 6.7.23R(1));

is ~~rescinded~~ terminated.

Automatic cancellation of an attached distance contract

6.7.51A G Regulation 11 (Automatic cancellation of an attached distance contract) of the *Distance Marketing Regulations*, has the effect that when notice of cancellation is given in relation to a contract, that notice also operates to cancel any attached distance financial services contract which does not fall within one of the exceptions to the right to cancel in regulation 10. So the attached contract will not be cancelled if the price of the service depends on fluctuations in the financial market outside the *firm's* control or if performance of the contract has been fully completed by both parties at the consumer's express request.

6.7.52 R When a *retail customer* exercises a right to cancel under *COB* 6.7.7R(1), (2), (3) or (4):

(1) the *firm* must:

(a) pay to the *retail customer* (or, in the case of a *pension transfer* or *pension annuity*, for the benefit of the *retail customer*) without delay, and no later than 30 days after the date on which the *firm* received notice of cancellation from the *retail customer*, any sums which the *customer* has paid to or for the benefit of the *firm* in connection with the ~~agreement~~ contract (including sums paid by the *retail customer* to agents of the *firm*) except for the amount referred to in (b);

(b) subject to (c), the *firm* is permitted to require the *retail customer* to pay for the services it has actually provided in connection with the contract; the amount payable, however, must be in accordance with the sums which the *retail customer* agreed to pay and must not:

(i) exceed an amount which is in proportion to the extent of the service already provided to the *retail customer* by the *firm*; and

(ii) be such that it could be construed as a penalty;

(c) sub-paragraph (b) applies only if:

(i) the contract is a *distance contract* within *COB* 6.7.17R, Row 1, case D (Distance contracts for certain designated investment business or accepting deposits);

(ii) where performance of the contract has

commenced before expiry of the cancellation period, this was requested by the *retail customer*; and

(iii) the *firm* can demonstrate that the *retail customer* was provided with details of the amount which he may be required to pay if exercising his right to cancel in accordance with COB App 1.1.1R(17)(a).

(2) The *firm* is entitled to receive without delay, and no later than 30 days after the date on which the *customer* posted or otherwise sent notice of cancellation to the *firm*:

(a) any sums or property or both that became the *customer's* under the contract; and

(b) payment of any *shortfall* due under COB 6.7.54R.

and the *firm* is entitled to receive:

(1) Any property that became the *customer's* under the agreement contract; plus

(2) Any sum which the *firm* has paid under the agreement contract; plus

(3) (subject to COB 6.7.56R) any *shortfall* due under COB 6.7.54R.

...

Shortfall where there is a right to cancel a non-distance contract

6.7.54 R If a *firm* has sent a post-sale notice that satisfies the rules in COB 6.7 and the market falls during the cancellation period, sSubject to COB 6.7.56R, the *firm* is entitled under COB 6.7.52R(2)(b) to charge the *retail customer* for the market loss (that is, *shortfall*), calculated in accordance with COB 6.7.58R, which the *firm* would incur in cancelling any contract investment agreement specified in COB 6.7.57R.

Shortfall: worked example

6.7.55 G COB 6.7.58R illustrates the process that *firms* need to undertake in order to discover the amount (that is, *shortfall*) by which the purchase price paid by the *retail customer* is greater than the purchase price prevailing when the *firm* becomes aware that the *retail customer* has cancelled. EXAMPLE: In the case of dual-priced *investments*, the *shortfall* on cancellation is calculated on an offer-to-offer basis; for example, 1,000 *units* are purchased at an offer price of 209.1p and the offer price is (or, in the case of a *forward price*, is subsequently ascertained to be) 196.2p as at the time when the *firm* became aware that notice of cancellation had been served by the *retail customer*. The *shortfall* on cancellation, therefore, is  $(209.1 - 196.2) = (12.9p \times 1,000) = \text{£}129$ .

Exceptions to shortfall

6.7.56 R A *firm* will have no right to charge a *retail customer* for any shortfall which results from the customer having exercised a right to cancel in any of the following circumstances:

- (1) if the *firm* ~~does not give the *customer* sends the~~ notice of his cancellation rights pre-sale notice, or the post-sale notice, as later than required by the rules in COB App 1.1.1R (17) (whether the *retail customer's* cancellation notice is valid or not);
- (2) if the *firm* fails to make any prominent mention of *shortfall* in the information about cancellation pre-sale or post-sale notice;
- (3) if the *firm* has failed to send a *post-sale reminder* notice as required by COB 6.7.30R (2);
- (4) if the *customer* has served the cancellation notice before the contract agreement is concluded.

6.7.57 R Table: Contracts Investment agreements which are subject to shortfall  
This table belongs to COB 6.7.54R

Investment agreements which are subject to shortfall	
Part I: any <u>contract investment agreement</u> specified in row <del>column</del> 1 of COB 6.7.15R (unless note 1 applies):	
...	
Part II: any <u>contract investment agreement</u> specified in row <del>column</del> 1 of COB 6.7.17R (unless note 2 applies):	
...	
Notes:	
<i>Shortfall</i> does not apply to any <u>contract investment agreement</u> which is established at the outset:	
...	

6.7.58 R Table: Calculation of shortfall  
This table belongs to COB 6.7.54R

Calculation of shortfall	
A <i>firm</i> must calculate <i>shortfall</i> as at the 'relevant date' (see note 1) as follows:	
...	

Calculation of shortfall	
B.	take the equivalent payment that would have been quoted (see notes 3, 4 and 5) to the same <i>retail customer</i> assuming an identical purchase was made at the 'relevant date';
C.	add to the figure at B the amount of any income included in the figure at A (but originally excluded from the figure at B for the purposes of distribution to <i>retail customers</i> ); and
...	
Notes:	
...	
2. If the agreement is a variation of a previous <b>agreement contract</b> (see <i>COB 6.7.23R</i> ), the <i>firm</i> must treat the increase in <i>premium</i> as the sum in A.	
...	

...

6.8.3 R A *firm* must ensure that, before entering into a *pure protection contract* with a *client*, it provides the *client* with the information specified in *COB 6.5.49R*, unless at the time of application, the *client*, other than an *EEA ECA recipient*, is *habitually resident*:

(1) (except for a *distance contract* with a *retail customer*) in an *EEA State* other than the *United Kingdom*; or

...

...

6.8.12 R Before entering into a *general insurance contract* with an individual when the *United Kingdom* is the *State of the risk* or the individual is an *EEA ECA recipient*, a *firm* must, subject to *COB 6.8.13* and *COB 6.8.13A* provide the individual with:

...

...

6.8.13A R *COB 6.8.12R* does not apply if the contract is a *distance contract* with a *retail customer* who is not present in the *United Kingdom*.

...

10 Operators of collective investment schemes

10.6.1 G Except in relation to a *distance contract* with a *retail customer* for the sale or purchase as *principal* of units in a *scheme* (for which see *COB 4.2.5R* and *COB 4 Ann 1R(6)(c)*), *COB 10.6.2R* fulfils the purpose of the *terms of business* (including the *client agreement*) requirements (see *COB 4.2*) in the context of an *unregulated collective investment scheme* by application of content requirements in scheme documents.

...

...

After COB 12, insert the following new Appendix:

COB Appendix 1 Required information for certain terms of business, key features and direct offer financial promotions

1.1.1 R Table Required information

This table belongs to COB 3.9.6R, COB 4.2.10R, COB 6.2.16R, COB 6.2.18R, COB 6.4.13R, COB 6.4.25R, COB 6.4.27R and COB 6.5.2R(6), COB 6.5.42R to COB 6.5.44R.

<b>Required information</b>	
The supplier	
(1)	The name and the main business of the <i>firm</i> , the geographical address at which it is established and any other geographical address relevant to the <i>customer's</i> relations with the <i>firm</i> .
(2)	Where the <i>firm</i> has a representative established in the <i>customer's</i> EEA State or other country of residence, the identity of that representative and the geographical address relevant to the <i>customer's</i> relations with him.
(3)	Where the <i>customer's</i> dealings are with any professional other than the <i>firm</i> , the identity of that professional, the capacity in which he is acting with respect to the <i>customer</i> , and the geographical address relevant to the <i>customer's</i> relations with that professional.

## Required information

(4)	<p>(a) For <i>authorised persons</i>:</p> <ul style="list-style-type: none"> <li>(i) the required disclosure statement in <i>GEN 4 Ann 1R</i> (Statutory status disclosure); and</li> <li>(ii) the fact that the <i>person</i> is entered on the <i>FSA Register</i> and his <i>FSA</i> registration number.</li> </ul> <p>(b) For <i>unauthorised persons</i>:</p> <ul style="list-style-type: none"> <li>(i) where the <i>person's</i> activity is subject to an authorisation scheme, the particulars of the relevant supervisory authority; and</li> <li>(ii) where the <i>person</i> is registered in a trade or similar public register, the trade register in which the <i>person</i> is registered and his registration number or an equivalent means of identification in that register.</li> </ul>
The financial service	
(5)	A description of the main characteristics of the service the <i>firm</i> will provide.
(6)	The total price to be paid by the <i>customer</i> to the <i>firm</i> for its services, including all related fees, charges and expenses, and all taxes paid through the <i>firm</i> or, where an exact price cannot be indicated, the basis for the calculation of the price enabling the <i>customer</i> to verify it.
(7)	Notice of the possibility that other taxes or costs may exist that are not paid through the <i>firm</i> or imposed by it.
(8)	Details of any specific additional cost to the <i>customer</i> for using a <i>means of distance communication</i> .

**Required information**

(9)	Where relevant, notice indicating that the service involves special risks related to its specific features or the operations to be executed or whose price depends on fluctuations in the financial markets outside the <i>firm's</i> control and that past performance is no indicator of future performance.
(10)	Any limitations of the period for which the information provided is valid.
(11)	The arrangements for payment and performance.
The contract	
(12)	In relation to services performed permanently or recurrently, the minimum duration of the contract.
(13)	The <i>EEA State</i> or <i>States</i> whose laws are taken by the <i>firm</i> as a basis for the establishment of relations with the <i>retail customer</i> prior to the conclusion of the contract.
(14)	Any contractual clause on law applicable to the contract or on competent court, or both.
(15)	The language in which the contract is supplied and in which the <i>firm</i> will communicate during the course of the contract.
(16)	Information on any rights the parties may have to terminate the contract early or unilaterally under its terms, including any penalties imposed by the contract in such cases.



## Required information

(17)	<p>The existence or absence of a right to cancel under <i>COB 6.7</i> and, where there is such a right:</p> <ul style="list-style-type: none"><li data-bbox="469 353 1334 613">(a) its duration and the conditions for exercising it, including information on the amount which the <i>customer</i> may be required to pay (or which may not be returned to the <i>customer</i>) in accordance with <i>COB 6.7.52R(1)(b)</i>, as well as the consequences of not exercising it; and</li><li data-bbox="469 636 1334 837">(b) practical instructions for exercising the right to cancel, including as a minimum the method in <i>COB 6.7.42R(1)</i> and details of the address to which any cancellation notice should be sent.</li></ul>
Redress	
(18)	<p>How to complain to the <i>firm</i>, whether or not complaints may subsequently be referred to the <i>Financial Ombudsman Service</i> and information about any other applicable named complaints scheme.</p>
(19)	<p>Whether or not compensation may be available from the <i>compensation scheme</i> should the <i>firm</i> be unable to meet its liabilities, and information about any other applicable named compensation scheme; and, for each applicable scheme, the extent and level of cover and how further information can be obtained. (See the example in <i>COB 5.5.11 G</i> (Investment firms: compensation information)).</p>

## Annex B

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### ICOB Transitional provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
5	<i>ICOB 4.7.1R and ICOB 8.4.1R</i>	G	<i>ICOB 4.7.1R and ICOB 8.4.1R apply equally to contracts sold before 14 January 2005 and which come up for <i>renewal</i> after that date as they do to contracts newly entered into after 14 January 2005. <i>Firms</i> may, if they wish, get consent for future <i>renewals</i> when the contract is first sold or at the next <i>renewal</i>.</i>		
...					

...

- 4.7.1 R ~~Unless Subject to ICOB 4.7.2R applies,~~ an *insurance intermediary* or an *insurer* must not, in relation to a *non-investment insurance contract* that is a *distance contract*:
- (1) *advise on, arrange, enter into, ~~renew,~~ carry out or assist in the administration and performance* of such a contract for a *retail customer* without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or
  - (2) enforce any obligation against a *retail customer* in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.

- 4.7.2 R *ICOB 4.7.1R does not prevent an insurance intermediary or an insurer from exercising any right that he may have, by contract or otherwise, to renew a distance contract with a retail customer without any request made by or on behalf of that retail customer prior to the renewal of the contract apply for a tacit renewal of a distance contract.*
- 4.7.3 G (1) ~~ICOB 4.7.1R(1) prohibits an insurance intermediary (or an insurer when acting as product provider) from advising on, arranging, entering into, renewing, carrying out or assisting in the administration and performance of a non-investment insurance contract that is a distance contract for a retail customer without the prior consent of that retail customer. This prohibition in ICOB 4.7.1R includes the continuation of insurance after a specified period where the insurance has been free of charge to the retail customer during that period unless the retail customer has agreed before the period expires to pay for the insurance once the period has expired.~~
- (2) ~~Where the payment for the contract is made by regular instalments (for example, by direct debit), the effect of ICOB 4.7.2R is that an insurance intermediary (or an insurer when acting as product provider) will be required to seek the retail customer's consent on renewal to continue to provide insurance only if the contract does not give it the right to do so without further reference to the retail customer.~~
- (3) ~~The prior consent of the retail customer can either be express, or deduced from the circumstances of the case (for instance, by the retail customer providing an updated direct debit mandate to the firm).~~
- ...
- 8.4.1 R ~~Unless Subject to ICOB 8.4.2R applies, an insurance intermediary must not, in relation to a distance non-investment mediation contract:~~
- (1) ~~advise on, arrange, enter into, renew, carry out or assist in the administration and performance of such a contract for a retail customer without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or~~
- (2) ~~enforce any obligation against a retail customer in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.~~
- 8.4.2 R *ICOB 8.4.1R does not prevent an insurance intermediary from exercising any right that he may have, by contract or otherwise, to renew a distance non-investment mediation contract with a retail customer without any request made by or on behalf of that retail customer prior to the renewal of the contract apply for a tacit renewal of a distance non-investment mediation contract.*

- 8.4.3 ~~G[deleted]~~ (1) Where the payment for the contract is made by regular instalments (for example, by direct debit), the effect of *ICOB* 8.4.2R is that an *insurance intermediary* will be required to seek the *retail customer's* consent on *renewal* to continue to provide mediation services only if the contract does not give him the right to do so without further reference to the *retail customer*.
- (2) The prior consent of the *retail customer* can either be express, or deduced from the circumstances of the case (for instance, by the *retail customer* providing an updated direct debit mandate to the *firm*).

## Annex C

### Amendments to the Mortgages: Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 4.5.4 R ~~Unless~~ Subject to MCOB 4.5.5R ~~applies~~, a *firm* must not:
- (1) *advise on, arrange, or enter into, or renew a distance mortgage mediation contract with a retail customer without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or*
  - (2) *enforce any obligation against a retail customer in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.*
- 4.5.5 R *MCOB 4.5.4R does not prevent an firm from exercising any right that he may have, by contract or otherwise, to renew a distance contract with a retail customer without any request made by or on behalf of that retail customer prior to the renewal of the contract* apply for a tacit renewal of a distance contract.

## Annex D

### Amendments to the Market Conduct sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

3.1.3 R This chapter does not apply to the carrying on of the following activities:

...

(3) *corporate finance business*; ~~or~~

(4) ~~Ssafeguarding and administering investments and agreeing to carry on that regulated activity~~; or

(5) concluding a distance contract with a retail customer.

## Annex E

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 5 Ann 3 G

...

#### 2 Table: G

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
...		
<i>COB</i>	<i>COB</i> applies.	<p>Where the activity:</p> <p>(1) <u>(a)</u> would fall within the <i>overseas persons</i> exclusions in article 72 of the <i>Regulated Activities Order</i>; or</p> <p><del>(b2)</del> would not be regarded as carried on in the <i>United Kingdom</i>; or</p> <p><del>(c3)</del> is not carried on with or for a <i>client</i> in the <i>United Kingdom</i>;</p> <p>then only the following apply:</p> <p><del>(d4)</del> <i>COB</i> 3 (Financial promotion), but see the territorial scope in <i>COB</i> 3.3 (Where?);</p> <p><del>(e5)</del> <i>COB</i> 5.5.7R and <del><i>COB</i> 5.5.8R</del> (Overseas business); and</p> <p><del>(f6)</del> <del><i>COB</i> 6.6 to <i>COB</i> 6.12, <i>COB</i> 6.7 and <i>COB</i> 6A.8 (Contents of key features, stakeholder pension schemes decision trees, Cancellation and withdrawal, Insurance contracts: life and general)</del> <u>certain parts of <i>COB</i> 6 (Product disclosure and the</u></p>

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
<p>...</p> <p>ECO</p> <p>...</p>	<p>ECO 2 applies if the <i>firm</i> is an <i>outgoing ECA provider</i>, ECO 3 applies if the <i>firm</i> is a <i>domestic ECA provider</i>, ECO 1 does not apply.</p>	<p><u>customer's right to cancel or withdraw</u>) but only in relation to <i>long-term insurance business</i> carried on with a <i>customer</i> habitually resident in the <i>United Kingdom</i> or if the <i>State of the risk</i> is the <i>United Kingdom</i> (see COB 1.4.7R and COB 1.4.8R) ;</p> <p>(2) <u>concerns a distance contract and is carried on with retail customers in the United Kingdom from an establishment maintained by the firm in an EEA State which:</u></p> <p>(a) <u>has implemented the DMD; or</u></p> <p>(b) <u>has obligations in its domestic law corresponding to those provided for by the DMD;</u></p> <p><u>COB 4.2, COB 5, and COB 6 do not apply.</u></p> <p>Otherwise, as column (2), (see COB 1.4.3R).</p> <p>ECO 1 applies if the <i>firm</i> is an <i>incoming ECA provider</i> <u>except for ECO 1.2.1R which does not apply if:</u></p> <p>(a) <u>the electronic commerce activity is not insurance business which:</u></p> <p>(i) <u>satisfies the conditions in ECO 1.2.3R; and</u></p> <p>(ii) <u>is carried on by an insurer; and</u></p> <p>(b) <u>the EEA State from which the activity is provided has implemented the DMD with the</u></p>



<b>(1) Module of Handbook</b>	<b>(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom</b>	<b>(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom</b>
		<p><u>result that the obligations provided for by the <i>DMD</i> are applied when the <i>incoming ECA provider</i> is carrying on the activity from an <i>establishment</i> in that State with a <i>UK ECA recipient</i> in the <i>United Kingdom</i>.</u></p> <p><i>ECO 2</i> and <i>ECO 3</i> do not apply.</p>

## Annex F

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place that it goes is indicated and the text is not underlined.

- 11.1.2 G (1) The *rules* and *guidance* set out in *COB* mainly apply to *designated investment businesses* and, as stated in *COB* 1.3.2G(2), have limited application to *deposits*.
- (2) The only parts of *COB* that sets out *rules* and *guidance* on *deposits*, other than for a cash deposit ISA, is that are those relating to *financial promotion* in *COB* 3 and those relating to distance contracts for accepting deposits in *COB* 2.6 (General provisions related to distance contracts), *COB* 6.7 (Cancellation and withdrawal) and *COB* 6.4.25R (Entering into a distance contract for accepting deposits). Guidance on the way in which those requirements apply to credit unions is set out in *CRED* 11.2 (Financial promotion) and *CRED* 11.4 (Entering into a distance contract for accepting deposits). These are summarised in *CRED* 11.2 (Financial Promotion).

...

- 11.2.1 G ~~The only part of *COB* that sets out *rules* and *guidance* on *deposits* other than a *cash deposit ISA* is that relating to *financial promotion* in *COB* 3. *Financial promotion* is defined as an invitation or inducement to *engage in investment activity*.~~

...

After *CRED* 11.3, insert the following new section:

- 11.4 Entering into a distance contract for accepting deposits
- 11.4.1 G Those parts of *COB* that relate to *distance contracts* for *accepting deposits* will have limited application to *credit unions*. This is because the *DMD* only applies where there is “an organised distance sales or service-provision scheme run by the supplier” (Article 2(a)). If, therefore, the *credit union* normally operates face-to-face and has not set up facilities to enable *customers* to deal with it at a distance, such as facilities for a *customer* to deal with it purely by post, telephone, fax or the Internet, the provisions will not be relevant. A one-off transaction dealt with by distance means in order to deal with a particular contingency or emergency will not fall under the *COB* provisions.
- 11.4.2 G For those *credit unions* to which the provisions in *COB* will apply, the provisions which are of particular relevance concern the general provisions (*COB* 2.6), pre-contract information (*COB* 6.4.25R), cancellation rights

(COB 6.7) and financial promotion (discussed at CRED 11.2). If the *credit union* provides *cash deposit ISAs* further rules may apply.

#### Pre-contract disclosure requirements

- 11.4.3 G *COB 6.4.25R* sets out the basic requirement that applies before a *credit union* enters into a *distance contract* for *accepting deposits*. The *credit union* has to ensure that the terms on which it will conduct business, including, in particular, certain required information, is provided to a *retail customer* (which means an individual, acting for purposes which are outside his trade, business or profession) in good time (that is, in sufficient time to enable a *customer* to consider properly the services on offer) in a *durable medium*, before the *retail customer* is bound by the *distance contract*, unless certain exemptions apply.
- 11.4.4 G The required information is the contractual terms and conditions and the other information set out in *COB App 1*, and covers basic information about the *credit union*, the main characteristics of the service on offer, the price, details about the *distance contract* such as its duration, cancellation rights and any other early termination rights and penalties, and information about out-of-court complaints and compensation arrangements.

#### Exemptions

- 11.4.5 G The exemptions referred to in *CRED 11.4.3G* are set out in *COB 6.4.25R*. They are relevant:
- (1) where the contract is concluded by telephone and the *retail customer* gives explicit consent to receiving a more limited range of information. *COB 6.4.27R* sets out the information to be provided in such cases. Full information has to be provided, in a *durable medium*, immediately after conclusion of the *distance contract* (*COB 6.4.25R(2)*);
  - (2) where a means of communication (other than telephone) is used which does not enable provision of the required information in a *durable medium* before conclusion of the contract; in this case full information must also be provided in a *durable medium* immediately after conclusion of the *distance contract* (*COB 6.4.25R(3)*);
  - (3) where there is an initial service agreement and the contract is in relation to a successive or separate operation of the same nature under that agreement, or there is no initial service agreement and the contract is in relation to a successive or separate operation of the same nature and is being performed no more than one year from the date of performance of the last operation (see *COB 1.10.2G*).
- 11.4.6 G The other provisions in *COB* which relate to the disclosure requirements and are of relevance to *credit unions* entering into a *distance contract* for *accepting deposits* are in *COB 2.6* (General provisions related to distance contracts). *COB 1.11.2R* (Exemption for firms which follow the Banking

Code Guidance) would be relevant if a *credit union* came within its scope and subscribed to the Banking Code Guidance.

#### Cancellation

11.4.7G *A retail customer* has a right to cancel a *distance contract* for accepting deposits without giving any reasons and without penalty. The right to cancel has to be exercised within 14 days of the day of the conclusion of the contract or the day on which he received the contractual terms and conditions, if later (COB 6.7.10R).

11.4.8G The only exemptions from the right to cancel are when:

- (1) the price of the service depends on fluctuations in the financial market outside the *credit union's* control which may occur during the cancellation period; or
- (2) the contract has already been fully performed with the *retail customer's* consent before he exercises his right to cancel; or
- (3) the *credit union* has an initial service agreement with the *retail customer* and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see COB 1.10.2G).

11.4.9G The effects of cancellation are set out in COB 6.7.51R to COB 6.7.52R. The *credit union* has to return, no later than 30 days after the date it received notice of cancellation, any sums paid by the customer in connection with the contract. The *customer* can be required to pay for any services provided up to the date of cancellation, provided that the sums payable are in proportion to the extent of the service actually provided and could not be construed as a penalty. No payment can be required if the *credit union* cannot prove that a *customer* was told the amount that would be payable as part of the pre-contract information or if the *credit union* starts performance of the contract without the *customer's* prior consent.

11.4.10G If there are other ancillary *distance contracts* related to the first, those ancillary contracts may also be cancelled automatically when a *retail customer* exercises a right to cancel (see COB 6.7.51R).

11.4.11G This *guidance* is not a substitute for, and should be read in conjunction with, the requirements contained in the relevant parts of COB.

...

Appendix 2.1  
Detailed content of CRED

2.1.1 P Table:

...	
<i>11</i>	Conduct of business <i>11.1</i> Introduction <i>11.2</i> Financial promotion <i>11.3</i> Statutory status disclosure <i>11.4</i> <u>Entering into a distance contract for accepting deposits</u>
...	

## Annex G

### Amendment to the Electronic Commerce Directive sourcebook

In this Annex, underlining indicates new text.

#### Exceptions: regulated mortgage contracts

1.2.4A R ECO 1.2.1R does not apply to an incoming ECA provider with respect to an electronic commerce activity which relates to a regulated mortgage contract.

...

#### Exception: activities (other than insurance) from EEA States which have implemented the DMD

1.2.5A R ECO 1.2.1R does not apply to an incoming ECA provider with respect to an electronic commerce activity, if the following conditions are satisfied:

- (1) the activity is not insurance business which:
  - (a) satisfies the conditions in ECO 1.2.3R; and
  - (b) is carried on by an insurer; and
- (2) the EEA State from which the activity is provided has implemented the DMD with the result that the obligations provided for by the DMD are applied when the incoming ECA provider is carrying on the activity from an establishment in that State with a UK ECA recipient in the United Kingdom.

## Annex H

### Amendments to the Professional firms sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 5.1.2 G This chapter:  
...
- (2) ...; ~~and~~
- (3) ... ;
- (4) gives effect to the *Distance Marketing Regulations* with respect to the *non-mainstream regulated activities of authorised professional firms*.

...

- 5.3.2 G *COB 1.2.1R(4)* provides that *COB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for *COB 2.1* (Clear, fair and not misleading communication), *COB 3* (Financial promotion) and *COB 4.2.1R* to *COB 4.2.6G*, ~~*COB 4.2.9R*~~ to ~~*COB 4.2.11E*~~ and ~~*COB 4.2.15E(26)*~~ (Terms of business and client agreements with customers) *COB 4.2.12AE* and *COB 4 Ann 2E(25)* (Content of terms of business).

...

#### 5.4 Application of the Distance Marketing Regulations

- 5.4.1 R (1) An authorised professional firm must, with respect to its non-mainstream regulated activities, comply with regulations 6 to 10, 14 to 15(2) and 16 to 20 of the *Distance Marketing Regulations* and those regulations have effect to cancel *distance contracts* the making or performance of which by such firms constitutes a *non-mainstream regulated activity*.
- (2) Paragraph (1) does not apply in relation to regulations 6 to 7 and 14 to 15(2) if the designated professional body of the authorised professional firm has rules equivalent to those regulations and:
- (a) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and
- (b) the authorised professional firm is subject to those rules in the form in which they have been approved.

- 5.4.2 G The effect of *PROF 5.4.1R* is that it allows *designated professional bodies* to make rules which allow an *authorised professional firm* to comply with the *Distance Marketing Regulations* in respect of its *non-mainstream regulated activities* in the same way as an *exempt professional firm* which is a member of the same *designated professional body* in respect of its *exempt regulated activities*.

## Annex I

### Amendments to the Electronic money sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Distance marketing activities

- 1.1.5 G (1) *ELM 1.4A* sets out certain minimum requirements under the *Distance Marketing Directive* in respect of a *customer's* cancellation rights. These *rules* are supplemented by the requirements in *COB 6.7.42R* (Exercising the right to cancel); *COB 6.7.47R* (Record keeping); *COB 6.7.48R* (Cancellation notices served out of time) and *COB 6.7.51R* to *COB 6.7.53R* (Effects of cancellation) which all apply to *e-money firms*.
- (2) As set out in *ELM 6.8*, *COB 6.4.25R* applies to *e-money firms* as if references to '*issuing deposits*' and '*deposits*' were references to '*issuing e-money*' and '*e-money*' respectively.

...

After *ELM 1.4*, insert the following new section:

1.4A Distance contracts: cancellation

#### Right to cancel

1.4A.1 R A *retail customer* has a right to cancel a *distance contract* the making or performance of which by the *firm* constitutes, or is part of, *issuing e-money* unless:

- (a) the performance of the *distance contract* has been fully completed by both parties at the *customer's* express request before the *customer* exercises his right to cancel; or
- (b) the *firm* has an initial service agreement with the *customer* and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see *COB 1.10.2G*).

#### Cancellation period

1.4A.2 R The right to cancel referred to in *ELM 1.4A.1R* starts on the later of:

- (a) the day of the conclusion of the contract; and
- (b) the day on which the *retail customer* receives the contractual terms and conditions and other information required by *ELM 6.8* (Information);

and lasts for 14 calendar days.



Failure to give information on cancellation rights

1.4A.3 R If a *firm* does not give a *retail customer* notice of his cancellation rights in accordance with *ELM* 6.8.2AR and *COB* 6.4.25R, the contract remains cancellable and the *retail customer* can cancel the agreement at any time.

Exercising the right to cancel

1.4A.4 R A *retail customer* may, without giving any reason, cancel the contract by serving notice upon the *firm*, before expiry of the relevant cancellation period, in accordance with the instructions for exercising that right provided to the *customer* in accordance with *ELM* 6.8.2AR and *COB* 6.4.25R.

1.4A.5R The following *rules* also apply as if *issuing e-money* were *accepting* deposits: *COB* 6.7.47R (Record keeping); *COB* 6.7.48R (Cancellation notices served out of time) and *COB* 6.7.51R to *COB* 6.7.53R (Effects of cancellation).

...

1.5.2 G

Table: Application of other parts of the Handbook to ELMIs

Block	Module	Application
...		
Block 2 (Business Standards)	...  Conduct of Business sourcebook (COB)	...  <u>The effect of :</u>  <u>(1) <i>ELM</i> 6.8.2AR is that <i>COB</i> 2.6 (General provisions in relation to distance contracts) applies;</u>  <u>(2) <i>ELM</i> 1.4A.5R is that <i>COB</i> 6.7.47R; <i>COB</i> 6.7.48R and <i>COB</i> 6.7.51R to <i>COB</i> 6.7.53R apply; and</u>  <u>(3) <i>ELM</i> 6.8.2AR is that <i>COB</i> 6.4.25R (Entering into a distance contract for accepting deposits) applies in relation to <i>distance contracts</i> concluded with <i>retail customers</i> as if references to '<i>accepting deposits</i>' and '<i>deposits</i>' were references to '<i>issuing e-money</i>' and '<i>e-money</i>' respectively.</u>  <u>Otherwise, <i>COB</i> does not apply to an <i>ELMI</i> when issuing e-money. ...</u>

6.8 Information

6.8.1 R A *firm* must not issue *e-money* to any *person* unless that *person* has been supplied with the information in *ELM* 6.8.2R and, where appropriate, *ELM* 6.8.2AR.

...

6.8.2A R *COB* 2.6 (General provisions related to distance contracts) and *COB* 6.4.25R (Entering into a distance contract for accepting deposits) applies to a *firm* as if references to ‘*accepting deposits*’ and ‘*deposits*’ were references to ‘*issuing e-money*’ and ‘*e-money*’ respectively.

6.8.3 R The information in *ELM* 6.8.2R must be in a *durable medium* ~~writing~~ and in a readily comprehensible form.

...

6.8.7 G ~~[deleted] Firms are reminded that *GEN* 2.2.14 R says that a provision in the Handbook that refers to a document "in writing" means a document in legible form and capable of being reproduced on paper, irrespective of the medium used. Thus the information that *ELM* 6.8.3 R says must be produced in writing does not have to be produced in the form of a physical document.~~

## Annex J

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

(1) New definitions:

Insert the following new definition in the appropriate alphabetical position:

<i>distance contract</i>	any contract concerning financial services, the making or performance of which constitutes or is part of a <i>regulated activity</i> , concluded under an organised distance sales or service provision scheme run by the contractual provider of the service who, for the purpose of that contract, makes exclusive use (directly or through an intermediary) of one or more <i>means of distance communication</i> up to and including the time at which the contract is concluded.
<i>Distance Marketing Directive</i>	The Directive of the Council and Parliament of 23 September 2002 on distance marketing of consumer financial services (No 2002/65/EC).
<i>Distance Marketing Regulations</i>	The Financial Services (Distance Marketing) Regulations 2004 (SI 2004/[ ]).
<i>DMD</i>	<i>Distance Marketing Directive</i> .
<i>durable medium</i>	(a) paper; or (b) (in accordance with article 2(f) of the <i>Distance Marketing Directive</i> and article 2(12) of the <i>Insurance Mediation Directive</i> ) any instrument which enables the recipient to store information in a way accessible for future reference for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored; this includes, in particular, floppy disks, CD-ROMs, DVDs and the hard drive of the recipient's computer on which electronic mail is stored, but not Internet websites unless they fulfil the criteria in this definition.
<i>means of distance communication</i>	(in accordance with article 2(e) of the <i>Distance Marketing Directive</i> ) any means used for the distance marketing of a service between parties which does not involve the simultaneous physical presence of those parties.
<i>retail customer</i>	(in accordance with the meaning of 'consumer' in article 2(d) of the <i>Distance Marketing Directive</i> ) an individual who is acting for purposes which are outside his trade, business or profession.

(2) Amendments to current definitions in the Glossary:

Amend the following definitions as shown:

<i>inter-professional business</i>	<p>...</p> <p>(b) but excluding the carrying on of the following activities:</p> <p>...</p> <p>(v) <u>concluding a distance contract with a retail customer.</u></p> <p>...</p>
<i>private customer</i>	<p>(1) (except in <i>COB</i> 3, 4.2 and 6.4) ...</p> <p>...</p> <p>(3) <u>(in <i>COB</i> 4.2 and 6.1 to 6.5) a person in (1) and, in relation to the conclusion of a distance contract, a retail customer.</u></p>
<i>terms of business</i>	<p>a <del>written</del> statement, <del>supplied to a client,</del> <u>in a durable medium</u> of the terms <u>and conditions</u> on which a firm will conduct <i>designated investment business</i> with or for <del>the</del> <u>a client or retail customer.</u></p>

**CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT NO 17)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Conduct of Business sourcebook.
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force as follows:
  - (1) Annex A comes into force on 1 May 2004;
  - (2) Annex B comes into force on 1 June 2004.

**Amendments to the Conduct of Business sourcebook (COB)**

- D. COB is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Conduct of Business Sourcebook (Amendment No 17) Instrument 2004.

By order of the Board  
15 April 2004

## Annex A

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 6.5.8A R A *firm* must ensure that its decision trees include:
- (1) (in the place in the relevant table in the ~~introductory~~ Further information text at COB 6 Ann 1R where the square brackets appear):
    - (a) in the heading of the table, the current tax year; and
    - (b) The Basic State Pension rates and Pension Credit ~~m~~Minimum ~~i~~Income ~~G~~uarantee rates for the current tax year;
  - (2) (where the square brackets appear) at the bottom of the cover page and at the bottom of each page of the flow charts, the current tax year; and
  - (3) (where the square brackets appear) in the introductory text where additional explanatory text within Further information is signposted, the appropriate page number.

Delete existing text in COB 6 Annex 1R and replace with the following text for Decision trees for stakeholder pension schemes (as required in COB 6.5.8R): text, content and format (R).

## **COB 6 Ann 1R**

**Decision trees for stakeholder  
pension schemes (as required in  
COB 6.5.8R): text, content and  
format (R)**

## STAKEHOLDER PENSION DECISION TREES

**Decision trees provide information and help you to answer the question: “Would a stakeholder pension be a good choice for me as part of my financial planning for retirement?”**

**Decision trees are intended to help you make your own choice about your pension arrangements. They do not give you financial or professional advice and you should not regard them as doing so.**



[Insert current tax year]



## ***You need to read the following notes before using the decision tree***

***flowcharts.*** There is also more information starting on page [insert page number] that you can refer to at any stage.

### ***What is a stakeholder pension?***

A stakeholder pension is a *private pension* - it's *not a State pension*. It must meet minimum standards laid down by the Government about charges, flexibility and the regular information you must be given. The standards are designed to help ensure that all stakeholder pensions give good basic value. There's more about this in the "Further information" section on page [insert page number].

With a stakeholder pension, you can pay regular contributions, and you can also make lump-sum contributions whenever you like. Your employer can also make contributions on your behalf. You will benefit from tax relief on your own contributions – there's more about the tax advantages in the "Further information" section on page [insert page number].

Your contributions are invested to build up your own pension fund. The amount of your fund when you come to retire is not guaranteed and depends on how much has been paid in, the type of investment fund you choose and how those investments perform. A stakeholder pension scheme will usually offer you a range of investment funds, with differing degrees of investment risk and potential investment growth.

You can retire and draw your stakeholder pension benefits at any time between the ages of 50 and 75. The Government has announced plans to increase the minimum age for drawing benefits to age 55. You will need to bear this in mind when deciding on your retirement plans. You can't withdraw any money from your pension fund before you retire and take your pension.

When you retire, you can choose to take up to 25% (a quarter) of your pension fund as a tax-free lump sum. And you use the rest of your pension fund (or all of it, if you decide against a tax-free lump sum) to buy an "annuity". The annuity will pay you a regular income during your retirement. That income will depend on the size of your pension fund and annuity rates at the time you take your pension. You may have to pay tax on your annuity income.

### ***Is a stakeholder pension a good choice for me?***

You can contribute to a stakeholder pension whether you are in employment, a fixed-contract worker, self-employed, or even not working. You can get one from a bank, building society, insurance company, investment company, or through a financial adviser.

Stakeholder pensions suit a wide range of people. But they are likely to be particularly attractive to people who have no existing pension provision apart from the State pensions, such as the self-employed or any employee whose employer does not contribute to a workplace-based pension scheme. In some cases, stakeholder pensions can be used to top up the benefits provided by an employer's own scheme. But if your employer offers to match any additional voluntary contributions (AVCs) that you choose to make to his scheme, this is likely to be a better way of topping-up than through your own separate stakeholder pension.

Stakeholder pensions have many advantages for many people, but they may not be the right choice for everyone. These decision trees are intended to help you decide what would be a good choice for you.

### ***Do I need to save for my retirement through a stakeholder pension?***

To answer this question, you must make your own judgment. Will your State pensions, any existing private pensions, any employer-sponsored pensions and any other sources of income be enough for you to live on when you retire? You need to think about the standard of living you want to enjoy when you retire and the income you'll need to support it.

***Ask yourself these seven questions:***

- ***Roughly how much will I need to live on when I retire?***

Try to work out how much money you will need to live on when you have retired to afford the things you'll want and the things you'll want to do.

- ***Will I qualify for the full basic State Pension?***

If you have paid National Insurance contribution for about 90% of your working life, you are entitled to the full basic State Pension. You can get a State Pension forecast to check the amount you will get. Details of how to get a forecast are on page [insert page number].

You cannot get your basic State Pension until you reach State pension age (currently 65 for men and 60 for women). Details of how the State Pension age for women is changing are on page [insert page number].

The Government reviews the amount of the basic State Pension every year. The current rates are shown in a table under "Further information" on page [insert page number].

- ***Will I qualify for an additional pension through the State Second Pension (formerly SERPS)?***

The State Second Pension is payable when you reach State pension age, on top of the basic State Pension. The amount depends on your earnings while you were in employment and the National Insurance contributions you paid.

**Self-employed people do not qualify for the State Second Pension (formerly SERPS).**

And those employees who were "contracted-out" of the Second State Pension will not qualify for the additional pension for the period when they were contracted out. Some people will be contracted out through an employer's occupational pension scheme and some through private pension arrangements. Check with your employer or pension provider if you are not sure.

- ***Does my current employer provide a pension scheme and how much will that give me?***

Check with your employer if you are not sure about membership. If you are a member of an employer's scheme, you should get regular statements setting out what your benefits might be when you retire. If you cannot find these statements, check with your employer.

- ***Am I already contributing to a personal pension scheme or a stakeholder pension? If so, how much income will they give me?***

If you are already contributing to a personal pension or stakeholder pension, you need to find out what retirement income they might provide. Look at the most recent benefit statements you have been sent, or check with your pension plan provider.

- ***Have I got any old pensions, maybe from previous employers' schemes or from personal pension schemes? If so, how much income will they give me?***

Check on the pension plans you have contributed to in the past but no longer pay into today. You need to have some idea of the retirement income you might get from them.

To check on the value of old pension plans, look at the most recent benefit statements you have been sent. If you cannot find any statements, contact your pension plan provider, for example the insurance company or the employer that offered the pension to you.

- ***Will the Government's new Pension Credit make a difference for me?***

The Government introduced the Pension Credit from October 2003. This is designed to make sure that people aged 60 and over have a minimum income and that those aged 65 and over with modest savings get some credit for having saved. These savings could, for example, be in the form of an employer's pension, a stakeholder or other personal pension, or the State Second Pension. This is not a complete list, and you could have other savings that will count.

The Pension Credit means that, for most people, most of the time, it will pay to save. For a limited group of people, however, the decision will not be so clear-cut, and these people will have to think carefully about their personal circumstances. In particular, people in their fifties and over who have not been able to save much and have only a limited ability to save as they approach retirement should seek expert advice before they take out a stakeholder pension. See "Where to get more help" on page [insert page number].

You need to bear in mind that governments can change the rules for State pensions and benefits at any time. So it may be unwise to rely on any particular type or level of benefit being available when you retire.

There's more information about getting a forecast of your State pensions (page [insert page number]) and how to track down pensions provided by any former employers' or personal pensions (page [insert page number]).

If the income you expect in retirement is less than what you want, you need to think about saving more to make up the difference. A stakeholder pension is one of your options. But before you decide anything, you need to think about your priorities.

## ***What else should I think about before contributing to a stakeholder pension?***

You might have other financial commitments that will affect what you can afford to contribute to a stakeholder pension. Or you might feel that other financial needs must come first. For example, ask yourself:

- ***What are my other financial commitments?***

For example, mortgage repayments, rent, life assurance, and credit cards. Make sure you do your sums before thinking about a stakeholder scheme and that you would still be able to afford your other commitments.

- ***Would I be prepared, if necessary, to give up anything so that I can pay into a stakeholder pension?***

Remember that saving through a pension scheme is a long-term commitment. Any change in how you spend your money may need to last for a long time.

- ***Should I be thinking of other things first?***

For example, you might want to consider life assurance protection for you and your family, or building up some “rainy-day” cash savings before thinking about a stakeholder pension.

If you are a member of your current employer’s pension scheme, it might make sense to pay additional voluntary contributions to that scheme rather than contribute to a stakeholder scheme. And if you are currently contributing to a personal pension or stakeholder pension, it might make sense to increase your contributions to that scheme rather than start a separate stakeholder pension.

## ***How much should I contribute to my stakeholder pension?***

Contributions to stakeholder pensions can be as low as £20. But, even a regular monthly contribution of £20 over several years will not give you a large pension when you retire. And the older you are when you start saving, the less time there is for your pension fund to grow to something worthwhile.

## ***Estimated pensions in the Pension Table***

The Pension Table later on will give you a fair idea of the pension income you could get, depending on your age and contributions. **But please remember that the figures in the table are only estimates and are not guaranteed. You might get less, or you might get more.**

The pension figures are also shown before income tax. When you receive your pension during retirement you may be taxed on it.

The figures in the table are calculated on the following basis:

**Before you retire**

Your monthly contributions increase in line  
with inflation.....2.5% a year.  
Before charges, your fund grows by.....7% a year.  
Charges deducted from your fund.....1% of fund a year.

**When you retire**

Your entire fund is used to buy an annuity, and  
you do not take any tax-free lump sum.  
Annuity rates assume that the investment  
return after retirement is.....1.8% a year in excess of inflation.  
Your pension increases in line with inflation.  
Your spouse will receive half your pension on your death.

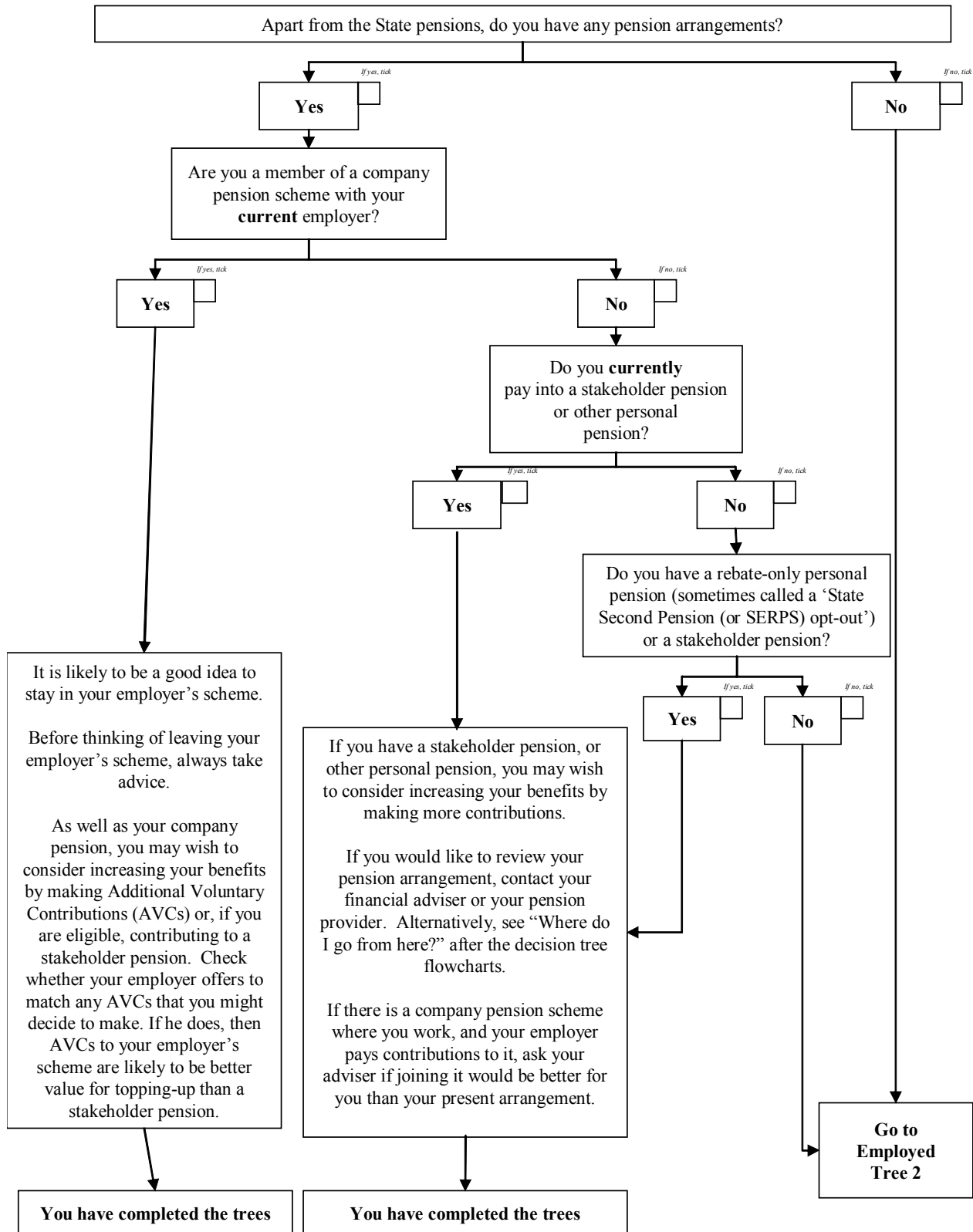
### ***How do I use the decision trees?***

- **These decision trees have been designed to help you decide whether a stakeholder pension would be a good choice for you. Please take the time to read and use them carefully, giving accurate answers to the questions. Because the decision trees do not give personalised advice, any decision you take is your own responsibility.**
- **There are separate decision trees for:**
  - **Employed people**
  - **Self-employed people**
  - **People who are not employed**
- **When you have found the right decision tree, work through the questions from the top of the page and tick the box for each question you answer.**
- **If the tree asks you about your present pension arrangements and you are not sure of the correct answer, find out the right information – don't guess.**
- **If the tree recommends you take advice, or if you are not sure what is right for you, then you should seek advice. You may have to pay for this advice.**
- **After the decision trees, you'll find further information about what to do next.**

Some of the information used in these materials comes from sources outside the FSA. The FSA does not guarantee or warrant the accuracy of the information included in these materials, and does not accept any liability for errors or omissions. The FSA shall not be liable for any damages arising from any action or decision taken as a result of using these materials or any of them.

*This information is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.*

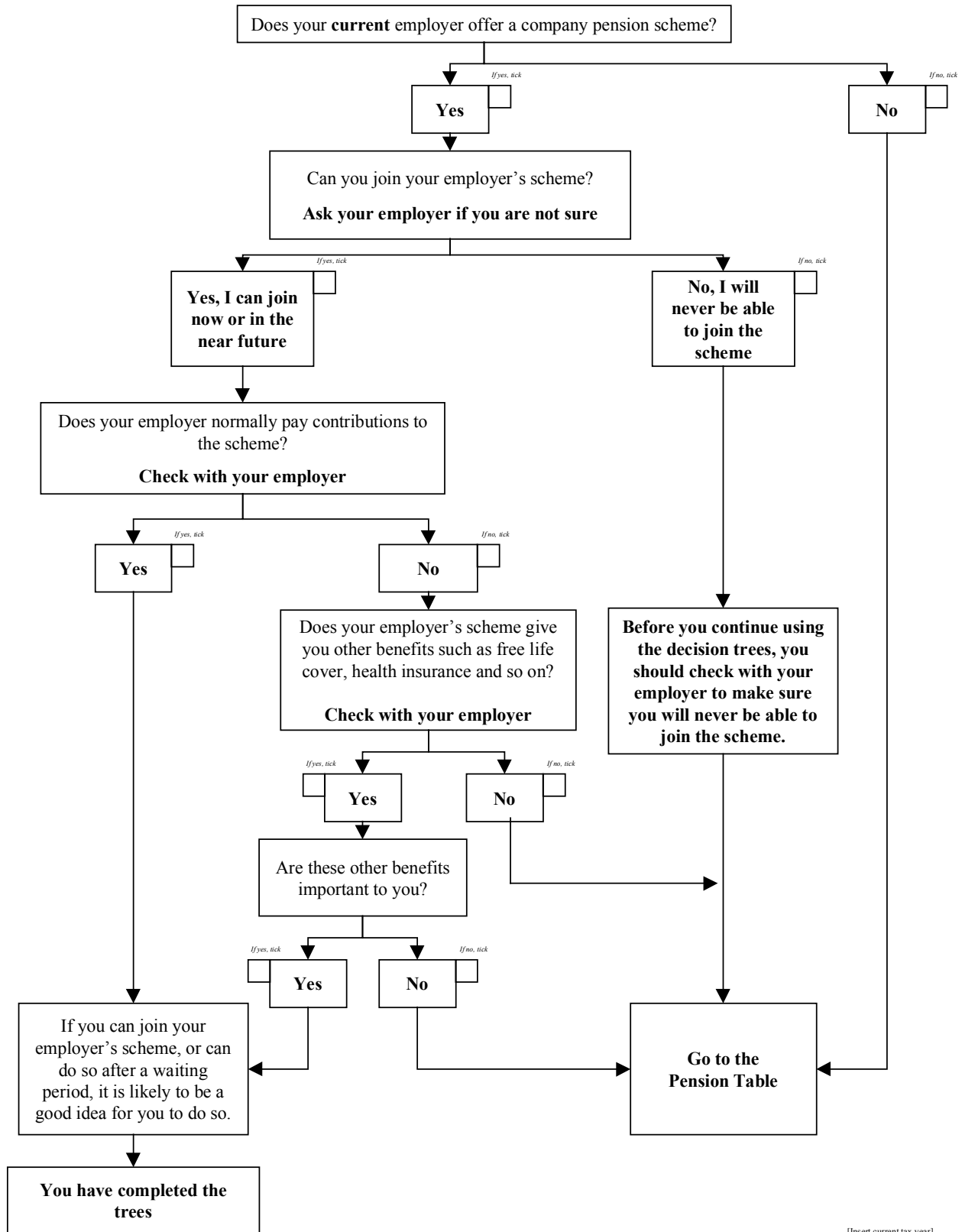
# Employed Tree 1 – Current pensions



[Insert current tax year]

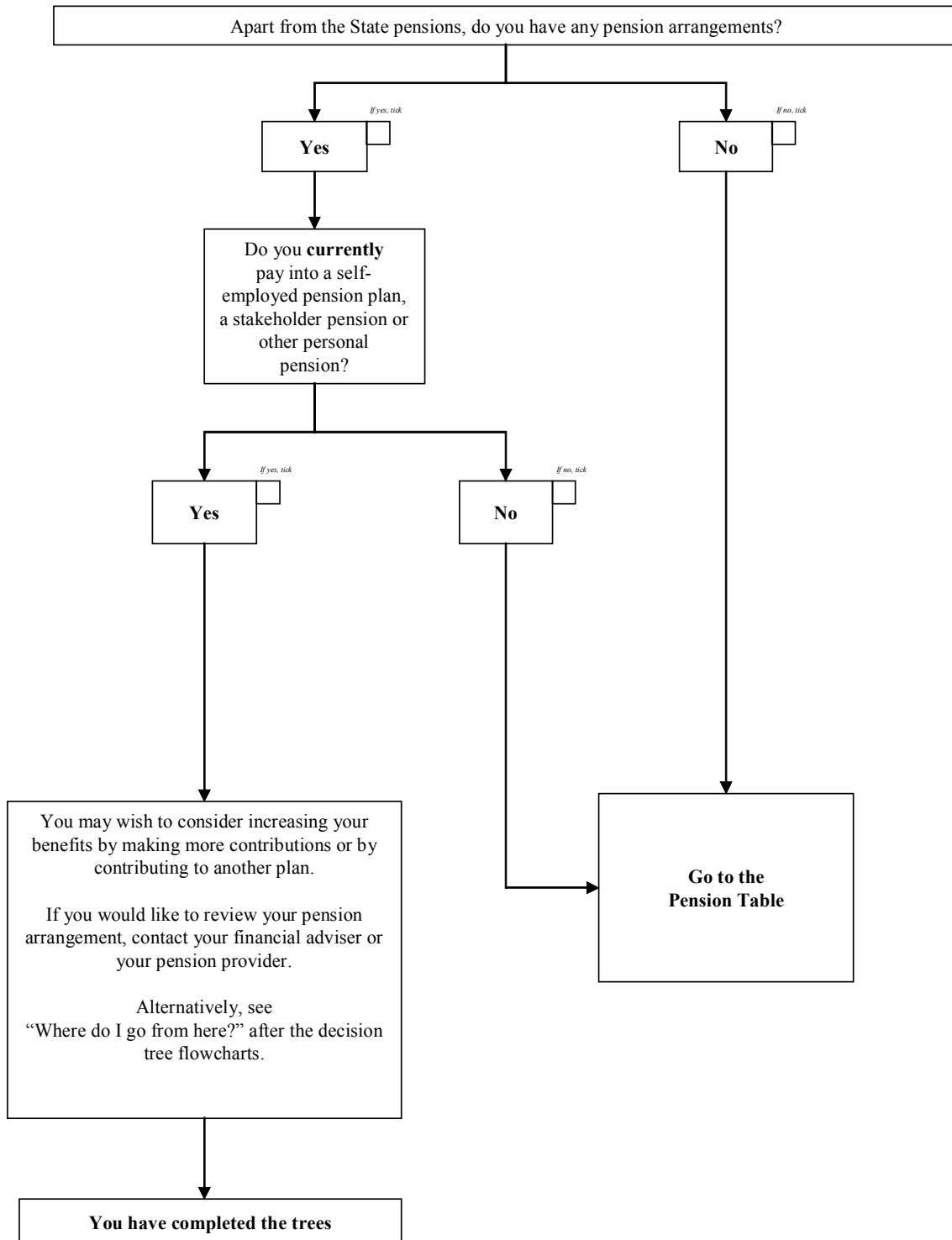
This information is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.

## Employed Tree 2 – No current pension



*This information is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.*

## Self-employed Tree

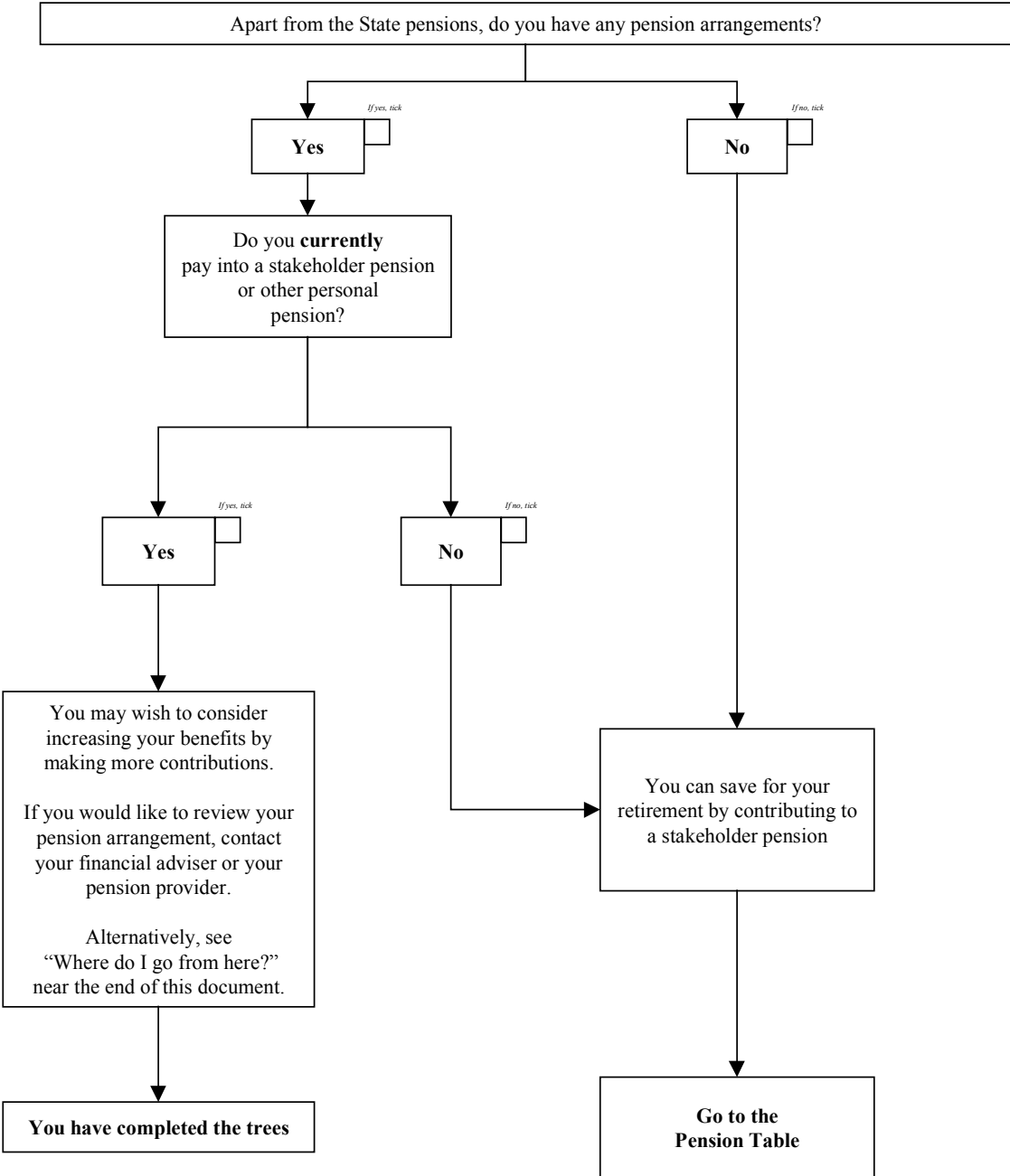


[Insert current tax year]



*This information is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.*

# Not employed Tree



This information is intended to help you make your own choice about your pension arrangements. It does not give you financial or professional advice and you should not regard it as doing so. You should get help if you require advice.

# Pension Table

## How much should I save towards a pension?

### THIS IS AN IMPORTANT DECISION

Most people save every month. It is better if you can keep up your monthly contributions.

The following table shows the **estimated monthly pension**, at today's prices, that you would get for different **regular monthly contributions**. The contribution shown is assumed to **increase each year in line with inflation**. The government will also add tax rebates to increase the actual amounts paid into your stakeholder pension (although all tax breaks are subject to change). The estimated pension figures include this tax rebate. They also assume that your pension will increase in line with inflation.

**Remember: these estimates are not guaranteed - you could get more or less than the amounts shown.  
A stakeholder pension would be on top of any State pensions you are entitled to.**

The table gives you an idea of how much you need to pay now - as a regular monthly contribution - to receive the monthly pension you want when you retire. First look down the left-hand column to find the age closest to your age now. Then look across to find the monthly contribution you want to pay and the age at which you want to retire.

Your approximate age now	What you pay per month for the first year (tax rebates will be added to this amount)							
	£ 20		£ 50		£ 100		£ 200	
	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60	Initial monthly pension if you retire at 65	Initial monthly pension if you retire at 60
20	£ 123	£ 86	£ 309	£ 217	£ 618	£ 434	£ 1,236	£ 869
25	£ 99	£ 69	£ 249	£ 172	£ 498	£ 345	£ 997	£ 691
30	£ 79	£ 54	£ 198	£ 135	£ 397	£ 270	£ 794	£ 540
35	£ 62	£ 41	£ 155	£ 102	£ 310	£ 205	£ 621	£ 411
40	£ 47	£ 30	£ 118	£ 75	£ 237	£ 151	£ 474	£ 302
45	£ 34	£ 20	£ 87	£ 52	£ 174	£ 104	£ 348	£ 208
50	£ 24	£ 12	£ 60	£ 32	£ 120	£ 64	£ 241	£ 128
55	£ 14	£ 5	£ 37	£ 14	£ 74	£ 29	£ 148	£ 59
60	£ 6		£ 17		£ 34		£ 69	

Have you found the level of monthly pension that you need in the table and can you afford the monthly contribution?

*If yes, tick*

Yes, I've found the pension I need and can afford the monthly contribution

*If no, tick*

No, I can't find the pension I need or I can't afford the contribution

Consider starting a stakeholder pension or restart making contributions to a stakeholder pension. If you are employed, check if your employer has designated a particular stakeholder pension.  
If in doubt seek help from an expert adviser.  
See "Where do I go from here?" on the next page.

**For details of where to get further help, see "Where do I go from here?" on the next page.**

**You have completed the trees**

## ***Where do I go from here?***

You've worked your way through the decision trees and now need to make some decisions. You might be confident that contributing to a stakeholder pension would be a good choice for you, or you might want more help before reaching a decision on what to do.

### ***If you have decided that a stakeholder pension is a good choice for you:***

It is a good idea to contact several firms selling stakeholder pensions and ask them for a brochure or a Key Features Document, so that you can compare products. The Key Features Document sets out important details about that particular firm's stakeholder pension product.

You can compare different stakeholder pension and personal pension schemes by using the FSA's *Comparative Tables*, which you can find at [www.fsa.gov.uk/tables](http://www.fsa.gov.uk/tables). You can also look at a register of stakeholder schemes published by the Occupational Pensions Regulatory Authority at [www.stakeholder.opra.gov.uk](http://www.stakeholder.opra.gov.uk)

You can also contact an adviser to help you choose a particular stakeholder provider. See the list below of useful contacts.

### ***Do you need more help?***

You may need to get more help before making a decision, particularly if you are in one or more of the following situations:

- You already have a pension arrangement but want to know if you should save more.
- Your personal circumstances do not seem to fit the questions in the decision trees.
- You wish to get advice that takes account of all your personal circumstances.
- You are not sure how to answer some of the questions in the decision trees.
- You are not sure if you are making the right decision.
- You feel you cannot afford to save for retirement.

You should consider getting advice if:

- You are not sure that saving through a pension plan is a good idea you; or
- You want to look at other ways of saving and investing for the long term.

Some organisations that might be able to help you are listed below.

### ***Where to get more help***

You could contact the OPAS Pensions Helpline provided by the Pensions Advisory Service on 0845 6012923. Their information is free but call charges may vary.

You can also visit their website at [www.stakeholderhelpline.org.uk](http://www.stakeholderhelpline.org.uk)

If you already have a financial adviser, you may want to speak to them about your retirement needs. If you do not have a financial adviser but want to talk to one, the following organisations can help:

- IFA Promotions: 0800 085 3250 (for a list of three local independent financial advisers)
- Institute of Financial Planning: 0117 945 2470 or at [www.financialplanning.org.uk](http://www.financialplanning.org.uk)
- Society of Financial Advisers: 020 7417 4419 or at [www.sofa.org](http://www.sofa.org)
- Solicitors for Independent Financial Advice: 01372 721172 or at [www.sifa.co.uk](http://www.sifa.co.uk)

Alternatively, contact the pension provider of your choice.

Remember that advisers may charge for any help or advice they give you, so check first on how much you would have to pay.

The next section gives further detailed information about stakeholder pensions, State pensions and how to track down old pension schemes.

## ***Further information***

### ***The minimum standards***

Stakeholder pensions must meet the standards laid down by the Government.

#### **The standards include:**

- **Charges**  
Providers of stakeholder pensions usually charge for managing your money. There is an upper limit of 1% of the value of your fund each year (so on a fund value of £10,000, the maximum charge is £100 a year).
- **Flexibility**  
You can contribute regularly or occasionally. It is always best to make regular weekly or monthly contributions but you can change the amount. You can pay in as little as £20, and you can stop paying in without having to pay any penalty, and restart later.

If you are employed and your employers provide a stakeholder pension, they may, if you wish, deduct your contributions direct from your pay and put them into your pension fund.

You can take your stakeholder pension with you when you change jobs. You can switch to another stakeholder pension at any time if you want to, without having to pay any charges for the transfer.

- **Information**  
Your stakeholder pension provider must give you regular information about your fund. This will include an annual statement to let you know how much you have paid in and how your fund is growing. It will also include a forecast of how much your pension might be in today's

prices. Look out for this forecast - it's called a Statutory Money Purchase Illustration - which is updated each year and will help you decide whether you are making enough provision for your retirement.

- **Investments**

But one thing you must understand is that **the minimum standards do not necessarily mean that your money is protected**. The performance of your stakeholder pension depends on the type of investment fund you choose and how those investments perform. Remember that investments linked to the stock market can fall as well as rise.

## *Tax relief*

Everybody who contributes to a stakeholder pension will get tax relief on their contributions.

Under present tax arrangements, for each £1 you pay into your stakeholder pension fund, the Inland Revenue will pay an extra 28p into your fund, even if you don't normally pay income tax.

### *Example*

***If you pay in £50 a month, income tax relief will increase your contribution to £64.10.***

Because of the tax advantages, there are limits on how much you can contribute to a stakeholder pension. These limits are set by the Inland Revenue and depend on your taxable earnings and your age. There are also special limits for people without any earnings and those who are members of employers' occupational pension schemes.

Most people can contribute up to £3,600 to a stakeholder pension in any tax year, including basic-rate tax relief. This means you could pay in £2,808 and the income tax relief would increase your contribution to £3,600.

If you are self-employed or in non-pensionable employment you might be able to contribute more than £3,600 and still get income tax relief, depending on your age and earnings. For example, up to age 35 you can contribute up to 17.5% of your earnings in any tax year. If you are over 35, there is a scale that allows you to contribute higher percentages of your earnings.

If you pay income tax at the higher rate, you will be able to claim back the extra tax from the Inland Revenue at the end of each tax year.

Even if you have no form of paid employment, you can set up a stakeholder pension. You can then benefit from tax relief on your contributions, even if you don't pay any income tax.

The Government is reviewing the limits on pension contributions that qualify for tax relief and plans to simplify the rules. These changes are provisionally due to come into effect in April 2006.

## *State pensions*

Rates of State pensions and benefits change every year. The following table shows the current rates of basic State Pension (assuming a full National Insurance contribution record) and the minimum income provided by the Pension Credit.

**THE BASIC STATE RETIREMENT PENSION AND PENSION CREDIT RATES GIVEN HERE ARE THOSE ANNOUNCED BY THE GOVERNMENT AS APPLYING IN THE TAX YEAR [Insert current tax year].**

	Weekly	Monthly equivalent
<b>BASIC STATE PENSION from age 65 (men) or 60 (women)</b>		
One person with a full NI contribution record	[...]	[...]
Full rate for man with dependent wife	[...]	[...]
Couples who have <i>both</i> paid full National Insurance contribution	each	[...] each
<b>PENSION CREDIT guarantees a minimum income from age 60 of at least:</b>		
Single person	[...]	[...]
Couple	[...]	[...]

You can get a forecast of your State pensions by calling the State Pension Forecasting Team on 0845 3000 168, or if you have hearing or speech difficulties and have a textphone, on textphone 0845 3000 169. Lines are open from 8am to 8pm Monday to Friday and 9am to 1pm on Saturday. You can complete an application form over the phone or ask for the forecast form BR19 to be sent to you. Or you can write to:

State Pension Forecasting Team  
 The Pension Service  
 Room TB001  
 Tyneview Park  
 Whitley Road  
 Newcastle upon Tyne  
 NE98 1BA

You can also complete the form on the Internet using the Pension Service website, [www.thepensionservice.gov.uk](http://www.thepensionservice.gov.uk) then print it out and post it in the normal way.

There are changes to the State Pension age which affect women born on or after 6 April 1950. The State Pension age for women will be increased gradually over a ten-year period from 2010 so that by 2020 women born on or after 6 April 1955 will not get a State Pension until age 65. For more information on these changes, see the Pension Service guide *Pensions for women – Your guide* (PM6).

The DWP produces a series of guides that give basic information on pensions. You can get copies by calling the DWP on 0845 731 3233. The line is open 24 hours a day and call charges may vary. A textphone service is available on 0845 604 0210. You can also order copies of these information guides on the Internet at [www.thepensionsservice.gov.uk](http://www.thepensionsservice.gov.uk)

You can get more information about the Pension Credit on the Pension Service's website at [www.thepensionsservice.gov.uk](http://www.thepensionsservice.gov.uk) or by telephoning 0800 99 1234.

### ***Old pension plans***

To check on the value of old pension plans, look at the most recent benefit statements you have been sent. If you cannot find any statements, contact the pension plan provider, for example the insurance company or the employer that offered the pension to you.

Alternatively, the Pension Schemes Registry provides a free tracing service. They can help you identify pension schemes you have belonged to in the past. To contact the Pension Schemes Registry, phone them on 0191 225 6316 and ask for a tracing request form or write to them at:

Pension Schemes Registry  
PO Box 1NN  
Newcastle upon Tyne  
NE99 1NN

There is also an online form available at [www.opra.gov.uk](http://www.opra.gov.uk).

### ***Using a stakeholder pension to contract out of the State Second Pension***

You can think about using a stakeholder pension to contract-out of the State Second Pension, but it's not an easy decision.

Everyone in employment earning above the lower earnings limit (a minimum level of earnings set by the Government for State benefit purposes) is automatically included in the State Second Pension unless they decide to leave it or are contracted-out through an employer's occupational pension scheme. Leaving the State Second Pension is called 'contracting-out'. If you contract-out, you give up your State Second Pension entitlement and instead build up a replacement for it in your own private pension arrangement, such as a stakeholder pension.

Whether you would be better off contracting-out of the Second State Pension or staying in it depends on your own personal circumstances. You need to get advice on what might be the best

thing for you to do. The FSA publishes a factsheet on its website at [www.fsa.gov.uk](http://www.fsa.gov.uk), designed to help you understand the issues, but it's not intended to replace professional advice.

Deciding to contract-out in one tax year does not commit you to do the same in later years. In fact, it's a good idea to review your decision regularly.



## Annex B

### Amendments to the Glossary

In this Annex, underlining indicates new text.

- market counterparty* (1) (except in COB 3) a *client* who is:  
...  
but excluding:  
(A) a regulated *collective investment scheme*; and  
(B) ...

**INTERIM PRUDENTIAL SOURCEBOOK FOR BANKS (MARKET RISK)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. Annex I comes into force on 1 July 2004. Otherwise this instrument comes into force on 1 July 2005.

**Amendments to the Interim Prudential sourcebook for banks**

- C. The Interim Prudential sourcebook for banks is amended in accordance with the Annexes to this instrument by:
- (1) deleting the text in Chapter FX and replacing it with that in Annex A;
  - (2) deleting the text in Chapter CM and replacing it with that in Annex B;
  - (3) deleting the text in Chapter TI and replacing it with that in Annex C;
  - (4) deleting the text in Chapter TE and replacing it with that in Annex D;
  - (5) deleting the text in Chapter TU and replacing it with that in Annex E;
  - (6) inserting a new Chapter TO between chapters TU and TS in volume 1 as set out in Annex F;
  - (7) deleting the text in Chapter TS and replacing it with that in Annex G;
  - (8) deleting the text in Chapter TV and replacing it with that in Annex H;
  - (9) inserting a new Chapter TRANS before Chapter GN in volume 1 as set out in Annex I; and
  - (10) deleting or inserting text as set out in Annex J.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004.

By order of the Board  
20 May 2004

## Annex A

### Chapter FX (Foreign exchange position risk requirement)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter FX in its entirety and replace with the following text:

FX

Foreign exchange PRR

General

- 1 G Every bank should apply this chapter and calculate its foreign exchange *PRR* by:
  - (1) identifying which *foreign currency* and gold positions to include in the *PRR* calculation;
  - (2) calculating the *open currency position* and net gold position; and
  - (3) multiplying the sum (ignoring the sign) of the *open currency position* and the net gold position by 8%.
- G For example, a bank has an *open currency position* of -£100 and a net gold position of £50. The sum (ignoring the sign) is £150, and so the foreign exchange *PRR* is £12.

Scope of the foreign exchange PRR calculation

- 2 G A bank's foreign exchange *PRR* calculation should include the following items regardless of whether they are *trading book* or *non-trading book* positions:
  - (1) all gold positions;
  - (2) all instruments which are denominated in a *foreign currency*, except:
    - (a) *foreign currency* assets which have been deducted in full from the bank's capital;
    - (b) instruments hedging (a);
    - (c) instruments hedging the bank's capital; or
    - (d) instruments hedging a future *foreign currency* income or expense which is known but not yet accrued; and
  - (3) notional positions arising from the instruments listed in table 4G:
- 3 G A bank should notify the FSA in writing if it uses the exclusions in 2G(2)(a)-(d).

- 4 G Table: instruments which result in notional *foreign currency* positions (see 2G)

Instrument	See
Foreign exchange <i>futures, forwards, CFDs</i> or <i>synthetic futures</i>	10G
Foreign exchange <i>swaps</i>	12G
Foreign exchange <i>options</i> (unless the bank calculates a <i>PRR</i> on the <i>option</i> under chapter TO)	14G
Gold <i>futures, forwards, synthetic futures</i> and <i>CFDs</i>	15G
Gold <i>options</i> (unless the bank calculates a <i>PRR</i> on the <i>option</i> under chapter TO)	16G

- 5 G Banks are reminded that table 5G in chapter TO divides foreign exchange *options* into:
- (1) those which should be treated under chapter TO; and
  - (2) those which should be treated under either chapter FX or chapter TO, but banks can choose whether chapter FX or TO is used.
- 6 G When determining the currency of denomination banks should:
- (1) use the currency in which the bank accounts for the instrument where an instrument is quoted in more than one currency; and
  - (2) treat depository receipts as positions in the underlying security.
- 7 G Instruments denominated in a foreign currency include, amongst other things, assets and liabilities (including accrued interest); non-foreign exchange *derivatives*; net *underwriting* positions; reduced net *underwriting* positions; and irrevocable guarantees (or similar instruments) that are certain to be called.
- 8 G Where a contract is based on a basket of currencies, the bank can choose either to derive notional positions in each of constituent currencies, or treat it as a single notional position in a separate hypothetical currency.

#### Derivation of notional positions

- 9 G This section derives notional currency positions for the instruments listed in table 4G.

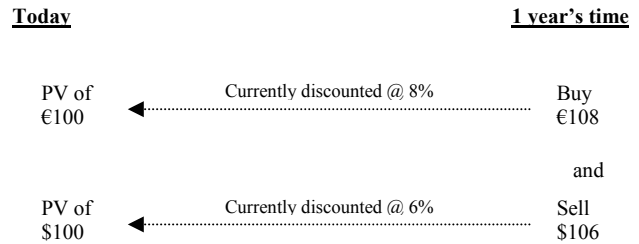
#### FOREIGN EXCHANGE FORWARDS, FUTURES, CFDs AND SYNTHETIC FUTURES

- 10 G A bank should treat a foreign exchange *forward, future* or *CFD* as two notional currency positions as follows:
- (1) a long notional position in the currency which the bank has contracted to buy; and

(2) a short notional position in the currency which the bank has contracted to sell;  
 where the notional positions have a value equal to either:

- (a) the contracted amount of each currency to be exchanged in the case of a *forward* or *future* held in the *non-trading book*; or
- (b) the present value of the amount of each currency to be exchanged in the case of a *forward* or *future* held in the *trading book*.

11 G For example, a bank contracts to sell \$106 for €108 in one year's time. The present values of each cash flow are \$100 and €100 respectively.



- In the *non-trading book*, this *forward* would be treated as a combination of a €108 long position and a \$106 short position.
- In the *trading book*, this *forward* would be treated as a combination of a €100 long position and a \$100 short position.

Banks are reminded that foreign exchange *forwards* held in the *trading book* should also be included in the bank's interest rate *PRR* calculation (see 4G of chapter TI).

#### FOREIGN EXCHANGE SWAPS

12 G A bank should treat a foreign exchange *swap* as:

- (1) a long notional position in the currency which the bank has contracted to receive interest and principal;
- (2) a short notional position in the currency which the bank has contracted to pay interest and principal; and
- (3) where the notional positions have a value equal to either:
  - (a) the nominal amount of each currency underlying the *swap* if it is held in the *non-trading book*; or
  - (b) the present value amount of all cash flows in the relevant currency in the case of a *swap* held in the *trading book*.

13 G For example, a bank enters into a five year foreign exchange *swap* where it contracts to pay six month US\$ Libor on \$100 in return for receiving 6% fixed on €100. The present values of each leg are \$100 and €98 respectively.

- In the *non-trading book*, this *swap* would be treated as a combination of a €100 long position and a \$100 short position.
- In the *trading book*, this *swap* would be treated as a combination of a €98 long position and a \$100 short position.

Banks are reminded that foreign exchange *swaps* held in the *trading book* should also be included in the bank's interest rate *PRR* calculation (see table 4G of chapter TI).

#### FOREIGN EXCHANGE OPTIONS AND WARRANTS

- 14 G Where included in this chapter's *PRR* calculation (see table 4G), a foreign exchange *option* or *warrant* should be treated as a foreign exchange *forward*.

#### GOLD FORWARDS, FUTURES AND CFDS

- 15 G A *forward*, *future* or *CFD* on gold must be treated as a notional position in gold with a value equal to the amount of gold underlying the contract multiplied by the current spot price for gold.

#### GOLD OPTIONS

- 16 G If included in the *PRR* calculation under this chapter (see table 4G), a gold *option* must be treated as a gold *forward*.

#### Open currency position

- 17 G A bank should calculate its *open currency position* by:
- (1) calculating the net position in each *foreign currency*;
  - (2) converting each net position into its *base currency* equivalent at current spot rates;
  - (3) summing all short net positions and summing all long net positions; and
  - (4) selecting the larger sum (ignoring the sign) from (3).

#### Net gold position

- 18 G A bank should calculate its net gold position by:
- (1) valuing all gold positions using the prevailing spot price for gold (regardless of the maturity of the positions);
  - (2) offsetting long and short positions; and
  - (3) converting the resulting net position into the *base currency* equivalent using the current spot foreign exchange rate.

#### Definitions used in chapter FX

- 19 G This chapter uses the following definitions:

Defined term	Definition
<i>Base currency</i>	The currency currently used by a firm to calculate its financial resource requirement.
<i>CFDs</i>	Means contract for differences.
<i>Derivative</i>	<i>Options, futures</i> and contracts for differences.
<i>Foreign currency</i>	A currency other than the bank's <i>base currency</i> .
<i>Forward</i>	A contract to buy or sell where the date of settlement has been agreed as a particular date in the future.
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures)
<i>Non trading book</i>	Items not in the <i>trading book</i> .
<i>Open currency position</i>	The position calculated under 17G.
<i>Option</i>	A contract which confers the right to buy or sell a <i>security</i> , contractually based investment, currency, gold or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>PRR</i>	Position risk requirement.
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.
<i>Synthetic future</i>	A combination of a long (short) call <i>option</i> and a short (long) put <i>option</i> which are based on the same underlying and have the same notional amount, strike and maturity.
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.
<i>Underwriting</i>	Means an arrangement made before the relevant securities are issued under which a party agrees to buy a specified quantity of those securities on a given date and at a given price, if no other has purchased or acquired them.
<i>Warrant</i>	The investment specified in article 79 of the Regulated Activities Order (instruments giving entitlement to investments).

## Annex B

### Chapter CM (Commodity position risk requirement)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter CM in its entirety and replace with the following text:

CM

Commodity PRR

General

- 1 G Every bank should apply this chapter and calculate its *commodity PRR* by:
- (1) identifying which *commodity* positions should be included within the *PRR* calculation (see 2G);
  - (2) calculating an individual *PRR* for each *commodity* (see 20G);
  - (3) converting each *PRR* to the bank's *base currency* at current spot foreign exchange rates; and
  - (4) summing the resulting individual *PRRs*.

Scope of the PRR calculation

- 2 G A bank's *commodity PRR* calculation should, regardless of whether the positions are *trading book* or *non-trading book* positions:
- (1) include *physical commodity* positions;
  - (2) include the notional positions derived from positions in the instruments listed in table 4G; and
  - (3) exclude positions constituting a *stock financing* transaction.
- 3 G Gold positions are excluded from the scope of the *commodity PRR*. Instead, they are included within the scope of the foreign exchange *PRR*.
- 4 G Table: Instruments which result in notional positions (see 2G(2))

Instrument	see
<i>Forwards, futures, CFDs, synthetic futures</i> and <i>options</i> on a single <i>commodity</i> (unless the bank calculates an <i>PRR</i> on the <i>option</i> under chapter TO)	8G
A commitment to buy or sell a single <i>commodity</i> at an average of	10G



spot prices prevailing over some future period	
<i>Forwards, futures, CFDs, synthetic futures and options on a commodity index (unless the bank calculates an PRR on the option under chapter TO)</i>	13G – 14G
<i>Commodity swaps</i>	16G – 17G

- 5 G 2G includes a *trading book* position in an *commodity* that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the *commodity* had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the *commodity* would not have been included in the *trading book* in the first place.
- 6 G Banks are reminded that table 5G in chapter TO divides *commodity options* into:
- (1) those which should be treated under chapter TO; and
  - (2) those which should be treated under either chapter CM or chapter TO, but banks can choose whether chapter CM or TO is used.

#### Derivation of notional positions

- 7 G This section converts the instruments listed in table 4G into notional positions in the relevant *commodities*. These notional positions are expressed in terms of quantity (tonnes, barrels, etc), not value. The maturity of the position is only relevant where the bank is using the maturity ladder approach.

#### FUTURES, FORWARDS, CFDs AND OPTIONS ON A SINGLE COMMODITY

- 8 G Where a *forward, future, CFD, synthetic future or option* (unless already included in the bank's *option PRR* calculation) settles according to:
- (1) the difference between the price set on trade date and that prevailing at contract expiry, the notional position:
    - (a) equals the total quantity underlying the contract; and
    - (b) has a maturity equal to the expiry date of the contract
  - (2) the difference between the price set on trade date and the average of prices prevailing over a certain period up to contract expiry, there is a notional position for each of the reference dates used in the averaging period to calculate the average price, which:
    - (a) equals a fractional share of the total quantity underlying the contract; and
    - (b) has a maturity equal to the relevant reference date.

- 9 G The following example illustrates 8G(2). A bank buys a Traded Average Price Option (TAPO - a type of Asian option) allowing it to deliver 100 tonnes of Grade A copper and receive \$1,750 in June. If there were twenty *business days* in June the short notional positions will each:

- (1) equal 5 tonnes per day (1/20 of 100 tonnes); and
- (2) have a maturity equal to one of the *business days* in June (one for each day).

In this example as each *business day* in June goes by the quantity per day for the remaining days does not change (5 tonnes per day) only the days remaining changes. Therefore, halfway through June there are 10, 5 tonne short notional positions remaining each for the ten remaining *business days* in June.

#### BUYING OR SELLING A SINGLE COMMODITY AT AN AVERAGE OF SPOT PRICES PREVAILING IN THE FUTURE

- 10 G Commitments to buy or sell at the average spot price of the *commodity* prevailing over some period between trade date and maturity should be treated as a combination of:

- (1) a position equal to the full amount underlying the contract with a maturity equal to the maturity date of the contract which is:
  - (a) long, where the bank will buy at the average price; or
  - (b) short, where the bank will sell at the average price
- (2) a series of notional positions, one for each of the reference dates where the contract price remains unfixed, each of which:
  - (a) is long if the position under (1) is short, or short if the position under (1) is long;
  - (b) equals a fractional share of the total quantity underlying the contract; and
  - (c) has a maturity date of the relevant reference date.

- 11 G The following guidance provides an example of 10G.

In January, a bank agrees to buy 100 tonnes of copper for the average spot price prevailing during the 20 *business days* in February, and will settle on 30 June. After entering into this agreement, the bank faces the risk that the average price for February increases relative to that for 30 June. Therefore, as highlighted in the table below:

- (1) the short positions reflect the fact that this could occur because any one of the remaining forward prices for February increase; and
- (2) the long position reflects the fact that this loss could occur because the forward price for 30 June falls.

- 12 G Table: Example of buying at the average spot price prevailing in the future (see 11G)

	Application of 10G(1)	Application of 10G(2)
From trade date to start of averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	A series of 20 notional short positions each equal to 5 tonnes of copper. Each position is allocated a maturity equal to one of the <i>business days</i> in February (one for each day).
During averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	As each <i>business day</i> goes by in February the price for 5 tonnes of copper is fixed and so there will be one less notional short position.
After averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	No short positions.

#### FUTURES, CFDS AND OPTIONS ON A COMMODITY INDEX

- 13 G *Commodity index futures or CFDs, and commodity index options* (unless the *option* is included in the bank's *option PRR* calculation), should be treated as follows:
- (1) Step 1: The total quantity underlying the contract should be either:
    - (a) treated as a single notional *commodity* position (separate from all other *commodities*); or
    - (b) divided into notional positions, one for each of the constituent *commodities* in the index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant *commodity* in the index.
  - (2) Step 2: Each notional position determined in step 1 should then be included:
    - (a) when using the simplified approach (24G); or
    - (b) when using the maturity ladder approach (25G).
- 14 G Table: Treatment of *commodity index futures* and *commodity index options* (see 13G(2)(b)).

Construction of index	Notional position (or positions) and maturity
Spot level of index is based on the spot price of each constituent <i>commodity</i>	Each quantity determined in step 1 is assigned a maturity equal to the expiry date of the contract.
Spot level of index is based on an average of the forward prices of each constituent <i>commodity</i>	Each quantity determined in step 1 is divided (on a pro-rata basis) into a series of forward positions to reflect the impact of each forward price on the level of the index. The maturity of each forward position equals the maturity of the relevant forward price determining the level of the index when the contract expires.

- 15 G An example of using 13G and table 14G is as follows. A bank is long a three-month *commodity index future* where the spot level of the index is based on the one, two and three month forward prices of aluminium, copper, tin, lead, zinc and nickel (18 prices in total).

Step 1: the bank should decide whether to treat the full quantity underlying the contract as a single notional *commodity* position, or disaggregate it into notional positions in aluminium, copper, tin, lead, zinc and nickel. In this case the bank decides to disaggregate the contract into notional positions in aluminium, copper, tin, lead, zinc and nickel.

Step 2: if the bank uses the simplified method, nothing more need be done to arrive at the notional position. In this case the bank uses the maturity ladder approach and so subdivides each position in each metal into three because the level of the index is based on the prevailing one, two and three month forward prices. Since the *future* will be settled in three months' time at the prevailing level of the index, the three positions for each metal will have maturities of four, five and six months respectively.

#### COMMODITY SWAPS

- 16 G A bank should treat a *commodity swap* as a series of notional positions, one position for each payment under the *swap*, each of which:
- (1) equals the total quantity underlying the contract;
  - (2) has a maturity corresponding to the payment date; and
  - (3) is long or short according to 17G
- 17 G Table: Treatment of *commodity swaps* (see 16G)

	Receiving amounts which are unrelated to any <i>commodity's</i> price	Receiving the price of <i>commodity 'b'</i>
Paying amounts which are unrelated to any <i>commodity's</i> price	N/A	Long positions in <i>commodity 'b'</i>
Paying the price of <i>commodity 'a'</i>	Short positions in <i>commodity 'a'</i>	Short positions in <i>commodity 'a'</i> and long positions in <i>commodity 'b'</i>

- 18 G Table 17G shows that where the legs of the *swap* are in different *commodities*, a series of forward positions are created for each *commodity* (that is, a series of short positions in *commodity 'a'* and a series of long positions in *commodity 'b'*).
- 19 G Table 17G also covers the case where one leg is unrelated to any *commodity's* price. This leg may be subject to a *PRR* under another chapter; for example, an interest rate based leg would have to be included in a bank's interest rate *PRR* calculation.

#### Calculating the *PRR* for each *commodity*

- 20 G A bank should calculate a *PRR* for each *commodity* separately using either the simplified approach (24G) or the maturity ladder approach (25G).
- 21 G A bank need not use the same approach for all *commodities*.
- 22 G A bank should treat positions in different grades or brands of the same *commodity*-class as different *commodities* unless they:
- (1) can be delivered against each other; or
  - (2) have price movements which have exhibited a stable correlation coefficient of at least 0.9 over the last 12 months. The bank should then monitor the correlation on a continuing basis
- 23 G If a bank intends to rely on the approach in 22G(2) it should:
- (1) notify the FSA in writing at least twenty *business days* prior to the date the bank starts relying on it.
  - (2) when it notifies the FSA under (1) the bank should also provide to the FSA the analysis of price movements on which it relies.

#### SIMPLIFIED APPROACH

- 24 G A bank which calculates *PRR* using the simplified approach should do so by summing:

- (1) 15% of the net position multiplied by the spot price for the *commodity*; and
- (2) 3% of the gross position (long plus short, ignoring the sign) multiplied by the spot price for the *commodity*.

#### MATURITY LADDER APPROACH

- 25 G A bank using the maturity ladder approach should calculate the *PRR* following the steps in 26G and then sum all the spread charges, carry charges and outright charge that result.
- 26 G The bank should calculate the charges referred to in 25G as follows:
- (1) Step 1: Offset long and short positions maturing:
    - (a) on the same day; or
    - (b) (in the case of positions arising under contracts traded in markets with daily delivery dates) within 10 *business days* of each other.
  - (2) Step 2: Allocate the positions remaining after step 1 to the appropriate maturity band in table 28G (*physical commodity* positions are allocated to band 1).
  - (3) Step 3: Match long and short positions within each band. In each instance, calculate a spread charge equal to the matched amount multiplied first by the spot price for the *commodity* and then by the spread rate of 3%.
  - (4) Step 4: Carry unmatched positions remaining after step 3 to another band where they can be matched, then match them. Do this until all matching possibilities are exhausted. In each instance, calculate:
    - (a) a carry charge equal to the carried position multiplied by the spot price for the *commodity*, the carry rate of 0.6% and the number of bands by which the position is carried; and
    - (b) a spread charge equal to the matched amount multiplied by the spot price for the *commodity* and the spread rate of 3%.
  - (5) Step 5: Calculate the outright charge on the remaining positions (which will either be all long positions or all short positions). The outright charge equals the remaining position (ignoring the sign) multiplied by the spot price for the *commodity* and the outright rate of 15%.
- 27 G The matched amount in 26G is the lesser (ignoring the sign) of either the total long position or the total short position. For example, a band with 1000 long and 700 short results in a matched amount of 700. The unmatched amount would be 300.

28 G Table: Maturity bands for the maturity ladder approach (see 26G))

<b>Band</b>	<b>Maturity of position</b>
Band 1	$0 \leq 1$ month
Band 2	$> 1$ month $\leq 3$ months
Band 3	$> 3$ months $\leq 6$ months
Band 4	$> 6$ months $\leq 1$ year
Band 5	$> 1$ year $\leq 2$ years
Band 6	$> 2$ years $\leq 3$ years
Band 7	$> 3$ years

- 29 G Figure: An example illustrating the calculation of the *PRR* on an individual *commodity* using the maturity ladder approach (26G).

Figure 29G: After a bank has carried out the pre-processing required by 26G(1) (that is, step 1), it follows steps 2 to 5 as shown below. Because the bank is using the maturity ladder approach the spread rate is 3%, the carry rate is 0.6% and the outright rate is 15%. The example assumes that the spot price for the *commodity* is £25.

Band	Step 2 Allocate remaining positions to appropriate maturity bands	Step 3 Match within bands. Each matched amount incurs a spread charge.	Step 4a Carry across bands. Each carried amount incurs a carry charge.	Step 4b Match within band. Each matched amount incurs a spread charge.	Step 6 Remaining position(s) incur an outright charge.
0 ≤ 1 month					
>1 month ≤ 3 months	1000 long 700 short	700 matched	300 carried		
>3 months ≤ 6 months					
>6 months ≤ 1 year					
>1 year ≤ 2 years	600 short	Nothing matched	100 carried	400 matched	200 short remains
>2 years ≤ 3 years					
> 3 years	100 long	Nothing matched			
Spread charges $700 * £25 * 3\% + 400 * £25 * 3\%$				=	£825
Carry charges $300 * £25 * 0.6\% * 3 + 100 * £25 * 0.6\% * 2$				=	£165
Outright charge $200 * £25 * 15\%$				=	£750
					<b>£1740</b>

Definitions used in chapter CM

- 30 G This chapter uses the following definitions:

Defined term	Definition
<i>Base currency</i>	The currency currently used by a firm to calculate its financial resource requirements.
<i>Business days</i>	Any day except Saturday, Sunday, bank holidays and public holidays (not being bank holidays).
<i>CFDs</i>	Means contract for differences.
<i>Commodity</i>	Any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB the definition of commodity used in CM deliberately differs from that in the main Handbook)



	Glossary).
<i>Forward</i>	A contract to buy or sell where the date of settlement has been agreed as a particular date in the future.
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>Non trading book</i>	Items not in the <i>trading book</i> .
<i>Option</i>	A contract which confers the right to buy or sell a <i>security</i> , contractually based investment, currency, gold or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>Physical commodity</i>	The actual <i>commodity</i> , documents of title to actual <i>commodities</i> , or shipping documents conveying actual title to <i>commodities</i> .
<i>PRR</i>	Position risk requirement.
<i>Repurchase agreement</i>	See section 3.2, and 2(b)a) of chapter TC.
<i>Reverse repurchase agreement</i>	See section 3.2, and 2(b)a) of chapter TC.
<i>Stock financing</i>	A transaction where a <i>physical commodity</i> is sold forward and the cost of funding is locked in until the date of the forward sale.
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.
<i>Synthetic future</i>	A combination of a long (short) call <i>option</i> and a short (long) put <i>option</i> which are based on the same underlying and have the same notional amount, strike and maturity.
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.

## Annex C

### Chapter TI (Interest rate position risk requirement)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter TI in its entirety and replace with the following text:

TI

Interest rate PRR

General

- 1 G A UK bank to which CAD applies should apply this chapter and calculate its interest rate *PRR* by:
  - (1) identifying which positions should be included within the *PRR* calculation;
  - (2) deriving the net position in each debt *security* in accordance with 37G - 41G;
  - (3) including these net positions in the *PRR* calculation for general market risk and the *PRR* calculation for specific risk; and
  - (4) summing all *PRRs* calculated for general market risk and specific risk.
- 2 G The interest rate *PRR* calculation divides the interest rate risk into the risk of loss from a general move in market interest rates, and the risk of loss from an individual debt *security's* price changing for reasons other than a general move in market interest rates. These are called general market risk and specific risk respectively.

Scope of the Interest rate PRR calculation

- 3 G A bank's interest rate *PRR* calculation should:
  - (1) include all *trading book* positions in debt *securities*, *preference securities* and *convertibles*, except:
    - (a) positions in *convertibles* which have been included in the bank's *PRR* calculation for *equities* under chapter TE;
    - (b) positions fully deducted from capital under 2(c) of section 10.2 of chapter CA, in which case the bank may exclude them; or
    - (c) positions hedging an *option* which is being treated under 26G of chapter TO; and
  - (2) include notional positions arising from *trading book* positions in the instruments listed in table 4G.

4 G Table: Instruments which result in notional positions (see 3G(2))

Instrument	See
<i>Futures, forwards</i> or <i>synthetic futures</i> on debt securities	13G
<i>Futures, forwards</i> or <i>synthetic futures</i> on debt indices or baskets	14G
Interest rate <i>futures</i> or <i>forward rate agreements (FRAs)</i>	18G
Interest rate <i>swaps</i> or foreign exchange <i>swaps</i>	21G
Deferred start interest rate <i>swaps</i> or foreign exchange <i>swaps</i>	24G
The interest rate leg of an <i>equity swap</i> (unless the bank calculates a <i>PRR</i> on the instrument using the basic interest rate <i>PRR</i> calculation in chapter TE)	27G
The cash leg of a <i>repurchase agreement</i> or a <i>reverse repurchase agreement</i>	30G
Cash borrowings or deposits	31G
<i>Options</i> or <i>warrants</i> on a debt security, interest rate or interest rate <i>future</i> or <i>swap</i> or on a <i>future</i> on a debt security (unless the bank calculates a <i>PRR</i> on the <i>option</i> under chapter TO)	32G
Dual currency bonds	33G
Foreign exchange <i>futures</i> or <i>forwards</i>	34G
Gold <i>futures</i> or <i>forwards</i>	34G
<i>Forwards, futures</i> or <i>options</i> (except cliquets) on an <i>equity</i> , basket of <i>equities</i> or <i>equity</i> index (unless the bank calculates a <i>PRR</i> on the instrument using the basic interest rate <i>PRR</i> calculation in chapter TE)	34G
Credit derivatives	Chapter CD

5 G 3G(1) includes a *trading book* position in debt security, preference security or convertible that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the security had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the security would not have been included in the *PRR* calculation in the first place.

6 G 3G(1) includes net *underwriting* positions or reduced net *underwriting* positions in debt securities.

- 7 G Banks are reminded that table 5G in chapter TO divides *options* or *warrants* on interest rates, debt *securities*, interest rate *futures* and *swaps* into:
- (1) those which should be treated under chapter TO; and
  - (2) those which should be treated under either chapter TI or chapter TO, but banks can choose whether chapter TI or TO is used.
- 8 G Cliquets on *equities*, baskets of *equities* or *equity* indices do not attract an interest rate *PRR*. Table 4G excludes them from the scope of the interest rate *PRR* calculation in this chapter, and 42G of chapter TE excludes them from the basic interest rate *PRR* calculation in that chapter.
- 9 G Table 4G shows that *equity derivatives* are excluded from this chapter's *PRR* calculation if they have been included in the basic interest rate *PRR* calculation in chapter TE (see 42G of chapter TE).

#### Derivation of notional positions

##### GENERAL APPROACH

- 10 G This section converts the instruments listed in table 4G into notional positions in:
- (1) the underlying debt *security*, where the instrument depends on the price (or yield) of a specific debt *security*; and/or
  - (2) hypothetical debt *securities* to capture the pure interest rate risk arising from future payments and receipts of cash (including notional payments and receipts). Because they are designed to represent pure general market risk (and not specific risk) they are called *zero-specific-risk securities*.
- 11 G For the purposes of calculating *PRR*, unless specified otherwise, a bank should derive the value of notional positions as follows:
- (1) notional positions in actual debt *securities* should be valued as the nominal amount underlying the contract at the current market price of the debt *security*; and
  - (2) positions in *zero-specific-risk securities* should be valued using one of the two following methods. A bank should use the same method for all positions denominated in the same currency:
    - (a) Present value approach: The *zero-specific-risk security* is assigned a value equal to the present value of all the future cash flows that it represents.
    - (b) Alternative approach: The *zero-specific-risk security* is assigned a value equal to:
      - (i) the market value of the underlying notional *equity* position in the case of an *equity derivative*;

- (ii) the notional principal amount in the case of an interest rate or foreign exchange *swap*; or
  - (iii) the notional amount of the future receipt or payment that it represents in the case of any other instrument.
- 12 G A bank should use 11G(2)(a) in respect of any positions that it includes in the duration method calculation of general market risk (see 60G).

FUTURES OR FORWARDS ON A DEBT SECURITY

- 13 G *Futures or forwards* on a single debt *security* should be treated as follows:
  - (1) A purchased *future* or *forward* is treated as:
    - (a) a notional long position in the underlying debt *security* (or the cheapest to deliver (taking into account the conversion factor) where the contract can be satisfied by delivery of one from a range of *securities*); and
    - (b) a notional short position in a zero coupon *zero-specific-risk security* with a maturity equal to the expiry date of the *future* or *forward*.
  - (2) A sold *future* or *forward* is treated as:
    - (a) a notional short position in the underlying *security* (or the cheapest to deliver (taking into account the conversion factor) where the contract can be satisfied by delivery of one from a range of *securities*); and
    - (b) a notional long position in a zero coupon *zero-specific-risk security* with a maturity equal to the expiry date of the *future* or *forward*.

FUTURES OR FORWARDS ON A BASKET OR INDEX OF DEBT SECURITIES

- 14 G *Futures or forwards* on a basket or index of debt *securities* should be converted into *forwards* on single debt *securities* as follows (and then the resulting positions are treated under 13G).
  - (1) *Futures or forwards* on a single currency basket or index of debt *securities* should be treated as either:
    - (a) a series of *forwards*, one for each of the constituent debt *securities* in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant debt *security* in the basket; or
    - (b) a single *forward* on a hypothetical debt *security*.
  - (2) *Futures or forwards* on multiple currency baskets or indices of debt *securities* should be treated as either:

- (a) a series of *forwards* (using the method described in (1)(a)); or
  - (b) a series of *forwards*, each one on a hypothetical debt *security* to represent one of the currencies in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant currency in the basket.
- 15 G Under 14G(2)(b), a *forward* on basket of 3 Euro denominated debt *securities* and 2 Dollar denominated debt *securities* would be treated as a *forward* on a single hypothetical Euro denominated debt *security* and a *forward* on a single hypothetical Dollar denominated debt *security*.
- 16 G The hypothetical debt *securities* in 14G are assigned a specific risk *PRA* and a general market risk *PRA* equal to the highest that would apply to the debt *securities* in the basket or index.
- 17 G The debt *security* with the highest specific risk *PRA* within the basket might be a different debt *security* to that with the highest general market risk *PRA*. When following 16G, a bank would select the highest percentages even where they relate to different debt *securities* in the basket or index, and regardless of the proportion of those debt *securities* in the basket or index.

INTEREST RATES FUTURES AND FORWARD RATE AGREEMENTS (FRAS)

- 18 G Interest rate *futures* or *FRAs* should be treated as the two notional positions (one long, one short) shown in table 19G.
- 19 G Table: Interest rate *futures* and *FRAs* (see 18G)

	1	2
	<b>A short position in a zero coupon zero-specific-risk-security</b>	<b>A long position in a zero coupon zero-specific-risk-security</b>
Where the bank buys an interest rate <i>future</i> or sells an <i>FRA</i>	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> )	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> ) plus the maturity of the borrowing/deposit
Where the bank sells an interest rate <i>future</i> or buys an <i>FRA</i>	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> ) plus the maturity of the borrowing/deposit	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> )

- 20 G The following example illustrates 18G and table 19G in conjunction with 11G (the latter guidance determines the value of notional positions). A bank sells £1mn notional of a 3v6 *FRA* at 6%. This results in:

- (1) a short position in a *zero-specific-risk-security* with a zero coupon, three month maturity, and a nominal amount of £1mn; and
- (2) a long position in a *zero-specific-risk-security* with a zero coupon, six month maturity, and nominal amount of £1,015,000 (i.e. notional plus interest at 6% over 90 days)

If a bank were to apply the approach in 11G(2)(a), the two nominal amounts would have to be present valued.

INTEREST RATE SWAPS OR FOREIGN EXCHANGE SWAPS

- 21 G Interest rate *swaps* or foreign exchange *swaps* without deferred starts should be treated as the two notional positions (one long, one short) shown in table 22G:
- 22 G Table: Interest rate and foreign exchange *swaps* (see 21G)

	<b>1. Paying leg</b> <i>A short position in a zero-specific-risk security</i>	<b>2. Receiving leg</b> <i>A long position in a zero-specific-risk security</i>
Receiving fixed and paying floating	coupon equals the floating rate and maturity equals the reset date	Coupon equals the fixed rate of the <i>swap</i> and maturity equals the maturity of the <i>swap</i>
Paying fixed and receiving floating	coupon equals the fixed rate of the <i>swap</i> and maturity equals the maturity of the <i>swap</i>	Coupon equals the floating rate and maturity equals the reset date
Paying floating and receiving floating	coupon equals the floating rate and maturity equals the reset date	Coupon equals the floating rate and maturity equals the reset date

- 23 G For a foreign exchange *swap*, the two notional *zero-specific-risk securities* would be denominated in different currencies. A foreign exchange *swap* is also included in the foreign exchange *PRR* calculation.

DEFERRED START INTEREST RATE SWAPS OR FOREIGN EXCHANGE SWAPS

- 24 G Interest rate *swaps* or foreign exchange *swaps* with a deferred start should be treated as the two notional positions (one long, one short) shown in table 25G.
- 25 G Table: Deferred start interest rate and foreign exchange *swaps* (see 24G)

	1. Paying leg A short position in a <i>zero-specific-risk security</i> with a coupon equal to the fixed rate of the <i>swap</i>	2. Receiving leg A long position in a <i>zero-specific-risk security</i> with a coupon equal to the fixed rate of the <i>swap</i>
Receiving fixed and paying floating	maturity equals the start date of the <i>swap</i>	maturity equals the maturity of the <i>swap</i>
Paying fixed and receiving floating	maturity equals the maturity of the <i>swap</i>	maturity equals the start date of the <i>swap</i>

- 26 G For example, a bank enters into a five year *swap* which starts in two year's time. The bank has contracted to receive 6% and pay six month Libor on a principal amount of £1mn. This results in a long position in a 7 year debt *security* and a short position in a 2 year debt *security*. Both have a coupon of 6%.

SWAPS WHERE ONLY ONE LEG IS AN INTEREST RATE LEG (E.G. EQUITY SWAPS)

- 27 G A bank should treat a *swap* with only one interest rate leg as a notional position in a *zero-specific-risk security*:
- (1) with a coupon equal to that on the interest rate leg;
  - (2) with a maturity equal to the date that the interest rate will be reset; and
  - (3) which is a long position if the bank is receiving interest payments and short if making interest payments.
- 28 G 27G includes *equity swaps*, *commodity swaps* and any other *swap* where only one leg is an interest rate leg.

CASH LEGS OF REPURCHASE AGREEMENTS AND REVERSE REPURCHASE AGREEMENTS

- 29 G Bank's are reminded that for the purposes of 30G, a *repurchase agreement* includes a sell/buy back or stock lending; and a *reverse repurchase agreement* includes a buy/sell back or a stock borrowing.
- 30 G The forward cash leg of a *repurchase agreement*; or *reverse repurchase agreement* should be treated as a notional position in a *zero-specific-risk security* which:
- (1) is a short notional position in the case of a *repurchase agreement*; and a long notional position in the case of a *reverse repurchase agreement*;
  - (2) has a value equal to the market value of the cash leg;



- (3) has a maturity equal to that of the *repurchase agreement* or *reverse repurchase agreement*; and
- (4) has a coupon equal to:
  - (a) zero, if the next interest payment date coincides with the maturity date; or
  - (b) the interest rate on the contract, if any interest is due to be paid before the maturity date.

#### CASH BORROWINGS AND DEPOSITS

- 31 G A cash borrowing or deposit should be treated as a notional position in a zero coupon *zero-specific-risk security* which:
- (1) is a short position in the case of a borrowing and a long position in the case of a deposit;
  - (2) has a value equal to the market value of the borrowing or deposit;
  - (3) has a maturity equal to that of the borrowing or deposit, or the next date the interest rate is reset (if earlier); and
  - (4) has a coupon equal to:
    - (a) zero, if the next interest payment date coincides with the maturity date; or
    - (b) the interest rate on the borrowing or deposit, if any interest is due to be paid before the maturity date.

#### OPTIONS AND WARRANTS

- 32 G Where included in this chapter's *PRR* calculation (see table 4G), *options* and *warrants* should be treated as follows:
- (1) An *option* or *warrant* on a debt *security* should be treated as a position in that debt *security*.
  - (2) An *option* on an interest rate should be treated as a position in a zero coupon *zero-specific-risk security* with a maturity equal to the sum of the time to expiry of the *option* and the length of the period for which the interest rate is fixed.
  - (3) An *option* on an *future* – where the *future* is based on an interest rate or debt *security* – should be treated as:
    - (a) a long position in that *future* for purchased call *options* and written put *options*; and

(b) a short position in that *future* for purchased put *options* and written call *options*.

(4) An *option* on a *swap* should be treated as a deferred starting *swap*.

#### BONDS WHERE THE COUPONS AND PRINCIPAL ARE PAID IN DIFFERENT CURRENCIES

33 G Where a debt *security* pays coupons in one currency, but will be redeemed in a different currency, it should be treated as:

(1) a debt *security* denominated in the coupon's currency; and

(2) a foreign exchange *forward* to capture the fact that the debt *security's* principal will be repaid in a different currency from that in which it pays coupons, specifically:

(a) a notional forward sale of the coupon currency and purchase of the redemption currency, in the case of a long position in the debt *security*; or

(b) a notional forward purchase of the coupon currency and sale of the redemption currency, in the case of a short position in the debt *security*.

#### INTEREST RATE RISK ON OTHER FUTURES, FORWARDS AND OPTIONS

34 G Other *futures, forwards, options* and *swaps* should be treated as positions in *zero-specific-risk securities*, each of which:

(1) has a zero coupon;

(2) has a maturity equal to that of the relevant contract; and

(3) is long or short according to table 35G.

35 G Table: Interest rate risk on other *futures, forwards, options* and *swaps* (see 34G).

Instrument	Notional positions		
Foreign exchange <i>forward</i> or <i>future</i>	a long position denominated in the currency purchased	<b>and</b>	a short position denominated in the currency sold
Gold <i>forward</i> or <i>future</i>	a long position if the <i>forward</i> or <i>future</i> involves an actual (or notional) sale of gold	<b>or</b>	a short position if the <i>forward</i> or <i>future</i> involves an actual (or notional) purchase of gold
<i>Equity forward</i> or <i>future</i> , or <i>option</i> (unless a <i>PRR</i> is calculated under the basic interest rate calculation in chapter TE)	A long position if the contract involves an actual (or notional) sale of the underlying <i>equity</i>	<b>or</b>	A short position if the contract involves an actual (or notional) purchase of the underlying <i>equity</i>

Deriving the net position in each debt security

36 G The net position is the difference between the value of the bank's long positions (including notional positions) and the value of its short positions (including notional positions) in the same debt *security*.

#### NETTING POSITIONS IN THE SAME DEBT SECURITY

37 G A bank should not net positions (including notional positions) unless:

- (1) long and short positions are in the same debt *security*, and a debt *security* is the same as another if and only if:
  - (a) they enjoy the same rights in all respects; and
  - (b) are fungible with each other; or
- (2) long and short positions are in different tranches of the same debt *security*, where the tranches:
  - (a) enjoy the same rights in all respects; and
  - (b) become fungible within 180 days, and thereafter the debt *security* of one tranche can be delivered in settlement of the other tranche.

#### NETTING THE CHEAPEST TO DELIVER SECURITY WITH OTHER DELIVERABLE SECURITIES

- 38 G A bank may net a short notional position in the cheapest to deliver *security* arising from a short *future* or *forward* (see 13G(2)(a)) against a long position in any deliverable *security* up to a maximum of 90% of the common nominal amounts. The residual long and short nominal amounts should be treated as separate long and short positions.
- 39 G The netting permitted by 38G only relates to where the bank has sold the *future* or *forward*. It does not relate to where the bank has bought a *future* or *forward*.

#### NETTING ZERO-SPECIFIC-RISK SECURITIES WITH DIFFERENT MATURITIES

- 40 G A bank may net a notional long position in a *zero-specific-risk security* against a notional short position in a *zero-specific-risk security* if:
- (1) they are denominated in the same currency;
  - (2) their coupons do not differ by more than 15 basis points; and
  - (3) they mature:
    - (a) on the same day, if they have residual maturities of less than one month;
    - (b) within seven days of each other, if they have residual maturities of between one month to one year; and
    - (c) within thirty days of each other, if they have residual maturities in excess of one year.

#### REDUCED NET UNDERWRITING POSITIONS IN DEBT SECURITIES

- 41 G A bank should not net a reduced net *underwriting* position in a debt *security* with any other debt *security* position.
- 42 G 41G only relates to reduced net *underwriting* positions.

#### Specific risk calculation

- 43 G A bank should calculate the specific risk *PRR* for each debt *security* by:
- (1) multiplying the market value of the individual net position (ignoring the sign) by the appropriate *PRA* from table 44G; and
  - (2) converting this amount into the bank's *base currency* at prevailing spot foreign exchange rates.
- 44 G Table: specific risk *PRAs* (see 43G).

Issuer	Residual maturity	PRA
An issue of, or fully guaranteed by, or fully collateralised by a <i>Zone A</i> central government or central bank or the European Communities	Any	0%
An issue of, or fully guaranteed by, a <i>Zone B</i> central government or central bank denominated in the local currency	Zero to 12 months	0%
Other <i>qualifying debt securities</i> (see 46G)	Zero to 6 months	0.25%
	6 to 24 months	1%
	Over 24 months	1.6%
<i>Non-qualifying debt securities</i>	Any	8%

45 G 43G includes both actual and notional positions. However, notional positions in *zero-specific-risk securities* do not attract specific risk. For example:

- (1) Interest rate *swaps*, foreign exchange *swaps*, *FRAs*, interest rate *futures*, foreign exchange *forwards*, foreign exchange *futures*, and the cash leg of *repurchase agreements* and *reverse repurchase agreements* create notional positions which will not attract specific risk; whilst
- (2) *Futures*, *forwards* and *swaps* which are based on the price (or yield) of one or more debt *securities* will create at least one notional position that attracts specific risk.

#### DEFINITION OF A QUALIFYING DEBT SECURITY

46 G A debt *security* is a *qualifying debt security* if:

- (1) it attracts zero specific risk under table 44G; or
- (2) it is issued by, or fully guaranteed by:
  - (a) a *Zone B* central government or central bank and the *security* is denominated in the local currency of the issuer;
  - (b) a multilateral development bank listed in 3.2.4 of chapter BC
  - (c) a *Zone A* public sector entity;

- (d) a company whose *equity* is a constituent of one of the indices making up the FTSE All-World Index; or
  - (e) an issue of, or fully guaranteed by an *investment firm* or *recognised third-country investment firm*.
- (3) it is issued by, fully guaranteed by, endorsed or accepted by:
- (a) a credit institution incorporated in a *Zone A* country; or
  - (b) a credit institution incorporated in a *Zone B* country and the debt *security* has a residual maturity of one year or less.
- (4) it is a mortgage backed security which meets the criteria in 7e of section 3.2.5 of chapter BC.
- (5) it is rated by at least one of the agencies shown in table 47G, and every such rating equals or exceeds the corresponding minimum shown in that table.

47 G Table: minimum ratings for *qualifying debt securities* (see 46G(5)).

Issuer	Rating agency	Minimum Rating	
		<i>Securities</i>	Money Market Obligations
Any	Moody's Investors Service	Baa3	P3
	Standard & Poor's Corporation	BBB-	A3
	FITCH Ratings Ltd	BBB-	F-3
Canadian	Canadian Bond Rating Service	B+++low	A-3
	Dominion Bond Rating Service	BBB low	R-2
Japanese	Japan Credit Rating Agency, Ltd	BBB-	J-2
	Mikuno & Co	BBB	M-3
	Japan Rating & Investment Information Inc	BBB-	a-2

#### General market risk calculation

- 48 G A bank should calculate the general market risk *PRR* for each currency using either:
- (1) the simplified maturity method;
  - (2) the maturity method; or
  - (3) the duration method (subject to 50G).

- 49 G A bank should convert all general market risk *PRRs* into its *base currency* using prevailing foreign exchange spot rates.
- 50 G A bank should not use the duration method for index-linked *securities*. Instead, these *securities* should:
- (1) be attributed a coupon of 3%; and
  - (2) treated separately under either the simplified maturity method or the maturity method.

#### SIMPLIFIED MATURITY METHOD

- 51 G The simplified maturity method weights individual net positions to reflect their price sensitivity to changes in interest rates. The weights are related to the coupon and the residual maturity of the instrument (or the next interest rate re-fix date for floating rate items).
- 52 G Under the simplified maturity method, the *PRR* for general market risk equals the sum of each individual net position (long or short) multiplied by the appropriate *PRA* in table 53G.
- 53 G Table: general market risk *PRAs* (see 52G).

Zone	Maturity band		<i>PRA</i>
	Coupon of 3% or more	Coupon of less than 3%	
One	0 ≤ 1month	0 ≤ 1month	0.00%
	> 1 ≤ 3months	> 1 ≤ 3months	0.20%
	> 3 ≤ 6 months	> 3 ≤ 6 months	0.40%
	> 6 ≤ 12 months	> 6 ≤ 12 months	0.70%
Two	> 1 ≤ 2 years	> 1.0 ≤ 1.9 years	1.25%
	> 2 ≤ 3 years	> 1.9 ≤ 2.8 years	1.75%
	> 3 ≤ 4 years	> 2.8 ≤ 3.6 years	2.25%
Three	> 4 ≤ 5 years	> 3.6 ≤ 4.3 years	2.75%
	> 5 ≤ 7 years	> 4.3 ≤ 5.7 years	3.25%
	> 7 ≤ 10 years	> 5.7 ≤ 7.3 years	3.75%
	> 10 ≤ 15 years	> 7.3 ≤ 9.3 years	4.50%
	> 15 ≤ 20 years	> 9.3 ≤ 10.6 years	5.25%
	> 20 years	> 10.6 ≤ 12.0 years	6.00%
		> 12.0 ≤ 20.0 years	8.00%
	> 20 years	12.50%	

#### THE MATURITY METHOD

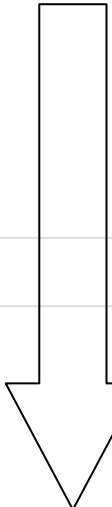
- 54 G The maturity method builds on the simplified maturity method by partially recognising offsetting positions. 57G provides an illustration of the maturity method.

- 55 G Under the maturity method, the *PRR* for general market risk is calculated as follows:
- (1) Step 1: each net position is allocated to the appropriate maturity band in table 53G and multiplied by the corresponding *PRR*.
  - (2) Step 2: weighted long and short positions are matched within:
    - (a) the same maturity band;
    - (b) the same zone (using unmatched positions from (a)); and
    - (c) different zones (using unmatched positions from (b)).
  - (3) Step 3: the *PRR* for general market risk is the sum of:
    - (a) 10% of the total amount matched within maturity bands;
    - (b) 40% of the amount matched within zone 1 under (2)(b);
    - (c) 30% of the amount matched within zones 2 & 3 under (2)(b);
    - (d) 40% of the amounts matched between zones 1 and 2, and between zones 2 and 3;
    - (e) 150% of the amount matched between zones 1 and 3; and
    - (f) 100% of the weighted positions remaining unmatched after (2)(c);
- 56 G Table 53G distinguishes between debt *securities* with a coupon of less than 3% and those with coupon in excess of 3%. However, this doesn't mean that the bank has to do a separate general market risk calculation for each, it merely ensures that when allocating debt *securities* to a particular band, their coupons are taken into account as well as their maturities. So for example, a 21 year 6% debt *security* falls into the same band as an 11 year 2% debt *security*. They are both weighted at 6%, and can be matched under the first part of step two because they fall within the same band.




57 G An example of the maturity method calculation. In this example, a bank with a £ sterling *base currency* is processing its euro denominated positions.

**Weight each position**



Zone	Totals of:		PRA		Weighted longs within each band	Weighted shorts within each band
	net longs within the band	net shorts within the band				
1	€100	€50	0.00%		0	0
	€250	€0	0.20%		<b>0.50</b>	0
	€200	€0	0.40%		<b>0.80</b>	0
	€0	€0	0.70%		0	0
2	€140	€0	1.25%		<b>1.75</b>	0
	€200	€300	1.75%		<b>3.50</b>	<b>5.25</b>
	€0	€400	2.25%		0	<b>9</b>
3	€0	€0	2.75%		0	0
	€200	€200	3.25%		<b>6.50</b>	<b>6.50</b>
	€300	€0	3.75%		<b>11.25</b>	0
	€200	€300	4.50%		<b>9</b>	<b>13.50</b>
	€0	€14.30	5.25%		0	<b>0.75</b>
	€300	€0	6.00%		<b>18.00</b>	0
	€0	€0	8.00%		0	0
€0	€0	12.50%		0	0	

**Match weighted positions**



same band		same zones		different zones	
Long	Short	Long	Short	Long	Short
0.50		0.50		1.30	
0.80		0.80			
1.75		1.75	1.75		9.00
3.50	5.25		9		
	9				
6.50	6.50				
11.25		11.25	4.50	24.00	
9	13.50		0.75		
	0.75				
18.00		18.00			
<b>19 matched</b>		<b>7 matched</b>		<b>9 matched</b>	

**Calculate the general market risk**

Matched within bands	19	@	10%	=	1.9
Matched within zone 1	0	@	40%	=	0
Matched within zones 2&3	7	@	30%	=	2.1
Matched between zones 1&2 and 2&3	9	@	40%	=	3.6
Matched between zones 1&3	0	@	150%	=	0
Unmatched after 2(c)	16.30	@	100%	=	16.30
<b>total = € 23.90</b>					
<b>general market risk PRR (if €1=£0.60) = £14.34</b>					

#### DURATION METHOD

- 58 G The duration method produces a more accurate measure of interest rate risk than the maturity methods but it is also more complex to calculate.
- 59 G Banks should use the following formula to calculate modified duration:

$$\text{Modified Duration} = \frac{D}{(1+r)} \qquad D = \frac{\sum_{t=1}^m \frac{tC_t}{(1+r)^t}}{\sum_{t=1}^m \frac{C_t}{(1+r)^t}}$$

Where:  $C_t$  = cash payment at time  $t$   
 $m$  = total maturity  
 $r$  = yield to maturity, based on the current mark to market of the debt *security*. In the case of a floating rate instrument, this is calculated on the assumption that the principal is due on the date that the interest rate can next be changed  
 $t$  = time

- 60 G Under the duration method, the *PRR* for general market risk is calculated as follows:
- (1) Step 1: allocate each net position to the appropriate duration zone in table 61G and multiply it by:
    - (a) its modified duration (using the formula in 59G); and
    - (b) the appropriate assumed interest rate change in table 61G.
  - (2) Step 2: match weighted long and short positions:
    - (a) within timebands;
    - (b) within zones (using unmatched positions from (2)(a)); and
    - (c) across zones (using unmatched positions from (2)(b));
  - (3) Step 3: calculate the general market risk as the sum of:
    - (a) 100% of the weighted positions remaining unmatched after (2)(c);
    - (b) 5% of the matched weighted position in each timeband;
    - (c) 40% of the matched weighted position in zone 1;

- (d) 30% of the matched weighted position in zones 2 and 3;
- (e) 40% of the matched weighted position between zones 1 and 2, and between zones 2 and 3; and
- (f) 150% of the matched weighted position between zones 1 and 3.

61 G Table: Assumed interest rate change in the duration method (see 60G).

Zone	Modified Duration	Assumed interest rate change (percentage points)
1	$0 \leq 1$ months	1.00
	$> 1 \leq 3$ months	1.00
	$> 3 \leq 6$ months	1.00
	$> 6 \leq 12$ months	1.00
2	$> 1.0 \leq 1.9$ years	0.90
	$> 1.9 \leq 2.8$ years	0.80
	$> 2.8 \leq 3.6$ years	0.75
3	$> 3.6 \leq 4.3$ years	0.75
	$> 4.3 \leq 5.7$ years	0.70
	$> 5.7 \leq 7.3$ years	0.65
	$> 7.3 \leq 9.3$ years	0.60
	$> 9.3 \leq 10.6$ years	0.60
	$> 10.6 \leq 12$ years	0.60
	$> 12.0 \leq 20$ years	0.60
	$> 20$ years	0.60

Definitions used in chapter TI

62 G This chapter uses the following definitions:

Defined term	Definition
<i>Base currency</i>	The currency in which the bank's accounts are prepared.
<i>Commodity</i>	Any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB the definition of commodity used in TI deliberately differs from that in the main Handbook Glossary).
<i>Convertible</i>	A <i>security</i> which gives the investor the right to convert the <i>security</i> into <i>equity</i> at an agreed price or on an agreed basis.
<i>Derivative</i>	<i>Options, futures</i> and contracts for differences.
<i>Equity</i>	See <i>share</i> .
<i>Forward</i>	A contract to buy or sell where the date of settlement has been agreed as a particular date in the future.
<i>Forward rate</i>	An agreement in which two parties agree on the payment by

<i>agreement</i>	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.
<i>FRA</i>	<i>Forward rate agreement.</i>
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>Investment firm</i>	As defined in section 1 of chapter CB.
<i>Option</i>	A contract which confers the right to buy a <i>security</i> , contractually based investment or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>Preference securities</i>	A share with rights, in respect of capital and dividends, superior to those of ordinary <i>equity</i> .
<i>PRA</i>	Percentage risk addition.
<i>PRR</i>	Position risk requirement.
<i>Qualifying debt security</i>	As defined in 46G.
<i>Recognised third country investment firm</i>	An <i>investment firm</i> which is subject to the prudential rules of one of the regulators listed in appendix C to chapter CS.
<i>Repurchase agreement</i>	See section 3.2, 2(b)a) of chapter TC.
<i>Reverse repurchase agreement</i>	See section 3.2, 2(b)a) of chapter TC.
<i>Security</i>	As defined in article 3(1) of the Regulated Activities Order.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.
<i>Synthetic future</i>	A combination of a long (short) call <i>option</i> and a short (long) put <i>option</i> which are based on the same underlying and have the same notional amount, strike and maturity.
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.
<i>Underwriting</i>	The arrangement under which a party agrees to buy, before issue, a specified quantity of securities in an issue of securities on a given date and at a given price, if no other has purchased or acquired them.
<i>Zero-specific-risk securities</i>	A hypothetical debt <i>security</i> used to represent the general interest rate risk arising from certain <i>derivative</i> and <i>forward</i> transactions.

<i>Warrant</i>	The investment specified in article 79 of the Regulated Activities Order (Instruments giving entitlement to investments).
<i>Zone A</i>	As defined in section 3.2.8 of chapter BC.
<i>Zone B</i>	As defined in section 3.2.8 of chapter BC.

## Annex D

### Chapter TE (Equity position risk requirement)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter TE in its entirety and replace with the following text:

TE

Equity PRR

General

- 1 G A UK bank to which CAD applies should apply this chapter and calculate its *equity PRR* by:
- (1) identifying which *equity* positions should be included within the scope of the *PRR* calculation (see 2G);
  - (2) deriving the net position in each *equity* in accordance with 22G -25G;
  - (3) including each of those net positions in either the simplified equity method (see 29G) or, subject to 27G, the standard equity method (see 32G); and
  - (4) summing the *PRR* on each net position as calculated under the simplified and standard equity methods.

Scope of the Equity PRR calculation

- 2 G A bank's *equity PRR* calculation should:
- (1) include all *trading book* positions in *equities*, unless:
    - (a) the position is fully deducted from capital under 2(c) of section 10.2 of chapter CA, in which case the bank may exclude it;
    - (b) the position is hedging an *option* or *warrant* which is being treated under 26G of chapter TO; and
  - (2) include notional positions arising from *trading book* positions in the instruments listed in table 3G.
- 3 G Table: Instruments which result in notional positions (see 2G(2))

Instrument	See
Depository receipts	12G
<i>Convertibles</i> where:(a) the <i>convertible</i> is trading at a market price of less than 110% of the underlying <i>equity</i> ; and the first date at which conversion can take place is	13G

less than three months ahead, or the next such date (where the first has passed) is less than a year ahead; or  (b) the conditions in (a) are not met but the bank includes the <i>convertible</i> in its <i>equity PRR</i> calculation rather than including it in its interest rate <i>PRR</i> calculation set out in chapter TI.	
<i>Futures, forwards, CFDs and synthetic futures on a single equity</i>	14G
<i>Futures, forwards, CFDs and synthetic futures on a basket of equities or an equity index</i>	15G
<i>Equity legs of an equity swap</i>	19G
<i>Options or warrants on a single equity, an equity future, a basket of equities or an equity index (unless the bank calculates a PRR on the option or warrant under chapter TO).</i>	21G

- 4 G 2G(1) includes a *trading book* position in an *equity* that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the *equity* had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the *equity* would not have been included in the *trading book* in the first place.
- 5 G 2G(1) includes net *underwriting* positions, or reduced net *underwriting* positions in *equities*. 27G requires banks to use the simplified equity method in the case of reduced net *underwriting* positions. In the case of net *underwriting* positions that haven't been reduced according to 24G of chapter TU, there is no such restriction; a bank can choose which of the two equity methods to use.
- 6 G Banks are reminded that table 5G in chapter TO divides *equity options* and *warrants* into:
- (1) those which should be treated under chapter TO; and
  - (2) those which should be treated under either chapter TE or chapter TO, but banks can choose whether chapter TE or TO is used.
- 7 G Under table 3G, not every *convertible* need be included in this chapter's *PRR* calculation. Where a *convertible* is not included in this chapter's *PRR* calculation, 3G(1)(a) of chapter TI states that it should be included in the chapter TI *PRR* calculation.
- 8 G Some of the instruments listed in table 3G are also included in a bank's interest rate *PRR* calculation. For simplicity, a bank may use the interest rate *PRR* calculation at the end of this chapter rather than the calculation in chapter TI. 41G explains this in more detail.

## Derivation of notional positions

- 9 G This section converts the instruments listed in table 3G into notional positions in individual *equities*, *equity* baskets, or *equity* indices.
- GENERAL
- 10 G Unless specified otherwise, the value of each notional *equity* position equals the quantity of that *equity* underlying the instrument multiplied by the current market value of the *equity*.
- 11 G For example, the current market value of a particular *equity* is £2.50. If a bank contracts to sell this *equity* in five years' time for £3 it would treat the notional short *equity* position as having a value of £2.50 when calculating the *equity PRR*.

In effect, the forward position has been treated as being equivalent to a spot position for the purposes of calculating *equity PRR*. To capture the risk that the forward price changes relative to the spot price, forward *equity* positions are included in the bank's interest rate *PRR* calculation (see 42G of this chapter or 4G of chapter TI).

## DEPOSITORY RECEIPTS

- 12 G A depository receipt should be treated as a notional position in the underlying *equity*.

## CONVERTIBLES

- 13 G Where a *convertible* is included in this chapter's *PRR* calculation (see table 3G):
- (1) it should be treated as a position in the *equity* into which it converts; and
  - (2) the bank's *equity PRR* should be adjusted by making:
    - (a) an addition equal to the current value of any loss which the bank would make if it did convert to *equity*; or
    - (b) a deduction equal to the current value of any profit which the bank would make if it did convert to *equity* (subject to a maximum reduction equal to the *PRR* on the notional position underlying the *convertible*).

## FUTURES, FORWARDS AND CFDs ON A SINGLE EQUITY

- 14 G A *future*, *forward* or *CFD* on a single *equity* should be treated as a notional position in that *equity*.

## FUTURES, FORWARDS AND CFDs ON EQUITY INDICES OR BASKETS

- 15 G A *future*, *forward* or *CFD* on an *equity* index or basket should be treated as either:
- (1) a position in each of the underlying *equities*; or



(2) the positions shown in table 16G.

16 G Table: equity index or basket contracts (see 15G(2))

	Under the simplified equity method (29G)	Under the standard equity method (32G)
Only one country in the index or basket (see 32G)	One position in the index or basket	One position in the index or basket
More than one country in the index or basket	One position in the index or basket	Several notional basket positions, one for each country Or One notional basket position in a separate, hypothetical country

17 G For example, a bank decides to treat a FTSE Eurotop 300 *future* under the standard equity method, and furthermore, chooses to treat it as one notional position. Under table 16G a bank should treat this notional position as if it were from a separate hypothetical “country” rather than any of the countries to which the underlying *equities* are from.

18 G The notional positions created under 15G have the following values:

- (1) where only one notional position is created, it has a value equal to the total market value of the *equities* underlying the contract; or
- (2) where more than one notional position is created, each one has a value which reflects that relevant *equity's* or country's contribution to the total market value of the *equities* underlying the contract.

#### EQUITY LEGS OF EQUITY SWAPS

19 G The *equity* leg of an *equity swap* should be treated as a position in the underlying *equity*, basket of *equities* or *equity* index, which is:

- (1) long, if the bank has contracted to receive any increase and pay any decrease in the value of the underlying *equities* or *equity* index; and
- (2) short, if the bank has contracted to receive any decrease and pay any increase in the value of the underlying *equities* or *equity* index.

- 20 G The interest rate leg of an *equity swap* is included in a bank's interest rate *PRR* calculation (see table 4G of chapter II).

#### OPTIONS

- 21 G If included in this chapter's *PRR* calculation (see table 3G), *options* should be treated as follows:
- (1) an *option* on a single *equity* should be treated as a notional position in that *equity*;
  - (2) an *option* on a basket of *equities* or *equity* index should be treated as a *future* on that basket or index; and
  - (3) an *option* on an *equity future* should be treated as:
    - (a) a long position in that *future*, for purchased call *options* and written put *options*; and
    - (b) a short position in that *future*, for purchased put *options* and written call *options*.

#### Deriving the net position in each equity

- 22 G The net position is the difference between the value of the bank's long positions (including notional positions) and the value of its short positions (including notional positions) in the same *equity*.
- 23 G When deriving the net position in each *equity*, a bank should not net long and short positions unless:
- (1) they are positions in the same *equity*. Two *equities* are the same if:
    - (a) they enjoy the same rights in all respects; and
    - (b) are fungible with each other; or
  - (2) they are positions in different tranches of the same *equity* and the tranches:
    - (a) enjoy the same rights in all respects; and
    - (b) become fungible for each other within 180 days, and thereafter the *equity* of one tranche can be delivered in settlement of the other tranche.
- 24 G A bank should not net a reduced net *underwriting* position with any other *equity* position.
- 25 G 24G only relates to reduced net *underwriting* positions.

Simplified and standard equity methods

- 26 G 1G(3) states that the net position in each *equity* should be included in either the simplified equity method or the standard equity method, though indicates that this choice should be subject to the restrictions in 27G. A bank does not have to use the same method for all *equities*.
- 27 G A bank should use the simplified equity method for reduced net *underwriting* positions.
- 28 G A bank may use either method for a net *underwriting* position; 27G only relates to reduced net *underwriting* positions.

SIMPLIFIED EQUITY METHOD

- 29 G Under the simplified method, the *PRR* for each *equity*, *equity* index or *equity* basket equals the market value of the net position (ignoring the sign) multiplied by the appropriate *PRA* from table 30G. The result should be converted into the bank's *base currency* at current spot foreign exchange rates.
- 30 G Table: simplified equity method *PRAs* (see 29G)

	<b>PRA</b>
Single <i>equities</i>	16%
<i>Qualifying equity indices</i> (see 38G)	8%
All other <i>equity</i> indices or baskets	16%

STANDARD EQUITY METHOD

- 31 G The standard equity method divides the risk of loss from a bank's *equity* positions into the risk of loss from a general move in that country's *equity* market and the risk of loss from an individual *equity's* price changing relative to that country's *equity* market. These are called general market risk and specific risk respectively.
- 32 G Under the standard equity method, a bank should:
- (1) Group *equity* positions into country portfolios as follows:
    - (a) A position in an individual *equity* belongs to:
      - (i) the country it is listed in;
      - (ii) any of the countries it is listed in, if more than one; or
      - (iii) the country it was issued from, if unlisted.

- (b) A position in *equity* basket or index that is treated under 15G(2), is allocated to one or more country portfolios based on the countries to which the underlying *equities* belong to under (a) above.
- (2) Sum:
  - (a) the *PRRs* for specific risk calculated under 33G; and
  - (b) the *PRRs* for general market risk for each country portfolio as calculated under 40G.

SPECIFIC RISK

- 33 G Under the standard equity method, a bank should calculate a *PRR* for specific risk based on the net position in each *equity*, *equity index* or *equity* index by:
  - (1) multiplying its market value (ignoring the sign) by the appropriate *PRA* from table 34G; and
  - (2) converting it into the bank's *base currency* using current spot foreign exchange rates.
- 34 G Table: *PRAs* for specific risk under the standard approach (see 33G(1))

	<b>PRA</b>
Qualifying <i>equities</i> (see 35G)	4%
Qualifying <i>equity indices</i> (see 38G)	0%
All other <i>equities</i> and <i>equity</i> indices	8%

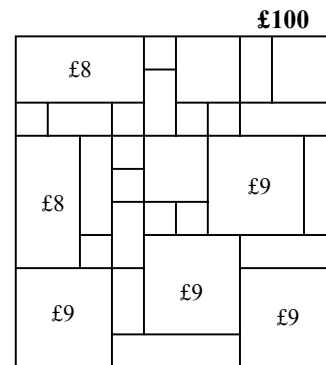
- 35 G For the purposes of table 34G, a qualifying *equity* is one which:
  - (1) belongs to a country portfolio where:
    - (a) no individual position exceeds 10% of the portfolio's gross value; and
    - (b) the sum of positions (ignoring the sign) which individually represent between 5% and 10% of the portfolio's gross value, does not exceed 50% of the portfolio's gross value; and
  - (2) is a constituent of an index in table 39G.

- 36 G The following example illustrates 35G(1). A country portfolio has a gross value of £100 and is made up of positions in 29 different *equities* (some are long positions, others are short positions). Not all the *equities* are constituents of an index used to create the FT All-World Index (this criteria only becomes relevant once a bank has determined whether the country portfolio meets the test in 35G(1)).

Six positions exceed the 5% threshold. The diagram below shows the composition of the portfolio.

Part (a): the portfolio meets the first part of the test because no individual position is worth more than 10% of the portfolio's value.

Part (b): the portfolio fails the second part of the test because the sum (ignoring the sign) of the six relevant positions is £52; this exceeds 50% of the portfolio's value.

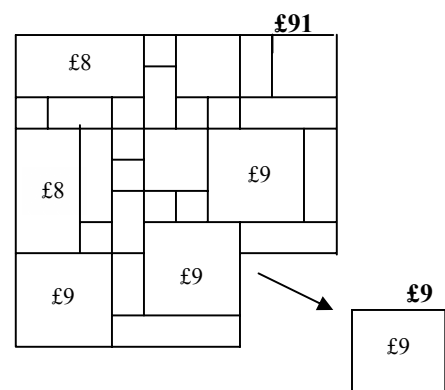


- 37 G A country portfolio can be split into two sub-portfolios if this enables one sub-portfolio to meet the conditions in 35G. Individual positions may be sub-divided between sub-portfolios.

Continuing the example above, one of the largest positions is taken out of the portfolio and put into a new portfolio. The new portfolio fails the two tests, but the amended portfolio meets both tests:

Part (a): no single remaining position exceeds £9.10.

Part (b): the sum of the five relevant positions is £43, this is less than 50% of the new portfolio's value of £91.



- 38 G A *qualifying equity index* is one which:

- (1) is listed in table 39G; or
- (2) is not listed in table 39G, but is constructed such that:
  - (a) it contains at least 20 *equities*;
  - (b) no single *equity* represents more than 20% of the total index; and

(c) no five *equities* combined represent more than 60% of the total index.

39 G Table: *Qualifying equity indices* (see 38G)

<b>Qualifying equity indices</b>	
Australia	All Ordinaries
Austria	Austrian Traded Index
Belgium	BEL 20
Canada	TSE 35, TSE 100, TSE 300
France	CAC 40, SBF 250
Germany	DAX
European	Dow Jones Stoxx 50 Index, FTSE Eurotop 300, MSCI Euro Index
Hong Kong	Hang Seng 33
Italy	MIB 30
Japan	Nikkei 225, Nikkei 300, TOPIX
Korea	Kospi
Netherlands	AEX
Singapore	Straits Times Index
Spain	IBEX 35
Sweden	OMX
Switzerland	SMI
UK	FTSE 100, FTSE Mid 250, FTSE All Share
US	S&P 500, Dow Jones Industrial Average, NASDAQ Composite, Russell 2000

#### GENERAL MARKET RISK

40 G The *PRR* for general market risk equals the net value (ignoring the sign) of the country portfolio multiplied by 8%. It should be converted into the bank's *base currency* using current spot foreign exchange rates.

#### Basic interest rate *PRR* calculation for equity instruments

41 G A basic *PRR* calculation is included in this chapter for those banks that do not wish to use the calculation in chapter TI. However, it tends to result in higher charges than the methods in chapter TI, largely because the interest rate *PRR* is calculated on each notional equity position separately and then summed without offsetting long and short positions.

42 G Where a bank does not include a *forward*, *future*, or *option* (except cliques) or *swap* on an *equity*, basket of *equities* or *equity* index in its chapter TI *PRR* calculation, it should calculate an interest rate *PRR* as follows:

- (1) multiplying the market value of the notional *equity* position underlying the instrument by the appropriate percentage from table 44G; and

(2) summing the results from (1), ignoring the sign.

- 43 G Cliquets on *equities*, baskets of *equities* or *equity* indices do not attract an interest rate *PRR*. 42G excludes them from the basic interest rate *PRR* calculation and table 4G excludes them from the scope of the interest rate *PRR* calculation in chapter TI.
- 44 G Table: Percentages used in the basic interest rate *PRR* calculation for *equity* instruments (see 42G(1))

Time to expiration	Percentage
$0 \leq 3$ months	0.20
$> 3 \leq 6$ months	0.40
$> 6 \leq 12$ months	0.70
$> 1 \leq 2$ years	1.25
$> 2 \leq 3$ years	1.75
$> 3 \leq 4$ years	2.25
$> 4 \leq 5$ years	2.75
$> 5 \leq 7$ years	3.25
$> 7 \leq 10$ years	3.75
$> 10 \leq 15$ years	4.50
$> 15 \leq 20$ years	5.25
$> 20$ years	6.00

Definitions used in chapter TE

- 45 G This chapter uses the following definitions:

Defined term	Definition
<i>Base currency</i>	The currency in which the bank's accounts are prepared.
<i>CFDs</i>	Means contract for differences.
<i>Convertible</i>	A <i>security</i> which gives the investor the right to convert the <i>security</i> into <i>equity</i> at an agreed price or on an agreed basis.
<i>Derivative</i>	<i>Options</i> , <i>futures</i> and contracts for differences.
<i>Equity</i>	See <i>share</i> .
<i>Forward</i>	A contract to buy or sell where the date of settlement has been agreed as a particular date in the future.
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>Option</i>	A contract which confers the right to buy a <i>security</i> , contractually based investment or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>PRA</i>	Percentage risk addition.

<i>PRR</i>	Position risk requirement.
<i>Qualifying equity index</i>	As defined in 38G.
<i>Repurchase agreement</i>	See section 3.2, and 2(b)a) of chapter TC.
<i>Reverse repurchase agreement</i>	See section 3.2, and 2(b)a) of chapter TC.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.
<i>Synthetic future</i>	A combination of a long (short) call <i>option</i> and a short (long) put <i>option</i> which are based on the same underlying and have the same notional amount, strike and maturity.
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.
<i>Underwriting</i>	The arrangement under which a party agrees to buy, before issue, a specified quantity of securities in an issue of securities on a given date and at a given price, if no other has purchased or acquired them.
<i>Warrant</i>	The investment specified in article 79 of the Regulated Activities Order (Instruments giving entitlement to investments).



## Annex E

### Chapter TU (Securities underwriting)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter TU in its entirety and replace with the following text:

TU

Securities Underwriting

General

- 1 G A UK bank to which CAD applies should apply this chapter. This chapter sets out the method for calculating a net *underwriting* position or reduced net *underwriting* position, which is then included in the *PRR* calculation in other chapters, or chapter BC if the bank does not have a *trading book*.
- 2 G A bank which *underwrites* or sub-*underwrites* an issue of *securities* should:
  - (1) identify commitments to *underwrite* or sub-*underwrite* which give rise to an *underwriting* position (see 8G);
  - (2) identify the time of initial commitment (see 14G);
  - (3) calculate the net *underwriting* position (set out in 18G) or reduced net *underwriting* position (in the circumstances set out in 24G);
- 3 G A bank should include the net *underwriting* position or reduced net *underwriting* position in:
  - (1) 3G(1) of chapter TI, where debt *securities* are being underwritten;
  - (2) 2G(1) of chapter TE, where *equities* are being underwritten;
  - (3) 22G of chapter TO, where *warrants* are being underwritten; or
  - (4) chapter BC, where the bank does not have a *trading book*; and
  - (5) 2G of chapter FX, where the *equities*, debt *securities* or *warrants* being underwritten are denominated in a *foreign currency*.
- 4 G A bank should comply with 2G from initial commitment (as determined under 8G) until the end of the fifth *business day* after *working day 0* (as determined under 23G).

- 5 G Sub-*underwriting* is a commitment given by one bank to someone other than the issuer or seller of the *securities*, to *underwrite* all or part of an issue of *securities*.
- 6 G The net *underwriting* position calculated in 18G will also be used in calculating the net *underwriting exposure* set out in 32G.
- 7 G The net *underwriting* position or reduced net *underwriting* position arising from *underwriting* or sub-*underwriting* a rights or *warrants* issue should be calculated using the current market price of the underlying *security* for the purposes of the *equity PRR* or *option PRR*. However, the *PRR* will be limited to the value of the net *underwriting* position calculated using the initial issue price of the rights or *warrants*.

#### Commitments to underwrite securities

- 8 G For the purpose of 2G(1), a bank has a commitment to *underwrite* or sub-*underwrite* an issue of *securities* where:
- (1) it gives a commitment to an issuer of *securities* to *underwrite* an issue of *securities*;
  - (2) it gives a commitment to a person, other than the issuer of *securities*, to sub-*underwrite* an issue of *securities*; or
  - (3) it is a member of a syndicate or group that gives a commitment to an issuer to *underwrite* an issue of *securities* or a commitment to a person other than the issuer of *securities*, to sub-*underwrite* an issue of *securities*.
- 9 G Block trades including bought deals, private placements, revolving *underwriting* facilities and *underwriting* syndicated loans are not within the scope of this chapter.
- 10 G For the purpose of this chapter, *securities* include debt and *equity* instruments and instruments which are convertible into *securities* but excludes loans.
- 11 G A bank that buys and sells *securities* before issue is dealing in the grey market. This chapter does not apply to a bank dealing in the grey market unless the bank:
- (1) has an *underwriting* commitment to the issuer in respect of those *securities*; or
  - (2) has a sub-*underwriting* commitment in respect of those *securities* and is using the grey market solely for the purpose of reducing that sub-*underwriting* commitment.
- 12 G In this chapter the grey market is the market in which dealers "buy" and "sell" *securities* ahead of issue. In reality the dealers are buying and selling promises to deliver the *securities* when issued.

- 13 G Where a single bank is involved in both *underwriting* or sub-*underwriting* an issue of *securities* as well as dealing in that issue for proprietary trading purposes this chapter will not apply to grey market transactions undertaken by the proprietary trading part of the bank.

#### Time of initial commitment

- 14 G Subject to 15G, the time of initial commitment is the earlier of:
- (1) the time the bank signs an agreement with the issuer of *securities* to *underwrite* those *securities*; or
  - (2) the time the price and allocation of the issue are set.
- 15 G If a bank has an irrevocable and unfettered right to withdraw from an *underwriting* commitment, exercisable within a certain period, the commitment commences when that right expires.
- 16 G Subject to the existence of a right described in 15G an *underwriting* commitment commences even if it is subject to formal, legal or other conditions that would normally be expected to be satisfied.
- 17 G A force majeure or material adverse change clause would not be a right of the sort referred to in 15G.

#### Calculating the net underwriting position

- 18 G A bank should calculate a net *underwriting* position by adjusting the gross amount it has committed to *underwrite* for:
- (1) any sales or sub-*underwriting* commitments received that have been confirmed in writing at the time of initial commitment;
  - (2) any *underwriting* or sub-*underwriting* commitments obtained from others since the time of initial commitment;
  - (3) any purchases or sales of the *securities* since the time of initial commitment, (other than those referred to in 13G); and
  - (4) any allocation of *securities* granted or received, arising from the commitment to *underwrite* the *securities*, since the time of initial commitment.
- 19 G A bank signing an *underwriting* agreement with an issuer of *securities* where the exact issue price or allocation of *securities* has not been fixed should calculate the gross amount, for the purposes of 18G, as the amount it has formally committed to under that agreement until the time the exact issue price and/or allocation is set.

- 20 G Allocations may arise, after date of initial commitment, from the agreement to *underwrite*. For example obligations or rights to or from the issuer, the *underwriting* group or syndicate.

#### GREY MARKET TRANSACTIONS

- 21 G Subject to 11G and 13G a bank can include grey market transactions when calculating the net *underwriting* position.

#### OVER-ALLOTMENT OPTIONS

- 22 G When calculating the net *underwriting* position, a bank should exclude an over-allotment option granted to it by the issuer, except to the extent it reduces:
- (1) from *working day 0* an over-allotment made by the bank; or
  - (2) from *working day 0* an over-allotment made by the bank on behalf of another member of the underwriting syndicate who has been granted the over-allotment option.
- 23 G For the purposes of this chapter *working day 0* is the *business day* on which the bank becomes unconditionally committed to accepting a known quantity of *securities* at a specified price, as follows:
- (1) For debt issues and *securities* which are issued in a similar manner, *working day 0* is the later of the date on which the *securities* are allotted, and the date on which payment for them is due.
  - (2) For *equity* issues and *securities* which are issued in a similar manner, *working day 0* is the later of the date on which the offer becomes closed for subscriptions and the date on which the allocations are made public.
  - (3) For rights issues, *working day 0* is first day after the date on which the offer becomes closed to acceptances for subscription.

#### Calculating the reduced net underwriting position

- 24 G A bank may apply the relevant reduction factors in table 27G to its net *underwriting* position if the *securities* it is *underwriting* or sub-*underwriting* are new *securities*.
- 25 G For the purposes of this chapter, a bank may treat as new *securities*:
- (1) *securities* that have not previously been offered for sale or subscription by an issuer; or
  - (2) *securities* that have not previously been traded on a *recognised investment exchange*, *designated investment exchange* or a *regulated market*.

26 G To calculate the reduced net *underwriting* position a bank should apply table 27G to the net *underwriting* position (calculated under 18G) as follows:

- (1) In respect of debt *securities*, a bank should calculate two reduced net *underwriting* positions; one for inclusion in the bank's specific risk calculation (see 43G of chapter TI), the other for inclusion in its general market risk calculation (see 48G of chapter TI).
- (2) In respect of *equities*, a bank should calculate only one reduced net *underwriting* position and then include it in the simplified equity method (see 27G of chapter TE).

27 G Table: Net *underwriting* position reduction factors (see 26G)

Underwriting timeline	Debt		Equity
	General market risk	Specific risk	
Time of initial commitment until <i>working day 0</i>	0%	100%	90%
Working day 1	0%	90%	90%
Working day 2	0%	75%	75%
Working day 3	0%	75%	75%
Working day 4	0%	50%	50%
Working day 5	0%	25%	25%
Working day 6 and onwards	0%	0%	0%

- 28 G Figure: An example of the reduced net *underwriting* position calculation. The example is based on the bank starting with a commitment to underwrite £100 million of a new *equity* issue.

Time	Net underwriting position (see 18G)	Percentage reduction (see 27G)	Reduced net underwriting position <sup>1</sup>
At initial commitment 9.00am Monday	£100m gross amount is reduced by £20m due to sales/ sub- <i>underwriting</i> commitments confirmed in writing at the time of initial commitment (see 12R(1)). = £80m	90%	£8m
Post initial commitment 9.02am Monday	Remaining £80m is reduced by £40m due to further sales, sub- <i>underwriting</i> commitments obtained and allocations granted (see 12R(2) – (4)). = £40m	90%	£4m
At the end of working day 1	Remaining £40m is reduced to £20m due to further sales. = £20m	90%	£2m
End of working day 3	Remaining £20m is reduced to £5m due to further sales. = £5m	75%	£1.25 m
End of working day 4	Remaining £5m is reduced to £2m due to further sales. = £2m	50%	£1m
End of working day 5	Remaining £2m is reduced to £1m due to further sales. = £1m	25%	£0.75 m
Start of working day 6	£1m remaining = £1m	0%	£1m

**Note:** <sup>1</sup> Banks are reminded that in the case of an *equity*, the reduced net *underwriting* position should be treated under the simplified equity method (see 27G of chapter TE)

## Large exposure risk from underwriting securities

### CALCULATING THE NET UNDERWRITING EXPOSURE

- 29 G The net *underwriting exposure* should be included as an *exposure* to the issuer for the purposes of determining the bank's total *exposure* to that issuer when applying chapters LE and TL.
- 30 G A bank should include counterparty exposures to any sub-underwriters for the purposes of determining the bank's total *exposure* to that counterparty when applying chapter LE.
- 31 G A bank, before entering into a new *underwriting* commitment should be able to recalculate its large *exposure* to the level of detail necessary for it to follow the guidance in chapters LE and TL.

- 32 G A bank should calculate the net *underwriting exposure* by applying the relevant reduction factors in table 33G to its net *underwriting* position calculated under 18G.
- 33 G Table: Calculation of net *underwriting exposure* (see 29G)

Time	Reduction factor to be applied to net underwriting position
Initial commitment to <i>working day 0</i>	100%
<i>Working day 0</i>	100%
Working day 1	90%
Working day 2	75%
Working day 3	75%
Working day 4	50%
Working day 5	25%
Working day 6 onwards	0%

- 34 G There is no large exposure limit (chapter LE) or incremental capital (chapter TL) for net *underwriting exposures* between initial commitment and *working day 0*, except where specified by a requirement on a bank's *Part IV permission*.

#### MONITORING AND REPORTING LARGE EXPOSURES

- 35 G For the purposes of large exposures monitoring only, a bank should report its net *underwriting exposure* from the date of initial commitment rather than *working day 0*.

#### RISK MANAGEMENT

- 36 G A bank should take reasonable steps to establish and maintain such systems and controls to monitor and manage its *underwriting* and sub-*underwriting* business as are appropriate to the nature, scale and complexity of its *underwriting* and sub-*underwriting* business.
- 37 G The general requirements for systems and controls are set out in SYSC. 36G is specific to a bank's *underwriting* and sub-*underwriting* business.
- 38 G A bank should take reasonable steps to:

- (1) allocate responsibility for the management of its *underwriting* and sub-*underwriting* business;
- (2) allocate adequate resources to monitor and control its *underwriting* and sub-*underwriting* business;
- (3) satisfy itself that its systems to monitor *exposure* to counterparties will calculate, revise and update its *exposure* to each counterparty arising from its *underwriting* or sub-*underwriting* business;
- (4) satisfy itself of the suitability of each person who performs functions for it in connection with the bank's *underwriting* business having regard for the person's skill and experience; and
- (5) satisfy itself that its procedures and controls to monitor and manage its *underwriting* business address, on an on-going basis, the capacity of sub-*underwriters* to meet sub-*underwriting* commitments.

Definitions used in chapter TU

39 G This chapter uses the following definitions:

Defined term	Definition
<i>Base currency</i>	The currency in which the bank's accounts are prepared.
<i>Business day</i>	Any day except Saturday, Sunday, bank holidays and public holidays (not being bank holidays).
<i>Designated investment exchange</i>	See Handbook Glossary.
<i>Equity</i>	See <i>share</i> .
<i>Foreign currency</i>	A currency other than the bank's <i>base currency</i> .
<i>Option</i>	A contract which confers the right to buy a <i>security</i> , contractually based investment or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>PRR</i>	Position risk requirement.
<i>Regulated investment exchange</i>	See Handbook Glossary.
<i>Regulated market</i>	See Handbook Glossary.
<i>Security</i>	See 10G.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.
<i>Underwriting</i>	The arrangement under which a party agrees to buy, before issue, a specified quantity of securities in an issue of securities on a given date



	and at a given price, if no other has purchased or acquired them.
<i>Warrant</i>	The investment specified in article 79 of the Regulated Activities Order (instruments giving entitlement to investments).
<i>Working day 0</i>	As defined in 23G.

## Annex F

### Chapter TO (Options position risk requirement)

In this Annex, text is being inserted that is not underlined.

Insert the following text between Chapters TU and TS in volume 1 as a new Chapter TO:

TO

Option PRR

General

- 1 G A UK bank to which CAD applies should apply this chapter and calculate its *option PRR* by:
  - (1) identifying which *option* positions must be included within the scope of the *option PRR* calculation under 3G to 5G;
  - (2) calculating the derived position in each *option* in accordance with 9G to 15G;
  - (3) calculating the *PRR* for each derived position in accordance with 16G to 32G;
  - (4) summing all of the *PRRs* calculated in accordance with (3).
- 2 G Banks are reminded that table 4G of chapter TI and table 3G of chapter TE also state that an interest rate *PRR* should be calculated for *options* on *equities*, baskets of *equities* or *equity* indices. The interaction between this chapter and others is illustrated in 33G.

Scope of the option PRR calculation

- 3 G Except as permitted under 5G, a bank's *option PRR* calculation must include:
  - (1) each *trading book* position in an *option* on an *equity*, interest rate or debt;
  - (2) each *trading book* position in a *warrant* on an *equity* or debt security; and
  - (3) each *trading book* and *non-trading book* position in an *option* on a *commodity*, currency or gold.
- 4 G 3G(2) includes net *underwriting* positions or reduced net *underwriting* positions in *warrants*.
- 5 G Table: Appropriate *PRR* calculation for *options* and *warrants* (see 3G)

<i>Option type (see 18G) or Warrant</i>	<i>PRR calculation</i>
American <i>option</i> , European <i>option</i> , Bermudan <i>option</i> , Asian <i>option</i> or <i>warrant</i> for which the <i>in the money</i> percentage (see 6G) is equal to or greater than the appropriate <i>PRA</i> (see 7G and 8G)	Calculate either an <i>option PRR</i> , or the most appropriate to the underlying position of: (a) an <i>equity PRR</i> (b) an interest rate <i>PRR</i> (c) a <i>commodity PRR</i> (d) a foreign exchange <i>PRR</i>
American <i>option</i> , European <i>option</i> , Bermudan <i>option</i> , Asian <i>option</i> or <i>warrant</i> : (a) for which the <i>in the money</i> percentage (see 6G) is less than the appropriate <i>PRA</i> (see 7G and 8G); or (b) that is <i>at the money</i> ; or (c) that is <i>out of the money</i> .	Calculate an <i>option PRR</i>
All other types of <i>option</i> included in 18G (regardless of whether <i>in the money</i> , <i>at the money</i> or <i>out of the money</i> )	

#### THE IN THE MONEY PERCENTAGE

- 6 G The *in the money* percentage is calculated as follows:

For a call *option*:

$$\frac{\text{Current market price of the underlying} - \text{Strike price of the option}}{\text{Strike price of the option}} * 100$$

For a put *option*:

$$\frac{\text{Strike price of the option} - \text{Current market price of the underlying}}{\text{Strike price of the option}} * 100$$

#### THE APPROPRIATE PRA

- 7 G The appropriate *PRA* for a position is that listed in table 8G against the relevant underlying position.
- 8 G Table: Appropriate *PRA* (see 7G)

<b>Underlying</b>	<b>Appropriate PRA</b>
<i>Equity</i>	The <i>PRA</i> applicable to the underlying <i>equity</i> or <i>equity</i> index in table 30G of chapter TE (simplified equity method)
Interest rate	The sum of the specific risk <i>PRA</i> (table 44G of chapter TI) and the general market risk <i>PRA</i> (table 53G of chapter TI) applicable to the underlying position
Debt <i>securities</i>	The sum of the specific risk <i>PRA</i> (table 44G of chapter TI) and the general market risk <i>PRA</i> (table 53G of chapter TI) applicable to the underlying position
<i>Commodity</i>	15%
Gold	8%
Currency	8%

#### Calculating derived positions

- 9 G A bank must calculate the derived position specified in the table in 13G for each position included in its *option PRR* calculation.

#### NETTING POSITIONS

- 10 G A bank may calculate a derived position for its net position in an *option* or a *warrant*, if the relevant *options* or *warrants* are identical or may be treated as identical under 11G or 12G.
- 11 G A bank may treat *options* or *warrants* as identical if they have the same strike price, maturity (except for an interest rate cap or floor – see 12G) and underlying.
- 12 G A firm may treat as identical a purchased interest rate cap (or floor) and a written interest rate cap (or floor) only if they mature within 30 days of each other and all other terms are identical (a cap may not be netted against a floor).

#### Derived positions

- 13 G Table: Derived positions (see 9G)

	<b><i>Option (or warrant)</i></b>	<b><i>Underlying position</i></b>
<i>Equity</i>	<i>Option (warrant)</i> on a single <i>equity</i> or <i>option</i> on a <i>future/forward</i> on a single <i>equity</i>	A notional position in the actual <i>equity</i> underlying the contract valued at the current market price of the <i>equity</i> .
	<i>Option (warrant)</i> on a basket of <i>equities</i> or <i>option</i> on a <i>future/forward</i> on a basket of <i>equities</i>	A notional position in the actual <i>equities</i> underlying the contract valued at the current market price of the <i>equities</i> .

	<i>Option (warrant) on an equity index or option on a future/forward on an equity index</i>	A notional position in the index underlying the contract valued at the current market price of the index.
Interest rate	<i>Option on an interest rate or an interest rate future/FRA</i>	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the sum of the time to expiry of the contract and the length of the period on which the settlement amount of the contract is calculated valued at the notional amount of the contract.
	<i>Option on an interest rate swap</i>	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the length of the <i>swap</i> valued at the notional principal amount.
	Interest rate <i>cap</i> or <i>floor</i>	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the remaining period of the <i>cap</i> or <i>floor</i> valued at the notional amount of the contract.
Debt securities	<i>Option (warrant) on a debt security or option on a future/forward on a debt security</i>	The underlying debt <i>security</i> with a maturity equal to the time to expiry of the <i>option</i> valued as the nominal amount underlying the contract at the current market price of the debt <i>security</i> .
Commodity	<i>Option on a commodity or option on a future/forward on a commodity</i>	An amount equal to the tonnage, barrels or kilos underlying the <i>option</i> with a maturity equal to the expiry date of the spot, <i>forward</i> or <i>futures</i> contract underlying the <i>option</i> .
Gold	<i>Option on gold or option on a future/forward on gold</i>	An amount equal to the troy ounces underlying the <i>option</i> with a maturity equal to the expiry date of the contract underlying the <i>option</i> .
Currency	Currency <i>option</i>	The amount of the underlying currency that the bank will receive if the <i>option</i> is exercised converted at the spot rate into the currency that the bank will sell if the <i>option</i> is exercised.

Combinations of options which can be treated as one option

- 14 G A bank may treat (for the purpose of calculating option *PRR* under this chapter) an *option* strategy in table 15G as a single position in a notional *option* specified against that strategy in table 15G, if:
- (1) each element of the strategy is transacted with the same counterparty;
  - (2) the strategy is documented as a single structure;
  - (3) each *option* in the structure has the same maturity and underlying; and
  - (4) the constituent parts of the structure form an indivisible single contract, so that neither counterparty can unwind or default on one part of the structure without doing so for the contract as a whole.

- 15 G Table: *Option* strategies (see 14G)

<b><i>Option strategy</i></b> (and an example)	<b><i>Notional option position</i></b> (and how it should be treated)
<b>Bull Spread</b> (e.g. buy 100 call and sell 101 call)	<b>One purchased <i>option</i></b> (treat under 20G)
<b>Bear Spread</b> (e.g. sell 100 put and buy 101 put)	<b>One written <i>option</i></b> (treat under 21G)
<b>Synthetic Long Call</b> (e.g. long underlying and buy 100 put)	<b>One purchased <i>option</i></b> (treat under 20G or 24G)
<b>Synthetic Short Call</b> (e.g. short underlying and sell 100 put)	<b>One written <i>option</i></b> (treat under 21G or 24G)
<b>Synthetic Long Put</b> (e.g. short underlying and buy 100 call)	<b>One purchased <i>option</i></b> (treat under 20G or 24G)
<b>Synthetic Short Put</b> (e.g. buy underlying and sell 100 call)	<b>One written <i>option</i></b> (treat under 21G or 24G)
<b>Long Straddle</b> (e.g. buy 100 call and buy 100 put)	<b>One purchased <i>option</i></b> (treat under 20G)
<b>Short Straddle</b> (e.g. sell 100 call and sell 100 put)	<b>One written <i>option</i></b> (treat under 21G but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )
<b>Long Strangle</b> (e.g. buy 101 call and buy 99 put)	<b>One purchased <i>option</i></b> (treat under 20G)

<b>Short Strangle</b> (e.g. sell 99 call and sell 101 put)	<b>One written <i>option</i></b> (treat under 21G but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )
<b>Long Butterfly</b> (e.g. buy one 100 call, sell two 101 calls, and buy one 102 call)	<b>One purchased <i>option</i></b> (treat under 20G)
<b>Short Butterfly</b> (e.g. sell one 100 put, buy two 101 puts, and sell one 102 put)	<b>One written <i>option</i></b> (treat under 21G but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )

The option PRR for an individual position

- 16 G A bank must calculate the *PRR* for each individual derived *option* position using the method specified in table 18G, or, if more than one method is permitted, using one of those methods.
- 17 G The resulting *PRRs* must be converted to the bank's *base currency* using spot foreign exchange rates.
- 18 G Table: *Option PRR* methods applied to different types of *option* (see 16G)

<b>Option</b>	<b>Description</b>	<b>Method</b>
<i>American option</i>	An <i>option</i> that may be exercised at any time over an extended period up to its expiry date.	Standard method or hedging method if appropriate
<i>European option</i>	An <i>option</i> that can only be exercised at expiry.	
<i>Bermudan option</i>	A cross between an <i>American option</i> and <i>European option</i> . The <i>Bermudan option</i> can only be exercised at specific dates during its life.	
<i>Asian option</i>	The buyer has the right to exercise at the average rate or price of the underlying over the period (or part of the period) of the <i>option</i> . One variant is where the payout is based on the average of the underlying against a fixed strike price; another variant is where the payout gives at expiry the price of the underlying against the average price over the <i>option</i> period.	

Barrier <i>option</i>	An <i>option</i> which is either cancelled or activated if the price of the underlying reaches a pre-set level regardless of the price at which the underlying may be trading at the expiry of the <i>option</i> . The knock-out type is cancelled if the underlying price or rate trades through the trigger; while the knock-in becomes activated if the price moves through the trigger.	
Corridor <i>option</i>	Provides the holder with a pay-out for each day that the underlying stays within a defined range chosen by the investor.	
Ladder <i>option</i>	Provides the holder with guaranteed pay-outs if the underlying trades through a pre-agreed price(s) or rate(s) at a certain point(s) in time, regardless of future performance.	
Lock-in <i>option</i>	An <i>option</i> where the pay-out to the holder is locked in at the maximum (or minimum) value of the underlying that occurred during the life of the <i>option</i> .	
Look-back <i>option</i>	An European style <i>option</i> where the strike price is fixed in retrospect, that is at the most favourable price (i.e. the lowest (highest) price of the underlying in the case of a call (put)) during the life of the <i>option</i> .	
Forward starting <i>option</i>	An <i>option</i> that starts at a future date.	
Compound <i>option</i>	An <i>option</i> where the underlying is itself an <i>option</i> (i.e. an <i>option</i> on an <i>option</i> ).	
Interest rate cap	An interest rate option or series of options under which a counterparty contracts to pay any interest costs arising as a result of an increase in rates above an agreed rate: the effect being to provide protection to the holder against a rise above that agreed interest rate.	Standard but with no reduction for the amount the <i>option</i> is out of the money
Interest rate floor	An interest rate option or series of options under which a counterparty contracts to pay any lost income arising as a result of a fall in rates below an agreed rate: the effect being to provide protection to the holder against a fall below that agreed interest rate.	



Performance <i>option</i>	An <i>option</i> based on a reference basket comprised of any number of assets, where the pay-out to the holder could be one of the following: the maximum of the worst performing asset, or 0; the maximum of the best performing asset, or 0; the maximum of the spreads between several pairs of the assets, or 0.	Standard or hedging, but use the highest <i>PRA</i> of the individual assets in the basket.
Quanto	Quanto stands for “Quantity Adjusted <i>Option</i> ”. A quanto is an instrument where two currencies are involved. The payoff is defined in terms of a variable that is measured in one of the currencies and the payoff is made the other currency.	Subject to 31G, the standard method
Cliquet <i>option</i>	A cliquet <i>option</i> consists of a series of forward starting <i>options</i> where the strike price for the next exercise date is set equal to a positive constant times the underlying price as of the previous exercise date. They initially act like a vanilla <i>option</i> with a fixed price but as time moves on, the strike is reset and the intrinsic value automatically locked in at pre-set dates. If the underlying price is below the previous level at the reset date no intrinsic value is locked in but the strike price will be reset to the current price attained by the underlying. If the underlying price exceeds the current level at the next reset the intrinsic value will again be locked in.	Standard method for a purchased cliquet or the method specified in 30G for a written cliquet
Digital <i>option</i>	A type of <i>option</i> where the pay-out to the holder is fixed. The most common types: all-or-nothing and one-touch <i>options</i> . All-or-nothing will pay out the fixed amount if the underlying is above (call) or below (put) a set value at expiry. The one-touch will pay the fixed amount if the underlying reaches a fixed point any time before expiry.	The method specified in 29G
Any other <i>option</i> or <i>warrant</i>		The method specified for the type of instrument whose description it most closely resembles.

## Calculating option PRR

19 G In the table 18G:

- (1) "standard method" refers to the method specified in 20G to 22G; and
- (2) "hedging method" refers to the method specified in 23G to 28G.

## The standard method

### PURCHASED OPTIONS AND WARRANTS

- 20 G Under the standard method, the *PRR* for a purchased *option* or *warrant* is the lesser of:
- (1) the market value of the derived position (see 9G) multiplied by the appropriate *PRA* (see 8G); and
  - (2) the market value of the *option* or *warrant*.

### WRITTEN OPTIONS AND WARRANTS

- 21 G Under the standard method, the *PRR* for a written *option* or *warrant* is the market value of the underlying position (see 9G) multiplied by the appropriate *PRA* (see 8G). This result may be reduced by the amount the *option* or *warrant* is *out of the money* (subject to a maximum reduction to zero).

### UNDERWRITING OR SUB-UNDERWRITING AN ISSUE OF WARRANTS

- 22 G Under the standard method, the *PRR* for *underwriting* or *sub-underwriting* an issue of *warrants* is the net *underwriting* position (or reduced net *underwriting* position) multiplied by the current market price of the underlying *securities* multiplied by the appropriate *PRA*, but the result can be limited to the value of the net *underwriting* position (or reduced net *underwriting* position) calculated using the issue price of the *warrant*.

## The hedging method

- 23 G The hedging method involves *option PRR* being calculated on a combination of the *option* and its hedge.
- 24 G Under the hedging method a bank must calculate *PRR* individual positions as follows:
- (1) for an *option* or *warrant* on an *equity*, basket of *equities* or *equity* index and its *equity* hedge(s), to the extent specified or permitted in table 26G, using the calculation in table 27G;

- (2) for an *option* or *warrant* on a *debt security*, basket of *debt securities* or *debt security* index and its *debt security* hedge(s), to the extent specified or permitted in table 26G, using the calculation in table 27G;
- for an *option* on gold and its gold hedge, to the extent specified or permitted in table
- (3) 26G, using the calculation in table 27G; and
- (4) for an *option* on a currency and its currency hedge, to the extent specified or permitted in table 26G, using the calculation in table 28G.

25 G A firm may not use the hedging method for:

- (1) an interest rate *option* and its hedge; or
- (2) a *commodity option* and its hedge.

26 G Table: Appropriate treatment for *equities*, *debt securities* or currencies hedging *options* (see 24G)

Hedge	PRR calculation for the hedge	Limits (if the hedging method is used)	Naked positions
An <i>equity</i> (hedging an <i>option</i> or <i>warrant</i> )	The <i>equity</i> should be treated in either chapter TE ( <i>equity PRR</i> ) or the hedging method (table 27G)	The hedging method should only be used up to the amount of the hedge that matches the notional amount underlying the <i>option</i> or <i>warrant</i>	To the extent that the amount of the hedge (or <i>option</i> ) exceeds the notional amount underlying the <i>option</i> or <i>warrant</i> (or hedge), a bank should apply an <i>equity PRR</i> , interest rate <i>PRR</i> or foreign exchange <i>PRR</i> (or <i>option PRR</i> )
A <i>debt security</i> (hedging an <i>option</i> or <i>warrant</i> )	The <i>debt security</i> should be treated in chapter TI (interest rate <i>PRR</i> ) or the hedging method (table 27G)		
Gold (hedging a gold <i>option</i> )	The gold should be treated in either chapter FX (foreign exchange <i>PRR</i> ) or the hedging method (table 27G)		
A currency or currencies (hedging a currency <i>option</i> )	The currency should be treated in either chapter FX (foreign exchange <i>PRR</i> ) or the hedging method (table 28G)		

- 27 G Table: The hedging method of calculating the *PRR* (*equities, debt securities and gold*) (see 24G(1) to (3))

	<i>Option or warrant position</i>	<i>PRR</i>		
		<i>In the money by more than the PRA</i>	<i>In the money by less than the PRA</i>	<i>Out of the money</i>
Long in <i>security</i>	Long put	Zero	Wp	X
	Short call	Y	Y	Z
Short in <i>security</i>	Long call	Zero	Wc	X
	Short put	Y	Y	Z
Where:				
Wp	[ $(PRA - 100\%) \times$ The underlying position valued at strike price ] + The market value of the underlying position			
Wc	[ $(100\% + PRA) \times$ The underlying position valued at strike price ] - The market value of the underlying position			
X	The market value of the underlying position multiplied by the appropriate <i>PRA</i>			
Y	The market value of the underlying position multiplied by the appropriate <i>PRA</i> . This result may be reduced by the market value of the <i>option</i> or <i>warrant</i> , subject to a maximum reduction to zero.			
Z	The standard method should be used.			

- 28 G Table: The hedging method of calculating the *PRR* (*currencies*) (see 24G(4))

<i>Option position</i>	<i>PRR</i>		
	<i>In the money by more than 8%</i>	<i>In the money by less than 8%</i>	<i>Out of the money</i>
Long calls & long puts	Zero	W <sub>L</sub>	X
Short calls & short puts	Zero	Y	X
Where:			
W <sub>L</sub>	[ $1.08 \times$ The amount of the underlying currency that the bank will receive if the <i>option</i> is exercised, converted at the strike price into the currency that the bank will sell if the <i>option</i> is exercised ] - The market value of the underlying position		
X	The market value of the underlying position multiplied by 8%.		
Y	The market value of the underlying position multiplied by 8%. This result may be reduced by the market value of the <i>option</i> , subject to a maximum reduction to zero.		

## Specific methods and treatments

### DIGITAL OPTIONS

- 29 G The *PRR* for a digital *option* is the maximum loss of the *option*.

### WRITTEN CLIQUET OPTIONS

- 30 G The *PRR* for a written cliquet *option* is the market value of the derived position (see 8G) multiplied by the appropriate *PRA* (see 8G) multiplied by F+1 (see below). This result may be reduced by the amount the *option* is *out of the money* (subject to a maximum reduction to zero).

$$\text{i.e. } [PRA * \text{underlying} * (F + 1)] - OTM$$

$$\text{where } F = \min \left[ FR, \max \left( \frac{FR}{2}, Y \right) \right]$$

FR: Number of forward re-sets

Y: Years to maturity

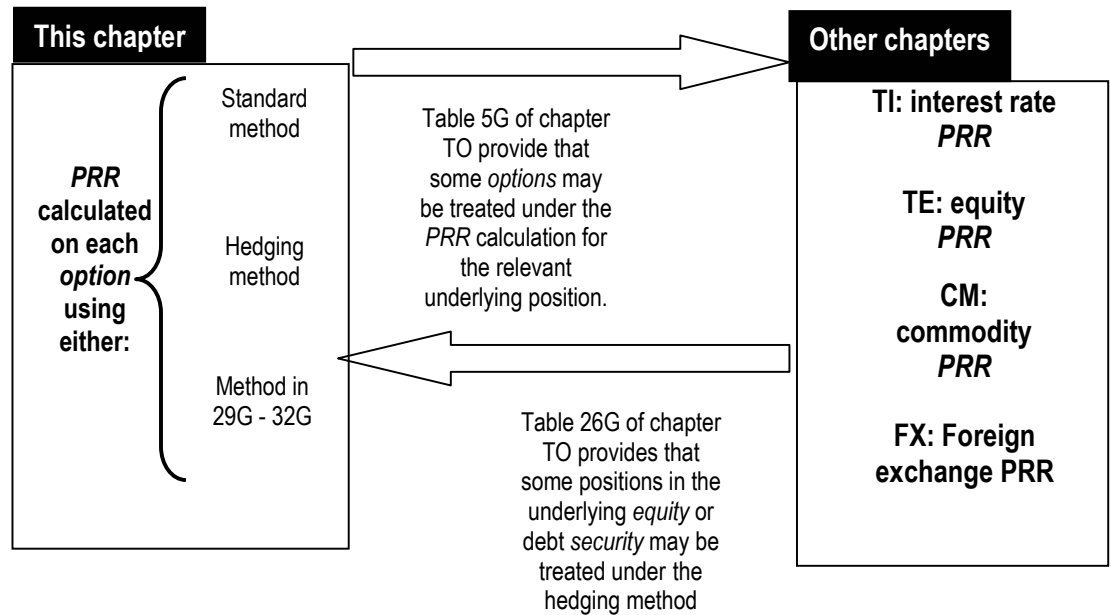
OTM: *out of the money* amount

### QUANTOS

- 31 G If the pay-out to the holder of a quanto *option* is fixed at the inception of the transaction a bank must add 8% to the *PRA* when applying the standard method.
- 32 G The additional *PRA* is to account for the forward foreign currency exchange risk.

Interaction with other chapters

33 G Figure: Diagram illustrating the relationship between this chapter and other chapters.



Definitions used in chapter TO

34 G This chapter uses the following definitions:

<i>At the money</i>	Where the strike price of the <i>option</i> or <i>warrant</i> is the same as the current market value of the underlying instrument.
<i>Base currency</i>	The currency in which the bank's accounts are prepared.
<i>Cap</i>	Means an agreement in respect of a borrowing under which a counterparty contracts to pay any interest costs arising as a result of an increase in rates above an agreed rate: the effect being to provide protection to the holder against a rise above that agreed rate.
<i>Commodity</i>	Any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB the definition of commodity used in chapter TO deliberately differs from that in the main Handbook Glossary).
<i>Equity</i>	See <i>share</i> .
<i>Floor</i>	Means an agreement in respect to a deposit under which a counterparty contracts to pay any lost income arising as a result of a fall in rates below an agreed rate: the effect being to provide protection to the holder against a fall below that agreed interest rate.
<i>Foreign currency</i>	A currency other than the bank's <i>base currency</i> .
<i>Forward</i>	A contract to buy or sell where the date of settlement has been

	agreed as a particular date in the future.
<i>Forward rate agreement</i>	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.
<i>FRA</i>	<i>Forward rate agreement.</i>
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>In the money</i>	Where the strike of a call <i>option</i> or <i>warrant</i> is less than the current market value of the underlying instrument, or vice versa for put <i>options</i> .
<i>Option</i>	A contract which confers the right to buy or sell a <i>security</i> , contractually based investment, currency, gold or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>Out of the money</i>	Where the strike price a call <i>option</i> or <i>warrant</i> is more than the current market value of the underlying instrument, or vice versa for a put <i>option</i> .
<i>PRA</i>	Percentage risk addition.
<i>PRR</i>	Position risk requirement.
<i>Security</i>	As defined in article 3(1) of the Regulated Activities Order.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.
<i>Trading book</i>	As defined in section 3.2.1 of chapter CB.
<i>Underwriting</i>	The arrangement under which a party agrees to buy, before issue, a specified quantity of securities in an issue of securities on a given date and at a given price, if no other has purchased or acquired them.
<i>Warrant</i>	The investment specified in article 79 of the Regulated Activities Order (instruments giving entitlement to investments).
<i>Zero-specific-risk security</i>	A hypothetical debt <i>security</i> used to represent the general interest rate risk arising from certain <i>derivative</i> and <i>forward</i> transactions.

## Annex G

### Chapter TS (CAD1 models)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter TS in its entirety and replace with the following text:

TS

Use of a CAD1 Model

Introduction

- 1 G A bank should, under Section 3.4 of chapter TO, calculate *PRR* using the guidance in chapters TI, TE, CM, FX and TO. However, at the bank's request, the FSA may give individual *guidance*, and thereby allow the bank to calculate all or part of its *PRR* using a Capital Adequacy Directive "CAD1" (for options risk aggregation and/or interest rate pre-processing) or "VaR" (value at risk) model instead. Chapter TV deals with the VaR model recognition process.
- 2 G The purpose of this chapter is to provide guidance on the FSA's policy for giving individual *guidance* on the use of CAD1 models. The policy recognises that CAD1 models may vary across banks but, as a minimum, the FSA will need to be satisfied about:
  - (1) the quality of the internal controls and risk management surrounding the model model (see 17G to 21G for further details); and
  - (2) the quality of the model standards and that the CAD1 model captures and produces an accurate measure of the risks inherent in the portfolio covered by the CAD1 model (see 22G to 51G for further details).
- 3 G It also explains how the output from the model is fed into the CO: Section 5 *PRR* calculation.
- 4 G If individual *guidance* to use a CAD1 model is given by the FSA, the individual *guidance* will contain certain conditions. In order to adequately address individual circumstances, these conditions may differ from the requirements set out in this chapter. The individual *guidance* will also confirm the scope of the CAD1 model recognition given to a bank.



- 5 G Individual *guidance* permitting the use of models in the calculation of *PRR* will not be given if that would be contrary to the CAD or Basel Accord, and any individual *guidance* which is given will only be given on terms that are compatible with the CAD and Basel Accord. The FSA considers it unlikely that it will deviate from this approach. Accordingly, the only individual *guidance* permitting the use of models that the FSA is likely to give are CAD1 and VaR models.
- 6 G If a bank ceases to meet any of these standards, the FSA’s policy is that the individual *guidance* should cease to have effect.

Scope of CAD1 models

- 7 G The FSA recognises two types of CAD1 model. The table below sets out :

Options risk aggregation models		Interest rate pre-processing models
Brief description and eligible instruments	Analyse and aggregate <i>options</i> risks for <ul style="list-style-type: none"> <li>• interest rate <i>options</i>;</li> <li>• equity <i>options</i>;</li> <li>• foreign exchange <i>options</i>; and</li> <li>• commodity <i>options</i>.</li> </ul>	May be used to calculate duration weighted positions for: <ul style="list-style-type: none"> <li>• <i>swaps</i> (<i>swaps</i> include <i>swaps</i> and their economic equivalent).</li> </ul>
The output and how it is used in the <i>PRR</i> calculation	Depending on the type of model and the conditions contained in any CAD1 model individual <i>guidance</i> given, the outputs from an <i>options</i> risk aggregation model may be used as an input to the <i>PRR</i> calculation set out in IPRU(Bank) chapters CO, TI, TE, CM, FX and TO).	Depending on the type of model and the conditions contained in any CAD1 model individual <i>guidance</i> given, the individual sensitivity figures produced by this type of CAD1 model may be either input into a bank's standard duration method <i>PRR</i> calculation (see 60G of Chapter TI) or be converted into notional positions and input into a bank's maturity method <i>PRR</i> (see 55G of Chapter TI).

The CAD1 model application and review process

- 8 G In order to consider a CAD1 model recognition individual *guidance* request, the FSA may undertake a review to ensure that it is adequate and appropriate for the *PRR* calculation.

- 9 G The model review process may be conducted through a series of visits covering various aspects of the bank's control and IT environment. Before these visits the FSA may ask the bank to provide some information relating to its individual *guidance* request accompanied by some specified background material. The model review visits are organised on a timetable that allows a bank being visited sufficient time to arrange the visit and provide the appropriate pre-visit information.
- 10 G As part of the model review process, the following may be reviewed: organisational structure and personnel; details of the bank's market position in the relevant products; profit and risk information; valuation and reserving policies; operational controls; IT systems; model release and control procedures; risk management and control framework; risk appetite and limit structure and future developments relevant to model recognition.
- 11 G The FSA will normally require meetings with senior management and staff from the front office, financial control, risk management, operations, systems development, information technology and audit areas.
- 12 G A review by a *skilled person* may be used before CAD1 model individual *guidance* is given to supplement the model review process, or after the individual *guidance* has been given to review the CAD1 model.
- 13 G If the FSA gives individual *guidance* to allow the use of a CAD 1 model, the individual *guidance* will set out the conditions on which the individual *guidance* has been given. Conditions may include:
- (1) the details of the calculation of *PRR*;
  - (2) the CAD1 model methodology to be employed;
  - (3) the products covered by the model (e.g. *option* type, maturity, currency);
  - (4) any notification requirements relating to the CAD1 model individual *guidance*; and
  - (5) any other conditions attached to the CAD1 model individual *guidance*.
- 14 G Where a bank operates any part of its CAD1 model outside the United Kingdom, the FSA may take into account the results of any home state supervisor's model review. The FSA may wish to receive information directly from the home state supervisor.

#### Maintenance of model recognition

- 15 G No changes should be made to a CAD1 model unless the change is not material. Material changes to a CAD1 model will require further individual *guidance* to be issued. Materiality is measured from the time that the individual *guidance* or further individual *guidance* has been given. If a bank is considering making material changes to its CAD1 model, then it should notify the FSA at once. A bank must request further individual *guidance* if the products covered by the model change.

- 16 G If the CAD1 model ceases to meet the conditions of the individual *guidance*, the bank should notify the FSA at once. The FSA may then withdraw the individual *guidance*, unless further individual *guidance* is given.

#### Risk management standards

- 17 G A bank with a complex portfolio is expected to demonstrate more sophistication in its modelling and risk management than a bank with a simple portfolio.
- 18 G A bank should be able to demonstrate that it meets the risk management standards set out in this appendix for each legal entity that will have the benefit of the CAD1 model individual *guidance*. This is particularly important for subsidiaries in groups subject to matrix management where the business lines cut across legal entity boundaries.
- 19 G A bank should have a conceptually sound risk management system which is implemented with integrity and should meet the following minimum standards:
- (1) A bank should have a risk control unit that is independent of business trading units and reports directly to senior management. The unit should be responsible for designing and implementing the bank's risk management system. It should produce and analyse daily reports on the risks run by the business and on the appropriate measures to be taken in terms of the trading limits.
  - (2) A bank's senior management should be actively involved in the risk control process, and the daily reports produced by the risk control unit should be reviewed by a level of management with sufficient authority to enforce reductions of positions taken by individual traders as well as in the bank's overall risk exposure.
  - (3) The risk control group should have a sufficient number of staff with appropriate skills in the use of models.
  - (4) A bank should have established procedures for monitoring and ensuring compliance with a documented set of appropriate internal policies and controls concerning the overall operation of the risk measurement and control framework. This should take into account the front, middle and back office functions.
  - (5) A bank should conduct, as part of its internal audit process, a review of the systems and controls surrounding its CAD1 model. This review should include the valuation process, compliance with the CAD1 model scope and the activities of the business trading units and the risk control units. This review should be undertaken by staff independent of the areas being reviewed.
- 20 G In assessing whether the risk management and control framework is implemented with integrity, the FSA will consider the IT systems used to run the CAD1 model and associated calculations. The assessment will include, where appropriate:

- (1) feeder systems; risk aggregation systems; the integrity of the data (i.e. it is complete, coherent and correct); reconciliations and checks on completeness of capture; and
  - (2) system development, change control and documentation; security and audit trails; system availability and contingency procedures; network adequacy.
- 21 G A bank should take appropriate steps to ensure that it has adequate controls surrounding:
- (1) the derivation of the *PRR* from the CAD1 model output;
  - (2) CAD1 model development, including independent validation;
  - (3) reserving;
  - (4) valuation (see IPRU(Bank), chapter VA) including independent validation; and
  - (5) the adequacy of the IT infrastructure.

#### Model standards

- 22 G A bank should take appropriate steps to ensure that its CAD1 model captures and produces an accurate measure of the risks inherent in the portfolio covered by the CAD1 model. These risks may include, but are not limited to, gamma, vega and rho.

#### OPTIONS RISK AGGREGATION MODELS

- 23 G For a bank to obtain CAD1 model individual *guidance* for its *options* risk aggregation model, it should have in place an appropriate *options* valuation model.
- 24 G The FSA does not specify the methodology that a bank should employ in order to produce the appropriate outputs from its CAD1 model. However, 25G to 41G provide conditions of how a bank could meet the requirements to capture gamma, vega and rho risks using a scenario matrix approach. Where a bank adopts the scenario matrix approach then the standards set out in 25G to 41G should be followed. The bank should also take into account other risks not captured by the scenario matrix approach. Otherwise, a bank may use an equivalent methodology. If a bank uses an equivalent methodology, then it will need to demonstrate that the approach used meets the requirements of this chapter.
- 25 G A scenario matrix is an approach by which an *options* portfolio is revalued given a number of simultaneous shifts in both the spot level of the underlying and the implied volatility.
- 26 G The scenario matrix approach may be employed for all types of *options* on all types of underlying asset.
- 27 G The following provides an outline of the initial steps to be taken when using the scenario matrix approach:

- (1) A value for an *option* should be obtained using the bank's *options* valuation model.
  - (2) The inputs into the *options* valuation model for implied volatility of the underlying asset and the price of the underlying asset should then be altered so that a new value for the *option* is obtained (details of the amount by which the implied volatility and the price of the underlying should be amended are set out in 28G-34G).
  - (3) The difference between the original value of the *option* and the new value obtained following the alterations should be input into the appropriate cell in the matrix, the value in the central cell where there is no change in implied volatility or price of the underlying should therefore be zero.
  - (4) The process of obtaining a new price for the *option* should be repeated until the matrix is completed.
- 28 G The alteration to the implied volatility (known as the implied volatility shift) referred to in 27(2) G may be a proportional shift, the size of which depends on the remaining life of the *option* and the asset class of the underlying. Table 30G sets out the shifts that should be applied where a proportional shift is used. Alternatively, a bank may use a single shift across all maturities or use an absolute rather than a proportional implied volatility shift. Where a single shift or an absolute shift is used it should be at least as conservative as the proportional shifts. This should be reviewed and, if necessary updated, on a regular basis.
- 29 G A bank may choose to use a less detailed term structure than that in Table 30G, but the shifts used should be no less conservative than those set out. For example, a bank that uses one <3 month band, rather than the two bands (<1 month, and 1-3 months) set out in the table, should use the most conservative shift set out in the table for the bands covered that is, 30% for the <3 month band.
- 30 G TABLE: PROPORTIONAL IMPLIED VOLATILITY SHIFTS (SEE 28G)

REMAINING LIFE OF OPTION	PROPORTIONAL SHIFT	
	EQUITIES & FX & COMMODITIES	INTEREST RATES
≤ 1 month	30%	30%
>1 ≤ 3 months	20%	20%
>3 ≤ 6 months	15%	15%
>6 ≤ 9 months	12%	12%
>9 ≤ 12 months	9%	9%
>1 ≤ 2 years	6%	9%
>2 ≤ 4 years	4.5%	9%
>4 years	3%	9%

31 G The size of the underlying price/rate shift depends on the asset class of the underlying, and is set out in 32G:

32 G TABLE: UNDERLYING PRICE/RATE SHIFTS (SEE 31G)

UNDERLYING ASSET CLASS	SHIFT
Equities	±8%
Foreign Exchange	±8%
Commodities	±15%, (but a bank may use the percentages applicable under the extended maturity ladder approach, where permitted by the requirements of Chapter CM).
Interest Rates	±100bp (but a bank may use the sliding scale of shifts by maturity as outlined in Chapter TI).

- 33 G The shifts outlined above are the maximum shifts required; in addition there will be a number of intermediate shifts as a result of the minimum matrix size criteria set out in 34G.
- 34 G The minimum size of the scenario matrix should be 3x7, that is, three observations for implied volatility (including the actual implied volatility) and seven observations for the price of the underlying (including the actual price of the underlying). A bank should be able to justify its choice of granularity. Greater granularity may be required where the portfolio contains, for example, a large proportion of barrier *options*.
- 35 G A different scenario matrix should be set up for each underlying asset type:
- (1) for *equities* (including single *equities*, baskets and indices) this means a separate matrix for each national market or non-decomposed basket or non-decomposed multi-national index;
  - (2) for foreign-exchange products this means a separate matrix for each currency pair where appropriate;
  - (3) for *commodity* products this means a separate matrix for each underlying as defined in Chapter CM; and
  - (4) for interest rate products this means a separate matrix for each currency; in addition, a bank should not offset the gamma and vega exposures (except in the circumstances set out in 36G) arising from any one of the following types of products with the gamma and vega exposures arising from any of the other products in the list:
    - (a) Swaptions (options on interest rate *swaps*);
    - (b) interest rate *options* (including *options* on exchange-traded *deposit* or bill *futures*);
    - (c) bond *options* (including *options* on exchange-traded bond *futures*);
    - (d) other types of exotic *option* which do not fall easily into one of the other three categories and are required by the FSA to form their own separate underlying asset.
- 36 G A bank may offset gamma and vega exposures arising from the products listed in 35(4) G where it can demonstrate that it trades different types of interest rate-related *options* as a portfolio and takes steps to control the basis risk between different types of implied volatility. If this is the case, then an individual matrix is not required for each of the products listed in 35(4) G and a combined scenario matrix may be used.
- 37 G Where it is imprudent to fully offset long-dated and short-dated vega exposure due to non-parallel shifts in the yield curve, a bank should use an appropriate number of scenario matrices to take account of non-parallel shifts in the yield curve according to the maturity of the *option* or underlying.

- 38 G Following the steps outlined in 27G, a bank then removes the portion of the values in the matrix that can be attributed to the effect that delta has had on the change in the value of the *option* (a process known as delta-stripping).
- 39 G Once the effect of delta has been removed from the matrix, the values left in the matrix relate to gamma and vega risk. A bank's market risk requirement in relation to gamma and vega risk on the individual *option* is the absolute of the most negative cell in the scenario matrix produced. Where all cells are positive the *PRR* is zero. The total *PRR* for the gamma and vega risk on the portfolio of *options* is a simple sum of the individual requirements. This amount should then be fed into a bank's *PRR* calculation.
- 40 G The values that have been obtained for the delta-equivalent positions of instruments included in the scenario matrix should then be treated in the same way as positions in the underlying. Where the delta obtained relates to interest rate position risk, the delta equivalent positions may be fed into a bank's interest rate pre-processing model providing that the positions fall within the scope of the interest rate pre-processing model set out in 7G, and that the bank has the appropriate CAD1 model individual *guidance*. Alternatively, the delta obtained should be fed into the standard *PRR* calculation in Chapter TI, TE, CM or FX as appropriate.
- 41 G In using the scenario matrix approach, none of the steps followed will take specific account of a bank's exposure to rho risk. Where a bank can demonstrate that for interest rate-related *options* the rho sensitivity is effectively included in the delta sensitivities produced, there is no separate capital requirement relating to rho. For all other *options* except commodity *options*, a bank should calculate a rho sensitivity ladder by currency as part of its CAD1 model and feed this either into the maturity or duration method *PRR* calculation set out in Chapter TI or, where a bank has the appropriate individual *guidance*, into an interest rate pre-processing model.

#### INTEREST RATE PRE-PROCESSING MODELS

- 42 G A bank that has been given individual *guidance* to use an interest rate pre-processing model is permitted to use it for the pre-processing of the instruments set out in 7G, from which the residual positions are fed into the maturity or duration method *PRR* calculation as set out in Chapter TI.
- 43 G There are a number of different methods of constructing pre-processing models. All pre-processing models should generate positions that have the same sensitivity to defined interest rate changes as the underlying cash flows.
- 44 G In an interest rate pre-processing model each transaction is converted into its constituent cash flows. The cash flows are discounted using zero coupon rates derived from the bank's own yield curves.
- 45 G The cash flows are then calculated again using the bank's own yield curve shifted by the amount set out in 47G.



46 G The difference between the present values calculated using the bank's own yield curve and those calculated using the bank's curve shifted by the amount specified are known as the sensitivity figures. Alternatively, banks may shift the yield curve by one basis point and multiply the sensitivity figures up by the appropriate amount in order to achieve the shifts set out in 47G. These sensitivity figures are then allocated to each of the 15 maturity bands set out in 47G.

47 G TABLE: YIELD CURVE SHIFTS (SEE 45G)

<b>Zone</b>	<b>Modified Duration</b>	<b>Assumed interest rate change (percentage points)</b>
1	0 ≤ 1 months	1.00
	> 1 ≤ 3 months	1.00
	> 3 ≤ 6 months	1.00
	> 6 ≤ 12 months	1.00
2	> 1.0 ≤ 1.9 years	0.90
	> 1.9 ≤ 2.8 years	0.80
	> 2.8 ≤ 3.6 years	0.75
3	> 3.6 ≤ 4.3 years	0.75
	> 4.3 ≤ 5.7 years	0.70
	> 5.7 ≤ 9.3 years	0.65
	> 7.3 ≤ 9.3 years	0.60
	> 9.3 ≤ 10.6 years	0.60
	> 10.6 ≤ 12 years	0.60
	> 12.0 ≤ 20 years	0.60
	> 20 years	0.60

48 G Sensitivity figures calculated by a bank using an interest rate pre-processing model are usually produced in the format of a net sensitivity by maturity bucket or by discrete gridpoint. These maturity buckets or gridpoints should then be allocated to the 15 bands set out in 47G. The number of maturity buckets or gridpoints used to represent a yield curve can be referred to as granularity. It is not a requirement that each of 15 bands for banks have one or more maturity buckets or gridpoints allocated; however, for all banks the granularity should be adequate to capture the material curve risk in the portfolio. Curve risk can be defined as the risk associated with holding long and short positions at different points along the yield curve.

49 G Positive and negative amounts in each of the different maturity bands of the sensitivity calculation should then be netted off to produce one figure for each of the bands. There is no capital requirement for this netting process.

50 G The individual sensitivity figures produced should then be input into a bank's duration method *PRR* calculation as set out in Chapter TI. The individual sensitivity figures for each band should be included with the other positions in the weighted net positions column used in the duration method.

- 51 G Alternatively, firms may choose to use an approach based on the maturity method set out in Chapter TI, making appropriate adjustments to the sensitivity figures.

Definitions used in Chapter TS

- 52 G This chapter uses the following definitions:

<b>Defined term</b>	<b>Definition</b>
<i>Commodity</i>	Any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB the definition of commodity used in TV deliberately differs from that in the main Handbook Glossary).
<i>Deposit</i>	See definition in the Glossary.
<i>Equity</i>	See <i>share</i> .
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>Guidance</i>	Guidance given by the FSA under the Act.
<i>Option</i>	A contract which confers the right to buy or sell a <i>security</i> , contractually based investment, currency, gold or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>PRR</i>	Position risk requirement.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Skilled person</i>	A person reported to make a report required by section 166 of the Act (Reports by skilled persons) for provision to the FSA and who must be a person: (a) nominated or approved by FSA; and (b) appearing to the FSA to have the skills necessary to make a report on the matter concerned.
<i>Swap</i>	A transaction in which two counterparties agree to exchange streams of payments over time according to a predetermined basis.

## Annex H

### Chapter TV (VaR models)

In this Annex, text is being deleted and replaced with new text that is not underlined.

Delete existing text in Chapter TV in its entirety and replace with the following text:

#### TV

#### Use of a Value at Risk Model

##### Introduction

- 1 G This chapter provides details of when the FSA expects to allow a bank to use its own Value at Risk (VaR) model for the purpose of calculating part or all of its *PRR*, and explains how the model will relate to the standard rules.
- 2 G The models described in this chapter are described as VaR models in order to distinguish them from the kinds of model originally contemplated by the Capital Adequacy Directive (CAD). (These are covered in Chapter TS and referred to as "CAD 1 models".) A VaR model is a risk management model which uses a statistical measure to predict profit and loss movement ranges with a confidence interval. The standards described in this chapter, and which will be applied by the FSA, are based on and implement Annex VIII of the CAD and the Basel Accord.
- 3 G The aim of the VaR model approach is to enable a bank with adequate risk management systems to benefit from more accurate capital requirements than those generated by standard requirements, and to provide a bank with an incentive to measure market risks as accurately and comprehensively as possible. It is crucial that those responsible for managing market risk at a bank should be aware of the assumptions and limitations of the bank's VaR model.
- 4 G A VaR measure provides an estimate of the worst expected loss on a portfolio resulting from market movements over a period of time with a given confidence level. The *PRR* relating to the risks covered by the VaR model is based on the value produced by the VaR model. In undertaking the *PRR* calculation, a bank should apply a multiplication factor to the value produced by the VaR model (details of how the multiplication factor will affect a *PRR* are set out in 75G). The multiplication factor that should be applied is set by the FSA. The multiplication factor may be increased by a plus factor, which relates to the results of a bank's back-testing process (for further details on the plus factor see 63G).

- 5 G There are a number of methodologies for calculating *PRR* using a VaR model. These include variance-covariance, historical simulation, Monte Carlo or a hybrid of these. Although the section on model standards in this appendix sets out some general model standards that should be met, the FSA does not prescribe any one method of computing *PRR* using a VaR model. Moreover, it does not wish to discourage any bank from developing alternative risk measurement techniques. A bank should discuss the use of any alternative techniques used to calculate *PRR* with the FSA.

## Overview

### LINK TO STANDARD PRR RULES

- 6 G Under section 3.4 of chapter CO a bank should use the rules in chapters TI, TE, CM FX and TO to calculate *PRR*. Therefore, a bank needs to apply for individual *guidance* in order to calculate its *PRR* using a VaR model instead of (or in combination with) the standard approaches required under section 3.4 of chapter CO.
- 7 G The VaR Model based *PRR* produced in accordance with this appendix should be included in the bank's *PRR* calculation set out in section 3.4 of chapter CO. The VaR model *PRR* should be used in place of the appropriate *PRR* for the risks covered by the VaR model.

### BASIC REQUIREMENTS / SUMMARY OF CHAPTER

- 8 G The FSA will not normally give individual *guidance* for the use of a VaR model unless it is satisfied about the quality of:
- (1) the internal controls and risk management surrounding the VaR model (see 28G to 35G);
  - (2) the VaR Model Standards (see 36G to 44G);
  - (3) risk management standards including stress testing and backtesting procedures surrounding a VaR model; (see 45G to 73G); and
  - (4) the procedures in place at a bank to calculate its VaR model based *PRR*.
- 9 G The FSA recognises that the nature of VaR models will vary across banks. The scope of and the conditions set out in VaR model individual *guidance* may therefore differ in substance or detail from the matters described in this chapter in order to address individual circumstances adequately. For example, a VaR model individual *guidance* may also include additional conditions to meet the particular circumstances of the bank or the model.

- 10 G If the bank ceases to meet any of these standards, the FSA's policy is that the individual *guidance* should cease to apply. In many cases the ongoing need to meet these standards will be included in the individual *guidance* direction by imposing certain conditions. Even if they are not formally included as conditions, the FSA is likely to consider withdrawing the individual *guidance* if the standards are not met.
- 11 G The VaR Model Waiver Application and Review section of this chapter sets out the FSA's general policy on the VaR model application and review process and the conditions that the FSA may impose relating to alterations of the model.
- 12 G Individual *guidance* permitting the use of models in the calculation of *PRR* will not be given if that would be contrary to the CAD or Basel Accord, and any individual *guidance* which is given will only be given on terms that are compatible with the CAD. The FSA considers it unlikely that it will deviate from this approach even where the bank making the individual *guidance* application is not subject to CAD and Basel Accord. Accordingly, the FSA is likely to give only individual *guidance* permitting the use of models that are of the same nature as CAD1 and VaR models.

#### SCOPE OF VAR MODELS

- 13 G This chapter sets out the FSA's policy on the scope of VaR model individual *guidance* and the manner in which the outputs of the model will be incorporated in the calculation set out in section 5 of chapter CO. Some of the standards described in this chapter may also be reflected in conditions attached to VaR model individual *guidance*.
- 14 G A VaR model will be expected to cover one or more of the following types of risk category:
- (1) interest rate general market risk;
  - (2) interest rate specific risk (in conjunction with interest rate general market risk);
  - (3) *equity* general market risk;
  - (4) *equity* specific risk (in conjunction with equity general market risk);
  - (5) foreign-exchange risk; and
  - (6) *commodity* risk.
- 15 G It is the FSA's view that, where a bank uses a VaR model for one risk category, it is good practice to extend its model over time to calculate all of its *PRR* risk categories.

- 16 G For the purposes of CO: Section 5, where a combination of the standard *PRR* rules, CAD1 model and VaR model approaches is used the *PRR* from each method should be added together. A bank should take appropriate steps to ensure that all of the approaches mentioned are applied in a consistent manner. For example, where the *PRR* for a particular portfolio is normally calculated using a VaR model, it should not switch between the standard market risk rules and a VaR model approach purely to achieve a more attractive *PRR*.
- 17 G A bank will not be required to capture immaterial risk or the market risk inherent in new products in a VaR model. If a bank does not capture immaterial risks or the market risk inherent in a new product in a VaR model, then the appropriate standard *PRR* rules to these risks will apply.

#### The VaR model application and review process

- 18 G In order for VaR model recognition individual *guidance* to be given, the FSA is likely to undertake a review to ensure that it is adequate and appropriate for the *PRR* calculation.
- 19 G The VaR model review process may be conducted through a series of visits covering various aspects of a bank's control and IT environment. Before these visits the FSA may ask that the bank provides some information relating to the bank's individual *guidance* request accompanied by some specified background material. The VaR model review visits are organised on a timetable that allows the bank being visited sufficient time to arrange the visit and provide the appropriate pre-visit information.
- 20 G As part of the of the VaR model review process the following may be reviewed: organisational structure and personnel; details of the bank's market position in the relevant products; profit and risk information; valuation and reserving policies; operational controls; IT systems; model release and control procedures; risk management and control framework; risk appetite and limit structure and future developments relevant to model recognition.
- 21 G A visit will usually involve the FSA wishing to meet senior management and staff from the front office, financial control, risk management, operations, systems development, information technology and internal audit areas.
- 22 G The FSA may complement its own review of a VaR model individual *guidance* request with one or more reviews by a *skilled person* under section 166 of the *Act*. Such a review may also be used where VaR model individual *guidance* has been given to ensure that the standards on which the VaR model individual *guidance* was based continue to be met.
- 23 G As set out in 9G the FSA will issue individual *guidance* containing certain conditions. These conditions are likely to cover the standards described in this chapter to the extent that they are relevant to the circumstances, and may set out:

- (1) the details of the calculation of VaR model based *PRR*, which will contain the multiplication factor to be applied;
  - (2) the method of separating out specific risk if appropriate;
  - (3) the method agreed of calculating profit and loss accounts for backtesting purposes;
  - (4) the circumstances in which model refinements, new products, new markets and new locations should be notified to the FSA;
  - (5) any notification requirements relating to the VaR model individual *guidance*;
  - (6) any additional reporting requirements (e.g. electronic reporting of backtesting results);
  - (7) details of the changes to the VaR model which would be considered material by the FSA; and
  - (8) any other conditions attached to the VaR model individual *guidance*.
- 24 G Where a VaR model used outside of the United Kingdom differs from that used in the United Kingdom a bank the FSA may request details on the reasons for using different models.
- 25 G Where a bank operates any part of its VaR model outside of the United Kingdom, the FSA may take into account the results of the home supervisor's VaR model review. The FSA may wish to receive information directly from the home supervisor.

#### Maintenance of VaR model

- 26 G No changes may be made to a VaR model which is the subject of individual *guidance* unless the change is not material. Material changes to a VaR model will require further individual *guidance* to be issued. Materiality is measured against the VaR model as it was at the time that the individual *guidance* was originally given. If a bank is considering making material changes to its VaR model then it should notify the FSA at once.
- 27 G If the VaR model ceases to meet the conditions of individual *guidance*, a bank should notify the FSA at once.

#### Risk management standards

- 28 G A bank with a complex portfolio is expected to demonstrate more sophistication in its modelling and risk management than a bank with a simple portfolio. For example, a bank will be expected to consider, where necessary, varying degrees of liquidity for different risk factors, the complexity of risk modelling across time zones, product categories and risk factors. Some trade-off is permissible between the sophistication and accuracy of the model and the conservatism of underlying assumptions or simplifications.
- 29 G A bank should be able to demonstrate that it meets the risk management standards set out in this section on a legal entity basis. This is particularly important for subsidiaries of *groups* subject to matrix management where the business lines cut across legal entity boundaries.
- 30 G A bank should have a conceptually sound risk management system surrounding the use of a VaR model which is implemented with integrity and should meet the following minimum standards:
- (1) the VaR model should be fully integrated into the daily risk management process of the bank, and serve as the basis for reporting risk exposures to senior management of the bank;
  - (2) a bank should have a risk control unit which is independent from business trading units, and which reports directly to senior management. The unit should be responsible for designing and implementing the bank's risk management system. It should produce and analyse daily reports on the output of the model and on the appropriate measures to be taken in terms of the trading limits;
  - (3) a bank's directors and senior management should be actively involved in the risk control process, and the daily reports produced by the risk control unit should be reviewed by a level of management with sufficient authority to enforce both reductions of positions taken by individual traders as well as in the bank's overall risk exposure;
  - (4) a bank should have sufficient numbers of staff skilled in the use of sophisticated models in the trading, risk control, audit and back office areas;
  - (5) a bank should have established procedures for monitoring and ensuring compliance with a documented set of appropriate internal policies and controls concerning the overall operation of the risk measurement system;
  - (6) a bank's VaR model should have a proven track record of acceptable accuracy in measuring risk;
  - (7) a bank should conduct a programme of stress testing frequently, and the results of these tests should be reviewed by senior management and reflected in the policies and limits set;



- (8) a bank should have procedures to ensure that the valuation of assets and liabilities is appropriate, and that valuation uncertainty is identified and appropriate reserving is undertaken where necessary; and
- (9) at least once a year, a bank should conduct, as part of its regular internal audit process, a review of its risk management process. This review should include both the activities of the business trading units and of the independent risk control unit, and should be undertaken by suitably qualified staff independent of the areas being reviewed. This review should consider, at a minimum:
  - (a) the adequacy of the documentation of the risk management system and process;
  - (b) the organisation of the risk control unit;
  - (c) the integration of market risk measures into daily risk management and the integrity of the management information system;
  - (d) the process for approving risk pricing models and valuation systems used in front and back offices;
  - (e) the validation of any significant changes in the risk management process;
  - (f) the scope of risks and products captured by the VaR model;
  - (g) the accuracy and completeness of position data;
  - (h) the process used to ensure the consistency, timeliness, independence and reliability of data sources;
  - (i) the accuracy and appropriateness of volatility and correlation assumptions;
  - (j) reserving policies, the accuracy of the valuation procedures, and risk sensitivity calculations;
  - (k) the process employed to evaluate the VaR model's accuracy, including the programme of backtesting;
  - (l) the controls surrounding VaR model development; and
  - (m) the process employed to produce the VaR model based *PRR*.

31 G A bank's VaR model output should be an integral part of the process of planning, monitoring and controlling a bank's market risk profile. The VaR model should be used in conjunction with internal trading and exposure limits. The links between these limits and the model should be consistent over time and understood by senior management.

- 32 G A bank should have adequate VaR model validation procedures to assess its model, and should have procedures in place to ensure that both the assumptions and approximations underlying the model and the limits of the model are appropriate. It should undertake testing of the accuracy of parts of the VaR models as well as the whole model. The FSA will require a period of initial monitoring or live testing before a VaR model can be recognised. Backtesting should be regarded as an additional safeguard rather than the primary model validation tool. A bank should therefore ensure that it has appropriate methods of assessing model validity and does not rely purely on the results of backtesting.
- 33 G In assessing whether the VaR model is implemented with integrity, the FSA will consider the IT systems used to run the model and associated calculations. The assessment may include:
- (1) feeder systems; risk aggregation systems; time series databases; the VaR model system; stress testing system; the backtesting system including profit & loss cleaning systems where appropriate; data quality; reconciliations and checks on completeness of capture;
  - (2) system development, change control and documentation; security and audit trails; system availability and contingency procedures; network adequacy; and
  - (3) operational statistics relating to VaR model production process; examples of these statistics are timeliness, number of re-runs required and the reliability of data feeds.
- 34 G It is the responsibility of a bank's own management to ensure the accuracy and integrity of its VaR model. This responsibility includes obtaining appropriate independent validation of the VaR model.
- 35 G A bank should ensure that it has adequate controls surrounding:
- (1) the derivation of the VaR model based *PRR*;
  - (2) the integrity of the backtesting programme, including the calculation of the profit and loss account;
  - (3) the integrity and appropriateness of the VaR model, including the model's geographic coverage and the completeness of data sources;
  - (4) the VaR model's initial and on going development, including independent validation;
  - (5) the valuation models, including independent validation; and
  - (6) the adequacy and security/integrity of the IT infrastructure.

## Model standards

- 36 G A bank should base its *PRR* calculation on the output of the VaR model which is used for its internal risk management rather than one developed specifically to calculate its *PRR*.
- 37 G The FSA accepts that the scope and nature of VaR models varies across banks. This means that different banks are likely to calculate different estimates of market risk for the same portfolio. Systematic differences are due to length of data series, choice of methodology (historical or Monte Carlo simulation or variance-covariance method or a hybrid of these), differences in aggregating risks within and across broad risk factors, the treatment of *options* and other non-linear products and the specification of risk factors.
- 38 G A bank that chooses to request individual *guidance* to use a VaR model for the calculation of its *PRR* should calculate its market risk using the appropriate model parameters as set out in 39G.
- 39 G A bank should calculate its market risk by adopting the following minimum standards:
- (1) VaR should be calculated at least daily, using a 99% one-tailed confidence limit.
  - (2) VaR should be calculated using a holding period equivalent to ten *business days*.
  - (3) VaR measures should be based on an effective historical observation period of at least one-year, except where a shorter observation period is justified by a significant change in price volatility. If a weighting scheme or other method is used, then the effective observation period should be at least one year. The weighted average time lag of the individual observations should not be less than six months.
  - (4) Data sets should be updated no less frequently than quarterly and more frequently whenever market prices are subject to material change.
- 40 G A bank may meet the appropriate model parameter requirement by using different model parameters and employing a suitable adjustment mechanism to produce a VaR figure which is equivalent to the figure produced using the parameters set out in 39G. For example, a bank's own model may use a 95% one-tailed confidence limit, but a mechanism to convert the output of the model to reflect a 99% one-tailed confidence limit should be employed.

## RISK FACTORS

- 41 G A VaR model should capture and accurately reflect, on a continuing basis, all material general market risks and, where VaR model individual *guidance* has been granted in relation to specific risk, specific risks arising on the underlying portfolio, and should ensure that sufficient risk factors are properly specified.

#### GENERAL MARKET RISK

- 42 G A bank's VaR model should capture a sufficient number of risk factors in relation to the level of activity of the bank, in particular the following:
- (1) For interest rate risk, the VaR model should incorporate a set of risk factors corresponding to the interest rate curves in each currency in which the bank has interest rate sensitive positions. A bank should ensure that it captures the variations of volatility of rates along the yield curve. In order to achieve this, a bank should divide the yield curves of, at a minimum, the major currencies and markets where it has material interest rate exposures into a minimum of six maturity segments. The risk measurement system should also capture the risk of less than perfectly correlated movements between different yield curves.
  - (2) For foreign exchange risk, the VaR model should incorporate risk factors corresponding to the individual foreign currencies, including gold, in which the bank's positions are denominated.
  - (3) For *equity* risk, the VaR model should use a separate risk factor at least for each of the *equity* markets in which the bank has material exposures.
  - (4) For *commodity* risk, the VaR model should use a separate risk factor at least for each *commodity* in which the bank has material exposures. The VaR model should capture the risk of less than perfectly correlated movements between similar, but not identical, *commodities* and the exposure to changes in forward prices arising from maturity mismatches. It should also take account of market characteristics, notably delivery dates and the scope provided to traders to close out positions.
  - (5) A bank that deals in *options*, or products with *option*-like characteristics, should ensure that their VaR model captures non-linear risk. Steps should also be taken to ensure that adequate capital is set aside for any other risks not captured by the model. Banks are reminded that, under 41G, the standard *PRR* rules may instead be applied to these risks.
  - (6) Correlations within and between the risk factors in (1) to (4) may be used provided the system for measuring these correlations is sound and implemented with integrity.

#### SPECIFIC RISK

- 43 G Where a bank wishes to use a VaR model in relation to specific risk it should meet the following additional standards:

- (1) The model on which the VaR estimate is based should explain the price variation in the portfolio. For example, the VaR model may be based on a factor model or on a historical simulation model. The ability of the model to explain price variation could be demonstrated by a statistical comparison over the same period of time between actual price changes on the portfolio and the profit and loss impact of risk factors included within the model. A bank may wish to include an estimate of residual variation not explained by the model.
- (2) The VaR model should be sensitive to changes in the level of concentration risk in the portfolio.
- (3) The VaR model should be robust to an adverse environment.
- (4) Where a bank calculates its specific risk surcharge under 77G(2) it should conduct specific risk backtesting for the traded debt portfolio and the *equity* portfolio separately. Specific risk backtesting is a comparison of the specific risk VaR measures against the corresponding actual P&L for sub-portfolios that contain material specific risk.
- (5) The VaR model should be validated through empirical testing appropriate to the level of complexity and the assumptions made in the VaR model, which should be aimed at assessing whether specific risk is being adequately captured. Where specific risk is identified by examining relevant sub-portfolios, then these should be chosen in a consistent manner.

- 44 G A bank should have means to assess and, if necessary, mitigate or control event risk. For example, possible means include stress-testing procedures, or reserving policies. It is not however necessary to include factors to model event risk within a specific risk model unless warranted by the nature of the portfolio.

#### Stress testing and backtesting

##### STRESS TESTING

- 45 G Stress testing should involve identifying market scenarios or other low probability events in all types of risks that generate the greatest losses on a bank's portfolio.
- 46 G A bank should periodically and actively identify all the worst case scenarios that are relevant to its portfolio. Scenarios used should be appropriate to test the effect of adverse movements in market volatilities and correlations and the effect of any change in the assumptions underlying the VaR model. Scenarios involving low probability market events should nevertheless be plausible.
- 47 G A bank should have procedures to assess and respond to the results produced from stress testing. In particular, stress testing results should be:

- (1) used to evaluate its capacity to absorb such losses or identify steps to be taken to reduce risk.
  - (2) communicated routinely to senior management and periodically to the directors.
- 48 G Stress testing should capture non-linear effects.
- 49 G A bank should have the capacity to run daily stress tests. A bank may want to conduct the more complex stress tests at longer intervals or on an ad hoc basis.

#### BACKTESTING

- 50 G Backtesting is the process of comparing VaR risk measures to portfolio performance. It is intended to act as one of the mechanisms for the ongoing validation of a bank's VaR model and to provide incentives for banks to improve their VaR measures.
- 51 G Backtesting is only one method of assessing the performance of a VaR model and, although banks are required to carry out a backtesting programme, they should adopt other methods of measuring performance as well.
- 52 G Before individual *guidance* will be given to use a VaR model, a bank should have a backtesting programme in place and should provide three months of backtesting history.
- 53 G A *bank* should have the capacity to analyse its daily profit and loss account and compare the results to the VaR measure used for backtesting, both at the level of the whole portfolio covered by the VaR model and at the level of individual books that contribute material amounts to risk or the profit and loss account.
- 54 G VaR models are likely to undergo almost continuous refinements. This may make it difficult to backtest using 250 days' data if it is based upon a previous version of the model. If a refinement is not regarded as material, then a bank may use the last 250 days' data for backtesting purposes.
- 55 G A bank should compare each of its 250 most recent *business days*' profit and loss account figures with the corresponding one-day VaR measures. This comparison should be made daily using a rolling 250-day period.
- 56 G The VaR measure used for backtesting for these purposes should be calibrated to a one-day holding period and a 99% one-tailed confidence level, but otherwise the VaR model should be the same as that used to calculate the VaR model based *PRR*.
- 57 G The positions underlying the profit and loss account and VaR measures should not be materially different.

- 58 G If a bank uses a combination of the standard rules (and, where appropriate, CAD1 model) and VaR model approaches or does not model specific risk it should take appropriate steps periodically to ensure that this is taken into account in its backtesting procedures.
- 59 G An exception occurs each time a day's loss exceeds the corresponding VaR measure (at bank level). When an exception occurs, a bank should notify its supervisor by close of business two *business days* after the exception occurs (oral notification is acceptable).
- 60 G On a monthly basis, a bank should submit to the FSA a written account of the previous month's exceptions. The written account should include the cause of the exceptions and the bank's planned response. Nil returns will not be required.
- 61 G Where multiple exceptions occur, the multiplication factor used by a bank in its VaR model based *PRR* calculation should be increased by the appropriate plus factor set out in Table 62G (details of how the multiplication factor affects a bank's VaR model based *PRR* are set out in the Calculation of a VaR model based *PRR* section of this chapter). The table sets out the plus factor to be applied given the number of exceptions over the most recent 250 *business days*.
- 62 G Table: backtesting plus factors (see 61G)

<b>Zone</b>	<b>Number of Exceptions</b>	<b>Plus Factor</b>
<b>Green</b>	Fewer than 5	0.00
<b>Yellow</b>	5	0.40
	6	0.50
	7	0.65
	8	0.75
	9	0.85
<b>Red</b>	10	1.00

- 63 G The addition of a plus factor for VaR models that appear to be under-performing is designed to act as an incentive to ensure that the VaR model continues to perform well, and where it does not, that a bank takes prompt action to remedy the situation.

- 64 G If ten or more exceptions are recorded in a 250 day period, the bank should to take immediate corrective action. In these circumstances, the FSA may apply a plus factor greater than one, or the FSA may consider withdrawing a bank's VaR model individual *guidance*.
- 65 G If ten or more exceptions are recorded in a 250 day period due to the specific risk backtesting required in 43(4) G then the bank should take immediate corrective action on the specific risk part of the model or set aside additional capital.
- 66 G If a bank believes an exception should be disregarded it should submit to the FSA a written explanation of why the exception occurred and why it would be appropriate to disregard it. An exception may be disregarded only in exceptional situations. One example of an exception might properly be disregarded is when it has arisen as a result of a risk that is not captured in its VaR model but against which regulatory capital is already held.
- 67 G The FSA may also consider disregarding a backtesting exception where, in a period of high volatility, multiple backtesting exceptions occur before the data set is updated.
- 68 G During the first 250 days after a bank starts to use its VaR model to calculate its VaR model based *PRR*, the policy in 61G relating to plus factors only applies to the period from the date that VaR model recognition is granted.

#### DEFINITION OF PROFIT AND LOSS ACCOUNT FOR BACKTESTING PURPOSES

- 69 G Backtesting should be performed using a measure of actual profit and loss.
- 70 G Actual profit and loss means the day's profit and loss account arising from the trading activities within the scope of the VaR model. This should exclude material non-market elements which might mask a loss. Such elements include *fees* and *commissions*, reserving which is not directly related market risk and one-off marketing profits from new deals.
- 71 G Actual profit and loss should reflect any price adjustments arising from position reconciliation in accordance with a bank's written policies and procedures. These policies and procedures should include a documented method of assigning valuation adjustments to backtesting data, such that the amount and the date of adjustment is unambiguous.
- 72 G A bank should have the capacity to perform backtesting against hypothetical profit and loss. The FSA may require banks to produce this information upon request. Hypothetical profit and loss means profit and loss that would have occurred had the portfolio remained unchanged.



- 73 G VaR models are likely to undergo almost continuous refinements. This may make it difficult to backtest using 250 days' data if it is based upon a previous version of the model. If a refinement is regarded as material then new individual *guidance* may be required to use a VaR model and the original individual *guidance* may be withdrawn (as set out in 27G). If a refinement is not material then a bank may use the last 250 days' data for backtesting purposes.

#### Calculation of VaR model based PRR

- 74 G The calculation of a *PRR* under the VaR model approach is set out in this section. As noted in section 5 of chapter CO the individual *guidance* will confirm that a bank should add its VaR model based to its other *PRRs* calculated under section 3.4 of chapter CO.
- 75 G A bank's VaR model based *PRR* on a daily basis is equal to the higher of:
- (1) its previous day's VaR number; and
  - (2) the average of its daily VaR measures on each of the preceding sixty *business days* multiplied by a multiplication factor (increased by the appropriate plus factor referred to in 62G).
- 76 G The multiplication factor to be used is specified by the FSA in the formal VaR model individual *guidance* direction as a condition of its use. The minimum multiplication factor that the FSA will set is 3, although a higher multiplication factor may be applied. This multiplication factor is the factor that should be used, unless individual *guidance* has been given.

- G The following equation expresses 75G and 76G mathematically

$$PRR_{VaR} = \text{Max} \left( VaR_t, f \times \frac{1}{60} \sum_{i=0}^{59} VaR_{t-i} \right) + SR$$

$PRR_{VaR}$  is a bank's VaR model based *PRR*;

$VaR_t$  represents the previous day's VaR figure;

$VaR_{t-i}$  represents the VaR calculated for *i business days* earlier;

$f$  is the multiplication factor referred to in 75(2)G and 76G;

$SR$  is the specific risk surcharge which is only included in the calculation set out 79G where a bank has been given VaR model individual *guidance* in relation to specific risk. Details on the specific risk surcharge can be found in 18G to 19G.

- 77 G If the VaR model individual *guidance* granted enables a bank to calculate a specific risk *PRR* by the use of its VaR model then it should calculate its specific risk surcharge as either:
- (1) an amount equal to the specific risk portion of the VaR measure; or
  - (2) an amount equal to the VaR measure of sub- portfolios that are subject to specific risk.

In both cases, the specific risk surcharge should be calculated as an average over the previous 60 *business days*.

- 78 G Where the bank calculates its specific risk surcharge using 77(1)G, then it should calculate specific risk for the purposes of calculating the surcharge as the difference between total value at risk and a measure of general market risk. In calculating general market risk for this purpose, positions that give rise to specific risk should be mapped to equivalent positions that bear general market risk only. In doing so, the following minimum standards should be adopted:
- (1) For *equities*, each position should be mapped to a factor that is representative of the national or international market to which they belong. For example, a stock may be mapped to a widely accepted broadly based stock market index for the country concerned.
  - (2) For bonds, each position should be mapped using a reference interest rate curve for the currency concerned. The interest rate curves should be generally accepted by the market as broadly based reference curves for the currency concerned, for example, a government bond curve or a swap curve.
- 79 G Where a bank calculates its specific risk surcharge using 77(2) G, then the sub-portfolio structure should be identified in advance and any changes to the structure should be pre-notified to FSA. The sub-portfolios chosen should be those which contain positions that would produce a specific risk *PRR* under the standard rules approach.

#### Definitions used in Chapter TV

This chapter uses the following definitions:

Defined term	Definition
<i>Act</i>	The Financial Services and Markets Act 2000.
<i>Business days</i>	(1) in relation to anything done or to be done in any part of the United Kingdom): (a) (except in REC) any day which is not a Saturday or Sunday, Christmas Day, Good Friday or a bank holiday in that part of the United Kingdom; (b) (in REC) (as defined in section 167 of the Companies Act 1988) any day which is not a Saturday or Sunday, Christmas Day, good Friday or a bank holiday in any part of the United Kingdom. (2) (in relation to anything done or to be done by reference to a market outside the United Kingdom) any day on which that market is normally open for business.
<i>Commission</i>	Any form of commission, including a benefit of any kind, offered or given in connection with designated investment business.
<i>Commodity</i>	Any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB the definition of commodity

	used in TV deliberately differs from that in the main Handbook Glossary).
<i>Equity</i>	See <i>share</i> .
<i>Fee</i>	Any payment offered or made by a client to a firm in connection with designated investment business or with any other business of the firm, including (where applicable) any mark-up or mark-down.
<i>Future</i>	As specified in article 78 of the Regulated Activities Order (Futures).
<i>Guidance</i>	Guidance given by the FSA under the Act.
<i>Option</i>	A contract which confers the right to buy or sell a <i>security</i> , contractually based investment, currency, gold or <i>commodity</i> at a given price on or before a given date. (NB: the definition of an option used for the purposes of this chapter deliberately differs from that in the main Handbook Glossary).
<i>PRR</i>	Position risk requirement.
<i>Share</i>	As specified in article 76 of the Regulated Activities Order (Shares etc).
<i>Skilled person</i>	A person reported to make a report required by section 166 of the Act (Reports by skilled persons) for provision to the FSA and who must be a person: (a) nominated or approved by FSA; and (b) appearing to the FSA to have the skills necessary to make a report on the matter concerned.

## Annex I

### Transitionals

In this Annex, text is being inserted that is not underlined.

Insert the following text as a new chapter TRANS before Chapter GN in volume 1 as follows:

TRANS

#### Transitional provisions

##### 1 Table

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1	The provisions of <i>IPRU(BANK)</i> added by the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004	G	<p>(A) A <i>bank</i> may treat the material in column (2) of paragraph 1:</p> <p>(a) as being in force; and</p> <p>(b) as having replaced the material in <i>IPRU(BANK)</i> that will be deleted by the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004;</p> <p>at any time when this transitional provision is in force.</p> <p>(B) For this purpose, the following applies.</p> <p>(a) A <i>bank</i> should notify the <i>FSA</i> if it takes advantage of this transitional provision.</p> <p>(b) A <i>bank's</i> choice to take advantage of this transitional provision takes effect when notified to the <i>FSA</i> under (a).</p> <p>(c) A <i>bank</i> should not revoke the choice to make use of this</p>	1 July 2004 – 30 June 2005	The material in the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004 comes into force for all <i>banks</i> on 1 July 2005.

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			<p>transitional provision.</p> <p>(d) Any choice to take advantage of this transitional provision:</p> <p>(i) applies on a consolidated basis and a solo basis; and</p> <p>(ii) applies to all the material in column (2) of paragraph 1 and not part only.</p> <p>(e) A <i>bank</i> should not take advantage of this transitional provision unless every <i>bank</i> in its consolidated group to which this transitional provision can apply does so too in accordance with (b).</p> <p>(f) The Glossary in chapter GN of <i>IPRU(BANK)</i> applies to italicised terms in this transitional provision.</p>		

## Annex J

### Consequential changes to IPRU(BANK)

In this Annex, underlining indicates new text and striking through indicates deleted text unless otherwise specified.

#### The contents pages for Volume 1

##### *Treatments common to the banking and trading book*

FX	Foreign exchange <u>position risk requirement</u>
CM	Commodities <u>position risk requirement</u>
DU	Common treatments for counterparty risk

##### *Specific trading book treatments*

TI	Interest rate position risk <u>requirement</u>
TE	Equity position risk <u>requirement</u>
TC	Counterparty risk in the trading book
TL	Incremental capital for large exposures
TU	<del>Underwriting in a capital adequacy framework</del> <u>Securities underwriting</u>
<u>TO</u>	<u>Options position risk requirement</u>
TS	CAD1 models
TV	<del>The use of internal models</del> <u>VaR models</u>

#### Chapter GN, s3.3.14G

- 3.3.14G Guidance on how a UK bank and an overseas bank should comply with IPRU(Bank)3.313R is set out in chapter CO (which provides an overview of the underlying policy) and more detailed guidance in chapters CB, CA, BC, FX, CM, DU, TI, TE, TC, TL, TU, TO, TS and TV.

#### Chapter CO, section 3.2

- 4 (a) Credit risk in the banking book should be included in the regime using a weighting approach to derive risk weighted assets and their equivalents for off balance sheet items. The approach is given in the chapter on credit risk in the banking book.
- (b) There are at present no explicit capital requirements for interest rate risk in the banking book. A bank should nevertheless maintain adequate capital to cover interest rate risk to which it is exposed in its banking book.

### Chapter CO, section 3.4

- See s4 10 The standard treatment of trading book capital requirements for market risk should include calculations under ~~five~~ six separate headings, as explained below. The following chapters each feed into a separate heading, as indicated:

*[Paragraphs (a) – (e) unchanged]*

- See ch TO (f) Option position risk in the trading book should form part of the calculation for option position risk.

### Chapter CO, section 4.1.3

- 7 For CAD banks, separate ICRs are set for the trading and banking books.
- a) Because the banking book regime is expressed in terms of a ratio in proportion to risk weighted assets, whilst the trading book regime established by the CAD expresses its requirement as capital ~~haircut~~ requirements (i.e. the level of capital required to support an associated risk), a method is needed to allow trading book ICRs to be brought into the framework. This has been achieved by multiplying the trading book aggregate capital ~~haircut~~ requirement by 12.5 to produce a notional risk weighted asset equivalent which can be multiplied by the trading book ICR. This system is purely supervisory and banks should not publish their ratios in this form.

### Chapter CO, section 5

- 3 Optimisation of the use of capital may be achieved by carrying out the calculations in the following order (although in which steps (b), (c) and (d) are carried out is not critical):

*[Paragraph (a) unchanged]*

- (b) Calculate trading book capital requirements.

Trading book trigger = X%

	<del>CAD</del> <del>Haircut</del> Capital <u>requirement</u>	Notional risk weighted assets	Capital required
FX position risk	A	12.5 x A	X% of (12.5 x A)
Equity position risk	B	12.5 x B	X% of (12.5 x B)
Interest rate position risk	C	12.5 x C	X% of (12.5 x C)
Large exposures position risk	D	12.5 x D	X% of (12.5 x D)
Trading book counterparty and settlement risk	E	12.5 x E	X% of (12.5 x E)
Commodity position risk	F	12.5 x F	X% of (12.5 x F)
Activities subject to internal models	G	12.5 x G	X% of (12.5 x G)
<u>Option position risk</u>	<u>I</u>	<u>12.5 x I</u>	<u>X% of (12.5 x I)</u>

- a) Note that multiplying by 12.5 is equivalent to dividing by 8%. See above for the explanation of why this is necessary to place the elements of the capital calculation on the same basis.
- b) Capital requirements G for activities subject to internal models is equal to F in the table in section 2.1 of the chapter on internal models are shown in 76G in chapter TV.

[Paragraphs (c) – (k) unchanged]

- (l) The capital adequacy ratio should be calculated by the following equation:

$$\frac{(\text{Tier 1} + \text{eligible Tier 2} + \text{used Tier 3} - \text{deductions}) \times 100}{X\% \text{ of } 12.5 \times (\text{A} + \text{B} + \text{C} + \text{D} + \text{E} + \text{F} + \text{G} + \text{I}) + Y\% \text{ of H}}$$

### Chapter CB, section 3.2.2

- 7 For the purpose of paragraph 4, *financial instruments* are as defined in Section B of the Annex to the ISD. They are:

[Paragraphs (a) – (g) unchanged]

See chs  
TI, TO  
eh and  
TE

For detailed lists of instruments within each of these categories that may be included in the trading book in their own rights, see the chapters on equity position, option risk and interest rate risk

### Chapter CB, section 5.2

- 8 There are several areas where a CAD bank has a choice of method for calculating various of its position risk capital requirements.

[Paragraph a) unchanged]

See chs FX,  
TI, CM,  
TO, TS and  
TV ~~TM~~

- i) For further details, see the relevant sections of the chapters on foreign exchange risk, interest rate risk, commodity risk, option risk and models.

### Chapter CA, section 10.2

- 2 [Unchanged up to paragraph (c)]

- (c) All holdings of capital instruments issued by other *credit institutions* and *financial firms* unless they are covered by a *trading book concession*;

- a) This deduction applies to:
  - All long, physical positions in instruments which are included in the capital of the issuing *credit* or *financial institution* (including such instruments sold under sale and repurchase agreements, instruments carrying third party guarantees (including central government guarantees), depository receipts, and net ~~commitments to underwrite~~ underwriting positions in issues of such instruments (from working day zero));
  - In the case of net commitments to underwrite (see indent above), the ~~scaling~~ reduction factors in the chapter on underwriting may be applied

See ch s-3  
TU27G



before deduction.

### Chapter DU, section 2.2

See chs 4 The bank should hold capital in respect of both market and counterparty risk. This chapter  
TI, TE, deals with counterparty risk, the treatment of market risk in the trading book is given in the  
CM, relevant chapters on equity position risk, interest rate position risk, commodity position risk,  
FX, TO foreign exchange position risk, option position risk and internal models.  
and TV

[Note: The word "both" in the first sentence is underlined in the original and is not new text.]

### Chapter TC, section 2.2

See chs 2 A bank should hold capital in respect of both market and counterparty risks in the trading  
TI, TE, book; the treatment of market risk which should be adopted is given in the relevant chapters on  
CM, equity position risk, interest rate position risk, commodity position risk, foreign exchange  
FX, TO position risk ~~and~~ internal models and option position risk.  
and TV

[Note: The word "both" in the first sentence is underlined in the original and is not new text.]

### Chapter LE, section 7.1

2 For the purposes of form LE2 (and LE3), where a bank deals in securities, the exposure to the issuer of the security should be calculated as follows:

[Paragraph (a) unchanged]

(b) for the trading book, first the excess of the current market value of all long positions over all short positions should be calculated for each instrument issued by the issuer. The exposure is then the excess, where positive, of the current market value of all long positions over all short positions in all the financial instruments issued by the counterparty.

See chs TI, 2 a) When netting long positions in different instruments, the short positions should  
TO and TE be netted against the long positions in instruments with the highest specific risk. Specific risk charges are covered in the chapters on interest rate, ~~and~~ equity and option position risk.

### Chapter CD, section 7

See chs TS 3 Banks may apply to the FSA to include credit derivatives in recognised models under CAD1  
and TV and also under ~~CAD2~~ VaR models. Banks may apply for recognition of ~~CAD2~~ VaR models which quantify partial offsets for specific risk positions where there is a maturity or asset mismatch.

10 As noted above, total return swaps, credit default products and credit-linked notes create a specific risk position in the reference asset; the credit risk seller has a short position and the credit risk buyer has a long position.

See ch TI a) For the specific risk position to be treated as a qualifying debt item, the reference asset  
s5 should meet the standard conditions for a qualifying debt item as defined in the chapter  
46G on interest rate position risk.

- 17 Where a multiple-name credit-linked note is rated such as to meet the conditions for recognition as a qualifying debt item, the buyer of credit risk may record the specific risk position in the reference assets as a single long specific risk position with the specific risk of the note issuer.
- See ch TI  
55  
46G
- a) Qualifying debt items are defined in the chapter on interest rate position risk.
- 19 Banks may net notional positions in reference asset created by credit derivatives with positions in underlying assets or other notional positions created by other credit derivatives if the following conditions are met:
- See ch TI  
53  
37G
- (a) the underlying and reference assets are issued by the same obligor;
- (b) the underlying and reference asset specific risk positions meet the matching criteria set out in the chapter on interest rate position risk; and
- See ch TI  
56
- 23 Credit default products do not normally create a general market risk position.

[Note: The phrase "Credit default products" is underlined in the original and is not new text.]

- 29 The add-on used when calculating the counterparty exposure for an unfunded OTC credit derivative is determined by whether the reference asset is recognised as a qualifying debt item. If the reference asset is a qualifying debt item, the counterparty risk charge is calculated using interest rate add-ons. Otherwise, equity add-ons should be used
- See ch TI  
55  
46G
- a) Qualifying debt items are defined in the chapter on interest rate position risk.

### Chapter CD, section 8.3

- 5 The option ~~carve-out treatment~~ standard method should be used for credit spread options only after consultation with the FSA. Banks should normally apply for recognition of option models covering credit spread options.

### Chapter SE, section 3.2.2

- 4 A bank acts as a *sponsor* or *repackager* when:
- [Paragraph (a) unchanged]
- (b) As a repackager, it sells *investment grade* third party *financial instruments* via its balance sheet to an SPV that then rebundles them and resells them to investors.
- a) In a *repackaging scheme*, the repackager is *not* the original lender and is therefore subject to fewer limitations than an originator.
- b) Where the assets are influenced in credit quality by reference to the repackaging bank, the bank will be regarded as an originator.
- See ch TI  
59  
47G
- c) For a definition of *investment grade* see the interest rate position risk chapter. Where the securities to be repackaged are not rated, the bank should be able to demonstrate that the asset are of a comparable quality.

### Chapter SE, section 9.3

- See ch TI  
~~s9~~  
47G
- 5 Securities issued that are deemed to be investment grade by relevant rating agencies, as defined, are deemed not to constitute credit enhancement if there is already sufficient credit enhancement within the terms of this section.

### Chapter SE, section 11.1

- See s6.2
- See ch TI  
~~s9~~  
47G
- 3 An originator should not deal in the securities issued by the SPV unless it has discussed its intentions with the FSA. The FSA considers that a bank's deals should be limited. Appropriate limits are likely to represent only a small fraction of the total securities issued
- a) Limit structures should generally be subject to limits specific to individual tiers of securities issued. Limits are likely to be more constraining for trading in securities other than the most senior debt.
  - b) It is an accepted role of an originating bank to promote an orderly market in the securities issued by the SPV, but not to the extent that the originator is or appears to be able to support the issue, which would be in contravention of the policy above.
  - c) The ability to deal in securities is limited to securities deemed to be of investment grade by a relevant rating agency as defined. Securities below investment grade fall within the definition of credit enhancement as described below.

### Chapter ST, section 2.1

- See ch FX  
~~s2~~
- 1 A bank which has *net open positions* in foreign currencies (including gold), either because of FX trading positions or because of exposures caused by its overall assets and liabilities, is exposed to the risk that the relevant exchange rate or rates might move against it -*FX risk* (or exchange rate risk). It is therefore important that a bank has adequate systems and controls to manage that risk.
- a) For the purpose of this chapter foreign currency / foreign exchange are referred to as FX.
  - b) ~~For the definition of net open position see the chapter on FX risk.~~

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(MARKET RISK) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157 (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. Annex A comes into force on 1 July 2004. Annexes B, C and D to this instrument come into force on 1 July 2005.

**Amendments to the Interim Prudential sourcebook for Investment Businesses**

- D. The Interim Prudential sourcebook for Investment Businesses is amended in accordance with the Annexes to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Market Risk) Instrument 2004.

By order of the Board  
20 May 2004

## Annex A

### Transitional provisions

In this Annex, underlining indicates new text.

Insert before Chapter 1 a new transitional provision as follows:

#### Transitional provisions

**1 Table Transitional provisions applying to IPRU(INV)**

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
<u>2</u>	<u>The provisions of IPRU(INV) added by the Interim Prudential Sourcebook for Investment Firms (Market Risk) Instrument 2004</u>	<u>R</u>	<p><u>(A) A securities and futures firm which is an investment firm may treat the material in column (2) of paragraph 2:</u></p> <p><u>(a) as being in force; and</u></p> <p><u>(b) as having replaced the material in IPRU(INV) that will be amended or deleted by the Interim Prudential Sourcebook for Investment Firms (Market Risk) Instrument 2004; at any time when this transitional provision is in force.</u></p> <p><u>(B) For this purpose, the following applies.</u></p> <p><u>(a) A firm must notify the FSA if it takes advantage of this transitional provision.</u></p> <p><u>(b) A firm's choice to take advantage of this transitional provision takes effect when notified to the FSA under (a).</u></p> <p><u>(c) A firm must not revoke the choice to make use of this transitional provision.</u></p> <p><u>(d) Any choice to take advantage of this transitional provision:</u></p> <p><u>(i) applies on a consolidated</u></p>	1 July 2004 – 30 June 2005	The material in the Interim Prudential Sourcebook for Investment Firms (Market Risk) Instrument 2004 comes into force for all securities and futures firms that are investment firms on 1 July 2005.

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			<p><u>basis and a solo basis; and</u></p> <p><u>(ii) applies to all the material in column (2) of paragraph 2 and not part only.</u></p> <p><u>(e) A <i>firm</i> must not take advantage of this transitional provision unless every <i>firm</i> in its consolidated group to which this transitional provision can apply does so too in accordance with (b).</u></p> <p><u>(f) The Glossary in chapter 10 of <i>IPRU(INV)</i> applies to italicised terms in this transitional provision.</u></p>		

## Annex B

### Amendments to Chapter 10

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted, the place where the change will be made is shown and the text is not struck through.

#### Valuation of positions

- 10-41(9) R A *firm* must value both *trading book* positions and *non-trading book investment* positions 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, and must adopt the following general policies:
- (a) a position must be valued at its close out price (close out price means that a long position is to be valued at current bid price and a short position at current offer price); where firm two way prices are not available a *firm* must value its position in accordance with the notes to this rule;
  - (b) ~~where a *firm* has been granted a modification or waiver by the FSA to use a risk assessment model in the calculation of its PRR on *options* positions (as described in the guidance at 10-82(4) and 10-101(2)), it may value its *options* using the values derived from the model;~~  
where a *firm* has been granted a modification or waiver by the FSA to use a CAD1 or VaR model in the calculation of its PRR (as described in the guidance at Appendix 10 and 11), it may value its positions in instruments within the scope of that waiver using the values derived from the internal valuation model(s) that the firm uses to produce feeds for that CAD1 or VaR model.
  - (c) ~~where a *firm* does not use a model as described in (b) above and prices are not published for its *options* positions where prices are not published for its *options* positions and a *firm* does not have a waiver to use a model to value them,~~ it must determine the *mark to market* value of standard European and American *options* as follows:
    - (i) for purchased options, the *mark to market* value must be the in the money amount multiplied by the quantity underlying the *option*;
    - (ii) for written *options* the *mark to market* value must be the sum of:
      - (aa) the *in the money* amount multiplied by the quantity underlying the option; and
      - (bb) the initial premium received for the *option*;

G Where a *firm* has been granted a waiver by the *FSA* to use a CAD1 or VaR model in the calculation of its *PRR* or *FER* (as described in the guidance in Appendix 11 and 12), it may value its positions in instruments that come within the scope of that waiver using the values derived from the internal valuation models that the *firm* uses to feed that CAD1 or VAR model;

G If a written *option* was *in the money* at the time the contract was written, *in the money* amount in (aa) may be taken to be the current *in the money* amount less the *in the money* amount at the time the contract was written.

...

#### Valuing instruments at maximum loss

10-41(11) R A *firm* may exclude a position from its *PRR*, *CRR* and *LER* calculations if it values the position in either of the two following ways and it notifies the *FSA* in writing that it is doing so:

(a) a short position that is valued at maximum loss; or

(b) a long position that is valued at zero.

G For example, a *firm* might write a one touch digital *option* which requires the *firm* to pay out £100 where the price of the underlying exceeds a certain threshold. In the worst case (including ignoring the time value of money) the *firm* would lose £100 overall. If the *firm* valued this position at -£100 it would not have to include this position in its *PRR*, *CRR* and *LER* calculations.

...

#### 10-64 LIQUIDITY AJUSTMENT

##### General rule

10-64 (1) R A *firm's* liquidity adjustment for its assets must be calculated -

(a) for *illiquid assets*, other than *commodities*, in accordance with rule 10-65;

(b) for other *non-trading book* assets, other than *commodities*, in accordance with rule 10-66; and

(c) for all *commodities* in accordance with ~~rule 10-166~~ appendix 6 (commodities *PRR*) and rule 10-170 (*CRR*).

...

#### PRIMARY REQUIREMENT

10-71 R A *firm's* primary requirement is the higher of:



- (a) the sum of its *PRR*, ~~*FER*~~, *CRR*, *LER* and base requirement (calculated in accordance with rule 10-72); or
- (b) the *firm's initial capital requirement* for a *category A, B, C* or *D firm*, calculated in accordance with 10-61(8).

BASE REQUIREMENT

10-72 R A *firm's* base requirement must be calculated in accordance with the following formula:

$$\text{Base requirement} = \text{expenditure requirement} \times \left[ \frac{\text{expenditure requirement}}{\text{PRR} + \del{FER} + \text{CRR} + \text{LER} + \text{expenditure requirement}} \right]$$

...

Obligation to calculate PRR

10-80(2) R ~~A *firm* must calculate a minimum *PRR* in respect of any position according to one of the methods available under the rules below but it may calculate a higher *PRR* in any other way at its option, provided it is able to demonstrate that, in all circumstances, the calculation being employed does give rise to a higher *PRR* for the position.~~

G ~~A *firm* that wishes to use its internal model to calculate *PRR* in respect of all, or some, of its positions should apply for a modification or waiver from the relevant rules from the *FSA*.~~

G ~~Further guidance on the criteria which such models must meet, and the review process, can be obtained from the *FSA*.~~

A *firm* must calculate a minimum *PRR* as the sum of the minimum *PRRs* calculated in respect of its positions using:

- (a) the *PRR* calculations contained in the rules and appendices listed in the table below; or
- (b) another method provided the *firm* is able to demonstrate that in all circumstances the calculation being employed results in a higher *PRR* for the position than would be required under (a).

Table 10-80(2)R

<u>10-120R</u>	<u>CIS PRR</u>
<u>Appendix 4</u>	<u>Interest rate PRR</u>

<u>Appendix 5</u>	<u>Equity PRR &amp; basic interest rate PRR for equity derivatives</u>
<u>Appendix 6</u>	<u>Commodity PRR</u>
<u>Appendix 8</u>	<u>Foreign exchange PRR</u>
<u>Appendix 9</u>	<u>Option PRR</u>

G A firm may seek a modification or a waiver to 10-80(2)R to use a CAD1 model or a VaR model as the basis for calculating part or all of the PRR on its positions. For further details on the use of such models see appendices 11 and 12 respectively.

G Appendix 7 (underwriting) does not contain a PRR calculation. Instead, it contains requirements on how to derive the net underwriting position or reduced net underwriting position. These positions are then included in the relevant PRR calculation listed above (i.e. appendix 4, appendix 5 or appendix 9, as well as appendix 8 if the position is denominated in a foreign currency).

...

10-81R to 10-111(5) [deleted]

...

10-130 to 10-169B(3) [deleted]

...

#### Counterparty exposure

10-174(3) R A firm must calculate the counterparty exposure on *derivative* transactions in accordance with either (a), (b) or (c) below:

- (a) where a counterparty has not fully paid a *margin requirement* on a *derivative* transaction listed on an *exchange* or cleared through a clearing house, or met it through the deposit of *acceptable collateral* not otherwise used, a firm must calculate the counterparty exposure as the shortfall;
- (b) where a *firm* sells or writes an *option* to a counterparty or buys an *option* on behalf of a counterparty and the counterparty has not paid the full *option* premium, or met it through the deposit of *acceptable collateral* not otherwise used, it must calculate the counterparty exposure as the uncovered premium on the transaction; or
- (c) a *firm* must calculate the counterparty exposure arising from a *derivative* transaction other than a written or sold *option* or a *derivative* transaction listed on an *exchange* or cleared through a *clearing house*, as the credit equivalent amount calculated in accordance with Table 10-174(3), not covered by the deposit of *acceptable collateral* not otherwise used.

...

If a *firm* uses the modified maturity ladder approach to calculate PRR under ~~rule 10-169~~ 30R of appendix 6, it may use Table 10-174(3B)

...

Calculation of LER

...

- 10-194(3) R Where the value of “R” is less than 25% of the value of *own funds*, the value of “T” may exceed 25% of the value of *financial resources*, subject to an *LER* calculated in accordance with (a) to (e) below –
- (a) calculate the excess of “T” over 25% of the value of *financial resources*, known as “D”;
  - (b) rank the *trading book exposures* in “T” on the basis of the specific risk weighting in the case of *positions*, discounted by the appropriate percentage ~~from table 10-133(5)~~ in accordance with table 27R of appendix 7 in respect of underwriting positions, and the counterparty weighting in the case of counterparty *exposures*, in descending order;
  - (c) sum the *trading book exposures* in “T”, starting with the *exposure* attracting the highest specific risk weighting or counterparty weighting, until the sum equals the excess “D”;

...

#### INTRA-GROUP OFFSETS AND NETTING

- 10-203 R If a group’s *financial resources*, calculated in accordance with rule 10-201, do not exceed the group’s *financial resources requirement*, calculated in accordance with rule 10-202, the *firm* may take into account:
- (a) the benefits of netting intra-group counterparty exposures;
  - (b) offsetting positions, for the purposes of the rules ~~10-80 to 10-153~~ in appendices 4, 5 and 8, held by different group companies; and
  - (c) the group’s share of capital surpluses in *subsidiaries* not subject to local regulatory capital requirements.

## Annex C

### Amendments to Chapter 10 Appendices

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted, the place where the change will be made is indicated and the text is not struck through.

Amend, delete or add definitions to IPRU(INV) Chapter 10 Appendix 1 as shown:

<u>base currency</u>	<u>means the currency currently used by a firm to calculate its financial resource requirements;</u>
<i>basic PRA</i>	<del>means for equities the equity method 1 PRAs in Appendix 49; and for interest rate instruments, the sum of the specific risk PRA and the maturity-based general market risk PRAs in Appendix 53;</del>
<i>eap</i>	<del>means an agreement in respect of a borrowing under which a counterparty contracts to pay any interest costs arising as a result of an increase in rates above an agreed rate: the effect being to provide protection to the holder against a rise above that agreed rate;</del>
<u>CFDs</u>	<u>means contract for differences;</u>
<u>commodity</u>	<u>means any physical or energy product (except gold) which is, or can be traded on a secondary market. (NB: the definition of a commodity used for the purposes of Chapter 10 of IPRU(INV) deliberately differs from that in the main Handbook Glossary);</u>
<u>company</u>	<u>means any body corporate;</u>
<i>company issued warrant</i>	<del>means a right (but not an obligation) to buy a security or other instrument at an agreed price or on an agreed basis, from the issuer of the security or instrument;</del>
<u>equity</u>	<u>means share;</u>
<i>FER</i>	<del>means the foreign exchange requirement of a firm as calculated in accordance with appendix 6;</del>
<u>foreign currency</u>	<u>means a currency other than the firm's base currency;</u>
<i>forward</i>	<del>means a security which is transacted for a settlement date beyond that which would normally apply in the market concerned, and where that forward settlement date is not yet passed; A contract to buy or sell where the date for settlement has been agreed as a particular date in the future;</del>
<i>floor</i>	<del>means an agreement in respect of a deposit under which a counterparty contracts to pay any lost income arising as a result of a fall in rates below an agreed rate: the effect being to provide protection to the holder against a fall below that agreed interest rate;</del>
<i>in the money</i>	<del>means, in relation to call options and warrants, that the exercise price is less than the current mark to market value of the underlying instrument and, in relation to put options, that the current mark to market value is less than the exercise price; <u>means the strike price of a call option or warrant is</u></del>

less than the current market value of the underlying instrument, or vice versa for a put *option*;

open currency position

means the position calculated under 18R of appendix 8;

*option*

means the investment specified in article 77 of the Regulated Activities Order (Options), which is an option to acquire or dispose of:

- (a) a security or contractually based investment (other than an option);
- (b) currency of the united Kingdom or of any other country or territory;
- (c) palladium, platinum, gold or silver; or
- (d) an option to acquire or dispose of an option specified in (a), (b) or (c);

means a contract which confers the right to buy or sell a security, contractually based investment, currency, gold or commodity at a given price on or before a given date. (NB: the definition of an option used for the purposes of Chapter 10 of IPRU (INV) deliberately differs from that in the main Handbook Glossary);

PRR

means the position risk requirement of a firm as calculated in accordance with rules 10-80 to 10-169B rule 10-120 and 4, 5, 6, 8 and 9;

*qualifying debt security*

means a debt *security* which-

- (1)(a) is, or has an "equivalent debt" which is, rated by a "relevant agency" at, or higher than, the level indicated in the Table in Appendix 34 and
- (i) there has been no announcement that the rating will be down-graded below the level so indicated; and
- (ii) the *firm* has no reasonable cause to believe that another "relevant agency" has rated the *security* or "equivalent debt" below the level so indicated;
- (b) is issued or fully guaranteed by-
- (i) a Zone A central government or central bank;
- (ii) a Zone B central government or central bank, provided that the security is denominated in its national currency;
- (iii) a Zone A public sector entity which represents no higher a risk than its central government ;
- (iv) an Zone A *credit institution*, provided that the security represents senior debt of the issuer;
- (v) a Zone B *credit institution*, provided that the security has a maturity of one year or less and is not part of the issuer's own funds;
- (vi) an *investment firm or recognised third country investment firm*;
- (vii) one of the following organisations—  
The African Development Bank;  
The Asian Development Bank;  
The Bank for International Settlements;  
The Caribbean Development Bank;  
The Council of Europe;  
Euratom (European Atomic Energy Community);  
Eurofina (European Company for Financing of Railroad Rolling Stock);  
The European Bank for Reconstruction and Development;  
The European Coal and Steel Community;

The European Economic Community;  
 The European Investment Bank;  
 The Inter-American Development Bank;  
 The International Bank for Reconstruction and Development (World Bank);  
 The International Finance Corporation;  
 The International Monetary Fund;  
 The Nordic Investment Bank;  
 (e) is collateralised by *securities* issued by a Zone A central government, Zone A central bank or one of the institutions listed in (a)(vii) above; or  
 (d) is issued or fully guaranteed by a company whose equity satisfies the criteria set out in section 5(b) of Appendix 49; and  
 (2) for the purposes of (1) above-  
 (a) the issuer or guarantor of the *security* is not in default as to any payment on any other *security* issued or guaranteed by it;  
 (b) in respect of any *security* of, or guaranteed by, any issuer or guarantor, "equivalent debt" means any debt which ranks pari passu with, or subordinated to, the security or (as the case may be) the guarantee; and  
 (c) in relation to any issuer or guarantor, a "relevant agency" means one of the agencies names in Appendix 34 by reference to the category of issue or guarantor;  
means a debt security which meets the conditions in 45R of appendix 4;  
means an equity which meets the conditions in 35R of appendix 5;  
means an equity index which meets the conditions in 38R of appendix 5;  
means a transaction where a physical commodity is sold forward and the cost of funding is locked in until the date of the forward sale;  
means a combination of a long (short) call option and a short (long) put option which are based on the same underlying and have the same notional amount, strike price and maturity;  
means an arrangement made before the relevant securities are issued under which a party agrees to buy a specified quantity of those in an issue of securities on a given date and at a given price, if no other has purchased or acquired them;  
means the working day on which the firm becomes unconditionally committed to accepting a known quantity of securities at an agreed price;  
means a hypothetical debt security used to represent the general interest rate risk arising from certain derivative and forward transactions;

qualifying equity

qualifying equity index

stock financing

synthetic future

underwriting

working day zero

zero specific risk security

Appendices 34 and 35 [deleted]

Appendices 49 to 54 [deleted]

## Annex D

### Additions to Chapter 10 Appendices

In this Annex, new text is being inserted and is not underlined.

Insert the following text as new IPRU(INV) Chapter 10 appendices 4 to 11 as follows:

#### Appendix 4

#### Interest rate PRR

#### General rule

- 1 R A *firm* must calculate its interest rate *PRR* by:
  - (1) identifying which positions must be included within the *PRR* calculation;
  - (2) deriving the net position in each debt *security* in accordance with 37R - 41R;
  - (3) including these net positions in the *PRR* calculation for general market risk and the *PRR* calculation for specific risk; and
  - (4) summing all *PRRs* calculated for general market risk and specific risk.
- 2 G The interest rate *PRR* calculation divides the interest rate risk into the risk of loss from a general move in market interest rates, and the risk of loss from an individual debt *security's* price changing for reasons other than a general move in market interest rates. These are called general market risk and specific risk respectively.

#### Scope of the Interest rate PRR calculation

- 3 R A *firm's* interest rate *PRR* calculation must:
  - (1) include all *trading book* positions in debt *securities*, *preference securities* and *convertibles*, except:
    - (a) positions in *convertibles* which have been included in the *firm's PRR* calculation for *equities* under appendix 5;
    - (b) positions fully deducted as *material holdings*, in which case the *firm* may exclude them; or
    - (c) positions hedging an *option* which is being treated under 26R of appendix 9; and
  - (2) include notional positions arising from *trading book* positions in the instruments listed in table 4R.
- 4 R Table: Instruments which result in notional positions (see 3R(2))

Instrument	See
<i>Futures, forwards or synthetic futures on debt securities</i>	13R
<i>Futures, forwards or synthetic futures on debt indices or baskets</i>	14R
Interest rate <i>futures</i> or <i>forward rate agreements (FRAs)</i>	18R
Interest rate <i>swaps</i> or foreign exchange <i>swaps</i>	21R
Deferred start interest rate <i>swaps</i> or foreign exchange <i>swaps</i>	24R
The interest rate leg of an <i>equity swap</i> (unless the <i>firm</i> calculates a <i>PRR</i> on the instrument using the basic interest rate <i>PRR</i> calculation in appendix 5)	27R
The cash leg of a <i>repurchase agreement</i> or a <i>reverse repurchase agreement</i>	30R
Cash borrowings or deposits	31R
<i>Options</i> or <i>warrants</i> on a <i>debt security</i> , interest rate or interest rate <i>future</i> or <i>swap</i> , or on a <i>future</i> on a <i>debt security</i> (unless the <i>firm</i> calculates a <i>PRR</i> on the <i>option</i> under appendix 9)	32R
Dual currency bonds	33R
Foreign exchange <i>futures</i> or <i>forwards</i>	34R
Gold <i>futures</i> or <i>forwards</i>	34R
<i>Forwards, futures</i> or <i>options</i> (except <i>cliquets</i> ) on an <i>equity</i> , basket of <i>equities</i> or <i>equity</i> index (unless the <i>firm</i> calculates a <i>PRR</i> on the instrument using the basic interest rate <i>PRR</i> calculation in appendix 5)	34R
Credit derivatives	Appendix 63

- 5 G 3R(1) includes a *trading book* position in *debt security*, *preference security* or *convertible* that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the *security* had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the *security* would not have been included in the *PRR* calculation in the first place.
- 6 G 3R(1) includes net *underwriting* positions or reduced net *underwriting* positions in *debt securities*.
- 7 G *Firms* are reminded that table 5R in appendix 9 divides *options* and *warrants* on interest rates, *debt securities*, interest rate *futures* and *swaps* into:



- (1) those which must be treated under appendix 9; and
  - (2) those which must be treated under either appendix 4 or appendix 9, but *firms* can choose whether appendix 4 or 9 is used.
- 8 G Cliquets on *equities*, baskets of *equities* or *equity* indices do not attract an interest rate *PRR*. Table 4R excludes them from the scope of the interest rate *PRR* calculation in this appendix, and 45R of appendix 5 excludes them from the basic interest rate *PRR* calculation in that appendix.
- 9 G Table 4R shows that *equity derivatives* are excluded from this appendix's *PRR* calculation if they have been included in the basic interest rate *PRR* calculation in appendix 5 (see 45R of appendix 5).

#### Derivation of notional positions

##### GENERAL APPROACH

- 10 G This section converts the instruments listed in table 4R into notional positions in:
- (1) the underlying debt *security*, where the instrument depends on the price (or yield) of a specific debt *security*; and/or
  - (2) hypothetical debt *securities* to capture the pure interest rate risk arising from future payments and receipts of cash (including notional payments and receipts). Because they are designed to represent pure general market risk (and not specific risk) they are called *zero-specific-risk securities*.
- 11 R For the purposes of calculating *PRR*, unless specified otherwise, a *firm* must derive the value of notional positions as follows:
- (1) notional positions in actual debt *securities* must be valued as the nominal amount underlying the contract at the current market price of the debt *security*; and
  - (2) positions in *zero-specific-risk securities* must be valued using one of the two following methods. A *firm* must use the same method for all positions denominated in the same currency:
    - (a) Present value approach: The *zero-specific-risk security* is assigned a value equal to the present value of all the future cash flows that it represents.
    - (b) Alternative approach: The *zero-specific-risk security* is assigned a value equal to:
      - (i) the market value of the underlying notional *equity* position in the case of an *equity derivative*;
      - (ii) the notional principal amount in the case of an interest rate or foreign exchange *swap*; or

- (iii) the notional amount of the future cash flow that it represents in the case of any other instrument.

12 R A *firm* must use 11R(2)(a) in respect of any positions that it includes in the duration method calculation of general market risk (see 60R).

#### FUTURES OR FORWARDS ON A DEBT SECURITY

13 R *Futures* or *forwards* on a single debt *security* must be treated as follows:

(1) A purchased *future* or *forward* is treated as:

- (a) a notional long position in the underlying debt *security* (or the cheapest to deliver (taking into account the conversion factor) where the contract can be satisfied by delivery of one from a range of *securities*); and
- (b) a notional short position in a zero coupon *zero-specific-risk security* with a maturity equal to the expiry date of the *future* or *forward*.

(2) A sold *future* or *forward* is treated as:

- (a) a notional short position in the underlying *security* (or the cheapest to deliver (taking into account the conversion factor) where the contract can be satisfied by delivery of one from a range of *securities*); and
- (b) a notional long position in a zero coupon *zero-specific-risk security* with a maturity equal to the expiry date of the *future* or *forward*.

#### FUTURES OR FORWARDS ON A BASKET OR INDEX OF DEBT SECURITIES

14 R *Futures* or *forwards* on a basket or index of debt *securities* must be converted into *forwards* on single debt *securities* as follows (and then the resulting positions are treated under 13R).

(1) *Futures* or *forwards* on a single currency basket or index of debt *securities* must be treated as either:

- (a) a series of *forwards*, one for each of the constituent debt *securities* in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant debt *security* in the basket; or
- (b) a single *forward* on a hypothetical debt *security*.

(2) *Futures* or *forwards* on multiple currency baskets or indices of debt *securities* must be treated as either:

- (a) a series of *forwards* (using the method described in (1)(a)); or

- (b) a series of *forwards*, each one on a hypothetical debt *security* to represent one of the currencies in the basket or index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant currency in the basket.
- 15 G Under 14R(2)(b), a *forward* on basket of 3 Euro denominated debt *securities* and 2 Dollar denominated debt *securities* would be treated as a *forward* on a single hypothetical Euro denominated debt *security* and a *forward* on a single hypothetical Dollar denominated debt *security*.
- 16 R The hypothetical debt *securities* in 14R are assigned a specific risk *PRA* and a general market risk *PRA* equal to the highest that would apply to the debt *securities* in the basket or index.
- 17 G The debt *security* with the highest specific risk *PRA* within the basket might be a different debt *security* to that with the highest general market risk *PRA*. 16R requires a *firm* to select the highest percentages even where they relate to different debt *securities* in the basket or index, and regardless of the proportion of those debt *securities* in the basket or index.

INTEREST RATES FUTURES AND FORWARD RATE AGREEMENTS (FRAS)

- 18 R Interest rate *futures* or *FRAs* must be treated as the two notional positions (one long, one short) shown in table 19R.
- 19 R Table: Interest rate *futures* and *FRAs* (see 18R)

	1	2
	A short position in a zero coupon <i>zero-specific-risk-security</i>	A long position in a zero coupon <i>zero-specific-risk-security</i>
Where the <i>firm</i> buys an interest rate <i>future</i> or sells an <i>FRA</i>	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> )	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> ) plus the maturity of the borrowing/deposit
Where the <i>firm</i> sells an interest rate <i>future</i> or buys an <i>FRA</i>	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> ) plus the maturity of the borrowing/deposit	Maturity equals the expiry date of the <i>future</i> (or settlement date of the <i>FRA</i> )

- 20 G The following example illustrates 18R and 19R in conjunction with 11R (the latter rule determines the value of notional positions). A *firm* sells £1mn notional of a 3v6 *FRA* at 6%. This results in:
- (1) a short position in a *zero-specific-risk-security* with a zero coupon, three month maturity, and a nominal amount of £1mn; and

- (2) a long position in a *zero-specific-risk-security* with a zero coupon, six month maturity, and nominal amount of £1,015,000 (i.e. notional plus interest at 6% over 90 days).

If a *firm* were to apply the approach in 11R(2)(a), the two nominal amounts would have to be present valued.

INTEREST RATE SWAPS OR FOREIGN EXCHANGE SWAPS

- 21 R Interest rate *swaps* or foreign exchange *swaps* without deferred starts must be treated as the two notional positions (one long, one short) shown in table 22R:
- 22 R Table: Interest rate and foreign exchange *swaps* (see 21R)

	<b>1. Paying leg</b> A short position in a <i>zero-specific-risk security</i>	<b>2. Receiving leg</b> A long position in a <i>zero-specific-risk security</i>
Receiving fixed and paying floating	coupon equals the floating rate and maturity equals the reset date	Coupon equals the fixed rate of the <i>swap</i> and maturity equals the maturity of the <i>swap</i>
Paying fixed and receiving floating	coupon equals the fixed rate of the <i>swap</i> and maturity equals the maturity of the <i>swap</i>	Coupon equals the floating rate and maturity equals the reset date
Paying floating and receiving floating	coupon equals the floating rate and maturity equals the reset date	Coupon equals the floating rate and maturity equals the reset date

- 23 G For a foreign exchange *swap*, the two notional *zero-specific-risk securities* would be denominated in different currencies. A foreign exchange *swap* is also included in the foreign exchange *PRR* calculation.

DEFERRED START INTEREST RATE SWAPS OR FOREIGN EXCHANGE SWAPS

- 24 R Interest rate *swaps* or foreign exchange *swaps* with a deferred start must be treated as the two notional positions (one long, one short) shown in table 25R.

- 25 R Table: Deferred start interest rate and foreign exchange *swaps* (see 24R)

	1. Paying leg	2. Receiving leg
	A short position in a <i>zero-specific-risk security</i> with a coupon equal to the fixed rate of the <i>swap</i>	A long position in a <i>zero-specific-risk security</i> with a coupon equal to the fixed rate of the <i>swap</i>
Receiving fixed and paying floating	maturity equals the start date of the <i>swap</i>	maturity equals the maturity of the <i>swap</i>
Paying fixed and receiving floating	maturity equals the maturity of the <i>swap</i>	maturity equals the start date of the <i>swap</i>

- 26 G For example, a *firm* enters into a five year *swap* which starts in two year's time. The *firm* has contracted to receive 6% and pay six month Libor on a principal amount of £1mn. This results in a long position in a 7 year debt *security* and a short position in a 2 year debt *security*. Both have a coupon of 6%.

SWAPS WHERE ONLY ONE LEG IS AN INTEREST RATE LEG (E.G. EQUITY SWAPS)

- 27 R A *firm* must treat a *swap* with only one interest rate leg as a notional position in a *zero-specific-risk security*:
- (1) with a coupon equal to that on the interest rate leg;
  - (2) with a maturity equal to the date that the interest rate will be reset; and
  - (3) which is a long position if the *firm* is receiving interest payments and short if making interest payments.
- 28 G 27R includes *equity swaps*, *commodity swaps* and any other *swap* where only one leg is an interest rate leg.

CASH LEGS OF REPURCHASE AGREEMENTS AND REVERSE REPURCHASE AGREEMENTS

- 29 G *Firm's* are reminded that for the purposes of 30R, a *repurchase agreement* includes a sell/buy back or stock lending; and a *reverse repurchase agreement* includes a buy/sell back or a stock borrowing.
- 30 R The forward cash leg of a *repurchase agreement*, or *reverse repurchase agreement*, must be treated as a notional position in a *zero-specific-risk security* which:

- (1) is a short notional position in the case of a *repurchase agreement*; and a long notional position in the case of a *reverse repurchase agreement*;
- (2) has a value equal to the market value of the cash leg;
- (3) has a maturity equal to that of the *repurchase agreement* or *reverse repurchase agreement*; and
- (4) has a coupon equal to:
  - (a) zero, if the next interest payment date coincides with the maturity date; or
  - (b) the interest rate on the contract, if any interest is due to be paid before the maturity date.

#### CASH BORROWINGS AND DEPOSITS

- 31 R A cash borrowing or deposit must be treated as a notional position in a zero coupon *zero-specific-risk security* which:
- (1) is a short position in the case of a borrowing and a long position in the case of a deposit;
  - (2) has a value equal to the market value of the borrowing or deposit;
  - (3) has a maturity equal to that of the borrowing or deposit, or the next date the interest rate is reset (if earlier); and
  - (4) has a coupon equal to:
    - (a) zero, if the next interest payment date coincides with the maturity date; or
    - (b) the interest rate on the borrowing or deposit, if any interest is due to be paid before the maturity date.

#### OPTIONS AND WARRANTS

- 32 R Where included in this appendix's *PRR* calculation (see table 4R), *options* and *warrants* must be treated as follows:
- (1) An *option* or *warrant* on a debt *security* must be treated as a position in that debt *security*.
  - (2) An *option* on an interest rate must be treated as a position in a zero coupon *zero-specific-risk security* with a maturity equal to the sum of the time to expiry of the *option* and the length of the period for which the interest rate is fixed.
  - (3) An *option* on an *future* – where the *future* is based on an interest rate or debt *security* – must be treated as:

- (a) a long position in that *future* for purchased call *options* and written put *options*; and
  - (b) a short position in that *future* for purchased put *options* and written call *options*.
- (4) An *option* on a *swap* must be treated as a deferred starting *swap*.

BONDS WHERE THE COUPONS AND PRINCIPAL ARE PAID IN DIFFERENT CURRENCIES

- 33 R Where a debt *security* pays coupons in one currency, but will be redeemed in a different currency, it must be treated as:
- (1) a debt *security* denominated in the coupon's currency; and
  - (2) a foreign exchange *forward* to capture the fact that the debt *security's* principal will be repaid in a different currency from that in which it pays coupons, specifically:
    - (a) a notional forward sale of the coupon currency and purchase of the redemption currency, in the case of a long position in the debt *security*; or
    - (b) a notional forward purchase of the coupon currency and sale of the redemption currency, in the case of a short position in the debt *security*.

INTEREST RATE RISK ON OTHER FUTURES, FORWARDS AND OPTIONS

- 34 R Other *futures, forwards, options* and *swaps* must be treated as positions in *zero-specific-risk securities*, each of which:
- (1) has a zero coupon;
  - (2) has a maturity equal to that of the relevant contract; and
  - (3) is long or short according to table 35R.

- 35 R Table: Interest rate risk on other *futures, forwards, options* and *swaps* (see 34R).

Instrument	Notional positions		
Foreign exchange <i>forward</i> or <i>future</i>	a long position denominated in the currency purchased	<b>and</b>	a short position denominated in the currency sold
Gold <i>forward</i> or <i>future</i>	a long position if the <i>forward</i> or <i>future</i> involves an actual (or notional) sale of gold	<b>or</b>	a short position if the <i>forward</i> or <i>future</i> involves an actual (or notional) purchase of gold
<i>Equity forward</i> or <i>future</i> , or <i>option</i> (unless a <i>PRR</i> is calculated under the basic interest rate calculation in appendix 5)	A long position if the contract involves an actual (or notional) sale of the underlying <i>equity</i>	<b>or</b>	A short position if the contract involves an actual (or notional) purchase of the underlying <i>equity</i>

Deriving the net position in each debt security

- 36 G The net position is the difference between the value of the *firm*'s long positions (including notional positions) and the value of its short positions (including notional positions) in the same debt *security*.

#### NETTING POSITIONS IN THE SAME DEBT SECURITY

- 37 R A *firm* must not net positions (including notional positions) unless:
- (1) Long and short positions are in the same debt *security*, and a debt *security* is the same as another if and only if:
    - (a) they enjoy the same rights in all respects; and
    - (b) are fungible with each other;
  - (2) Long and short positions are in different tranches of the same debt *security*, where the tranches:
    - (a) enjoy the same rights in all respects; and
    - (b) become fungible within 180 days, and thereafter the debt *security* of one tranche can be delivered in settlement of the other tranche.



NETTING THE CHEAPEST TO DELIVER SECURITY WITH OTHER DELIVERABLE SECURITIES

- 38 R A *firm* may net a short notional position in the cheapest to deliver *security* arising from a short *future* or *forward* (see 13R(2)(a)) against a long position in any deliverable *security* up to a maximum of 90% of the common nominal amounts. The residual long and short nominal amounts must be treated as separate long and short positions.
- 39 G The netting permitted by 38R only relates to where the *firm* has sold the *future* or *forward*. It does not relate to where the *firm* has bought a *future* or *forward*.

NETTING ZERO-SPECIFIC-RISK SECURITIES WITH DIFFERENT MATURITIES

- 40 R A *firm* may net a notional long position in a *zero-specific-risk security* against a notional short position in a *zero-specific-risk security* if:
- (1) they are denominated in the same currency;
  - (2) their coupons do not differ by more than 15 basis points; and
  - (3) they mature:
    - (a) on the same day, if they have residual maturities of less than one month;
    - (b) within seven days of each other, if they have residual maturities of between one month to one year; and
    - (c) within thirty days of each other, if they have residual maturities in excess of one year.

REDUCED NET UNDERWRITING POSITIONS IN DEBT SECURITIES

- 41 R A *firm* must not net a reduced net *underwriting* position in a debt *security* with any other debt *security* position.
- 42 G 41R only relates to reduced net *underwriting* positions.

Specific risk calculation

- 43 R A *firm* must calculate the specific risk *PRR* for each debt *security* by:
- (1) multiplying the market value of the individual net position (ignoring the sign) by the appropriate *PRA* from table 44R; and
  - (2) converting this amount into the *firm's base currency* at prevailing spot foreign exchange rates.

44 R Table: specific risk *PRAs* (see 43R).

<b>Issuer</b>	<b>Residual maturity</b>	<b><i>PRA</i></b>
An issue of, or fully guaranteed by, or fully collateralised by a <i>Zone A</i> central government or central bank or the European Communities	Any	0%
An issue of, or fully guaranteed by, a <i>Zone B</i> central government or central bank denominated in the local currency	Zero to 12 months	0%
Other <i>qualifying debt securities</i> (see 46R)	Zero to 6 months	0.25%
	6 to 24 months	1%
	Over 24 months	1.6%
<i>Non-qualifying debt securities</i>	Any	8%

45 G 43R includes both actual and notional positions. However, notional positions in *zero-specific-risk securities* do not attract specific risk. For example:

- (1) Interest rate *swaps*, foreign exchange *swaps*, *FRAs*, interest rate *futures*, foreign exchange *forwards*, foreign exchange *futures*, and the cash leg of *repurchase agreements* and *reverse repurchase agreements* create notional positions which will not attract specific risk; whilst
- (2) *Futures*, *forwards* and *swaps* which are based on the price (or yield) of one or more debt *securities* will create at least one notional position that attracts specific risk.

#### DEFINITION OF A QUALIFYING DEBT SECURITY

46 R A debt *security* is a *qualifying debt security* if:

- (1) it attracts zero specific risk under table 44R; or
- (2) it is issued by, or fully guaranteed by:
  - (a) a *Zone B* central government or central bank and the *security* is denominated in the local currency of the issuer;
  - (b) a *multilateral development bank*;

- (c) a *Zone A* public sector entity;
  - (d) a company whose *equity* is a constituent of one of the indices making up the FTSE All-World Index; or
  - (e) an issue of, or fully guaranteed by an *investment firm* or *recognised third-country investment firm*.
- (3) it is issued by, fully guaranteed by, endorsed or accepted by:
- (a) a *credit institution* incorporated in a *Zone A* country; or
  - (b) a *credit institution* incorporated in a *Zone B* country and the debt *security* has a residual maturity of one year or less.
- (4) it is a mortgage backed *security* which meets the criteria in 7e of section 3.2.5 of chapter BC of IPRU(Bank).
- (5) it is rated by at least one of the agencies shown in table 47R, and every such rating equals or exceeds the corresponding minimum shown in that table.

47 R Table: minimum ratings for *qualifying debt securities* (see 46R(5)).

Issuer	Rating agency	Minimum Rating	
		<i>Securities</i>	Money Market Obligations
Any	Moody's Investors Service	Baa3	P3
	Standard & Poor's Corporation	BBB-	A3
	FITCH Ratings Ltd	BBB-	F-3
Canadian	Canadian Bond Rating Service	B++low	A-3
	Dominion Bond Rating Service	BBB low	R-2
Japanese	Japan Credit Rating Agency, Ltd	BBB-	J-2
	Mikuno & Co	BBB	M-3
	Japan Rating & Investment Information Inc	BBB-	a-2

General market risk calculation

48 R A *firm* must calculate the general market risk *PRR* for each currency using either:

- (1) the simplified maturity method;
- (2) the maturity method; or

- (3) the duration method (subject to 50R).
- 49 R A *firm* must convert all general market risk *PRRs* into its *base currency* using prevailing foreign exchange spot rates.
- 50 R A *firm* must not use the duration method for index-linked *securities*. Instead, these *securities* must:
- (1) be attributed a coupon of 3%; and
  - (2) treated separately under either the simplified maturity method or the maturity method.

#### SIMPLIFIED MATURITY METHOD

- 51 G The simplified maturity method weights individual net positions to reflect their price sensitivity to changes in interest rates. The weights are related to the coupon and the residual maturity of the instrument (or the next interest rate re-fix date for floating rate items).
- 52 R Under the simplified maturity method, the *PRR* for general market risk equals the sum of each individual net position (long or short) multiplied by the appropriate *PRA* in table 53R.
- 53 R Table: general market risk *PRAs* (see 52R).

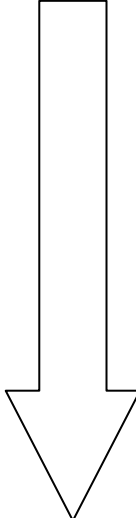
Zone	Maturity band		<i>PRA</i>
	Coupon of 3% or more	Coupon of less than 3%	
One	$0 \leq 1$ month	$0 \leq 1$ month	0.00%
	$> 1 \leq 3$ months	$> 1 \leq 3$ months	0.20%
	$> 3 \leq 6$ months	$> 3 \leq 6$ months	0.40%
	$> 6 \leq 12$ months	$> 6 \leq 12$ months	0.70%
Two	$> 1 \leq 2$ years	$> 1.0 \leq 1.9$ years	1.25%
	$> 2 \leq 3$ years	$> 1.9 \leq 2.8$ years	1.75%
	$> 3 \leq 4$ years	$> 2.8 \leq 3.6$ years	2.25%
Three	$> 4 \leq 5$ years	$> 3.6 \leq 4.3$ years	2.75%
	$> 5 \leq 7$ years	$> 4.3 \leq 5.7$ years	3.25%
	$> 7 \leq 10$ years	$> 5.7 \leq 7.3$ years	3.75%
	$> 10 \leq 15$ years	$> 7.3 \leq 9.3$ years	4.50%
	$> 15 \leq 20$ years	$> 9.3 \leq 10.6$ years	5.25%
	$> 20$ years	$> 10.6 \leq 12.0$ years	6.00%
		$> 12.0 \leq 20.0$ years	8.00%
		$> 20$ years	12.50%

## THE MATURITY METHOD

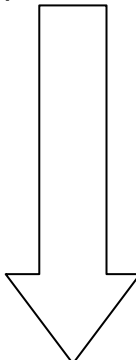
- 54 G The maturity method builds on the simplified maturity method by partially recognising offsetting positions. 57G provides an illustration of the maturity method.
- 55 R Under the maturity method, the *PRR* for general market risk is calculated as follows:
- (1) Step 1: each net position is allocated to the appropriate maturity band in table 53R and multiplied by the corresponding *PRA*.
  - (2) Step 2: weighted long and short positions are matched within:
    - (a) the same maturity band;
    - (b) the same zone (using unmatched positions from (a)); and
    - (c) different zones (using unmatched positions from (b)).
  - (3) Step 3: the *PRR* for general market risk is the sum of:
    - (a) 10% of the total amount matched within maturity bands;
    - (b) 40% of the amount matched within zone 1 under (2)(b);
    - (c) 30% of the amount matched within zones 2 & 3 under (2)(b);
    - (d) 40% of the amounts matched between zones 1 and 2, and between zones 2 and 3;
    - (e) 150% of the amount matched between zones 1 and 3; and
    - (f) 100% of the weighted positions remaining unmatched after (2)(c);
- 56 G Table 53R distinguishes between debt *securities* with a coupon of less than 3% and those with coupon in excess of 3%. However, this doesn't mean that the *firm* has to do a separate general market risk calculation for each, it merely ensures that when allocating debt *securities* to a particular band, their coupons are taken into account as well as their maturities. So for example, a 21 year 6% debt *security* falls into the same band as an 11 year 2% debt *security*. They are both weighted at 6%, and can be matched under the first part of step two because they fall within the same band.

57 G An example of the maturity method calculation. In this example, a *firm* with a £ sterling *base currency* is processing its euro denominated positions.

Weight each position



Match weighted positions



Calculate the general market risk

Zone	Totals of:		PRA		Weighted longs within each band	Weighted shorts within each band
	net longs within the band	net shorts within the band				
1	€100	€50	0.00%		0	0
	€250	€0	0.20%		<b>0.50</b>	0
	€200	€0	0.40%		<b>0.80</b>	0
	€0	€0	0.70%		0	0
2	€140	€0	1.25%		<b>1.75</b>	0
	€200	€300	1.75%		<b>3.50</b>	<b>5.25</b>
	€0	€400	2.25%		0	<b>9</b>
3	€0	€0	2.75%		0	0
	€200	€200	3.25%		<b>6.50</b>	<b>6.50</b>
	€300	€0	3.75%		<b>11.25</b>	0
	€200	€300	4.50%		<b>9</b>	<b>13.50</b>
	€0	€14.30	5.25%		0	<b>0.75</b>
	€300	€0	6.00%		<b>18.00</b>	0
	€0	€0	8.00%		0	0
€0	€0	12.50%		0	0	

same band		same zones		different zones	
Long	Short	Long	Short	Long	Short
0.50		0.50		1.30	
0.80		0.80			
		1.75	↔ 1.75		
1.75					9.00
<b>3.50</b>	↔ <b>5.25</b>				
	9		9		
<b>6.50</b>	↔ <b>6.50</b>				
11.25		11.25	↔ 4.50	24.00	
<b>9</b>	↔ <b>13.50</b>				
	0.75		↔ 0.75		
18.00		18.00			
<b>19 matched</b>		<b>7 matched</b>		<b>9 matched</b>	

Matched within bands	19	@	10%	=	1.9
Matched within zone 1	0	@	40%	=	0
Matched within zones 2&3	7	@	30%	=	2.1
Matched between zones 1&2 and 2&3	9	@	40%	=	3.6
Matched between zones 1&3	0	@	150%	=	0
Unmatched after 2(c)	16.30	@	100%	=	16.30
<b>total = € 23.90</b>					
<b>general market risk PRR (if €1=£0.60) = £14.34</b>					

## DURATION METHOD

- 58 G The duration method produces a more accurate measure of interest rate risk than the maturity methods but it is also more complex to calculate.
- 59 R *Firms* must use the following formula to calculate modified duration:

$$\text{Modified Duration} = \frac{D}{(1+r)} \qquad D = \frac{\sum_{t=1}^m \frac{tC_t}{(1+r)^t}}{\sum_{t=1}^m \frac{C_t}{(1+r)^t}}$$

Where:  $C_t$  = cash payment at time  $t$   
 $m$  = total maturity

$r$  = yield to maturity, based on the current mark to market of the debt *security*. In the case of a floating rate instrument, this is calculated on the assumption that the principal is due on the date that the interest rate can next be changed

$t$  = time

- 60 R Under the duration method, the *PRR* for general market risk is calculated as follows:
- (1) Step 1: allocate each net position to the appropriate duration zone in table 61R and multiply it by:
    - (a) its modified duration (using the formula in 59R); and
    - (b) the appropriate assumed interest rate change in table 61R.
  - (2) Step 2: match weighted long and short positions:
    - (a) within zones; and
    - (b) across zones (using unmatched positions from (2)(a)); and
  - (3) Step 3: calculate the general market risk as the sum of:
    - (a) 100% of the weighted positions remaining unmatched after (2)(b);
    - (b) 2% of the matched weighted position in each zone;
    - (c) 40% of the matched weighted position between zones 1 and 2, and between zones 2 and 3; and
    - (d) 150% of the matched weighted position between zones 1 and 3.

61 R Table: Assumed interest rate change in the duration method (see 60R).

Zone	Modified Duration	Assumed interest rate change (percentage points)
1	$0 \leq 12$ months	1.00
2	$> 12$ months $\leq 3.6$ years	0.85
3	$> 3.6$ years	0.70



## Appendix 5

### Equity PRR

#### General rule

- 1 R A *firm* must calculate its *equity PRR* by:
- (1) identifying which *equity* positions must be included within the scope of the *PRR* calculation (see 2R);
  - (2) deriving the net position in each *equity* in accordance with 23R;
  - (3) including each of those net positions in either the simplified equity method (see 29R) or, subject to 27R, the standard equity method (see 32R); and
  - (4) summing the *PRR* on each net position as calculated under the simplified and standard equity methods.

#### Scope of the Equity PRR calculation

- 2 R A *firm's equity PRR* calculation must:
- (1) Include all *trading book* positions in *equities*, unless:
    - (a) the position is fully deducted as a *material holding*, in which case the *firm* may exclude it;
    - (b) the position is hedging an *option* or *warrant* which is being treated under 26R of appendix 9; and
  - (2) include notional positions arising from *trading book* positions in the instruments listed in table 3R.
- 3 R Table: Instruments which result in notional positions (see 2R(2))

Instrument	See
Depository receipts	12R
<i>Convertibles</i> where: (a) the <i>convertible</i> is trading at a market price of less than 110% of the underlying <i>equity</i> ; and the first date at which conversion can take place is less than three months ahead, or the next such date (where the first has passed) is less than a year ahead; or (b) the conditions in (a) are not met but the <i>firm</i> includes the <i>convertible</i> in its <i>equity PRR</i> calculation rather than including it in its interest rate <i>PRR</i>	13R

	calculation set out in appendix 4.	
	<i>Futures, forwards, CFDs and synthetic futures on a single equity</i>	14R
	<i>Futures, forwards, CFDs and synthetic futures on a basket of equities or equity index</i>	15R
	<i>Equity legs of an equity swap</i>	19R
	<i>Options or warrants on a single equity, an equity future, a basket of equities or an equity index (unless the firm calculates a PRR on the option or warrant under appendix 9).</i>	21R

- 4 G 2R(1) includes a *trading book* position in an *equity* that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the *equity* had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the *equity* would not have been included in the *trading book* in the first place.
- 5 G 2R(1) includes net *underwriting* positions, or reduced net *underwriting* positions in *equities*. 27R requires *firms* to use the simplified equity method in the case of reduced net *underwriting* positions. In the case of net *underwriting* positions that haven't been reduced according to 24R of appendix 7, there is no such restriction; a *firm* can choose which of the two equity methods to use.
- 6 G *Firms* are reminded that table 5R in appendix 9 divides *equity options* and *warrants* into:
- (1) those which must be treated under appendix 9; and
  - (2) those which must be treated under either appendix 5 or appendix 9, but *firms* can choose whether appendix 5 or 9 is used.
- 7 G Table 3R doesn't require every *convertible* to be included in this appendix's *PRR* calculation. Where a *convertible* is not included in this appendix's *PRR* calculation, 3R(1)(a) of appendix 4 requires that it is included in the appendix 4 *PRR* calculation.
- 8 G Some of the instruments listed in table 3R are also included in a *firm's* interest rate *PRR* calculation. For simplicity, a *firm* may use the interest rate *PRR* calculation at the end of this appendix rather than the calculation in appendix 4. 44G explains this in more detail.

## Derivation of notional positions

- 9 G This section converts the instruments listed in table 3R into notional positions in individual *equities*, *equity* baskets or *equity* indices.

### GENERAL RULE

- 10 R Unless specified otherwise, the value of each notional *equity* position equals the quantity of that *equity* underlying the instrument multiplied by the current market value of the *equity*.
- 11 G For example, the current market value of a particular *equity* is £2.50. If a *firm* contracts to sell this *equity* in five year's time for £3 it would treat the notional short *equity* position as having a value of £2.50 when calculating the *equity PRR*.

In effect, the forward position has been treated as being equivalent to a spot position for the purposes of calculating *equity PRR*. To capture the risk that the forward price changes relative to the spot price, forward *equity* positions are included in the *firm's* interest rate *PRR* calculation (see 45R of this appendix or table 4R of appendix 4).

### DEPOSITORY RECEIPTS

- 12 R A depository receipt must be treated as a notional position in the underlying *equity*.

### CONVERTIBLES

- 13 R Where a *convertible* is included in this appendix's *PRR* calculation (see table 3R):
- (1) it must be treated as a position in the *equity* into which it converts; and
  - (2) the *firm's equity PRR* must be adjusted by making:
    - (a) an addition equal to the current value of any loss which the *firm* would make if it did convert to *equity*; or
    - (b) a deduction equal to the current value of any profit which the *firm* would make if it did convert to *equity* (subject to a maximum deduction equal to the *PRR* on the notional position underlying the *convertible*).

### FUTURES, FORWARDS AND CFDS ON A SINGLE EQUITY

- 14 R A *future*, *forward* or *CFD* on a single *equity* must be treated as a notional position in that *equity*.

### FUTURES, FORWARDS AND CFDS ON EQUITY INDICES OR BASKETS

- 15 R A *future*, *forward* or *CFD* on an *equity* index or basket must be treated as either:
- (1) a position in each of the underlying *equities*; or
  - (2) the positions shown in table 16R.

16 R Table: *equity* index or basket contracts (see 15R(2))

	Under the simplified equity method (29R)	Under the standard equity method (32R)
Only one country in the index or basket (see 32R)	One position in the index or basket	One position in the index or basket
More than one country in the index or basket	One position in the index or basket	Several notional basket positions, one for each country Or One notional basket position in a separate, hypothetical country

17 G For example, a *firm* decides to treat a FTSE Eurotop 300 *future* under the standard equity method, and furthermore, chooses to treat it as one notional position. Table 16R requires that this notional position must be treated as if it were from a separate hypothetical “country” rather than any of the countries to which the underlying *equities* are from.

18 R The notional positions created under 15R have the following values:

- (1) where only one notional position is created, it has a value equal to the total market value of the *equities* underlying the contract; or
- (2) where more than one notional position is created, each one has a value which reflects the relevant *equity's* or country's contribution to total market value of the *equities* underlying the contract.

#### EQUITY LEGS OF EQUITY SWAPS

19 R The *equity* leg of an *equity swap* must be treated as a position in the underlying *equity*, *equity* basket or *equity* index, which is:

- (1) long, if the *firm* has contracted to receive any increase and pay any decrease in the value of the underlying *equities* or *equity* index; and
- (2) short, if the *firm* has contracted to receive any decrease and pay any increase in the value of the underlying *equities* or *equity* index.

20 G The interest rate leg of an *equity swap* is included in a *firm's* interest rate *PRR* calculation (see table 4R of appendix 4).

#### OPTIONS

- 21 R If included in this appendix's *PRR* calculation (see table 3R), *options* must be treated as follows:
- (1) an *option* on a single *equity* must be treated as a notional position in that *equity*;
  - (2) an *option* on a basket of *equities* or *equity* index must be treated as a *future* on that basket or index; and
  - (3) an *option* on an *equity future* must be treated as:
    - (a) a long position in that *future*, for purchased *call options* and written *put options*; and
    - (b) a short position in that *future*, for purchased *put options* and written *call options*.

#### Deriving the net position in each equity

- 22 G The net position is the difference between the value of the *firm*'s long positions (including notional positions) and the value of its short positions (including notional positions) in the same *equity*.
- 23 R When deriving the net position in each *equity*, a *firm* must not net long and short positions unless:
- (1) they are positions in the same *equity*. Two *equities* are the same if:
    - (a) they enjoy the same rights in all respects; and
    - (b) are fungible with each other; or
  - (2) they are positions in different tranches of the same *equity* and the tranches:
    - (a) enjoy the same rights in all respects; and
    - (b) become fungible for each other within 180 days, and thereafter the *equity* of one tranche can be delivered in settlement of the other tranche.
- 24 R A *firm* must not net a reduced net *underwriting* position with any other *equity* position.
- 25 G 24R only relates to reduced net *underwriting* positions.

#### Simplified and standard equity methods

- 26 G 1R(3) requires that the net position in each *equity* is included in either the simplified equity method or the standard equity method, though indicates that this choice is subject to the restriction in 27R. A *firm* does not have to use the same method for all *equities*.
- 27 R A *firm* must use the simplified equity method for reduced net *underwriting* positions.

- 28 G A *firm* may use either method for a net *underwriting* position; 27R only relates to reduced net *underwriting* positions.

SIMPLIFIED EQUITY METHOD

- 29 R Under the simplified method, the *PRR* for each *equity*, *equity* index, or *equity* basket equals the market value of the net position (ignoring the sign) multiplied by the appropriate *PRA* from table 30R. The result must be converted into the *firm's* base currency at current spot foreign exchange rates.
- 30 R Table: simplified equity method *PRAs* (see 29R)

	PRA
Single <i>equities</i>	12%
<i>Qualifying equity indices</i> (see 38R)	8%
All other <i>equity</i> indices or baskets	12%

STANDARD EQUITY METHOD

- 31 G The standard equity method divides the risk of loss from a *firm's* *equity* positions into the risk of loss from a general move in that country's *equity* market and the risk of loss from an individual *equity's* price changing relative to that country's *equity* market. These are called general market risk and specific risk respectively.
- 32 R Under the standard equity method, a *firm* must:
- (1) Group *equity* positions into country portfolios as follows:
    - (a) A position in an individual *equity* belongs to:
      - (i) the country it is listed in;
      - (ii) any of the countries it is listed in, if more than one; or
      - (iii) the country it was issued from, if unlisted.
    - (b) A position in *equity* basket or index that is treated under 15R(2), is allocated to one or more country portfolios based on the countries to which the underlying *equities* belong to under (a) above.
  - (2) Sum:
    - (a) the *PRRs* for specific risk calculated under 33R; and
    - (b) the *PRRs* for general market risk for each country portfolio as calculated under 41R and 42R.

STANDARD EQUITY METHOD: SPECIFIC RISK

- 33 R Under the standard equity method, a *firm* must calculate a *PRR* for specific risk based on the net position in each *equity*, *equity* index or *equity* basket by:
- (1) multiplying its market value (ignoring the sign) by the appropriate *PRA* from table 34R; and
  - (2) converting it into the *firm's base currency* using current spot foreign exchange rates.

- 34 R Table: *PRAs* for specific risk under the standard approach (see 33R(1))

	<b>PRA</b>
<i>Qualifying equities</i> (see 35R)	2%
<i>Qualifying equity indices</i> (see 38R)	0%
All other <i>equities</i> , <i>equity</i> indices or <i>equity</i> baskets	4%

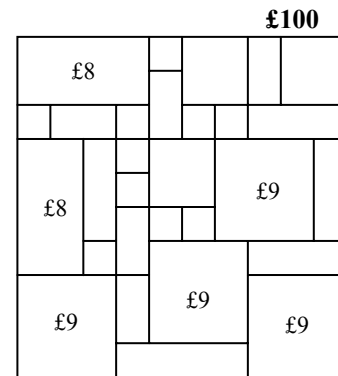
- 35 R For the purposes of table 34R, a *qualifying equity* is one which:
- (1) belongs to a country portfolio where:
    - (a) no individual position exceeds 10% of the portfolio's gross value; and
    - (b) the sum of positions (ignoring the sign) which individually represent between 5% and 10% of the portfolio's gross value, does not exceed 50% of the portfolio's gross value; and
  - (2) is a constituent of an index in table 39R.

- 36 G The following example illustrates 35R(1). A country portfolio has a gross value of £100 and is made up of positions in 29 different *equities* (some are long positions, others are short positions). Not all the *equities* are constituents of an index used to create the FT All-World Index (this criterion only becomes relevant once a *firm* has determined whether the country portfolio meets the test in 35R(1)).

Six positions exceed the 5% threshold. The diagram below shows the composition of the portfolio.

Part (a): the portfolio meets the first part of the test because no individual position is worth more than 10% of the portfolio's value.

Part (b): the portfolio fails the second part of the test because the sum (ignoring the sign) of the six relevant positions is £52; this exceeds 50% of the portfolio's value.

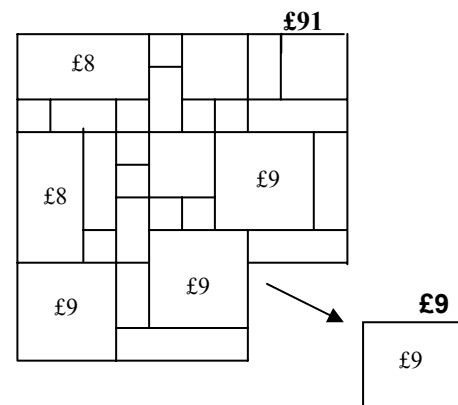


- 37 G A country portfolio can be split into two sub-portfolios if this enables one sub-portfolio to meet the requirements in 35R. Individual positions may be sub-divided between sub-portfolios.

Continuing the example above, one of the largest positions is taken out of the portfolio and put into a new portfolio. The new portfolio fails the two tests, but the amended portfolio meets both tests:

Part (a): no single remaining position exceeds £9.10.

Part (b): the sum of the five relevant positions is £43, this is less than 50% of the new portfolio's value of £91.



- 38 R A *qualifying equity index* is one which:

- (1) is listed in table 39R; or
- (2) is not listed in table 39R, but is constructed such that:
  - (a) it contains at least 20 *equities*;
  - (b) no single *equity* represents more than 20% of the total index; and
  - (c) no five *equities* combined represent more than 60% of the total index.



39 R Table: *Qualifying equity indices* (see 38R)

Qualifying equity indices	
Australia	All Ordinaries
Austria	Austrian Traded Index
Belgium	BEL 20
Canada	TSE 35, TSE 100, TSE 300
France	CAC 40, SBF 250
Germany	DAX
European	Dow Jones Stoxx 50 Index, FTSE Eurotop 300, MSCI Euro Index
Hong Kong	Hang Seng 33
Italy	MIB 30
Japan	Nikkei 225, Nikkei 300, TOPIX
Korea	Kospi
Netherlands	AEX
Singapore	Straits Times Index
Spain	IBEX 35
Sweden	OMX
Switzerland	SMI
UK	FTSE 100, FTSE Mid 250, FTSE All Share
US	S&P 500, Dow Jones Industrial Average, NASDAQ Composite, Russell 2000

#### STANDARD EQUITY METHOD: GENERAL MARKET RISK

40 R Under the standard equity method, a *firm* must apply approach one to each country portfolio (or part portfolio) unless the conditions in 42R are met, in which case the *firm* may instead apply approach two to the relevant country portfolios (or part portfolios).

#### APPROACH ONE: NO OFFSET BETWEEN DIFFERENT COUNTRY PORTFOLIOS

41 R Under approach one, the *PRR* for general market risk equals the net value (ignoring the sign) of the country portfolio multiplied by 8%. It must be converted into the *firm's base currency* using current spot foreign exchange rates.

#### APPROACH TWO: LIMITED OFFSET BETWEEN DIFFERENT COUNTRY PORTFOLIOS

42 R Under approach two, the *PRR* for general market risk is calculated using the following formula:

$$\sqrt{(8\% * CP_1)^2 + (8\% * CP_2)^2 + (8\% * CP_3)^2 + \dots + (8\% * CP_n)^2}$$

where  $CP_i$  denotes the net value of *i*th country portfolio (converted to the *firm's base currency* using current spot foreign exchange rates), and:

- (1) at least four country portfolios are included (that is:  $n \geq 4$ );
- (2) only country portfolios for countries which are full members of the *OECD*, Hong Kong or Singapore are included;
- (3) no individual country portfolio comprises more than 30% of the total gross value of country portfolios included; and
- (4) the total net value of country portfolios included equals zero, that is:

$$\sum_1^n CP_i = 0$$

- 43 G In order to meet 42R(4), it is likely that part of a country portfolio will have to be excluded from approach two (and therefore included in approach one), even if that country portfolio meets (1) to (3).

#### Basic interest rate PRR calculation for equity instruments

- 44 G A basic *PRR* calculation is included in this appendix for those *firms* that do not wish to use the calculation in appendix 4. However, it tends to result in higher charges than the methods in appendix 4, largely because the interest rate *PRR* is calculated on each notional equity position separately and then summed without offsetting long and short positions.
- 45 R Where a *firm* does not include a *forward*, *future*, or *option* (except cliquets) or *swap* on an *equity*, basket of *equities* or *equity* index in its appendix 4 *PRR* calculation, it must calculate an interest rate *PRR* as follows:
- (1) multiplying the market value of the notional *equity* position underlying the instrument by the appropriate percentage from table 47R; and
  - (2) summing the results from (1), ignoring the sign.
- 46 G Cliquets on *equities*, baskets of *equities* or *equity* indices do not attract an interest rate *PRR*. 45R excludes them from the basic interest rate *PRR* calculation and table 4R excludes them from the scope of the interest rate *PRR* calculation in appendix 4.

- 47 R Table: Percentages used in the basic interest rate *PRR* calculation for *equity* instruments (see 45R(1)).

<b>Time to expiration</b>	<b>Percentage</b>
$0 \leq 3$ months	0.20
$> 3 \leq 6$ months	0.40
$> 6 \leq 12$ months	0.70
$> 1 \leq 2$ years	1.25
$> 2 \leq 3$ years	1.75
$> 3 \leq 4$ years	2.25
$> 4 \leq 5$ years	2.75
$> 5 \leq 7$ years	3.25
$> 7 \leq 10$ years	3.75
$> 10 \leq 15$ years	4.50
$> 15 \leq 20$ years	5.25
$> 20$ years	6.00

## Appendix 6

### Commodity PRR

#### General rule

- 1 R A *firm* must calculate its *commodity PRR* by:
- (1) identifying which *commodity* positions must be included within the scope of the *PRR* calculation (see 2R);
  - (2) calculating an individual *PRR* for each *commodity* (see 20R);
  - (3) converting each *PRR* to the *firm's base currency* at current spot foreign exchange rates; and
  - (4) summing the resulting individual *PRRs*.

#### Scope of the commodity PRR calculation

- 2 R A *firm's commodity PRR* calculation must, regardless of whether the positions concerned are *trading book* or *non-trading book* positions:
- (1) include *physical commodity* positions;
  - (2) include notional positions arising from positions in the instruments listed in table 4R; and
  - (3) exclude positions constituting a *stock financing* transaction.
- 3 G Gold positions are excluded from the scope of the *commodity PRR*. Instead, they are included within the scope of the foreign exchange *PRR* (Appendix 8).
- 4 R Table: Instruments which result in notional positions (see 2R(3))

<i>Forwards, futures, CFDs, synthetic futures and options</i> on a single <i>commodity</i> (unless the <i>firm</i> calculates an <i>PRR</i> on the <i>option</i> under appendix 9)	8R
A commitment to buy or sell a single <i>commodity</i> at an average of spot prices prevailing over some future period	10R
<i>Forwards, futures, CFDs, synthetic futures and options</i> on a <i>commodity index</i> (unless the <i>firm</i> calculates an <i>PRR</i> on the <i>option</i> under appendix 9)	13R – 14R
<i>Commodity swaps</i>	16R – 17R

- 5 G 2R includes a *trading book* position in an *commodity* that is subsequently repo'd under a *repurchase agreement* or lent under a stock lending agreement. Clearly, if the *commodity* had initially been obtained via a *reverse repurchase agreement* or stock borrowing agreement, the *commodity* would not have been included in the *trading book* in the first place.
- 6 G *Firms* are reminded that table 5R in appendix 9 divides *commodity options* into:
- (1) those which must be treated under appendix 9; and
  - (2) those which must be treated under either appendix 6 or appendix 9, but *firms* can choose whether appendix 6 or 9 is used.

#### Derivation of notional positions

- 7 G This section converts the instruments listed in table 4R into notional positions in the relevant *commodities*. These notional positions are expressed in terms of quantity (tonnes, barrels, etc), not value. The maturity of the position is only relevant where the *firm* is using the maturity ladder approach or the modified maturity ladder approach.

#### Futures, forwards, CFDs and options on a single commodity

- 8 R Where a *forward, future, CFD, synthetic future* or *option* (unless already included in the *firm's option PRR* calculation) settles according to:
- (1) the difference between the price set on trade date and that prevailing at contract expiry, the notional position:
    - (a) equals the total quantity underlying the contract; and
    - (b) has a maturity equal to the expiry date of the contract
  - (2) the difference between the price set on trade date and the average of prices prevailing over a certain period up to contract expiry, there is a notional position for each of the reference dates used in the averaging period to calculate the average price, which:
    - (a) equals a fractional share of the total quantity underlying the contract; and
    - (b) has a maturity equal to the relevant reference date.
- 9 G The following example illustrates 8R(2). A *firm* buys a Traded Average Price Option (TAPO - a type of Asian option) allowing it to deliver 100 tonnes of Grade A copper and receive \$1,750 in June. If there were twenty *business days* in June the short notional positions will each:
- (1) equal 5 tonnes per day (1/20 of 100 tonnes); and
  - (2) have a maturity equal to one of the *business days* in June (one for each day).

In this example as each *business day* in June goes by the quantity per day for the remaining days does not change (5 tonnes per day) only the days remaining changes. Therefore, halfway through June there are 10, 5 tonne short notional positions remaining each for the ten remaining *business days* in June.

Buying or selling a single commodity at an average of spot prices prevailing in the future

- 10 R Commitments to buy or sell at the average spot price of the *commodity* prevailing over some period between trade date and maturity must be treated as a combination of:
- (1) a position equal to the full amount underlying the contract with a maturity equal to the maturity date of the contract which is:
    - (a) long, where the *firm* will buy at the average price; or
    - (b) short, where the *firm* will sell at the average price
  - (2) a series of notional positions, one for each of the reference dates where the contract price remains unfixed, each of which:
    - (a) is long if the position under (1) is short, or short if the position under (1) is long;
    - (b) equals a fractional share of the total quantity underlying the contract; and
    - (c) has a maturity date of the relevant reference date.

- 11 G The following guidance provides an example of 10R.

In January, a *firm* agrees to buy 100 tonnes of copper for the average spot price prevailing during the 20 *business days* in February, and will settle on 30 June. After entering into this agreement, the *firm* faces the risk that the average price for February increases relative to that for 30 June. Therefore, as highlighted in the table below:

- (1) the short positions reflect the fact that this could occur because any one of the remaining forward prices for February increase; and
  - (2) the long position reflects the fact that this loss could occur because the forward price for 30 June falls.
- 12 G Table: Example of buying at the average spot price prevailing in the future (see 11G)

	Application of 10R(1)	Application of 10R(2)
From trade date to start of averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	A series of 20 notional short positions each equal to 5 tonnes of copper. Each position is allocated a maturity equal to one of the <i>business days</i> in February (one for each day).
During averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	As each <i>business day</i> goes by in February the price for 5 tonnes of copper is fixed and so there will be one less notional short position.
After averaging period	Long position in 100 tonnes of copper with a maturity of 30 June.	No short positions.

#### Futures, CFDs and options on a commodity index

- 13 R *Commodity index futures and commodity index options* (unless the *option* is included in the *firm's option PRR* calculation), must be treated as follows:
- (1) Step 1: The total quantity underlying the contract must be either:
    - (a) treated as a single notional *commodity* position (separate from all other *commodities*); or
    - (b) divided into notional positions, one for each of the constituent *commodities* in the index, of an amount which is a proportionate part of the total underlying the contract according to the weighting of the relevant *commodity* in the index.
  - (2) Step 2: Each notional position determined in step 1 must then be included:
    - (a) when using the simplified approach (24R), without adjustment; or
    - (b) when using the maturity ladder (25R) or modified maturity ladder approach (30R), with the adjustments in table 32R.
- 14 R Table: Treatment of *commodity index futures* and *commodity index options* (see 13R(2)(b)).

Construction of index	Notional position (or positions) and maturity
Spot level of index is based on the spot price of each constituent <i>commodity</i>	Each quantity determined in step 1 is assigned a maturity equal to the expiry date of the contract.
Spot level of index is based on an average of the forward prices of each constituent <i>commodity</i>	Each quantity determined in step 1 is divided (on a pro-rata basis) into a series of forward positions to reflect the impact of each forward price on the level of the index. The maturity of each forward position equals the maturity of the relevant forward price determining the level of the index when the contract expires.

- 15 G An example of using 13R and table 14R is as follows. A *firm* is long a three-month *commodity index future* where the spot level of the index is based on the one, two and three month forward prices of aluminium, copper, tin, lead, zinc and nickel (18 prices in total).

Step 1: the *firm* must decide whether to treat the full quantity underlying the contract as a single notional *commodity* position, or disaggregate it into notional positions in aluminium, copper, tin, lead, zinc and nickel. In this case the firm decides to disaggregate the contract into notional positions in aluminium, copper, tin, lead, zinc and nickel.

Step 2: if the *firm* uses the simplified method, nothing more need be done to arrive at the notional position. In this case the *firm* uses the maturity ladder approach and so subdivides each position in each metal into three because the level of the index is based on the prevailing one, two and three month forward prices. Since the *future* will be settled in three months' time at the prevailing level of the index, the three positions for each metal will have maturities of four, five and six months respectively.

#### Commodity swaps

- 16 R A *firm* must treat a *commodity swap* as a series of notional positions, one position for each payment under the *swap*, each of which:
- (1) equals the total quantity underlying the contract;
  - (2) has a maturity corresponding to the payment date; and
  - (3) is long or short according to 17R.
- 17 R Table: Treatment of *commodity swaps* (see 16R)

	Receiving amounts which are unrelated to any <i>commodity's</i> price	Receiving the price of <i>commodity 'b'</i>
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Paying amounts which are unrelated to any <i>commodity's</i> price	N/A	Long positions in <i>commodity</i> 'b'
Paying the price of <i>commodity</i> 'a'	Short positions in <i>commodity</i> 'a'	Short positions in <i>commodity</i> 'a' and long positions in <i>commodity</i> 'b'

- 18 G Table 17R shows that where the legs of the *swap* are in different *commodities*, a series of forward positions are created for each *commodity* (that is, a series of short positions in *commodity* 'a' and a series of long positions in *commodity* 'b').
- 19 G Table 17R also covers the case where one leg is unrelated to any *commodity's* price. This leg may be subject to a *PRR* under another appendix; for example, an interest rate based leg would have to be included in a *firm's* interest rate *PRR* calculation.

#### Calculating the *PRR* for each commodity

- 20 R A *firm* must calculate a *PRR* for each *commodity* separately using either the simplified approach (24R), the maturity ladder approach (25R) or the modified maturity ladder approach (30R).
- 21 G A *firm* need not use the same approach for all *commodities*.
- 22 R A *firm* must treat positions in different grades or brands of the same *commodity*-class as different *commodities* unless they:
- (1) can be delivered against each other; or
  - (2) have price movements which have exhibited a stable correlation coefficient of at least 0.9 over the last 12 months. The *firm* must then monitor the correlation on a continuing basis
- 23 R If a *firm* intends to rely on the approach in 22R(2) it must:
- (1) notify the *FSA* in writing at least twenty *business days* prior to the date the *firm* starts relying on it.
  - (2) when it notifies the *FSA* under (1) the *firm* must also provide to the *FSA* the analysis of price movements on which it relies.

#### SIMPLIFIED APPROACH

- 24 R A *firm* which calculates *PRR* using the simplified approach must do so by summing:
- (1) 15% of the net position multiplied by the spot price for the *commodity*; and

- (2) 3% of the gross position (long plus short, ignoring the sign) multiplied by the spot price for the *commodity*.

**Maturity ladder approach**

- 25 R A *firm* using the maturity ladder approach must calculate the *PRR* following the steps in 26R and then sum all spread charges, carry charges and outright charges that result.
- 26 R The *firm* must calculate the charges referred to in 25R as follows:
- (1) Step 1: Offset long and short positions maturing:
    - (a) on the same day; or
    - (b) (in the case of positions arising under contracts traded in markets with daily delivery dates) within 10 *business days* of each other.
  - (2) Step 2: Allocate the positions remaining after step 1 to the appropriate maturity band in table 28R (*physical commodity* positions are allocated to band 1).
  - (3) Step 3: Match long and short positions within each band. In each instance, calculate a spread charge equal to the matched amount multiplied first by the spot price for the *commodity* and then by the spread rate of 3%.
  - (4) Step 4: Carry unmatched positions remaining after step 3 to another band where they can be matched, then match them. Do this until all matching possibilities are exhausted. In each instance, calculate:
    - (a) a carry charge equal to the carried position multiplied by the spot price for the *commodity*, the carry rate of 0.6% and the number of bands by which the position is carried; and
    - (b) a spread charge equal to the matched amount multiplied by the spot price for the *commodity* and the spread rate of 3%.
  - (5) Step 5: Calculate the outright charge on the remaining positions (which will either be all long positions or all short positions). The outright charge equals the remaining position (ignoring the sign) multiplied by the spot price for the *commodity* and the outright rate of 15%.
- 27 G The matched amount in 26R is the lesser (ignoring the sign) of either the total long position or the total short position. For example, a band with 1000 long and 700 short results in a matched amount of 700. The unmatched amount would be 300.
- 28 R Table: Maturity bands for the maturity ladder approach (see 26R))

<b>Band</b>	<b>Maturity of position</b>
Band 1	$0 \leq 1$ month
Band 2	$> 1$ month $\leq 3$ months
Band 3	$> 3$ months $\leq 6$ months

Band 4	> 6 months ≤ 1 year
Band 5	> 1 year ≤ 2 years
Band 6	> 2 years ≤ 3 years
Band 7	> 3 years

- 29 G Figure: An example illustrating the calculation of the *PRR* on an individual *commodity* using the maturity ladder approach (26R).

Figure 29G: After a *firm* has carried out the pre-processing required by 26R(1) (that is, step 1), it follows steps 2 to 5 as shown below. Because the *firm* is using the maturity ladder approach the spread rate is 3%, the carry rate is 0.6% and the outright rate is 15%. The example assumes that the spot price for the *commodity* is £25.

Band	Step 2 Allocate remaining positions to appropriate maturity bands	Step 3 Match within bands. Each matched amount incurs a spread charge.	Step 4a Carry across bands. Each carried amount incurs a carry charge.	Step 4b Match within band. Each matched amount incurs a spread charge.	Step 6 Remaining position(s) incur an outright charge.																
0 ≤ 1 month																					
>1 month ≤ 3 months	1000 long 700 short	700 matched	300 carried																		
>3 months ≤ 6 months																					
>6 months ≤ 1 year																					
>1 year ≤ 2 years	600 short	Nothing matched	100 carried	400 matched	200 short remains																
>2 years ≤ 3 years																					
> 3 years	100 long	Nothing matched																			
<table style="width: 100%; border-collapse: collapse;"> <tr> <td style="width: 20%; padding-left: 40px;">Spread charges</td> <td style="padding-left: 20px;">700*£25*3% + 400*£25*3%</td> <td style="padding-left: 20px;">=</td> <td style="padding-left: 20px;">£825</td> </tr> <tr> <td style="padding-left: 40px;">Carry charges</td> <td style="padding-left: 20px;">300*£25*0.6%*3 + 100*£25*0.6%*2</td> <td style="padding-left: 20px;">=</td> <td style="padding-left: 20px;">£165</td> </tr> <tr> <td style="padding-left: 40px;">Outright charge</td> <td style="padding-left: 20px;">200*£25*15%</td> <td style="padding-left: 20px;">=</td> <td style="padding-left: 20px;">£750</td> </tr> <tr> <td colspan="3"></td> <td style="text-align: right; border-top: 1px solid black; border-bottom: 3px double black;">£1740</td> </tr> </table>						Spread charges	700*£25*3% + 400*£25*3%	=	£825	Carry charges	300*£25*0.6%*3 + 100*£25*0.6%*2	=	£165	Outright charge	200*£25*15%	=	£750				£1740
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Outright charge	200*£25*15%	=	£750																		
			£1740																		

#### Modified maturity ladder approach

- 30 R Until 31 December 2006 a *firm* may use the modified maturity ladder approach to calculate the *PRR* for a particular *commodity* provided the *firm*:
- (1) has a diversified *commodities* portfolio;

- (2) undertakes significant *commodities* business; and
- (3) notifies the *FSA* in writing:
  - (a) at least twenty *business days* before the date the *firm* intends to start using the modified maturity method; and
  - (b) If the facts and matters relied on to demonstrate that the *firm* meets the criteria in (1) and (2).

31 R A *firm* using the modified maturity ladder approach must calculate the *PRR* by:

- (1) following the same steps as in 26R but using the rates from table 32R rather than those in 26R; and
- (2) summing all spread charges, carry charges and outright charge that result.

32 R Table: Alternative spread, carry and outright rates (see 31R).

	Precious metals (excluding gold)	Base metals	Softs (agricultural)	Other (including energy)
Spread rate (%)	2	2.4	3	3
Carry rate (%)	0.3	0.5	0.6	0.6
Outright rate (%)	8	10	12	15

33 G For the purposes of 30R(1) a *firm* has a diversified *commodity* portfolio where it holds positions in more than one of the *commodities* falling in any of the categories set out in table 32R and holds positions across different maturities in those individual *commodities*. A *firm* would not have a diversified *commodity* portfolio if it held positions in only one *commodity* in each of the categories set out in table 32R. This is because the rates in table 32R assume *firms* have positions in more than one of that category's *commodities*. Different *commodities* within a given category are likely to exhibit different volatilities, so where a *firm* does not have a diversified *commodity* portfolio in that category, the rates applying to that category might underestimate the regulatory capital required for a certain *commodity* at certain times.

34 G What constitutes significant business in 30R(2) will vary from *firm* to *firm*. The more regularly the *firm* undertakes trades in *commodities* and the more consistently it has positions in the relevant *commodity*, the more likely it is to be undertaking significant business for the purposes of 30R(2).

35 R Where a *firm* is:

- (1) treating a *commodity* index derivative as if it was based on a single separate *commodity* (see 13R(1)(a)); and

- (2) uses the modified maturity ladder approach to calculate the *PRR* for that *commodity*;

it must determine which index constituent incurs the highest rate in table 32R and apply that rate to the notional position for the purposes of 31R.

- 36 G Where an index is only based on precious metals, 13R allows the *firm* to treat the single notional position as precious metal for the purposes of 31R. However, if the index contained a mix of precious metals and base metals the *firm* would have to treat the notional position under 35R as a base metal (because base metals attract a higher rate than precious metals in table 32R).

## Appendix 7

### Securities Underwriting

#### General rules

- 1 G This appendix sets out the method for calculating a net *underwriting* position or reduced net *underwriting* position, which is then included in the *PRR* calculation in other appendices, or the liquidity adjustment calculation.

- 2 R A *firm* which *underwrites* or *sub-underwrites* an issue of *securities* must:
- (1) identify commitments to *underwrite* or *sub-underwrite* which give rise to an *underwriting* position (see 8R);
  - (2) identify the time of initial commitment (see 14R);
  - (3) calculate the net *underwriting* position (set out in 18R) or reduced net *underwriting* position (if permitted under 24R);
- 3 R A *firm* must include the net *underwriting* position or reduced net *underwriting* position in:
- (1) 3R(1) of appendix 4, where debt *securities* are being underwritten;
  - (2) 2R(1) of appendix 5, where *equities* are being underwritten;
  - (3) 22R of appendix 9, where *warrants* are being underwritten; or
  - (4) 10-66(1)R where the *firm* does not have a *trading book*; and
  - (5) 2R of appendix 8, where the *equities*, debt *securities* or *warrants* being underwritten are denominated in a *foreign currency*.
- 4 R A *firm* must comply with 2R from initial commitment (as determined under 8R) until the end of the fifth *business day* after *working day 0* (as determined under 23R).
- 5 G *Sub-underwriting* is a commitment given by one *firm* to someone other than the issuer or seller of the *securities*, to *underwrite* all or part of an issue of *securities*.
- 6 G The net *underwriting* position calculated in 18R will also be used in calculating the net *underwriting exposure* set out in 32R.
- 7 G The net *underwriting* position or reduced net *underwriting* position arising from *underwriting* or *sub-underwriting* a rights or *warrants* issue should be calculated using the current market price of the underlying *security* for the purposes of the *equity PRR* or *option PRR*. However, the *PRR* will be limited to the value of the net *underwriting* position calculated using the initial issue price of the rights or *warrants*.

#### Commitments to underwrite securities

- 8 R For the purpose of 2R(1), a *firm* has a commitment to *underwrite* or *sub-underwrite* an issue of *securities* where:
- (1) it gives a commitment to an issuer of *securities* to *underwrite* an issue of *securities*;
  - (2) it gives a commitment to a person, other than the issuer of *securities*, to *sub-underwrite* an issue of *securities*; or

- (3) it is a member of a syndicate or group that gives a commitment to an issuer to *underwrite* an issue of *securities* or a commitment to a person other than the issuer of *securities*, to sub-*underwrite* an issue of *securities*.
- 9 G Block trades including bought deals, private placements, revolving *underwriting* facilities and *underwriting* syndicated loans are not within the scope of this appendix.
- 10 R For the purpose of this appendix, *securities* include debt and *equity instruments*, and *instruments* which are convertible into *securities* but excludes loans.
- 11 R A *firm* that buys and sells *securities* before issue is dealing in the grey market. This appendix does not apply to a *firm* dealing in the grey market unless the *firm*:
- (1) has an *underwriting* commitment to the issuer in respect of those *securities*; or
  - (2) has a sub-*underwriting* commitment in respect of those *securities* and is using the grey market solely for the purpose of reducing that sub-*underwriting* commitment.
- 12 G In this appendix the grey market is the market in which dealers "buy" and "sell" securities ahead of issue. In reality the dealers are buying and selling promises to deliver the securities when issued.
- 13 R Where a single *firm* is involved in both *underwriting* or sub-*underwriting* an issue of *securities* as well as dealing in that issue for proprietary trading purposes this appendix will not apply to grey market transactions undertaken by the proprietary trading part of the *firm*.

#### Time of initial commitment

- 14 R Subject to 15R, the time of initial commitment is the earlier of:
- (1) the time the *firm* signs an agreement with the issuer of *securities* to *underwrite* those *securities*; or
  - (2) the time the price and allocation of the issue are set.
- 15 R If a *firm* has an irrevocable and unfettered right to withdraw from an *underwriting* commitment, exercisable within a certain period, the commitment commences when that right expires.
- 16 G Subject to the existence of a right described in 15R an *underwriting* commitment commences even if it is subject to formal, legal or other conditions that would normally be expected to be satisfied.
- 17 G A force majeure or material adverse change clause would not be a right of the sort referred to in 15R.

#### Calculating the net underwriting position

- 18 R A *firm* must calculate a net *underwriting* position by adjusting the gross amount it has committed to *underwrite* for:

- (1) any sales or sub-*underwriting* commitments received that have been confirmed in writing at the time of initial commitment;
  - (2) any *underwriting* or sub-*underwriting* commitments obtained from others since the time of initial commitment;
  - (3) any purchases or sales of the *securities* since the time of initial commitment, (other than those referred to in 13R); and
  - (4) any allocation of *securities* granted or received, arising from the commitment to *underwrite* the *securities*, since the time of initial commitment.
- 19 R A *firm* signing an *underwriting* agreement with an issuer of *securities* where the exact issue price or allocation of *securities* has not been fixed must calculate the gross amount, for the purposes of 18R, as the amount it has formally committed to under that agreement until the time the exact issue price and/or allocation is set.
- 20 G Allocations may arise, after date of initial commitment, from the agreement to *underwrite*. For example obligations or rights to or from the issuer, the *underwriting* group or syndicate.

#### GREY MARKET TRANSACTIONS

- 21 R Subject to 11R and 13R a *firm* may include grey market transactions when calculating the net *underwriting* position.

#### OVER-ALLOTMENT OPTIONS

- 22 R When calculating the net *underwriting* position, a *firm* must exclude an over-allotment option granted to it by the issuer, except to the extent it reduces:
- (1) from working day 0 an over-allotment made by the *firm*; or
  - (2) from working day 0 an over-allotment made by the *firm* on behalf of another member of the *underwriting* syndicate who has been granted the over-allotment option.
- 23 R For the purposes of this appendix ‘working day 0’ is the *business day* on which the *firm* becomes unconditionally committed to accepting a known quantity of *securities* at a specified price, as follows:
- (1) For debt issues and *securities* which are issued in a similar manner, ‘working day 0’ is the later of the date on which the *securities* are allotted, and the date on which payment for them is due.
  - (2) For *equity* issues and *securities* which are issued in a similar manner, ‘working day 0’ is the later of the date on which the offer becomes closed for subscriptions and the date on which the allocations are made public.
  - (3) For rights issues, ‘working day 0’ is first day after the date on which the offer becomes closed to acceptances for subscription.



## Calculating the reduced net underwriting position

- 24 R A *firm* may apply the relevant reduction factors in table 27R to its net *underwriting* position if the *securities* it is *underwriting* or sub-*underwriting* are new *securities*.
- 25 R For the purposes of this appendix, a *firm* may treat as new *securities*:
- (1) *securities* that have not previously been offered for sale or subscription by an issuer;  
or
  - (2) *securities* that have not previously been traded on a *recognised investment exchange*, *designated investment exchange* or a *regulated market*.
- 26 R To calculate the reduced net *underwriting* position a *firm* must apply table 27R to the net *underwriting* position (calculated under 18R) as follows:
- (1) In respect of debt *securities*, a *firm* must calculate two reduced net *underwriting* positions; one for inclusion in the *firm's* specific risk calculation (43R of appendix 4), the other for inclusion in its general market risk calculation (48R of appendix 4).
  - (2) In respect of *equities*, a *firm* must calculate only one reduced net *underwriting* position, and then include it in the simplified equity method (see 27R of appendix 5).

27 R Table: Net *underwriting* position reduction factors (see 26R)

<b><i>Underwriting timeline</i></b>	<b>Debt</b>		<b>Equity</b>
	General market risk	Specific risk	
Time of initial commitment until <i>working day 0</i>	0%	100%	90%
Working day 1	0%	90%	90%
Working day 2	0%	75%	75%
Working day 3	0%	75%	75%
Working day 4	0%	50%	50%
Working day 5	0%	25%	25%
Working day 6 and onwards	0%	0%	0%

28 G Figure: An example of the reduced net *underwriting* position calculation. The example is based on the *firm* starting with a commitment to underwrite £100 million of a new *equity* issue.

<b>Time</b>	<b>Net <i>underwriting</i> position (see 18R)</b>	<b>Percentage reduction (see 27R)</b>	<b>Reduced net <i>underwriting</i> position<sup>1</sup></b>
At initial commitment 9.00am Monday	£100m gross amount is reduced by £20m due to sales/ sub- <i>underwriting</i> commitments confirmed in writing at the time of initial commitment (see 18R(1)). = £80m	90%	<b>£8m</b>
Post initial commitment 9.02am Monday	Remaining £80m is reduced by £40m due to further sales, sub- <i>underwriting</i> commitments obtained and allocations granted (see 18R (2) – (4)). = £40m	90%	<b>£4m</b>
At the end of working day 1	Remaining £40m is reduced to £20m due to further sales. = £20m	90%	<b>£2m</b>
End of working day 3	Remaining £20m is reduced to £5m due to further sales. = £5m	75%	<b>£1.25 m</b>
End of working day 4	Remaining £5m is reduced to £2m due to further sales. = £2m	50%	<b>£1m</b>
End of working day 5	Remaining £2m is reduced to £1m due to further sales. = £1m	25%	<b>£0.75 m</b>
Start of working day 6	£1m remaining = £1m	0%	<b>£1m</b>

**Note:** <sup>1</sup> *Firms* are reminded that in the case of an *equity*, the reduced net *underwriting* position must be treated under the simplified equity method (see 27R of appendix 5)

Large exposure risk from underwriting securities

CALCULATING THE NET UNDERWRITING EXPOSURE

- 29 R For the purposes of calculating the *LER* set out in 10-194R a *firm* must include net *underwriting exposures* to an issuer in the calculation of its total *exposure* to that issuer.
- 30 R A *firm* must include counterparty exposures to any sub-underwriters for the purposes of calculating the *LER* set out in 10-194R.
- 31 R A *firm*, before entering into a new *underwriting* commitment must be able to recalculate *LER* to the level of detail necessary to ensure that the *firm's financial resources requirement* does not exceed the *firm's financial resources*.
- 32 R A *firm* must calculate the net *underwriting exposure* to an issuer by applying the relevant reduction factors in table 33R to its net *underwriting* position calculated under 18R.
- 33 R Table: Calculation of net *underwriting exposure* (see 32R)

Time	Reduction factor to be applied to net <i>underwriting</i> position
Initial commitment to <i>working day 0</i>	100%
<i>Working day 0</i>	100%
Working day 1	90%
Working day 2	75%
Working day 3	75%
Working day 4	50%
Working day 5	25%
Working day 6 onwards	0%

- 34 R There is no *large exposure* limit or *LER* for net *underwriting exposures* between initial commitment and working day 0, except where specified by a requirement on a *firm's Part IV permission*. The *large exposure* requirements are set out in 10-190 to 10-196.

MONITORING AND REPORTING LARGE EXPOSURES

- 35 R For the purposes of *large exposures* monitoring only, a *firm* must report its net *underwriting exposure* from the date of initial commitment rather than working day 0.

## Risk management

- 36 R A *firm* must take reasonable steps to establish and maintain such systems and controls to monitor and manage its *underwriting* and sub-*underwriting* business as are appropriate to the nature, scale and complexity of its *underwriting* and sub-*underwriting* business.
- 37 G The general requirements for systems and controls are set out in SYSC. 36G is specific to a *firm's underwriting* and sub-*underwriting* business.
- 38 G A *firm* must take reasonable steps to:
- (1) allocate responsibility for the management of its *underwriting* and sub-*underwriting* business;
  - (2) allocate adequate resources to monitor and control its *underwriting* and sub-*underwriting* business;
  - (3) satisfy itself that its systems to monitor *exposure* to counterparties will calculate, revise and update its *exposure* to each counterparty arising from its *underwriting* or sub-*underwriting* business;
  - (4) satisfy itself of the suitability of each person who performs functions for it in connection with the *firm's underwriting* business having regard for the person's skill and experience; and
  - (5) satisfy itself that its procedures and controls to monitor and manage its *underwriting* business address, on an on-going basis, the capacity of sub-*underwriters* to meet sub-*underwriting* commitments.

## Appendix 8

### Foreign exchange PRR

#### General rule

- 1 R A *firm* must calculate its foreign exchange *PRR* by:
- (1) identifying which *foreign currency* and gold positions to include in the *PRR* calculation;
  - (2) calculating the *open currency position* and net gold position; and
  - (3) multiplying the sum (ignoring the sign) of the *open currency position* and the net gold position by 8%.
- G For example, a *firm* has an *open currency position* of -£100 and a net gold position of £50. The sum (ignoring the sign) is £150, and so the foreign exchange *PRR* is £12.

#### Scope of the foreign exchange PRR calculation

- 2 R A *firm*'s foreign exchange *PRR* calculation must include the following items regardless of whether they are *trading book* or *non-trading book* positions:
- (1) all gold positions;
  - (2) all instruments which are denominated in a *foreign currency*, except:
    - (a) *foreign currency* assets which have been deducted in full from the *firm*'s *financial resources*;
    - (b) instruments hedging (a);
    - (c) instruments hedging the *firm*'s capital; or
    - (d) instruments hedging a future *foreign currency* income or expense which is known but not yet accrued; and
  - (3) notional positions arising from the instruments listed in table 4R:
- 3 R A *firm* must notify the *FSA* in writing if it uses the exclusions under 2R(2)(a)-(d).

4 R Table: instruments which result in notional *foreign currency* positions (see 2R(3)).

Foreign exchange <i>futures, forwards, synthetic futures</i> and <i>CFDs</i>	10R
Foreign exchange <i>swaps</i>	12R
Foreign exchange <i>options</i> or <i>warrants</i> (unless the <i>firm</i> calculates a <i>PRR</i> on the <i>option</i> or <i>warrant</i> under appendix 9).	14R
Gold <i>futures, forwards, synthetic futures</i> and <i>CFDs</i>	15R
Gold <i>options</i> (unless the <i>firm</i> calculates a <i>PRR</i> on the <i>option</i> under appendix 9).	16R

5 G *Firms* are reminded that table 5R in appendix 9 divides foreign exchange *options* and *warrants* into:

- (1) those which must be treated under appendix 9; and
- (2) those which must be treated under either appendix 8 or appendix 9, but *firms* can choose whether appendix 8 or 9 is used.

6 R When determining the currency of denomination *firms* must:

- (1) use the currency in which the *firm* accounts for the instrument where an instrument is quoted in more than one currency; and
- (2) treat depository receipts as positions in the underlying security.

7 G Instruments denominated in a foreign currency include, amongst other things, assets and liabilities (including accrued interest); non-foreign exchange *derivatives*; net *underwriting* positions; reduced net *underwriting* positions; and irrevocable guarantees (or similar instruments) that are certain to be called.

8 G Where a contract is based on a basket of currencies, the *firm* can choose either to derive notional positions in each of constituent currencies, or treat it as a single notional position in a separate hypothetical currency.

#### Derivation of notional positions

9 G This section derives notional currency positions for the instruments listed in table 4R.

#### FOREIGN EXCHANGE FORWARDS, FUTURES, CFDs AND SYNTHETIC FUTURES

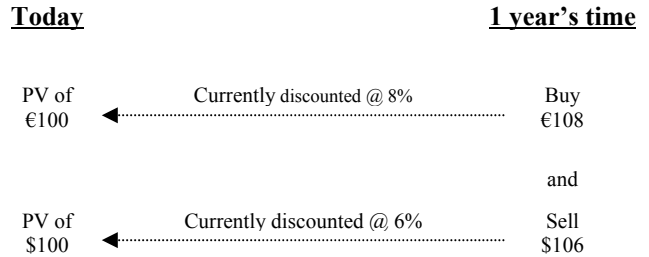
10 R A *firm* must treat a foreign exchange *forward, future* or *CFD* as two notional currency positions as follows:

- (1) a long notional position in the currency which the *firm* has contracted to buy; and
- (2) a short notional position in the currency which the *firm* has contracted to sell;

where the notional positions have a value equal to either:

- (a) the contracted amount of each currency to be exchanged in the case of a *forward* or *future* held in the *non-trading book*; or
- (b) the present value of the amount of each currency to be exchanged in the case of a *forward* or *future* held in the *trading book*.

- 11 G For example, a *firm* contracts to sell \$106 for €108 in one year's time.  
The present values of each cash flow are \$100 and €100 respectively.



- In the *non-trading book*, this *forward* would be treated as a combination of a €108 long position and a \$106 short position.
- In the *trading book*, this *forward* would be treated as a combination of a €100 long position and a \$100 short position.

*Firms* are reminded that foreign exchange *forwards* held in the *trading book* must also be included in the *firm's* interest rate *PRR* calculation (see 4R of appendix 4).

#### FOREIGN EXCHANGE SWAPS

- 12 R A *firm* must treat an foreign exchange *swap* as:
- (1) a long notional position in the currency which the *firm* has contracted to receive interest and principal;
  - (2) a short notional position in the currency which the *firm* has contracted to pay interest and principal; and
  - (3) where the notional positions have a value equal to either:
    - (a) the nominal amount of each currency underlying the *swap* if it is held in the *non-trading book*; or
    - (b) the present value amount of all cash flows in the relevant currency in the case of a *swap* held in the *trading book*.
- 13 G For example, a *firm* enters into a five year foreign exchange *swap* where it contracts to pay six month US\$ Libor on \$100 in return for receiving 6% fixed on €100. The present values of each leg are \$100 and €98 respectively.

- In the *non-trading book*, this *swap* would be treated as a combination of a €100 long position and a \$100 short position.
- In the *trading book*, this *swap* would be treated as a combination of a €98 long position and a \$100 short position.

*Firms* are reminded that foreign exchange *swaps* held in the *trading book* must also be included in the *firm's* interest rate *PRR* calculation (see table 4R of appendix 4).

#### FOREIGN EXCHANGE OPTIONS AND WARRANTS

- 14 R Where included in this appendix's *PRR* calculation (see table 4R), a foreign exchange *option* or *warrant* must be treated as a foreign exchange *forward*.

#### GOLD FORWARDS, FUTURES AND CFDS

- 15 R A *forward*, *future* or *CFD* on gold must be treated as a notional position in gold with a value equal to the amount of gold underlying multiplied by the current spot price for gold.

#### GOLD OPTIONS

- 16 R If included in the *PRR* calculation under this appendix (see table 4R), a gold *option* must be treated as a gold *forward*.

#### Open currency position

- 17 R A *firm* must calculate its *open currency position* by:
- (1) calculating the net position in each *foreign currency*;
  - (2) converting each net position into its *base currency* equivalent at current spot rates;
  - (3) summing all short net positions and summing all long net positions; and
  - (4) selecting the larger sum (ignoring the sign) from (3).

#### Net gold position

- 18 R A *firm* must calculate its net gold position by:
- (1) valuing all gold positions using the prevailing spot price for gold (regardless of the maturity of the positions);
  - (2) offsetting long and short positions; and
  - (3) converting the resulting net position into the *base currency* equivalent using the current spot foreign exchange rate.



## Appendix 9

### Option PRR

#### Option PRR calculation

- 1 R A *firm* must calculate its *option PRR* by:
  - (1) identifying which *option* positions must be included within the scope of the *option PRR* calculation under 3R to 5R;
  - (2) calculating the derived position in each *option* in accordance with 9R to 15R;
  - (3) calculating the *PRR* for each derived position in accordance with 16R to 32G;
  - (4) summing all of the *PRRs* calculated in accordance with (3).
- 2 G *Firms* are reminded that table 4R of appendix 4 and table 3R of appendix 5 also require an interest rate *PRR* to be calculated for *options* on *equities*, baskets of *equities* or *equity* indices. The interaction between this appendix and others is illustrated in 33G.

#### Scope of the option PRR calculation

- 3 R Except as permitted under 5R, a *firm's option PRR* calculation must include:
  - (1) each *trading book* position in an *option* on an *equity*, interest rate or debt *security*;
  - (2) each *trading book* position in a *warrant* on an *equity* or debt *security*; and
  - (3) each *trading book* and *non-trading book* position in an *option* on a *commodity*, currency or gold.
- 4 G 3R(2) includes net *underwriting* positions or reduced net *underwriting* positions in *warrants*.

5 R Table: Appropriate *PRR* calculation for an *option* or warrant (see 3R)

<b><i>Option type (see 18R) or Warrant</i></b>	<b><i>PRR calculation</i></b>
American <i>option</i> , European <i>option</i> , Bermudan <i>option</i> , Asian <i>option</i> or <i>warrant</i> for which the <i>in the money</i> percentage (see 6R) is equal to or greater than the appropriate <i>PRA</i> (see 7R and 8R)	Calculate either an <i>option PRR</i> , or the most appropriate to the underlying position of: (a) an <i>equity PRR</i> (b) an interest rate <i>PRR</i> (c) a <i>commodity PRR</i> (d) a foreign exchange <i>PRR</i>
American <i>option</i> , European <i>option</i> , Bermudan <i>option</i> , Asian <i>option</i> or <i>warrant</i> :  (a) for which the <i>in the money</i> percentage (see 6R) is less than the appropriate <i>PRA</i> (see 7R and 8R); or (b) that is <i>at the money</i> ; or (c) that is <i>out of the money</i> .	Calculate an <i>option PRR</i>
All other types of <i>option</i> listed in 18R (regardless of whether <i>in the money</i> , <i>at the money</i> or <i>out of the money</i> ).	

THE IN THE MONEY PERCENTAGE

6 R The *in the money* percentage is calculated as follows:

For a call *option*:

$$\frac{\text{Current market price of the underlying} - \text{Strike price of the option}}{\text{Strike price of the option}} * 100$$

For a put *option*:

$$\frac{\text{Strike price of the option} - \text{Current market price of the underlying}}{\text{Strike price of the option}} * 100$$

THE APPROPRIATE *PRA*

7 R The appropriate *PRA* for a position is that listed in table 8R against the relevant underlying position.

8 R Table: Appropriate *PRA* (see 7R)

<b>Underlying Position</b>	<b>Appropriate PRA</b>
<i>Equity</i>	The <i>PRA</i> applicable to the underlying <i>equity</i> or <i>equity</i> index in table 30R of Appendix 5 (simplified equity method)
Interest rate	The sum of the specific risk <i>PRA</i> (table 44R of appendix 4) and the general market risk <i>PRA</i> (53R of appendix 4) applicable to the underlying position
Debt <i>securities</i>	The sum of the specific risk <i>PRA</i> (table 43R of appendix 4) and the general market risk <i>PRA</i> (table 52R of appendix 4) applicable to the underlying position
<i>Commodity</i>	15% (unless the <i>firm</i> uses the modified maturity ladder approach in which case it is the outright rate applicable to the underlying position; see 30R-32R of appendix 6)
Currency	8%
Gold	8%

#### Calculating derived positions

- 9 R A *firm* must calculate the derived position specified in the table in 13R for each position included in its *option PRR* calculation.

#### NETTING POSITIONS

- 10 R A *firm* may calculate a derived position for its net position in an *option* or a *warrant*, if the relevant *options* or *warrants* are identical or may be treated as identical under 11R or 12R.
- 11 R A *firm* may treat *options* or *warrants* as identical if they have the same strike price, maturity (except for an interest rate cap or floor – see 12R) and underlying.
- 12 R A *firm* may treat as identical a purchased interest rate cap (or floor) and a written interest rate cap (or floor) only if they mature within 30 days of each other and all other terms are identical (a cap may not be netted against a floor).

#### DERIVED POSITIONS

- 13 R Table: Derived positions (see 9R)

	<b><i>Option (or warrant)</i></b>	<b>Derived position</b>
<i>Equity</i>	<i>Option (warrant)</i> on a single <i>equity</i> or <i>option</i> on a <i>future/forward</i> on a single <i>equity</i>	A notional position in the actual <i>equity</i> underlying the contract valued at the current market price of the <i>equity</i> .

	<i>Option (warrant) on a basket of equities or option on a future/forward on a basket of equities</i>	A notional position in the actual <i>equities</i> underlying the contract valued at the current market price of the <i>equities</i> .
	<i>Option (warrant) on an equity index or option on a future/forward on an equity index</i>	A notional position in the index underlying the contract valued at the current market price of the index.
Interest rate	<i>Option on an interest rate or an interest rate future/FRA</i>	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the sum of the time to expiry of the contract and the length of the period on which the settlement amount of the contract is calculated valued at the notional amount of the contract.
	<i>Option on an interest rate swap</i>	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the length of the <i>swap</i> valued at the notional principal amount.
	Interest rate cap or floor	A zero coupon <i>zero-specific-risk security</i> in the currency concerned with a maturity equal to the remaining period of the cap or floor valued at the notional amount of the contract.
Debt securities	<i>Option (warrant) on a debt security or option on a future/forward on a debt security</i>	The underlying debt <i>security</i> with a maturity equal to the time to expiry of the <i>option</i> valued as the nominal amount underlying the contract at the current market price of the debt <i>security</i> .
Commodity	<i>Option on a commodity or option on a future/forward on a commodity</i>	An amount equal to the tonnage, barrels or kilos underlying the <i>option</i> with a maturity equal to the expiry date of the <i>forward</i> or <i>futures</i> contract underlying the <i>option</i> .
Gold	<i>Option on gold or option on a future/forward on gold</i>	An amount equal to the troy ounces underlying the <i>option</i> with a maturity equal to the expiry date of the <i>forward</i> or <i>futures</i> contract underlying the <i>option</i> .

Currency	Currency <i>option</i>	The amount of the underlying currency that the <i>firm</i> will receive if the <i>option</i> is exercised converted at the spot rate into the currency that the <i>firm</i> will sell if the <i>option</i> is exercised.
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Combinations of options which can be treated as one option

- 14 R** A *firm* may treat (for the purpose of calculating an *option PRR* under this appendix) an *option* strategy listed in table 15R as the single position in a notional *option* specified against that strategy in table 15R, if:
- (1) each element of the strategy is transacted with the same *counterparty*;
  - (2) the strategy is documented as a single structure;
  - (3) each *option* in the structure has the same maturity and underlying; and
  - (4) the constituent parts of the structure form an indivisible single contract, so that neither party can unwind or default on one part of the structure without doing so for the contract as a whole.

15 R Table: *Option strategies* (see 14R)

<b><i>Option strategy</i></b> (and an example)	<b><i>Notional option position</i></b> (and rule it must be treated under)
<b>Bull Spread</b> (e.g. buy 100 call and sell 101 call)	<b>One purchased <i>option</i></b> (treat under 20R)
<b>Bear Spread</b> (e.g. sell 100 put and buy 101 put)	<b>One written <i>option</i></b> (treat under 21R)
<b>Synthetic Long Call</b> (e.g. long underlying and buy 100 put)	<b>One purchased <i>option</i></b> (treat under 20R or 24R)
<b>Synthetic Short Call</b> (e.g. short underlying and sell 100 put)	<b>One written <i>option</i></b> (treat under 21R or 24R)
<b>Synthetic Long Put</b> (e.g. short underlying and buy 100 call)	<b>One purchased <i>option</i></b> (treat under 20R or 24R)
<b>Synthetic Short Put</b> (e.g. buy underlying and sell 100 call)	<b>One written <i>option</i></b> (treat under 21R or 24R)
<b>Long Straddle</b> (e.g. buy 100 call and buy 100 put)	<b>One purchased <i>option</i></b> (treat under 20R)
<b>Short Straddle</b> (e.g. sell 100 call and sell 100 put)	<b>One written <i>option</i></b> (treat under 21R but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )
<b>Long Strangle</b> (e.g. buy 101 call and buy 99 put)	<b>One purchased <i>option</i></b> (treat under 20R)
<b>Short Strangle</b> (e.g. sell 99 call and sell 101 put)	<b>One written <i>option</i></b> (treat under 21R but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )
<b>Long Butterfly</b> (e.g. buy one 100 call, sell two 101 calls, and buy one 102 call)	<b>One purchased <i>option</i></b> (treat under 20R)
<b>Short Butterfly</b> (e.g. sell one 100 put, buy two 101 puts, and sell one 102 put)	<b>One written <i>option</i></b> (treat under 21R but with no reduction for the amount the <i>option</i> is <i>out of the money</i> )

The option PRR for an individual position

- 16 R A *firm* must calculate the *PRR* for each individual derived *option* position using the method specified in table 18R, or, if more than one method is permitted, using one of those methods.
- 17 R The resulting *PRRs* must be converted to the *firm's base currency* using spot foreign exchange rates.
- 18 R Table: *Option PRR* methods for different types of *option* (see 16R)

Option	Description	Method
American <i>option</i>	An <i>option</i> that may be exercised at any time over an extended period up to its expiry date.	Standard method or hedging method if appropriate
European <i>option</i>	An <i>option</i> that can only be exercised at expiry.	
Bermudan <i>option</i>	A cross between an American <i>option</i> and European <i>option</i> . The Bermudan <i>option</i> can only be exercised at specific dates during its life.	
Asian <i>option</i>	The buyer has the right to exercise at the average rate or price of the underlying over the period (or part of the period) of the <i>option</i> . One variant is where the payout is based on the average of the underlying against a fixed strike price; another variant is where the payout gives at expiry the price of the underlying against the average price over the <i>option</i> period.	
Barrier <i>option</i>	An <i>option</i> which is either cancelled or activated if the price of the underlying reaches a pre-set level regardless of the price at which the underlying may be trading at the expiry of the <i>option</i> . The knock-out type is cancelled if the underlying price or rate trades through the trigger; while the knock-in becomes activated if the price moves through the trigger.	
Corridor <i>option</i>	Provides the holder with a pay-out for each day that the underlying stays within a defined range chosen by the investor.	
Ladder <i>option</i>	Provides the holder with guaranteed pay-outs if the underlying trades through a pre-agreed price(s) or rate(s) at a certain point(s) in time, regardless of future performance.	
Lock-in <i>option</i>	An <i>option</i> where the pay-out to the holder is locked in at the maximum (or minimum) value of the underlying that occurred during the life of the <i>option</i> .	
Look-back <i>option</i>	An European style <i>option</i> where the strike price is fixed in retrospect, that is at the most favourable price (i.e. the lowest (highest) price of the underlying in the case of a call (put)) during the life of the <i>option</i> .	

Forward starting <i>option</i>	An <i>option</i> that starts at a future date.	
Compound <i>option</i>	An <i>option</i> where the underlying is itself an <i>option</i> (i.e. an <i>option</i> on an <i>option</i> ).	
Interest rate cap	An interest rate <i>option</i> or series of <i>options</i> under which a <i>counterparty</i> contracts to pay any interest costs arising as a result of an increase in rates above an agreed rate: the effect being to provide protection to the holder against a rise above that agreed interest rate.	Standard method, but no reduction for the amount the <i>option</i> is <i>out of the money</i> is permitted.
Interest rate floor	An interest rate <i>option</i> or series of <i>options</i> under which a <i>counterparty</i> contracts to pay any lost income arising as a result of a fall in rates below an agreed rate: the effect being to provide protection to the holder against a fall below that agreed interest rate.	
Performance <i>option</i>	An <i>option</i> based on a reference basket comprising any number of assets, where the pay-out to the holder could be one of the following: the maximum of the worst performing asset, or 0; the maximum of the best performing asset, or 0; the maximum of the spreads between several pairs of the assets, or 0.	Standard method or hedging method - using the highest <i>PRA</i> of the individual assets in the basket
Quanto	Quanto stands for “Quantity Adjusted <i>Option</i> ”. A quanto is an instrument where two currencies are involved. The payoff is depended on a variable that is measured in one of the currencies and the payoff is made in the other currency.	Subject to 31R, the standard method
Cliquet <i>option</i>	A cliquet <i>option</i> consists of a series of forward starting <i>options</i> where the strike price for the next exercise date is set equal to a positive constant times the underlying price as of the previous exercise date. They initially act like a vanilla <i>option</i> with a fixed price but as time moves on, the strike is reset and the intrinsic value automatically locked in at pre-set dates. If the underlying price is below the previous level at the reset date no intrinsic value is locked in but the strike price will be reset to the current price attained by the underlying. If the underlying price exceeds the current level at the next reset the intrinsic value will again be locked in.	Standard method for a purchased cliquet, or the method specified in 30R for a written cliquet
Digital <i>option</i>	A type of <i>option</i> where the pay-out to the holder is fixed. The most common types: all-or-nothing and one-touch <i>options</i> . All-or-nothing will pay out the fixed amount if the underlying is above (call) or below (put) a set value at expiry. The one-touch will pay the fixed amount if the underlying reaches a fixed point any time before expiry.	The method specified in 29R
Any other		The method



<i>option or warrant</i>		specified for the type of instrument whose description it most closely resembles.
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19 R In table 18R:

- (1) "standard method" refers to the method specified in 20R to 22R; and
- (2) "hedging method" refers to the method specified in 23R to 28R.

The standard method

PURCHASED OPTIONS AND WARRANTS

20 R Under the standard method, the *PRR* for a purchased *option* or *warrant* is the lesser of:

- (1) the market value of the derived position (see 9R) multiplied by the appropriate *PRA* (see 8R); and
- (2) the market value of the *option* or *warrant*.

WRITTEN OPTIONS AND WARRANTS

21 R Under the standard method, the *PRR* for a written *option* or *warrant* is the market value of the derived position (see 9R) multiplied by the appropriate *PRA* (see 8R). This result may be reduced by the amount the *option* or *warrant* is *out of the money* (subject to a maximum reduction to zero).

UNDERWRITING OR SUB-UNDERWRITING AN ISSUE OF WARRANTS

22 R Under the standard method, the *PRR* for *underwriting* or *sub-underwriting* an issue of *warrants* is the net *underwriting* position (or reduced net *underwriting* position) multiplied by the current market price of the underlying *securities* multiplied by the appropriate *PRA*, but the result can be limited to the value of the net *underwriting* position (or reduced net *underwriting* position) calculated using the issue price of the *warrant*.

The hedging method

23 G The hedging method involves *option PRR* being calculated on a combination of the *option* and its hedge.

24 R Under the hedging method a *firm* must calculate *PRR* for individual positions as follows:

- (1) for an *option* or *warrant* on an *equity*, basket of *equities* or *equity* index and its *equity* hedge(s), to the extent specified or permitted in table 26R, using the calculation in table 27R;
  - (2) for an *option* or *warrant* on a debt *security*, basket of debt *securities* or debt *security* index and its debt *security* hedge(s), to the extent specified or permitted in table 26R, using the calculation in table 27R;
  - (3) for an *option* on gold and its gold hedge, to the extent specified or permitted in table 26R, using the calculation in table 27R; and
  - (4) for an *option* on a currency and its currency hedge, to the extent specified or permitted in table 26R, using the calculation in table 28R.
- 25 R A *firm* may not use the hedging method for:
- (1) an interest rate *option* and its hedge; or
  - (2) a *commodity option* and its hedge.
- 26 R Table: Appropriate treatment for *equities*, debt *securities* or currencies hedging *options* (see 24R)

Hedge	PRR calculation for the hedge	Limits (if the hedging method is used)	Naked positions
An <i>equity</i> (hedging an <i>option</i> or <i>warrant</i> )	The <i>equity</i> must be treated in either appendix 5 ( <i>equity PRR</i> ) or the hedging method (table 27R)	The hedging method must only be used up to the amount of the hedge that matches the notional amount underlying the <i>option</i> or <i>warrant</i>	To the extent that the amount of the hedge (or <i>option</i> ) exceeds the notional amount underlying the <i>option</i> or <i>warrant</i> (or hedge), a <i>firm</i> must apply an <i>equity PRR</i> , interest rate <i>PRR</i> or foreign exchange <i>PRR</i> (or <i>option PRR</i> )
A debt <i>security</i> (hedging an <i>option</i> or <i>warrant</i> )	The debt <i>security</i> must be treated in appendix 4 (interest rate <i>PRR</i> ) or the hedging method (table 27R)		
Gold (hedging a gold <i>option</i> )	The gold must be treated in either appendix 8 (foreign exchange <i>PRR</i> ) or the hedging method (table 27R)		
A currency or currencies (hedging a currency <i>option</i> )	The currency must be treated in either appendix 8 (foreign exchange <i>PRR</i> ) or the hedging method (table 28R)		

- 27 R Table: The hedging method of calculating the *PRR* (*equities*, debt *securities* and gold) (see 24R(1) to (3))

	<i>Option or warrant position</i>	<i>PRR</i>		
		<i>In the money by more than the PRA</i>	<i>In the money by less than the PRA</i>	<i>Out of the money</i>
Long in security	Long put	Zero	Wp	X
	Short call	Y	Y	Z
Short in security	Long call	Zero	Wc	X
	Short put	Y	Y	Z
Where:				
Wp	$[(PRA - 100\%) \times \text{The underlying position valued at strike price} + \text{The market value of the underlying position}]$			
Wc	$[(100\% + PRA) \times \text{The underlying position valued at strike price} - \text{The market value of the underlying position}]$			
X	The market value of the underlying position multiplied by the appropriate <i>PRR</i>			
Y	The market value of the underlying position multiplied by the appropriate <i>PRR</i> . This result may be reduced by the market value of the <i>option</i> or <i>warrant</i> , subject to a maximum reduction to zero.			
Z	The hedging method is not permitted; the standard method must be used.			

28 R Table: The hedging method of calculating the *PRR* (currencies) (see 24R(4))

<i>Option position</i>	<i>PRR</i>		
	<i>In the money by more than 8%</i>	<i>In the money by less than 8%</i>	<i>Out of the money</i>
Long calls & long puts	Zero	$W_L$	X
Short calls & short puts	Zero	Y	X
Where:			
$W_L$	[ 1.08 x The amount of the underlying currency that the <i>firm</i> will receive if the <i>option</i> is exercised, converted at the strike price into the currency that the <i>firm</i> will sell if the <i>option</i> is exercised		- The market value of the underlying position
X	The market value of the underlying position multiplied by 8%.		
Y	The market value of the underlying position multiplied by 8%. This result may be reduced by the market value of the <i>option</i> , subject to a maximum reduction to zero.		

### Specific methods and treatments

#### DIGITAL OPTIONS

29 R The *PRR* for a digital *option* is the maximum loss of the *option*.

#### WRITTEN CLIQUET OPTIONS

30 R The *PRR* for a written cliquet *option* is the market value of the derived position (see 9R) multiplied by the appropriate *PRA* (see 8R) multiplied by  $F+1$  (see below). This result may be reduced by the amount the *option* is *out of the money* (subject to a maximum reduction to zero).

$$\text{i.e. } [PRA * \text{underlying} * (F + 1)] - OTM$$

$$\text{where } F = \min \left[ FR, \max \left( \frac{FR}{2}, Y \right) \right]$$

FR: Number of forward re-sets

Y: Years to maturity

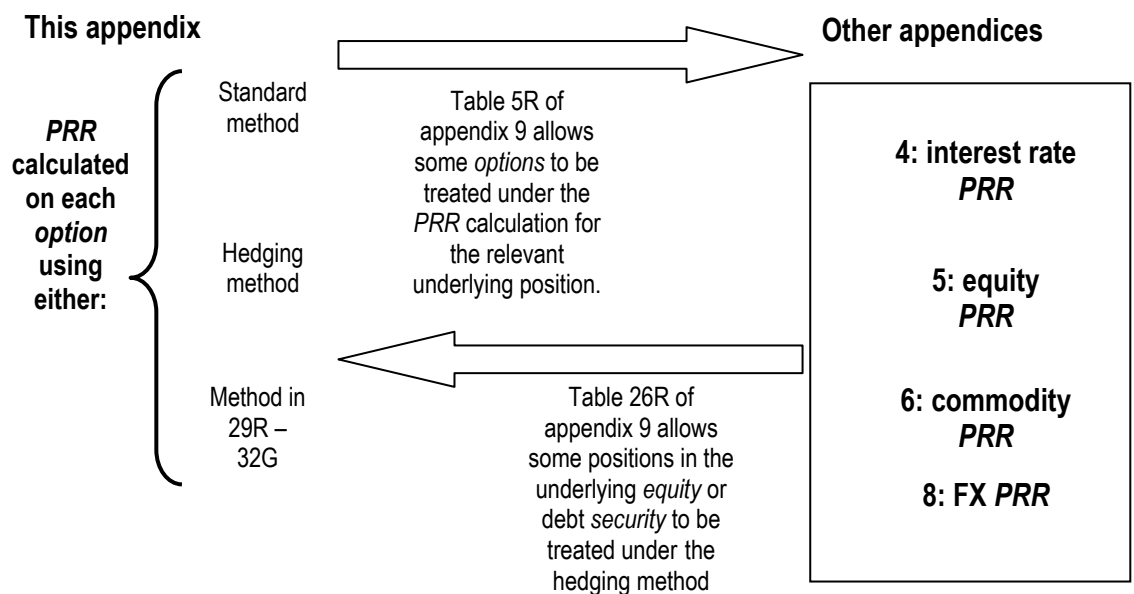
OTM: Out of the money amount

#### QUANTOS

- 31 R If the pay-out to the holder of a quanto *option* is fixed at the inception of the transaction a *firm* must add 8% to the *PRA* when applying the standard method.
- 32 G The additional *PRA* is to account for the forward foreign currency exchange risk.

#### Interaction with other appendices

- 33 G Figure: Diagram illustrating the relationship between this appendix and other appendices.



## Appendix 10

### Use of a CAD1 Model

#### Introduction

1. G A *firm* is required under 10-80(2)R to calculate *PRR* using the rules and appendices listed in table 10-80(2)R. However, the *FSA* may at the *firm's* request, waive or modify 10-80(2)R and thereby allow the *firm* to calculate all or part of its *PRR* using a "CAD1" (Capital Adequacy Directive) (for options risk aggregation and/or interest rate pre-processing) or "VaR" (value at risk) model instead. Appendix 11 deals with VaR model *waivers*.
2. G The purpose of this appendix is to provide guidance on the *FSA's* policy for granting CAD1 model *waivers* under section 148 of the *Act*. The policy recognises that CAD1 models may vary across *firms* but, as a minimum, the *FSA* will need to be satisfied about:
  - (1) the quality of the internal controls and risk management surrounding the model (see 18G to 22G for further details); and
  - (2) the quality of the model standards and that the CAD1 model captures and produces an accurate measure of the risks inherent in the portfolio covered by the CAD1 model (see 23G to 52G for further details).
3. G It also explains how the output from the model is fed into the 10-80 *PRR* calculation.
4. G If a CAD1 model recognition *waiver* is granted by the *FSA*, the *waiver* will contain certain conditions. In order to adequately address individual circumstances, these conditions may differ from the requirements set out in this appendix. The *waiver* will also confirm the *rules* to which the *waiver* applies, and the scope of CAD1 model recognition granted to a *firm*.
5. G As explained in *SUP* 8.3.1G, *waivers* permitting the use of models in the calculation of *PRR* will not be granted if that would be contrary to the CAD, and any *waiver* which is granted will only be granted on terms that are compatible with the CAD. The *FSA* considers it unlikely that it will deviate from this approach even where the *firm* making the *waiver* application is not subject to CAD. Accordingly, the only *waivers* permitting the use of models that the *FSA* is likely to grant are CAD1 and VaR models.
6. G If a *firm* ceases to meet any of these standards, the *FSA's* policy is that the *waiver* should cease to have effect.

#### Scope of CAD1 models

7. G The *FSA* recognises two types of CAD1 model. The table below sets out:

Options risk aggregation models		Interest rate pre-processing models
Brief description and eligible instruments	Analyse and aggregate <i>options</i> risks for <ul style="list-style-type: none"> <li>• interest rate <i>options</i>,</li> <li>• <i>equity options</i>,</li> <li>• foreign exchange <i>options</i>; and</li> <li>• <i>commodity options</i>.</li> </ul>	May be used to calculate duration weighted positions for: <ul style="list-style-type: none"> <li>• interest rate <i>futures</i>;</li> <li>• forward rate agreements (<i>FRAs</i>);</li> <li>• forward commitments to buy or sell debt instruments;</li> <li>• <i>options</i> on interest rates, debt instruments, and <i>swaps</i>;</li> <li>• <i>warrants</i>;</li> <li>• <i>swaps</i>;</li> <li>• amortising bonds;</li> <li>• <i>equity futures, forwards</i> and <i>options</i> (but only in relation to the interest rate risk inherent in these products); and</li> <li>• Foreign exchange <i>futures, forwards</i> and <i>options</i>, but only in relation to the interest rate risk inherent in these products.</li> </ul>
The output and how it is used in the <i>PRR</i> calculation	Depending on the type of model and the conditions contained in any CAD1 model <i>waiver</i> granted, the outputs from an <i>options</i> risk aggregation model may be used as an input to the <i>PRR</i> calculation set out in <i>IPRU(INV)10-80R</i> .	Depending on the type of model and the conditions contained in any CAD1 model <i>waiver</i> granted, the individual sensitivity figures produced by this type of CAD1 model may be either input into a <i>firm's</i> standard duration method <i>PRR</i> calculation (see 60R of Appendix 4) or be converted into notional positions and input into a <i>firm's</i> maturity method <i>PRR</i> (see 55R of Appendix 4).

The CAD1 model waiver application and review process

8. G Details of the general *waiver* process are set out in *SUP 8*. Because of the complexity of a CAD1 model recognition *waiver*, it is recommended that, as set out in *SUP 8.3.3G*, a *firm* contact its usual contact at the *FSA* to discuss its proposed application. It should also be noted that the *waiver* recognition process in the case of a CAD1 model recognition *waiver* may take longer than the timescales indicated in *SUP 8.3.3G*.
9. G In order to consider a CAD1 model recognition *waiver* request, the *FSA* may undertake a review to ensure that it is adequate and appropriate for the *PRR* calculation.

10. G The model review process may be conducted through a series of visits covering various aspects of the *firm's* control and IT environment. Before these visits the *FSA* may ask the *firm* to provide some information relating to its *waiver* request accompanied by some specified background material. The model review visits are organised on a timetable that allows a *firm* being visited sufficient time to arrange the visit and provide the appropriate pre-visit information.
11. G As part of the model review process, the following may be reviewed: organisational structure and personnel; details of the *firm's* market position in the relevant products; profit and risk information; valuation and reserving policies; operational controls; IT systems; model release and control procedures; risk management and control framework; risk appetite and limit structure and future developments relevant to model recognition.
12. G The *FSA* will normally require meetings with senior management and staff from the front office, financial control, risk management, operations, systems development, information technology and audit areas.
13. G A review by a *skilled person* may be used before a CAD1 model *waiver* is granted to supplement the *waiver* process, or after the *waiver* has been granted to review the CAD1 model.
14. G If the *FSA* grants a *waiver* to allow the use of a CAD1 model, the *waiver* direction will specify the particular rule which has been modified, and set out the conditions on which the *waiver* has been granted. Conditions may include:
  - (1) the details of the calculation of *PRR*;
  - (2) the CAD1 model methodology to be employed;
  - (3) the products covered by the model (e.g. *option* type, maturity, currency);
  - (4) any notification requirements relating to the CAD1 model *waiver*; and
  - (5) any other conditions attached to the CAD1 model *waiver*.
15. G Where a *firm* operates any part of its CAD1 model outside the United Kingdom, the *FSA* may take into account the results of any home state supervisor's model review. The *FSA* may wish to receive information directly from the home state supervisor.

#### Maintenance of model recognition

16. G No changes should be made to a CAD1 model unless the change is not material. Material changes to a CAD1 model will require a renewed *waiver* to be issued. Materiality is measured from the time that the *waiver* is granted or, if the *waiver* has been varied in accordance with section 148 of the *Act*, the time of that variation. If a *firm* is considering making material changes to its CAD1 model, then it should notify the *FSA* at once. A *firm* must re-apply for a *waiver* if the products covered by the model change.
17. G If the CAD1 model ceases to meet the conditions of the *waiver*, the *firm* should notify the *FSA* at once. The *FSA* may then revoke the *waiver*, unless it is varied in accordance with section 148 of the *Act*.



## Risk management standards

18. G A *firm* with a complex portfolio is expected to demonstrate more sophistication in its modelling and risk management than a *firm* with a simple portfolio.
19. G A *firm* should be able to demonstrate that it meets the risk management standards set out in this appendix for each legal entity that will have the benefit of the CAD1 model *waiver*. This is particularly important for subsidiaries in *groups* subject to matrix management where the business lines cut across legal entity boundaries.
20. G A *firm* should have a conceptually sound risk management system which is implemented with integrity and should meet the following minimum standards:
  - (1) A *firm* should have a risk control unit that is independent of business trading units and reports directly to senior management. The unit should be responsible for designing and implementing the *firm's* risk management system. It should produce and analyse daily reports on the risks run by the business and on the appropriate measures to be taken in terms of the trading limits.
  - (2) A *firm's* senior management should be actively involved in the risk control process, and the daily reports produced by the risk control unit should be reviewed by a level of management with sufficient authority to enforce reductions of positions taken by individual traders as well as in the *firm's* overall risk exposure.
  - (3) The risk control group should have a sufficient number of staff with appropriate skills in the use of models.
  - (4) A *firm* should have established procedures for monitoring and ensuring compliance with a documented set of appropriate internal policies and controls concerning the overall operation of the risk measurement and control framework. This should take into account the front, middle and back office functions.
  - (5) A *firm* should conduct, as part of its internal audit process, a review of the systems and controls surrounding its CAD1 model. This review should include the valuation process, compliance with the CAD1 model scope and the activities of the business trading units and the risk control units. This review should be undertaken by staff independent of the areas being reviewed.
21. G In assessing whether the risk management and control framework is implemented with integrity, the *FSA* will consider the IT systems used to run the CAD1 model and associated calculations. The assessment will include, where appropriate:
  - (1) feeder systems; risk aggregation systems; the integrity of the data (i.e. it is complete, coherent and correct); reconciliations and checks on completeness of capture; and
  - (2) system development, change control and documentation; security and audit trails; system availability and contingency procedures; network adequacy.
22. G A *firm* should take appropriate steps to ensure that it has adequate controls surrounding:

- (1) the derivation of the *PRR* from the CAD1 model output;
- (2) CAD1 model development, including independent validation;
- (3) reserving;
- (4) valuation (see *IPRU(INV)10-41(9)R*), including independent validation; and
- (5) the adequacy of the IT infrastructure.

#### Model standards

23. G A *firm* should take appropriate steps to ensure that its CAD1 model captures and produces an accurate measure of the risks inherent in the portfolio covered by the CAD1 model. These risks may include, but are not limited to, gamma, vega and rho.

#### OPTIONS RISK AGGREGATION MODELS

24. G For a *firm* to obtain a CAD1 model *waiver* for its *options* risk aggregation model, it should have in place an appropriate *options* valuation model.
25. G The *FSA* does not specify the methodology that a *firm* should employ in order to produce the appropriate outputs from its CAD1 model. However, 26G to 42G provide details of how a *firm* could meet the requirements to capture gamma, vega and rho risks using a scenario matrix approach. Where a *firm* adopts the scenario matrix approach then the standards set out in 26G to 42G should be followed. The *firm* should also take into account other risks not captured by the scenario matrix approach. Otherwise, a *firm* may use an equivalent methodology. If a *firm* uses an equivalent methodology, then it will need to demonstrate that the approach used meets the requirements of this appendix.
26. G A scenario matrix is an approach by which an *options* portfolio is revalued given a number of simultaneous shifts in both the spot level of the underlying and the implied volatility.
27. G The scenario matrix approach may be employed for all types of *options* on all types of underlying asset.
28. G The following provides an outline of the initial steps to be taken when using the scenario matrix approach:
  - (1) A value for an *option* should be obtained using the *firm's options* valuation model.
  - (2) The inputs into the *options* valuation model for implied volatility of the underlying asset and the price of the underlying asset should then be altered so that a new value for the *option* is obtained (details of the amount by which the implied volatility and the price of the underlying should be amended are set out in 29G-35G).
  - (3) The difference between the original value of the *option* and the new value obtained following the alterations should be input into the appropriate cell in the matrix, the value in the central cell where there is no change in implied volatility or price of the underlying should therefore be zero.

- (4) The process of obtaining a new price for the *option* should be repeated until the matrix is completed.
29. G The alteration to the implied volatility (known as the implied volatility shift) referred to in 28(2)G may be a proportional shift, the size of which depends on the remaining life of the *option* and the asset class of the underlying. Table 31G sets out the shifts that should be applied where a proportional shift is used. Alternatively, a *firm* may use a single shift across all maturities or use an absolute rather than a proportional implied volatility shift. Where an absolute shift is used it should be at least as conservative as the proportional shifts. This should be reviewed and, if necessary updated, on a regular basis.
30. G A *firm* may choose to use a less detailed term structure than that in Table 31G, but the shifts used should be no less conservative than those set out. For example, a *firm* that uses one <3 month band, rather than the two bands (<1 month, and 1-3 months) set out in the table, should use the most conservative shift set out in the table for the bands covered that is, 30% for the <3 month band.
31. G TABLE: PROPORTIONAL IMPLIED VOLATILITY SHIFTS (SEE 29G)

REMAINING LIFE OF OPTION	PROPORTIONAL SHIFT	
	EQUITIES & FX & COMMODITIES	INTEREST RATES
≤1 month	30%	30%
>1≤3 months	20%	20%
>3≤6 months	15%	15%
>6≤9 months	12%	12%
>9≤12 months	9%	9%
>1≤2 years	6%	9%
>2≤4 years	4.5%	9%
>4 years	3%	9%

32. G The size of the underlying price/rate shift depends on the asset class of the underlying and is set out in 33G:
33. G TABLE: UNDERLYING PRICE/RATE SHIFTS (SEE 32G)

UNDERLYING ASSET CLASS	SHIFT
Equities	±8%
Foreign Exchange	±8%
Commodities	±15%, (but a <i>firm</i> may use the percentages applicable under the extended maturity ladder approach, where permitted by the requirements of Appendix 6).
Interest Rates	±100bp (but a <i>firm</i> may use the sliding scale of shifts by maturity as outlined in Appendix 4).

34. G The shifts outlined above are the maximum shifts required; in addition there will be a number of intermediate shifts as a result of the minimum matrix size criteria set out in 35G.
35. G The minimum size of the scenario matrix should be 3x7, that is, three observations for implied volatility (including the actual implied volatility) and seven observations for the price of the underlying (including the actual price of the underlying). A *firm* should be able to justify its choice of granularity. Greater granularity may be required where the portfolio contains, for example, a large proportion of barrier *options*.
36. G A different scenario matrix should be set up for each underlying asset type:
- (1) for *equities* (including single *equities*, baskets and indices) this means a separate matrix for each national market or non-decomposed basket or non-decomposed multi-national index;
  - (2) for *foreign exchange* products this means a separate matrix for each currency pair where appropriate;
  - (3) for *commodity* products this means a separate matrix for each underlying as defined in Appendix 6; and
  - (4) for interest rate products this means a separate matrix for each currency; in addition, a *firm* should not offset the gamma and vega exposures (except in the circumstances set out in 37G) arising from any one of the following types of products with the gamma and vega exposures arising from any of the other products in the list:
    - (a) swaptions (options on interest rates);
    - (b) interest rate *options* (including *options* on exchange-traded *deposit* or bill *futures*);
    - (c) bond *options* (including *options* on exchange-traded bond *futures*);

- (d) other types of exotic *option* which do not fall easily into one of the other three categories and are required by the *FSA* to form their own separate underlying asset.
37. G A *firm* may offset gamma and vega exposures arising from the products listed in 36(4)G where it can demonstrate that it trades different types of interest rate-related *options* as a portfolio and takes steps to control the basis risk between different types of implied volatility. If this is the case, then an individual matrix is not required for each of the products listed in 36(4)G and a combined scenario matrix may be used.
38. G Where it is imprudent to fully offset long-dated and short-dated vega exposure due to non-parallel shifts in the yield curve, a *firm* should use an appropriate number of scenario matrices to take account of non-parallel shifts in the yield curve according to the maturity of the *option* or underlying.
39. G Following the steps outlined in 28G, a *firm* then removes the portion of the values in the matrix that can be attributed to the effect that delta has had on the change in the value of the *option* (a process known as delta-stripping).
40. G Once the effect of delta has been removed from the matrix, the values left in the matrix relate to gamma and vega risk. A *firm's PRR* in relation to gamma and vega risk on the individual *option* is the absolute of the most negative cell in the scenario matrix produced. Where all cells are positive the *PRR* is zero. The total *PRR* for the gamma and vega risk on the portfolio of *options* is a simple sum of the individual requirements. This amount should then be fed into a *firm's PRR* calculation.
41. G The values that have been obtained for the delta-equivalent positions of instruments included in the scenario matrix should then be treated in the same way as positions in the underlying. Where the delta obtained relates to interest rate position risk, the delta equivalent positions may be fed into a *firm's* interest rate pre-processing model providing that the positions fall within the scope of the interest rate pre-processing model set out in 7G, and that the *firm* has the appropriate CAD1 model *waiver*. Alternatively, the delta obtained should be fed into the standard *PRR* calculation in Appendix 4, 5, 6 or 8 as appropriate.
42. G In using the scenario matrix approach, none of the steps followed will take specific account of a *firm's* exposure to rho risk. Where a *firm* can demonstrate that for interest rate-related *options* the rho sensitivity is effectively included in the delta sensitivities produced, there is no separate capital requirement relating to rho. For all other *options* except commodity *options*, a *firm* should calculate a rho sensitivity ladder by currency as part of its CAD1 model and feed this either into the maturity or duration method *PRR* calculation set out in Appendix 4 or, where a *firm* has the appropriate *waiver*, into an interest rate pre-processing model.

#### INTEREST RATE PRE-PROCESSING MODELS

43. G A *firm* granted a *waiver* to use an interest rate pre-processing model is permitted to use it for the pre-processing of the instruments set out in 7G, from which the residual positions are fed into the maturity or duration method *PRR* calculation as set out in Appendix 4.

44. G There are a number of different methods of constructing pre-processing models. All pre-processing models should generate positions that have the same sensitivity to defined interest rate changes as the underlying cash flows.
45. G In an interest rate pre-processing model each transaction is converted into its constituent cash flows. The cash flows are discounted using zero coupon rates derived from the *firm's* own yield curves.
46. G The cash flows are then calculated again using the *firm's* own yield curve shifted by the amount set out in 48G.
47. G The difference between the present values calculated using the *firm's* own yield curve and those calculated using the *firm's* curve shifted by the amount specified are known as the sensitivity figures. Alternatively, *firms* may shift the yield curve by one basis point and multiply the sensitivity figures up by the appropriate amount in order to achieve the shifts set out in 48G. These sensitivity figures are then allocated to each of the 15 maturity bands set out in 48G.
48. G TABLE: YIELD CURVE SHIFTS (SEE 46G)

Zone	Modified Duration	Assumed interest rate change (percentage points)
1	0 ≤ 1 months	1.00
	> 1 ≤ 3 months	1.00
	> 3 ≤ 6 months	1.00
	> 6 ≤ 12 months	1.00
2	> 1.0 ≤ 1.9 years	0.90
	> 1.9 ≤ 2.8 years	0.80
	> 2.8 ≤ 3.6 years	0.75
3	> 3.6 ≤ 4.3 years	0.75
	> 4.3 ≤ 5.7 years	0.70
	> 5.7 ≤ 9.3 years	0.65
	> 7.3 ≤ 9.3 years	0.60
	> 9.3 ≤ 10.6 years	0.60
	> 10.6 ≤ 12 years	0.60
	> 12.0 ≤ 20 years	0.60
	> 20 years	0.60

49. G Sensitivity figures calculated by a *firm* using an interest rate pre-processing model are usually produced in the format of a net sensitivity by maturity bucket or by discrete gridpoint. These maturity buckets or gridpoints should then be allocated to the 15 bands set out in 48G. The number of maturity buckets or gridpoints used to represent a yield curve can be referred to as granularity. It is not a requirement that each of the 15 bands for *firms* have one or more maturity buckets or gridpoints allocated; however, for all *firms* the granularity should be adequate to capture the material curve risk in the portfolio. Curve risk can be defined as the risk associated with holding long and short positions at different points along the yield curve.

50. G Positive and negative amounts in each of the different maturity bands of the sensitivity calculation should then be netted off to produce one figure for each of the bands. There is no capital requirement for this netting process.
51. G The individual sensitivity figures produced should then be input into a *firm's* duration method *PRR* calculation as set out in Appendix 4. The individual sensitivity figures for each band should be included with the other positions in the weighted net positions column used in the duration method.
52. G Alternatively, *firms* may choose to use an approach based on the maturity method set out in Appendix 4, making appropriate adjustments to the sensitivity figures.

## Appendix 11

### Use of a Value at Risk Model

#### Introduction

- 1 G This appendix provides details of when the *FSA* expects to allow a *firm* to use its own Value at Risk (VaR) model for the purpose of calculating part or all of its *PRR*, and explains how the model will relate to the standard rules.
- 2 G The models described in this appendix are described as VaR models in order to distinguish them from the kinds of model originally contemplated by the Capital Adequacy Directive (CAD). (These are covered in Appendix 10 and referred to as "CAD 1 models".) A VaR model is a risk management model which uses a statistical measure to predict profit and loss movement ranges with a confidence interval. The standards described in this appendix, and which will be applied by the *FSA*, are based on and implement Annex VIII of the CAD.
- 3 G The aim of the VaR model approach is to enable a *firm* with adequate risk management systems to benefit from more accurate *financial resources requirements* than those generated by standard requirements, and to provide a *firm* with an incentive to measure market risks as accurately and comprehensively as possible. It is crucial that those responsible for managing market risk at a *firm* should be aware of the assumptions and limitations of the *firm's* VaR model.
- 4 G A VaR measure provides an estimate of the worst expected loss on a portfolio resulting from market movements over a period of time with a given confidence level. The *PRR* relating to the risks covered by the VaR model is based on the value produced by the VaR model. In undertaking the *PRR* calculation, a *firm* should apply a multiplication factor to the value produced by the VaR model (details of how the multiplication factor will affect a *PRR* are set out in 76G). The multiplication factor that should be applied is set by the *FSA*. The multiplication factor may be increased by a plus factor, which relates to the results of a *firm's* back-testing process (for further details on the plus factor see 63G).
- 5 G There are a number of methodologies for calculating *PRR* using a VaR model. These include variance-covariance, historical simulation, Monte Carlo or a hybrid of these. Although the section on model standards in this appendix sets out some general model standards that should be met, the *FSA* does not prescribe any one method of computing *PRR* using a VaR model. Moreover, it does not wish to discourage any *firm* from developing alternative risk measurement techniques. A *firm* should discuss the use of any alternative techniques used to calculate *PRR* with the *FSA*.

#### Overview

[LINK TO STANDARD PRR RULES](#)



- 6 G 10-80(2)R requires a *firm* to use the rules in appendices 4 to 9 to calculate *PRR*. Therefore, a *firm* needs to apply for a *waiver* in order to calculate its *PRR* using a VaR model instead of (or in combination with) the standard approaches required under 10-80(2)R.
- 7 G The VaR Model based *PRR* produced in accordance with this appendix should be included in the *firm's PRR* calculation set out in 10-80(2)R. The VaR model *PRR* should be used in place of the appropriate *PRR* for the risks covered by the VaR model.

#### BASIC REQUIREMENTS / SUMMARY OF CHAPTER

- 8 G Details of the general *waiver* process can be found in *SUP* 8. The *FSA* will not normally grant a VaR model *waiver* unless it is satisfied about the quality of:
- (1) the internal controls and risk management surrounding the VaR model (see 29G to 36G);
  - (2) the VaR Model Standards (see 37G to 45G);
  - (3) risk management standards including stress testing and backtesting procedures surrounding a VaR model; (see 46G to 74G); and
  - (4) the procedures in place at a *firm* to calculate its VaR model based *PRR*.
- 9 G The *FSA* recognises that the nature of VaR models will vary across *firms*. The scope of and the conditions set out in a VaR model *waiver* may therefore differ in substance or detail from the matters described in this appendix in order to address individual circumstances adequately. For example, a VaR model *waiver* may also include additional conditions to meet the particular circumstances of the *firm* or the model.
- 10 G If the *firm* ceases to meet any of these standards, the *FSA's* policy is that the *waiver* should cease to have effect. In many cases the ongoing need to meet these standards will be included in the *waiver* direction by imposing certain conditions. Even if they are not formally included as conditions, the *FSA* is likely to consider revoking the *waiver* if the standards are not met.
- 11 G The VaR Model Waiver Application and Review section of this appendix sets out the *FSA's* general policy on the VaR model application and review process and the conditions that the *FSA* may impose relating to alterations of the model.
- 12 G As explained in *SUP* 8.3.1G, *wavers* permitting the use of models in the calculation of *PRR* will not be granted if that would be contrary to the CAD, and any *waiver* which is granted will only be granted on terms that are compatible with the CAD. The *FSA* considers it unlikely that it will deviate from this approach even where the *firm* making the *waiver* application is not subject to CAD. Accordingly, the *FSA* is likely to grant only *wavers* permitting the use of models that are of the same nature as CAD1 and VaR models.

#### SCOPE OF VAR MODELS

- 13 G This appendix sets out the *FSA's* policy on the scope of a VaR model *waiver* and the manner in which the outputs of the model will be incorporated in the calculation set out in 10-80(2). Some of the standards described in this appendix may also be reflected in conditions attached to a VaR model *waiver*.
- 14 G A VaR model will be expected to cover one or more of the following types of risk category:
- (1) interest rate general market risk;
  - (2) interest rate specific risk (in conjunction with interest rate general market risk);
  - (3) *equity* general market risk;
  - (4) *equity* specific risk (in conjunction with equity general market risk);
  - (5) foreign-exchange risk; and
  - (6) *commodity* risk.
- 15 G It is the *FSA's* view that, where a *firm* uses a VaR model for one risk category, it is good practice to extend its model over time to calculate all of its *PRR* risk categories.
- 16 G For the purposes of 10-80(2)R, where a combination of the standard *PRR* rules, CAD1 model and VaR model approaches is used the *PRR* from each method should be added together. A *firm* should take appropriate steps to ensure that all of the approaches mentioned are applied in a consistent manner. For example, where the *PRR* for a particular portfolio is normally calculated using a VaR model, it should not switch between the standard market risk rules and a VaR model approach purely to achieve a more attractive *PRR*.
- 17 G A *firm* will not be required to capture immaterial risk or the market risk inherent in new products in a VaR model. If a *firm* does not capture immaterial risks or the market risk inherent in a new product in a VaR model, then the appropriate standard *PRR* rules to these risks will apply.

#### The VaR model waiver application and review process

- 18 G Details of the general *waiver* process are set out in *SUP* 8. Because of the complexity of a VaR model recognition *waiver*, it is recommended that, as set out in *SUP* 8.3.3G, a *firm* discusses its proposed application with its usual contact at the *FSA*. It should also be noted that the *waiver* recognition process in the case of VaR model recognition *waivers* is likely to take longer than the time-scale guidance set out in *SUP* 8.3.3G.
- 19 G In order for a VaR model recognition *waiver* to be granted, the *FSA* is likely to undertake a review to ensure that it is adequate and appropriate for the *PRR* calculation.

- 20 G The VaR model review process may be conducted through a series of visits covering various aspects of a *firm's* control and IT environment. Before these visits the *FSA* may ask that the *firm* provides some information relating to the *firm's waiver* request accompanied by some specified background material. The VaR model review visits are organised on a timetable that allows the *firm* being visited sufficient time to arrange the visit and provide the appropriate pre-visit information.
- 21 G As part of the of the VaR model review process the following may be reviewed: organisational structure and personnel; details of the *firm's* market position in the relevant products; profit and risk information; valuation and reserving policies; operational controls; IT systems; model release and control procedures; risk management and control framework; risk appetite and limit structure and future developments relevant to model recognition.
- 22 G A visit will usually involve the *FSA* wishing to meet senior management and staff from the front office, financial control, risk management, operations, systems development, information technology and internal audit areas.
- 23 G The *FSA* may complement its own review of a VaR model *waiver* request with one or more reviews by a *skilled person* under section 166 of the *Act*. Such a review may also be used where a VaR model *waiver* has been granted to ensure that the standards on which a VaR model *waiver* was based continue to be met.
- 24 G As set out in 9G the *FSA* will issue a *waiver* containing certain conditions. These conditions are likely to cover the standards described in this appendix to the extent that they are relevant to the circumstances, and may set out:
- (1) the details of the calculation of VaR model based *PRR*, which will contain the multiplication factor to be applied;
  - (2) the method of separating out specific risk if appropriate;
  - (3) the method agreed of calculating profit and loss accounts for backtesting purposes;
  - (4) the circumstances in which model refinements, new products, new markets and new locations should be notified to the *FSA*;
  - (5) any notification requirements relating to the VaR model *waiver*;
  - (6) any additional reporting requirements (e.g. electronic reporting of backtesting results);
  - (7) details of the changes to the VaR model which would be considered material by the *FSA*; and
  - (8) any other conditions attached to the VaR model *waiver*.
- 25 G Where a VaR model used outside of the United Kingdom differs from that used in the United Kingdom a *firm* the *FSA* may request details on the reasons for using different models.

- 26 G Where a *firm* operates any part of its VaR model outside of the United Kingdom, the *FSA* may take into account the results of the home supervisor's VaR model review. The *FSA* may wish to receive information directly from the home supervisor.

#### MAINTENANCE OF VaR MODEL WAIVER

- 27 G No changes may be made to a VaR model which is the subject of a *waiver* direction, unless the change is not material. Material changes to a VaR model will require a renewed *waiver* to be issued. Materiality is measured against the VaR model as it was at the time that the *waiver* was originally granted or, if the *waiver* has been varied in accordance with section 148 of the *Act*, as it was at the time of that variation. If a *firm* is considering making material changes to its VaR model then it should notify the *FSA* at once.
- 28 G If the VaR model ceases to meet the conditions of the *waiver*, a *firm* should notify the *FSA* at once. The *FSA* is likely then to revoke the *waiver*, unless it is varied in accordance with section 148 of the *Act*.

#### Risk management standards

- 29 G A *firm* with a complex portfolio is expected to demonstrate more sophistication in its modelling and risk management than a *firm* with a simple portfolio. For example, a *firm* will be expected to consider, where necessary, varying degrees of liquidity for different risk factors, the complexity of risk modelling across time zones, product categories and risk factors. Some trade-off is permissible between the sophistication and accuracy of the model and the conservatism of underlying assumptions or simplifications.
- 30 G A *firm* should be able to demonstrate that it meets the risk management standards set out in this section on a legal entity basis. This is particularly important for subsidiaries of *groups* subject to matrix management where the business lines cut across legal entity boundaries.
- 31 G A *firm* should have a conceptually sound risk management system surrounding the use of a VaR model which is implemented with integrity and should meet the following minimum standards:
- (1) the VaR model should be fully integrated into the daily risk management process of the *firm*, and serve as the basis for reporting risk exposures to senior management of the *firm*;
  - (2) a *firm* should have a risk control unit which is independent from business trading units, and which reports directly to senior management. The unit should be responsible for designing and implementing the *firm's* risk management system. It should produce and analyse daily reports on the output of the model and on the appropriate measures to be taken in terms of the trading limits;

- (3) a *firm's* directors and senior management should be actively involved in the risk control process, and the daily reports produced by the risk control unit should be reviewed by a level of management with sufficient authority to enforce both reductions of positions taken by individual traders as well as in the *firm's* overall risk exposure;
- (4) a *firm* should have sufficient numbers of staff skilled in the use of sophisticated models in the trading, risk control, audit and back office areas;
- (5) a *firm* should have established procedures for monitoring and ensuring compliance with a documented set of appropriate internal policies and controls concerning the overall operation of the risk measurement system;
- (6) a *firm's* VaR model should have a proven track record of acceptable accuracy in measuring risk;
- (7) a *firm* should conduct a programme of stress testing frequently, and the results of these tests should be reviewed by senior management and reflected in the policies and limits set;
- (8) a *firm* should have procedures to ensure that the valuation of assets and liabilities is appropriate, and that valuation uncertainty is identified and appropriate reserving is undertaken where necessary; and
- (9) at least once a year, a *firm* should conduct, as part of its regular internal audit process, a review of its risk management process. This review should include both the activities of the business trading units and of the independent risk control unit, and should be undertaken by suitably qualified staff independent of the areas being reviewed. This review should consider, at a minimum:
  - (a) the adequacy of the documentation of the risk management system and process;
  - (b) the organisation of the risk control unit;
  - (c) the integration of market risk measures into daily risk management and the integrity of the management information system;
  - (d) the process for approving risk pricing models and valuation systems used in front and back offices;
  - (e) the validation of any significant changes in the risk management process;
  - (f) the scope of risks and products captured by the VaR model;
  - (g) the accuracy and completeness of position data;
  - (h) the process used to ensure the consistency, timeliness, independence and reliability of data sources;
  - (i) the accuracy and appropriateness of volatility and correlation assumptions;

- (j) reserving policies, the accuracy of the valuation procedures, and risk sensitivity calculations;
  - (k) the process employed to evaluate the VaR model's accuracy, including the programme of backtesting;
  - (l) the controls surrounding VaR model development; and
  - (m) the process employed to produce the VaR model based *PRR*.
- 32 G A *firm's* VaR model output should be an integral part of the process of planning, monitoring and controlling a *firm's* market risk profile. The VaR model should be used in conjunction with internal trading and exposure limits. The links between these limits and the model should be consistent over time and understood by senior management.
- 33 G A *firm* should have adequate VaR model validation procedures to assess its model, and should have procedures in place to ensure that both the assumptions and approximations underlying the model and the limits of the model are appropriate. It should undertake testing of the accuracy of parts of the VaR models as well as the whole model. The *FSA* will require a period of initial monitoring or live testing before a VaR model can be recognised. Backtesting should be regarded as an additional safeguard rather than the primary model validation tool. A *firm* should therefore ensure that it has appropriate methods of assessing model validity and does not rely purely on the results of backtesting.
- 34 G In assessing whether the VaR model is implemented with integrity, the *FSA* will consider in particular the IT systems used to run the model and associated calculations. The assessment may include:
- (1) feeder systems; risk aggregation systems; time series databases; the VaR model system; stress testing system; the backtesting system including profit & loss cleaning systems where appropriate; data quality; reconciliations and checks on completeness of capture;
  - (2) system development, change control and documentation; security and audit trails; system availability and contingency procedures; network adequacy; and
  - (3) operational statistics relating to VaR model production process; examples of these statistics are timeliness, number of re-runs required and the reliability of data feeds.
- 35 G It is the responsibility of a *firm's* own management to ensure the accuracy and integrity of its VaR model. This responsibility includes obtaining appropriate independent validation of the VaR model.
- 36 G A *firm* should ensure that it has adequate controls surrounding:
- (1) the derivation of the VaR model based *PRR*;
  - (2) the integrity of the backtesting programme, including the calculation of the profit and loss account;

- (3) the integrity and appropriateness of the VaR model, including the model's geographic coverage and the completeness of data sources;
- (4) the VaR model's initial and ongoing development, including independent validation;
- (5) the valuation models, including independent validation; and
- (6) the adequacy and security/integrity of the IT infrastructure.

#### Model standards

- 37 G A *firm* should base its *PRR* calculation on the output of the VaR model which is used for its internal risk management rather than one developed specifically to calculate its *PRR*.
- 38 G The *FSA* accepts that the scope and nature of VaR models varies across *firms*. This means that different *firms* are likely to calculate different estimates of market risk for the same portfolio. Systematic differences are due to length of data series, choice of methodology (historical or Monte Carlo simulation or variance-covariance method or a hybrid of these), differences in aggregating risks within and across broad risk factors, the treatment of *options* and other non-linear products and the specification of risk factors.
- 39 G A *firm* that chooses to apply for a *waiver* to use a VaR model for the calculation of its *PRR* should calculate its market risk using the appropriate model parameters as set out in 40G.
- 40 G A *firm* should calculate its market risk by adopting the following minimum standards:
- (1) VaR should be calculated at least daily, using a 99% one-tailed confidence limit.
  - (2) VaR should be calculated using a holding period equivalent to ten *business days*.
  - (3) VaR measures should be based on an effective historical observation period of at least one-year, except where a shorter observation period is justified by a significant change in price volatility. If a weighting scheme or other method is used, then the effective observation period should be at least one year. The weighted average time lag of the individual observations should not be less than six months.
  - (4) Data sets should be updated no less frequently than quarterly, and more frequently whenever market prices are subject to material change.
- 41 G A *firm* may meet the appropriate model parameter requirement by using different model parameters and employing a suitable adjustment mechanism to produce a VaR figure which is equivalent to the figure produced using the parameters set out in 40G. For example, a *firm's* own model may use a 95% one-tailed confidence limit, but a mechanism to convert the output of the model to reflect a 99% one-tailed confidence limit should be employed.

## RISK FACTORS

- 42 G A VaR model should capture and accurately reflect, on a continuing basis, all material general market risks and, where a VaR model *waiver* has been granted in relation to specific risk, specific risks arising on the underlying portfolio, and should ensure that sufficient risk factors are properly specified.

## GENERAL MARKET RISK

- 43 G A *firm's* VaR model should capture a sufficient number of risk factors in relation to the level of activity of the *firm*, in particular the following:
- (1) For interest rate risk, the VaR model should incorporate a set of risk factors corresponding to the interest rate curves in each currency in which the *firm* has interest rate sensitive positions. A *firm* should ensure that it captures the variations of volatility of rates along the yield curve. In order to achieve this, a *firm* should divide the yield curves of, at a minimum, the major currencies and markets where it has material interest rate exposures into a minimum of six maturity segments. The risk measurement system should also capture the risk of less than perfectly correlated movements between different yield curves.
  - (2) For foreign exchange risk, the VaR model should incorporate risk factors corresponding to the individual foreign currencies, including gold, in which the *firm's* positions are denominated.
  - (3) For *equity* risk, the VaR model should use a separate risk factor at least for each of the *equity* markets in which the *firm* has material exposures.
  - (4) For *commodity* risk, the VaR model should use a separate risk factor at least for each *commodity* in which the *firm* has material exposures. The VaR model should capture the risk of less than perfectly correlated movements between similar, but not identical, *commodities* and the exposure to changes in forward prices arising from maturity mismatches. It should also take account of market characteristics, notably delivery dates and the scope provided to traders to close out positions.
  - (5) A *firm* that deals in *options*, or products with *option*-like characteristics, should ensure that their VaR model captures non-linear risk. Steps should also be taken to ensure that adequate capital is set aside for any other risks not captured by the model. *Firms* are reminded that, under 42G, the standard *PRR* rules may instead be applied to these risks.
  - (6) Correlations within and between the risk factors in (1) to (4) may be used provided the system for measuring these correlations is sound and implemented with integrity.

## SPECIFIC RISK

- 44 G Where a *firm* wishes to use a VaR model in relation to specific risk it should meet the following additional standards:



- (1) The model on which the VaR estimate is based should explain the price variation in the portfolio. For example, the VaR model may be based on a factor model or on a historical simulation model. The ability of the model to explain price variation could be demonstrated by a statistical comparison over the same period of time between actual price changes on the portfolio and the profit and loss impact of risk factors included within the model. A *firm* may wish to include an estimate of residual variation not explained by the model.
  - (2) The VaR model should be sensitive to changes in the level of concentration risk in the portfolio.
  - (3) The VaR model should be robust to an adverse environment.
  - (4) Where a *firm* calculates its specific risk surcharge under 78G(2) it should conduct specific risk backtesting for the traded debt portfolio and the *equity* portfolio separately. Specific risk backtesting is a comparison of the specific risk VaR measures against the corresponding actual P&L for sub-portfolios that contain material specific risk.
  - (5) The VaR model should be validated through empirical testing appropriate to the level of complexity and the assumptions made in the VaR model, which should be aimed at assessing whether specific risk is being adequately captured. Where specific risk is identified by examining relevant sub-portfolios, then these should be chosen in a consistent manner.
- 45 G A *firm* should have means to assess and, if necessary, mitigate or control event risk. For example, possible means include stress-testing procedures, or reserving policies. It is not however necessary to include factors to model event risk within a specific risk model unless warranted by the nature of the portfolio.

#### Stress testing and backtesting

##### STRESS TESTING

- 46 G Stress testing should involve identifying market scenarios or other low probability events in all types of risks that generate the greatest losses on a *firm's* portfolio.
- 47 G A *firm* should periodically and actively identify all the worst case scenarios that are relevant to its portfolio. Scenarios used should be appropriate to test the effect of adverse movements in market volatilities and correlations and the effect of any change in the assumptions underlying the VaR model. Scenarios involving low probability market events should nevertheless be plausible.
- 48 G A *firm* should have procedures to assess and respond to the results produced from stress testing. In particular, stress testing results should be:
- (1) used to evaluate its capacity to absorb such losses or identify steps to be taken to reduce risk.
  - (2) communicated routinely to senior management and periodically to the directors.

- 49 G Stress testing should capture non-linear effects.
- 50 G A *firm* should have the capacity to run daily stress tests. A *firm* may want to conduct the more complex stress tests at longer intervals or on an ad hoc basis.

#### BACKTESTING

- 51 G Backtesting is the process of comparing VaR risk measures to portfolio performance. It is intended to act as one of the mechanisms for the ongoing validation of a *firm's* VaR model and to provide incentives for *firms* to improve their VaR measures.
- 52 G Backtesting is only one method of assessing the performance of a VaR model and, although *firms* are required to carry out a backtesting programme, they should adopt other methods of measuring performance as well.
- 53 G Before a *waiver* will be granted to use a VaR model, a *firm* should have a backtesting programme in place and should provide three months of backtesting history.
- 54 G A *firm* should have the capacity to analyse its daily profit and loss account and compare the results to the VaR measure used for backtesting, both at the level of the whole portfolio covered by the VaR model and at the level of individual books that contribute material amounts to risk or the profit and loss account.
- 55 G VaR models are likely to undergo almost continuous refinements. This may make it difficult to backtest using 250 days' data if it is based upon a previous version of the model. If a refinement is not regarded as material, then a *firm* may use the last 250 days' data for backtesting purposes.
- 56 G A *firm* should compare each of its 250 most recent *business days'* profit and loss account figures with the corresponding one-day VaR measures. This comparison should be made daily using a rolling 250-day period.
- 57 G The VaR measure used for backtesting for these purposes should be calibrated to a one-day holding period and a 99% one-tailed confidence level, but otherwise the VaR model should be the same as that used to calculate the VaR model based *PRR*.
- 58 G The positions underlying the profit and loss account and VaR measures should not be materially different.
- 59 G If a *firm* uses a combination of the standard rules (and, where appropriate, CAD1 model) and VaR model approaches or does not model specific risk it should take appropriate steps periodically to ensure that this is taken into account in its backtesting procedures.
- 60 G An exception occurs each time a day's loss exceeds the corresponding VaR measure (at *firm* level). When an exception occurs, a *firm* should notify its supervisor by close of business two *business days* after the exception occurs (oral notification is acceptable).

- 61 G On a monthly basis, a *firm* should submit to the *FSA* a written account of the previous month's exceptions. The written account should include the cause of the exceptions and the *firm's* planned response. Nil returns will not be required.
- 62 G Where multiple exceptions occur, the multiplication factor used by a *firm* in its VaR model based *PRR* calculation should be increased by the appropriate plus factor set out in Table 63G (details of how the multiplication factor affects a *firm's* VaR model based *PRR* are set out in the Calculation of a VaR model based *PRR* section of this appendix). The table sets out the plus factor to be applied given the number of exceptions over the most recent 250 *business days*.
- 63 G Table: backtesting plus factors (see 62G)

Green	Fewer than 5	0.00
Yellow	5	0.40
	6	0.50
	7	0.65
	8	0.75
	9	0.85
Red	10	1.00

- 64 G The addition of a plus factor for VaR models that appear to be under-performing is designed to act as an incentive to ensure that the VaR model continues to perform well, and where it does not, that a *firm* takes prompt action to remedy the situation.
- 65 G If ten or more exceptions are recorded in a 250 day period, the *firm* should to take immediate corrective action. In these circumstances, the *FSA* may apply a plus factor greater than one, or the *FSA* may consider revoking a *firm's* VaR model *waiver*, unless it is varied in accordance with section 148 of the *Act*.
- 66 G If ten or more exceptions are recorded in a 250 day period due to the specific risk backtesting required in 44(4)G then the *firm* should take immediate corrective action on the specific risk part of the model or set aside additional capital.
- 67 G If a *firm* believes an exception should be disregarded it should submit to the *FSA* a written explanation of why the exception occurred and why it would be appropriate to disregard it. An exception may be disregarded only in exceptional situations. One example of when an exception might properly be disregarded is when it has arisen as a result of a risk that is not captured in its VaR model but against which regulatory capital is already held.

- 68 G The *FSA* may also consider disregarding a backtesting exception where, in a period of high volatility, multiple backtesting exceptions occur before the data set is updated.
- 69 G During the first 250 days after a *firm* starts to use its VaR model to calculate its VaR model based *PRR* the policy in 62G relating to plus factors only applies to the period from the date that VaR model recognition is granted.

#### DEFINITION OF PROFIT AND LOSS ACCOUNT FOR BACKTESTING PURPOSES

- 70 G Backtesting should be performed using a measure of actual profit and loss.
- 71 G Actual profit and loss means the day's profit and loss account arising from the trading activities within the scope of the VaR model. This should exclude material non-market elements which might mask a loss. Such elements include *fees* and *commissions*, reserving which is not directly related to market risk and one-off marketing profits from new deals.
- 72 G Actual profit and loss should reflect any price adjustments arising from position reconciliation in accordance with a *firm's* written policies and procedures. These policies and procedures should include a documented method of assigning valuation adjustments to backtesting data, such that the amount and the date of adjustment is unambiguous.
- 73 G A *firm* should have the capacity to perform backtesting against hypothetical profit and loss. The *FSA* may require firms to produce this information upon request. Hypothetical profit and loss means profit and loss that would have occurred had the portfolio remained unchanged.
- 74 G VaR models are likely to undergo almost continuous refinements. This may make it difficult to backtest using 250 days' data if it is based upon a previous version of the model. If a refinement is regarded as material then a new *waiver* may be required to use a VaR model and the original *waiver* may be revoked (as set out in 28G). If a refinement is not material then a *firm* may use the last 250 days' data for backtesting purposes.

#### Calculation of VaR model based *PRR*

- 75 G The calculation of a *PRR* under the VaR model approach is set out in this section. A *firm* will be required by the *waiver* to add its VaR model based *PRR* to its other *PRRs* calculated under 10-80(2)R.
- 76 G A *firm's* VaR model based *PRR* on a daily basis is equal to the higher of:
- (1) its previous day's VaR number; and
  - (2) the average of its daily VaR measures on each of the preceding sixty *business days* multiplied by a multiplication factor (increased by the appropriate plus factor referred to in 63G).

- 77 G The multiplication factor to be used is specified by the *FSA* in the formal VaR model *waiver* direction as a condition of its use. The minimum multiplication factor that the *FSA* will set is 3, although a higher multiplication factor may be applied. This multiplication factor is the factor that should be used, unless the *waiver* has been varied in relation to this factor in accordance with Section 148 of the *Act*.

G The following equation expresses 76G and 77G mathematically:

$$PRR_{VaR} = \text{Max} \left( VaR_t, f \times \frac{1}{60} \sum_{i=0}^{59} VaR_{t-i} \right) + SR$$

$PRR_{VaR}$  is a *firm's* VaR model based *PRR*;

$VaR_t$  represents the previous day's VaR figure;

$VaR_{t-i}$  represents the VaR calculated for *i business days* earlier;

*f* is the multiplication factor referred to in 76(2)G and 77G;

*SR* is the specific risk surcharge which is only included in the calculation set out 78G where a *firm* has been granted a VaR model *waiver* in relation to specific risk. Details on the specific risk surcharge can be found in 79G to 80G.

- 78 G If the VaR model *waiver* granted enables a *firm* to calculate a specific risk *PRR* by the use of its VaR model then it should calculate its specific risk surcharge as either:

- (1) an amount equal to the specific risk portion of the VaR measure; or
- (2) an amount equal to the VaR measure of sub- portfolios that are subject to specific risk.

In both cases, the specific risk surcharge should be calculated as an average over the previous 60 *business days*.

- 79 G Where a *firm* calculates its specific risk surcharge using 78(1)G, then it should calculate specific risk for the purposes of calculating the surcharge as the difference between total value at risk and a measure of general market risk. In calculating general market risk for this purpose, positions that give rise to specific risk should be mapped to equivalent positions that bear general market risk only. In doing so, the following minimum standards should be adopted:

- (1) For *equities*, each position should be mapped to a factor that is representative of the national or international market to which they belong. For example, a stock may be mapped to a widely accepted broadly based stock market index for the country concerned.
- (2) For bonds, each position should be mapped using a reference interest rate curve for the currency concerned. The interest rate curves should be generally accepted by the market as broadly based reference curves for the currency concerned, for example, a government bond curve or a swap curve.

- 80 G Where a *firm* calculates its specific risk surcharge using 78(2)G, then the sub-portfolio structure should be identified in advance and any changes to the structure should be pre-notified to *FSA*. The sub-portfolios chosen should be those which contain positions that would produce a specific risk *PRR* under the standard rules approach

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(AMENDMENT NO 8) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power); and
  - (2) section 156 (General supplementary powers).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Interim Prudential sourcebook for investment businesses**

- D. Interim Prudential Sourcebook for investment businesses is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Amendment No 8) Instrument 2004.

By order of the Board  
20 May 2004

## **Annex**

### **Amendments to the Interim Prudential Sourcebook for investment businesses**

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Appendix 13(1) Defined terms for Chapter 13

...



connected  
person

- ~~(1) (in relation to the FSA's consideration of an application for, or of whether to vary or cancel, a Part IV permission) any person appearing to the FSA to be, or likely to be, in a relationship with the applicant or person given permission, which is relevant, in accordance with section 49(1) of the Act (*Persons connected with an applicant*);~~
- ~~(2) (in relation to the FSA's powers to gather information under section 165 of the Act (Authority's power to require information)) (as defined in section 165(11) of the Act) a person which has or has at any relevant time had the following relationship to an authorised person (A):~~
- ~~(a) it is a member of A's group;~~
  - ~~(b) it is a controller of A;~~
  - ~~(c) it is a member of a partnership of which A is a member;~~
  - ~~(d) it is or has been an employee of A;~~
  - ~~(e) if A is a company it is or has been:~~
    - ~~(i) an officer or manager of A or of a parent undertaking of A; or~~
    - ~~(ii) an agent of A or of a parent undertaking of A;~~
  - ~~(f) if A is a partnership, it is or has been a member, manager, or agent of A;~~
  - ~~(g) if A is an unincorporated association of persons which is neither a partnership nor an unincorporated friendly society, it is or has been an officer, manager, or agent of A;~~
  - ~~(h) if A is a friendly society, it is or has been an officer or manager of A as defined in section 119(1) of the Friendly Societies Act 1992;~~
  - ~~(i) if A is a building society, it is or has been an officer of A as defined in section 119(1) of the Building Societies Act 1986;~~
  - ~~(j) if A is an individual, it is or has been an agent of A;~~
- ~~(3) (in relation to the FSA's powers of investigation under section 171 and 172 of the Act) (Powers of persons appointed under section 167; Additional power of persons appointed as a result of section 168(1) or (4)) (as defined in section 171(4) of the Act) a person which has or has at any relevant time had the following relationship to a person under investigation (P):~~
- ~~(a) it has the relationship specified in any of paragraphs (2) (a) to (j) inclusive to P (where references in those paragraphs to A are taken to be references to P);~~
  - ~~(b) it is a partnership of which A is a member;~~
  - ~~(c) it is the partner, manager, employee, agent, appointed representative, banker, auditor, actuary or solicitor of:~~
    - ~~(i) A;~~
    - ~~(ii) a parent undertaking of A;~~
    - ~~(iii) a subsidiary undertaking of A;~~
    - ~~(iv) a subsidiary undertaking of a parent undertaking of A; or~~
    - ~~(v) a parent undertaking of a subsidiary undertaking of A.~~

connected  
person

in relation to a *person*,

- (a) its *controller*;
- (b) a partner in it, or his or its partner;
- (c) a director of it;
- (d) its employee (whether under a contract of service or a contract for services) or an employee of its *appointed representative*;
- (e) another *undertaking* having the same *controller* as that *person*;
- (f) an *undertaking* which is an *associate* of that *person*;
- (g) (if the *person* is not a *body corporate*)
  - (i) a *close relative* of any *person* within (a) to (d) above; or
  - (ii) a *body corporate* controlled by that *person* or by any partner of that *person*; or
- (h) a trustee of a trust (other than an *occupational pension scheme*) the beneficiaries of which the *firm* knows or ought to know include any individual within (a) to (d) or (g)(i) above.

material  
holding

means a holding of -

- (a) ordinary share capital and non cumulative preference share capital; or
- (b) subordinated loan and non fixed-term cumulative preference share capital, in a *credit institution* or a *financial institution* where -
  - (i) (a) or (b) above exceeds 10% of the share capital plus share premium of the issuer; or
  - (ii) the aggregate of (a) and (b) above exceeds 10% of the *firm's own funds*, before deducting the holding.

## LONG-TERM CARE INSURANCE CONTRACTS INSTRUMENT 2004

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 141 (Insurance business rules);
  - (3) section 145 (Financial promotion rules);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### **Commencement**

- C. This instrument comes into force as follows:
- (1) Part B of Annex E comes into force on 31 October 2004 and ceases to have effect on 13 January 2005;
  - (2) Part C of Annex E comes into force on 14 January 2005; and
  - (3) the remainder of this instrument comes into force on 31 October 2004.

### **Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with Annex A to this instrument.

### **Amendments to the Insurance: Conduct of Business sourcebook**

- E. The Insurance: Conduct of Business sourcebook is amended in accordance with Annex B to this instrument.

### **Amendments to the Training and Competence sourcebook**

- F. The Training and Competence sourcebook is amended in accordance with Annex C to this instrument.

### **Amendments to the Authorisation manual**

- G. The Authorisation manual is amended in accordance with Annex D to this instrument.

### **Amendments to the Glossary**

- H. The Glossary is amended in accordance with Annex E to this instrument.

### **Citation**

- I. This instrument may be cited as the Long-Term Care Insurance Contracts Instrument 2004.

By order of the Board  
20 May 2004

Amended by Addendum  
19 October 2004

Amended by Addendum  
5 November 2004

Amended by Addendum  
25 November 2004

## Annex A

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

Transitional provisions

...

COB TR1

(1)	(2) Material to which the transitional provision applies: The COB provisions in Table COB TR 2 with the labels indicated	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
1.0	<i>Extra time provisions</i>				
1.1	<i>ETPI</i>	R	Transitional Relief		
			<p>...</p> <p>(2) Paragraph (1) does not apply to the following:</p> <p>...</p> <p>(k) ...;</p> <p><u>(l) (from 31 October 2004) any rule in COB inserted or amended by the Long-Term Care Insurance Contracts Instrument 2004 and, in the case of an amendment, to the extent of such amendment.</u></p>	...	...
	...				

...

3.8.7 G ...

- (6) A firm which offers general insurance contracts, providing benefits for the policyholder's care in the event of the policyholder's disability or incapacity, should avoid using terms which state expressly or imply that the policy will be available for the policyholder to claim on in the long-term, that is, for any period beyond the expiry of the policy. So a general insurance contract should not be promoted as being capable of providing long-term care insurance for the policyholder in the long-term, and expressions such as "long-term care" and "lifetime care" should generally be avoided in relation to general insurance contracts. If a general insurance contract provides benefits over the long-term in the event of a claim being made, a firm should make clear that the long-term aspect relates only to the availability of benefits in the event of a claim, not to the duration of the policy itself.

...

5.3.13 G ...

- (4) COB 5.3.29G contains guidance which is relevant for assessing the suitability of:

...

- (f) ISA or PEP transfers;~~and~~
- (g) contracting out of SERPS; and
- (h) borrowing to invest.

...

5.3.29 G Table Guidance on matters which should be taken into account when assessing the suitability of ...

...

H Borrowing to invest

When considering the suitability of a particular investment product which is linked directly or indirectly to any form of loan or mortgage, a firm

- (a) should take account of the source of the funds being invested and the suitability of the overall transaction; and

- (b) must follow any relevant suitability and other rules in COB and MCOB.

For example, the circumstances in which a recommendation to enter into a regulated lifetime mortgage contract and invest the funds into a long-term care insurance contract might be appropriate are limited, and both COB 5.3 and MCOB 8.5 apply.

...

- 6.2.16A R (1) When a long-term care insurance contract which is
- (a) not a pure protection contract and which was issued on or after 1 January 1995; or
- (b) a pure protection contract and which was issued on or after 31 October 2004;

is varied so as to bring into effect provisions for long-term care benefits, the firm must provide the private customer with appropriate key features in good time sufficient to enable the private customer to consider them before the variation takes effect.

- (2) If the circumstances of the variation, whether by the exercise of an option or otherwise, make it impossible to provide the key features before the variation takes effect, the firm must do so as soon as possible afterwards.

...

- 6.2.18 R When a *policyholder* applies to vary
- (1) a life policy issued before 1 January 1995; or
- (2) a pure protection contract issued before 31 October 2004 and which would after 30 October 2004 be a long-term care insurance contract ;

(or is personally recommended to do so) and the variation of the policy gives rise to a right to cancel under COB 6.7.7R, information must be given to the policyholder by the firm that is personally recommending, arranging or effecting the variation before it is put into effect, unless COB 6.2.19R applies. The firm must believe on reasonable grounds that the information given is sufficient to enable the policyholder to understand the consequences of the variation.

...

- 6.4.1 R COB 6.4 applies to a firm in accordance with COB 6.1.1R, in respect of occupational pension schemes, self invested personal pension schemes, income withdrawals, cash deposit ISAs, traded life policies, stakeholder pension schemes, packaged products, and other deposits and long-term care insurance contracts.

...

Long-term care insurance

6.4.29 R At each anniversary of the date on which a long-term care insurance contract which is based on single premium investment bonds was entered into, the insurer must:

- (1) provide the private customer with a table based on the format of COB 6.5.24R containing at least the current fund value and projected future policy values (as in the column "What you might get back");
- (2) where it is the case, inform the private customer of the possibility that future policy values may be insufficient to fulfil the original purpose of the contract; and
- (3) inform the private customer how to obtain advice on investments in respect of long-term care insurance contracts, and that it is in his best interest to do so.

6.4.30 G In the case of a long-term care insurance contract in which:

- (1) long-term care benefits are available after commencement of the policy at the option of the policyholder; and
- (2) as a result of the exercise of that option a new contract of insurance is offered to the policyholder;

provision is made in TC 2.5.5AR so that, in respect of the contract containing the option, an employee, although engaged in advising on long-term care insurance contracts need not be required to pass an appropriate examination for long-term care insurance contracts to do so.

...

6.5.14 G A firm might include information on the following under 'risk factors', when relevant:

...

- (14) ...;
- (15) ...; and
- (16) in the case of a long-term care insurance contract which is based on single premium investment bonds, the fact that the income produced by the bonds may be insufficient to continue to meet the premiums of the underlying contract of insurance. The description could also explain the consequences of this, including, if it is the case, that capital may be eroded, further single premiums may be payable, or the cover reduced.



6.5.15 R *A firm must include a projection, illustrating how the principal terms of the proposed transaction apply to the private customer:*

- (1) *where the proposed transaction is for a life policy (other than a long-term care insurance contract which is a pure protection contract); or*

...

6.5.16A G *A projection is not appropriate for a long-term care insurance contract which is a pure protection contract. Policy benefits and premiums must be illustrated in accordance with the relevant provisions of COB 6.5.49R.*

...

6.5.21 G The information required by COB 6.5.20R should include:

...

(3A) for a long-term care insurance contract, information to make policyholders aware of the importance of:

- (a) regularly reviewing their circumstances and the likely costs of long-term care with a view to ensuring that their long-term care needs continue to be appropriately covered; and
- (b) seeking advice in the event of change affecting the policyholder's long-term care needs, or in the event of a variation of the contract terms so as to provide long-term care benefits;

(3B) for a long-term care insurance contract in which the insurer has the right to review the premium:

- (a) a statement of that fact, the frequency of any right to vary the premium payable and a description of the circumstances which would give rise to a variation of the premium, for example, a change in claims experience;
- (b) a statement of the consequences of not paying any increased or extra premium resulting from any review, such as a reduction in policy benefits;
- (c) a statement of the rate of investment return assumed in the premium calculation together with a note of each other main assumption subject to variation;
- (d) a statement that the higher the assumed rate of investment return, the greater the chances of being asked to pay increased or extra premiums following a premium review;

(e) if the rate of investment growth assumed in the *premium* calculation is more than the intermediate rate shown in COB 6.6.50R, an illustration of the potential increased regular *premium* or additional single *premium* that may be payable following the first *premium* review, assuming that the rate of investment return achieved up to the review and assumed thereafter was at the intermediate rate shown in COB 6.6.50R;

(3C) for a *long-term care insurance contract* in which long-term care benefits are available after commencement of the *policy* at the option of the *policyholder*, a statement of the amount of *premium* payable for that option. Where any change to the level of cover requires further underwriting this should, where possible, be made clear at the outset.

(4) for a *long-term care insurance contract* which is based on single *premium* investment bonds -

...

6.5.25 R When completing COB 6.5.24R, a *firm* must:

...

(9) ~~in the case of a *long-term care insurance contract packaged product*~~ in the case of a *long-term care insurance contract* based on a single *premium* investment bonds, where the standard ten-year table does not illustrate adequately how the charges taken from a *policy* can increase considerably with age:

...

6.5.38 R A *firm* must include under the heading 'How much will the advice cost?' either the statement prescribed in (1), ~~or (1A)~~ or (1B), as applicable, or the information required by (2):

(1) for *life policies* (other than *long-term care insurance contracts* which are *pure protection contracts*) or *stakeholder pension schemes*: 'Your adviser will give you details about the cost. The amount will depend on the size of the *premium* and the length of the *policy* term. It will be paid for out of the deductions'; or

...

(1B) for *long-term care insurance contracts* which are *pure protection contracts*: 'Your adviser will give you details about the cost. The amount will depend on the size of the *premium* and the length of the *policy* term.'

...

Right to cancel

6.7.7 R A *customer*, who is an individual, has a right to cancel:

...

- (4) a variation of a *life policy, pension contract or stakeholder pension scheme* for which a right to cancel applies under *COB 6.7.23R, COB 6.7.23AR* and *COB 6.7.26AR*.

...

- 6.7.23 R (1) After an increase in regular or single *premiums* or payments (including a *pension transfer*) to a *life policy, pension contract or stakeholder pension scheme*, a *retail customer* has a right to cancel (see *COB 6.7.7R(4)*) in the following circumstances unless (2) applies:

...

- (b) ...; or
- (c) any variation where the increase represents the proceeds of a *pension transfer*; or
- (d) the variation of a long-term care insurance contract to provide long-term care benefits.

- 6.7.23A R When under a long-term care insurance contract, a new contract is issued to provide for long-term care benefits, a policyholder who is an individual has a right to cancel unless COB 6.7.23R(2) applies.

...

After *COB 8* insert the following new chapter, *COB 8A*:

8A Claims handling

8A.1 Application and purpose

Who and what ?

8A.1.1 R This chapter applies in respect of *claims handling* under *long-term care insurance contracts* to:

- (1) an *insurer*;
- (2) a *firm* acting on behalf of a *policyholder*; and
- (3) a *managing agent*.

8A1.2 R Throughout this chapter, references to an *insurer* apply equally to a *managing agent*.

8A1.3 G An *insurer* is responsible for *claims handling*. A *managing agent* is responsible for *claims handling* for *policies* underwritten at Lloyd's. An *insurer* or a *managing agent* remains responsible for *claims handling* if it outsources any of its *claims*-related activities, including where it gives an intermediary authority to *handle claims* on its behalf. An *insurer* or a *managing agent* is not responsible for the administration and performance activities that a *firm* carries out on behalf of a *policyholder* in connection with a *claim*. In relation to these activities, a *firm* which acts on behalf of *policyholders* should refer to COB 8A.3.

8A1.4 G An *insurer* should refer to the *rules* and *guidance* set out in SUP 2.3.5R to SUP 2.3.10G in respect of any *person* to whom it outsources its *claims handling* functions.

8A1.5 G This chapter applies to *claims* made by or on behalf of *policyholders*.

#### Purpose

8A.1.6 G (1) The purpose of this chapter is to ensure that:

- (a) *claims* are handled fairly;
- (b) *claims* are settled promptly;
- (c) *policyholders* are provided with information on the *claims handling* process and with an explanation of why a *claim* is rejected or not settled in full, where relevant; and
- (d) *firms* acting on behalf of *policyholders* disclose and manage any conflicts of interest that may exist.

(2) This chapter reinforces:

- (a) *Principle 3* (Management and control), which requires a *firm* to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems;
- (b) *Principle 6* (Customers' interests), which requires a *firm* to pay due regard to the interests of its *policyholders* and treat them fairly; and
- (c) *Principle 8* (Conflicts of interest), which requires a *firm* to manage conflicts of interest fairly, both between itself and its *policyholders* and between a *policyholder* and another *client*.

8A.2 Claims handling: general

#### Requirements to handle *claims* promptly and fairly

8A.2.1 R An *insurer* must carry out *claims handling* promptly and fairly.

8A.2.2 G When handling the *claim* of a *policyholder*, an *insurer* should comply with the *rules* and *guidance* in COB 8A.4.

8A.2.3 G An *insurer* should refer to the *guidance* in SYSC 3.2 (Areas covered by systems and controls) in its procedures for *claims handling*. For example, an *insurer* should have in place systems and controls which take account of reasonably foreseeable peaks in demand, to allow it to deal with *claims* promptly in such circumstances.

8A.2.4 G An *insurer* should refer to the *guidance* set out in TC 1 (Commitments) in respect of the competence of any *person* who carries out *claims handling* on its behalf.

#### Giving policyholders guidance on claiming

8A.2.5 R When an *insurer* is informed that a *policyholder* wishes to *claim* under his *policy* it must give the *policyholder* reasonable guidance to help him make a *claim* under his *policy*.

#### Rejecting or refusing claims

8A.2.6 R An *insurer* must not:

- (1) unreasonably reject a *claim* made by a *policyholder*;
- (2) except where there is evidence of fraud, refuse to meet a *claim* made by a *policyholder* on the grounds:
  - (a) of non-disclosure of a fact material to the risk which the *policyholder* could not reasonably be expected to have disclosed;
  - (b) of misrepresentation of a fact material to the risk unless the misrepresentation is negligent; or
  - (c) of breach of warranty, unless the circumstances of the *claim* are connected with the breach and unless:
    - (i) under a ‘life of another’ contract, the warranty relates to a statement of fact concerning the life to be assured and that statement would have constituted grounds for rejection of a *claim* by the *insurer* under COB 8A.2.6R(2)(a) or (b) if it had been made by the life to be assured under an ‘own life’ contract; or
    - (ii) the warranty is material to the risk and was drawn to the attention of the *policyholder* before the conclusion of the contract.

8A.3 Duties of firms acting on behalf of policyholders

8A.3.1 R COB 8A.3 applies to a *firm*.

8A.3.2 G COB 8A.3 will usually apply to a *firm* that is not an *insurer*, but it may also apply to an *insurer*, for example, if it were dealing with a *claim* on a *policy* insured by another *insurer*.

A firm's duty of care, skill and diligence

- 8A.3.3 R A *firm* when acting for a *policyholder* in relation to a *claim* must act with due care, skill and diligence.
- 8A.3.4 G The *rules* and *guidance* in COB 8A.3 do not seek to set out the full extent of the duties owed by *firms* to any *person* for whom they act, nor do they displace the general law on the duties of *agents*.

A firm's duty to avoid conflicts of interest

- 8A.3.5 R (1) A *firm* must not, in connection with any *claim*, put itself in a position where its own interest, or its duty to any *person* for whom it acts, conflicts with its duty to any *policyholder* for whom it acts, unless:
- (a) it made proper disclosure to that *policyholder* of all information needed to put the *policyholder* in a position where he can give informed consent to the arrangement; and
  - (b) it has obtained the prior informed consent of the *policyholder*.
- (2) A *firm* must decline to act for the *person* or *policyholder* referred to in (1), or any of them, unless in the particular circumstances of the case disclosure and informed consent are sufficient to enable it to reconcile the conflict.
- 8A.3.6 G COB 8A.3.5R imposes a requirement on a *firm* to avoid conflicts of interest in relation to *claims* where it acts on behalf of a *policyholder* unless it can manage them by disclosure to, and the obtaining of consent from, the *policyholder*.
- 8A.3.7 G A *firm* should consider whether it is possible to manage the conflict by disclosing the conflict to the *policyholder* and obtaining his consent. Where a *firm* acts for a *policyholder* in arranging a *policy*, it is likely to be the agent for the *policyholder* in connection with the preparation and handling of any *claim* against the *insurer*. If the *firm* intends to be the agent of an *insurer* in relation to *claims* under that *policy*, it will need to consider whether it is at risk of putting itself in the position where it cannot act without some breach of duty either to the *insurer* or the *policyholder*. The *firm* should consider whether disclosure and consent are sufficient to reconcile the conflicting obligations. An example of a circumstance in which disclosure and consent are unlikely to be sufficient and when a *firm* may well consider it should not act for the *insurer* or the *policyholder* or either, is where the *firm* knows that the *policyholder* will, to obtain a quick payment, accept a low amount in settlement of a *claim* and also knows the *insurer* is willing to settle for a higher amount.
- 8A.3.8 R If a *firm* acts for an *insurer* and not for a *policyholder* in relation to a *claim* on a contract which it *arranged* for that *policyholder*, the *firm* must inform the *policyholder* that, in relation to that *claim*, it is acting on behalf of the *insurer* and not the *policyholder*.

- 8A.3.9 G *COB* 8A.3.8R would apply, for example, where a *firm* has delegated authority for *claims handling* and deals with a *claim* in relation to a contract that is sold to a *policyholder*, if the *firm* is not acting on behalf of that *policyholder* in relation to the *claim*.
- 8A.3.10 R If a *firm* is notified of a *claim* in relation to a *policy* which it has *arranged*, and the *insurer* has not given it the authority to deal with that *claim*, it must:
- (1) forward the notification to the *insurer* promptly; or
  - (2) inform the *policyholder* immediately that it cannot deal with the notification.
- 8A.4 Policyholders: performance standards for handling claims
- Responding to notification of the claim
- 8A.4.1 R An *insurer* must respond promptly to a notification by a *policyholder* of a *claim*.
- 8A.4.2 G Notification of a *claim* is a demand of the *insurer* to pay or provide a benefit insured under the *policy*, for example, by submitting a *claim* form or giving the equivalent information orally, where permitted by the *policy*. An enquiry that precedes such a demand, for example, as to whether a particular loss is covered, and therefore whether a *claim* could be made under the terms of the *policy*, is not notification of a *claim*.
- 8A.4.3 G *COB* 8A.4.1R requires an *insurer* to respond promptly once it has received notification of a *claim*. Generally a prompt response would be one within *five business days* of a *policyholder* making a *claim*, although in some circumstances a prompt response could be less than *five business days*, such as where the *policyholder* would expect a swifter response because of the nature of the *claim* or the terms of the *policy*.
- 8A.4.4 R The response referred to in *COB* 8A.4.1 R must:
- (1) provide the information set out in *COB* 8A.4.5 R;
  - (2) be in a *durable medium*, unless the notification by the *policyholder* is made orally and the *insurer* does not require the *policyholder* to complete a *claim* form; and
  - (3) provide the *policyholder* with a *claim* form, if the *insurer* requires one to be completed.
- 8A.4.5 R The information referred to in *COB* 8A.4.4 R (1) is:
- (1) that the *claim* relates to a risk that is clearly outside the scope of the *policy*, if that is the case (in which case no further information need be provided);

- (2) the action that will be taken by the *insurer* and when that action will be taken;
- (3) if the *insurer* is appointing any other parties to contact the *policyholder* on the *insurer's* behalf, in respect of each other party appointed the following information, if known (but, if the purpose of the appointment is to investigate the validity of a *claim*, the information need not be given if it would limit or prevent the effective investigation of the *claim* or any part of it):
  - (a) its name (unless the other party trades under the name of the *insurer*);
  - (b) its function; and
  - (c) the work it will carry out in relation to the *claim*.

8A.4.6 G The purpose of the *rules* and *guidance* in COB 8A.4.1R to COB 8A.4.5R is to provide the *policyholder* at an early stage with information in relation to the processing and settlement of his *claim* by the *insurer*. COB 8A.4.5R (1) is intended to prevent a *policyholder* pursuing a *claim* for which he is clearly not covered. It is not intended to pre-empt the outcome of an investigation of a *claim*.

8A.4.7 G The purpose of COB 8A.4.5R (3) is to ensure that a *policyholder* knows the name and function of any party who will contact him in relation to a *claim* as a representative of the *insurer*, for example, an outsourced *claims handling* company. An *insurer* would not be expected to notify the *policyholder* of other parties who are appointed to investigate the validity of a *claim* if this would limit or prevent an effective investigation. However, if a third party is appointed to liaise with the *policyholder* on the *insurer's* behalf, as well as assess the validity of the *claim*, the *insurer* would be expected to disclose the information in COB 8A.4.5R (3) unless it would limit or prevent an effective investigation.

#### Investigation and processing of the claim

8A.4.8 R An *insurer* must keep the *policyholder* reasonably informed about the progress of his *claim*.

8A.4.9 G Where the investigation of a *claim* is likely to be protracted, an *insurer* should provide periodic progress or status reports, when appropriate, to a *policyholder*, including providing the *policyholder* with any relevant update in relation to the information provided under COB 8A.4.4R. The *insurer* should also respond without undue delay to any reasonable request by the *policyholder* for information.

#### Determining the claim

8A.4.10 R An *insurer* must notify the *policyholder* as soon as practicable whether it:

- (1) rejects all of his *claim*;



- (2) rejects his *claim* but without prejudice to the rejection makes an offer in compromise; or
- (3) accepts all or part of his *claim*.

8A.4.11 R If the *insurer* rejects the *claim* but without prejudice to the rejection makes an offer in compromise, it must notify the *policyholder* of the terms of that offer as soon as practicable.

8A.4.12 R If the *insurer* accepts all or part of the *policyholder's claim*, it must notify the *policyholder* as soon as practicable whether:

- (1) as to the parts it accepts, it agrees to provide the money, property or service claimed by the *policyholder* in full; or
- (2) it makes some other offer in compromise. In that event, it must notify the *policyholder* of the terms of its offer.

8A.4.13 R (1) Unless the *insurer* accepts the *policyholder's claim* in full, the *insurer* must explain why it rejects all or part of the *policyholder's claim* or accepts his *claim* or makes a compromise offer, specifying any relevant term of the policy.

- (2) The *insurer* must offer the *policyholder* the choice of receiving the information at COB 8A.4.13R (1) in a *durable medium*.

8A.4.14 R The *insurer* must, in respect of each part of the *claim* which it accepts, inform the *policyholder* whether the *claim* will be settled by paying him, or by paying another *person* to provide goods or services, or by providing those goods or services.

#### Settling a claim

8A.4.15 R An *insurer* must settle a *claim* by a *policyholder* promptly.

8A.4.16 G (1) Settlement terms are agreed when:

- (a) the *insurer* accepts the *policyholder's claim*; and
- (b) the *policyholder* accepts the *insurer's* offer of settlement.

- (2) When the *insurer* settles the *claim* by paying the *policyholder*, the *insurer* should aim to make payment within five *business days* after the *insurer* and the *policyholder* have agreed settlement terms, subject to any pre-conditions laid down by the *insurer* or in law being met by the *policyholder*. This does not prevent the *insurer* paying a *claim* before the *policyholder* has finally agreed settlement terms.

- (3) The *guidance* in (2) will not apply if the *insurer* settles the *claim* by:

- (a) payment against a liability due on a future date;
- (b) the provision of goods or services;

- (c) making payments on a date specified by the *policyholder*; or
- (d) payment of the *claim* through another party (eg a care home) on a monthly or some other basis;

and in the case of (a) or (b) the *insurer* should make prompt payment or arrange for prompt provision of the goods or services after the *insurer* and the *policyholder* have agreed settlement terms.

8A.4.17 G The arrangements for settlement set out in COB 8A.4.16G (3)(b) apply to arrangements to supply goods or services to the *policyholder*. In such situations, the goods or services should be provided promptly but where they cannot be, the *insurer* should inform the *policyholder* when to expect them.

8A.4.18 G An *insurer* should note that unless it has previously informed a *policyholder* that a *claim* will not be met in full or in part until *premiums* have been paid, the *insurer* may not delay the payment of a *claim* on the grounds that *premiums* are outstanding.

#### Pre-Action Protocols

8A.4.19 G A *policyholder* who does not accept an *insurer's* rejection of his *claim* (or part of it) may challenge that rejection. If he chooses to do so through the courts, *firms* should be aware that, in England and Wales, there are pre-action protocols which lay down certain requirements as to the steps to be taken before proceedings are issued. This chapter does not displace these requirements, to which *firms* should have regard in the event that a rejection of a *claim* moves towards litigation.

#### 8A.5 Record keeping

8A.5.1 R An *insurer* must make and retain, for the duration of the *claim* and for a minimum of six years after the *insurer's* obligations to the *policyholder* under the *long-term care insurance contract* have ceased, the following information in relation to each *claim* made against a *policy* issued by it or handled by it:

- (1) details of the *claim*;
- (2) a record of each communication with the *policyholder* including the date on which it was made; and
- (3) the date the *claim* was settled or rejected and details of settlement or rejection including information relevant to the basis for the settlement or rejection.

12.1.15 R Table: This table applies *COB* to *firms* when carrying on the activity to which *COB* 12.1.7R (2) relates.

Chapter	Description	Application
...	...	...
<u>8A</u>	<u>Claims handling</u>	<u>Applied</u>

Schedule 1  
Record keeping requirements

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
<u>COB 8A 5.1</u>	<u>Claim under a long-term care insurance contract</u>	<u>Details of the claim; a record of each communication with the policyholder, including the date it was made; the date the claim was settled or rejected.</u>	<u>As soon as practicable</u>	<u>The duration of the claim and 6 years after the insurer's obligations to the policyholder under the long-term care insurance contract have ceased</u>
....				

## Annex B

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex, underlining denotes new text .

...

2.2.8      G    A firm which offers general insurance contracts, providing benefits for the customer's care in the event of the customer's disability or incapacity, should avoid using terms which state expressly or imply that the policy will be available for the customer to claim on in the long-term, that is, for any period beyond the expiry of the policy. So a general insurance contract should not be promoted as being capable of providing long-term care insurance for the customer in the long-term, and expressions such as "long-term care" and "lifetime care" should generally be avoided in relation to general insurance contracts. If a general insurance contract provides benefits over the long-term in the event of a claim being made, a firm should make clear that the long-term aspect relates only to the availability of benefits in the event of a claim, not to the duration of the policy itself.

...

...

3.8.3      G    ...

(8)    A firm which offers general insurance contracts, providing benefits for the customer's care in the event of the customer's disability or incapacity, should avoid using terms which state expressly or imply that the policy will be available for the customer to claim on in the long-term, that is, for any period beyond the expiry of the policy. So a general insurance contract should not be promoted as being capable of providing long-term care insurance for the customer in the long-term, and expressions such as "long-term care" and "lifetime care" should generally be avoided in relation to general insurance contracts. If a general insurance contract provides benefits over the long-term in the event of a claim being made, a firm should make clear that the long-term aspect relates only to the availability of benefits in the event of a claim, not to the duration of the policy itself.

## Annex C

### Amendments to Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

TC Table: Transitional Provisions relating to designated investment business  
1

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision : coming into force
7	<u>TC 2.4.1R (1) and (2), TC 2.4.5R, TC 2.7.5R</u>	<u>R</u>	(1) <u>This transitional provision applies in respect of an <i>employee</i> of a <i>firm</i> employed at 31 October 2004 to engage in or supervise the activities referred to at TC 2.1.4R 1(ha), if the <i>employee</i> has been assessed by the <i>firm</i> as competent to engage in or supervise the activities specified at TC 2.1.4R 1 (f) and those activities involve selling <i>contracts of insurance</i> which after 30 October 2004 would be <i>long-term care insurance contracts</i>, and that assessment is current as at 30 October 2004.</u>	<u>From 31 October 2004 to 30 October 2006</u>	<u>31 October 2004</u>
			(2) <u>A <i>firm</i> may for the purposes of TC 2.4.1R (1) and (2), TC 2.4.5R and TC 2.7.5R assess an <i>employee</i> described in (1) as competent to engage in or supervise the activities referred to at TC 2.1.4R 1(ha), without requiring the <i>employee</i> to pass an appropriate examination in <i>long-term care insurance</i> under TC 2.4.5 R or TC 2.7.5R (1), but only if the activity or role for that <i>employee</i> after 30 October 2004 is the same or substantially</u>		

			<u>the same as that in respect of which the <i>employee</i> had been assessed as competent at 30 October 2004.</u>		
			<p>(3) <u>If a <i>firm</i> has assessed an <i>employee</i> as competent under (1) and (2), any other <i>firm</i> which subsequently employs the individual may also assess him as competent on the same basis provided that:</u></p> <p>(a) <u>the activity which the <i>employee</i> engages in or supervises continues to be the same, or substantially the same, as that in respect of which the <i>employee</i> had been previously assessed as competent; and</u></p> <p>(b) <u>the individual has not experienced any significant break of relevant employment as described in (a) since the previous assessment.</u></p>		
<u>8</u>	<u>Paragraph 7 above</u>	<u>G</u>	<p><u>Until 30 October 2006, a <i>firm</i> may rely on paragraph 7 to assess as competent an <i>employee</i> who advises on or supervises those advising on <i>long-term care insurance contracts</i>, if that <i>employee</i> had been assessed by the <i>firm</i> as competent at 30 October 2004 to advise or supervise those advising on <i>investments</i> which would be, after 30 October 2004, <i>long-term care insurance contracts</i>, and the activity or role of that <i>employee</i> after 30 October 2004 remains the same or substantially the same as it was prior to that date.</u></p> <p><u>After 30 October 2006 a <i>firm</i> may not rely on paragraph 7 to assess an <i>employee</i> as competent: the <i>employee</i> must be assessed as competent and must have passed an appropriate examination on long</u></p>	<u>From 31 October 2004 to 30 October 2006</u>	<u>31 October 2004</u>

			<u>term care insurance if they are to advise on or supervise advising on long-term care insurance contracts.</u>		
9	<u>Paragraph 7 above</u>	G	<u>A firm which relies on paragraph 7 of this table in establishing the competence of an individual advising on or supervising those advising on long-term care insurance contracts should have regard to TC 2.6. In particular, a firm should keep under review the status of an employee deemed competent under paragraph 7 and consider whether an employee may no longer be competent to advise or supervise advising on long-term care insurance contracts (for example in the light of repeated failures to pass an appropriate exam).</u>	<u>From 31 October 2004 to 30 October 2006</u>	<u>31 October 2004</u>
...					

2.1.4 R Table: Activities to which TC2 applies

	Activity	Extent of Application
1. Employees engaging in:	...	...
	(f) <i>advising on investments</i> which are <i>packaged products</i> (other than <i>broker funds</i> or as in (g), <del>(h)</del> or (ha));	
	...	
	<u>(ha) advising on investments which are long-term care insurance contracts;</u>	

...

2.5.1A <sup>1</sup>	R	The time limits to which TC 2.5.1 applies	
		Activity in TC 2.1.4 R	Examination must be passed:
		1. (a) - (c)	before starting the activity
		(d) - (e)	within 30 months of starting the activity
		(f) - (g)	within two years of starting the activity

<sup>1</sup> The table at 2.5.1AR will become part of the Handbook from 1 July 2004 under the provisions of FSA 2004/26

		(h)	(no examination requirement)
		<del>(ha)(i)</del> - (l)	within two years of starting the activity
		(m) - (o)	before starting the activity
		(p) - (q)	within two years of starting the activity
		(r)	(no examination requirement)
		2. (a) - (g)	within two years of starting the activity

Exemption from an appropriate examination

...

2.5.5A R If a long-term care insurance contract provides that:

- (1) long-term care benefits are available after commencement of the policy at the option of the policyholder; and
- (2) as a result of the exercise of that option a new contract of insurance is offered to the policyholder;

an employee engaged in the activities referred to at TC 2.1.4R 1(ha) need not, in respect of the contract containing the option, be required to pass an appropriate examination for long-term care insurance contracts.

2.5.5B G TC 2.5.5AR applies to the situation where a contract contains an option for the policyholder to take out a second, separate contract and that second contract provides for long-term care benefits. Both contracts will be long-term care insurance contracts and subject to the rules applying to such contracts. However, TC 2.5.5AR provides that, where the two contracts are separate, an employee engaged in advising on the first contract (containing the option) need not be required to pass an appropriate exam for long-term care insurance. An employee advising on the second contract, which provides the long-term care benefits, must, however, have passed an appropriate exam for long-term care insurance.

2.5.6 G A firm should, for the purposes of TC 2.8.1R (Record keeping), make and retain records of the criteria governing its decision to apply ~~TC 2.5.5R to an employee.~~

- (1) TC 2.5.5R; or
- (2) TC 2.5.5AR;

to an employee.

...



Schedule 1  
Record keeping requirements

...

Table: Record keeping requirements

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
<u>TC 2.5.6G(1)</u>	Appropriate examinations - regulatory module only	Criteria for application of <u>TC 2.5.5R</u> to the <i>employee</i>	At the time of the application of the <i>rule</i>	For 3 years only after an <i>employee</i> ceases to engage in or oversee an activity or for PTS indefinite
<u>TC 2.5.6G(2)</u>	<u>Appropriate examinations</u>	<u>Criteria for application of TC 2.5.5AR to the employee</u>	<u>At the time of the application of the rule</u>	<u>For 3 years only after an employee ceases to engage in or oversee an activity or for PTS indefinite</u>
...				

## Annex D

### Amendments to the Authorisation sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.6.28 G Rights to, or interests in, all the *specified investments* in AUTH 2.6 (except rights to, or interests in, rights under a regulated mortgage contract) are themselves treated as *specified investments*. The effect is that, in most cases, an activity carried on in relation to rights or interests derived from any of those *investments* is also a *regulated activity* if the activity would be regulated if carried on in relation to the *investment* itself. The exception is where the rights or interests relate to a *pure protection contract* or a *general insurance contract*.

...

2.9.8 G Broadly speaking, the exclusions focus on cases where the main business of a *person* is to sell goods or supply services but where certain activities may have to be carried on for the purposes of that business which would otherwise be *regulated activities*. The exclusions are not available where the customer to whom goods are sold or services are supplied is an individual. They are also not available where what is at issue is a transaction entered into, or service provided, in relation to rights under a ~~*life policy contract of insurance*~~ or units in a *collective investment scheme* (or rights to, or interests in, either).

...

AUTH 2 Annex 2

...

AUTH Table:

3 Notes to Table 1

...

Note 5B:

*Life policy* is the term used in the *Handbook* to mean ‘qualifying contract of insurance’ (as defined in Article 3(1) of the *Regulated Activities Order*), and except in COB 3, AUTH App 1 and AUTH App 5 the term also includes a *long-term care insurance contract* which is a *pure protection contract*.

...

AUTH Table:

5

Table 3: Securities, contractually based investments and relevant investments [see notes 1 and 2 to Table 3]		
SECURITY (ARTICLE 3(1))	CONTRACTUALLY BASED INVESTMENT (ARTICLE 3(1))	RELEVANT INVESTMENT (ARTICLE 3(1))
...	...	
	<i>life policy (but excluding a <u>long-term care insurance contract which is a pure protection contract</u>) [see note 5B to Table 1]</i>	...

## Annex E

### Amendments to the Glossary of definitions

In this Annex, underlining denotes new text and striking through denotes deleted text.

#### PART A

<i>claim</i>	(1) (in <i>COMP</i> ) a valid claim made in respect of a civil liability owed by a <i>relevant person</i> to the claimant.  (2) (in <u><i>COB</i></u> , <i>ICOB</i> , <i>LLD</i> , <i>SUP</i> and <i>TC</i> ) a claim under a <i>contract of insurance</i> .
<u><i>claims handling</i></u>	<u>(in <i>COB</i>) in relation to a claim under a long-term care insurance contract, carrying out the contract (by an <i>insurer</i>) or paying or declining to pay a claim on behalf of a member (by a <i>managing agent</i>).</u>
<i>contractually based investment</i>	(in accordance with article 3(1) of the <i>Regulated Activities Order</i> (Interpretation)):  (a) a <i>life policy</i> <u>(except a long-term care insurance contract which is not a qualifying contract of insurance)</u> ;  (b) an <i>option, future, contract for differences or funeral plan contract</i> ;  (c) <i>rights to or interests in an investment</i> falling within (a) or (b).
<i>designated investment</i>	a <i>security</i> or a <i>contractually-based investment</i> (other than a <i>funeral plan contract</i> and a <i>right to or interest in a funeral plan contract</i> ), that is, any of the following <i>investments</i> , specified in Part III of the <i>Regulated Activities Order</i> (Specified Investments), <u>and a long-term care insurance contract which is a pure protection contract</u> :  ...  (l) <i>rights to or interests in investments</i> in (a) to (k) (article 89) <u>but not including rights to or interests in rights under a long-term care insurance contract which is a pure protection contract</u> .
<i>designated investment business</i>	...  (ea) <u>assisting in the administration and performance of a contract of insurance, but only if the contract of insurance is a designated investment</u> .  ...

*life policy*

- (1) (except in *COB*, *AUTH App 1* and *AUTH App 5*):
  - (a) (in accordance with the definition of "qualifying contract of insurance" in article 3(1) of the *Regulated Activities Order*) a *long-term insurance contract* other than a reinsurance contract and a *pure protection contract*; or
  - (b) a *long-term care insurance contract*.
- (2) (in *COB* except COB 3):
  - (a) a *long-term insurance contract* in (1) or
  - (b) a *pension policy*.
- (3) (in COB 3, *AUTH App 1* and *AUTH App 5*) a *long-term insurance contract* in (1) (a) or a *pension policy*.

PART B

long-term care  
insurance contract

(in accordance with article 1 of the Financial Services and Markets Act 2000 (Regulated Activities) (Amendment) (No 2) Order 2003) a contract of insurance in respect of which the following conditions are met:

- (a) the purpose (or one of the purposes) of the policy is to protect the policyholder against the risk of becoming unable to live independently without assistance in consequence of a deterioration of mental or physical health, injury, sickness or other infirmity;
- (b) benefits under the contract are payable in respect of:

  - (i) services;
  - (ii) accommodation; or
  - (iii) goods;

which are (or which is) necessary or desirable due to a deterioration of mental or physical health, injury, sickness or other infirmity;
- (c) the contract is expressed to be in effect until the death of the policyholder (except that the contract may give the policyholder the option to surrender the policy); and
- (d) the benefits under the contract are capable of being paid throughout the life of the policyholder.

PART C

long-term care  
insurance contract

a long-term insurance contract which:

- (a) (i) provides (or would at the *policyholder's* option provide) benefits for the *policyholder* which are payable or provided in the event that the *policyholder's* mental or physical health has deteriorated to the extent that he is incapacitated so that he is unable to live independently without assistance, and is not expected to recover to the extent that he can live independently without assistance; and
  - (ii) those benefits are payable or provided in respect of:
    - (A) services;
    - (B) accommodation; or
    - (C) goods;

which are necessary or desirable for the continuing care of the *policyholder* because of the incapacity referred to in (i); and
  - (iii) the benefits under the contract are capable of being paid periodically for all or part of the period during which the *policyholder* is unable to live independently without assistance;
- or
- (b) is sold or held out as providing benefits for the *policyholder* as set out in (a).

**ADDENDUM**

**LONG-TERM CARE INSURANCE CONTRACTS INSTRUMENT 2004**

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex A of this instrument is amended as follows:

...

...

Long-term care insurance

6.4.~~2932~~2932 R At each anniversary of the date on which a *long-term care insurance contract* which is based on single *premium* investment bonds was entered into, the *insurer* must:

...

6.4.~~3033~~3033 G In the case of a *long-term care insurance contract* in which:

...

...



## ADDENDUM

### LONG-TERM CARE INSURANCE CONTRACTS INSTRUMENT 2004

This addendum inserts new text into this instrument to reflect the Handbook text previously introduced by an earlier instrument, FSA 2004/39.

Annex A to this instrument is amended by deleting the text in COB 6.2.18R in its entirety and replacing it with text which is not underlined. Otherwise, underlining indicates new text and striking through indicates deleted text.

- 6.2.18 R (1) When a *policyholder* applies to vary:
- (a) a *life policy* issued before 1 January 1995; or
  - (b) a *pure protection contract* issued before 31 October 2004 and which would after 30 October 2004 be a *long-term care insurance contract*;  
  
(or is *personally recommended* to do so) and the variation of the *policy* gives rise to a right to cancel under COB 6.7.7R, information must be given to the *policyholder* by the *firm* that is *personally recommending*, arranging or effecting the variation before it is put into effect, unless COB 6.2.19R or COB 6.4.27R to COB 6.4.31R (telephone sales and other exemptions) applies.
- (2) When giving the information in (1), the *firm* must:
- (a) believe on reasonable grounds that the information given is sufficient to enable the *policyholder* to understand the consequences of the variation; and
  - (b) in the case of a variation which results in a new *distance contract*, in good time before the variation is put into effect, provide all the contractual terms and conditions and the information in COB App 1.

...

#### Post-sale rRight to cancel

- 6.7.7 R A retail customer, ~~who is an individual~~, has a right to cancel:

## ADDENDUM

### LONG-TERM CARE INSURANCE CONTRACTS INSTRUMENT 2004

Annex A to this instrument is amended by replacing the text shown amending COB 6.5.14G with the following text:

- 6.5.14 G The description which a *firm* is required to provide under COB 6.5.13R(2) might include information on the matters set out in the following non-exhaustive list:

...

(17) ...: and

(18) in the case of a long-term care insurance contract which is based on single premium investment bonds, the fact that the income produced by the bonds may be insufficient to continue to meet the premiums of the underlying contract of insurance. The description could also explain the consequences of this, including, if it is the case, that capital may be eroded, further single premiums may be payable, or the cover reduced.

**CONDUCT OF BUSINESS SOURCEBOOK (DISAPPLICATION OF PROSPECTUS  
RULES TO AUTHORISED FUNDS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Conduct of Business sourcebook.
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Conduct of Business Sourcebook (Disapplication of Prospectus Rules to Authorised Funds) Instrument 2004.

By order of the Board  
20 May 2004

**Annex**  
**Amendment to the Conduct of Business sourcebook**

In this Annex underlining indicates new text.

...

Standardised past performance information

3.8.13 R (1) ...

(5) This rule does not apply to a *prospectus* drawn up in accordance with CIS 3.2.1R (Drawing up of prospectus) or COLL 4.2.2R (Publishing the prospectus).<sup>1</sup>

...

---

<sup>1</sup> COB 3.8.13R was substantially amended by the Financial Promotions (Past Performance) Instrument 2003 (FSA 2003/96) to come into effect on 1 June 2004. The amendment in this instrument adds to the provisions in that instrument and comes into effect at the same time.

**TRAINING AND COMPETENCE SOURCEBOOK  
(MONITORING OF EMPLOYEES) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157 (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act .

**Commencement**

- C. This instrument comes into force on 1 July 2004.

**Amendments to the Training and Competence sourcebook**

- D. The Training and Competence sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Training and Competence Sourcebook (Monitoring of Employees) Instrument 2004.

By order of the Board  
20 May 2004

## Annex

### Amendments to the Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 2.7 Supervising and monitoring

Supervising employees not ~~yet~~ assessed as competent

- 2.7.1 R If a *firm's employees* engage in an activity with or for *private customers*, the *firm* must ensure that if an *employee* has is not ~~yet been~~ assessed as competent, but is permitted in accordance with *TC 2.4.2R* to engage in a particular activity under supervision, the *employee* is appropriately supervised until assessed as competent in that activity.

...

~~Supervising employees assessed as competent~~

- ~~2.7.3 R A *firm* must have *arrangements* in place to ensure that an *employee* who has been assessed as competent is appropriately supervised.~~

- ~~2.7.4 G Appropriate supervision will vary according to the competence of the *employee* and is likely to be less intense once competence has been attained. [If the *employee* is, for example, a *sole trader*, or the only *director* or *partner* engaging in the activity, the *firm* should make whatever arrangements are appropriate in the circumstances, bearing in mind that it can become difficult to be objective about one's own performance.]<sup>1</sup>~~

Supervisors of employees advising private customers on packaged products

- 2.7.5 R If an *employee* who is not assessed as competent is engaging in the activity of giving advice on *investments* which are packaged products to *private customers*, the *firm* must ensure that the individual supervising that *employee*:
- (1) has passed an appropriate [examination]<sup>2</sup>; and
  - (2) has the technical knowledge, assessment skills and coaching skills to act as supervisor, before acting as supervisor, and that this competence is maintained.

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<sup>1</sup> The words in square brackets were added by the Training and Competence Sourcebook (Examinations and Miscellaneous Amendments) Instrument 2004 (FSA 2004/26) with effect from 1 May 2004.

<sup>2</sup> The word in square brackets was added by the Training and Competence Sourcebook (Examinations and Miscellaneous Amendments) Instrument 2004 (FSA 2004/26) in substitution for '*approved examination*' with effect from 1 July 2004.

Monitoring employees assessed as competent

2.7.5A R A firm must have arrangements in place to ensure that an employee who is engaging in an activity with or for private customers and who has been assessed as competent is appropriately monitored.

2.7.5B G What level of monitoring is appropriate will depend on all the circumstances including the knowledge and skills of the employee. It is likely to be less intense than the level of supervision carried out under TC 2.7.1R. If the employee is, for example, a sole trader, or the only director or partner engaging in the activity, the firm should make whatever arrangements are appropriate in the circumstances, bearing in mind that it can become difficult to be objective about one's own performance.

2.7.5C R If an employee who is engaging in an activity with or for private customers falls below the standard expected of a competent employee, the firm must make arrangements for supervising the employee, having regard to the provisions of TC 2.7.1R and TC 2.7.5R.

Supervising and monitoring: record keeping

2.7.6 G A firm should, for the purposes of TC 2.8.1R (Record keeping), make and retain records of:

- (1) the criteria applied in deciding the level of supervision and monitoring required in respect of its employees; and
- (2) how the supervision and monitoring of its employees is carried out.

## PERIODIC FEES (2004/2005) INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers);
  - (2) section 157(1) (Guidance); and
  - (3) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- C. This instrument comes into force on 1 June 2004.

### Amendments to the Handbook

- D.
- (1) The General provisions (GEN) are amended in accordance with Annex A to this instrument.
  - (2) The Authorisation manual (AUTH) is amended in accordance with Annex B to this instrument.
  - (3) The Supervision manual (SUP) is amended in accordance with Annex C to this instrument.
  - (4) The Dispute resolution: Complaints sourcebook (DISP) is amended in accordance with Annex D to this instrument.
  - (5) The Collective Investment Schemes sourcebook (CIS) is amended in accordance with Annex E to this instrument.
  - (6) The New Collective Investment Schemes sourcebook (COLL) is amended in accordance with Annex F to this instrument.
  - (7) The Professional firms sourcebook (PROF) is amended in accordance with Annex G to this instrument.
  - (8) The Recognised Investment Exchange and Recognised Clearing House sourcebook (REC) is amended in accordance with Annex H to this instrument.

### Citation

- E. This instrument may be cited as the Periodic Fees (2004/2005) Instrument 2004.

By order of the Board  
20 May 2004



## Annex A

### Amendments to the General provisions

In this Annex underlining indicates new text.

3.3.1R A *person* need not pay a fee on the date on which it is due under the relevant provision in the *Handbook*, if:

(1) ...

(2) unless SUP 20.2.7R(4) or SUP 20.2.7R(5) (Time and method for payment) applies, that date would otherwise fall on or before the 30th *day* after the date on which the *FSA* has sent written notification to that *person* of the fee payable on that date, in which case he must pay on or before the 30th *day* after the date on which the *FSA* sends the notification.

## Annex B

### Amendments to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text.

AUTH 4 Ann 1R

...

Part 2 – Complexity Groupings

...

Complex cases

<b>Activity grouping</b>	<b>Description</b>
...	...
A.3	<del>Firms conducting insurance activities subject only to prudential regulation</del> <u>Insurers – general</u> (excluding <i>friendly societies</i> )
A.4	<del>Firms conducting insurance activities subject to both prudential and conduct of business regulation</del> <u>Insurers – life</u> (excluding <i>friendly societies</i> )

## Annex C

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

- 6.3.22R If a *firm* applies for a variation of its *Part IV permission*, it must pay the fee specified in Part 3 of *AUTH 4 Annex 1R* in either of the following cases:
- (1) if the variation is granted, the business of the *firm* will fall within one or more activity groups specified in Part 1 of *SUP 20 Annex 1R* not applicable before the grant of the variation, ~~except the A.13 activity group if, before the variation, the A.12 activity group tariff applied to the *firm's* business;~~ or
  - (2) ...
- 6.3.22AR The sum payable under *SUP 6.3.22R* must be paid:
- (1) by banker's draft, cheque or other payable order;
  - (2) in full without deduction;
  - (3) on or before the date on which the application is made.
- 6.3.22BG The appropriate fee is an integral part of an application for a variation of a *Part IV permission*. Any application received by the *FSA* without the accompanying appropriate fee, in full and without deduction (see *SUP 6.3.22AR*) will not be treated as an application made in accordance with section 44 of the *Act*. Where this is the case, the *FSA* will contact the applicant to point out that the variation cannot be progressed until the appropriate fee has been received. In the event that the appropriate fee, in full and without deduction, is not forthcoming, the application will be returned to the applicant and no application will have been made.
- 6.3.22CG Fees paid for an application to vary a *Part IV permission* are not refundable.
- 20.2.4R The periodic fee referred to in *SUP 20.2.1R* is (except in relation to the *Society*) calculated as follows:
- (1) ...
  - (2) ...
  - (3) ...

(4) apply any applicable payment charge or discount specified in *SUP* 20.2.7AR, provided that:

(a) for payment by direct debit, successful collection of the amount due is made at the first attempt by the *FSA*; or

(b) for payment by credit transfer, the amount due is received by the *FSA* on or before the due date.

20.2.7R

(1) ...

(2) ...

(3) ~~In any other case~~ If the *firm's* periodic fee for the previous financial year was less than £50,000, the *firm* must pay the periodic fee due in full by 1 July in the financial year to which that sum relates.

(4) If a *firm* has applied to cancel its *Part IV permission* in the way set out in *SUP* 6.4.5D (Cancellation of permission), then (2) and (3) do not apply but it must pay the total amount due when the application is made.

(5) If the *FSA* has exercised its *own-initiative powers* to cancel a *firm's Part IV permission* in the way set out in *ENF* 5 (Cancellation of Part IV permission on the *FSA's* own initiative), then (2) and (3) do not apply but the *firm* must pay the total amount due immediately before the cancellation becomes effective.

20.4.4R

A *firm* which becomes authorised, or whose *permission* is extended, during the course of the financial year must pay a fee which is calculated by:

(1) identifying each of the tariffs set out in Part 1 of *SUP* 20 Ann 2R for the relevant financial year that apply to the *firm* only after the *permission* is received or extended, but ignoring:

(a) the A.13 activity group if, before the variation, the A.12 activity group applied to the *firm's* business; or

(b) the A.12 activity group if, before the variation, the A.13 activity group applied to the *firm's* business;

(2) ...

(3) ...

(4) ...

20.4.12AG Where a *firm* has applied to cancel its *Part IV permission*, or the *FSA* has exercised its *own-initiative powers* to cancel a *firm's Part IV permission*, the due dates for payment of periodic fees are modified by *SUP 20.2.7R(4)* and *SUP 20.2.7R(5)* respectively.

SUP 20 Annex 1R

Part 1

This table shows how the *regulated activities* for which a *firm* has permission are linked to activity groups ('fee-blocks'). A *firm* can use the table to identify which fee-blocks it falls into based on its *permission*.

Activity group	Fee-payer falls in the activity group if
...	...
<b>A.3</b> <b>Firms</b> <b>conducting</b> <b>insurance</b> <b>activities</b> <b>subject only to</b> <b>prudential</b> <b>regulation</b> <b>Insurers -</b> <b>general</b>	its <i>permission</i> includes one or more of the following: <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <b>BUT ONLY</b> in respect of <i>specified investments</i> that are: <ul style="list-style-type: none"> <li>- <i>general insurance contracts</i>; or</li> <li>- <i>long-term insurance contracts other than life-policies</i>.</li> </ul>
<b>A.4</b> <b>Firms</b> <b>conducting</b> <b>insurance</b> <b>activities</b> <b>subject to both</b> <b>prudential and</b> <b>conduct of</b> <b>business</b> <b>regulation</b> <b>Insurers - life</b>	its <i>permission</i> includes one or more of the following: <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <b>both</b> in respect of <i>specified investments</i> including <i>life policies</i> ; <ul style="list-style-type: none"> <li>• <i>entering as provider into a funeral plan contract</i>.</li> </ul>
...	...
<p><b>Note for authorised professional firms:</b></p> <p>Generally, for fee-blocks A.7 to A.14 A.19 below, only those <i>regulated activities</i> that are not limited to <i>non-mainstream regulated activities</i> should be taken into account in determining which fee-block(s) fee-payers belong to <u>for the purpose of charging periodic fees</u>.</p> <p>However, in the case that all the <i>regulated activities</i> within a <i>firm's permission</i> are limited to <i>non-mainstream regulated activities</i>, then that <i>firm</i> will be allocated to fee-block A.13 alone.</p> <p><u>This does not prevent a fee being payable by an authorised professional firm under SUP 6.3.22R where it applies to vary its <i>Part IV permission</i> such that it would normally be allocated to fee-block(s) other than A.13 if the variation was granted.</u></p>	
...	...

<p><b>A.12</b>  <b>Advisory arrangers, dealers or brokers (holding or controlling client money or assets, or both)</b></p>	<p>its <i>permission</i>:</p> <p>(a) includes one or more of the following, <u>in relation to one or more designated investments</u>:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>;</li> <li>• <i>arranging (bringing about) deals in investments</i>;</li> <li>• <i>making arrangements with a view to transactions in investments</i>;</li> <li>• <i>dealing as principal in investments</i> where the activity is carried on as a matched principal broker, <i>oil market participant, energy market participant</i> or <i>local</i>;</li> <li>• <i>advising on investments (except pension transfers and pension opt-outs)</i>;</li> <li>• <i>advising on pension transfers and pension opt-outs</i>;</li> <li>• <i>advising on syndicate participation at Lloyd's</i>;</li> </ul> <p>(b) <b>BUT NONE</b> of the following:</p> <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>; or</li> <li>• <i>carrying out contracts of insurance</i>;</li> </ul> <p><b>AND</b></p> <p>(c) <b>CAN HAVE</b> one or more of the following:</p> <ul style="list-style-type: none"> <li>• <i>safeguarding and administering of assets</i>;</li> <li>• <i>arranging safeguarding and administration of assets</i>;</li> <li>• the ability to hold or control <i>client money</i>, or both: <ul style="list-style-type: none"> <li>- that is, there is no <i>requirement</i> which prohibits the <i>firm</i> from doing this; and</li> <li>- provided that the <i>client money</i> in question does not only arise from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> </li> </ul> <p><b>AND</b></p> <p>(d) <b>PROVIDED</b> the fee-payer is <b>NOT</b> any of the following:</p> <ul style="list-style-type: none"> <li>• a <i>corporate finance advisory firm</i>;</li> <li>• a <i>firm</i> for whom all of the applicable activities above are otherwise limited to carrying out <i>corporate finance business</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>venture capital business</i>;</li> <li>• a <i>firm</i> whose activities are limited to acting as an operator of a <i>regulated collective investment scheme</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>trustee</i> activities;</li> <li>• a <i>service company</i>.</li> </ul>
<p><b>A.13</b>  <b>Advisory arrangers, dealers or brokers (not holding or controlling client money or assets, or both)</b></p>	<p>(1) it is an <i>authorised professional firm</i> and <b>ALL</b> the <i>regulated activities</i> in its <i>permission</i> are limited to <i>non-mainstream regulated activities</i>;</p> <p><b>OR</b></p> <p>(2) its <i>permission</i>:</p> <p>(a) includes one or more of the following, <u>in relation to one or more designated investments</u>:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>;</li> <li>• <i>arranging (bringing about) deals in investments</i>;</li> <li>• <i>making arrangements with a view to transactions in investments</i>;</li> <li>• <i>dealing as principal in investments</i> where the activity is carried on as a matched principal broker, <i>oil market participant, energy market participant</i> or <i>local</i>;</li> <li>• <i>advising on investments (except pension transfers and pension opt-outs)</i>;</li> <li>• <i>advising on pension transfers and pension opt-outs</i>;</li> <li>• <i>advising on syndicate participation at Lloyd's</i>;</li> </ul>

	<p>(b) <b>BUT NONE</b> of the following:</p> <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance;</i></li> <li>• <i>carrying out contracts of insurance;</i></li> <li>• <i>safeguarding and administration of assets;</i></li> <li>• <i>arranging safeguarding and administration of assets;</i></li> </ul> <p><b>AND</b></p> <p>(c) <b>MUST EITHER:</b></p> <ul style="list-style-type: none"> <li>• have a <i>requirement</i> that prohibits the <i>firm</i> from holding or controlling <i>client money</i>, or both;</li> </ul> <p><b>OR</b></p> <ul style="list-style-type: none"> <li>• if it does not have such a <i>requirement</i>, only holds or controls <i>client money</i> (or both), arising from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> <p><b>AND</b></p> <p>(d) <b>PROVIDED</b> the fee-payer is <b>NOT</b> one of the following:</p> <ul style="list-style-type: none"> <li>• a <i>corporate finance advisory firm</i>;</li> <li>• a <i>firm</i> for whom all of the applicable activities above are otherwise limited to carrying out <i>corporate finance business</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>venture capital business</i>;</li> <li>• a <i>firm</i> whose activities are limited to acting as an <i>operator</i> of a <i>regulated collective investment scheme</i>;</li> <li>• a <i>firm</i> whose activities are limited to carrying out <i>trustee</i> activities;</li> <li>• a <i>service company</i>.</li> </ul>
...	...
<b>A.19 General insurance mediation</b>	<p>its <i>permission</i> includes one or more of the following in relation to a <del><i>general insurance contract</i></del> or a <del><i>pure protection contract</i></del>: <u><i>non-investment insurance contract</i></u>:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>; or</li> <li>• <i>arranging (bringing about) deals in investments</i>; or</li> <li>• <i>making arrangements with a view to transactions in investments</i>; or</li> <li>• <i>assisting in the administration and performance of a contract of insurance</i>; or</li> <li>• <i>advising on investments</i>; or</li> <li>• <i>agreeing to carry on a regulated activity</i> which is within any of the above.</li> </ul>
...	...

## Part 2

This table indicates the tariff base for each fee-block. The tariff base is the means by which we measure the 'amount of business' conducted by a *firm*.

Activity group	Tariff-base
A.1	<p><b>MODIFIED ELIGIBLE LIABILITIES</b></p> <p><del>For banks and e-money issuers:</del></p> <p><b>Part 1:</b></p> <p><b>Liabilities</b></p>

	<p>In sterling:  <math>\pounds 2 + \pounds 3 + \pounds 4 + \pounds 5A + \pounds 5B + \pounds 6B + \pounds 6C + \pounds 6D + \pounds 6E + \pounds 6F + \pounds 6G + \pounds 6H + \pounds 6J + \pounds 7B + \pounds 7C + \pounds 7D + \pounds 7E + \pounds 7F + \pounds 7G + \pounds 7H + \pounds 7J + \pounds 8 + \pounds 10 + 60\% \text{ of } \pounds 11A + \pounds 44</math>  plus  In foreign currency, one-third of:  <math>E2 + E3 + E4 + E5A + E5B + E6B + E6C + E6D + E6E + E6F + E6G + E6H + E6J + E7B + E7C + E7D + E7E + E7F + E7G + E7H + E7J + E8 + E10 + 60\% \text{ of } E11A + E44 + C2 + C3 + C4 + C5A + C5B + C6B + C6C + C6D + C6E + C6F + C6G + C6H + C6J + C7B + C7C + C7D + C7E + C7F + C7G + C7H + C7J + C8 + C10 + 60\% \text{ of } C11A</math>: less</p> <p><b>Assets</b>  In sterling:  <math>\pounds 21B + 60\% \text{ of } \pounds 22A + \pounds 23D + \pounds 23E + \pounds 23F + \pounds 30A + \pounds 30B + \pounds 31A + \pounds 31B + \pounds 32AA</math>  plus  In foreign currency, one-third of:  <math>E21B + 60\% \text{ of } E22A + E23D + E23E + E23F + E30A + E30B + E31A + E31B + E32AA + C21B + 60\% \text{ of } C22A + C23D + C23E + C23F + C30A + C30B + C31A + C31B + C32AA</math></p> <p><b>Part 2: Non-resident office offset</b>  The fee base is adjusted by deducting from the amount calculated in accordance with part 1 above, the Non-Resident Office Offset amount obtained by subtracting item 45D from item 45BA in the Form BT. The Non-Resident Office Offset amount, if it would otherwise have been a negative number, is zero.</p> <p><b>Notes:</b>  (1) All references in the above formula are to entries on Form BT (that is, the Balance Sheet Form completed to provide information required following the Banking Statistics Review 1997 and returned by <i>banks</i> to the Bank of England as required by the Bank of England Act 1998).  (2) 'E' refers to assets and liabilities denominated in euro (as referred to in column 2 of Form BT) and 'C' refers to assets and liabilities denominated in currencies other than sterling and euro (as referred to in column 3 of Form BT). In accordance with Form BT, assets and liabilities in currencies other than sterling are to be recorded in sterling.  (3) The figures reported on the Form BT relate to business conducted out of offices in the <i>United Kingdom</i>.</p> <p><b><u>For e-money issuers:</u></b>  <u>Outstanding balance of e-money liabilities</u>  ...  ...</p>
...	...
A.3	<p><b>GROSS PREMIUM INCOME AND GROSS TECHNICAL LIABILITIES</b></p> <p><b>For insurers:</b>  The amount of <i>premiums</i> receivable which must be included in the documents required to be deposited under <i>IPRU (INS)</i> 9.6 in relation to the financial year to which the documents relate but disregarding for this purpose such amounts as are not included in the document by reason of a <i>waiver</i> or an order under section 68 of the Insurance Companies Act 1982 carried forward as an amendment to <i>IPRU (INS)</i> under transitional provisions relating to written concessions in <i>SUP</i>;</p>



	<p>less, <i>premiums</i> relating to <i>pension fund management</i> business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk;</p> <p><b>AND</b></p> <p>the amount of gross technical liabilities (<i>IPRU (INS)</i> Appendix 9.1 – Form 15, line 19) which must be included in the documents required to be deposited under <i>IPRU (INS)</i> 9.6R in relation to the financial year to which the documents relate but disregarding for this purpose such amounts as are not included in the document by reason of a <i>waiver</i> or an order under section 68 of the Insurance Companies Act 1982 carried forward as an amendment to <i>IPRU(INS)</i> under transitional provisions relating to written concessions in <i>SUP</i>;</p> <p>less, the amount of gross technical liabilities relating to <i>pension fund management</i> business where the <i>firm</i> owns the <i>investments</i> and there is no transfer of risk.</p> <p><b>Notes:</b></p> <p>(1) in the case of either:</p> <p>(a) a <i>pure reinsurer</i> carrying on <i>general insurance business</i> through a <i>branch</i> in the <i>United Kingdom</i>; or</p> <p>(b) an <i>insurer</i> whose head office is not in an <i>EEA State</i> carrying on <i>general insurance business</i> through a <i>branch</i> in the <i>United Kingdom</i>; or</p> <p>(c) a <i>non-EEA insurer</i> other than a <i>Swiss general insurer</i> which has <i>permission</i> to carry on <i>direct insurance business</i> and which has made a deposit in an <i>EEA state</i> other than the <i>United Kingdom</i> in accordance with <i>IPRU(INS)</i> 8.1(2),</p> <p>the amount only includes <i>premiums</i> received and gross technical liabilities held in respect of its <i>United Kingdom</i> business; <del>and</del></p> <p>(2) for a <i>Swiss general insurance company</i>, <i>premiums</i> and gross technical liabilities include those relevant to the operations of the company's <i>United Kingdom branch</i>; <del>and</del></p> <p>(3) a <i>firm</i> need not include <u><i>premiums</i> and <i>gross technical liabilities</i> relating to <i>pure protection contracts</i> which it reports, and pays a fee on, in the A.4 activity group.</u></p> <p>...</p>
...	...

Part 3

This table indicates the valuation date for each fee-block. A *firm* can calculate its tariff data by applying the tariff bases set out in Part 2 above with reference to the valuation dates shown in this table.

Activity group	Valuation date
<p>IN THIS TABLE, REFERENCES TO SPECIFIC DATES OR MONTHS ARE REFERENCES TO THE LATEST ONE OCCURRING BEFORE THE START OF THE PERIOD TO WHICH THE FEE APPLIES, UNLESS OTHERWISE SPECIFIED – E.G. FOR 2004/05 FEES (1 APRIL 2004 TO 31 MARCH 2005), A REFERENCE TO DECEMBER MEANS DECEMBER 2003.</p>	

Activity group	Valuation date
Where a <i>firm's</i> tariff data is in a currency other than sterling, it should be converted into sterling at the exchange rate prevailing on the relevant valuation date.	
A.1	<p><b><del>For banks; and e-money issuers:</del></b> Modified eligible liabilities (MELs), valued at:</p> <ul style="list-style-type: none"> <li>• for a <i>firm</i> which reports monthly, the average of the MELs for October, November and December;</li> <li>• for a <i>firm</i> which reports quarterly, the MELs for December.</li> </ul> <p><b><u>For e-money issuers:</u></b> <u>MELs, valued at the end of the financial year ended in the calendar year ending 31 December.</u></p> <p>...</p>
...	...
A.3	<p>Annual gross <i>premium</i> income (GPI), <del>valued at the period to which the most recent annual return relates [Note: for most <i>firms</i> this will be the 12 months ended 31 December].</del> <u>for the financial year ended in the calendar year ending 31 December.</u></p> <p><b>AND</b></p> <p>Gross technical liabilities (GTL) valued at the end of <del>the period to which the most recent annual return related [Note: for most <i>firms</i> this will be the 12 months ended 31 December].</del> <u>the financial year ended in the calendar year ending 31 December.</u></p>
...	...

SUP 20 Annex 2R

Part 1

This table shows the tariff rates applicable to each fee-block.

(1)	...
(2)	...
(3)	For a <i>firm</i> which has not complied with SUP 20.3.2R (Information on which fees are calculated) for this period:
(a)	the fee is calculated using (where relevant) the valuation or valuations of business applicable to the previous period, multiplied by the factor of 1.10;
(b)	an additional administrative fee of <del>£250</del> <u>£500</u> is payable; and
(c)	the minimum total fee (including the administrative fee in (b)) is <del>£350</del> <u>£650</u> .

Activity group	Fee payable

<b>A.1</b>	<p><del>[to be made later]</del></p> <p><b><u>Minimum fee (£)</u></b></p> <p><b><u>£ million of Modified Eligible Liabilities (MELs)</u></b></p> <p><u>0 – 0.5</u>  <u>&gt;0.5 – 2</u>  <u>&gt;2 – 10</u>  <u>&gt;10 – 200</u>  <u>&gt;200 – 2,000</u>  <u>&gt;2,000 – 10,000</u>  <u>&gt;10,000 – 20,000</u>  <u>&gt;20,000</u></p>	<p>150</p> <p><b><u>Fee (£/£m or part £m of MELs)</u></b></p> <p><u>0</u>  <u>additional flat-rate fee of £350</u>  <u>additional flat-rate fee of £500</u>  <u>32.63</u>  <u>32.47</u>  <u>32.31</u>  <u>32.16</u>  <u>31.84</u></p>				
<p>For a <i>firm</i> in A.1 which has a <i>limitation on its permission</i> to the effect that it may <i>accept deposits from wholesale depositors only</i>, the fee is calculated as above less 30%.</p> <p>In addition, the fee specified below is payable by <i>UK banks and building societies</i>. The <i>wholesale depositors discount and permitted deductions in Part 2 of SUP 20 Ann 2R</i> do not apply to this fee.</p>						
<table border="1"> <tr> <td data-bbox="438 1003 933 1108"> <p><b><u>Minimum fee (£m of MELs)</u></b></p> <p><u>if 0 – 2,000</u>  <u>if &gt;2,000</u></p> </td> <td data-bbox="933 1003 1428 1108"> <p><b><u>Fee (£)</u></b></p> <p><u>0</u>  <u>2,000</u></p> </td> </tr> <tr> <td data-bbox="438 1108 933 1344"> <p><b><u>£ million of MELs</u></b></p> <p><u>0 – 5,000</u>  <u>&gt;5,000 – 10,000</u>  <u>&gt;10,000 – 20,000</u>  <u>&gt;20,000</u></p> </td> <td data-bbox="933 1108 1428 1344"> <p><b><u>Fee (£/£m or part £m of MELs)</u></b></p> <p><u>0</u>  <u>0.93</u>  <u>0.85</u>  <u>0.79</u></p> </td> </tr> </table>			<p><b><u>Minimum fee (£m of MELs)</u></b></p> <p><u>if 0 – 2,000</u>  <u>if &gt;2,000</u></p>	<p><b><u>Fee (£)</u></b></p> <p><u>0</u>  <u>2,000</u></p>	<p><b><u>£ million of MELs</u></b></p> <p><u>0 – 5,000</u>  <u>&gt;5,000 – 10,000</u>  <u>&gt;10,000 – 20,000</u>  <u>&gt;20,000</u></p>	<p><b><u>Fee (£/£m or part £m of MELs)</u></b></p> <p><u>0</u>  <u>0.93</u>  <u>0.85</u>  <u>0.79</u></p>
<p><b><u>Minimum fee (£m of MELs)</u></b></p> <p><u>if 0 – 2,000</u>  <u>if &gt;2,000</u></p>	<p><b><u>Fee (£)</u></b></p> <p><u>0</u>  <u>2,000</u></p>					
<p><b><u>£ million of MELs</u></b></p> <p><u>0 – 5,000</u>  <u>&gt;5,000 – 10,000</u>  <u>&gt;10,000 – 20,000</u>  <u>&gt;20,000</u></p>	<p><b><u>Fee (£/£m or part £m of MELs)</u></b></p> <p><u>0</u>  <u>0.93</u>  <u>0.85</u>  <u>0.79</u></p>					
<b>A.2</b>	<p>...</p>					
<b>A.3</b>	<p><del>[to be made later]</del></p> <p><b><u>Gross premium income (GPI)</u></b></p> <p><b><u>Minimum fee (£)</u></b></p> <p><b><u>£ million of GPI</u></b></p> <p><u>0 – 0.5</u>  <u>&gt;0.5 – 2</u>  <u>&gt;2 – 5</u>  <u>&gt;5 – 20</u>  <u>&gt;20 – 75</u>  <u>&gt;75 – 150</u>  <u>&gt;150</u></p> <p><b><u>PLUS</u></b>  <b><u>Gross technical liabilities (GTL)</u></b></p> <p><b><u>Minimum fee (£)</u></b></p>	<p>400</p> <p><b><u>Fee (£/£m or part £m of GPI)</u></b></p> <p><u>0</u>  <u>1,612.24</u>  <u>1,490.88</u>  <u>1,369.52</u>  <u>433.35</u>  <u>372.73</u>  <u>52.03</u></p> <p>0</p>				

	<u>£ million of GTL</u> <u>0 – 1</u> <u>&gt;1 – 5</u> <u>&gt;5 – 50</u> <u>&gt;50 – 100</u> <u>&gt;100 – 1,000</u> <u>&gt;1,000</u>	<u>Fee (£/£m or part £m of GTL)</u> <u>0</u> <u>39.29</u> <u>36.33</u> <u>33.38</u> <u>10.56</u> <u>4.22</u>
A.4	<del>[to be made later]</del>  <u>Adjusted annual gross premium income (AGPI)</u>  <u>Minimum fee (£)</u>  <u>£ million of AGPI</u> <u>0 – 1</u> <u>&gt;1 – 50</u> <u>&gt;50 – 1,000</u> <u>&gt;1,000 – 2,000</u> <u>&gt;2,000</u>  <u>PLUS</u>  <u>Mathematical reserves (MR)</u>  <u>Minimum fee (£)</u>  <u>£ million of MR</u> <u>0 – 1</u> <u>&gt;1 – 10</u> <u>&gt;10 – 100</u> <u>&gt;100 – 1,000</u> <u>&gt;1,000 – 5,000</u> <u>&gt;5,000 – 15,000</u> <u>&gt;15,000</u>	  <u>200</u>  <u>Fee (£/£m or part £m of AGPI)</u> <u>0</u> <u>700.00</u> <u>631.95</u> <u>418.08</u> <u>281.98</u>    <u>200</u>  <u>Fee (£/£m or part £m of MR)</u> <u>0</u> <u>37.63</u> <u>33.97</u> <u>22.47</u> <u>15.16</u> <u>11.55</u> <u>8.88</u>
A.5	<del>[to be made later]</del>  <u>Minimum fee (£)</u>  <u>£ million of Active Capacity (AC)</u> <u>0 – 50</u> <u>&gt;50 – 150</u> <u>&gt;150 – 250</u> <u>&gt;250</u>	  <u>500</u>  <u>Fee (£/£m or part £m of AC)</u> <u>0</u> <u>95.95</u> <u>80.75</u> <u>22.80</u>
A.6	<del>[to be made later]</del>	<u>£1,204,000</u>
A.7	For class 1(C), (2) and (3) <i>firms</i> : <del>[to be made later]</del>  <u>Minimum fee (£)</u>	    <u>1,200</u>

	<p><b><u>£ million of Funds under Management (FuM)</u></b></p> <p><u>0 – 10</u>  <u>&gt;10 – 100</u>  <u>&gt;100 – 2,500</u>  <u>&gt;2,500 – 10,000</u>  <u>&gt;10,000</u></p>	<p><b><u>Fee (£/£m or part £m of FuM)</u></b></p> <p><u>0</u>  <u>65.55</u>  <u>20.81</u>  <u>11.35</u>  <u>1.25</u></p>
	<p>For class 1(B) <i>firms</i>: the fee calculated as for class 1(C) <i>firms</i> above, less 15%.  For class 1(A) <i>firms</i>: the fee calculated as for class 1(C) <i>firms</i> above, less 50%.</p>	
A.8	...	
A.9	<p>[to be made later]</p> <p><b><u>Minimum fee (£)</u></b></p> <p><b><u>£ million of Gross Income (GI)</u></b></p> <p><u>0 – 1</u>  <u>&gt;1 – 20</u>  <u>&gt;20 – 500</u>  <u>&gt;500 – 1,000</u>  <u>&gt;1,000</u></p>	<p><u>1,800</u></p> <p><b><u>Fee (£/£m or part £m of GI)</u></b></p> <p><u>0</u>  <u>1,761.34</u>  <u>1,427.02</u>  <u>1,219.88</u>  <u>918.36</u></p>
A.10	<p>[to be made later]</p> <p><b><u>Minimum fee (£)</u></b></p> <p><b><u>No. of traders</u></b></p> <p><u>0 – 2</u>  <u>3 – 5</u>  <u>6 – 10</u>  <u>11 – 50</u>  <u>51 – 200</u>  <u>&gt;200</u></p>	<p><u>2,100</u></p> <p><b><u>Fee (£/trader)</u></b></p> <p><u>0</u>  <u>1,978</u>  <u>1,405</u>  <u>1,277</u>  <u>1,081</u>  <u>864</u></p>
	<p>In addition, the fee specified below is payable by <i>UK domestic firms</i>. The permitted deductions in Part 2 of <i>SUP 20 Ann 2R</i> do not apply to this fee.</p>	
	<p><b><u>Minimum fee (No. of traders)</u></b></p> <p>if <u>0 - 100</u>  if <u>&gt;100</u></p> <p><b><u>No. of traders</u></b></p> <p><u>0 - 125</u>  <u>126 – 250</u>  <u>&gt;250</u></p>	<p><b><u>Fee (£)</u></b></p> <p><u>0</u>  <u>2,000</u></p> <p><b><u>Fee (£/trader)</u></b></p> <p><u>0</u>  <u>70</u>  <u>51</u></p>
A.11	...	
A.12	<p>[to be made later]</p> <p><b><u>Minimum fee (£)</u></b></p> <p><b><u>No. of persons</u></b></p>	<p><u>1,650</u></p> <p><b><u>Fee (£/person)</u></b></p>

	<u>0 – 1</u> <u>2 – 4</u> <u>5 – 10</u> <u>11 – 25</u> <u>26 – 150</u> <u>151 – 1,500</u> <u>&gt;1,500</u>	<u>0</u> <u>960</u> <u>478</u> <u>332</u> <u>178</u> <u>133</u> <u>89</u>
	For a <i>professional firm</i> in A.12 the fee is calculated as above less 10%.	
<b>A.13</b>	For class (2) <i>firms</i> :	
	[to be made later]	
	<b><u>Minimum fee (£)</u></b>	<u>1,560</u>
	<b><u>No. of persons</u></b>	<b><u>Fee (£/person)</u></b>
	<u>0 – 1</u>	<u>0</u>
	<u>2 – 4</u>	<u>850</u>
	<u>5 – 10</u>	<u>815</u>
	<u>11 – 25</u>	<u>777</u>
	<u>26 – 500</u>	<u>708</u>
	<u>501 – 4,000</u>	<u>637</u>
	<u>&gt;4,000</u>	<u>592</u>
	For class (1) <i>firms</i> : £1,560	
	For a <i>professional firm</i> in A.13 the fee is calculated as above less 10%.	
<b>A.14</b>	[to be made later]	
	<b><u>Minimum fee (£)</u></b>	<u>1,200</u>
	<b><u>No. of persons</u></b>	<b><u>Fee (£/person)</u></b>
	<u>0 – 1</u>	<u>0</u>
	<u>2</u>	<u>1,155</u>
	<u>3 – 4</u>	<u>1,040</u>
	<u>5 – 10</u>	<u>935</u>
	<u>11 – 100</u>	<u>843</u>
	<u>101 – 200</u>	<u>590</u>
	<u>&gt;200</u>	<u>353</u>
<b>A.15</b>	...	
<b>A.16</b>	[to be made later]	
	<u>0</u>	
<b>A.17</b>	...	
<b>A.18</b>	...	
<b>A.19</b>	...	
<b>B. Market operators</b>	[to be made later]	
	<u>£20,000</u>	
<b>B. Service companies</b>	[to be made later]	
	<u>Bloomberg LP</u>	<u>£31,500</u>
	<u>EMX Co Ltd</u>	<u>£21,000</u>
	<u>LIFFE Services Ltd</u>	<u>£21,000</u>
	<u>Ofex plc</u>	<u>£51,500</u>

<u>OMGEO Ltd</u>	<u>£21,000</u>
<u>Reuters Ltd</u>	<u>£31,500</u>
<u>Swapswire Ltd</u>	<u>£21,000</u>
<u>Thomson Financial Ltd</u>	<u>£21,000</u>

## Part 2

This table shows the permitted deductions that apply:

<b>Activity group</b>	<b>Nature of deduction</b>	<b>Amount of deduction</b>
<u>[to be made later]</u>		
<u>A.1</u>	<u>Financial penalties received</u>	<u>9.5% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>
<u>A.4</u>	<u>Financial penalties received</u>	<u>8.8% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>
<u>A.7</u>	<u>Financial penalties received</u>	<u>1.3% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>
<u>A.10</u>	<u>Financial penalties received</u>	<u>1.2% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>
<u>A.12</u>	<u>Financial penalties received</u>	<u>22.9% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>
<u>A.13</u>	<u>Financial penalties received</u>	<u>0.9% of the fee payable by the <i>firm</i> for the activity group (see Part 1)</u>

## Part 3

This table shows the modifications to fee tariffs that apply to *incoming EEA firms* and *incoming Treaty firms*.

<b>Activity group</b>	<b>Percentage of tariff payable under Part 1 applicable to the firm subject to a minimum amount payable of £100 (unless specified below)</b>
A.1	20% (for a <i>firm</i> operating on cross-border services basis only, 0% and the minimum sum is not applicable)
A.3	0% and the minimum sum is not applicable
A.4	75%
A.7, A.8 and A.9	95%
A.10, A.11, A.12, and A.13 and A.19	90%

## SUP 20 Annex 3R

### Part 1

This table shows the fees payable for transaction reporting.

<b>Fee per transaction</b>	<b>Date payable</b>	<b>Method of payment</b>
----------------------------	---------------------	--------------------------

[to be made later]

<b>Fee type</b>	<b>Fee amount (including VAT)</b>		<b>Date payable</b>
<u>Transaction charge</u>	<u>Number of transactions per annum</u>	<u>Fee per transaction (inc. VAT)</u>	<u>First working day of each month</u>
	<u>For the first 1,000</u>	<u>0p</u>	
	<u>1,001 – 1,000,000</u>	<u>3p</u>	
	<u>1,000,001 – 4,000,000</u>	<u>2.75p</u>	
	<u>4,000,001 – 8,000,000</u>	<u>2.5p</u>	
	<u>8,000,001 – 13,000,000</u>	<u>2.25p</u>	
	<u>13,000,001 – 20,000,000</u>	<u>2p</u>	
	<u>&gt;20,000,000</u>	<u>1.75p</u>	

- Notes:
1. Firms using the Direct Reporting System software will be additionally invoiced for:
    - (a) an initial software licence fee of £587.50 (including VAT); and
    - (b) an annual enrolment fee of £235 (including VAT) per licence held on 1 April each year.
  2. The applicable methods of payment of these fees are listed at SUP 20.2.7AR.

## Part 2

The periodic fee payable under SUP 20.6.1R for a certificate issued under Article 54 of the *Regulated Activities Order* is [to be made later] £1,000.



## Annex D

### Amendments to the Dispute resolution: Complaints sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

DISP 5 Annex 1R

...

Part 2: Fee tariffs for general levy and supplementary levy

...

<b>Industry block</b>	<b>Tariff base</b>	<b>General levy payable by firm</b>
...	...	...
<del>2 – Firms that undertake insurance activities, subject to prudential regulation only</del> <u>Insurers – general</u> (excluding <i>firms</i> in blocks 13 & 15)	...	...
...	...	...
<del>4 – Firms that undertake insurance activities, subject to both prudential and conduct of business regulation</del> ( <del>long-term insurers</del> ) <u>Insurers – life</u> (excluding <i>firms</i> in block 15)	...	...
...	...	...

## Annex E

### Amendments to the Collective Investment Schemes sourcebook

In this Annex striking through indicates deleted text. Where an entire new section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

18.2.1R A *person* identified in ~~part B~~ of CIS 18 Annex 1R as the "relevant fee payer" for a *regulated collective investment scheme* must pay each "periodic fee" applicable to it in full and without deduction.

Delete existing CIS 18 Annex 1R and insert new CIS 18 Annex 1R as follows:

#### Periodic fees payable for the period 1 April 2004 to 31 March 2005

##### Part 1 – Periodic fees payable

Nature and purpose of fee	Payable by	Amount of fee	Umbrella scheme factor (note 1)
Periodic fee for an <i>ICVC</i>	The <i>authorised corporate director</i>	£1,100	2
Periodic fee for an <i>AUT</i>	The <i>manager</i>	£1,100	2
Periodic fee for a <i>scheme</i> recognised under section 264 of the <i>Act</i>	The <i>operator</i>	£1,100	2
Periodic fee for a <i>scheme</i> recognised under section 270 of the <i>Act</i>	The <i>operator</i>	£1,100	2
Periodic fee for a <i>scheme</i> recognised under section 272 of the <i>Act</i>	The <i>operator</i>	£6,400	2

Note:

1. For an *umbrella scheme* the fee is multiplied by the factor shown in the final column of the table.

## Annex F

### Amendments to the New Collective Investment Schemes sourcebook

In this Annex all the text is new and is not underlined.

Insert new Transitional Provision as follows:

(1)	(2)	(3)	(4)	(5)	(6)
	<b>Material to which the transitional provision applies</b>		<b>Transitional provision</b>	<b>Transitional provision: dates in force</b>	<b>Handbook provision: coming into force</b>
...	...	...	...	...	...
12	<i>COLL</i> 10.2.1R	R	<i>COLL</i> 10.2.1R does not apply if the <i>scheme</i> has paid a periodic fee for the same period under <i>CIS</i> 18.2.	From 1 April 2004 until 12 February 2007	1 April 2004

Before *COLL* 10 Annex 2R, insert new *COLL* 10 Annex 1R as follows:

#### **Periodic fees payable for the period 1 April 2004 to 31 March 2005**

Part 1 – Periodic fees payable

Nature and purpose of fee	Payable by	Amount of fee	Umbrella scheme factor (note 1)
Periodic fee for an <i>ICVC</i> , where the <i>scheme</i> is: - <i>UCITS scheme</i> - <i>non-UCITS retail scheme</i> - <i>qualified investor scheme</i>	<i>The authorised corporate director</i>	£1,100 £1,100 £1,300	2
Periodic fee for an <i>AUT</i> , where the <i>scheme</i> is: - <i>UCITS scheme</i> - <i>non-UCITS retail scheme</i> - <i>qualified investor scheme</i>	<i>The manager</i>	£1,100 £1,100 £1,300	2
Periodic fee for a <i>scheme</i> recognised under section 264 of the <i>Act</i>	<i>The operator</i>	£1,100	2
Periodic fee for a <i>scheme</i> recognised under section 270 of the <i>Act</i>	<i>The operator</i>	£1,100	2
Periodic fee for a <i>scheme</i> recognised under section 272 of the <i>Act</i>	<i>The operator</i>	£6,400	2

Note:

1. For an *umbrella scheme* the fee is multiplied by the factor shown in the final column of the table.

## Annex G

### Amendments to the Professional firms sourcebook

In this Annex all the text is new and is not underlined.

Delete existing PROF 6 Annex 1R and insert new PROF 6 Annex 1R as follows:

#### Periodic fees payable for the period from 1 April 2004 to 31 March 2005

Table. Fees payable by Designated Professional Bodies

Name of Designated Professional Body	Amount payable	Due date
The Law Society	£47,285 £56,115	30 April 2004 1 September 2004
The Law Society of Scotland	£15,900	1 July 2004
The Law Society of Northern Ireland	£17,950	1 July 2004
The Institute of Actuaries	£10,300	1 July 2004
The Institute of Chartered Accountants in England and Wales	£31,305 £36,695	30 April 2004 1 September 2004
The Institute of Chartered Accountants of Scotland	£15,250	1 July 2004
The Institute of Chartered Accountants in Ireland	£13,100	1 July 2004
The Association of Chartered Certified Accountants	£20,100	1 July 2004

## Annex H

### Amendments to the Recognised Investment Exchange and Recognised Clearing House sourcebook

In this Annex striking through indicates deleted text. Where an entire new section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

7.1.5G The fee applicable to a *recognised body* reflects the estimated cost to the *FSA* of discharging its functions in relation to that *recognised body*. Fees are set for ~~UK~~ *recognised bodies* on an individual basis.

Delete existing REC 7 Annex 1R and insert new REC 7 Annex 1R as follows:

#### Periodic fees payable for the period from 1 April 2004 to 31 March 2005

In this Annex:

- the term *recognised body* includes a body which was a recognised investment exchange or a recognised clearing house recognised under the Financial Services Act 1986 and which is a *recognised body* as a result of Regulation 9 of the *Recognition Requirements Regulations*; and

- the term recognition order includes a recognition order made by the *FSA* under section 37 or section 39 of the Financial Services Act 1986 or a recognition order made by the Treasury under section 40 of the Financial Services Act 1986.

Part 1- Periodic fees for UK recognised bodies

Name of UK recognised body	Amount payable	Due date
CRESTCo Limited	£290,000	30 April 2004
	£298,000	1 September 2004
The International Petroleum Exchange of London Limited	£162,500	30 April 2004
	£169,500	1 September 2004
LIFFE Administration and Management	£330,000	30 April 2004
	£392,000	1 September 2004
LCH.Clearnet Limited	£285,000	30 April 2004
	£334,000	1 September 2004
The London Metal Exchange Limited	£240,000	30 April 2004
	£195,000	1 September 2004
The London Stock Exchange plc	£355,000	30 April 2004
	£350,000	1 September 2004
OM London Exchange Limited	£87,500	30 April 2004
	£101,500	1 September 2004
virt-x plc	£112,500	30 April 2004
	£121,500	1 September 2004

EDX	£75,000 £115,000	30 April 2004 1 September 2004
Any other <i>UK recognised investment exchange</i> recognised as such by a <i>recognition order</i> made in the period	£150,000	30 days after the date on which the <i>recognition order</i> is made
Any other <i>UK recognised clearing house</i> recognised as such by a <i>recognition order</i> made in the period	£250,000	30 days after the date on which the <i>recognition order</i> is made

Part 2 – Periodic fees for overseas recognised bodies

<b>Name of overseas recognised body</b>	<b>Amount payable</b>	<b>Due date</b>
Cantor Financial Futures Exchange	£10,000	1 July 2004
Chicago Mercantile Exchange	£10,000	1 July 2004
Chicago Board of Trade	£10,000	1 July 2004
Eurex Zurich	£10,000	1 July 2004
NASDAQ	£10,000	1 July 2004
NQLX	£10,000	1 July 2004
New York Mercantile Exchange	£10,000	1 July 2004
Swiss Exchange	£10,000	1 July 2004
Sydney Futures Exchange	£10,000	1 July 2004
Wareterminborse Hannover	£10,000	1 July 2004
Any other <i>overseas investment exchange</i> recognised as such by a <i>recognition order</i> made in the period	£10,000	30 days after the date on which the <i>recognition order</i> is made
Any other <i>overseas clearing house</i> recognised as such by a <i>recognition order</i> made in the period	£35,000	30 days after the date on which the <i>recognition order</i> is made

**SUPERVISION MANUAL (GUIDANCE AMENDMENT NO 1) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force as follows:
- (1) Annexes A and B come into force on 1 June 2004; and
  - (2) Annex C comes into force on 14 January 2005.

**Amendments to the Supervision manual**

- C. The Supervision manual is amended in accordance with Annexes A and C to this instrument.

**Amendments to the Glossary**

- D. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- E. This instrument may be cited as the Supervision Manual (Guidance Amendment No 1) Instrument 2004.

By order of the Board  
20 May 2004

Amended by Addendum  
17 August 2004



## Annex A

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

SUP 16 Annex 2G: Guidance notes on completion of banks' reporting forms (including validations)

...

#### BSD3 REPORTING INSTRUCTIONS

...

##### A610 Subordinated term debt

Report here the amount of subordinated term debt (i.e. the amount of principal outstanding before amortisation) which has been approved by the FSA as qualifying for inclusion in Tier 2 capital under the terms of Chapter CA (Definition of capital), Sections 7 and 8, of the FSA Policy Guide/IPRU (BANK) (see item A790). This item should equal the ~~sum of items A790.21 column "Sterling equivalent", A790.22 column "Sterling equivalent" and A790.1 amount of principal outstanding, converted to sterling at the current exchange rate for the currency concerned on the day of the report unless, via a subordinated swap or some other hedging mechanism that is an integral part of the original preference share or subordinated loan stock agreement, the exchange rate has effectively been fixed - in which case that fixed rate may be used. The reporting institution should obtain the FSA's agreement before doing this.~~

...

#### FORM BSD3 – CAPITAL ADEQUACY RETURN

...

##### SECTION A: BANKING BOOK

##### INTERNAL VALIDATIONS

...

Ref No	Item Number
--------	-------------

...

70	<del>A623</del>	<del>= (AS790.21+AS790.22) - (AA790.21+AA790.22)</del> <u>Withdrawn July 2004</u>
----	-----------------	---

...

#### FORM BSD3 – SECTION B: TRADING BOOK FOR SOLO BANK AND LINE BY LINE CONSOLIDATED ENTRIES

...

##### APPENDIX B-IV VALIDATIONS

...

Ref No	Appx B-IV Item No
--------	-------------------

...

37	<del>A110</del>	<del>= S110 - C110 if positive, else zero</del> <u>Introduced March 2004 Replaced by validation 44 July 2004</u>
----	-----------------	--

38	<del>A120</del>	<del>= S120 - C120 if positive, else zero</del> <u>Introduced March 2004 Replaced by validation 45 July 2004</u>
----	-----------------	--

39	<del>W120</del>	<del>= 10% x (S120 - C120) if positive, else zero</del> <u>Introduced March 2004 Replaced by validation 46 July 2004</u>
----	-----------------	--

40	A130	= S130 – C130 if positive, else zero Introduced March 2004 <u>Replaced by validation 47 July 2004</u>
41	W130	= 20% x (S130 – C130) if positive, else zero Introduced March 2004 <u>Replaced by validation 48 July 2004</u>
42	A140	= S140 – C140 if positive, else zero Introduced March 2004 <u>Replaced by validation 49 July 2004</u>
43	W140	= S140 – C140 if positive, else zero Introduced March 2004 <u>Replaced by validation 50 July 2004</u>
44	A110	= C110 – S110 if positive, else zero Introduced July 2004
45	A120	= C120 – S120 if positive, else zero Introduced July 2004
46	W120	= 10% x (C120 - S120) if positive, else zero Introduced July 2004
47	A130	= C130 – S130 if positive, else zero Introduced July 2004
48	W130	= 20% x (C130 – S130) if positive, else zero Introduced July 2004
49	A140	= C140 – S140 if positive, else zero Introduced July 2004
50	W140	= C140 – S140 if positive, else zero Introduced July 2004
...	"	

#### Large Exposures (Form LE3) Exposure categories

...

#### PART 3

This covers total exposures to banks<sup>11</sup> (or groups of closely related banks), irrespective of the ~~original~~ maturity of the exposure(s), where the exposure has equalled or exceeded 10% of the LECB in the reporting period.

...

#### PART 4

This covers exposures to banks where the (~~original~~) maturity is 1 year or less. You should show exposures to groups of closely related bank counterparties in total.

...

#### Liquidity Return (Form LR)

...

#### Off balance sheet cashflows

...

60 Convertible debt securities should be treated as equities where:

- i) the first date at which conversion may take place is less than three months ahead, or the next such date (where the first has passed) is less than a year ahead; and
- ii) the convertible debt security is trading at a premium of less than 10%, where the premium is defined as the current mark-to-market value of the convertible debt security less the mark-to-market value of the underlying equity, expressed as a percentage of the mark-to-market value of the underlying equity.

Convertible debt securities other than those defined above may be treated as equity or debt securities.

...

Supervisory Guidance Notes (SGN)

...

Appendix D

Central banks (central monetary institutions)

...

Middle East oil exporting countries

...

Iraq Central Bank of Iraq

Kuwait Bank al-Kuwayt al-Markazi

Central Bank of Kuwait

Kuwait Investment Authority

~~Kuwait Investment Office (London) — regard as non-resident~~

~~Government of Kuwait: Ministry of Finance~~

...

## Annex B

### Amendments to the Glossary

In this Annex underlining indicates new text and striking through indicates deleted text.

#### *EEA State*

(in accordance with paragraph 8 of Schedule 3 to the *Act* (EEA Passport Rights)) a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992, as it has effect for the time being; as at ~~21 June 2001~~ 1 May 2004, the following are the *EEA States*: Austria, Belgium, Cyprus, ~~the Czech Republic~~, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, the Netherlands, Norway, Poland, Portugal, the Slovak Republic, Slovenia, Spain, Sweden, and the *United Kingdom*.

#### *European Economic Area*

the area established by the agreement on the European Economic Area signed at Oporto on 2 May 1992, as it has effect for the time being, and which consists of the *EEA States*.

## Annex C

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

13.9 ~~[deleted] How does the Handbook apply to branches and cross-border services?~~

Delete the text in section 13.9 'How does the Handbook apply to branches and cross-border services?'

...

Appendix 3.2  
Purpose

Delete existing text in *SUP* Appendix 3.2 and insert following text as the new *SUP* Appendix 3.2:

3.2 Purpose

3.2.1 G The purpose of this appendix is to give *guidance*:

- (1) to *UK firms* on some of the issues that arise when carrying on *passported activities* (see *SUP* App 3.5 and *SUP* App 3.6);
- (2) to all *firms* on the relationship between *regulated activities* and activities passported under the *Single Market Directives* (see *SUP* App 3.9 and *SUP* App 3.10).

...

3.3.1 G (1) The European Community Treaty (the '*Treaty*'), as amended by later Treaties, established in EC law the rights of freedom of establishment and freedom to provide services in the European Community.

- (2) The *Treaty* lays down central principles governing the legal framework for freedom of establishment and the free movement of services in the European Community. There are, however, a number of areas where the legal position is not clear. This includes, for example, identifying whether a service is provided through an establishment, where the issues involved are complex. Therefore, this Appendix is intended to provide *guidance* but cannot be regarded as comprehensive. Ultimately, the construction of the *Treaty* and relevant Directive provisions is a matter for the European Court of Justice.

3.3.2 G The *Treaty* provides the framework for the provision of banking, ~~insurance and investment business~~, insurance business, investment business, UCITS management services and insurance mediation, while the *Single Market Directives* clarify the rights and freedoms within that framework.

...

- 3.3.6 G (1) The European Commission has not produced an interpretative communication on the *Investment Services Directive*. It is arguable, however, that the principles in the communication on the Second Banking Directive can be applied to *investment services*. This is because article 11 of the *Investment Services Directive* (containing provisions relating to conduct of business rules) also applies to the *investment services* of *firms* operating under the *Banking Consolidation Directive*.
- (2) The European Commission has not produced an interpretative communication on either the *Insurance Mediation Directive* or on the *UCITS Directive*.

...

Notification of establishing a branch or of providing cross border services

- 3.3.13 G The *Single Market Directives* require *credit institutions, insurance undertakings, investment firms, UCITS management companies* and *insurance intermediaries* to make a notification to the *Home State* before establishing a *branch* or provide *cross border services*.

SUP 13.5 (Notices of intention) sets out the notification requirements for a *firm* seeking to establish a *branch* or provide *cross border services*. As *firms* will note, the decision whether a passport notification needs to be made will be a matter of interpretation. The onus is on *firms* to comply with the requirements of the *Act* and, where relevant, the laws of other *EEA States*. So, in cases of doubt, *firms* should obtain their own legal advice on the specific issues involved.

- 3.3.14 G Blanket notification is the practice of the *Home State regulator* notifying all *Host State regulators* in respect of all activities regardless of any genuine intention to carry on the activity. This practice is discouraged by the *FSA*. However, a *firm* may be carrying on activities in the *United Kingdom* or elsewhere in a way that necessarily gives rise to a real possibility of the provision of services in other *EEA States*. In such cases, the *firm* should consider with its advisers whether it should notify the relevant authorities and include that possibility in its business plan.

...

Delete SUP App 3.4 and SUP App 3.5 in their entirety.

...

Delete SUP App 3.6.4 in its entirety.

- 3.6.4 G [deleted]

...

- 3.6.8 G The *FSA* is of the opinion that *UK firms* that are *credit institutions* and *ISD investment firms* should apply the 'characteristic performance' test (as referred to in ~~AUTH 3.6.7G~~ SUP App 3.6.7G) when considering whether prior notification is

required for services business. *Firms* should note that other *EEA States* may take a different view. Some *EEA States* may apply a solicitation test. This is a test as to whether it is the consumer or the provider that initiates the business relationship.

...  
Delete *SUP* App 3.6.12G, 3.6.13G, and 3.6.14G in their entirety.

....

Delete *SUP* App 3.6.16G to 3.6.24G in their entirety.

.....

Delete *SUP* App 3.6.28G to 3.6.31G in their entirety.

Delete *SUP* App 3.7 and *SUP* App 3.8 in their entirety.

...

3.9 Mapping of the Investment Services Directive ~~and~~ Banking Consolidation Directive, UCITS Directive and Insurance Mediation Directive to the Regulated Activities Order

3.9.1 G The following Tables 1 ~~and 2~~, 2, 2A and 2B provide an outline of the *regulated activities* and *specified investments* that may be of relevance to *firms* considering undertaking *passported activities* under the *Banking Consolidation Directive* ~~or~~ the *Investment Services Directive*, the *UCITS Directive* and the *Insurance Mediation Directive*. The tables may be of assistance to *UK firms* that are thinking of offering financial services in another *EEA State* and to *EEA firms* that may offer those services in the *United Kingdom*.

3.9.2 G The tables provide a general indication of the *investments* and activities specified in the *Regulated Activities Order* that may correspond to categories provided for in ~~either~~ the *Banking Consolidation Directive* ~~or~~ the *Investment Services Directive*, the *UCITS Directive* or the *Insurance Mediation Directive*. ~~The guidance does not cover the *UCITS Directive*~~. The tables do not provide definitive *guidance* as to whether a *firm* is carrying on an activity that is capable of being *passported*, nor do the tables take account of exceptions that remove the effect of articles. Whether a *firm* is carrying on a *passported activity* will depend on the particular circumstances of the *firm*. If a *firm's* activities give rise to potential *passporting* issues, it should obtain specialist advice on the relevant issues.

...

3.9.4 G Table: Activities set out in Annex I of the BCD

Table 1: BCD activities		Part II RAO Activities	Part III RAO Investments
...			

14.	Safe custody services	Article 64	Article 76-81, 83-85, 89
-----	-----------------------	------------	--------------------------

...

3.9.5 G Table: Services set out in Annex to the ISD

...

3.9.6 G Table: Activities set out in Article 5(2) and (3) of the UCITS Directive

<b><u>Table 2A: UCITS Directive activities</u></b>		<b><u>Part II RAO Activities</u></b>	<b><u>Part III RAO Investments</u></b>
1.	<u>The management of UCITS in the form of unit trusts / common funds or of investment companies; this includes the functions mentioned in Annex II of the UCITS Directive (see Note 2).</u>	<u>Article 14, 21, 25, 37, 51, 53, 64</u>	<u>Article 76-81, 83-85, 89</u>
2.	<u>Managing portfolios of investments, including those owned by pension funds, in accordance with mandates given by investors on a discretionary, client-by-client basis, where such portfolios include one or more of the instruments listed in Section B of the Annex to the ISD.</u>	<u>Article 14, 21, 25, 37, 53, 64</u>	<u>Article 76-81, 83-85, 89</u>
3.	<u>Investment advice concerning one or more of the instruments listed in Section B of the Annex to the ISD.</u>	<u>Article 53, 64</u>	<u>Article 76-81, 83-85, 89</u>
4.	<u>Safekeeping and administration services in relation to units of collective investment undertakings.</u>	<u>Article 40, 45, 64</u>	<u>Article 76-81, 83-85, 89</u>

Note 1. A UCITS management company can only exercise passport rights under the UCITS Directive (article 2(2)(h) of the ISD). A UCITS management company can only be authorised to carry on the non-core services set out in rows (3) and (4) of Table 2A if it is also authorised to carry on the activity set out in row (2) of the table.

Note 2. The functions set out in Annex 2 to the UCITS Directive are:

1. Investment management.



2. Administration:
  - a. legal and fund management accounting services;
  - b. customer inquiries;
  - c. valuation and pricing (including tax returns);
  - d. regulatory compliance monitoring;
  - e. maintenance of unit-holder register;
  - f. distribution of income;
  - g. unit issues and redemptions;
  - h. contract settlements (including certificate dispatch);
  - i. record keeping.
3. Marketing.

3.9.7

G

Table: Activities set out in Article 2(3) of the IMD

<b><u>Table 2B: IMD activities</u></b>		<b><u>Part II RAO Activities</u></b>	<b><u>Part III RAO Investments</u></b>
<u>1.</u>	<u>Introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance.</u>	<u>Articles 25, 53 and 64</u>	<u>Article 75, 89 (see Note 1)</u>
<u>2.</u>	<u>Concluding contracts of insurance</u>	<u>Article 21, 25, 53 and 64</u>	<u>Article 75, 89</u>
<u>3.</u>	<u>Assisting in the administration and performance of contracts of insurance, in particular in the event of a claim.</u>	<u>Article 39A, 64</u>	<u>Article 75, 89</u>

Note 1. Rights to or interests in *life policies* are *specified investments* under Article 89 of the *Regulated Activities Order*, but rights to or interests in *general insurance contracts* are not.

## **ADDENDUM**

### **SUPERVISION MANUAL (GUIDANCE AMENDMENT NO 1) INSTRUMENT 2004**

The cover sheet of this instrument, as adopted by order of the Board on 20 May 2004, is amended by the insertion of the underlined text and the deletion of the strikethrough text. For the sake of clarity, and following the adoption of the addendum, this amendment will be made to the cover sheet without showing the change.

#### **Commencement**

B. This instrument comes into force as follows:

- (1) Annexes A and B come into force on 1 June 2004; and
- (2) Annex C comes into force on ~~15~~ 14 January 2005.

**COMPENSATION SOURCEBOOK (REVIEWS OF PENSIONS BUSINESS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 213 (The compensation scheme); and
  - (4) section 214 (General).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 July 2004.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Compensation Sourcebook (Reviews of Pensions Business) Instrument 2004.

By order of the Board  
20 May 2004

## Annex

### Amendment to the Compensation sourcebook

Insert the following new provisions:

- 8.2.7 R        The *FSCS* may reject an application for compensation if:
- (1)        it relates to an event or transaction which has been reviewed under the provisions of a 'deemed scheme' as defined in the Financial Services and Markets Act 2000 (Transitional Provisions) (Reviews of Pensions Business) Order 2001 (SI 2001/2512); and
  - (2)        as a result of the review in (1) no redress was payable, or redress was paid, in accordance with the regulatory standards for the review of such events or transactions, and the terms of any scheme order, applicable as at the date of the review.
- 8.2.8 G        The purpose of *COMP* 8.2.7R is to allow the *FSCS* to reject claims relating to pensions review cases where a review was carried out in accordance with the relevant regulatory standards applicable at the time. 'Deemed schemes' are those review schemes set up before *commencement* (that is, 30 November 2001) but which are treated as schemes for the review of past business under the *Act*, namely the pensions review and *FSAVC* review.

**COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK  
(INCREASING CHOICE OF INVESTMENT FOR FUND OF FUNDS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) (a) section 138 (General rule-making power);  
(b) section 156 (General supplementary powers);  
(c) section 247 (Trust scheme rules); and
  - (2) regulation 6 (FSA rules) of The Open-Ended Investment Companies Regulations 2001 (SI 2001/1228).
- B. The rule-making powers identified above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Collective Investment Schemes sourcebook**

- D. The Collective Investment Schemes sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Collective Investment Schemes Sourcebook (Increasing Choice of Investment for Fund of Funds) Instrument 2004.

By order of the Board  
20 May 2004

## Annex

### Amendments to the Collective Investment Schemes sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Eligible combinations of scheme

5A.11.4R (1) A *fund of funds* scheme may invest in *units* in any five or more *authorised funds* within:

(a) any one of:

(i) UCITS schemes;

(ii) CIS 5A.4 (Securities schemes);

(iii) CIS 5A.5 (Money market schemes);

(iv) CIS 5A.6 (Futures and options schemes);

(v) CIS 5A.7 (Geared futures and options schemes);

(vi) CIS 5A.8 (Property schemes); and

(vii) CIS 5A.9 (Warrant schemes); or

(b) any combination of:

(i) UCITS schemes;

(ii) CIS 5A.4 (Securities schemes); and

(iii) CIS 5A.5 (Money market schemes).

(2) A *fund of funds scheme* may invest in *units* in any one or more *money market schemes* (within CIS 5A.5 (Money market schemes)) and in *units* in any one or more *authorised funds* ~~within any one of the other sections mentioned in~~ (1) within any one scheme type in (1)(a) or any combination permitted by (1)(b).

.....

**UKLA FEES (2004/2005) AND RELATED LISTING RULES (AMENDMENT)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 72 (The competent authority);
  - (2) section 74(4) (The official list);
  - (3) section 99(1) (Fees);
  - (4) section 101 (Listing rules: general provisions); and
  - (5) paragraphs 1 (General), 4 (Rules) and 7 (Fees) of Schedule 7 (The Authority as Competent Authority for Part VI).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Listing Rules**

- D. The Listing Rules are amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the UKLA Fees (2004/2005) and Related Listing Rules (Amendment) Instrument 2004.

By order of the Board  
20 May 2004



## Annex

### Amendments to the Listing Rules

In this Annex all the text is new and is not underlined; the places where the changes will be made are indicated.

Insert the following two rules after 1.2 and 2.5 respectively:

1.2A Issuers must pay the 'Annual fees' referred to in Schedule 13 within 30 days of receiving written notification of the fee payable. If an issuer has not paid the total amount of an annual fee by that date, then the issuer must pay an additional amount as follows:

- (1) if the fee was not paid in full by the due date, an administrative fee of £250; plus
- (2) if the fee was not paid in full before the end of 15 days after the due date, interest on any unpaid part of the fee at the rate of 5% per annum above the Bank of England's repo rate from time to time in force, accruing on a daily basis from the date on which the amount concerned became due.

2.5A Sponsors must pay the 'Annual fee' referred to in Schedule 13 within 30 days of receiving written notification of the fee payable. If a sponsor has not paid the total amount of an annual fee by that date, then the sponsor must pay an additional amount as follows:

- (1) if the fee was not paid in full by the due date, an administrative fee of £250; plus
- (2) if the fee was not paid in full before the end of 15 days after the due date, interest on any unpaid part of the fee at the rate of 5% per annum above the Bank of England's repo rate from time to time in force, accruing on a daily basis from the date on which the amount concerned became due.

Delete existing Schedule 13 and insert new Schedule 13 as follows:

#### **SCHEDULE 13**

#### **FEES**

#### **Fees for the period 1 June 2004 to 31 May 2005**

<b>Fee type</b>	<b>Fee amount</b>
<b>Annual fees</b>	
Note: Annual fees are charged in annual cycles beginning on 1 April of each year and ending on 31 March of the following year.	
Listing – All issuers of shares and certificates representing shares	<b>£3,950</b>

## Vetting fees

Note: Transaction fees relate to specific events or transactions that an issuer might be involved in during the year and fall due when documentation is first submitted to the UKLA.

<b>Category 1</b> – Documents relating to the following transactions:	<b>£5,700</b>
- Listing particulars / prospectuses for share and debt listings which fall outside Chapter 23 of the Listing Rules	
- New applicants for Certificates Representing Shares	
- Asset-backed securities	
- Placing and open offers	
- Rights issues	
- Class 1 transactions	

<b>Category 2</b> – Documents relating to the following transactions:	<b>£2,500</b>
- Debt issues falling in Chapter 23	
- Debt programmes falling in Chapter 23	
- Securitised derivatives falling in Chapter 24	
- Related party transactions	

<b>Category 3</b> – All other "vet only" transactions (except those which are specified in Category 4 below)	<b>£2,000</b>
--	---------------

<b>Category 4</b> – Vet only documents relating to the following:	<b>£500</b>
- Cancellation circulars / winding up circulars that do not require shareholder approval	
- Supplementary listing particulars	

Note: If a single vetting transaction includes elements which fall into two or more of the above fee categories, only one fee is payable being the highest fee of all the fees that would otherwise apply to that transaction.

## Application fees

Note: Application fees become payable when an issuer makes an application for listing

Tranches from debt issuance programmes falling in Chapter 23 and securitised derivative tranches	<b>£100</b>
All other applications	<b>£225</b>

## Sponsor fees

Note: Annual fees are charged in annual cycles beginning on 1 April of each year and ending on 31 March of the following year. Application fees become payable when a person applies for approval as a sponsor.

Annual fee	<b>£5,000</b>
Application fee	<b>£2,000</b>

**LISTING RULES (ANNOUNCEMENT HEADLINES) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 74 (The official list);
  - (2) section 96 (Obligations of issuers of listed securities);
  - (3) section 157 (Guidance); and
  - (4) paragraph 1 of Schedule 7 of the Act.

**Commencement**

- B. This instrument comes into force on 1 July 2004.

**Amendments to the Listing Rules**

- C. The Listing Rules are amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Listing Rules (Announcement Headlines) Instrument 2004.

By order of the Board  
20 May 2004

Amended by Addendum  
7 July 2004

## Annex

### Amendments to the Listing Rules

In this Annex, underlining indicates new text.

UK LISTING AUTHORITY GUIDANCE MANUAL

Appendix 5

PIP SERVICE CRITERIA

Procedures in relation to applications for the approval of services provided by a Primary Information Provider ("PIP")

...

Appendix to PIP service criteria – Headline categories for use with regulatory announcements

...	
MEDIUM PRIORITY	
Headline category	Description
Additional Listing	Notification of any addition to a company's existing share capital
...	
<u>Portfolio update</u>	<u>Periodic notification by an investment company/trust of its investment</u>
<u>Rule 2.10 Announcement</u>	<u>Announcement by an offeree company at the beginning of an offer period regarding details of all relevant securities issued by the company together with the numbers of such securities in issue as required by POTAM</u>
...	

**ADDENDUM**

**LISTING RULES (ANNOUNCEMENT HEADLINES) INSTRUMENT 2004**

This instrument is amended by the insertion of the underlined text.

Portfolio update	Periodic notification by an investment company/trust of its investment <u>portfolio as required by listing rule 21.20(1)</u>
------------------	--

**PERIODIC FEES (UNAUTHORISED MUTUAL SOCIETIES REGISTRATION)  
(2004/2005) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 156 (General supplementary powers); and
  - (2) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Unauthorised mutuals registration fees rules**

- D. The Unauthorised mutuals registration fees rules are amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Periodic Fees (Unauthorised Mutual Societies Registration) (2004/2005) Instrument 2004.

By order of the Board  
20 May 2004

## Annex

### Amendments to the Unauthorised mutuals registration fees rules

In this Annex all the text is new and is not underlined.

Insert new Annex 1R:

#### Periodic fees payable for the period 1 April 2004 to 31 March 2005

##### Part 1

Periodic fee payable by Registered Societies (on 30 June 2004)

This fee is not payable by a *credit union*.

Transaction	Total assets (£'000s)	Amount payable (£)
Periodic fee	0 to 50	60
	> 50 to 100	100
	> 100 to 250	150
	> 250 to 1,000	200
	> 1,000	370

##### Part 2

Periodic fee payable by sponsoring bodies (on 30 June 2004)

This fee is not payable by sponsoring bodies in respect of the model rules of *credit unions*.

Transaction	Amount payable (£)
Periodic fee payable for each set of <i>model rules</i>	150

##### Part 3

Methods of payment of periodic fees

Payment method	Additional amount or discount applicable
Direct debit	Discount of £20
Credit transfer (BACS, CHAPS)	Discount of £10
Cheque	None
Switch	None
Credit card (Visa or Mastercard only)	Additional 2% of sum paid

**COMPLAINTS SOURCEBOOK (MORTGAGE ENDOWMENT COMPLAINTS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers and related provisions listed in Schedule 4 to the Complaints sourcebook (Powers exercised).
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force on 1 June 2004.

**Amendments to the Dispute resolution: Complaints sourcebook**

- D. The Dispute resolution: Complaints sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Complaints Sourcebook (Mortgage Endowment Complaints) Instrument 2004.

By order of the Board  
20 May 2004



## Annex

### Amendment to the Dispute resolution: Complaints sourcebook

In this Annex, underlining indicates new text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

After provision No. 7 in this table, insert the following new provisions:

DISP Table: Transitional provisions table

1

(1)	(2)	(3)	(4)	(5)	(6)
Material provision to which transitional provision applies	Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force		
...					
7A	<i>DISP</i> 2.3.6R	R	Nothing in <i>DISP</i> 2.3.6R affects the position of a complaint which, on 31 May 2004, could not have been considered by the <i>Ombudsman</i> under <i>DISP</i> 2.3.1R(1)(c); or <i>DISP</i> 2.3.6R(1)(b) as it then stood.	From 1 June 2004	Amended with effect from 1 June 2004
7B	<i>DISP</i> 2.3.6R	R	In the case of a complainant falling within <i>DISP</i> 2.3.6R as amended by this instrument, (and whose time for referring a complaint under the <i>rules</i> as they stood before amendment has not expired), time will expire in accordance with the amended <i>rule</i> , save that if the final date would otherwise be before 30 November 2004 an explanation of	From 1 June 2004	Amended with effect from 1 June 2004

			<p>the final date will be in conformity with <i>DISP</i> 2.3.6R(2) provided it stipulates a final date which is not less than two months from the date on which the explanation is likely to be received by the complainant.</p>		
--	--	--	--	--	--

...

2.3.1

R (2) The *Ombudsman* can consider complaints outside the time limits in (1)(b) or (c) or in *DISP* 2.3.6R when, in his view, the failure to comply with the time limits was as a result of exceptional circumstances or where he is required to do so by the *Ombudsman Transitional Order* (see *DISP* 2.3.2 G) or where the *firm* has not objected to the *Ombudsman* considering the complaint.

...

## Exceptions for certain mortgage endowment complaints

- 2.3.6 R (1) If a complaint relates to the sale of an endowment *policy* for the purpose of achieving capital repayment of a mortgage and the complainant ~~would, as a result of this rule DISP 2.3.6, have more time to refer the complaint than under DISP 2.3.1 R(1)(c), the time for referring a complaint to the *Financial Ombudsman Service*:-~~ receives a letter from a *firm* or a *VJ participant* warning that there is a high risk that the *policy* will not, at maturity, produce a sum large enough to repay the target amount then, subject to (2), (3), (4) and (5):
- (a) ~~starts to run from the date the complainant receives a letter from a *firm* or *VJ participant* warning the complainant that there is a high risk that the *policy* will not, at maturity, produce a sum large enough to repay the target amount~~ time for referring a complaint to the *Financial Ombudsman Service* starts to run from the date the complainant receives the letter; and
  - (b) ~~ends six months from the date the complainant receives a second letter from a *firm* or *VJ participant* containing the same warning or other reminder of the need to act~~ ends three years from that date ("the final date").
- (2) Paragraph (1)(b) applies only if the complainant also receives within the three year period mentioned in (1)(b) and at least six months before the final date an explanation that the complainant's time to refer such a complaint would expire at the final date.
- (3) If an explanation is given but is sent outside the period referred to in (2), time for referring a complaint will run until a date specified in such an explanation which must not be less than six months after the date on which the notice is sent.
- (4) A complainant will be taken to have complied with the time limits in (1) to (3) above if in any case he refers the complaint to the *firm* or *VJ participant* within those limits and has a written acknowledgement or some other record of the complaint having been received.
- (5) Paragraph (1) does not apply if: (a) the *Ombudsman* is of the opinion that, in the circumstances of the case, it is appropriate for *DISP* 2.3.1 R(1)(c) to apply without modification; or (b) in respect of any particular complaint, the *firm* can show that the three year period specified in *DISP* 2.3.1 R(1)(c) had started to run before the complainant received any such letter as mentioned in *DISP* 2.3.6R(1)(a) .
-

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(AMENDMENT NO 9) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157 (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 August 2004.

**Amendments to the Interim Prudential sourcebook for investment businesses**

- C. The Interim Prudential sourcebook for investment businesses (IPRU(INV)) is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Amendment No 9) Instrument 2004.

By order of the Board  
17 June 2004

## Annex

### Amendments to the Interim Prudential sourcebook for investment businesses

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(INV), chapter 5 as follows:

5.7.1(6)(f) G Rule 5.7.1(4)(e) refers to group *large exposures*, which should be measured against group consolidated own funds or (if this would result in all *exposures* being classified as *large exposures*) by aggregating all the *exposures* of the individual entities in the group and measuring them against the *own funds* of the individual *firm* giving rise to the consolidated supervision requirement. If there is more than one *firm* in the group giving rise to the consolidated supervision requirement, the group *large exposures* should be measured against the *firm* with the smallest *own funds*.

...

5.7.2(4) G *A firm's parent is a financial holding company* if it carries out mainly *listed activities* or if its main business is to acquire holdings in companies undertaking these activities. For this purpose, the *FSA* interprets the phrases 'mainly' or 'main business' to mean where the balance of business, ~~i.e.~~ is over 50% of the relevant group or sub-group's balance sheet (measured on the basis of total assets) or profit and loss statement (measured on the basis of gross income).


**FINANCIAL CONGLOMERATES AND OTHER FINANCIAL GROUPS  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 150(2) (Action for damages);
  - (3) section 156 (General supplementary powers);
  - (4) section 157(1) (Guidance); and
  - (5) section 340 (Appointment).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. The annexes to this instrument come into force as indicated in the following table.

Annex	Commencement Date
D. (IPRU (FSOC))	With respect to a particular firm, group or financial conglomerate, from the earlier of the day on which rule 4.2 of the Interim Prudential sourcebook for insurers ceases to be of effect and the first day of its financial year beginning in 2005.
G. (PRU)	<ul style="list-style-type: none"> <li>• Transitional provisions: on the dates specified in the transitional provisions;</li> <li>• PRU 8.1, PRU 8.4.25 to 8.4.31, PRU 8.4.34 to 8.4.36, as well as the guidance thereon, PRU 8.5.8 and 8.5.9 (with respect to a particular firm, group or financial conglomerate) from the first day of its financial year beginning in 2005; and</li> <li>• remaining provisions on 11 August 2004.</li> </ul>
L. (Glossary)	As for the provision in which a term is used.
A. (COND) B. (IPRU(BANK)) C. (IPRU(BSOC)) E. (IPRU(INS)) F. (IPRU(INV)) H. (AUTH) I. (SUP) J. (DEC) K. (ELM)	 <p>With respect to a particular firm, group or financial conglomerate, from the first day of its financial year beginning in 2005.</p>

## Amendments to the Handbook

- D. The modules of the FSA's Handbook listed in column (1) are amended or inserted in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Threshold Conditions (COND)	Annex A
Interim Prudential sourcebook for banks (IPRU(BANK))	Annex B
Interim Prudential sourcebook for building societies (IPRU(BSOC))	Annex C
Interim Prudential sourcebook for building societies (IPRU(FSOC))	Annex D
Interim Prudential sourcebook for insurers (IPRU(INS))	Annex E
Interim Prudential sourcebook for investment business (IPRU(INV))	Annex F
Integrated Prudential sourcebook (PRU)	Annex G
Authorisation manual (AUTH)	Annex H
Supervision manual (SUP)	Annex I
Decision making manual (DEC)	Annex J
Electronic money sourcebook (ELM)	Annex K
Glossary of definitions	Annex L

## Citation

- E. This instrument may be cited as the Financial Conglomerates and Other Financial Groups Instrument 2004.

By order of the Board  
15 July 2004

Amended by Addendum  
17 August 2004

## Annex A

### Amendments to the Threshold Conditions

In this Annex, underlining indicates new text.

2.5.3 G ...

- (3) In relation to a firm which is an EEA regulated entity, the Financial Groups Directive provides that the FSA should consult other competent authorities when assessing the suitability of the shareholders and the reputation and experience of directors involved in the management of another entity in the same group.



## Annex B

### Amendments to the Interim Prudential sourcebook for banks

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

Amend IPRU(BANK), Volume 1, Chapter GN, Sections 2 and 3 as follows:

#### PURPOSE

3. ...
4. The purpose of the prudential standards set out in this sourcebook is to ensure that banks maintain capital and other financial resources commensurate with their risks and appropriate systems and controls to enable them to manage those risks. The FSA requires in particular that banks maintain adequate capital against their risks: capital enables banks to absorb losses without endangering customer deposits; that they maintain adequate liquidity; and that they identify and control their large credit exposures - which might otherwise be a source of loss to a bank on a scale that might threaten a bank's solvency.
5. This sourcebook, together with the separate prudential sourcebook applying to building societies, also implements EC directives setting out prudential standards as these apply to *credit institutions*. Where a bank is part of a financial conglomerate, it will also be subject to additional rules and guidance set out in PRU 8.4. A bank with an ultimate non-EEA parent may also be subject to some provisions in PRU 8.5. And all banks that are part of a group are subject to the general provisions in PRU 8.1.

...

#### Definitions

Insert new definitions in the following table in the appropriate alphabetical position:

- 3.5.1 R In this section the term or phrase in the first column of the following table has the meaning given to it in the second column:

...	
<u>financial holding company</u>	<u>A financial institution whose subsidiary undertakings are either exclusively or mainly credit institutions or financial institutions ( at least one being a credit institution ) and which is not a mixed financial holding company.</u>
<u>financial institution</u>	<u>( when used in chapters GN, CA and CS ) See definition in <i>Glossary</i></u>
firm	
...	
<u>mixed-activity</u>	<u>A parent undertaking that is not a financial holding company, or</u>

<u>holding company</u>	<u>a credit institution, or a mixed financial holding company, whose subsidiaries include at least one credit institution.</u>
<u>mixed financial holding company</u>	<u>See definition in the <i>Glossary</i>.</u>
...	
<u>participation</u>	<u>See definition in the <i>Glossary</i>, except where the context otherwise requires (such as in the phrase "sub-participation" ).</u>
...	
<u>PRU</u>	<u>See definition in the <i>Glossary</i>.</u>
...	...

...

Amend IPRU(BANK), Volume 1, Chapter CA, Section 1 as follows:

1.2 Legal sources

- 3 The sources noted in the Legal Sources section of the Capital Adequacy Overview chapter are also relevant to this chapter.
- 4 The Banking Consolidation Directive (formerly The Directive on Own Funds, “Own Funds Directive”, “OFD” - 89/299/EEC) establishes a standard EU definition of capital for prudential supervisory purposes. This follows closely the Basel Convergence Agreement on capital standards. The Directive has been amended by the Financial Groups Directive (2002/87/EC) and some of the resulting changes are given effect in this chapter.
- 5 The Capital Adequacy Directive (“CAD” - 93/6/EC) introduced Tier 3 capital for use in supporting trading book activities.
- 6 The Banking Consolidation Directive (formerly the Second Banking Co-ordination Directive, “2BCD” - 89/646/EEC) sets the minimum initial capital requirement and minimum ongoing capital requirement for banks incorporated in the European Economic Area.

See s3

...

Amend IPRU(BANK), Volume 1, Chapter CA, Section 10 as follows:

10.2 Deductions from the total of Tier 1 capital and Tier 2 capital

- 2 Certain deductions should be made from the total of Tier 1 (after Tier 1 deductions) and Tier 2 capital:
  - (a) Investments in subsidiaries and associates which fall outside the scope of a bank’s capital adequacy return (including all *material insurance holdings*);
    - (a) ...
    - (b) ...

- (c) ...
- (d) Investments in life assurance companies should be treated on the same principles as other investments. The amount of any *material insurance holding* should (subject to (i) below ) be deducted from the total of Tier 1 and Tier 2 capital. A *material insurance holding* means the higher of:

- (1) the book value of an *investment* held in an insurance undertaking, reinsurance undertaking, or insurance holding company (*investment* for this purpose is either a participation, or the investment in a subsidiary undertaking); or
- (2) the bank's proportionate share of that undertaking's local or notional regulatory capital requirement.

Where the undertaking is a subsidiary and it has a solvency deficit, the subsidiary's local or notional regulatory requirement should be deducted in full. A description of how a notional capital requirement is to be calculated is set out in paragraphs 6.7 and 6.8 in Part 6 of PRU 8 Annex 1. A notional requirement should be calculated in all cases where the undertaking is not regulated to EEA or equivalent standards: this is also explained in paragraphs 6.7 and 6.8 in Part 6 of PRU 8 Annex 1.

- (i) ~~However, w~~Where an insurance affiliate undertaking is accounted for using the *embedded value* method, theis following treatment should be ~~applied~~ modified as follows (unless the regulatory capital requirement is the higher figure):

- On acquisition, any “goodwill” element, i.e. the difference between the acquisition value according to the *embedded value* method and the actual investment, should be deducted from Tier 1 capital.
- The *embedded value* should be deducted from the total of Tier 1 & 2 capital.
- Post-acquisition, where the *embedded value* of the ~~company~~ undertaking increases, the increase should be added to reserves, while the new *embedded value* is deducted from total capital. This means that the net impact on the level of capital is zero, although Tier 2 headroom will increase with any increase in Tier 1 reserves.

- (ii) *Embedded value* is the value of the company taking into account the present value of the expected future inflows from existing life assurance business.

- (e) ...

See ch CS s2 & s9

(b)...

(c) All holdings of capital instruments issued by other *credit institutions* and *financial firms-institutions* unless these are covered by a *trading book concession*;

(a) ...

See s3.1

(b) ...

(c) ~~For the purposes of this sub-section~~ The definition of a financial institution is defined as a directly supervised institution (or a financial holding company above a supervised financial institution) whose exclusive or main business is to carry out one or more of the activities listed in points 2-12 in Annex I to The Banking Consolidation Directive (formerly the Annex to 2BCD). These activities are listed in items (b) to (l) of the Appendix to Chapter EU, given in the Glossary

...

10.4 Deductions of qualifying holdings from Tiers 1 and 2 capital

...

22 For the purposes of qualifying holding deductions, ~~commercial~~ non-financial undertakings are defined as all undertakings other than:

See s10.4

(a) Credit *and certain* financial institutions;

*a) ~~The above are defined to be credit institutions, supervised financial firms and financial holding companies whose exclusive or main business is to carry out one or more of the activities listed in points 2-12 of Annex I to the Banking Consolidation Directive (formerly the Annex to 2BCD). These activities are also listed in points (b) to (l) of the Appendix to Chapter EU~~*

The capital instruments of institutions which meet the definition of financial and credit institutions in section 10.2 fall outside the scope of qualifying holdings. (The full definition of *financial institution* is in the Glossary.)

(b) Institutions whose exclusive or main activities are a direct extension of banking, or concern services ancillary to banking, such as leasing, factoring, the management of unit trusts, the management of data processing services supporting banking services or any other similar activity; and

a) These activities are set out in Article 43(2)(f) of the Bank Accounts Directive (86/635/EEC).

(c) Insurance and reinsurance companies, and insurance holding

companies.

- a) The definition of an insurance ~~company~~ undertaking is contained in the First Non-Life Insurance Directive (73/239/EC) ~~as amended by the Second Non-Life Insurance Directive and Article 4 of the First Life Insurance Assurance Directive (-79/267/EEC-) (2002/83/EC) as amended by the Act of Accession of 1985.~~ The definition of reinsurance undertaking is contained in the Insurance Groups Directive (98/78/EC).

...

Amend IPRU(BANK), Volume 2, Chapter LE as follows:

- 2 The rationale for a large exposures policy  
1 ...  
2 ...  
3 ...  
4 The need to control risk concentration was the main reason for the minimum standards for a limits-based approach towards large exposures brought in by the LED (now replaced by The Banking Consolidation Directive). Where appropriate, the FSA's policy goes further, to reflect its own view of what constitutes a prudent approach in this key area of banks' internal management controls. ( Following the amendments to the Banking Consolidation Directive resulting from the Financial Groups Directive, the FSA is also required to supervise transactions between a bank and a mixed activity holding company (MAHC), to have significant transactions with the MAHC reported to the FSA; and to take appropriate action if these intra-group transactions pose a threat to the bank's financial position.)

These requirements are set out below.

- (i) The FSA's existing requirements for the control and monitoring of exposures to connected counterparties , set out in this chapter LE (particularly section 9.2.2 ) and the large exposures reporting forms in SUP 16 Ann 1R.
- (ii) A specific new requirement in SUP 16.7 to report significant transactions with an MAHC that do not constitute exposures; and
- (iii) The requirements (Rule 3.3.19 and PRU 8.1) for a bank to have the systems to enable the control and monitoring described above, and provide the necessary information for reporting to the FSA.

Amend IPRU(BANK), Volume 2, Chapter CS as follows:

## CONSOLIDATED SUPERVISION

### 1. INTRODUCTION

#### 1.1 Legal sources

See COND1

- A bank's compliance with the policy set out in this chapter will help establish that it satisfies the Threshold Conditions (as to "Adequate resources" and "Suitability") and complies with the Principles (as to "Management and control" and "Financial prudence").
- 2 The Banking Consolidation Directive (2000/12/EC) ~~formerly the Second Consolidated Supervision Directive 92/30/EEC~~ sets required minimum standards for the performance of consolidated supervision of groups including banks within the EEA. This chapter on consolidated supervision is the principal vehicle implementing ~~2CSD (now replaced by those parts of The Banking Consolidation Directive)~~ that derive originally from the Second Consolidated Supervision Directive (92/30/EEC) and have now been further amended by the Financial Groups Directive (2002/87/EC). Banks that are part of a group should also refer to the rules and guidance on group risks in PRU 8.1.
- 3 The Capital Adequacy Directive (CAD - 93/6/EEC) introduced both a framework for capital requirements for market risk and a requirement for a consolidated assessment of groups including investment firms. This chapter includes the updates to the consolidated supervision regime applied to banks which resulted from its implementation, most notably the introduction of aggregation plus as a technique for consolidating trading book exposures in some cases for CAD banks.
- 4 The obligations in these directives require consolidation ~~only~~ up to the highest relevant parent incorporated in the EEA. ~~and not to~~ Where the ultimate parents is outside the EEA, the FSA also needs to establish whether the bank is subject to equivalent consolidated supervision by the competent authorities in the ultimate parent's home country, and if not, to take appropriate measures to achieve the objectives of the Banking Consolidation Directive. This is covered in more detail in PRU 8.5: banks with non-EEA parents should therefore note that they are also subject to the relevant provisions in PRU 8.5.
- 4A It is open, however, to supervisors to go further than the minimum requirements. It may be important to consolidate other parts of the group, in order to have all the relevant risks included. The FSA is committed to extending its consolidated supervision beyond the requirements of the directives if the result is a more accurate assessment of risk to a bank. Moreover, where a banking group includes an entity active in the insurance sector, it may possibly constitute a *financial conglomerate* and would then be subject to additional rules and guidance necessary to implement the Financial Groups Directive in such cases. The exact definitions and criteria as to what constitutes a *financial conglomerate*, and the additional rules and guidance that apply to them, are set out in PRU 8.4. If a banking group is, or becomes, a *financial*

conglomerate, it will be subject to these additional rules and guidance, as well as to the rules and guidance in this chapter.

## 1.2 Application

5 This chapter applies to UK-incorporated banks (and banking groups with UK-incorporated non-bank parents) only.

- (a) Banks incorporated elsewhere in the EEA with UK branches are, of course, subject to the requirements of the "2CSD" (now replaced by The Banking eConsolidation Directive as implemented by their home supervisors.

## 1.3 How this chapter is organised

6 ...

7 ...

8 ~~Section 8 covers~~ Material on qualitative consolidated supervision, formerly in section 8 of this chapter (now deleted), has been replaced by the rules and guidance in PRU 8.1. And Section 9 explains the solo consolidation treatment which may be adopted for solo purposes.

...

## 2 THE FSA'S APPROACH TO CONSOLIDATED SUPERVISION

1 ...

2 ...

3 ...

4 ...

5 The FSA regards consolidated supervision as a complement to, not a substitute for, solo supervision.

- (a) Solo supervision is needed as well. For events elsewhere in the group and the activities of other group companies can pose a threat to the bank in ways which consolidated supervision alone cannot detect: for example, intra-group linkages arising from transactions between the bank and other group companies will only be revealed by solo supervision. And a complementary assessment of solo capital adequacy permits an assessment of whether, so far as the bank itself is concerned, there is an appropriate distribution of capital in a group.
- (b) So institutions should comply with the FSA's policy on capital adequacy and large exposure on both a solo (or solo-consolidated) and a consolidated basis.

The FSA also seeks to ensure that persons who effectively direct the business of a financial holding company are of sufficiently good repute and have sufficient experience to perform these duties. This requirement was introduced into the Banking Consolidation Directive by the Financial Groups Directive ( article 54a of the Banking Consolidation Directive as inserted by article 29(8) of the Financial Groups Directive). But without prejudice to this specific requirement , the Directive also makes clear that the consolidation of the financial situation of a financial holding company ( as part of the consolidated supervision of its banking subsidiary by the FSA ) in no way implies that the FSA is required to play a supervisory role in relation to that financial holding company on a stand-alone basis .

Article 55a of the Banking Consolidation Directive (as inserted by article 29(9) of the Financial Groups Directive ) also requires the FSA to exercise general supervision over transactions between a bank that is a subsidiary of a mixed activity holding company ( MAHC ), and the MAHC itself and its other subsidiaries. The relevant guidance to banks is set out in section 3 of this chapter, para 3.1.4. If these intra-group transactions were to pose a threat to the bank's financial position , the FSA will take appropriate measures.

...

### 3 QUANTITATIVE CONSOLIDATED SUPERVISION

...

#### 3.1.3 Adequate controls

See ch GN s3

5 A bank should have adequate internal control mechanisms to produce any data and information which might be relevant for the purpose of supervision on a consolidated basis :this is now placed on a new and stronger footing in PRU 8.1 (see also rule 3.3.19 which requires a bank to have adequate systems and controls which enable it to monitor, control and calculate its large exposures).

#### 3.1.4 Intra group transactions with MAHC

5A Where a bank's parent is a mixed-activity holding company (MAHC), the FSA is required to supervise transactions between the bank, and the MAHC and its other subsidiaries, and any significant transactions are to be reported to the FSA. The most important category of such transactions will be those ( i.e. credit exposures and off balance sheet items ) that give rise to "exposures" to the relevant connected counterparty for the purposes of chapter LE and the large exposure reporting forms . The FSA considers that in these cases the directive requirement is adequately met by the existing arrangements under which the bank's exposures to individual, or groups of, connected counterparties are reported and monitored ( see 3.1.2 above, and also chapter LE section 9.2.2, and the large exposure reporting forms in SUP 16Ann 1R ). Reporting of other significant transactions (that do not give rise to “exposures”) is also now required as a separate item by SUP 16.7.8R. The requirements for the bank to have adequate systems and controls to produce the necessary information (see 3.1.3 above), and systems and controls generally to mitigate group risk, are also covered in PRU 8.1 which applies to all banks that are part of groups.

...



## 4 Scope of consolidation

### 4.1 INTRODUCTION

See Supervision Manual chapter 16

1 ...

### 4.2 Domain of consolidation within a group including a bank

2 Consolidation should be undertaken in the following cases:

...

(a) ...

(b) when the bank is not the *parent* company, but:

(i) the bank is part of a group or sub-group whose business wholly or *mainly* comprises the *listed activities*; and

(ii) the *parent* of the group or sub-group is itself a *financial institution*.

See a10.1

(a) The *listed activities* are those given in the first paragraph of the first appendix to this chapter.

See s4.3

(b) The definition of *parent* is given below.

(c) To qualify as a *financial institution*, the exclusive or *main business* of a company should be either to carry out one or more of the listed activities or to acquire holdings in companies undertaking these activities. The formal definition of a *financial institution* is given in the Glossary.

(d) ...

...

### 4.3 Companies to be consolidated

3 Consolidation then extends to all relevant financial companies within that domain: that is the *parent company*; its *subsidiaries*; and companies in which the parent or its subsidiaries have a *participation*.

(a) The definitions used of *parent* and *subsidiary* are those contained in the Seventh Company Law Directive (83/349/EEC); these are implemented in the United Kingdom in section 258 of the Companies Act 1985. The definition of *participation* is set out in the Table in chapter GN.

(b) The notion of *subsidiary* is also normally extended to cover a company over which the parent or one of its subsidiaries exercises *dominant influence*. The criteria used to determine whether dominant influence exists are those provided by the contemporary UK accounting standards.

(i) The relevant accounting standard is FRS2, Accounting for Subsidiary Undertakings.

- (c) The threshold for the consolidation of group companies which are not subsidiaries – *participations* – is the ownership of 20% or more of the voting rights or capital.
- (d) In the case where undertakings are linked to the domain of consolidation by a relationship within the meaning of article 12(1) of Directive 83/349/EEC (see definition of "consolidation article 12(1) relationship" in the Glossary), the FSA will determine how consolidation is to be carried out.
- (e) Asset management companies ( which for this purpose has the meaning given in the Glossary ) are also to be consolidated, whether or not they come within the definition of *financial institution* , thereby fulfilling specific requirements in the Financial Groups Directive.

4 Companies whose business is not financial are not usually included in the consolidation; however, the FSA may consider that it is appropriate to include them.

- (a) Insurance and the broking of insurance are not financial activities for this purpose, and so these companies are not usually included in a consolidation.

See ch CA s10

- (i) For an explanation of the treatment of investments in insurance companies, see the chapter on the definition of capital.

5 A non-financial subsidiary or *participation* should be excluded from the consolidation only with the FSA's prior agreement. If the exclusion is agreed, the investment in that company should be deducted from consolidated capital and its assets not included in group weighted risk assets.

...

4.4 General exceptions to the above policy

6 As provided for by ~~article 3.3 of the 2CSD (now replaced by Article 52.3 of The Banking Consolidation Directive,~~ in a limited number of cases the FSA may permit the exclusion from a bank's consolidated returns of subsidiaries or participations which otherwise meet the criteria for consolidation, where:

...

4.5 The policy where a bank is subject to consolidated supervision elsewhere

9 Where a bank is a member of a group including a number of EEA-incorporated banks, the FSA may, following discussion with the other supervisor(s), agree that consolidation is not necessary.

10 For a group including a bank whose ultimate parent is incorporated in a country outside the EEA, the treatment of the whole group is set out in PRU 8.5. This does not affect the usual operation of the Banking Consolidation Directive for the EEA sub-group i.e. from the highest relevant EEA parent down. ~~consolidation of the whole group is not normally necessary.~~

~~In determining the appropriate treatment in these cases, the FSA takes into account whether the parent company is subject to consolidation supervision (by another~~

~~supervisor) that adheres to the Basel minimum standards for the supervision of international banking groups and their cross border establishments~~

In those cases in which it determines that a whole-group consolidation would not be appropriate, the FSA nonetheless considered that sub-consolidation from the highest relevant EEA parent down, as outlined above, would be appropriate.

#### 4.6 Groups not subject to consolidation

- 11 When a bank belongs to a group or sub-group for which the FSA determines consolidation would be inappropriate (for example in cases where the preponderance of the group's business comprises industrial or insurance business), the FSA may ask the parent institution and its other subsidiaries to supply it with any data or information which it considers relevant to the purpose of supervising the bank.
- 12 When the parent of a bank is an insurance company (but the whole group does not constitute a financial conglomerate), the FSA does not normally consider it necessary to consolidate down from the insurance company, pending further harmonisation of the basis of accounting for banks and insurance companies. However, the FSA seeks to liaise with the supervisors of the insurance company parent if that supervisor is not the FSA. Where the group as a whole constitutes a financial conglomerate, it will in any case be subject to the additional rules and guidance on consolidated supervision set out at PRU 8.4.

...

After Chapter CS, Section 7 delete Section 8 in its entirety.

## 8 QUALITATIVE CONSOLIDATED SUPERVISION

[deleted]

## Annex C

### Amendments to the Interim Prudential sourcebook for building societies

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

Amend IPRU(BSOC), Volume 1, Chapter 1 as follows:

1 SOLVENCY

...

1.4 EU Directives

...

1.4.6 G The BCD also requires the FSA to carry out consolidated supervision of building society groups. The EU provisions for consolidated supervision have been supplemented by the Financial Groups Directive (2002/87/EC). Where a building society group includes an entity active in the insurance sector, while the group's main business lies in the deposit-taking sector, it may possibly constitute a "financial conglomerate" ( though the FSA expects this will be rare, at least in the near future ). The exact definitions and criteria as to what constitutes a "financial conglomerate" and the additional rules and guidance that apply to them, are set out in the Integrated Prudential Sourcebook (PRU) at PRU 8.4. If (but only if) a building society is, or becomes , a financial conglomerate, it will be subject to these additional rules and guidance , as well as to the rules and guidance in this IPRU (BSOC). Moreover, all building societies that are part of a group are subject to the general provisions in PRU 8.1.

...

1.8 Deductions

1.8.1 G Societies should make certain deductions from own funds and observe certain restrictions on the inclusion of Tier 2 items. The deductions comprise:

(1) ...

(2) ...

(3) ...

(4) ...

- (5) the amount of any material insurance holding (see Annex 1 D for definitions), relating to an insurance undertaking, reinsurance undertaking, or insurance holding company.

1.8.2 G Societies may be expected to make a deduction from own funds to reflect the existence of a contingent liability which, if called, would create an asset that societies would be required to deduct from own funds.

N B: See section 1.13 for ~~deductions in respect~~the treatment of insurance companies that are subsidiaries, section 1.14 for MIG captives, section 1.16 for holdings in other institutions, and for possible deductions arising out of securitisation, section 1.15.

...

### 1.13 Exclusions from Consolidation

1.13.1 G Subject to a limited degree of discretion allowed to the supervisory authorities, the BCD requires building societies to consolidate subsidiary undertakings which are financial or credit institutions (defined in Annex 1D) for the purposes of calculating their solvency ratio. However unless:

- (1) the inclusion of a particular non financial institution or non-credit institution subsidiary undertaking would result in a higher solvency ratio than if it were to be excluded; or
- (2) the FSA specifically requires the subsidiary undertaking to be excluded;

societies should include all their subsidiary undertakings when calculating their solvency ratio. Exclusion is likely where the FSA believes that a subsidiary's inclusion in the consolidation would be misleading or inappropriate. Life insurance ~~and~~ general insurance, reinsurance and insurance holding companies fall into this category : societies are already expected to deduct material insurance holdings from own funds (see section 1.8 above ). ~~and~~ Societies should calculate their solvency ratio after reversing the impact of the investment in, or consolidation of, these subsidiary undertakings. In the society only ratio calculation, the carrying value of the investment should be removed from the weighted asset total, and an equal deduction made from the society's own funds. In the consolidated ratio calculation, the weighted assets of the insurance subsidiary should be removed from the consolidated weighted assets, and the reserves of the subsidiary consolidated into group own funds should be reversed out, including any benefit of the embedded value taken through the group's reserves. The only profits of the subsidiary that may count as group own funds are those that have been distributed to the parent society i.e. as dividends. Societies should also note that the consolidation of asset management companies ( which for this purpose have the meaning given in the Handbook Glossary ) is now required by article 30 of the Financial Groups Directive, whether or not they come within the definition of a financial institution.

...

## 1.16 Deductions in Respect of Holdings in Other Institutions

....

1.16.3 G The Directive gives member states the option not to apply the restrictions to life and general insurance companies or reinsurance companies; and not to apply them in other cases provided they require a deduction from the credit institution's own funds of 100% of the amount in excess of the 15% or 60% limits.

1.16.4 G The FSA has decided not to apply the limits to participation in insurance or reinsurance companies but under section 1.8 above - "material insurance holdings" – see Annex 1D for definitions - are already subject to deduction from the society's own funds; see also section 1.13 for capital treatment in respect of holdings on the exclusion of insurance companies subsidiaries from consolidation. The FSA has also decided not to apply the limits in other cases but to recommend a 100% deduction from own funds of the amount of the holding in excess of 15%.

...

Calculation of "Own Funds"

...

### 1A.6 *Own funds*

1A.6.1 Gross own funds comprise Tier 1 capital plus Tier 2 capital. From this should be deducted:

- (1) ...
- ...
- (4) any deductions in respect of insurance reinsurance or insurance holding companies (section ~~1.13~~1.8), MIG Captives (section 1.14), holdings in other undertakings (section 1.16) and securitisation (paragraph 1.15.2);

to arrive at "own funds".

...

## ANNEX 1D

~~HOLDINGS OF CAPITAL INSTRUMENTS OF OTHER CREDIT AND FINANCIAL INSTITUTIONS TO BE EXCLUDED DEDUCTIONS FROM "OWN FUNDS" CALCULATIONS~~

### DEFINITIONS ( for section 1.8 )

G

Insert the following new definitions in Annex 1D.1:

## 1D.1 Definitions

...

1D.1.4 Material Insurance Holding means the higher of

- a. the book value of an investment held in an insurance undertaking, reinsurance undertaking, or insurance holding company ("investment" for this purpose is either a participation, or the investment in a subsidiary undertaking), or
- b. the society's proportionate share of that undertaking's local or notional regulatory capital requirement.

Where the undertaking is a subsidiary and it has a solvency deficit, the subsidiary's local or notional regulatory requirement should be deducted in full.

A description of how a notional capital requirement is to be calculated is set out in paragraphs 6.7 and 6.8 in Part 6 of PRU 8 Annex 1. A notional requirement should be calculated in all cases where the undertaking is not regulated to EEA or equivalent standards : this is also explained in paragraphs 6.7 and 6.8 in Part 6 of PRU 8 Annex 1.

1D.1.5 Participation means

- (1) a participating interest as defined in section 260 of the Companies Act 1985 (participating interests): or
- (2) the direct or indirect ownership of 20% or more of the voting rights or capital of an undertaking.

## Annex D

### Amendments to the Interim Prudential sourcebook for friendly societies

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Chapter 7

#### DEFINITIONS

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##### Part I Definitions

7.1 In this Part of the *IPRU(FSOC)*, unless the contrary intention appears, the following definitions apply –

*insurance holding company* means a parent undertaking whose main business is to acquire and hold participations in subsidiary undertakings, where:

- (a) those subsidiary undertakings are exclusively or mainly insurance undertakings;
- (b) at least one of those subsidiary undertakings is a UK insurer or an EEA firm that is a regulated insurance entity; and
- (c) it is not a mixed financial holding company. ~~an undertaking whose main business is to acquire and hold participations in subsidiary undertakings, where those subsidiary undertakings are exclusively or mainly insurance undertakings;~~

*notional required minimum margin* means:

- (a) in the case of an insurance undertaking (other than a pure reinsurer) that has its head office in a designated state or territory, the amount of the required minimum margin, or the equivalent requirement under the regulatory requirements of that state or territory;
- (b) in the case of a pure reinsurer that has its head office in a designated state or territory, the amount that would be the required minimum margin, or the equivalent requirement under the regulatory requirements of that state or territory, if the regulatory requirements of that state or territory applicable to undertakings carrying on direct insurance business were applied to the pure reinsurer (whether they are or not); and
- (c) in all other cases, the amount of the required minimum margin that would apply if the insurance undertaking were an insurer (other than a pure reinsurer), with its head office in the United Kingdom (whether it



is or not)
<u>participating undertaking</u> means <u>an undertaking which is either a parent undertaking or other undertaking which holds a participation in or is linked by a consolidation Article 12(1) relationship with the undertaking in question</u> <del>an undertaking which holds a participation in another undertaking;</del>
<u>proxy capital resources requirement</u> means the <u>solo capital resources requirement to which an undertaking would have been subject if it had a permission for each activity it carries on anywhere in the world, so far as that activity is a regulated activity.</u>
<u>regulated related undertaking</u> means a <u>related undertaking that is any of the following:</u>
(a) <u>a regulated entity;</u>
(b) <u>an insurance undertaking which is not a regulated insurance entity;</u>
(c) <u>an asset management company;</u>
(d) <u>a financial institution which is neither a credit institution nor an investment firm;</u>
(e) <u>a financial holding company; or</u>
(f) <u>an insurance holding company.</u>
<u>related undertaking</u> means <u>in relation to an undertaking 'U':</u>
(a) <u>any subsidiary undertaking of U;</u>
(b) <u>any undertaking in which U or any of U's subsidiary undertakings holds a participation;</u>
(c) <u>any undertaking linked to U by a consolidation Article 12(1) relationship; or</u>
(d) <u>any undertaking linked by a consolidation Article 12(1) relationship to an undertaking in (a), (b) or (c).</u>
<del>an undertaking in which a participation is held by another undertaking or which is a subsidiary undertaking;</del>
<u>relevant regulatory requirements</u> means:
(a) <u>in the case of a related undertaking that is an insurance undertaking, established in a designated state or territory, at the option of the friendly society:</u>
(i) <u>the regulatory requirements of that state or territory applicable to</u>

an undertaking carrying on *direct insurance business* (even if it only carries on *reinsurance* business or is an *insurance holding company*), or

(ii) the requirements referred to in (b);

(b) in the case of any other *insurance undertaking* or *insurance holding company*, the rules in *IPRU(INS)* applicable to an *insurer* (other than a *pure reinsurer*) with its head office in the United Kingdom (whether or not it is such an *insurer*)

*surplus assets* has the meaning given in paragraph 3(3) of Appendix 4 ~~except that in relation to a *related undertaking* which is an *insurance undertaking* or an *insurance holding company* it has the meaning given in *IPRU (INS)*;~~

PART II – General Provisions

7.2 A word or phrase which is printed in italics is used in the defined sense. Where a word or phrase is printed in italics and is not given a meaning in Part 1 of Chapter 7, that word or phrase has the meaning given to it in the Handbook Glossary.

7.3 ...

## Appendix 4

### ASSET VALUATION RULES

#### Shares in a related undertaking

- ~~3. (1) Where any *shares* are held by a *friendly society* in a *related undertaking*, which is an *insurance undertaking* or *insurance holding company*:~~
- ~~(a) the value of the *shares* must not exceed the value, determined in accordance with rule 4.2 of *IPRU(INS)* of the *related undertaking's* surplus assets (as defined in *IPRU(INS)*);~~
  - ~~(b) the *friendly society* must make provision in respect of the *related undertaking* in accordance with rule 5.3A of *IPRU(INS)*.~~
- ~~(2) Where any *shares* are held by a *friendly society* in a *related undertaking* which is not an *insurance undertaking* or *insurance holding company*, the value of the *shares* must not exceed the greater of:~~
- ~~(a) the value (or, where the shareholding, whether held directly or indirectly, is less than 100%, the relevant *proportional share* of the value), determined in accordance with this Appendix (other than 15(1)(a) to (c)), of the *related undertaking's surplus assets*; and~~
  - ~~(b) the value of those *shares* as determined under 9 reduced:~~
    - ~~(i) by an appropriate amount, to the extent that the *shares* cannot effectively be made available or realised to meet losses (if any) arising in the *friendly society*;~~
    - ~~(ii) by an appropriate amount, to the extent needed to exclude value attributable to goodwill generated from business with the *friendly society* or any *related undertaking* of the *friendly society* that is an *insurance undertaking* or an *insurance holding company*; and~~
    - ~~(iii) by the amount by which the value of any *shares* held by the *group undertaking* in a *related undertaking* of the *friendly society* which is an *insurance undertaking* or an *insurance holding company* exceeds the value (or *proportional share*); determined in accordance with this Appendix (other than 15(1)(a) to (c)), of the *surplus assets* of the *related undertaking*.~~
- ~~(3) The surplus assets of a *related undertaking* (other than an *insurance undertaking* or an *insurance holding company*) are its total assets excluding:~~
- ~~(a) the assets that are selected to cover liabilities;~~

- ~~(b) — assets that are interests directly or indirectly held in the *related undertaking's* own capital;~~
  - ~~(c) — amounts due, or to become due, in respect of *share* capital, or other contributions from members of the *related undertaking*, subscribed or called for but not fully paid up; and~~
  - ~~(d) — assets that cannot effectively be made available or realised to meet losses (if any) arising in the *friendly society*, including assets that represent capital not owned, directly or indirectly, by the *friendly society*.~~
- ~~(4) — The assets selected in (3)(a) to be excluded from the total assets:~~
- ~~(a) — must be of a value at least equal to the amount of the liabilities of the *related undertaking*, determining that value and that amount in accordance with this Appendix (other than 15(1)(a) to (c)) and Appendix 5; and~~
  - ~~(b) — must not include:~~
    - ~~(i) — assets falling within (3)(b), or~~
    - ~~(ii) — assets falling within (3)(c) where the amount is due, or to become due, from a *related undertaking*; but~~
  - ~~(c) — notwithstanding (a), a liability of the *related undertaking* which is a *debt due to the friendly society* is not required to be determined at an amount which is higher than the value placed on that *debt* as an asset of the *friendly society*.~~
3. (1) Where any *shares* are held by a *friendly society* in a *related undertaking*, which is a *regulated related undertaking* the value of the *shares* may be taken as, and in any event must not exceed, the value (or, where the shareholding, whether held directly or indirectly, is less than 100%, the relevant *proportional share* of the value), determined in accordance with this Appendix (other than paragraph 15(1)(a) to (c)), of the *surplus assets* of the *regulated related undertaking*.
- (2) Where any *shares* are held by a *friendly society* in a *related undertaking* which is not a *regulated related undertaking*, the value of the *shares* must not exceed the greater of:
- (a) the value (or, where the shareholding, whether held directly or indirectly, is less than 100%, the relevant *proportional share* of the value), determined in accordance with this Appendix (other than 15(1)(a) to (c)), of the *related undertaking's surplus assets*; and
  - (b) the value of those *shares* as determined under paragraph 9 reduced:

- (i) by an appropriate amount, to the extent that the *shares* cannot effectively be made available or realised to meet losses (if any) arising in the *friendly society*.
  - (ii) by an appropriate amount, to the extent needed to exclude value attributable to goodwill generated from business with the *friendly society* or any *related undertaking* of the *friendly society* that is a *regulated related undertaking*, and
  - (iii) by the amount by which the value of any *shares* held by the *related undertaking* in a *related undertaking* of the *friendly society* which is a *regulated related undertaking* exceeds the value (or *proportional share*), determined in accordance with this Appendix (other than 15(1)(a) to (c)), of the *surplus assets* of the *related undertaking*.
- (3) The surplus assets of a *related undertaking* are its total assets excluding:
- (a) the assets that are selected to cover liabilities and, in the case of a *related undertaking* which is a *regulated related undertaking*, to cover its regulatory requirement;
  - (b) the regulatory requirement of a *regulated related undertaking* is:
    - (i) in respect of an *insurance undertaking*, the *notional required minimum margin*;
    - (ii) in respect of a *regulated entity* with its head office in the *EEA* (excluding an *insurance undertaking*), the *solo capital resources requirement* calculated in accordance with the *sectoral rules* for the *financial sector* applicable to it;
    - (iii) in respect of a *regulated entity* not within (ii) (excluding an *insurance undertaking*), its *proxy capital resources requirement*;
    - (iv) in respect of *asset management company*, the *solo capital resources requirement* that would apply to it if, in connection with its activities, it were treated as an *investment firm* for the purposes of calculating the *solo capital resources requirement*;
    - (v) in respect of a *financial institution* (including a *financial holding company*) which is not a *regulated entity*, the *solo capital resources requirement* that would apply to it if, in connection with its activities, it were treated as being within the *banking sector*; and
    - (vi) in respect of an *insurance holding company*, zero.

- (c) assets that are interests directly or indirectly held in the *related undertaking's* own capital (as defined in the *relevant regulatory requirements* for that undertaking);
  - (d) where the *related undertaking* carries on *long-term insurance business*, profit reserves and future profits;
  - (e) assets which represent either a *long-term insurance fund* or a fund the allocation of which as between *policy holders* and other purposes has yet to be determined;
  - (f) amounts due, or to become due, in respect of *share capital*, or other contributions from members of the *related undertaking*, subscribed or called for but not fully paid up; and
  - (g) assets that cannot effectively be made available or realised to meet losses (if any) arising in the *friendly society*, including assets that represent capital not owned, directly or indirectly, by the *friendly society*.
- (4) The assets selected in (3)(a) to be excluded from the total assets:
- (a) where the *related undertaking* is an *insurance undertaking*, must be identified and valued in accordance with *relevant regulatory requirements* as to the value, admissibility, nature, location or matching that apply to the assets available to cover its liabilities (determined under the *relevant regulatory requirements*) and the *notional required minimum margin*;
  - (b) where the *group undertaking* is a *regulated related undertaking* (excluding an *insurance undertaking*), must be identified and valued in accordance with the *relevant sectoral rules* applicable to the *regulated related undertaking* as to cover its liabilities and the applicable regulatory requirement identified in paragraph 3(3)(b);
  - (c) where the *group undertaking* is not a *regulated related undertaking*, must be of a value at least equal to the amount of its liabilities, determining that value and that amount in accordance with this Appendix (other than 15(1)(a) to (c)) and Appendix 5; and
  - (d) in all cases, must not include:
    - (i) assets falling within (3)(c), or
    - (ii) assets falling within (3)(f) where the amount is due, or to become due, from a *related undertaking*; but
  - (e) notwithstanding (a), (b) and (c), a liability of a *related undertaking* which is a *debt* due to the *friendly society* is not required to be

determined at an amount which is higher than the value placed on that debt as an asset of the friendly society.

- (5) For the purposes of (4), the relevant regulatory requirements must be treated as if paragraphs 15(1)(a) to (c) (or their equivalent in a designated State or territory) do not apply for the purpose of valuing shares in related undertakings that are not dependants.
- (6) For the purposes of this Appendix, any value attributed to any shares held directly or indirectly in a related undertaking which is an ancillary insurance service undertaking, an ancillary investment services undertaking or an ancillary banking services undertaking, calculated in accordance with paragraph 3, must be deducted from the assets of the friendly society.

### **Value of non capital interests in a group undertaking**

- 4A (1) A friendly society must notify the FSA of:
- (a) any related undertaking which:
- (i) no participation is held in by another related undertaking; and
- (ii) is not a subsidiary undertaking; but
- (iii) is linked by a consolidation Article 12(1) relationship with another related undertaking; and
- (b) the value of that undertaking calculated on the basis of paragraph 3.
- (2) For the purposes of this Appendix, the related undertaking referred to in (1)(a)(iii)'s proportional share of the value of the related undertaking in (1)(a) is determined in accordance with Article 28(5) of the Financial Groups Directive.



## Appendix 5

### *LIABILITY VALUATION RULES*

#### **Provision for related undertakings**

- 3A (1) Except to the extent that provision for the deficit has been made (whether in the calculation of *surplus assets* or otherwise) in another *related undertaking* the value of whose *shares* is taken to be the value of its *surplus assets* under paragraph 3(1) or (2) of Appendix 4 (but only to the extent of the *friendly society's proportional share* of that *undertaking*), a *friendly society* must make provision in respect of a *related undertaking* that is a *regulated related undertaking*:
- (a) where the *related undertaking* is also a *subsidiary undertaking* of the *friendly society*, for the whole of any *solvency deficit*; and
  - (b) in any other case, for the *friendly society's proportional share* of any such deficit.
- (2) For the purposes of (1), the identification and valuation of assets of *regulated related undertaking* available to cover liabilities and the regulatory requirement, set out in paragraph 3(3)(b) of Appendix 4 must be determined in accordance with paragraph 3(4) of Appendix 4.

## Annex E

### Amendments to Interim Prudential Sourcebook for Insurers (IPRU(INS))

In this Annex, underlining indicates new text and striking through indicates deleted text:

#### IPRU(INS) - VOLUME 1

#### Chapter 4

#### VALUATION OF ASSETS

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##### Shares in a group undertaking

- 4.2 (1) Notwithstanding rule 4.8, the value of any *shares* held in a *group undertaking* which is ~~an *insurance undertaking* or an *insurance holding company*~~ a *regulated related undertaking* may be taken as, and, in any event, must not exceed, the value (or, where the shareholding, whether held directly or indirectly, is less than 100%, the relevant *proportional share* of the value), determined in accordance with the *Valuation of Assets Rules* (other than rule 4.14(1)(a) to (c)), of the ~~its~~ *surplus assets of the regulated related undertaking*.
- (1A) The value of any *shares* held in a *group undertaking* which is not ~~an *insurance undertaking* or an *insurance holding company*~~ a *regulated related undertaking* must not exceed the greater of:
- (a) ...
  - (b) ...
    - (i) ...
    - (ii) ....
    - (iii) by the amount by which the value of any *shares* held by the *group undertaking* in a *related undertaking* of the *insurer* which is an *regulated related undertaking* ~~*insurance undertaking* or an *insurance holding company*~~ exceeds the value (or *proportional share*), determined in accordance with the *Valuation of Assets Rules* (other than rule 4.14(1)(a) to (c)), of the *surplus assets* of the *related undertaking*.
- (2) The surplus assets of a *group undertaking* are its total assets excluding:
- (a) the assets that are selected to cover liabilities and, in the case of a *group undertaking* which is ~~an *insurance undertaking*~~, ~~to cover the *notional required minimum margin*~~ a *regulated related undertaking*, to cover its regulatory requirement;

- (aa) the regulatory requirement of a regulated related undertaking is:
- (i) in respect of an insurance undertaking, the notional required minimum margin;
  - (ii) in respect of a regulated entity with its head office in the EEA (excluding an insurance undertaking), the solo capital resources requirement calculated in accordance with the sectoral rules for the financial sector applicable to the regulated related undertaking;
  - (iii) in respect of a regulated entity not within (ii) (excluding an insurance undertaking), its proxy capital resources requirement;
  - (iv) in respect of an asset management company, the solo capital resources requirement that would apply to it if, in connection with its activities, it were treated as an investment firm for the purposes of calculating the solo capital resources requirement;
  - (v) in respect of a financial institution (including a financial holding company) which is not a regulated entity, the solo capital resources requirement that would apply to it if, in connection with its activities, it were treated as being within the banking sector; and
  - (vi) in respect of an insurance holding company, zero.
- (c) ....
- (d) ....
- (e) ....
- (f) ....
- (3) The assets selected in (2)(a) to be excluded from the total assets:
- (a) ...
  - (b) where the group undertaking is a regulated related undertaking (excluding an insurance undertaking), must be identified and valued in accordance with the relevant sectoral rules applicable to the regulated related undertaking as to cover its liabilities and the applicable regulatory requirement identified in rule 4.2(2)(aa);
  - (c) where the group undertaking is not an insurance undertaking a regulated related undertaking, must be of a value at least equal to the amount of its liabilities, determining that value and that amount in accordance with the Valuation of Assets Rules (other than 4.14(1)(a) to (c)) and the Determination of Liabilities Rules; and
  - (d) in all both cases, must not include:

- (i) assets falling within (2)(b), or
  - (ii) assets falling within (2)(e) where the amount is due, or to become due, from a *group undertaking*; but
- (~~de~~) notwithstanding (a), ~~and~~ (b) and (c), a liability of a *group undertaking* which is a *debt* due to the *insurer* is not required to be determined at an amount which is higher than the value placed on that *debt* as an asset of the *insurer*.
- (5) For the purposes of the *Valuation of Assets Rules*, any value attributed to any *shares* held directly or indirectly in a *group undertaking* which is an *ancillary insurance services undertaking*, an *ancillary investment services undertaking* or an *ancillary banking services undertaking*, calculated in accordance with rule 4.2, shall be deducted from the assets of the *insurer*.

**Value of non capital interests in a group undertaking**

- 4.3A (1) An *insurer* must notify the *FSA* of:
- (a) any *group undertaking* which:
    - (i) no *participation* is held in by another *group undertaking*; and
    - (ii) is not a *subsidiary undertaking*; but
    - (iii) is linked by a *consolidation Article 12(1) relationship* with another *group undertaking*; and
  - (b) the value of that *undertaking* calculated on the basis of rule 4.2.
- (2) For the purposes of *Valuation of Assets Rules*, the *group undertaking* referred to in (1)(a)(iii)'s proportional share of the value of the *group undertaking* in (1)(a) shall be determined in accordance with Article 28(5) of the *Financial Groups Directive*.

## Chapter 5

### DETERMINATION OF LIABILITIES

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#### *Provision for related undertakings*

- 5.3A (1) Except to the extent that provision for the deficit has been made (whether in the calculation of *surplus assets* or otherwise) in another *group undertaking* the value of whose *shares* is taken to be the value of its *surplus assets* under rule 4.2(1) or (1A)(a) (but only to the extent of the *insurer's proportional share* of that undertaking), an *insurer* must make provision in respect of a *related undertaking* that is ~~an insurance undertaking or insurance holding company~~ a regulated related undertaking:
- (a) where the *related undertaking* is also a *subsidiary undertaking* of the *insurer*, for the whole of any *solvency deficit*; and
  - (b) in any other case, for the *insurer's proportional share* of any such deficit.
- (2) For the purposes of (1), the identification and valuation of assets of a regulated related undertaking available to cover liabilities and the regulatory requirement, set out in rule 4.2(2)(aa), notional required minimum margin must be determined in accordance with rule 4.2(3).

**PARENT UNDERTAKING SOLVENCY CALCULATION**

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**Information to be provided to FSA**

- 10.2 (1) ...
- (b) the relationship with each other member of the *insurance group*, including the amounts and descriptions of holdings of *share capital* and voting rights and the nature of any consolidation Article 12(1) relationship;
- ...
- (4) ...
- (c) the valuation of assets and the determination of liabilities of regulated related undertakings ~~insurance undertakings~~ and ~~insurance holding companies~~; and
- (d) the calculation of the required minimum solvency margin or capital resources requirement of those undertakings ~~insurance undertakings~~.

## Chapter 11

### DEFINITIONS

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#### PART I

#### DEFINITIONS

- 11.1 For the purposes of *IPRU(INS)*, the term or phrase in the first column has the meaning given to it in the second column unless the context otherwise requires.

<i>Banking Co-ordination Directive</i> or <i>BCD</i>	Council Directive of 20 March 2000, relating to the taking up and pursuit of the business of credit institutions (2000/12/EC)
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<i>Directive</i>	see –  <i>Insurance Groups Directive</i> <i>Investment Services Directive</i> <i>Financial Groups Directive</i> <i>First Life Directive</i> <i>First Non-Life Directive</i> <i>Banking Co-ordination Directive</i> <i>Third Life Directive</i> <i>Third Non-Life Directive</i> <i>Consolidated Life Directive</i>
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<i>insurance group</i>	an <i>insurance parent undertaking</i> and its <i>related undertakings</i>  (a) — <i>insurance undertakings</i> ; or  (b) — <i>insurance holding companies</i>
<i>insurance holding company</i>	a <i>parent undertaking</i> whose main business is to acquire and hold <i>participations</i> in <i>subsidiary undertakings</i> , where:  (a) those <i>subsidiary undertakings</i> are exclusively or

	<p>mainly <i>insurance undertakings</i>;</p> <p>(b) <u>at least one of such <i>subsidiary undertakings</i> is a <i>UK insurer</i> or an <i>EEA firm</i> that is a <i>regulated insurance entity</i>; and</u></p> <p>(c) <u>it is not a <i>mixed financial holding company</i>.</u></p>
<i>insurance parent undertaking</i>	<p><del>in relation to an <i>insurer</i>, is a <i>parent undertaking</i> which is</del></p> <p>(1) <u>an <del>of that</del> <i>insurer</i> which has a <i>subsidiary undertaking</i> which is an <i>insurance undertaking</i>;</u></p> <p>(2) <u>an <del>which is either itself an <i>insurance undertaking</i> or an <i>insurance holding company</i></del> which has a <i>subsidiary undertaking</i> which is an <i>insurer</i>; or</u></p> <p>(3) <u>an <i>insurance undertaking</i> which has a <i>subsidiary undertaking</i> which is an <i>insurer</i></u></p>

<i>notional group solvency margin</i>	<p>in relation to an <i>ultimate insurance parent undertaking</i> or an <i>ultimate EEA insurance parent undertaking</i>, the sum of:</p> <p>(a) the <i>notional required minimum margin</i> (if any) of that parent; and</p> <p>(b) the sum of that parent's <i>proportional shares</i> of the <u>regulatory requirements referred to in Rule 4.2(2)(aa) <del>notional required minimum margins</del></u> of its <u><i>regulated related insurance undertakings</i></u></p>
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<i>participating undertaking</i>	<u>an <i>undertaking</i> which is either a <i>parent undertaking</i> or other <i>undertaking</i> which holds a <i>participation</i> in or is linked by a <i>consolidation Article 12(1) relationship</i> with an <i>undertaking</i> which holds a <i>participation</i> in the undertaking in question</u>
<i>participation</i>	<p>(a) the holding of a participating interest within the meaning of section 421(2) of the <i>Act</i>; or</p> <p>(b) the holding, directly or indirectly, of 20% or more of the voting rights or capital <u>of an <i>undertaking</i></u></p>
<i>proxy capital resources</i>	<u>the <i>solo capital resources requirement</i> to which an <i>undertaking</i> would have been subject if it had a</u>



<i>requirement</i>	<u>permission</u> for each activity it carries on anywhere in the world, so far as that activity is a <i>regulated activity</i> .
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<i>regulated related undertaking</i>	<p><u>a group undertaking</u> that is any of the following:</p> <p>(a) <u>a regulated entity</u>,</p> <p>(b) <u>an insurance undertaking</u> which is not a <i>regulated insurance entity</i>,</p> <p>(c) <u>an asset management company</u>,</p> <p>(d) <u>a financial institution</u> which is not either a <i>credit institution</i> or <i>investment firm</i>,</p> <p>(e) <u>a financial holding company</u>, or</p> <p>(f) <u>an insurance holding company</u>.</p>
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<i>related undertaking</i>	<p>in relation to an <i>undertaking 'U'</i>:</p> <p>(a) <u>any subsidiary undertaking</u> of U;</p> <p>(b) <u>any undertaking</u> in which U or any of U's <u>subsidiary undertakings</u> holds a <i>participation</i> is held by another undertaking; or</p> <p>(c) <u>any undertaking</u> which is linked to U by a <u>consolidation</u> a <u>subsidiary undertaking</u> <u>Article 12(1) relationship</u>; or</p> <p>(d) <u>any undertaking</u> linked by a <u>consolidation</u> <u>Article 12(1) relationship</u> to an undertaking in (a), (b) or (c).</p>
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<i>solvency deficit</i>	a or any deficit in the assets available to cover the undertaking's liabilities and represent its <u>regulatory requirement</u> referred to in Rule 4.2(2)(aa) <del>notional required minimum margin</del> (if any)
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<i>ultimate insurance parent undertaking</i>	<del>an insurance</del> <u>parent undertaking</u> that is either an <u>insurance undertaking</u> or an <u>insurance holding company</u> and is not itself the <i>subsidiary undertaking</i> of another <i>insurance parent undertaking</i>
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## **PART 2**

### **GENERAL PROVISIONS**

#### **Use of definitions**

- 11.5 A word or phrase which is printed in italics is used in the defined sense. Where a word or phrase is printed in italics and is not given a meaning in Part 1 of Chapter 11, that word or phrase has the meaning given to it in the Handbook Glossary.

GUIDANCE NOTE 4.1

GUIDANCE FOR INSURERS AND AUDITORS ON THE VALUATION OF ASSET RULES

Annex C

SHARES IN AND DEBTS DUE TO A GROUP UNDERTAKING

Shares in a group undertaking (rule 4.2)

2. *Shares in a group undertaking* may be valued either as arms-length investments under rule 4.8 (see paras 4.63 to 4.76 of Guidance Note 4.1) or under rules 4.2 (1) to (4). *Shares in group undertakings* that are *insurance undertakings* or *insurance holding companies* (see paragraph 4 of Guidance Note 10.1 for guidance on *insurance holding companies*) may not be given a higher value than the *surplus assets* in those undertakings calculated according to rules 4.2(2) to (4), but otherwise the *insurer* has the option whether or not to use rule 4.8<sup>1</sup>. If rule 4.8 is used, then admissibility limits apply and from 1 May 2003 there must be a deduction for intra-group goodwill under rule 4.2(1A)(b)(ii) (see 5). When valuing *shares* in a *group undertaking*, rules 4.2 (2) to (4) require net asset value to be used with certain adjustments.

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<sup>1</sup> For the purposes of implementing the *Financial Groups Directive* and the amendments to the *Insurance Groups Directive*, with effect from 1 January 2005, *shares* held by an *insurer* in a *group undertaking* that is a *regulated related undertaking* (including *insurance undertakings* and *insurance holding companies*) are to be valued in accordance with the amended rules 4.2(1) to (5) and the *insurer* will not have the option to use rule 4.8 in respect of a *regulated related undertaking*. For the purposes of Annex C of this Guidance Note 4.1, references to *group undertakings* that are either *insurance undertakings* or *insurance holding companies*, or both should be read as references to *group undertakings* that are *regulated related undertakings*. Please note that the examples on pages 76J, K & L have not been amended to take account of this change (although they remain correct for a *firm* which does not have any *regulated related undertakings* which are not *insurance undertakings*).

## GUIDANCE NOTE 10.1

### THE PARENT UNDERTAKING SOLVENCY CALCULATION

#### Introduction

1. This guidance relates to the *parent undertaking solvency calculation* required by the *Insurance Groups Directive* and implemented in Chapter 10 of *IPRU(INS)*. The calculation is formulated on a basis analogous to the basis on which *shares in group undertakings* are valued for the *required solvency margin* (see Annex C paragraphs 4.7 to 4.12 of Guidance Note 4.1)<sup>1</sup>, but in contrast the *parent undertaking solvency calculation* is applied to an *insurer's ultimate insurance parent undertaking* and its *ultimate EEA insurance parent undertaking*, if different. Valuation of *shares in group undertakings* at the solo level focus "downwards" on the *insurer's* holdings in *group undertakings*, whereas the *parent undertaking solvency calculation* focuses "upwards" towards the ultimate parent of the *insurance group* of which it is a member.

#### Application and scope

3. The information and calculations to be provided under Chapter 10 are in respect of the *insurer* and each member of its *insurance group*. The *insurance group* consists of the *insurer's ultimate insurance parent undertaking* and its *related undertakings* ~~which are insurance undertakings or insurance holding companies.~~

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<sup>1</sup> Annex C of Guidance Note 4.1 has been amended with effect from 1 January 2005 for the purposes of implementing the *Financial Groups Directives* and amendments to the *Insurance Groups Directive* to include *regulated related undertakings* within the scope of rule 4.2(1).

## Annex F

### Amendments to the Interim Prudential sourcebook for investment business

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

IPRU(INV), Chapter 1.

...

1.2.4	R	<i>A firm</i> of a kind listed in the left-hand column of Table 1.2.4R must comply with the provisions of <i>IPRU(INV)</i> shown in the right hand column <u>and, where relevant, the provisions of Chapter 14.</u>
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...

In Chapter 3, after the heading "CONSOLIDATED SUPERVISION" insert the following text as a footnote:

Under the Financial Conglomerates and Other Financial Groups Instrument 2004, the rules in Chapter 14 shall (with respect to a particular firm, group or financial conglomerate) apply from the first day of its financial year beginning in 2005 in place of rules 3-190(1) to 3-195.

In IPRU(INV), Chapter 5, Table 5.2.2(1), insert the following:

**PART II  
DETAILED REQUIREMENTS**

...

**10 Illiquid assets**  
(Item 16)

Illiquid assets comprise:

...

(i) if not otherwise covered, any holding in eligible capital instruments of an insurance undertaking, insurance holding company, or reinsurance undertaking that is a subsidiary or participation. Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans, that are eligible for insurance undertakings under PRU 2.

...

In Chapter 5, after the heading "CONSOLIDATED SUPERVISION" insert the following text as a footnote:

Under the Financial Conglomerates and Other Financial Groups Instrument 2004, the rules in Chapter 14 shall (with respect to a particular firm, group or financial conglomerate) apply from the first day of its financial year beginning in 2005 in place of rules 5.7.1(1) to 5.7.5(4).

In Table 7.3.1 R, insert the following:

**PART II  
DETAILED REQUIREMENTS**

...

**10 Illiquid assets (Item 14)**

...

Illiquid assets comprise:

...

(i) if not otherwise covered, any holding in eligible capital instruments of an insurance undertaking, insurance holding company, or reinsurance undertaking that is a subsidiary or participation. Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans, that are eligible for insurance undertakings under PRU 2.

...

In table 10-61(1)B insert the following items:

R TABLE 10-61(1)B – Own funds

the sum of -

*material holdings in credit and financial institutions*  
*material insurance holdings*

**(E)**

In table 10-62(2)A insert the following items:

R TABLE 10-62(2)A - Financial resources - version I

the sum of -

*material holdings in credit and financial institutions*  
*material insurance holdings*

**(G)**

In table 10-62(2)B insert the following items:

R TABLE 10-62(2)B - Financial resources - version II

the sum of -

*material holdings in credit and financial institutions*  
*material insurance holdings*

**(H)**

In table 10-62(2)C insert the following items:

R TABLE 10-62(2)C - Financial resources - version II.2

the sum of -

**(G)**

*non-trading book material holdings in credit and financial institutions*  
*material insurance holdings*

In Chapter 10, after the heading "CONSOLIDATED SUPERVISION" insert the following text as a footnote:

Under the Financial Conglomerates and Other Financial Groups Instrument 2004, the rules in Chapter 14 shall (with respect to a particular firm, group or financial conglomerate) apply from the first day of its financial year beginning in 2005 in place of rules 10-200(1) to 10-204.

...

Insert in the Chapter 10, Appendix 1, Glossary of Terms for IPRU(INV) 10:

Material insurance holdings This is calculated as the higher of –

- (a) the book value of an investment held in an insurance undertaking, reinsurance undertaking or insurance holding company; and
- (b) the group's proportionate share of that undertaking's local or notional regulatory requirement.

Investment for this purpose includes both a participation and the investment in a subsidiary undertaking.

...

In Table 13.5.4(1) PART I insert the following:

<b>FIRMS IN CATEGORY A1</b>		
<b>ASSETS</b>	<b>CALCULATION</b>	<b>TYPE OF ADJUSTMENT</b>
...	...	...
(13) All other assets	<p>Exclude in full.</p> <p><u>If not otherwise excluded in full in this table, this category should include any holding in eligible capital instruments of an insurance undertaking, insurance holding company, or reinsurance undertaking that is a subsidiary or participation.</u></p> <p><u>Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans, that are eligible for insurance undertakings under PRU 2.</u></p>	<p>An Illiquid Adjustment</p>
...	...	...

In Table 13.5.4(2) PART I insert the following:

<b>FIRMS IN CATEGORY A2 AND A3</b>
------------------------------------

ASSETS	CALCULATION	TYPE OF ADJUSTMENT
...	...	...
(13) All other assets	<p>Exclude in full.</p> <p><u>If not otherwise excluded in full in this table, this category should include any holding in eligible capital instruments of an insurance undertaking, insurance holding company, or reinsurance undertaking that is a subsidiary or participation.</u></p> <p><u>Eligible capital instruments include ordinary share capital, cumulative preference shares, perpetual securities and long-term subordinated loans, that are eligible for insurance undertakings under PRU 2.</u></p>	An Illiquid Adjustment
...	...	...

In Chapter 13, after the heading "Consolidated Supervision of Group Companies" insert the following text as a footnote:

Under the Financial Conglomerates and Other Financial Groups Instrument 2004, the rules in Chapter 14 shall (with respect to a particular firm, group or financial conglomerate) apply from the first day of its financial year beginning in 2005 in place of rules 13.7.1 to 13.7.2B.



After IPRU, Chapter 13, insert the following new Chapter 14:

## CHAPTER 14: CONSOLIDATED SUPERVISION FOR INVESTMENT BUSINESSES

### 14.1 Application

- 14.1.1 R Subject to rule 14.1.2, *consolidated supervision* and this chapter apply to a *firm* which is a member of a group if it is:
- (1) a *securities and futures firm*, subject to the financial rules in Chapter 3, which is a *broad scope firm* but not a *venture capital firm*;
  - (2) an *investment management firm*, which is a *CAD investment firm* subject to the financial rules in Chapter 5;
  - (3) a *UCITS investment firm*, subject to the financial rules in chapter 7;
  - (4) a *securities and futures firm*, subject to the financial rules in Chapter 10, unless the *firm* is a *category D firm*; or
  - (5) a *category A personal investment firm*, subject to the financial rules in Chapter 13.

Cases where consolidated supervision under this chapter will not apply

- 14.1.2 R A *firm* is not subject to *consolidated supervision* under the rules in this Chapter where any of the following conditions are fulfilled:
- (1) the *firm* is included in the supervision on a consolidated basis of the group of which it is a member by a *competent authority* other than the *FSA*; or
  - (2) the *firm* is already included in the supervision on a consolidated basis of the group of which it is a member by the *FSA* under IPRU(BANK) or IPRU(BSOC).
- 14.1.3 G (1) The rules in this chapter apply even if the *firm* is subject to the rules in PRU 8.4 (the financial conglomerates rules) or PRU 8.3 (the insurance group rules), if the *firm* is part of an investment sub-group. Financial conglomerates are subject to the Financial Groups Directive (2002/87/EC). Insurance groups are subject to the Insurance Groups Directive (98/78/EC). Neither directive allows a waiver of consolidation of a Capital Adequacy Directive group. So if there is an investment sub-group within an insurance group, the rules in this chapter apply, regardless of the application of a group capital assessment to the wider group.

- (2) Where firms authorised in two or more member states have as their parent the same *financial holding company*, supervision on a consolidated basis will be exercised by the competent authority of the firms authorised in the member state in which the *financial holding company* was set up. If no firm has been authorised in the Member State in which the financial holding company was set up, the competent authorities of the Member States concerned will seek to reach agreement as to who amongst them will exercise supervision on a consolidated basis. In the absence of such an agreement, supervision on a consolidated basis will be exercised by the competent authority that granted authorisation to the firms with the greatest balance-sheet total (measured on the basis of total assets). If that figure is the same for more than two authorised firms, supervision on a consolidated basis will be exercised by the competent authority which first gave the authorisation.
- (3) Where there is more than one authorised *firm* in the group, subject to the rules of this chapter, one consolidated supervision return may be submitted on behalf of all the *firms* in the group in accordance with SUP 16.3.25G.

#### Exemption from consolidated supervision

14.1.4 R A *firm* need not meet the requirements in rules 14.3.1 and 14.3.2 if:

- (1) there is no *credit institution* in the group;
- (2) no *firm* in the group *deals in investments as principal*, except where it is an *operator* of a *collective investment scheme* dealing solely as a result of its activity of operating a *collective investment scheme*, or where the *firm's* positions fulfil the *CAD Article 3 exempting criteria*;
- (3) each member of the group which is a *CAD investment firm*:
  - (a) deducts any *material holdings* in *credit* and *financial institutions* from its financial resources;
  - (b) complies with its solo applicable financial resources requirement and the *large exposures requirements*; and
  - (c) has systems and controls to monitor and control the sources of capital and funding of all other *financial institutions* within the group;
- (4) the *firm* notifies the *FSA* of any serious risk that could undermine the financial stability of the group as soon as it becomes aware of that risk;
- (5) the *firm* reports to the *FSA* all group *large exposures* as at the end of each quarter, and within the period specified in SUP 16;
- (6) the *firm* meets the conditions in rule 14.1.5; and

- (7) the *firm* has first notified the *FSA* in writing that it intends to rely on this rule.

14.1.5 R If the *firm* notifies the *FSA* under *rule* 14.1.4 that it will not apply the rules in this section, it must:

- (1) submit to *FSA* a consolidated supervision return within the time period specified by *SUP* 16, together with a consolidated profit and loss account;
- (2) ensure that each *firm* in the group deducts from its solo financial resources any quantifiable *contingent liability* in respect of other group entities;
- (3) ensure that the solo financial resources requirement of each *firm* in the group incorporates the full value of the expenditures of the *firm* wherever they are incurred on behalf of the *firm*; and
- (4) make a note in its audited financial statements that it is not subject to regulatory consolidated capital requirements.

14.1.6 G (1) The Capital Adequacy Directive (articles 7(4) to 7(6)) provides that a *competent authority* such as the *FSA* may waive *consolidated supervision* provided certain conditions are met. The conditions in *rule* 14.1.4 are mainly derived from the Capital Adequacy Directive.

(2) The conditions in *rule* 14.1.5 aim to ensure that the *firm* is protected from weaknesses in other group entities.

(3) In *rule* 14.1.5(2), *contingent liabilities* includes direct and indirect guarantees.

(4) 14.1.5(3) aims to ensure that the expenditure-based requirement incorporates the *firm's* actual ongoing annual expenditures (including any share of depreciation on fixed assets) where these have been met by another group entity.

(5) The *FSA* may require further information from the *firm* if it considers that the *firm's* consolidated financial position raises undue risks to consumers. It may also seek reassurance that the *firm* has sufficiently robust *client money* and asset controls - for example, it may require a *skilled person's* report. The *FSA* may also use its *own initiative power* to impose conditions on the *firm*. This could include raising additional capital or further limitations on the *firm's* intra-group exposures.

- (6) Rule 14.1.4(5) refers to *large exposures*, which should be measured against group consolidated own funds or (if this would result in all *exposures* being classified as *large exposures*) by aggregating all the *exposures* of the individual entities in the group and measuring them against the own funds of the individual *firm* giving rise to the consolidated supervision requirement. If there is more than one *firm* in the group giving rise to the consolidated supervision requirement, the group *large exposures* should be measured against the *firm* with the smallest own funds.

## 14.2 Scope of consolidation

14.2.1 R For the purposes of the rules in this chapter, a *firm's* group means the *firm* and:

- (1) any *EEA parent* in the group which is a *financial holding company*, a *credit institution*, or an *investment firm*;
- (2) any *credit institution*, *investment firm* or *financial institution* which is a *subsidiary* either of the *firm* or of the *firm's EEA parent* as defined in (1); and
- (3) any *credit institution*, *investment firm* or *financial institution* in which the *firm* or one of the entities in (1) or (2) holds a *participation*.

14.2.2 R If a group exists under rule 14.2.1, the *firm* must also include in the scope of consolidation any *ancillary services undertaking* and *asset management company* in the group.

14.2.3 G Rule 14.1.1 states what type of *firm* may be subject to consolidated supervision (trigger firm). Rule 14.2.1 states what type of relationship triggers the existence of a group for consolidated supervision purposes. Rules 14.2.1 and 14.2.2 specify what entities should be included in the scope of consolidated supervision.

14.2.4(1) G A *firm's parent* is a *financial holding company* if it carries out mainly *listed activities* or activities undertaken by a Chapter 3 *broad scope firm* or if its main business is to acquire holdings in companies undertaking these activities. For this purpose the *FSA* interprets the phrases 'mainly' or 'main business' to mean where the balance of business is over 40% of the relevant group or sub-group's balance sheet (measured on the basis of total assets) or profit and loss statement (measured on the basis of gross income). In addition, if the *firm's parent* has significant holdings in *insurance undertakings* or *reinsurance undertakings*, it is a *mixed financial holding company*, and the *firm* is subject to the rules in PRU 8.4 instead of the rules in this chapter. This is because a *parent* cannot be a *financial holding company* and a *mixed financial holding company* at the same time. PRU 8.4 sets out what constitutes significant insurance holdings (broadly more than 10% of the financial sector activities of the group).

14.2.4(2) G A *firm* with an ultimate non-EEA parent may also be subject to the provisions in PRU 8.5.

14.2.4(3) In the case where undertakings are linked to the domain of consolidation by a  
G relationship within the meaning of article 12(1) of Directive (83/349/EEC), the *FSA* will determine how consolidation is to be carried out.

#### Exclusions

14.2.5 R A *firm* may, having first notified the *FSA* in writing, exclude from its group the following:

- (1) any entity the total assets of which are less than the smaller of the following two amounts:
  - (a) 10 million euros; or
  - (b) 1% of the total assets of the group's *parent* or the undertaking that holds the *participation*;

provided that the total assets of such entities do not collectively breach these limits.

- (2) any entity the inclusion of which within the group would be misleading or inappropriate for the purposes of *consolidated supervision*.

14.2.6 G (1) The *FSA* may require a *firm* to provide information about the position in the group of any undertaking excluded from the consolidation under rule 14.2.5.

(2) An exclusion under rule 14.2.5(2) would normally be appropriate when an entity would be excluded from the scope of consolidation under the relevant UK generally accepted accounting principles.

#### 14.3 Consolidated supervision requirement

14.3.1 R A *firm* must at all times ensure that its group maintains *group financial resources* in excess of its *group financial resources requirement*.

14.3.2 R A *firm*, other than one which is defined in rule 14.1.1(1), must at all times comply with *large exposures* limits applied on a group basis.

#### 14.4 Group financial resources

14.4.1 R A *firm* must calculate its *group financial resources* on the basis of the consolidated accounts of the relevant group, subject to the adjustments in rule 14.4.2 and on the basis specified in rule 14.4.3.

- 14.4.2 R (1) If more than one *firm* in the group is subject to the rules of this chapter, *group financial resources* are defined according to the relevant rules applicable to the main *firm* in the group, with Tier 1 minority interests being allowed as Group Tier 1 capital and Tier 2 minority interests being allowed as Group Tier 2 capital.
- (2) In calculating the *group financial resources*, deductions should be made for intangible assets, material unaudited losses incurred since the balance sheet date and investments in own shares.
- (3) *Material holdings* and *material insurance holdings* must be recalculated on a group basis and deducted in arriving at the *group financial resources*.
- 14.4.3 R Financial resources will be defined based upon the main *firm* in the group as follows:
- (1) if a *broad scope securities and futures firm* (excluding a *venture capital firm*), Table 3-61R;
- (2) if an *investment management firm*, Table 5.2.2(1)R but excluding any illiquid assets or qualifying property adjustments required by that Table;
- (3) if a *UCITS investment firm*, Table 7.3.1R but excluding any illiquid assets or qualifying property adjustments required by that Table;
- (4) if an *ISD securities and futures firm*, Table 10-62(2)AR, but excluding any adjustment in (E) of that Table;
- (5) if a *personal investment firm*, Table 13.3.2(1)R.
- 14.4.4 G (1) The *FSA* interprets ‘main’ by reference to the share of the *firm*’s business in the group, its contribution to the group’s balance sheet (measured on the basis of total assets) or profit and loss statement (measured on the basis of gross income).
- (2) The form in *SUP 16 Ann 19 R*, together with the guidance in *SUP 16 Ann 20G*, shows the mechanics of the calculation.
- 14.4.5G A *firm* may apply for a *waiver* of rule 14.4.1 to permit an aggregation approach to determine *group financial resources*. Any *waiver* application should guarantee future compliance with any relevant own funds limit.

## 14.5 Group financial resources requirement

- 14.5.1 R A *firm* must calculate its *group financial resources requirement* as the aggregate of:

- (1) the sum of the financial resources requirements of all group entities within the scope of consolidation calculated in accordance with rule 14.5.2, except that:
  - (a) requirements in respect of intra-group balances with other entities within the scope of consolidation should be excluded;
  - (b) *large exposures requirements* of individual group entities should be excluded;
- (2) the sum of any adjustments that are made to each *firm's* financial resources, calculated on a solo basis in accordance with rule 14.4.3, in order to arrive at the amount of financial resources used to meet its solo financial resources requirement. These adjustments must exclude deductions in respect of the investment in and other relationships with other entities that are included within the scope of consolidation; and:
- (3) if the main *firm* in the group is a *securities and futures firm* under rule 14.1.1(4), a group *large exposures requirement*.

The financial resources requirements of entities in which the group holds a *participation* must be included proportionately.

14.5.2 R Financial resources requirements for individual entities in the group are:

- (1) for *firms* regulated by the *FSA*, their regulatory capital requirement under *FSA* rules;
- (2) for entities regulated by an *EEA regulator* or one of the regulators listed in IPRU(INV) 10-App 59 or IPRU(BANK) CS Appendix D, their local regulatory capital requirement; and
- (3) for other entities in the group, a notional financial resources requirement calculated as if the entity were regulated by the *FSA*.

- 14.5.3 G
- (1) For the purposes of rule 14.5.2(3) the notional financial resources requirements of group entities should normally be calculated as if the entities were subject to the financial rules in IPRU(INV) relevant to the main *firm* in the group. The interpretation of 'main' given in 14.4.4 G applies here.
  - (2) For the purposes of calculating an expenditure-based requirement, no account should be taken of expenses that have been recharged to another entity included in the scope of consolidation. For example, in calculating the notional requirement for a service company, the expenditure-based requirement should be calculated net of recharged expenses. This is to avoid double counting of the expenses.

- (3) In 14.5.1(2), the adjustments referred to, are for *investment management firms*, the illiquid assets and qualifying property adjustments, and for *securities and futures firms*, the adjustments referred to in item (E) of Table 10-62(2)A. For *personal investment firms*, the adjustment required by 14.5.1(1) and (2) combined is the higher of:
- (a) the own funds requirement in 13.3.1R or 13.10.1R and;
  - (b) the sum of the relevant expenditure-based requirement and illiquid assets, position risk, and counterparty risk adjustments required by Chapter 13 of IPRU(INV).

14.5.4G A *firm* may apply for a *waiver* of rule 14.5.1R, to permit a line-by-line approach to determine its *group financial resources requirement*. Any *waiver* application should demonstrate (where relevant) that the constraints for intra-group offsets under the Capital Adequacy Directive (article 7) are met. A *firm* should also demonstrate that calculating its requirement in this way does not result in a distortion of the *group financial resources requirement*.

## APPENDIX 14(1) (INTERPRETATION)

### Glossary of defined terms for Chapter 14

Note: If a defined term does not appear in the glossary below, the definition appearing in the Glossary annexed to the General Provisions Instrument 2001 applies.

<i>ancillary services undertaking</i>	an undertaking the principal activity of which consists of owning or managing property, managing data-processing services, or any other similar activity which is ancillary to the principal activity of one or more of the <i>firms</i> subject to this chapter.
<i>asset management company</i>	in accordance with Article 2(5) of the <i>Financial Groups Directive</i> (Definitions) a management company within the meaning of Article 1a(2) of the <i>UCITS Directive</i> , as well as an <i>undertaking</i> the registered office of which is outside the <i>EEA</i> and which would require authorisation in accordance with Article 5(1) of the <i>UCITS Directive</i> if it had its registered office within the <i>EEA</i> .
<i>broad scope firm</i>	as in the Glossary in IPRU(INV) chapter 3.
<i>CAD Article 3 exempting criteria</i>	the following criteria in respect of the <i>firm's</i> dealing positions: <ul style="list-style-type: none"> <li>- such positions arise only as a result of the <i>firm's</i> failure to match investors orders precisely;</li> <li>- the total market value of all such positions is subject to a ceiling of 15% of the <i>firm's</i> initial capital; and</li> <li>- such positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question.</li> </ul>
<i>CAD investment firm</i>	a <i>firm</i> subject to the requirements of the Capital Adequacy Directive (CAD) (93/6/EEC) excluding a person to whom the CAD does not apply under Article 2.2 of that Directive.



<i>Category A personal investment firm</i>	as in the Glossary in IPRU(INV) chapter 13.
<i>Category D firm</i>	as in the Glossary in IPRU(INV) chapter 10.
<i>contingent liability</i>	<p>the meaning in FRS 12 which states that it is:</p> <p>(a) a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence of one or more uncertain future events not wholly within the entity's control or</p> <p>(b) a present obligation that arises from past events but is not recognised because:</p> <p>(i) it is not probable that a transfer of economic benefits will be required to settle the obligation; or</p> <p>(ii) the amount of the obligation cannot be measured with sufficient reliability.</p>
<i>consolidated supervision</i>	the application of the financial rules in the Interim Prudential sourcebook for investment businesses in accordance with rules and guidance in 14.1.1 to 14.5.4.
<i>EEA parent</i>	a <i>firm's</i> direct or indirect <i>parent</i> which has its head office in the <i>EEA</i> .
<i>financial holding company</i>	a <i>financial institution</i> the <i>subsidiary undertakings</i> of which are either exclusively or mainly <i>credit institutions, investment firms</i> and <i>financial institutions</i> , one of which at least is a <i>credit institution</i> or an <i>investment firm</i> and which is not a <i>mixed financial holding company</i> within the meaning of PRU 8.4.
<i>financial institution</i>	an undertaking other than a <i>credit institution</i> , the principal activity of which is to acquire holdings or to carry on a <i>listed activity</i> .
<i>group of connected third parties</i>	as in the Glossary in IPRU(INV) chapter 10.
<i>group financial resources</i>	the resources of a <i>firm's</i> group calculated in accordance with rules 14.4 (Group financial resources).
<i>group financial resources requirement</i>	the requirement that a <i>firm's</i> group maintains financial resources calculated in accordance with the rules in 14.5 (Group financial resources requirement).
<i>investment firm</i>	<i>investment firm</i> as in the main <i>Glossary</i> except that it excludes persons to which the <i>ISD</i> does not apply as a result of article 2.2 of the <i>ISD</i> .
<i>large exposure</i>	<p>(a) in relation to <i>non-trading book exposures</i>, an <i>exposure</i> or number of <i>exposures</i> to a third party or <i>group of connected third parties</i> which exceed 10% of group consolidated own funds; and</p> <p>(b) in relation to the aggregate of <i>non-trading book</i> and <i>trading book exposures</i>, an <i>exposure</i> or number of <i>exposures</i> to a third</p>

party or group of connected third parties which exceed 10% of group financial resources;

*large exposures requirement*

as set out in Rule 10-194 of IPRU(INV).

*listed activity*

a listed activity within the meaning of the *BCD*, that is one or more of the following activities:

- (a) lending;
- (b) financial leasing;
- (c) money transmission services;
- (d) issuing and administering means of payment;
- (e) guarantees and commitments;
- (f) trading for own account or for the account of customers in:
  - (i) money market instruments (cheques, bills, certificates of deposit, etc);
  - (ii) foreign exchange;
  - (iii) financial futures and options;
  - (iv) exchange and interest rate instruments;
  - (v) transferable securities;
- (g) participation in share issues and the provision of services related to such issues;
- (h) corporate finance advice;
- (i) money broking;
- (j) portfolio management and advice; or
- (k) safekeeping and administration of securities.

*material holding*

a holding of -  
(a) ordinary share capital and non cumulative preference share capital; or  
(b) subordinated loan and non fixed-term cumulative preference share capital,  
in a *credit institution* or a *financial institution* where -  
(i) (a) or (b) above exceeds 10% of the share capital plus share premium of the issuer; or  
(ii) the aggregate of (a) and (b) above exceeds 10% of the *firm's own funds*, before deducting the holding.

*material insurance holding*

the higher of –  
(1) the book value of an *investment* held in an insurance undertaking, reinsurance undertaking, or insurance holding company (*investment* for this purpose is either a *participation* or the *investment* in a *subsidiary* undertaking); or  
(2) the group's proportionate share of that undertaking's local or notional regulatory capital requirement."

*non-trading book parent*

as in the Glossary in IPRU(INV) chapter 10.  
any parent undertaking as defined in section 258 of the Companies Act 1985 or paragraph 14 of Financial Reporting Standard No 2 and any undertaking which effectively exercises a dominant influence over

	another undertaking.
<i>participation</i>	a participation within the meaning of Article 17 of Directive 78/660/EEC or the ownership either direct or indirect of 20% or more of the voting rights or capital of another undertaking which is not a <i>subsidiary</i> .
<i>securities and futures firm</i>	as in the Glossaries in IPRU(INV) chapter 3 and IPRU(INV) chapter 10.
<i>subsidiary</i>	as in section 736 of the Companies Act 1985.
<i>trading book</i>	as in the Glossary in IPRU(INV) chapter 10.
<i>UCITS investment firm</i>	a <i>firm</i> which: (1) is the <i>operator</i> of a <i>UCITS scheme</i> including where in addition the <i>firm</i> is the <i>operator</i> of a <i>collective investment scheme</i> which is not a <i>UCITS scheme</i> ; and (2) has <i>permission</i> to <i>manage investments</i> where the <i>investments managed</i> include one or more of the instruments listed in Section B of the Annex to the <i>ISD</i> .
<i>venture capital firm</i>	as in the Glossary in IPRU(INV) chapter 3.

## Annex G

### Amendments to the Integrated Prudential sourcebook (PRU)

In this Annex, all the text is new and is not underlined.

Insert the following:

Transitional provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
3	<i>PRU 8.1, PRU 8.4, PRU 8.5, PRU 8 Ann 1R, PRU 8 Ann 2R, PRU 8 Ann 4R</i> and, so far as it applies for the purposes of those provisions, the <i>Glossary</i> .	R	<p>(1) References to the <i>Financial Groups Directive Regulations</i> have no effect.</p> <p>(2) Any reference to notices served under regulation 2 of those Regulations is replaced by a reference to the corresponding notice under Article 4(2) of the <i>Financial Groups Directive</i>.</p>	From the date on which the <i>Handbook</i> material to which those transitional provisions apply come into force until revoked.	The date in column (5) on which the corresponding transitional <i>rule</i> ceases to apply.
4	<i>PRU 8.1, PRU 8.4, PRU 8.5, PRU 8 Ann 1R, PRU 8 Ann 2R, PRU 8 Ann 4R</i> and, so far as it applies for the purposes of those provisions, the	R	<p>(1) References to the <i>EEA</i> are replaced by references to the European Union and so that in particular:</p> <p>(a) an <i>EEA State</i> that is not a member of the European Union is treated in the same way as a state or territory that is neither an <i>EEA State</i> nor a member of the European Union;</p> <p>(b) if:</p>	From the date on which the <i>Handbook</i> material to which it applies comes into force until the <i>Financial Groups Directive</i> is adopted by	The date in column (5) on which the corresponding transitional <i>rule</i> ceases to apply.

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
	<i>Glossary.</i>		<p>(i) an <i>EEA financial conglomerate</i>; or</p> <p>(ii) an <i>EEA banking and investment group</i>;</p> <p>would come within the definition of <i>third-country financial conglomerate</i> or, as the case may be, <i>third-country banking and investment group</i> if the reference in those definitions to the <i>EEA</i> were replaced with a reference to the European Union, it must be treated as a <i>third-country financial conglomerate</i> or a <i>third-country banking and investment group</i> respectively; and</p> <p>(c) the definition of <i>competent authority</i> is, for the purposes of the provisions in column (2), amended by replacing references to <i>EEA States</i> with ones to member states of the European Union.</p> <p>(2) Paragraph 6.6 of <i>PRU 8 Ann 1</i> is amended so as to include the <i>sectoral rules</i> of an <i>EEA State</i> that is not a member of the European Union.</p>	the <i>EEA</i> .	

Insert new Section 1.8 as follows:

1.8                    Actions for damages

- 1.8.1            R    A contravention of the *rules* in *PRU* does not give rise to a right of action by a *private person* under section 150 of the *Act* (and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action).

Sections 2 to 7 – to follow.

Insert new Section 8.1 as follows:

8.1                    Group risk systems and controls requirement

Application

- 8.1.1            R    Subject to *PRU* 8.1.3R to *PRU* 8.1.5R, *PRU* 8.1 applies to each of the following which is a member of a *group*:
- (1)    a *firm* that falls into any of the following categories:
    - (a)    a *regulated entity*;
    - (b)    a *bank*, *ELMI* or *building society*;
    - (c)    an *insurer*;
    - (d)    an *own account dealer*;
    - (e)    a *matched principal broker*;
    - (f)    a *UCITS investment firm*; and
    - (g)    a *broker/manager* or an *arranger* that satisfies the following conditions:
      - (i)    it is an *ISD investment firm*; and
      - (ii)   it is not an *exempt CAD firm*;
  - (2)    a *UCITS firm*, but only if its *group* contains a *firm* falling into (1); and
  - (3)    the *Society*.
- 8.1.2            R    Except as set out in *PRU* 8.1.5R, *PRU* 8.1 applies with respect to different types of *group* as follows:

- (1) *PRU 8.1.9R and PRU 8.1.11R apply with respect to all groups, including FSA regulated EEA financial conglomerates, other financial conglomerates and groups dealt with in PRU 8.1.14R and PRU 8.1.15R;*
  - (2) *the additional requirements set out in PRU 8.1.12R and PRU 8.1.13R only apply with respect to FSA regulated EEA financial conglomerates; and*
  - (3) *the additional requirements set out in PRU 8.1.14R and PRU 8.1.15R only apply with respect to groups of the kind dealt with by whichever of those rules apply.*
- 8.1.3 R *PRU 8.1 does not apply to:*
- (1) *an incoming EEA firm; or*
  - (2) *an incoming Treaty firm; or*
  - (3) *a UCITS qualifier; or*
  - (4) *an ICVC.*
- 8.1.4 R *A venture capital firm that would otherwise be included in PRU 8.1.1R(1)(d) to PRU 8.1.1R(1)(g) is excluded from those rules if it is not an ISD investment firm.*
- 8.1.5 R (1) *This rule applies to:*
- (a) *PRU 8.1.9R(2);*
  - (b) *PRU 8.1.11R(1), so far as it relates to PRU 8.1.9R(2);*
  - (c) *PRU 8.1.11R(2); and*
  - (d) *PRU 8.1.12R to PRU 8.1.14R.*
- (2) *The rules referred to in (1):*
- (a) *only apply with respect to a financial conglomerate if it is an FSA regulated EEA financial conglomerate;*
  - (b) *(so far as they apply with respect to a group that is not a financial conglomerate) do not apply with respect to a group for which a competent authority in another EEA state is lead regulator;*
  - (c) *(so far as they apply with respect to a financial conglomerate) do not apply to a firm with respect to a financial conglomerate of which it is a member if the interest of the financial conglomerate in that firm is no more than a participation;*

(d) (so far as they apply with respect to other *groups*) do not apply to a *firm* with respect to a *group* of which it is a member if the only relationship of the kind set out in paragraph (3) of the definition of *group* between it and the other members of the *group* is nothing more than a *participation*; and

(e) do not apply with respect to a *third-country group*.

8.1.6 G For the purposes of *PRU* 8.1, a *group* is defined in the *Glossary*, and includes the whole of a firm's group, including financial and non-financial undertakings. It also covers undertakings with other links to *group* members if their omission from the scope of *group* risk systems and controls would be misleading. The scope of the *group* systems and controls requirements may therefore differ from the scope of the quantitative requirements for *groups*.

#### Purpose

8.1.7 G The purpose of this chapter is to set out how systems and controls requirements apply where a *firm* is part of a *group*. *SYSC* 3.1 (Systems and controls) requires a *firm* to take reasonable care to establish and maintain such systems and controls as are appropriate to the nature, scale and complexity of its business. If a *firm* is a member of a *group*, it should be able to assess the potential impact of risks arising from other parts of its *group* as well as from its own activities.

8.1.8 G *PRU* 8.1 implements Articles 52(6) (Supervision on a consolidated basis of credit institutions) and 55a (Intra-group transactions with mixed activity holding companies) of the *Banking Consolidation Directive*, Article 9 of the *Financial Groups Directive* (Internal control mechanisms and risk management processes) and Article 8 of the *Insurance Groups Directive* (Intra-group transactions).

#### General rules

8.1.9 R A *firm* must:

- (1) have adequate, sound and appropriate risk management processes and internal control mechanisms for the purpose of assessing and managing its own exposure to *group* risk, including sound administrative and accounting procedures; and
- (2) ensure that its *group* has adequate, sound and appropriate risk management processes and internal control mechanisms at the level of the *group*, including sound administrative and accounting procedures.

8.1.10 G For the purposes of *PRU* 8.1.9R, the question of whether the risk management processes and internal control mechanisms are adequate, sound and appropriate should be judged in the light of the nature, scale and complexity of the *group*'s business.

8.1.11 R The internal control mechanisms referred to in *PRU* 8.1.9R must include:



- (1) mechanisms that are adequate for the purpose of producing any data and information which would be relevant for the purpose of monitoring compliance with any prudential requirements (including any reporting requirements and any requirements relating to capital adequacy, solvency and large exposures):
  - (a) to which the *firm* is subject with respect to its membership of a *group*; or
  - (b) that apply to or with respect to that *group* or part of it; and
- (2) mechanisms that are adequate to monitor funding within the *group*.

Financial conglomerates

- 8.1.12 R Where *PRU* 8.1 applies with respect to a *financial conglomerate*, the risk management processes referred to in *PRU* 8.1.9R(2) must include:
- (1) sound governance and management processes, which must include the approval and periodic review by the appropriate managing bodies within the *financial conglomerate* of the strategies and policies of the *financial conglomerate* in respect of all the risks assumed by the *financial conglomerate*, such review and approval being carried out at the level of the *financial conglomerate*;
  - (2) adequate capital adequacy policies at the level of the *financial conglomerate*, one of the purposes of which must be to anticipate the impact of the business strategy of the *financial conglomerate* on its risk profile and on the capital adequacy requirements to which it and its members are subject;
  - (3) adequate procedures for the purpose of ensuring that the risk monitoring systems of the *financial conglomerate* and its members are well integrated into their organisation; and
  - (4) adequate procedures for the purpose of ensuring that the systems and controls of the members of the *financial conglomerate* are consistent and that the risks can be measured, monitored and controlled at the level of the *financial conglomerate*.
- 8.1.13 R Where *PRU* 8.1 applies with respect to a *financial conglomerate*, the internal control mechanisms referred to in *PRU* 8.1.9R(2) must include:
- (1) mechanisms that are adequate to identify and measure all material risks incurred by members of the *financial conglomerate* and appropriately relate capital in the *financial conglomerate* to risks; and
  - (2) sound reporting and accounting procedures for the purpose of identifying, measuring, monitoring and controlling *intra-group transactions* and *risk concentrations*.

Credit institutions and investment firms

8.1.14 R In the case of a *firm* that:

(1) is a *credit institution* or *investment firm*; and

(2) has a *mixed-activity holding company* as a *parent undertaking*;

the risk management processes and internal control mechanisms referred to in *PRU* 8.1.9R must include sound reporting and accounting procedures and other mechanisms that are adequate to identify, measure, monitor and control transactions between the *firm's parent undertaking mixed-activity holding company* and any of the *mixed-activity holding company's subsidiary undertakings*.

Insurance undertakings

8.1.15 R In the case of an *insurer* that has a *mixed-activity insurance holding company* as a *parent undertaking*, the risk management processes and internal control mechanisms referred to in *PRU* 8.1.9R must include sound reporting and accounting procedures and other mechanisms that are adequate to identify, measure, monitor and control transactions between the *firm's parent undertaking mixed-activity insurance holding company* and any of the *mixed-activity insurance holding company's subsidiary undertakings*.

8.1.16 G *PRU* 8.1.14R cannot apply to a *building society* as it cannot have a *mixed-activity holding company* as a *parent undertaking*. *PRU* 8.1.15R cannot apply to a *friendly society* as it cannot have a *mixed-activity insurance holding company* as a *parent undertaking*.

Nature and extent of requirements and allocation of responsibilities within the group

8.1.17 G Assessment of the adequacy of a *group's* systems and controls required by *PRU* 8.1 will form part of the *FSA's* risk management process.

8.1.18 G The nature and extent of the systems and controls necessary under *PRU* 8.1.9R(1) to address *group* risk will vary according to the materiality of those risks to the *firm* and the position of the *firm* within the *group*.

8.1.19 G In some cases the management of the systems and controls used to address the risks described in *PRU* 8.1.9R(1) may be organised on a *group-wide* basis. If the *firm* is not carrying out those functions itself, it should delegate them to the *group* members that are carrying them out. However, this does not relieve the *firm* of responsibility for complying with its obligations under *PRU* 8.1.9R(1). A *firm* cannot absolve itself of such a responsibility by claiming that any breach of that *rule* is caused by the actions of another member of the *group* to whom the *firm* has delegated tasks. The risk management arrangements are still those of the *firm*, even though personnel elsewhere in the *firm's group* are carrying out these functions on its behalf.

- 8.1.20 G *PRU 8.1.9R(1)* deals with the systems and controls that a *firm* should have in respect of the exposure it has to the rest of the *group*. On the other hand, the purpose of *PRU 8.1.9R(2)* and the *rules* in *PRU 8.1* that amplify it is to require *groups* to have adequate systems and controls. However a *group* is not a single legal entity on which obligations can be imposed. Therefore the obligations have to be placed on individual *firms*. The purpose of imposing the obligations on each *firm* in the *group* is to make sure that the *FSA* can take supervisory action against any *firm* in a *group* whose systems and controls do not meet the standards in *PRU 8.1*. Thus responsibility for compliance with the *rules* for *group* systems and controls is a joint one.
- 8.1.21 G If both a *firm* and its *parent undertaking* are subject to *PRU 8.1.9R(2)*, the *FSA* would not expect systems and controls to be duplicated. In this case, the *firm* should assess whether and to what extent it can rely on its parent's *group* risk systems and controls.

Sections 8.2 and 8.3 - to follow.

Insert new Sections 8.4 and 8.5 as follows:

8.4 Cross sector groups

Application

- 8.4.1 R (1) *PRU 8.4* applies to every *firm* that is a member of a *financial conglomerate* other than:
- (a) an *incoming EEA firm*;
  - (b) an *incoming Treaty firm*;
  - (c) a *UCITS qualifier*; and
  - (d) an *ICVC*.
- (2) *PRU 8.4* does not apply to a *firm* with respect to a *financial conglomerate* of which it is a member if the interest of the *financial conglomerate* in that *firm* is no more than a *participation*.
- (3) *PRU 8.4.25* (Capital adequacy requirements: high level requirement), *PRU 8.4.26R* (Capital adequacy requirements: application of Method 4 from Annex I of the Financial Groups Directive), *PRU 8.4.29R* (Capital adequacy requirements: application of Methods 1, 2 or 3 from Annex I of the Financial Groups Directive) and *PRU 8.4.35* (Risk concentration and intra group transactions: the main rule) do not apply with respect to a *third-country financial conglomerate*.

## Purpose

- 8.4.2 G PRU 8.4 implements the *Financial Groups Directive*. However, material on the following topics is to be found elsewhere in the *Handbook* as follows:
- (1) further material on *third-country financial conglomerates* can be found in PRU 8.5;
  - (2) SUP 15.9 contains notification *rules* for members of *financial conglomerates*;
  - (3) material on reporting obligations can be found in SUP 16.7.73R and SUP 16.7.74R; and
  - (4) material on systems and controls in *financial conglomerates* can be found in PRU 8.1.

## Introduction: identifying a financial conglomerate

- 8.4.3 G
- (1) In general the process in (2) to (8) applies for identifying *financial conglomerates*.
  - (2) *Competent authorities* that have authorised *regulated entities* should try to identify any *consolidation group* that is a *financial conglomerate*. If a *competent authority* is of the opinion that a *regulated entity* authorised by that *competent authority* is a member of a *consolidation group* which may be a *financial conglomerate* it should communicate its view to the other *competent authorities* concerned.
  - (3) A *competent authority* may start (as described in (2)) the process of deciding whether a group is a *financial conglomerate* even if it would not be the *coordinator*.
  - (4) A member of a group may also start that process by notifying one of the *competent authorities* that have authorised group members that its group may be a *financial conglomerate*, for example by notification under SUP 15.9.
  - (5) If a group member gives a notification in accordance with (4), that does not automatically mean that the group should be treated as a *financial conglomerate*. The process described in (6) to (9) still applies.
  - (6) The *competent authority* that would be *coordinator* will take the lead in establishing whether a group is a *financial conglomerate* once the process has been started as described in (2) and (3).
  - (7) The process of establishing whether a group is a *financial conglomerate* will normally involve discussions between the *financial conglomerate* and the *competent authorities* concerned.

- (8) A *financial conglomerate* should be notified by its *coordinator* that it has been identified as a *financial conglomerate* and of the appointment of the *coordinator*. The notification should be given to the *parent undertaking* at the head of the group or, in the absence of a *parent undertaking*, the *regulated entity* with the largest balance sheet total in the *most important financial sector*. That notification does not of itself make a group into a *financial conglomerate*; whether or not a group is a *financial conglomerate* is governed by the definition of *financial conglomerate* as set out in PRU 8.4.
- (9) PRU 8 Ann 4G is a questionnaire (together with its explanatory notes) that the FSA asks groups that may be *financial conglomerates* to fill out in order to decide whether or not they are.

Introduction: The role of other competent authorities

- 8.4.4 G A lead supervisor (called the *coordinator*) is appointed for each *financial conglomerate*. Article 10 of the *Financial Groups Directive* describes the criteria for deciding which *competent authority* is appointed as *coordinator*. Article 11 of the *Financial Groups Directive* sets out the tasks of the *coordinator*.

Definition of financial conglomerate: basic definition

- 8.4.5 R A *financial conglomerate* means a *consolidation group* that is identified as a *financial conglomerate* in accordance with the decision tree in PRU 8 Ann 3R.

Definition of financial conglomerate: sub-groups

- 8.4.6 R A *consolidation group* is not prevented from being a *financial conglomerate* because it is part of a wider:

- (1) *consolidation group*; or
- (2) *financial conglomerate*; or
- (3) group of persons linked in some other way.

Definition of financial conglomerate: the financial sectors: general

- 8.4.7 R For the purpose of the definition of *financial conglomerate*, there are two *financial sectors* as follows:

- (1) the *banking sector* and the *investment services sector*, taken together; and
- (2) the *insurance sector*.

- 8.4.8 R (1) This *rule* applies for the purpose of the definition of *financial conglomerate* and the *financial conglomerate definition decision tree*.
- (2) Any *mixed financial holding company* is considered to be outside the *overall financial sector* for the purpose of the tests set out in the boxes titled Threshold Test 1, Threshold Test 2 and Threshold Test 3 in the *financial*

*conglomerate definition decision tree.*

- (3) Determining whether the tests set out in the boxes titled Threshold Test 2 and Threshold Test 3 in the *financial conglomerate definition decision tree* are passed is based on considering the consolidated and/or aggregated activities of the members of the *consolidation group* within the *insurance sector* and the consolidated and/or aggregated activities of the members of the *consolidation group* within the *banking sector* and the *investment services sector*.

Definition of financial conglomerate: adjustment of the percentages

- 8.4.9 R Once a *financial conglomerate* has become a *financial conglomerate* and subject to supervision in accordance with the *Financial Groups Directive*, the figures in the *financial conglomerate definition decision tree* are altered as follows:
- (1) the figure of 40% in the box titled Threshold Test 1 is replaced by 35%;
  - (2) the figure of 10% in the box titled Threshold Test 2 is replaced by 8%; and
  - (3) the figure of six billion Euro in the box titled Threshold Test 3 is replaced by five billion Euro.

- 8.4.10 R The alteration in *PRU 8.4.9R* only applies to a *financial conglomerate* during the period that:
- (1) begins when the *financial conglomerate* would otherwise have stopped being a *financial conglomerate* because it does not meet one of the unaltered thresholds referred to in *PRU 8.4.9R*; and
  - (2) covers the three years following that date.

Definition of financial conglomerate: balance sheet totals

- 8.4.11 R The calculations referred to in the *financial conglomerate definition decision tree* regarding the balance sheet must be made on the basis of the aggregated balance sheet total of the members of the *consolidation group*, according to their annual accounts. For the purposes of this calculation, *undertakings* in which a *participation* is held must be taken into account as regards the amount of their balance sheet total corresponding to the aggregated proportional share held by the *consolidation group*. However, where consolidated accounts are available, they must be used instead of aggregated accounts.

Definition of financial conglomerate: solvency requirement

- 8.4.12 R The solvency and capital adequacy requirements referred to in the *financial conglomerate definition decision tree* must be calculated in accordance with the provisions of the relevant *sectoral rules*.

Definition of financial conglomerate: discretionary changes to the definition

- 8.4.13 G Articles 3(3) to 3(6), Article 5(4) and Article 6(5) of the *Financial Groups Directive* allow *competent authorities*, on a case by case basis, to:
- (1) change the definition of *financial conglomerate* and the obligations applying with respect to a *financial conglomerate*;
  - (2) apply the scheme in the *Financial Groups Directive* to *EEA regulated entities* in specified kinds of group structures that do not come within the definition of *financial conglomerate*; and
  - (3) exclude a particular entity in the scope of capital adequacy requirements that apply with respect to a *financial conglomerate*.

Capital adequacy requirements: introduction

- 8.4.14 G The capital adequacy provisions of PRU 8.4 are designed to be applied to *EEA-based financial conglomerates*.
- 8.4.15 G *PRU 8.4.25R* is a high level capital adequacy *rule*. It applies whether or not the *FSA* is the *coordinator* of the *financial conglomerate* concerned.
- 8.4.16 G *PRU 8.4.26R* to *PRU 8.4.31R* and *PRU 8 Ann 1R* implement the detailed capital adequacy requirements of the *Financial Groups Directive*. They only deal with a *financial conglomerate* for which the *FSA* is the *coordinator*. If another *competent authority* is *coordinator* of a *financial conglomerate*, those *rules* do not apply with respect to that *financial conglomerate* and instead that *coordinator* will be responsible for implementing those detailed requirements.
- 8.4.17 G Annex I of the *Financial Groups Directive* lays down four methods for calculating capital adequacy at the level of a *financial conglomerate*. Those four methods are implemented as follows:
- (1) Method 1 calculates capital adequacy using accounting consolidation. It is implemented by *PRU 8.4.29R* to *PRU 8.4.31R* and Part 1 of *PRU 8 Ann 1R*.
  - (2) Method 2 calculates capital adequacy using a deduction and aggregation approach. It is implemented by *PRU 8.4.29R* to *PRU 8.4.31R* and Part 2 of *PRU 8 Ann 1R*.
  - (3) Method 3 calculates capital adequacy using book values and the deduction of capital requirements. It is implemented by *PRU 8.4.29R* to *PRU 8.4.31R* and Part 3 of *PRU 8 Ann 1R*.
  - (4) Method 4 consists of a combination of Methods 1, 2 and 3 from Annex I of the *Financial Groups Directive*, or a combination of two of those Methods. It is implemented by *PRU 8.4.26R* to *PRU 8.4.28R*, *PRU 8.4.30R* and Part 4 of *PRU 8 Ann 1R*.

- 8.4.18 G Part 4 of *PRU 8 Ann 1R* (Use of Method 4 from Annex I of the *Financial Conglomerates Directive*) applies the *FSA's sectoral rules* with respect to the *financial conglomerate* as a whole, with some adjustments. Where Part 4 of *PRU 8 Ann 1R* applies the *FSA's sectoral rules* for:
- (1) the *insurance sector*, that involves a combination of Methods 2 and 3; and
  - (2) the *banking sector* and the *investment services sector*, that involves a combination of Methods 1 and 3.
- 8.4.19 G Paragraph 5.5 of *PRU 8 Ann 1R* (Capital adequacy calculations for financial conglomerates) deals with a case in which there are no capital ties between entities in a *financial conglomerate*. In particular, the *FSA*, after consultation with the other *relevant competent authorities* and in accordance with Annex I of the *Financial Groups Directive*, will determine which proportional share of a solvency deficit in such an entity will have to be taken into account, bearing in mind the liability to which the existing relationship gives rise.
- 8.4.20 G (1) In the following cases, the *FSA* (acting as *coordinator*) may choose which of the four methods for calculating capital adequacy laid down in Annex I of the *Financial Groups Directive* should apply:
- (a) where a *financial conglomerate* is headed by a *regulated entity* that has been authorised by the *FSA*; or
  - (b) the only *relevant competent authority* for the *financial conglomerate* is the *FSA*.
- (2) *PRU 8.4.28R* automatically applies Method 4 from Annex I of the *Financial Groups Directive* in these circumstances except in the cases set out in *PRU 8.4.28R(1)(e)* and *PRU 8.4.28R(1)(f)*. The process in *PRU 8.4.22G* does not apply.
- 8.4.21 G Where *PRU 8.4.20G* does not apply, the Annex I method to be applied is decided by the *coordinator* after consultation with the *relevant competent authorities* and the *financial conglomerate* itself.
- 8.4.22 G The method of calculating capital adequacy chosen in respect of a *financial conglomerate* as described in *PRU 8.4.21G* will be applied with respect to that *financial conglomerate* by varying the *Part IV permission* of a *firm* in that *financial conglomerate* to include a *requirement*. That *requirement* will have the effect of obliging the *firm* to ensure that the *financial conglomerate* has capital resources of the type and amount needed to comply with whichever of the methods in *PRU 8 Ann 1R* is to be applied with respect to that *financial conglomerate*. The powers in the *Act* relating to *waivers* and varying a *firm's Part IV permission* can be used to implement one of the methods from Annex I of the *Financial Groups Directive* in a way that is different from that set out in *PRU 8.4* and *PRU 8 Ann 1R* if that is necessary to reflect the consultations referred to in *PRU 8.4.21G*.



8.4.23 G If there is more than one *firm* in a *financial conglomerate* with a *Part IV permission*, the *FSA* would not normally expect to apply the *requirement* described in *PRU 8.4.22G* to all of them. Normally it will only be necessary to apply it to one.

8.4.24 G The *FSA* expects that in all or most cases falling into *PRU 8.4.21G*, the *rules* in Part 4 of *PRU 8 Ann 1R* will be applied.

Capital adequacy requirements: high level requirement

8.4.25 R (1) A *firm* that is a member of a *financial conglomerate* must at all times have capital resources of such an amount and type that results in the capital resources of the *financial conglomerate* taken as a whole being adequate.

(2) This *rule* does not apply with respect to any *financial conglomerate* until notification has been made that it has been identified as a *financial conglomerate* as contemplated by Article 4(2) of the *Financial Groups Directive*.

Capital adequacy requirements: application of Method 4 from Annex I of the *Financial Groups Directive*

8.4.26 R If this *rule* applies under *PRU 8.4.27R* to a *firm* with respect to a *financial conglomerate* of which it is a member, the *firm* must at all times have capital resources of an amount and type:

(1) that ensure that the *financial conglomerate* has capital resources of an amount and type that comply with the *rules* applicable with respect to that *financial conglomerate* under Part 4 of *PRU 8 Ann 1R* (as modified by that annex); and

(2) that as a result ensure that the *firm* complies with those *rules* (as so modified) with respect to that *financial conglomerate*.

8.4.27 R *PRU 8.4.26R* applies to a *firm* with respect to a *financial conglomerate* of which it is a member if one of the following conditions is satisfied:

(1) the condition in *PRU 8.4.28R* is satisfied; or

(2) this *rule* is applied to the *firm* with respect to that *financial conglomerate* as described in *PRU 8.4.30R*.

Capital adequacy requirements: compulsory application of Method 4 from Annex I of the *Financial Groups Directive*

8.4.28 R (1) The condition in this *rule* is satisfied for the purpose of *PRU 8.4.27R*(1) with respect to a *firm* and a *financial conglomerate* of which it is a member (with the result that *PRU 8.4.26R* automatically applies to that *firm*) if:

- (a) notification has been made in accordance with regulation 2 of the *Financial Groups Directive Regulations* that the *financial conglomerate* is a *financial conglomerate* and that the *FSA* is *coordinator* of that *financial conglomerate*;
  - (b) the *financial conglomerate* is not part of a wider *FSA regulated EEA financial conglomerate*;
  - (c) the *financial conglomerate* is not an *FSA regulated EEA financial conglomerate* under another *rule* or under paragraph (b) of the definition of *FSA regulated EEA financial conglomerate* (application of supplementary supervision through a *firm's Part IV permission*);
  - (d) one of the following conditions is satisfied:
    - (i) the *financial conglomerate* is headed by a *regulated entity* that is a *UK domestic firm*; or
    - (ii) the only *relevant competent authority* for that *financial conglomerate* is the *FSA*;
  - (e) this *rule* is not disapplied under paragraph 5.5 of *PRU 8 Ann 1R* (No capital ties); and
  - (f) the *financial conglomerate* meets the condition set out in the box titled Threshold Test 2 (10% average of balance sheet and solvency requirements) in the *financial conglomerate definition decision tree*.
- (2) Once *PRU 8.4.26R* applies to a *firm* with respect to a *financial conglomerate* of which it is a member under *PRU 8.4.27R(1)*, (1)(f) ceases to apply with respect to that *financial conglomerate*. Therefore the fact that the *financial conglomerate* subsequently ceases to meet the condition in (1)(f) does not mean that the condition in this *rule* is not satisfied.

Capital adequacy requirements: application of Methods 1, 2 or 3 from Annex I of the Financial Groups Directive

- 8.4.29 R If with respect to a *firm* and a *financial conglomerate* of which it is a member, this *rule* is applied to the *firm* with respect to that *financial conglomerate* as described in *PRU 8.4.30R*, the *firm* must at all times have capital resources of an amount and type that ensures that the *conglomerate capital resources* of that *financial conglomerate* at all times equal or exceed its *conglomerate capital resources requirement*.

Capital adequacy requirements: use of Part IV permission to apply Annex I of the Financial Groups Directive

- 8.4.30 R With respect to a *firm* and a *financial conglomerate* of which it is a member:

- (1) *PRU 8.4.26R* (Method 4 from Annex I of the *Financial Groups Directive*) is applied to the *firm* with respect to that *financial conglomerate* for the purposes of *PRU 8.4.27R(2)*; or
- (2) *PRU 8.4.29R* (Methods 1 to 3 from Annex I of the *Financial Groups Directive*) is applied to the *firm* with respect to that *financial conglomerate*;

if the *firm's Part IV permission* contains a *requirement* obliging the *firm* to comply with *PRU 8.4.26R* or, as the case may be, *PRU 8.4.29R*.

- 8.4.31 R If *PRU 8.4.29R* (Methods 1-3 from Annex I of the *Financial Groups Directive*) applies to a *firm* with respect to a *financial conglomerate* of which it is a member, the definitions of *conglomerate capital resources* and *conglomerate capital resources requirement* that apply for the purposes of that *rule* are the ones from whichever of Part 1, Part 2 or Part 3 of *PRU 8 Ann 1R* is specified in the *requirement* referred to in *PRU 8.4.30R*.

Risk concentration and intra-group transactions: introduction

- 8.4.32 G *PRU 8.4.35R* implements Article 7(4) and Article 8(4) of the *Financial Groups Directive*, which provide that where a *financial conglomerate* is headed by a *mixed financial holding company*, the *sectoral rules* regarding *risk concentration* and *intra-group transactions* of the *most important financial sector* in the *financial conglomerate*, if any, shall apply to that sector as a whole, including the *mixed financial holding company*.

- 8.4.33 G Articles 7(3) (Risk concentration) and 8(3) (Intra-group transactions) and Annex II (Technical application of the provisions on intra-group transactions and risk concentration) of the *Financial Groups Directive* say that Member States may apply at the level of the *financial conglomerate* the provisions of the *sectoral rules* on *risk concentrations* and *intra-group transactions*. *PRU 8.4* does not take up that option, although the *FSA* may impose such obligations on a case by case basis.

Risk concentration and intra-group transactions: application

- 8.4.34 R *PRU 8.4.35R* applies to a *firm* with respect to a *financial conglomerate* of which it is a member if:
- (1) the condition in Articles 7(4) and 8(4) of the *Financial Groups Directive* is satisfied (the *financial conglomerate* is headed by a *mixed financial holding company*); and
  - (2) that *financial conglomerate* is an *FSA regulated EEA financial conglomerate*.

Risk concentration and intra group transactions: the main rule

- 8.4.35 R A firm must ensure that the *sectoral rules* regarding *risk concentration* and *intra-group transactions* of the *most important financial sector* in the *financial conglomerate* referred to in PRU 8.4.34R are complied with with respect to that *financial sector* as a whole, including the *mixed financial holding company*. The *FSA's sectoral rules* for these purposes are those identified in the table in PRU 8.4.36R.

Risk concentration and intra-group transactions: Table of applicable sectoral rules

- 8.4.36 R Table: application of sectoral rules  
This table belongs to PRU 8.4.35R

The most important financial sector	Applicable sectoral rules	
	Risk concentration	Intra-group transactions
<i>Banking sector</i>	<i>Rules 3.3.13, 3.3.19 and 3.3.21 of chapter GN of IPRU(BANK) (as they apply to large exposures on a consolidated basis)</i>	<i>Rules 3.3.13, 3.3.19 and 3.3.21 of chapter GN of IPRU(BANK) (as they apply to large exposures on a solo basis)</i>
<i>Insurance sector</i>	None	<i>Rule 9.39 of IPRU(INS)</i>
<i>Investment services sector</i>	<i>Rule 14.3.2 in Chapter 14 of IPRU(INV)</i>	<i>Rule 10-190 in Chapter 10 of IPRU(INV) as it applies on a solo basis</i>
Note:	The <i>rules</i> as applied in column three apply without any concession or exemption for exposures to other group members.	
Note	The decision tree in paragraph 4.5 of PRU 8 Ann 1R applies for the purpose of identifying the <i>most important financial sector</i> .	

- 8.4.37 G The material in *IPRU(BANK)* that has particular application to the *rules* in *IPRU(BANK)* referred to in the table in PRU 8.4.36R is:
- (1) (in the case of column 2) Chapter LE as it applies on a consolidated basis;
  - (2) (in the case of column 3) Chapter LE as it applies on a solo basis.
- 8.4.38 G The table in PRU 8.4.36R does not refer to the *rules* for *building societies* as a *building society* cannot have a *mixed financial holding company* as a parent.

The financial sectors: asset management companies

- 8.4.39 R (1) In accordance with Article 30 of the *Financial Groups Directive* (Asset management companies), this *rule* deals with the inclusion of an *asset management company* that is a member of a *financial conglomerate* in the scope of regulation of *financial conglomerates*. This *rule* does not apply to the definition of *financial conglomerate*.
- (2) An *asset management company* is in the *overall financial sector* and is a *regulated entity* for the purpose of:
- (a) *PRU 8.4.26R* to *PRU 8.4.36R*;
  - (b) *PRU 8 Ann 1R* (Capital adequacy calculations for financial conglomerates) and *PRU 8 Ann 2R* (Prudential rules for third country groups); and
  - (c) any other provision of the *Handbook* relating to the supervision of *financial conglomerates*.
- (3) In the case of a *financial conglomerate* for which the *FSA* is the *coordinator*, all *asset management companies* must be allocated to one *financial sector* for the purposes in (2), being either the *investment services sector* or the *insurance sector*. But if that choice has not been made in accordance with (4) and notified to the *FSA* in accordance with (4)(d), an *asset management company* must be allocated to the *investment services sector*.
- (4) The choice in (3):
- (a) must be made by the *undertaking* in the *financial conglomerate* holding the position referred to in Article 4(2) of the *Financial Groups Directive* (group member to whom notice must be given that the group has been found to be a *financial conglomerate*);
  - (b) applies to all *asset management companies* that are members of the *financial conglomerate* from time to time;
  - (c) cannot be changed; and
  - (d) must be notified to the *FSA* as soon as reasonably practicable after the notification in (4)(a).

8.5 Third-country groups  
Application

8.5.1 R *PRU 8.5 applies to every firm that is a member of a third-country group. But it does not apply to:*

- (1) *an incoming EEA firm; or*
- (2) *an incoming Treaty firm; or*
- (3) *a UCITS qualifier; or*
- (4) *an ICVC.*

#### Purpose

8.5.2 G *PRU 8.5 implements in part Article 18 of the Financial Groups Directive and Article 56a of the Banking Consolidation Directive.*

#### Equivalence

8.5.3 G *The first question that must be asked about a third-country financial group is whether the EEA regulated entities in that third-country group are subject to supervision by a third-country competent authority, which is equivalent to that provided for by the Financial Groups Directive (in the case of a financial conglomerate) or the EEA prudential sectoral legislation for the banking sector or the investment services sector (in the case of a banking and investment group). Article 18(1) of the Financial Groups Directive sets out the process for establishing equivalence with respect to third-country financial conglomerates and the first three paragraphs of Article 56a of the Banking Consolidation Directive does so with respect to third-country banking and investment groups.*

#### Other methods: General

8.5.4 G *If the supervision of a third-country group by a third-country competent authority does not meet the equivalence test referred to in PRU 8.5.3G, competent authorities may apply other methods that ensure appropriate supervision of the EEA regulated entities in that third-country group in accordance with the aims of supplementary supervision under the Financial Groups Directive or consolidated supervision under the applicable EEA prudential sectoral legislation.*

Supervision by analogy: introduction

- 8.5.5 G If the supervision of a *third-country group* by a *third-country competent authority* does not meet the equivalence test referred to in *PRU 8.5.3G*, a *competent authority* may, rather than take the measures described in *PRU 8.5.4G*, apply, by analogy, the provisions concerning supplementary supervision under the *Financial Groups Directive* or, as applicable, consolidated supervision under the applicable *EEA prudential sectoral legislation*, to the *EEA regulated entities* in the *banking sector*, *investment services sector* and (in the case of a *financial conglomerate* ) *insurance sector*.
- 8.5.6 G The *FSA* believes that it will only be right to adopt the option in *PRU 8.5.5G* in response to very unusual group structures.
- 8.5.7 G *PRU 8.5.8R* and *PRU 8.5.9R* and *PRU 8 Ann 2* set out *rules* to deal with the situation covered in *PRU 8.5.5G*. Those *rules* do not apply automatically. Instead, they can only be applied with respect to a particular *third-country group* through the *Part IV permission* of a *firm* in that *third-country group*. Broadly speaking the procedure described in *PRU 8.4.22G* also applies to this process.

Supervision by analogy: rules for third-country conglomerates

- 8.5.8 R If the *Part IV permission* of a *firm* contains a *requirement* obliging it to comply with this *rule* with respect to a *third-country financial conglomerate* of which it is a member, it must comply, with respect to that *third-country financial conglomerate*, with the *rules* in Part 1 of *PRU 8 Ann 2R*, as adjusted by Part 3 of that annex.

Supervision by analogy: rules for third-country banking and investment groups

- 8.5.9 R If the *Part IV permission* of a *firm* contains a *requirement* obliging it to comply with this *rule* with respect to a *third-country banking and investment group* of which it is a member, it must comply, with respect to that *third-country banking and investment group*, with the *rules* in Part 2 of *PRU 8 Ann 2R*, as adjusted by Part 3 of that annex.

PRU 8 Ann 1R

Capital adequacy calculations for financial conglomerates (PRU 8.4.26R and PRU 8.4.29R)

1 Table: PART 1: Method of Annex I of the Financial Groups Directive (Accounting Consolidation Method)

Capital resources	1.1	The <i>conglomerate capital resources</i> of a <i>financial conglomerate</i> calculated in accordance with this Part are the capital of that <i>financial conglomerate</i> , calculated on an accounting consolidation basis, that qualifies under paragraph 1.2.	
	1.2	The elements of capital that qualify for the purposes of paragraph 1.1 are those that qualify in accordance with the <i>applicable sectoral rules</i> , in accordance with the following:	
		(1)	the <i>conglomerate capital resources requirement</i> is divided up in accordance with the contribution of each <i>financial sector</i> to it; and
		(2)	the portion of the <i>conglomerate capital resources requirement</i> attributable to a particular <i>financial sector</i> must be met by capital resources that are eligible in accordance with the <i>applicable sectoral rules</i> for that <i>financial sector</i> .
Capital resources requirement	1.3	The <i>conglomerate capital resources requirement</i> of a <i>financial conglomerate</i> calculated in accordance with this Part is equal to the sum of the capital adequacy and solvency requirements for each <i>financial sector</i> calculated in accordance with the <i>applicable sectoral rules</i> for that <i>financial sector</i> .	
Consolidation	1.4	The information required for the purpose of establishing whether or not a <i>firm</i> is complying with PRU 8.4.29R (insofar as the definitions in this Part are applied for the purpose of that <i>rule</i> ) must be based on the consolidated accounts of the <i>financial conglomerate</i> , together with such other sources of information as appropriate.	
	1.5	The <i>applicable sectoral rules</i> that are applied under this Part are the <i>applicable sectoral consolidation rules</i> . Other <i>applicable sectoral rules</i> must be applied if required.	



2 Table: PART 2: Method 2 of Annex I of the Financial Groups Directive (Deduction and aggregation Method)

Capital resources	2.1	<p>The <i>conglomerate capital resources</i> of a <i>financial conglomerate</i> calculated in accordance with this Part are equal to the sum of the following amounts (so far as they qualify under paragraph 2.3) for each member of the <i>overall financial sector</i>:</p> <p>(1) (for the <i>person</i> at the head of the <i>financial conglomerate</i>) its <i>solo capital resources</i>;</p> <p>(2) (for any other member):</p> <p>(a) its <i>solo capital resources</i>; less</p> <p>(b) the book value of the <i>financial conglomerate's</i> investment in that member.</p>
	2.2	<p>The deduction in paragraph 2.1(2) must be carried out separately for each type of capital represented by the <i>financial conglomerate's</i> investment in the member concerned.</p>
	2.3	<p>The elements of capital that qualify for the purposes of paragraph 2.1 are those that qualify in accordance with the <i>applicable sectoral rules</i>. In particular, the portion of the <i>conglomerate capital resources requirement</i> attributable to a particular member of a <i>financial sector</i> must be met by capital resources that would be eligible under the <i>sectoral rules</i> that apply to the calculation of its <i>solo capital resources</i>.</p>
Capital resources requirement	2.4	<p>The <i>conglomerate capital resources requirement</i> of a <i>financial conglomerate</i> calculated in accordance with this Part is equal to the sum of the <i>solo capital resources requirement</i> for each member of the <i>financial conglomerate</i> that is in the <i>overall financial sector</i>.</p>
Partial inclusion	2.5	<p>The capital resources and capital resources requirements of a member of the <i>financial conglomerate</i> in the <i>overall financial sector</i> must be included proportionally. If however the member is a <i>subsidiary undertaking</i> and it has a <i>solvency deficit</i>, they must be included in full.</p>
Accounts	2.6	<p>The information required for the purpose of establishing whether or not a <i>firm</i> is complying with <i>PRU 8.4.29R</i> (insofar as the definitions in this Part are applied for the purpose of that <i>rule</i>) must be based on the individual accounts of members of the <i>financial conglomerate</i>, together with such other sources of information as appropriate.</p>

3. Table: PART 3: Method 3 of Annex I of the Financial Groups Directive  
(Book value/Requirement Method)

Capital resources	3.1	The <i>conglomerate capital resources</i> of a <i>financial conglomerate</i> calculated in accordance with this Part are equal to the capital resources of the <i>person</i> at the head of the <i>financial conglomerate</i> that qualify under paragraph 3.2.
Capital resources requirement	3.2	The elements of capital that qualify for the purposes of paragraph 3.1 are those that qualify in accordance with the <i>applicable sectoral rules</i> . In particular, the portion of the <i>conglomerate capital resources requirement</i> attributable to a particular member of a <i>financial sector</i> must be met by capital resources that would be eligible under the <i>sectoral rules</i> that apply to the calculation of its <i>solo capital resources</i> .
Capital resources requirement	3.3	The <i>conglomerate capital resources requirement</i> of a <i>financial conglomerate</i> calculated in accordance with this Part is equal to the sum of the following amounts for each member of the <i>overall financial sector</i> :  (1) (in the case of the <i>person</i> at the head of the <i>financial conglomerate</i> ) its <i>solo capital resources requirement</i> ;  (2) (in the case of any other member) the higher of the following two amounts:  (a) its <i>solo capital resources requirement</i> ; and  (b) the book value of the interest of the <i>person</i> at the head of the <i>financial conglomerate</i> in that member.
Capital resources requirement	3.4	A <i>participation</i> may be valued using the equity method of accounting.
Partial inclusion	3.5	The capital resources requirement of a member of the <i>financial conglomerate</i> in the <i>overall financial sector</i> must be included proportionally. If however the member has a <i>solvency deficit</i> and is a <i>subsidiary undertaking</i> , it must be included in full.
Accounts	3.6	The information required for the purpose of establishing whether or not a <i>firm</i> is complying with <i>PRU 8.4.29R</i> (insofar as the definitions in this Part are applied for the purpose of that <i>rule</i> ) must be based on the individual accounts of members of the <i>financial conglomerate</i> , together with such other sources of information as appropriate.

**4 Table: PART 4: Method 4 of Annex I of the Financial Groups Directive**  
(Combination of Methods 1, 2 and 3)

Applicable sectoral rules	4.1	The <i>rules</i> that apply with respect to a particular <i>financial conglomerate</i> under <i>PRU</i> 8.4.26R are those relating to capital adequacy and solvency set out in the table in paragraph 4.2.
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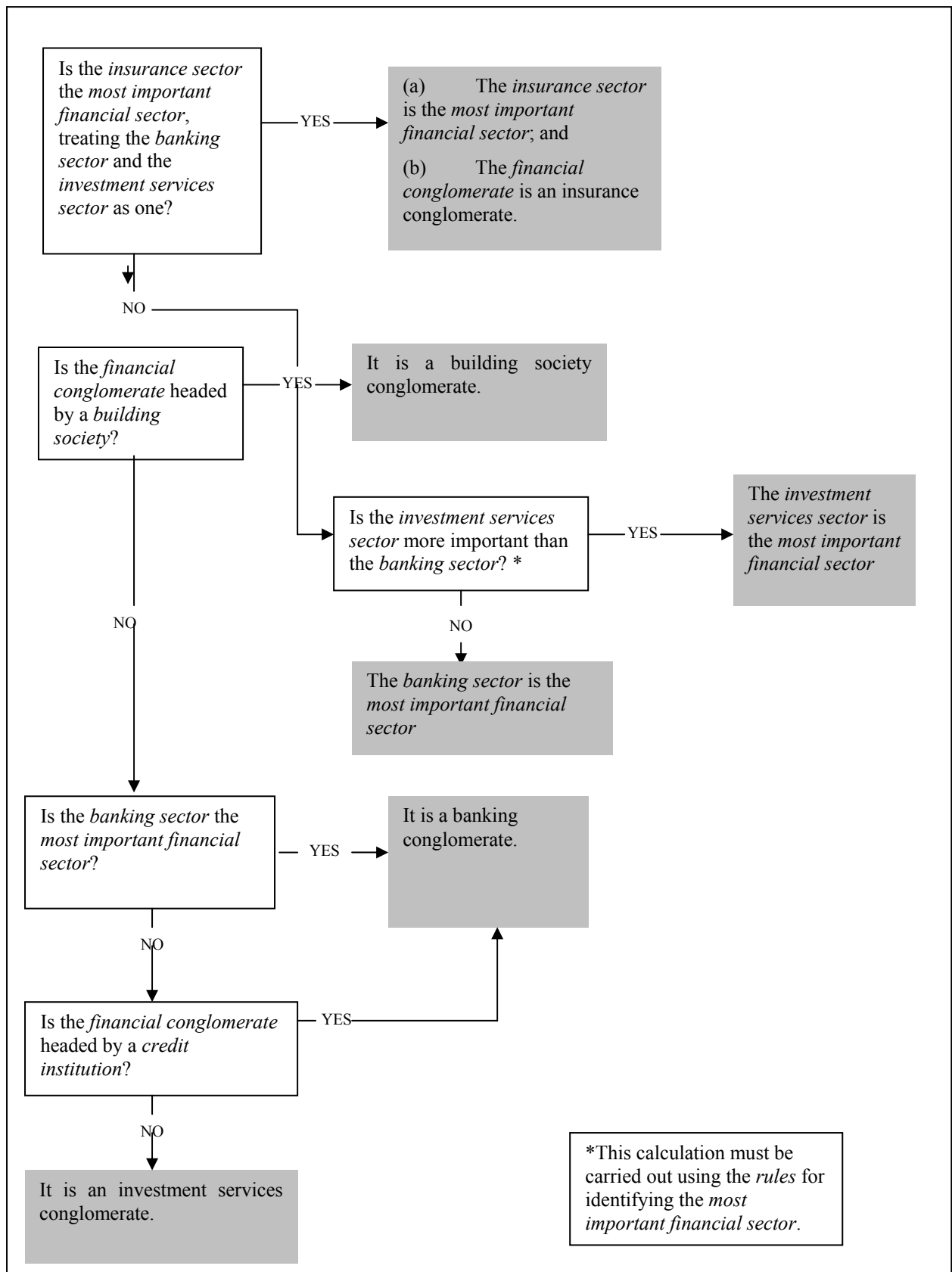
**5 Table: Paragraph 4.2: Application of sectoral consolidation rules**

Type of financial conglomerate	Applicable sectoral consolidation rules
<i>Banking conglomerate</i>	<i>IPRU(BANK)</i> Chapter GN <i>rule</i> 3.3.13 (as it applies on a consolidated basis), subject to paragraph 4.7.
<i>Insurance conglomerate</i>	Whichever of <i>IPRU(INS)</i> or <i>IPRU(FSOC)</i> would apply if those <i>rules</i> were amended in accordance with Part 5.
<i>Building society conglomerate</i>	<i>IPRU(BSOC)</i> (Volume 1) Chapter 1, <i>rule</i> 1.2.1 (as it applies on a consolidated basis).
<i>Investment services conglomerate</i>	Chapter 14 of <i>IPRU(INV)</i> .

6 Table

How to apply chapter 14 of IPRU(INV)	4.3	<p>Where chapter 14 of <i>IPRU(INV)</i> applies:</p> <ol style="list-style-type: none"> <li>(1) the <i>main investment services undertaking</i> is treated as being the main firm for the purpose of <i>rule 14.4.2</i> of chapter 14 of <i>IPRU(INV)</i>;</li> <li>(2) if the <i>main investment services undertaking</i> is not subject to any of the <i>FSA's sectoral rules</i> applied by chapter 14 of <i>IPRU(INV)</i>, then the <i>FSA's sectoral rules</i> that are applied are those that would do so if: <ol style="list-style-type: none"> <li>(a) it were a <i>UK domestic firm</i>; and</li> <li>(b) it had a <i>permission</i> that includes all the <i>regulated activities</i> that it would need to have in its <i>Part IV permission</i> if it carried on all its activities in the <i>United Kingdom</i>.</li> </ol> </li> </ol>
The different types of financial conglomerate	4.4	<ol style="list-style-type: none"> <li>(1) The decision tree in paragraph 4.5: <ol style="list-style-type: none"> <li>(a) decides into which of the categories listed in the table in paragraph 4.2 a <i>financial conglomerate</i> falls; and</li> <li>(b) modifies the definition of the <i>most important financial sector</i> for the purposes of <i>PRU 8 Ann 1R</i> and for the purposes of any other provision in <i>PRU 8 (Group risk)</i> that applies that decision tree.</li> </ol> </li> <li>(2) Paragraph 6.1(2) (<i>financial institution</i> allocated to the <i>banking sector</i>) and paragraph 6.1(3) (allocation of <i>asset management companies</i>) apply for the purpose of 4.4 and the table in paragraph 4.5.</li> </ol>

Table: Paragraph 4.5: Types of financial conglomerate and definition of most important financial sector



8 Table

A mixed financial holding company	4.6	<p>A <i>mixed financial holding company</i> must be treated in the same way as:</p> <ol style="list-style-type: none"> <li>(1) a <i>financial holding company</i> (if the <i>rules</i> in <i>IPRU(BANK)</i> or <i>IPRU(INV)</i>) are applied; or</li> <li>(2) an <i>insurance holding company</i> (if the <i>rules</i> in <i>IPRU(INS)</i> are applied).</li> </ol>
E-money	4.7	<p>If there are no <i>full credit institutions</i> or <i>investment firms</i> in a <i>banking conglomerate</i> but there are one or more <i>e-money issuers</i>, the <i>sectoral rules</i> in <i>IPRU(BANK)</i> are amended as follows :</p> <ol style="list-style-type: none"> <li>(1) the <i>rules</i> in <i>ELM</i> that apply on a solo basis must be used to establish the capital requirement for the <i>e- money issuers</i>; and</li> <li>(2) for the purpose of (1), those <i>rules</i> in <i>ELM</i> shall be amended by calculating the amount of the deductions in respect of <i>ownership shares</i> and capital falling into <i>ELM 2.4.17R(6)</i> in accordance with paragraph 3.3(2).</li> </ol>

9 Table: **PART 5: Principles applicable to all methods**

Transferability of capital	5.1	<p>Capital may not be included in:</p> <ol style="list-style-type: none"> <li>(1) a <i>firm's conglomerate capital resources</i> under <i>PRU 8.4.29R</i>; or</li> <li>(2) in the capital resources of the <i>financial conglomerate</i> for the purposes of <i>PRU 8.4.26R</i>;</li> </ol> <p>if the effectiveness of the transferability and availability of the capital across the different members of the <i>financial conglomerate</i> is insufficient, given the objectives (as referred to in the third unnumbered sub-paragraph of paragraph 2(ii) of Annex I of the <i>Financial Groups Directive</i> (Technical principles)) of the capital adequacy rules for <i>financial conglomerates</i>.</p>
Double counting	5.2	<p>Capital must not be included in:</p> <ol style="list-style-type: none"> <li>(1) a <i>firm's conglomerate capital resources</i> under <i>PRU 8.4.29R</i>;</li> </ol>

		<p>or</p> <p>(2) the capital resources of the <i>financial conglomerate</i> for the purposes of <i>PRU 8.4.26R</i>;</p> <p>if:</p> <p>(3) it would involve double counting or multiple use of the same capital; or</p> <p>(4) it results from any inappropriate intra-group creation of capital.</p>
Cross sectoral capital	5.3	<p>In accordance with the second sub-paragraph of paragraph 2(ii) of Section I of Annex I of the <i>Financial Groups Directive</i> (Other technical principles and insofar as not already required in Parts 1-3):</p> <p>(1) the solvency requirements for each different <i>financial sector</i> represented in a <i>financial conglomerate</i> required by <i>PRU 8.4.26R</i> or, as the case may be, <i>PRU 8.4.29R</i> must be covered by own funds elements in accordance with the corresponding <i>applicable sectoral rules</i>; and</p> <p>(2) if there is a deficit of own funds at the <i>financial conglomerate</i> level, only cross sectoral capital (as referred to in that sub-paragraph) shall qualify for verification of compliance with the additional solvency requirement required by <i>PRU 8.4.26R</i> or, as the case may be, <i>PRU 8.4.29R</i>.</p>
Application of sectoral rules	5.4	<p>The following adjustments apply to the <i>applicable sectoral rules</i> as they are applied by the <i>rules</i> in this annex.</p> <p>(1) The scope of those <i>rules</i> will be extended to cover any <i>mixed financial holding company</i> and each other member of the <i>overall financial sector</i>.</p> <p>(2) If any of those <i>rules</i> would otherwise not apply to a situation in which they are applied by <i>PRU 8 Ann 1R</i>, those <i>rules</i> nevertheless still apply (and in particular, any of those <i>rules</i> that would otherwise have the effect of disapplying consolidated supervision (or, in the case of the <i>insurance sector</i>, supplementary supervision) do not apply).</p> <p>(3) (If it would not otherwise have been included) an <i>ancillary investment services undertaking</i> is included in the <i>investment services sector</i>.</p> <p>(4) (If it would not otherwise have been included) an <i>ancillary insurance services undertaking</i> is included in the <i>insurance sector</i>.</p>

		<p>(5) (In relation to the <i>insurance sector</i>) to the extent that:</p> <ul style="list-style-type: none"> <li>(a) those <i>rules</i> merely require a report on whether or not a specified level of solvency is met (a soft limit); or</li> <li>(b) the requirements in those <i>rules</i> concern having certain net assets of an amount at or above certain levels;</li> </ul> <p>those requirements are restated so as to include an obligation at all times actually to have capital at or above that level (a hard limit), thereby turning a soft limit drafted by reference to assets and liabilities into a hard limit requiring capital to be held at or above specified levels. If those <i>rules</i> apply both a hard and a soft limit, and the level of the soft limit is higher, that soft limit is applied under this annex, but translated into a hard limit in accordance with the earlier provisions of (5).</p> <p>(6) The scope of the those <i>rules</i> is amended so as to remove restrictions relating to where members of the <i>financial conglomerate</i> are incorporated or have their head office, so that the scope covers every member of the <i>financial conglomerate</i> that would have been included in the scope of those <i>rules</i> if those members had their head offices in an <i>EEA State</i>.</p> <p>(7) (For the purposes of Parts 1 to 3) those <i>rules</i> must be adjusted, if necessary, when calculating the capital resources, capital resources requirements or solvency requirements for a particular <i>financial sector</i> to exclude those for a member of another <i>financial sector</i>.</p>
No capital ties	5.5	<p>(1) This <i>rule</i> deals with a <i>financial conglomerate</i> in which some of the members are not linked by capital ties at the time of the notification referred to in <i>PRU 8.4.28R(1)</i> (Capital adequacy requirements: Compulsory application of Method 4 from Annex I of the Financial Groups Directive).</p> <p>(2) If:</p> <ul style="list-style-type: none"> <li>(a) <i>PRU 8.4.26R</i> (Capital adequacy requirements: Application of Method 4 from Annex I of the Financial Groups Directive) would otherwise apply with respect to a <i>financial conglomerate</i> under <i>PRU 8.4.28R</i>; and</li> </ul>



- (b) all members of that *financial conglomerate* are linked directly or indirectly with each other by capital ties except for members that collectively are of negligible interest with respect to the objectives of supplementary supervision of *regulated entities* in a *financial conglomerate* (the "peripheral members");

*PRU 8.4.28R* continues to apply. Otherwise *PRU 8.4.28R* does not apply with respect to a *financial conglomerate* falling into (1).

- (3) If *PRU 8.4.28R* applies with respect to a *financial conglomerate* in accordance with (2) the peripheral members must be excluded from the calculations under *PRU 8.4.26R*.

- (4) If:

- (a) *PRU 8.4.26R* applies with respect to a *financial conglomerate* falling into (1) under *PRU 8.4.27R(2)* (Use of *Part IV permission* to apply Annex I of the *Financial Groups Directive*); or
- (b) *PRU 8.4.49R* (Capital adequacy requirements: Application of Methods 1, 2 or 3 from Annex I of the *Financial Groups Directive*) applies with respect to a *financial conglomerate* falling into (1);

then:

- (c) the treatment of the links in (1) (including the treatment of any *solvency deficit*) is as provided for in the *requirement* referred to in *PRU 8.4.30R*; and
  - (d) *PRU 8.4.26R* or *PRU 8.4.29R*, as the case may be, apply even if the *applicable sectoral rules* do not deal with how *undertakings* not linked by capital ties are to be dealt with for the purposes of consolidated supervision (or, in the case of the *insurance sector*, supplementary supervision).
- (5) Once *PRU 8.4.26R* applies to a *firm* with respect to a *financial conglomerate* of which it is a member under *PRU 8.4.27R(1)* (automatic application of Method 4 from Annex I of the *Financial Groups Directive* on satisfaction of the condition in *PRU 8.4.28R*), the disapplication of *PRU 8.4.28R* under (2) ceases to apply with respect to that *financial conglomerate*.

10 Table: PART 6: Definitions used in this Annex

Defining the financial sectors	6.1	<p>For the purposes of Parts 1 to 3 of this annex (but, unless specified otherwise in paragraph 4.4, not for the purposes of the definition of <i>most important financial sector</i>):</p> <ol style="list-style-type: none"> <li>(1) the <i>banking sector</i> and the <i>investment services sector</i> are considered separately;</li> <li>(2) if a <i>financial institution</i> could otherwise fall into both the <i>banking sector</i> and the <i>investment services sector</i>, it must be allocated to the <i>banking sector</i>;</li> <li>(3) an <i>asset management company</i> is allocated in accordance with PRU 8.4.39R; and</li> <li>(4) a <i>mixed financial holding company</i> must be treated as being a member of the <i>most important financial sector</i>.</li> </ol>
Solo capital resources requirement: UK domestic firms	6.2	<p>The <i>solo capital resources requirement</i> for a <i>regulated entity</i> that is a <i>UK domestic firm</i> is its solo regulatory capital requirement under the <i>FSA's sectoral rules</i> for its <i>financial sector</i> applicable to it.</p>
Solo capital resources requirement: EEA firms	6.3	<p>The <i>solo capital resources requirement</i> for an <i>EEA regulated entity</i> that is subject to the solo capital adequacy <i>sectoral rules</i> for its <i>financial sector</i> of the <i>competent authority</i> that authorised it is equal to the amount of capital resources it is obliged to hold under those <i>sectoral rules</i>.</p>
Solo capital resources requirement: mixed financial holding company	6.4	<p>The <i>solo capital resources requirement</i> for a <i>mixed financial holding company</i> is a notional capital requirement. It is the capital adequacy requirement that applies to <i>regulated entities</i> in the <i>most important financial sector</i> under the table in paragraph 6.8.</p>
Solo capital resources requirement: non-EEA firms subject to equivalent regimes	6.5	<p>The <i>solo capital resources requirement</i> for a <i>regulated entity</i> that:</p> <ol style="list-style-type: none"> <li>(1) does not fall into paragraphs 6.2 to 6.4;</li> <li>(2) is subject to any of the <i>sectoral rules</i> referred to in paragraph 6.6 applicable to its <i>financial sector</i>; and</li> <li>(3) is incorporated in and has its head office in: <ol style="list-style-type: none"> <li>(a) (where the <i>sectoral rules</i> in (2) are for the <i>banking sector</i> or the <i>investment services sector</i>) the same state</li> </ol> </li> </ol>

Solo capital resources requirement: other members		<p>or territory as the regulator for those <i>sectoral rules</i>, as referred to in paragraph 6.6(1) or 6.6(2)); or</p> <p>(b) (where the <i>sectoral rules</i> in (2) are for the <i>insurance sector</i>) the designated state or territory in question, as referred to in 6.6(3);</p>
	6.6	<p>is equal to the amount of capital resources it is obliged to hold under those <i>sectoral rules</i>. However, where 3(b) would otherwise apply, paragraph 6.7 may be applied instead.</p> <p>The <i>sectoral rules</i> referred to in paragraph 6.5 are:</p> <p>(1) (for the <i>banking sector</i>) the <i>sectoral rules</i> of or administered by one of the regulators listed in Appendix D of chapter CS of <i>IPRU(BANK)</i>;</p> <p>(2) (for the <i>investment services sector</i>) the <i>sectoral rules</i> of or administered by one of the regulators listed in Appendix 59 of chapter 10 of <i>IPRU(INV)</i>; and</p> <p>(3) (for the <i>insurance sector</i>) the <i>sectoral rules</i> of the states or territories referred to in the definition of designated states or territories in chapter 11 of <i>IPRU(INS)</i> (Definitions), but excluding <i>EEA States</i>.</p>
	6.7	<p>The <i>solo capital resources requirement</i> for any member of a <i>financial conglomerate</i> in the <i>overall financial sector</i> not treated under paragraphs 6.2 to 6.6 is a notional capital requirement. It is the capital resources requirement that would apply to it under the following <i>rules</i>:</p> <p>(1) (in the case of an <i>asset management company</i>) the <i>rules</i> in Chapter 7 of <i>IPRU(INV)</i>; and</p> <p>(2) (in any other case) the <i>rules</i> applicable to its <i>financial sector</i> under the table in paragraph 6.8.</p>

11 Table: Paragraph 6.8: The FSA's sectoral rules for the solo capital resources requirement

Financial sector	FSA's sectoral rules
<i>Banking sector</i>	The <i>FSA's sectoral rules</i> for <i>banks</i> , except that <i>e-money issuers</i> are subject to <i>ELM</i> .
<i>Insurance sector</i>	The <i>FSA's sectoral rules</i> for <i>insurance undertakings</i> .
<i>Investment services sector</i>	(1) The <i>rules</i> in <i>IPRU(INV)</i> that would apply on the assumptions in paragraph 4.3(2).  (2) (If (1) does not result in the application of any <i>rules</i> in <i>IPRU(INV)</i> ) the <i>rules</i> in <i>IPRU(INV)</i> that would be applied to it under <i>rule</i> 14.5.2 of Chapter 14 of <i>IPRU(INV)</i> (Group financial resources requirement).

12 Table

Solo capital resources requirement: the insurance sector	6.9	References to capital requirements in the provisions of <i>PRU</i> 8 Ann 1R defining <i>solo capital resources requirement</i> must be interpreted in accordance with paragraph 5.4(5).
Applicable sectoral consolidation rules	6.10	The <i>applicable sectoral consolidation rules</i> for a <i>financial sector</i> are the <i>FSA's sectoral rules</i> about capital adequacy and solvency on a consolidated basis that are applied in the table in paragraph 6.11.

13 Table: Paragraph 6.11: Application of sectoral consolidation rules

Financial sector	Type of financial conglomerate	FSA's sectoral rules
<i>Banking sector</i>	<i>Building society conglomerate</i>	The <i>rules</i> for <i>building societies</i> .
	Any other type	The <i>rules</i> for <i>banks</i> .
<i>Insurance sector</i>	N/A	The <i>rules</i> for <i>insurance undertakings</i> .
<i>Investment services sector</i>	N/A	The <i>rules</i> for <i>investment firms</i> .
Note 1: Paragraph 4.6 applies for the purposes of those <i>rules</i> .		

14 Table:

Applicable sectoral consolidation rules (contd.)	6.12	<p>The <i>rules</i> referred to in the third column of the table in paragraph 6.11 are as follows:</p> <ol style="list-style-type: none"> <li>(1) the <i>rules</i> for <i>building societies</i> are the ones for <i>building society conglomerates</i> listed in the table in paragraph 4.2;</li> <li>(2) the <i>rules</i> for <i>banks</i> are the ones for <i>banking conglomerates</i> listed in the table in paragraph 4.2 as adjusted under paragraph 4.7;</li> <li>(3) the <i>rules</i> for <i>insurance undertakings</i> are whichever of the ones for <i>insurance conglomerates</i> that are applied by the table in paragraph 4.2; and</li> <li>(4) the <i>rules</i> for <i>investment firms</i> are the ones for <i>investment services conglomerates</i> listed in the table in paragraph 4.2 as applied under paragraph 4.3 (How to apply chapter 14 of IPRU(INV)).</li> </ol>
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Prudential rules for third country groups (PRU 8.5.8R to PRU 8.5.9R)

1 Table: PART 1: Third-country financial conglomerates

1.1	This Part of this annex sets out the <i>rules</i> with which a <i>firm</i> must comply under <i>PRU 8.5.8R</i> with respect to a <i>financial conglomerate</i> of which it is a member.
1.2	A <i>firm</i> must comply, with respect to the <i>financial conglomerate</i> referred to in paragraph 1.1, with whichever of <i>PRU 8.4.26R</i> and <i>PRU 8.4.29R</i> is applied under paragraph 1.3.
1.3	For the purposes of paragraph 1.2: <ol style="list-style-type: none"> <li>(1) the <i>rule</i> in <i>PRU 8.4</i> that applies as referred to in paragraph 1.2 is the one that is specified by the <i>requirement</i> referred to in <i>PRU 8.5.8R</i>;</li> <li>(2) (where <i>PRU 8.4.29R</i> is applied) the definitions of <i>conglomerate capital resources</i> and <i>conglomerate capital resources requirement</i> that apply for the purposes of that <i>rule</i> are the ones from whichever of Part 1, Part 2 or Part 3 of <i>PRU 8 Ann 1R</i> is specified in that <i>requirement</i>; and</li> <li>(3) the <i>rules</i> so applied (including those in <i>PRU 8 Ann 1R</i>) are adjusted in accordance with paragraph 3.1.</li> </ol>
1.4	If the condition in Articles 7(4) and 8(4) of the <i>Financial Groups Directive</i> is satisfied (the <i>financial conglomerate</i> is headed by a <i>mixed financial holding company</i> ) with respect to the <i>financial conglomerate</i> referred to in paragraph 1.1 the <i>firm</i> must also comply with <i>PRU 8.4.35R</i> (as adjusted in accordance with paragraph 3.1) with respect to that <i>financial conglomerate</i> .
1.5	A <i>firm</i> must comply with the following with respect to the <i>financial conglomerate</i> referred to in paragraph 1.1: <ol style="list-style-type: none"> <li>(1) <i>PRU 8.1</i> (as it applies to <i>financial conglomerates</i> and as adjusted under paragraph 3.1); and</li> <li>(2) <i>PRU 8.4.25R</i>.</li> </ol>

2 Table: PART 2: Third-country banking and investment groups

2.1	This Part of this annex sets out the <i>rules</i> with which a <i>firm</i> must comply under <i>PRU 8.5.9R</i> with respect to a <i>third-country banking and investment group</i> of which it is a member.
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2.2	A <i>firm</i> must comply with one of the sets of <i>rules</i> specified in paragraph 2.3 as adjusted under paragraph 3.1 with respect to the <i>third-country banking and investment group</i> referred to in paragraph 2.1.
2.3	The <i>rules</i> referred to in paragraph 2.2 are as follows: <ul style="list-style-type: none"> <li>(1) the <i>applicable sectoral consolidation rules</i> in <i>IPRU(BANK)</i>; or</li> <li>(2) the <i>applicable sectoral consolidation rules</i> for the <i>investment services sector</i>; or</li> <li>(3) the <i>rules</i> in <i>ELM 7</i>.</li> </ul>
2.4	The set of <i>rules</i> from paragraph 2.3 that apply with respect to a particular <i>third-country banking and investment group</i> (as referred to in paragraph 2.1) are those that would apply if they were adjusted in accordance with paragraph 3.1.
2.5	The <i>sectoral rules</i> applied by Part 2 of this annex cover all prudential <i>rules</i> applying on a consolidated basis including those relating to large exposures.
2.6	A <i>firm</i> must comply with <i>PRU 8.1</i> (as it applies to <i>banking and investment groups</i> and as adjusted under paragraph 3.1) with respect to the <i>third-country banking and investment group</i> referred to in paragraph 2.1.

3 Table: PART 3: Adjustment of scope

3.1	The adjustments that must be carried out under this paragraph are that the scope of the <i>rules</i> referred in Part 1 or Part 2 of this annex, as the case may be, are amended: <ul style="list-style-type: none"> <li>(1) so as to remove any provisions disapplying those <i>rules</i> for <i>third-country groups</i>;</li> <li>(2) so as to remove all limitations relating to where a member of the <i>third-country group</i> is incorporated or has its head office; and</li> <li>(3) so that the scope covers every member of the <i>third-country group</i> that would have been included in the scope of those <i>rules</i> if those members had their head offices in, and were incorporated in, an <i>EEA State</i>.</li> </ul>
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**PRU 8 Ann 3G: CLASSIFICATION OF GROUPS (PRU 8.4.3G)**

(form ref)

**Part 1 : General Information**

<b>A</b>	Name of Group:	
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<b>B</b>	Name of FSA supervisor:	
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<b>C</b>	Name of entity at head of the group:	
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<b>D</b>	Type of entity at head of the group:	<b>D1</b>	EU regulated entity country of authorisation	
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(select one of D1, D2, D3 and D4)

<b>(a)</b>	Credit institution	<input type="checkbox"/>
<b>(b)</b>	Investment firm	<input type="checkbox"/>
<b>(c)</b>	Insurance firm	<input type="checkbox"/>

(tick one)

<b>D2</b>	EU non-regulated entity country of location	
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<b>D3</b>	Non-EU regulated entity country of authorisation	
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<b>D4</b>	Non- EU non-regulated entity country of location	
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<b>E</b>	Year-end for group consolidation purposes	
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## Part 2 : Threshold Information

F1	Is at least one of the entities in the group within the insurance sector and at least one in the banking/investment sector?	<input type="checkbox"/> Yes	<input type="checkbox"/> No (go to part 3)
F2	For D2 & D4 groups only: enter the ratio of the balance sheet total of the financial sectors in the group to the balance sheet total of the group as a whole. <i>Enter percentage in box*.</i>	<input type="text"/>	%
F3	What is the smallest financial sector?	<input type="checkbox"/>	Insurance
		<input type="checkbox"/>	Banking/Investment
F4	Ratio of balance sheet total of smallest financial sector to the balance sheet total of the financial sector entities in the group. <i>Enter percentage in box*.</i>	<input type="text"/>	%
F5	Ratio of the solvency requirement of the smallest financial sector to the solvency requirements of the total financial sector entities in the group. <i>Enter percentage in box*.</i>	<input type="text"/>	%
F6	What is the balance sheet total of the smallest financial sector in the group (identified in F3)*?	<input type="text"/>	(€'m)

\*see guidance notes on a recommended method of calculation

**Part 3: Conclusion on reason for becoming a financial conglomerate**

**G** Select **ONE** of the following based on the answers in section 1 & 2.

**If answer to F1 is NO or if none of the following are met then select type Z:**

<b>Z</b>		Not a conglomerate.
----------	--	---------------------

If the group is category D1 or D3 and the average of F4 and F5 is greater than 10% then select type i.

<b>i</b>		Conglomerate headed by a regulated institution with significant cross sector activities. [article 3(2)]
----------	--	---

If the group is category D1 or D3 and the average of F4 and F5 is less than 10% but F6 is greater than €6bn then select ii.

<b>ii</b>		Possible conglomerate headed by a regulated institution with presumed significant cross sector activities. [article 3(3)]
-----------	--	---

If the group is category D2 or D4 and the answer to F2 is greater than 40% AND the average of F4 and F5 is greater than 10% then select type iii.

<b>iii</b>		Conglomerate headed by non-regulated entity with significant cross sector activities. [article 3(1) & 3(2)]
------------	--	---

If the group is category D2 or D4 and the answer to F2 is greater than 40% AND the average of F4 and F5 is less than 10% but F6 is greater than €6bn then select type iv.

<b>iv</b>		Possible conglomerate headed by non-regulated entity with presumed significant cross sector activities. [article 3(1) & 3(3)]
-----------	--	---

**Part 4: Other relevant information**

H1	<p>Who do you think are the relevant competent authorities for your group (i.e. supervisors in EEA States in which the group has significant regulated activity)?</p> <p>See article 2 (17)(a) for definition of relevant competent authorities.</p>	
H2	<p>Who do you think should be the likely coordinator for the group (i.e. EEA supervisor of the group's most important regulated activity in the EU)?</p> <p>See article 10(1) and 10(2).</p>	
H3	<p>Do you consider that balance sheet value and solvency requirements were an appropriate criterion to determine whether a group is financial and whether cross sector activities exist? If not, do you consider there are other parameters (as referred to in article 3(5)) that would be more appropriate?</p>	
H4	<p>Do you have any other relevant comments? (use continuation sheet if necessary)</p>	

## **PRU 8 Ann 3G: Guidance Notes for Classification of Groups**

### **Purpose and scope**

The form is designed to identify groups and sub-groups that are likely to be financial conglomerates under the Financial Groups Directive. A group may be a financial conglomerate if it contains both insurance and banking/investment businesses and meets certain threshold tests. The FSA needs to identify conglomerates with their head offices in the EEA and those with their head offices outside the EEA, although this does not necessarily mean that the latter will be subject to EEA conglomerate supervision.

This form's purpose is to enable the FSA to obtain sufficient information so as to be able to determine how likely a group/sub-group is to be a financial conglomerate. In certain cases this can only be determined after consultation with the other EU relevant competent authorities. A second purpose of the form is therefore to identify any groups and sub-groups that may need such consultation so that this can be made as soon as possible. This should allow firms time to prepare to comply.

The third purpose of the form is to gain information from firms on the most efficient way to implement the threshold calculations in detail (consistently with the directive). We have, therefore, asked for some additional information in part 4 of the form.

A copy of this form will can be found on the FSA's Financial Groups Website with current contact details.

Please include workings showing the method employed to determine the percentages in part 2 (for the threshold conditions) and giving details of all important assumptions / approximations made in doing the calculations.

The definition of financial conglomerate includes not only conventional groups made up of parent-subsidiary relationships but groups linked by control and "consolidation Article 12(1) relationships". If this is the case for your group, please submit along with this form a statement that this is the case. Please include in that statement an explanation of how you have included group members not linked by capital ties in the questionnaire calculations.

A consolidation Article 12(1) relationship arises between undertakings in the circumstances set out in Article 12(1) of the Seventh Company Law Directive. These are set out in the Handbook Glossary (in the definition of consolidation Article 12(1) relationship). Broadly speaking, undertakings come within this definition if they do not form a conventional group but:

- (a) are managed on a unified basis; or
- (b) have common management.

## *General guidance*

We would like this to be completed based on the most senior parent in the group, and, if applicable, for the company heading the most senior conglomerate group in the EEA. If appropriate, please also attach a list of all other likely conglomerate sub-groups.

Please use the most recent accounts for the top level company in the group together with the corresponding accounts for all subsidiaries and participations that are included in the consolidated accounts. Please indicate the names of any significant subsidiaries with a different year-end from the group's year-end.

Please note the following:

- (a) Branches should be included as part of the parent entity.
- (b) Include in the calculations overseas entities owned by the relevant group or sub-group.
- (c) There are only two sectors for this purpose: banking/investment and insurance.
- (d) You will need to assign non-regulated financial entities to one of these sectors:
  - **banking/investment** activities are listed in - IPRU Banks CS 10 Appendix A
  - **insurance** activities are listed in - IPRU Insurers Annex 11.1 and 11.2 p 163-168.
  - Any **operator of a UCITS scheme, insurance intermediary, mortgage broker and mixed financial holding company** does not fall into the directive definitions of either financial sector or insurance sector. They should therefore be ignored for the purposes of these calculations.

## Threshold tests

For the purpose of completing section 2 of the form relating to the threshold tests, the following guidance should be used. However, if you consider that for your group there is a more appropriate calculation then you may use this calculation so long as the method of computation is submitted with the form.

## Calculating balance sheet totals

Generally, use total (gross) assets for the balance sheet total of a group/entity. However, investments in other entities that are part of the group will need to be deducted from the sector that has made the investment and the balance sheet total of the entity is added to the sector in which it operates.

Our expectation of how this may be achieved efficiently is as follows:

- (i) Off-balance-sheet items should be excluded.
- (ii) Where off-balance sheet treatment of **funds under management** and on-balance sheet treatment of **policy holders' funds** may distort the threshold calculation, groups should consult the FSA on the appropriateness of using other measures under article 3.5 of the Financial Groups Directive.
- (iii) If consolidated accounts exist for a sub-group consisting of financial entities from only one of the two sectors, these consolidated accounts should be used to measure the balance-sheet total of the sub-group (i.e. total assets less investments in entities in the other sector). If consolidated accounts do not exist, intra-group balances should be netted out when calculating the balance sheet total of a single sector (but cross-sector intra-group balances should not be netted out).
- (iv) Where consolidated accounts are used, minority interests should be excluded and goodwill should be included.
- (v) Where accounting standards differ between entities, groups should consult the FSA if they believe this is likely materially to affect the threshold calculation.
- (vi) Where there is a subsidiary or participation in the opposite sector from its parent (i.e. insurance sector for a banking/investment firm parent and vice versa), the balance sheet amount of the subsidiary or participation should be allocated to its sector using its individual accounts.
- (vii) The balance-sheet total of the parent entity/sub-group is measured as total assets of the parent/sub-group less the book value of its subsidiaries or participations in the other sector (i.e. the value of the subsidiary or participation in the parent's consolidated accounts is deducted from the parent's consolidated assets).
- (viii) The cross-sector subsidiaries or participations referred to above, valued according to their own accounts, are allocated pro-rata, according to the aggregated share owned by the parent/sub-group, to their own sector.

- (ix) If the cross-sector entities above themselves own group entities in the first sector (i.e. that of the top parent/sub-group) these should (in accordance with the methods above) be excluded from the second sector and added to the first sector using individual accounts.

#### Solvency (capital adequacy) requirements

Generally, the solvency requirements should be according to sectoral rules (that is EEA prudential sectoral legislation – see Glossary). However, for convenience, you may choose to use either EEA rules, FSA rules or local rules. But if this choice makes a significant difference, either with respect to whether the group is a financial conglomerate or with respect to which sector is the biggest, you should consult with the FSA. Non-regulated financial entities should have proxy requirements calculated on the basis of the most appropriate sector. If sub-groups submit single sector consolidated returns then the solvency requirement may be taken from those returns.

Our expectation of how this may be achieved efficiently is as follows:

- (i) If you complete a solvency return for a sub-group consisting of financial entities from only one of the two sectors, the total solvency requirement for the sub-group should be used.
- (ii) Solvency requirements taken must include any deductions from available capital so as to allow the appropriate aggregation of requirements.
- (iii) Where there is a regulated subsidiary or participation in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be from its individual regulatory return. If there is an identifiable contribution to the parent's solvency requirement in respect of the cross-sector subsidiary or participation, the parent's solvency requirement may be adjusted to exclude this.
- (iv) Where there is an unregulated financial undertaking in the opposite sector from its parent/sub-group, the solvency requirement of the subsidiary or participation should be one of the following:
  - (a) as if the entity were regulated by the FSA under the appropriate sectoral rules;
  - (b) using EU minimum requirements for the appropriate sector; or
  - (c) using non-EU local requirements\* for the appropriate sector.

Please note on the form which of these options you have used, according to the country and sector, and whether this is the same treatment as in your latest overall group solvency calculation.

(v) For banking/investment requirements, use the total amount of capital required.

(vi) For insurance requirements, use the Required Minimum Margin:

(a) UK firms, Form 9: for general insurance business = capital resources requirement [line 29]; for long-term insurance business = capital resources requirement (higher of Minimum Capital Requirement and Enhanced Capital Resources Requirement) [line 52].

(b) Overseas firms, either:

- the local requirement\*;
- the EU minimum; or
- the FSA requirement.

\* N.B. local requirements may only be used if they are at least equivalent to the EU minimum (designated states or territories). However, local requirements of a non-designated state or territory may be used if the resulting ratio in F5 is significantly below the 10% threshold (for this purpose "significantly below" may be taken to mean <5%).

### Market share measures

These are not defined by the directive. The aim is to identify any standard industry approaches to measuring market share in individual EU countries by sector, or any data sources which are commonly used as a proxy.

### Threshold tests

#### *Test F2*

**B/S of banking/investment + insurance sector = result %**  
**B/S total**

#### *Test F3/F4/F5*

**B/S of insurance sector**  
**B/S of banking/investment sector + insurance sector = A%**



**B/S of banking/investment sector**

**B/S of banking/investment sector + insurance sector = B%**

**Solvency requirement of insurance sector**

Solvency requirement of banking/investment sector + insurance sector = C%

**Solvency requirement of banking/investment sector**

Solvency requirement of banking/investment sector + insurance sector = D%

The relevant percentage for the insurance sector is:

$$(A\% + C\%)/2 = I\%$$

The relevant percentage for the banking/investment sector is:

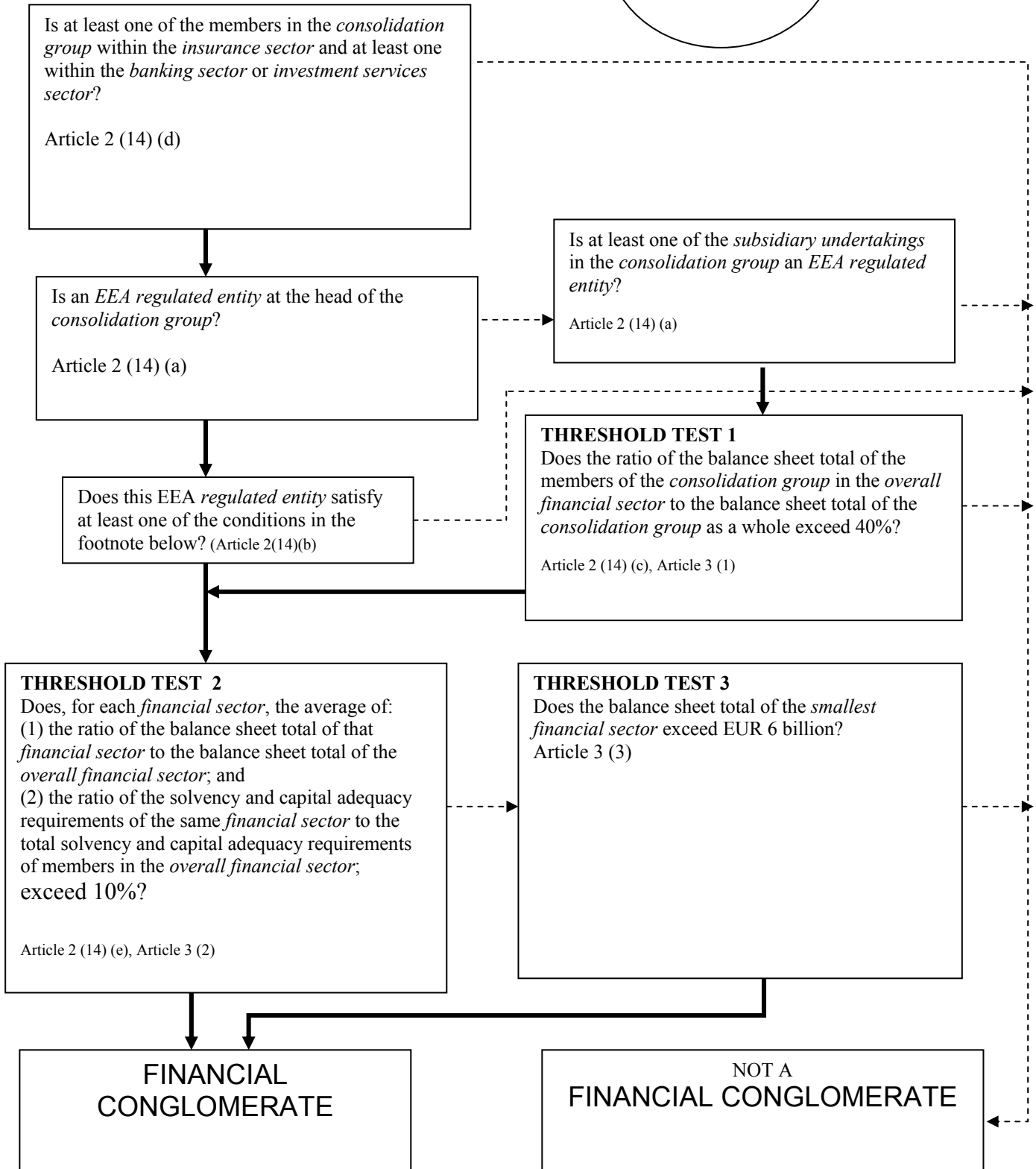
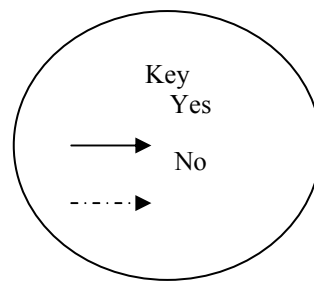
$$(B\% + D\%)/2 = BI\%$$

The smallest sector is the sector with the smallest relevant percentage.

**If  $I\% < BI\%$  then F3 is insurance, F4 = A%, and F5 = C%**

**If  $BI\% < I\%$  then F3 is banking/investment, F4 = B% and F5 = D%**

**PRU 8 Ann 4R (see PRU 8.4.5R)**



Footnote: The conditions are that the EEA regulated entity at the head of the consolidation group: (1) is a parent undertaking of a member of the consolidation group in the overall financial sector; (2) has a participation in a member of the consolidation group that is in the overall financial sector; or (3) has a consolidation Article 12(1) relationship with a member of the consolidation group that is in the overall financial sector.

Insert schedules into PRU as follows:

# The Integrated Prudential Sourcebook

## Schedule 1

### Record Keeping Requirements

G

1 There are no record keeping requirements in *PRU 1* or *PRU 8*. This Schedule does not cover any other chapter of *PRU*.

# The Integrated Prudential Sourcebook

## Schedule 2

### Notification requirements

#### G

- 1 There are no notification requirements in *PRU* 1 or *PRU* 8. This Schedule does not cover any other chapter of *PRU*.

# The Integrated Prudential Sourcebook

## Schedule 3

### Fees and other required payments

#### G

- 1 There are no requirements for fees or other payments in *PRU 1* or *PRU 8*. This Schedule does not cover any other chapter of *PRU*.

# The Integrated Prudential Sourcebook

## Schedule 4

### Powers Exercised

#### G

- 1 The following powers and related provision in the *Act* have been exercised by the *FSA* to make the *rules* in *PRU 1* and *PRU 8*:
  - (1) section 138 (General rule -making power)
  - (2) section 150(2) (Actions for damages)
  - (3) section 156 (General Supplementary powers).
- 2 The following power in the *Act* has been exercised by the *FSA* to give the *guidance* in *PRU 1* and *PRU 8*:

Section 157(1) (Guidance).
- 3 This Schedule does not cover any other chapter of *PRU*.

# The Integrated Prudential Sourcebook

## Schedule 5

### Rights of action for damages

G

- 1 The table below sets out the rules in *PRU* contravention of which by an *authorised person* may be actionable under section 150 of the *Act* (Actions for damages) by a person who suffers loss as a result of the contravention.
- 2 If a "Yes" appears in the column headed "For private person", the *rule* may be actionable by a *private person* under section 150 (or, in certain circumstances, his fiduciary or representative; see article 6(2) and (3)(c) of the Financial Services and Markets Act 2000 (Rights of Action) Regulations 2001 (SI 2001 No 2256)). A "Yes" in the column headed "Removed" indicates that the *FSA* has removed the right of action under section 150(2) of the *Act*. If so, a reference to the *rule* in which it is removed is also given.
- 3 The column headed "For other person" indicates whether the *rule* may be actionable by a person other than a *private person* (or his fiduciary or representative) under article 6(2) and (3) of those Regulations. If so, an indication of the type of person by whom the *rule* may be actionable is given.
- 4 Table

Chapter/Appendix	Section/Annex	Rights of action under section 150			
		For private person	Removed	For other person	
All <i>rules</i> in <i>PRU</i>		No	Yes ( <i>PRU</i> 1.8.1R)	No	

# The Integrated Prudential Sourcebook

## Schedule 6

### Rules that can be waived

#### G

- 1 The *rules* in *PRU 8* can be waived by the *FSA* under section 148 of the *Act* (Modification or waiver of rules). This Schedule does not cover any other chapter of *PRU*.



## Annex H

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text.

Connected persons

3.9.22 G (1) ...

- (1A) The *Financial Groups Directive Regulations* make special provision where the *FSA* is exercising its functions under Part IV of the *Act* (Permission to carry on regulated activities) for the purposes of carrying on supplementary supervision. Broadly, where the *FSA*, in the course of carrying on supplementary supervision, is considering varying the *Part IV permission* of a *person* who is a member of a group which is a *financial conglomerate*, the consultation provisions in section 49(2) of the *Act* are disapplied. In their place, the regulations impose special obligations, linked to the *Financial Groups Directive*, to obtain the consent of the relevant *competent authorities*, to consult those authorities and to consult with the group itself.

## Annex I

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

3.9.5 R Table Auditor's report

...

whether in the auditor's opinion:	
(14)	... if the <i>firm</i> prepares a consolidated <del>reporting statement</del> <u>supervision return</u> at its <i>accounting reference date</i> , that it has been prepared in accordance with the <i>rules</i> .

...

When will the FSA grant an application for variation of permission?

...

6.3.31 G In considering whether to grant a *firm's* application to vary its *Part IV permission*, the *FSA* will also have regard, under section 49(1) of the *Act* (Persons connected with an applicant), to any ~~person~~ person appearing to be, or likely to be, in a relationship with the *firm* which is relevant (see *AUTH 3.9.22G* to *AUTH 3.9.24G* (Connected persons)). The *Financial Groups Directive Regulations* make special consultation provisions where the *FSA* is exercising its functions under Part IV of the *Act* (Permission to carry on regulated activities) for the purposes of carrying on supplementary supervision – see *AUTH 3.9.22G(1A)*.

...

7.3: Criteria for varying a firm's permission

...

7.3.2 G The *FSA* may seek to vary a *firm's Part IV permission* on its own initiative in certain situations, including the following:

...

(4) If a *firm* is a member of a *financial conglomerate* and the *FSA* is implementing supplementary supervision under the *Financial Groups Directive* with respect to that *financial conglomerate* by imposing obligations on the *firm*. Further material on this can be found in *PRU 8.4* (Cross sector groups) and *SUP 16.7.73R* to *SUP*

16.7.74R (reporting requirements with respect to *financial conglomerates*).

...

8.9: Decision making

...

8.9.2 G If the FSA, in the course of carrying on supplementary supervision of a *financial conglomerate*, is considering exercising its powers under section 148 of the *Act* (Modification or waiver of rules), regulation 4 of the *Financial Groups Directive Regulations* contains special provisions. The FSA must, in broad terms, do two things. Where required by those regulations, it must obtain the consent of the relevant competent authorities of the group. And, where required by those Regulations, it must consult those competent authorities.

...

11.5: Form of notification by firms

...

11.5.4A G *Firms* are also reminded that a change in *control* may give rise to a notification as a *financial conglomerate* or a change in the supplementary supervision of a *financial conglomerate* (see PRU 8.4 (Cross sector groups) and PRU 8.5 (Third country groups)).

...

The FSA's timeframe for responding to a notification

...

11.7.13 G Before giving an approval notice or *warning notice*, the FSA ~~may be required to consult with~~ must comply with certain requirements as to consultation with competent authorities outside the *United Kingdom* (sections 183(2) and 188(2) of the *Act* and the *Financial Services and Markets Act 2000 (Consultation with Competent Authorities) Regulations 2001*). The *Financial Groups Directive Regulations* make special provision in relation to (the change in *control* over a UK authorised person (within the meaning of section 178(4) of the *Act*) which is a member of a *third country group*.

...

After SUP 15.8.7G insert the following new section SUP 15.9:

15.9 Notifications by members of financial conglomerates

15.9.1 R A *firm* that is a *regulated entity* must notify the FSA immediately it becomes aware that any *consolidation group* of which it is a member:

- (1) is a *financial conglomerate*; or
- (2) has ceased to be a *financial conglomerate*.

- 15.9.2 R (1) A *firm* that is a *regulated entity* must establish whether or not any *consolidation group* of which it is a member:
- (a) is a *financial conglomerate*; or
  - (b) has ceased to be a *financial conglomerate*;
- if:
- (c) the *firm* believes; or
  - (d) a reasonable *firm* that is complying with the requirements of the *regulatory system* would believe; that it is likely that (a) or (b) is true.
- (2) A *firm* does not need to determine whether (1)(a) is the case if the *consolidation group* is already being regulated as a *financial conglomerate*.
- (3) A *firm* does not need to determine whether (1)(b) is the case if notification has already been given as contemplated by SUP 15.9.4R
- 15.9.3 G A *firm* should consider the requirements in SUP 15.9.2R on a continuing basis, and in particular, when the *group* prepares its financial statements and on the occurrence of an event affecting the *consolidated group*. Such events include, but are not limited to, an acquisition, merger or sale.
- 15.9.4 R A *firm* does not have to give notice to the *FSA* under SUP 15.9.1R if it or another member of the *consolidation group* has already given notice of the relevant fact to:
- (1) the *FSA*; or
  - (2) (if another *competent authority* is *co-ordinator* of the *financial conglomerate*) that *competent authority*; or
  - (3) (in the case of a *financial conglomerate* that does not yet have a *co-ordinator*) the *competent authority* who would be *co-ordinator* under Article 10(2) of the *Financial Groups Directive* (Competent authority responsible for exercising supplementary supervision (the *co-ordinator*)).

...

#### Reports from groups

- 16.3.25 G If this chapter requires the submission of a report covering a *group*, a single report may be submitted, and so satisfy the requirements of all *firms* in the *group*. Such a report should contain the information required from all of them, meet all relevant due dates and indicate all the *firms* on whose behalf it is submitted; if necessary a separate covering sheet should list the *firms* on whose behalf a report is submitted. Nevertheless, the requirement to provide a report, and the responsibility for the report, remains with each *firm* in the *group*. However, reporting requirements that apply to a *firm*, by reason of the *firm* being a member of a *financial conglomerate*, are imposed on only one member of the *financial conglomerate* (see, for example, SUP 16.7.73R).

...

16.4.5 R Reporting requirement

(4) ...

(4A) A firm that is a regulated entity must include in its report to the FSA under (1) whether any consolidation group of which it is a member is a third-country banking and investment group.

(4B) A firm does not have to give notice to the FSA under (4A) if it, or another member of the third-country banking and investment group, has already given notice to the FSA of the relevant fact.

(5) ...

...

16.7.5 G Applicable rules and guidance on financial reports (see SUP 16.7.1G)

Firm category	Applicable rules and guidance
<i>Bank, other than an EEA bank with permission for cross border services only</i>	<i>SUP 16.7.7R - SUP 16.7.15R</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
<i>Building society</i>	<i>SUP 16.7.16R - SUP 16.7.19R</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
...	
<i>Securities and futures firm (Note 1)</i>	<i>SUP 16.7.22R - SUP 16.7.34G</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
<i>Investment management firm</i>	<i>SUP 16.7.35R - SUP 16.7.41R</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
<i>Personal investment firm</i>	<i>SUP 16.7.42G - SUP 16.7.53G</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
...	
<i>ELMI</i>	<i>SUP 16.7.64R - SUP 16.7.66R</i> <i><u>SUP 16.7.73R - SUP 16.7.74R</u></i>
...	

...

16.7.8 R Financial reports from a UK bank (see SUP 16.7.7R)

Content of Report	Form (Note 1)	Frequency	Due date
...			
Analysis of large exposures (Consolidated)	LE2 or LE3 (Note 2) (Note 7)	Quarterly	20 <i>business days</i> after quarter end (Note 6) (24 <i>business days</i> if LE3 is submitted electronically)
<u>Analysis of significant transactions (other than those resulting in large exposures) with the mixed-activity holding company and its subsidiaries</u>	<u>LE2 or LE3 (Note 8)</u>	<u>Quarterly</u>	<u>20 business days after quarter end (Note 6) (24 business days if LE3 is submitted electronically)</u>
...			
<p>...</p> <p><u>Note 8 = A bank must add the required information to the relevant large exposures reporting form (LE2 or LE3). For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the group.</u></p>			

...

16.7.25 R Financial reports required from a securities and futures firm which is a category A or B firm or a broad scope firm (see SUP 16.7.24R)

Report	Frequency	Due date
.....		
<del>Consolidated supervision return reporting statement</del> (Note 2)	Half-yearly	<del>1 month after period end</del>  <u>3 months after end of the relevant six-month period</u>

Report	Frequency	Due date
...		
Large exposures quarterly reporting statement (Form LEM 1 or LEM 2) – consolidated (Notes 2 and 4)	Quarterly	1 month after quarter end
<u>(Only for CAD investment firms) Analysis of significant transactions (other than those resulting in large exposures) with the mixed-activity holding company and its subsidiaries (Note 5).</u>	<u>Quarterly</u>	<u>1 month after quarter end</u>
<u>If the firm's ultimate parent is a mixed-activity holding company, the annual accounts of the mixed-activity holding company (Note 2)</u>	<u>Annually</u>	<u>As soon as available after year end</u>
<p>....</p> <p>Note 2 = Only for category A and B firms which are subject to the consolidation rules set out in IPRU (INV) Chapter 14 <del>10-200R–10-203R</del>, and are not exempt from the consolidation rules under IPRU (INV) <del>10-200R(2) or IPRU (INV) 10-204R</del>.</p>		
<p>...</p> <p><u>Note 5 = Securities and futures firms that are CAD investment firms must add the required information to the large exposures reporting form (QFS1). For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the group.</u></p>		

...

- 16.7.27 R Financial reports from a securities and futures firm which is a category C or D firm or an arranger or venture capital firm (see SUP 16.7.26R)

Report	Frequency	Due date
...		

Report	Frequency	Due date
Consolidated <u>supervision return reporting statement</u> (Note 2)	Half yearly	<del>1 month after period end</del>  <u>3 months after end of relevant six-month period</u>
...		
Large exposures quarterly reporting (Form LEM 1 or LEM 2) - consolidated (Notes 2 and 4)	Quarterly	1 month after quarter end
<u>(Only for CAD investment firms) Analysis of significant transactions (other than those resulting in large exposures) with the mixed-activity holding company and its subsidiaries</u> (Note 5)	<u>Quarterly</u>	<u>1 month after quarter end</u>
<u>If the firm's ultimate parent is a mixed-activity holding company, the annual accounts of the mixed-activity holding company</u> (Note 2)	<u>Annually</u>	<u>As soon as available after year end</u>
...		
<p>...</p> <p>Note 2 = Only for category C firms (as defined in the glossaries located in IPRU(INV) 10), which are subject to the consolidation rules set out in <del>IPRU(INV) 10-200R—10-203R</del> Chapter 14, and are not exempt from the consolidation rules under <del>IPRU(INV) 10-200R(2) or IPRU(INV) 10-204R</del>.</p> <p>...</p> <p><u>Note 5 = Securities and futures firms that are CAD investment firms must add the required information to their large exposures reporting. For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the group.</u></p>		

...

- 16.7.31 R A securities and futures firm must submit the reports in SUP 16.7.25R and SUP 16.7.27R in accordance with, and in the same format as:
- (1) the forms contained in SUP 16 Ann 10R, and as required by section 6 of that annex; and
  - (2) the form contained in SUP 16 Ann 20R, and having regard to SUP 16 Ann 21G.



...

16.7.36 R Table Financial reports from an investment management firm (see SUP 16.7.35R)

Report	Frequency	Due date
Annual Financial Return (Note 1)	Annually	4 months after the <i>firm's accounting reference date</i>
<u>(Only for CAD investment firms) Analysis of significant transactions (other than those resulting in large exposures) with the mixed-activity holding company and its subsidiaries. (Note 6)</u>	Annually	<u>4 months after the firm's accounting reference date</u>
<u>Consolidated supervision return (only for firms subject to IPRU(INV) Chapter 14)</u>	Half-yearly	<u>4 months after end of relevant six-month period</u>
<u>If the firm's ultimate parent is a mixed-activity holding company, the annual accounts of the mixed-activity holding company.</u>	Annually	<u>As soon as available after year end</u>
...		
<p>...</p> <p><u>Note 6 = Investment management firms that are CAD investment firms must add the required information to their large exposure reporting in the Annual Financial Return. For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the group.</u></p>		

...

16.7.38 R An investment management firm must submit the required reports in SUP 16.7.36R in accordance with, and in the same format as; :

- (1) the forms contained in SUP 16 Ann 5R, and according to the requirements contained in as required by section 4 of that annex; and
- (2) the forms contained in SUP 16 Ann 20R, and having regard to SUP 16 Ann 21G.

...

16.7.47 R Additional financial reports required from a Category A1, A2 or A3

firm (see SUP 16.7.46R)

Report	Frequency	Due date
...		
Consolidated <u>supervision financial resources return</u> (Note 1)	<u>Quarterly</u> <u>Half-yearly</u>	<del>3 weeks after</del> <u>quarter end</u>  <u>4 months after end of relevant six-month period</u>
<u>If the firm's ultimate parent is a mixed-activity holding company, the annual accounts of the mixed-activity holding company</u>	<u>Annually</u>	<u>As soon as available after year end</u>
...		
Form 13I (Consolidated statement of large exposures) (Note 1)	Quarterly	3 weeks after quarter end
<u>(Only for CAD investment firms) Analysis of significant transactions (other than those resulting in large exposures) with the mixed-activity holding company and its subsidiaries</u> (Note 3)	<u>Quarterly</u>	<u>3 weeks after quarter end</u>
...		
<p>Note 1 = This report is only required from a <i>firm</i> if it is a member of a <i>group</i>, and it is subject to consolidated supervision as set out in <i>IPRU(INV)</i> 13.7.1R to 13.7.2R-Chapter 14.</p> <p>...</p> <p>Note 3 = <u>Personal investment firms that are CAD investment firms must add the required information to the large exposure reporting in Form 13I. For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the group.</u></p>		

...

- 16.7.51 R (1) A Category A1, A2 or A3 *firm* must submit the reports in SUP 16.7.45R and SUP 16.7.47R in accordance with, and in the same format as:
- (a) the forms contained in SUP 16 Ann 7R (sections 1, 3 and 6), and as required by section 5 of that annex; and
  - (b) the forms contained in SUP 16 Ann 20R, and having regard to SUP 16 Ann 21G.

...

- 16.7.52 G ~~Guidance notes for the completion of reports for the purposes of consolidated supervision, and of the annual questionnaire required under SUP 16.7.48R can be found in SUP 16 Ann 8G.~~

...

- 16.7.66 R Financial reports from an ELMI (see SUP 16.7.65R)

Content of Report	Form (Note 1)	Frequency	Due Date
...			
Consolidated large exposures reporting statement	ELM-CA/LE	Half-yearly	20 <i>business days</i> after period end (22 <i>business days</i> if submitted electronically)
<u>Analysis of significant transactions (other than those resulting in large exposures) with the <i>mixed-activity holding company</i> and its <i>subsidiaries</i></u>	<u>ELM-CA/LE</u> (Note 2)	<u>Half-yearly</u>	<u>20 <i>business days</i> after period end (22 <i>business days</i> if submitted electronically)</u>
...			
<p>...</p> <p><u>Note 2 = <i>ELMIs</i> must add the required information to the large exposures reporting form (QFS1). For the purposes of this reporting requirement, a transaction will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the <i>group</i>.</u></p>			

...

- 16.7.68R Table: Financial reports from a UCITS management company

Report	Frequency	Due date
--------	-----------	----------

...		
<u>Consolidated supervision return (Only for UCITS investment firms)</u>	<u>Half-yearly</u>	<u>4 months after end of relevant six-month period</u>
<u>If the firm's ultimate parent is a mixed-activity holding company, the annual accounts of the mixed- activity holding company (Only for UCITS investment firms)</u>	<u>Annually</u>	<u>As soon as available after year-end</u>
...		

- 16.7.69R A UCITS management company must submit the ~~required~~ reports in SUP 16.7.68R in accordance with, and in the same format as:
- (1) the forms contained in SUP 16 Ann 16R, and ~~according to the requirements contained in~~ as required by section 3 of that annex; and
  - (2) the form contained in SUP 16 Ann 20R, and having regard to SUP 16 Ann 21G.

...

After SUP 16.7.72R, insert the following new rules, SUP 16.7.73R and SUP 16.7.74R:

#### Financial conglomerates

- 16.7.73 R (1) A *firm* that is a member of a *financial conglomerate* must submit financial reports to the *FSA* in accordance with the table in SUP 16.7.74R if:
- (a) it is at the head of an *FSA regulated EEA financial conglomerate*; or
  - (b) its *Part IV permission* contains a relevant *requirement*.
- (2) In (1)(b), a relevant *requirement* is one which:
- (a) applies SUP 16.7.74R to the *firm*; or
  - (b) applies SUP 16.7.74R to the *firm* unless the *mixed financial holding company* of the *financial conglomerate* to which the *firm* belongs submits the report required under this *rule* (as if the *rule* applied to it).

- 16.7.74 R Table Financial reports from a member of a financial conglomerate (see SUP 16.7.73R)

Content of Report	Form (Note 1)	Frequency	Due Date
Calculation of supplementary capital adequacy requirements in accordance with one of the four technical calculation methods	Note 2	Note 5	Note 5
Identification of significant <i>risk concentration</i> levels	Note 3	Yearly	4 months after year end
Identification of significant <i>intra-group transactions</i>	Note 4	Yearly	4 months after year end
Report on compliance with <i>PRU</i> 8.4.35R where it applies	Note 6	Note 5	Note 5

Note 1 = When giving the report required, a *firm* must use the form indicated, if any.

Note 2 = If Part 1 of *PRU* 8 Annex 1 (method 1), Part 2 of *PRU* 8 Annex 1 (method 2), or Part 3 of *PRU* 8 Annex 1 (method 3) applies, there is no specific form. Adequate information must be provided, and each *financial conglomerate* for which the *FSA* is the *co-ordinator* must discuss with the *FSA* how to do this.

If Part 4 of *PRU* 8 Annex 1 applies (method 4):

- (1) a *banking conglomerate* must use form *SUP* 16 Ann 1R (BSD3);
- (2) a *building society conglomerate* must use form *SUP* 16 Ann 3R (MFS1 Tables D&F);
- (3) an *investment services conglomerate* must use form *SUP* 16 Ann 20R;
- (4) an *insurance conglomerate* must use the Parent Undertaking Reporting Format example in GN 10.1 of *IPRU(INS)*.

Note 3 = Rather than specifying a standard format for each *financial conglomerate* to use, each *financial conglomerate* for which the *FSA* is the *co-ordinator* must discuss with the *FSA* the form of the information to be reported. This should mean that usual information management systems of the *financial conglomerate* can be used to the extent possible to generate and analyse the information required.

When reviewing the *risk concentration* levels, the *FSA* will in particular monitor the possible risk of contagion in the *financial conglomerate*, the risk of a conflict of interests, the risk of circumvention of sectoral *rules*, and the level or volume of risks.

Note 4 = For the purposes of this reporting requirement, an *intra-group transaction* will be presumed to be significant if its amount exceeds 5% of the total amount of capital adequacy requirements at the level of the *financial conglomerate*.

Rather than specifying a standard format for each *financial conglomerate* to use,

each *financial conglomerate* for which the *FSA* is the *co-ordinator* will need to discuss with the *FSA* the form of the information to be reported. This should mean that usual information management systems of the *financial conglomerate* can be used to the extent possible to generate and analyse the information required.

When reviewing the *intra-group transactions*, the *FSA* will in particular monitor the possible risk of contagion in the *financial conglomerate*, the risk of a conflict of interests, the risk of circumvention of *sectoral rules*, and the level or volume of risks.

Note 5 = The frequency and due date will be as follows:

1. *banking conglomerate*: frequency is half-yearly with due date 20 *business days* after period end (24 *business days* if submitted electronically);
2. *building society conglomerate*: frequency is quarterly with due date seven *business days* after *month end* (largest societies) and ten *business days* after *month end* (other societies);
3. *investment services conglomerate*: frequency is half yearly with due date three *months* after period end;
4. *insurance conglomerate*: frequency is yearly with due date four *months* after period end for the capital adequacy return and three *months* after period end for the *intra-group transactions*.

Note 6 = Adequate information must be added as a separate item to the relevant form for sectoral reporting.

...

Ann 2G: Guidance notes on completion of banks' reporting forms (including validations)

In "Form BSD3 –Reporting instructions", "D400-D470 Deductions from capital", insert the following paragraph at the end of item D460:

Where the reporting institution is required to deduct the amount of material insurance holdings (see IPRU (BANK) Chapter CA, section 10.2), the deduction should be the higher of the book value and the regulatory capital requirement of the affiliate concerned, the latter pro rata to the interest held. The book value should already have been included in item A160, and deducted from capital in item D400; where the regulatory capital requirement is a higher figure, the difference over the book value should be included here.

...

Ann 3R: Building societies' reporting forms  
Building society quarterly statement - QFS1; D Capital Available: Own Funds: Society and Group

Note (d) Capital instruments in other CFI's, deductions in respect of ~~life companies~~ material insurance holdings, mortgage indemnity insurance captives, securitisations etc. - [Chapter 1 (Solvency) of Volume 1 of the IPSB for building societies refers].

...

Ann 4G: Guidance notes on completion of building societies' reporting forms  
Quarterly statement QSF1 – Guidance notes; Section D: Capital available: own funds

#### D3.1 Deductions not shown elsewhere

Deduct all holdings of capital instruments of other credit or financial institutions, CFIs. (See Annex of P/G for fuller definitions). This means holdings of share capital in a society's connected undertakings. For society columns it is any such holdings in CFIs; for Group columns only include holdings in such bodies that are not consolidated in Group figures.

Also include deductions (described in P/G) in respect of the following: ~~life and general insurance companies~~ material insurance holdings, mortgage indemnity insurance captives, securitisations, etc.

...

After SUP 16 Ann 19, insert the following new provisions, SUP 16 Ann 20R and SUP 16 Ann 21G:

SUP 16 ANN 20R: CONSOLIDATED SUPERVISION RETURN FOR INVESTMENT FIRMS

PART 1: GROUP FINANCIAL RESOURCES:

Name of regulated firm:

Name of ultimate EEA financial holding company for group (“parent”):


Group Tier 1:

ordinary share capital  
 share premium  
 audited consolidated reserves  
 non-cumulative preference shares  
 other reserves  
 minority interests  
 externally verified interim profits  
 Less:  
 intangible assets  
 material unaudited consolidated losses since balance sheet date (for half-yearly return)

A1


Group Tier 2:

non-fixed-term cumulative preference shares  
 non-fixed-term long term subordinated loans  
 consolidated revaluation reserves  
 minority interests  
 fixed-term cumulative preference shares  
 fixed-term long term subordinated loan  
 minority interests

B1


Group Tier 3:

short term subordinated loan  
 unaudited consolidated trading book profits  
 Total Group Tier 3:  
 Group Material Holdings in credit and financial institutions:

C

D1




investments in own shares

*B2*

*Group Material  
Insurance Holdings:*

*D2*

Total Group Net Tier 1:

*A2*

Total Group Tier 2:  
B=B1+B2

*B*

Group Financial Resources:

*E*

E = A2 + B1 + B2 + C – D1 – D2  
B, B1, B2, and C are subject to eligibility limits as set out in the relevant chapter of IPRU(INV).

PART 2: GROUP FINANCIAL RESOURCES REQUIREMENT:

Name of regulated firm:


Name of ultimate EEA financial holding company for group (“parent”):

F	F1	F2
Name of <i>subsidiary</i> or <i>participation</i>	% ownership	Local regulator (or state if unregulated)

G	H
Financial Resources Requirement of F	State how Financial Resources Requirement has been calculated.



(G1)

--

Parent’s Financial Resources Requirement

(I)

--

Large Exposures Requirement on Group Basis

(J)

--

Total Group Financial Resources Requirement (=G1+I+J)

(K)

--

Total Group Financial Resources (=E)

--

---

Total Group Surplus / (Deficit) (=E-K)

(L)

SUP 16 ANN 21G: CONSOLIDATED SUPERVISION RETURN FOR INVESTMENT FIRMS

Notes to the completion of Part 1: Group Financial Resources

Ref	Notes
A1	The material unaudited consolidated losses since balance sheet date only need to be reported on in the half-yearly return.
A2	<p>The Group should calculate its financial resources based on the consolidated financial statements prepared at the level of the ultimate EEA financial holding company in the group. The financial statements should be prepared in accordance with the relevant accounting standards but investments in insurance companies should be de-consolidated.</p> <p>The Group Tier 1 capital should be calculated by taking the relevant capital items from the consolidated balance sheet. Deductions must be made in arriving at Tier 1 for intangible assets (including goodwill arising from consolidation), investments in own shares and for material unaudited losses since the balance sheet date. Unaudited losses should be regarded as material if they exceed 10% of Group Tier 1 before taking into account this deduction.</p>
B1	This is the sum of non-fixed-term (undated) cumulative preference shares, non-fixed-term (undated) long-term subordinated loans and revaluation reserves and other consolidated reserves.
B2	This is the sum of fixed-term cumulative preference shares and fixed-term long-term subordinated loans.
C	The total of short-term subordinated loans external to the group and unaudited consolidated profits arising from trading book activities should be shown here.
D1	The definition of material holdings in non-group credit institutions and investment firms should be derived on the basis of the prudential rules applied to the most significant sector in the group except that references to “own funds” should be replaced by “consolidated own funds”. For this purpose consolidated own funds is equal to A+B after the application of the eligibility limits as set out in the relevant chapter of IPRU(INV).
D2	Insurance members of the group should be de-consolidated and material insurance holdings should be deducted here. They normally represent the book value of the investment in insurance undertakings, reinsurance undertakings and insurance holding companies in which the group holds a participation, unless the group’s share of the undertaking’s notional or local requirement is higher, in which case, there is a

Ref	Notes
	deduction in full.
E	<p>The Group Financial Resources should be shown here. This represents the sum of eligible capital in A, B1, B2 and C, minus the deductions in D1 and D2. No other deductions should be made. Liquidity adjustments and other similar deductions that are made at the solo level should be included in the Group Financial Resources Requirement.</p> <p>The limits applied at the group level to the inclusion of items in the group financial resources should be the same as the limits applied at the level of the main firm in the group.</p>

Notes to the completion of PART 2: Group Financial Resources Requirement

Ref	Notes
F	<p>List the name of each <i>subsidiary</i> and <i>participation</i>.</p> <p>A <i>firm</i> may combine several entities together where these are not material in relation to the group. For example, entities where total assets are in aggregate less than 5% of the group's total assets. The <i>firm</i> should list the relevant entities in a note to the return and should be able to demonstrate the contribution of the individual entities to the group calculation.</p>
F1	<p>List the percentage interest in the <i>subsidiary</i> or <i>participation</i> held by the parent. If the shares are not held directly by the parent, but by another group company, enter the effective percentage interest of the parent in the company. Where the entity is a <i>subsidiary</i> of a <i>subsidiary</i> of the parent, indicate (S) after the effective percentage interest. Such an entity will be treated as a <i>subsidiary</i> of the parent and will be included in full in the calculations.</p>
F2	<p>Specify if the <i>subsidiary</i> or <i>participation</i> is regulated by the <i>FSA</i> or another regulator. If the entity is unregulated, state "unregulated".</p>
G	<p>The financial resources requirement of entity F should be shown here. The financial resources requirement for a participation must be pro-rated (i.e. it should be multiplied by F1).</p> <p>This should be equal to the solo financial resources requirement plus any deductions from own funds made in arriving at the solo financial resources.</p> <p>In the case of a firm regulated by the FSA under IPRU(INV) Chapter 5 rules (as an investment management firm) this should be equal to the financial resources requirement calculated in accordance with IPRU(INV) 5.2.3 plus the illiquid assets adjustment calculated in accordance with IPRU(INV) Table 5.2.2(1) part II paragraph 10, but less any qualifying property adjustment.</p> <p>For unregulated firms this should be equal to the proxy financial resources requirement, which should also include illiquid assets and other deductions (where appropriate).</p>
G1	<p>This is the sum of figures in column G.</p>
H	<p>Details of the method used to calculate G (the financial resources requirement) for each firm should be given here. For example for an</p>

<i>Ref</i>	<i>Notes</i>
	<p>FSA-regulated firm column H should contain the IPRU reference (eg IPRU(INV) Chapter 5). For an overseas regulated firm where the prudential calculation is recognised by FSA as being equivalent the applicable overseas regulator should be given.</p> <p>For proxy requirements for unregulated firms column H should state the regulatory rules that have been applied to calculate the proxy requirement.</p>
I	<p>The financial resources requirement of the parent should be shown here.</p> <p>This should be equal to the solo financial resources requirement (excluding any large exposures requirement and requirements in respect of intra-group balances) and any adjustments made to financial resources in accordance with Rule 14.4.3R.</p>
J	<p>The group large exposures requirement should be shown here. This will only be calculated if there are trading book activities within the group.</p>
K	<p>The Group Financial Resources Requirement should be shown here. It is equal to the sum of G1, I and J.</p>
L	<p>The overall group surplus or deficit is equal to the difference between the Total Group Financial Resources (E) and the Group Financial Resources Requirement (K).</p>

...

SUP Schedule 2 - Notification requirements:

...				
<i>SUP</i> 15.8.4R	Delegation by <i>UCITS</i> <i>management</i> <i>company</i>	The fact that a function of the <i>UCITS</i> <i>management</i> <i>company</i> has been delegated together with (a) the identity of the party to whom the function has been delegated and (b) the period during which the delegation will apply.	The delegation of a function by a <i>UCITS</i> <i>management</i> <i>company</i> .	As soon as reasonably practicable.
<u><i>SUP</i></u> 15.9.1R	<u>Being or ceasing to be a <i>financial conglomerate</i></u>	<u>The fact of being or ceasing to be a <i>financial conglomerate</i></u>	<u>Being or ceasing to be a <i>financial conglomerate</i></u>	<u>immediately</u>
<u><i>SUP</i></u> 15.9.2R	<u>Reasonable likelihood of becoming or ceasing to be a <i>financial conglomerate</i></u>	<u>Reasonable likelihood of becoming or ceasing to be a <i>financial conglomerate</i></u>	<u>Reasonable likelihood of becoming or ceasing to be a <i>financial conglomerate</i></u>	<u>immediately</u>
<i>SUP</i> 16.3.17 R	Reporting ? change of <i>accounting</i> <i>reference</i> <i>date</i>	The fact of a change in <i>accounting</i> <i>reference</i> <i>date</i>	A change in <i>accounting</i> <i>reference</i> <i>date</i>	If extending its <i>accounting</i> <i>reference</i> <i>period</i> , before the previous <i>accounting</i> <i>reference</i> <i>date</i>
				If shortening its <i>accounting</i> <i>period</i> , it must make



				the notification in (1) before the new <i>accounting</i> <i>reference</i> <i>date.</i>
...				

...

## Annex J

### Amendments to the Decision making manual

In this Annex, underlining indicates new text.

- 4.1.8 G Examples of matters decided by *executive procedures* (where the *FSA* decides or is required to use the statutory powers in question rather than to achieve the action required in other ways, for example through individual *guidance* or securing the agreement of a *firm* to take action on a voluntary basis) include:
- ...
- (4A) in relation to a *financial conglomerate*, using the *own-initiative power* to apply one of the methods for calculating capital adequacy in Annex 1 of the *Financial Groups Directive* (see *PRU 8.4.50R (Capital adequacy requirement: Use of Part IV permission to apply Annex 1 of the Financial Groups Directive)* or to impose a reporting requirement under *SUP 16 (Reporting requirements)*;
- ...

**Annex K**  
**Amendments to the Electronic money sourcebook**

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being deleted or inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

Insert the following new entry to the table in ELM 1.5.2G:

Block	Module	Application
Block 2 (Business Standards)	The Integrated Prudential Sourcebook ( <i>PRU</i> )	<i>PRU</i> 1.8 (Action for damages), <i>PRU</i> 8.1 (Group risk systems and controls requirement), <i>PRU</i> 8.4 (Cross sector groups), <i>PRU</i> 8.5 (Third country groups), <i>PRU</i> 8 Ann 1R (Capital adequacy calculations for financial conglomerates), <i>PRU</i> 8 Ann 2R (Prudential rules for third country groups), <i>PRU</i> 8 Ann 3G (Financial Conglomerates: Cooperative decision making by competent authorities and consultation) and <i>PRU</i> 8 Ann 4G (Classification of groups) apply to an <i>ELMI</i> .

...

*ELM* 2.4.2R Table: Calculation of initial capital and own funds

...

~~material holdings in financial institutions or credit institutions~~ the total amount of material holdings in certain persons (see *ELM* 2.4.17R)

...

*ELM* 2.4.17R Material holdings

- (1) The total amount of a firm's material holdings as referred to at stage F of the calculation in the table in *ELM* 2.4.2R is ~~in financial institutions or credit institutions~~ are the sum of:

- (a) the total value of all *ownership shares* and all ~~subordinated loan~~ capital coming within (6) owned by the *firm* (or in which it has a position) in any *relevant financial services company* or *financial institution* in which the *firm* owns more than 10% of the *ownership shares*; ~~and~~
- (b) the amount by which the total amount specified in (3) exceeds 10% of the *firm's own funds* (calculated before the deduction of *material holdings* at stage F of the calculation in *ELM 2.4.2 R*);<sub>2</sub>
- (c) *ownership shares* in any:
- (i) *insurance undertaking*; or
- (ii) *insurance holding company*;
- if it fulfils one of the following conditions:
- (iii) it is a *subsidiary undertaking* of the *firm*; or
- (iv) the *firm* holds a *participation* in it; and
- (d) any item of capital of a type referred to in (6) in an *insurance undertaking* or *insurance holding company* coming within (1)(c).
- (2) ...
- (3) The amount referred to in (1)(b) is the sum of the total value of all the *ownership shares* and all ~~subordinated loan~~ capital coming within (6) owned by the *firm* (or in which it has a position) in *financial institutions* or ~~*credit institutions*~~ *relevant financial services companies* except for *financial institutions* or ~~*credit institutions*~~ *relevant financial services companies* that fall into (1)(a).
- (4) The *firm* must include *ownership shares* and ~~subordinated loan capital~~ any item of capital of the type referred to in (6); and *ownership shares*<sub>2</sub> and ~~subordinated loan capital~~
- (a) of which it is not the registered owner but which it owns beneficially;  
or
- (b) that are or should be included as an asset in its accounting records.
- (5) The value of *ownership shares* and ~~subordinated loan~~ capital coming within (6) for the purposes of *ELM 2.4.17R* ~~(1)(a) and (3)~~ is the full balance sheet value.
- (6) An item falls into this paragraph if it is a subordinated debt or other item of capital that:

- (a) (in the case of an *insurance undertaking* or *insurance holding company*) falls into Article 16(3) of the *First Non-Life Directive* or, as applicable, Article 27(4) of the *Consolidated Life Directive*; or
- (b) (in the case of a *relevant financial services company* or *financial institution*) falls into Article 35 or Article 36(3) of the *Banking Consolidation Directive*.

...

After ELM 7.8.8G insert the following new provisions, ELM 7.8.9G and ELM 7.8.10G:

- 7.8.9 G If a *firm* is linked to other *financial services undertakings* by a *consolidation Article 12(1) relationship*, the *FSA* will determine how to apply the provisions of this chapter.
- 7.8.10 G If a *firm* is part of a *financial conglomerate*, the provisions of *PRU 8.4* apply. If a *firm* is part of a *third-country group*, the provisions of *PRU 8.5* apply.

**Annex L**  
**Amendments to the Glossary**

**PART 1 (NEW DEFINITIONS)**

In this part of this Annex, all the text is new and is not underlined.

*ancillary insurance services undertaking* (in relation to any *undertaking* in a *consolidation group, sub-group* or other group of *persons*) an *undertaking* complying with the following conditions:

- (a) its principal activity consists of:
  - (i) owning or managing property; or
  - (ii) managing data-processing services; or
  - (iii) any other similar activity;
- (b) the activity in (a) is ancillary to the principal activity of one or more *insurance undertakings*;
- (c) those *insurance undertakings* are also members of that *consolidation group, sub-group* or other group of *persons*; and
- (d) (for the purpose of *PRU 8.4* (Cross sector groups), *PRU 8.5* (Third country groups), *PRU 8 Ann 1R* (Capital adequacy calculations for financial conglomerates) and *PRU 8 Ann 2R* (Prudential rules for third country groups) it is not an *ancillary banking services undertaking*.

*ancillary investment services undertaking* (in relation to any *undertaking* in a *consolidation group, sub-group* or other group of *persons*) an *undertaking* complying with the following conditions:

- (a) its principal activity consists in:
  - (i) owning or managing property; or
  - (ii) managing data-processing services; or
  - (iii) any other similar activity;
- (b) the activity in (a) is ancillary to the principal activity of one or more *investment firms*;
- (c) those *investment firms* are also members of that *consolidation group, sub-group* or other group of *persons*; and

	(d) (for the purpose of <i>PRU 8.4</i> (Cross sector groups), <i>PRU 8.5</i> (Third country groups), <i>PRU 8 Ann 1R</i> (Capital adequacy calculations for financial conglomerates) and <i>PRU 8 Ann 2R</i> (Prudential rules for third country groups) it is not an <i>ancillary banking services undertaking</i> .
<i>applicable sectoral consolidation rules</i>	(in respect of a <i>financial sector</i> and in accordance with paragraph 6.10 of <i>PRU 8 Ann 1R</i> (Applicable sectoral consolidation rules)) the <i>FSA's sectoral rules</i> about capital adequacy and solvency on a consolidated basis applicable to that <i>financial sector</i> under the table in paragraph 6.11 of <i>PRU 8 Ann 1R</i> .
<i>applicable sectoral rules</i>	(in respect of a <i>financial sector</i> ) <i>applicable sectoral consolidation rules</i> for that <i>financial sector</i> and the <i>FSA's sectoral rules</i> about capital adequacy and solvency applicable to that <i>financial sector</i> under the table in paragraph 6.8 of <i>PRU 8 Ann 1R</i> ; which of those sets of <i>rules</i> apply for the purpose of a particular calculation depends on the nature of that calculation.
<i>asset management company</i>	(for the purpose of <i>ELM</i> and <i>PRU 8</i> (Group risk) and in accordance with Article 2(5) of the <i>Financial Groups Directive</i> (Definitions)) a management company within the meaning of Article 1a(2) of the <i>UCITS Directive</i> , as well as an <i>undertaking</i> the registered office of which is outside the <i>EEA</i> and which would require authorisation in accordance with Article 5(1) of the <i>UCITS Directive</i> if it had its registered office within the <i>EEA</i> .
<i>Bank Accounts Directive</i>	Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions.
<i>banking and investment group</i>	a group of <i>persons</i> (at least one of which is an <i>EEA regulated entity</i> that is a <i>credit institution</i> or an <i>investment firm</i> ) who: <ul style="list-style-type: none"> <li>(a) form a group in respect of which the consolidated capital adequacy requirements for the <i>banking sector</i> or the <i>investment services sector</i> under: <ul style="list-style-type: none"> <li>(i) the <i>FSA's sectoral rules</i>; or</li> <li>(ii) the <i>sectoral rules</i> of another <i>competent authority</i>; apply; or</li> </ul> </li> <li>(b) would form such a group if the scope of those <i>sectoral rules</i> were amended as described in paragraph 3.1 of <i>PRU 8 Ann 2R</i> (removing restrictions relating to place of incorporation or head office of members of those <i>financial sectors</i>).</li> </ul>

<i>banking conglomerate</i>	a <i>financial conglomerate</i> identified as a banking conglomerate in the decision tree in paragraph 4.5 of <i>PRU 8 Ann 1R</i> (Decision tree for types of <i>financial conglomerate</i> and definition of <i>most important financial sector</i> ).
<i>banking sector</i>	a sector composed of one or more of the following entities: <ul style="list-style-type: none"> <li>(a) a <i>credit institution</i>;</li> <li>(b) a <i>financial institution</i>; and</li> <li>(c) an <i>ancillary banking services undertaking</i>.</li> </ul>
<i>broker/manager</i>	a <i>firm</i> with <i>permission</i> for <i>dealing in investments as agent or managing investments</i> (including an <i>operator</i> of an <i>unregulated collective investment scheme</i> ) but which: <ul style="list-style-type: none"> <li>(a) does not have <i>permission</i> to <i>deal in investments as principal</i>;</li> <li>(b) is not a <i>UCITS management company</i>;</li> <li>(c) is not an <i>insurer</i>; and</li> <li>(d) is not a <i>bank</i>, a <i>building society</i> or an <i>ELMI</i>.</li> </ul>
<i>building society conglomerate</i>	a <i>financial conglomerate</i> identified as a <i>building society conglomerate</i> in the decision tree in paragraph 4.5 of <i>PRU 8 Ann 1R</i> (Decision tree for types of <i>financial conglomerate</i> and definition of <i>most important financial sector</i> ).
<i>coordinator</i>	(in relation to a <i>financial conglomerate</i> ) the <i>competent authority</i> which has been appointed, in accordance with Article 10 of the <i>Financial Groups Directive</i> (Competent authority responsible for exercising supplementary supervision (the coordinator)), as the <i>competent authority</i> which is responsible for the co-ordination and exercise of supplementary supervision of that <i>financial conglomerate</i> .
<i>conglomerate capital resources</i>	(in relation to a <i>financial conglomerate</i> with respect to which <i>PRU 8.4.29R</i> (Application of methods 1, 2 or 3 from Annex I of the <i>Financial Groups Directive</i> ) applies) capital resources as defined in whichever of paragraphs 1.1, 2.1 or 3.1 of <i>PRU 8 Ann 1R</i> (Capital adequacy calculations for financial conglomerates) applies with respect to that <i>financial conglomerate</i> .
<i>conglomerate capital resources requirement</i>	(in relation to a <i>financial conglomerate</i> with respect to which <i>PRU 8.4.29R</i> (Application of methods 1, 2 or 3 from Annex I of the <i>Financial Groups Directive</i> ) applies) the capital resources requirement defined in whichever of paragraphs 1.3, 2.4 or 3.3 of <i>PRU 8 Ann 1R</i> (Capital adequacy calculations for financial conglomerates) applies with respect to that <i>financial conglomerate</i> .



*consolidation Article 12(1) relationship*

a relationship between one *undertaking* (the first undertaking) and one or more other *undertakings* satisfying the conditions set out in Article 12(1) of the *Seventh Company Law Directive*, which in summary are as follows:

- (a) those *undertakings* are not connected, as described in article 1(1) or (2) of that Directive; and
- (b) one of the following conditions is satisfied:
  - (i) they are managed on a unified basis pursuant to a contract concluded with the first undertaking or provisions in the memorandum or articles of association of those *undertakings*; or
  - (ii) the administrative, management or supervisory bodies of those *undertakings* consist, for the major part, of the same *persons* in office during the financial year in respect of which it is being decided whether such a relationship exists.

*consolidation group*

the following:

- (a) a *conventional group*; or
- (b) *undertakings* linked by a *consolidation Article 12(1) relationship*.

If a *parent undertaking* or *subsidiary undertaking* in a *conventional group* (the first person) has a *consolidation Article 12(1) relationship* with another *person* (the second person), the second person (and any *subsidiary undertaking* of the second person) is also a member of the same *consolidation group*.

*conventional group*

(for the purposes of PRU 8 (Group Risk)) a group of *undertakings* that consists of a *parent undertaking* and the rest of its *sub-group*.

*EEA banking and investment group*

a *banking and investment group* that satisfies one or more of the following conditions:

- (a) it is headed by:
  - (i) an *investment firm* or *credit institution* that is authorised and incorporated in an *EEA State*; or
  - (ii) a *financial holding company* that has its head office in an *EEA State*; or
- (b) it has as a member an *investment firm* or *credit institution* that:

- (i) is authorised and incorporated in an *EEA State*; and
- (ii) is linked with another member that is in the *banking sector* or the *investment services sector* by a *consolidation Article 12(1) relationship*; or
- (c) it is otherwise required by *EEA prudential sectoral legislation* for the *banking sector* or the *investment services sector* (except Article 56a of the *Banking Consolidation Directive* (Third-country parent undertakings)) to be subject to consolidated supervision by a *competent authority*.

*EEA financial conglomerate* a *financial conglomerate* that is of a type that falls under Article 5(2) of the *Financial Groups Directive* (Scope of supplementary supervision of *regulated entities* referred to in Article 1 of that Directive) which in summary means a *financial conglomerate*:

- (a) that is headed by an *EEA regulated entity*; or
- (b) in which the *parent undertaking* of an *EEA regulated entity* is a *mixed financial holding company* which has its head office in the *EEA*; or
- (c) in which an *EEA regulated entity* is linked with a member of the *financial conglomerate* in the *overall financial sector* by a *consolidation Article 12(1) relationship*.

*EEA prudential sectoral legislation*

(in relation to a *financial sector*) requirements applicable to *persons* in that *financial sector* in accordance with *EEA* legislation about prudential supervision of *regulated entities* in that *financial sector* and so that:

- (a) (in relation to the *banking sector* and the *investment services sector*) in particular this includes the requirements laid down in the *Banking Consolidation Directive* and the *Capital Adequacy Directive*; and
- (b) (in relation to the *insurance sector*) in particular this includes requirements laid down in the *First Non-Life Directive*, the *Consolidated Life Directive* and the *Insurance Groups Directive*.

*EEA regulated entity*

a *regulated entity* that is an *EEA firm* or a *UK firm*.

*exempt CAD firm*

(in accordance with Article 2(2) of the *Capital Adequacy Directive* (Definitions)) a *firm* that satisfies the following conditions:

- (a) it is an *ISD investment firm*;
- (b) it is not an *insurer*, a *bank*, a *building society* or an *ELMI*;

	(c) its <i>permission</i> is subject to a <i>limitation or requirement</i> preventing it from holding <i>client money</i> or <i>clients' assets</i> and for that reason it may not at any time place itself in debit with its <i>clients</i> ; and
	(d) the only <i>core investment service</i> for which it has <i>permission</i> is receiving and transmitting on behalf of investors orders in relation to one or more of the instruments listed in Section B of the Annex to the <i>ISD</i> .
<i>financial conglomerate</i>	(in accordance with Article 2(14) of the <i>Financial Groups Directive</i> (Definitions)) a <i>consolidation group</i> that is identified as a <i>financial conglomerate</i> by the <i>financial conglomerate definition decision tree</i> .
<i>financial conglomerate definition decision tree</i>	the decision tree in <i>PRU 8 Ann 4R</i> .
<i>Financial Groups Directive</i>	Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate.
<i>Financial Groups Directive Regulations</i>	<i>[To be included in the Glossary when those Regulations are made]</i>
<i>financial sector</i>	one of the <i>banking sector</i> , the <i>insurance sector</i> or the <i>investment services sector</i> .
<i>FSA regulated EEA financial conglomerate</i>	a <i>financial conglomerate</i> (other than a <i>third-country financial conglomerate</i> ) that satisfies one of the following conditions: <ul style="list-style-type: none"> <li>(a) <i>PRU 8.4.26R</i> or <i>PRU 8.4.29R</i> (Capital adequacy calculations for <i>financial conglomerates</i>) applies with respect to it; or</li> <li>(b) a <i>firm</i> that is a member of that <i>financial conglomerate</i> is subject to obligations imposed through its <i>Part IV permission</i> to ensure that that <i>financial conglomerate</i> meets levels of capital adequacy based or stated to be based on Annex I of the <i>Financial Groups Directive</i>.</li> </ul>
<i>insurance conglomerate</i>	a <i>financial conglomerate</i> identified as an insurance conglomerate in the decision tree in paragraph 4.5 of <i>PRU 8 Ann 1R</i> (Decision tree for types of <i>financial conglomerate</i> and definition of <i>most important financial sector</i> ).
<i>Insurance Groups Directive</i>	Directive of the European Parliament and of the Council of 27 October 1998 on the supplementary supervision of insurance undertakings in an insurance group (1998/78/EC).

- insurance holding company* (1) a *parent undertaking*, other than an *insurance undertaking*, the main business of which is to acquire and hold participations in *subsidiary undertakings* and which fulfils the following conditions:
- (a) its *subsidiary undertakings* are either exclusively or mainly *insurance undertakings*;
  - (b) at least one of those *subsidiary undertakings* is a *UK insurer* or an *EEA firm* that is a *regulated insurance entity*; and
  - (c) it is not a *mixed financial holding company*.
- (2) For the purposes of:
- (a) the definition of the *insurance sector*; and
  - (b) *ELM*;
- paragraph (1)(b) of this definition does not apply.
- insurance sector* a sector composed of one or more of the following entities:
- (a) an *insurance undertaking*;
  - (b) an *insurance holding company*; and
  - (c) (in the circumstances described in *PRU 8.4.39R* (The financial sectors: Asset management companies)) an *asset management company*.
- intra-group transactions* (in accordance with Article 2(18) of the *Financial Groups Directive* (Definitions)) all transactions by which *regulated entities* within a *financial conglomerate* rely either directly or indirectly upon other *undertakings* within the same *financial conglomerate* or upon any *person* linked to the *undertakings* within that *financial conglomerate* by *close links*, for the fulfilment of an obligation whether or not contractual, and whether or not for payment.
- investment services conglomerate* a *financial conglomerate* identified as an investment services conglomerate in the decision tree in paragraph 4.5 of *PRU 8 Ann 1R* (Decision tree for types of *financial conglomerate* and definition of *most important financial sector*).
- investment services sector* a sector composed of one or more of the following entities:
- (a) an *investment firm*;
  - (b) a *financial institution*; and

- (c) (in the circumstances described in *PRU 8.4.39R* (The financial sectors: Asset management companies)) an *asset management company*.

*main investment services undertaking*

(for the purpose of *PRU 8* (Group Risk) and in relation to a *financial conglomerate*):

- (a) (if there is only one *investment firm* in that *financial conglomerate*) that *investment firm*; and
- (b) (if there is more than one *investment firm* in that *financial conglomerate*) the member of the *financial conglomerate* identified in the same way as the main firm for the purposes of *rule 14.4.2* of Chapter 14 of *IPRU(INV)* (Group Financial Resources), but so that the comparison required by that *rule* must be carried out with respect to all *investment firms* in the *financial conglomerate*.

*matched principal broker*

a *firm* with *permission to deal in investments as principal* other than:

- (a) a *bank*, a *building society* or an *ELMI*; or
- (b) a *UCITS management company*; or
- (c) an *insurer*; or
- (d) a *local*;

and which satisfies the following conditions:

- (e) it *deals* as principal only to fulfil customer orders;
- (f) it holds positions for its own account only as a result of a failure to match investors' orders precisely;
- (g) the total market value of the positions is no higher than 15% of the *firm's initial capital*; and
- (h) the positions are incidental and provisional in nature and strictly limited to the time required to carry out the transaction in question.

*mixed-activity holding company*

one of the following:

- (a) (in accordance with Article 1(22) of the *Banking Consolidation Directive* (Definitions)) a *parent undertaking*, other than a *financial holding company*, a *credit institution* or a *mixed financial holding company*, the *subsidiary undertakings* of which include at least one *credit institution*; or

	(b) (in accordance with Article 7(3) of the <i>Capital Adequacy Directive</i> (Supervision on a consolidated basis) and in relation to a <i>banking and investment group</i> without any <i>credit institutions</i> in it) a <i>parent undertaking</i> , other than a <i>financial holding company</i> , an <i>investment firm</i> or a <i>mixed financial holding company</i> , the <i>subsidiary undertakings</i> of which include at least one <i>investment firm</i> .
<i>mixed-activity insurance holding company</i>	(in accordance with Article 1(j) of the <i>Insurance Groups Directive</i> (Definitions)) a <i>parent undertaking</i> , other than an <i>insurance undertaking</i> , an <i>insurance holding company</i> or a <i>mixed financial holding company</i> , the <i>subsidiary undertakings</i> of which include at least one <i>insurance undertaking</i> .
<i>mixed financial holding company</i>	(in accordance with Article 2(15) of the <i>Financial Groups Directive</i> (Definitions)) a <i>parent undertaking</i> , other than a <i>regulated entity</i> , which together with its <i>subsidiary undertakings</i> , at least one of which is an <i>EEA regulated entity</i> , and other entities, constitutes a <i>financial conglomerate</i> .
<i>most important financial sector</i>	(in relation to a <i>financial sector</i> in a <i>consolidation group</i> or a <i>financial conglomerate</i> and in accordance with PRU 8.4 (Cross sector groups)) the <i>financial sector</i> with the largest average referred to in the box titled Threshold Test 2 in the <i>financial conglomerate definition decision tree</i> (10% ratio of balance sheet size and solvency requirements); and so that: <ul style="list-style-type: none"> <li>(a) the <i>investment services sector</i> and the <i>banking sector</i> are treated as one for the purposes set out in PRU 8.4.7R (Definition of financial conglomerate: The financial sectors: General); and</li> <li>(b) the definition is altered as set out in paragraph 4.4 and the decision tree in paragraph 4.5 of PRU 8 Ann 1R (Types of financial conglomerate and definition of most important financial sector) for the purposes set out in paragraph 4.4 of PRU 8 Ann 1R.</li> </ul>
<i>overall financial sector</i>	a sector composed of one or more the following types of entities: <ul style="list-style-type: none"> <li>(a) members of each of the <i>financial sectors</i>; and</li> <li>(b) (except where PRU 8.4 (Cross sector groups) or PRU 8 Ann 1R (Capital adequacy calculations for financial conglomerates) provide otherwise) a <i>mixed financial holding company</i>.</li> </ul>
<i>own account dealer</i>	a <i>firm</i> with <i>permission to deal in investments as principal</i> other than: <ul style="list-style-type: none"> <li>(a) a <i>bank</i>, a <i>building society</i> or an <i>ELMI</i>; or</li> </ul>

- (b) an *insurer*; or
- (c) a *UCITS management company*; or
- (d) a *matched principal broker*; or
- (e) an *ICVC*; or
- (f) a *local*.

*participation*

(for the purposes of *ELM* and *PRU* 8 (Group risk)):

- (a) a participating interest as defined in section 260 of the Companies Act 1985; or
- (b) the direct or indirect ownership of 20% or more of the voting rights or capital of an *undertaking*;

but excluding the interest of a *parent undertaking* in its *subsidiary undertaking*.

*PRU*

the Integrated Prudential Sourcebook.

*regulated entity*

one of the following:

- (a) a *credit institution*; or
- (b) a *regulated insurance entity*; or
- (c) an *investment firm*;

whether or not it is incorporated in, or has its head office in, an *EEA State*.

An *asset management company* is treated as a regulated entity for the purposes described in *PRU* 8.4.39R (The financial sectors: asset management companies).

*regulated insurance entity*

an insurance undertaking within the meaning of Article 4 of the *Consolidated Life Directive*, Article 6 of the *First Non-Life Directive* or Article 1(b) of the *Insurance Groups Directive*.

*relevant competent authorities*

(in relation to a *financial conglomerate*) those *competent authorities* which are, or which have been appointed as, relevant competent authorities in relation to that *financial conglomerate* under Article 2(17) of the *Financial Groups Directive* (Definitions).

*risk concentration*

(in accordance with Article 2(19) of the *Financial Groups Directive* (Definitions)) all exposures with a loss potential borne by entities within a *financial conglomerate*, which are large enough to threaten the solvency or the financial position in general of the *regulated entities* in the *financial conglomerate*; such exposures may be caused by counterparty risk, credit risk, investment risk, insurance risk, market risk, other risks, or a combination or interaction of these risks.

*sectoral rules*

(in relation to a *financial sector*) rules and requirements relating to the prudential supervision of *regulated entities* applicable to *regulated entities* in that *financial sector* as follows:

- (a) (for the purposes of *PRU 8.4.12R* (Definition of financial conglomerate: Solvency requirement)) *EEA prudential sectoral legislation* for that *financial sector* together with as appropriate the rules and requirements in (c); or
- (b) (for the purpose of calculating *solo capital resources* and a *solo capital resources requirement*):
  - (i) (to the extent provided for in paragraph 6.5 of *PRU 8 Ann 1R*) rules and requirements that are referred to in paragraph 6.6 of *PRU 8 Ann 1R* (Solo capital resources requirement: Non-EEA firms subject to equivalent regimes); and
  - (ii) the rules and requirements in (c); or
- (c) (for all other purposes) rules and requirements:
  - (i) of the *FSA*; or
  - (ii) of or administered by another *competent authority*;

and so that:

- (d) (in relation to prudential rules about consolidated supervision for any *financial sector*) those requirements include ones relating to the form and extent of consolidation;
- (e) (in relation to any *financial sector*) those requirements include ones relating to the eligibility of different types of capital;
- (f) (in relation to any *financial sector*) those requirements include both ones applying on a solo basis and ones applying on a consolidated basis;



- (g) (in relation to the *insurance sector*) references in this definition to consolidated supervision are to supplementary supervision, similar expressions being interpreted accordingly; and
- (h) references to the *FSA's sectoral rules* are to *sectoral rules* in the form of *rules*.

*smallest financial sector* (in relation to a *financial sector* in a *consolidation group* or a *financial conglomerate* and in accordance with *PRU 8.4* (Cross sector groups)) the *financial sector* with the smallest average referred to in the box titled Threshold Test 2 in the *financial conglomerate definition decision tree* (10% ratio of balance sheet size and solvency requirements), the *banking sector* and *investment services sector* being treated as one *financial sector* in the circumstances set out in *PRU 8.4*.

*solo capital resources* (for the purposes of *PRU 8* (Group risk) and in relation to a member of a *financial conglomerate* in the *overall financial sector*) capital resources that are or would be eligible as capital under the *sectoral rules* that apply for the purpose of calculating its *solo capital resources requirement*. Paragraph 6.9 of *PRU 8 Ann 1R* (Solo capital resources requirement: the insurance sector) applies for the purpose of this definition in the same way as it does for the definition of *solo capital resources requirement*.

*solo capital resources requirement* (for the purpose of *PRU 8* (Group risk)) a capital resources requirement calculated on a solo basis as defined in paragraphs 6.2-6.9 of *PRU 8 Ann 1R* (Solo capital resources requirement: the insurance sector).

*solvency deficit* (in *PRU 8 Ann 1R* (Capital adequacy calculations with respect to financial conglomerates) and in respect of a member of the *overall financial sector*) the amount (if any) by which its *solo capital resources* fall short of its *solo capital resources requirement*.

*third-country banking and investment group* a *banking and investment group* that meets the following conditions:

- (a) it is headed by:
  - (i) a *credit institution*; or
  - (ii) an *asset management company*; or
  - (iii) an *investment firm*; or
  - (iv) a *financial holding company*;
 that has its head office outside the *EEA*; and

(b) it is not part of a wider *EEA banking and investment group*.

*third-country competent authority*

the authority of a country or territory which is not an *EEA State* that is empowered by law or regulation to supervise (whether on an individual or group-wide basis) *regulated entities*.

*third-country financial conglomerate*

a *financial conglomerate* that is of a type that falls under Article 5(3) of the *Financial Groups Directive*, which in summary is a *financial conglomerate* headed by a *regulated entity* or a *mixed financial holding company* that has its head office outside the *EEA*.

*third-country group*

a *third-country financial conglomerate* or a *third-country banking and investment group*.

## PART 2 (AMENDED DEFINITIONS)

In this part of this Annex, underlining indicates new text and striking through indicates deleted text.

- ancillary banking services undertaking* (~~in ELM~~) (as defined in article 1.23 of the ~~Banking Coordination Consolidation Directive~~ (Definitions)) and in relation to an undertaking in a consolidation group, sub-group or another group of persons) an undertaking complying with the following conditions:
- (a) its ~~the~~ principal activity ~~of which~~ consists in:
    - (i) owning or managing property;
    - (ii) managing data-processing services; or
    - (iii) any other similar activity;
  - (b) the activity in (a) ~~which~~ is ancillary to the principal activity of one or more *credit institutions*; and
  - (c) those credit institutions are also members of that consolidation group, sub-group or group.
- arranger* (1) (For the purposes of PRU 8 (Group risk) a firm with permission for one or more of the following:
- (a) arranging (bringing about) deals in investments; or
  - (b) making arrangements with a view to transactions in investments;
- and which:
- (c) is not a bank, a building society or an ELMI;
  - (d) is not an insurer;
  - (e) is not a UCITS management company;
  - (f) is not a local; and
  - (g) does not have permission:
    - (i) to deal in investments as principal; or
    - (ii) for dealing in investments as agent; or
    - (iii) for managing investments.

- (2) (for all other purposes) a person who is arranging (bringing about) deals in investments, making arrangements with a view to transactions in investments, or agreeing to carry on any of those regulated activities.
- competent authority*
- (1) ...
- (2) ...
- (3) (for the purposes of PRU 8.1 (Group risk systems and controls requirement), PRU 8.4 (Cross sector groups), PRU 8.5 (Third country groups), PRU 8 Ann 1R (Capital adequacy calculations for financial conglomerates) and PRU 8 Ann 2R (Prudential rules for third country groups)) any national authority of an EEA State which is empowered by law or regulation to supervise regulated entities, whether on an individual or group-wide basis.
- financial holding company* ~~(in ELM)~~ a financial institution, that fulfils the following conditions:
- (a) ~~the~~ its subsidiary undertakings of which are either exclusively or mainly ~~relevant financial services companies credit institutions, investment firms or financial institutions;~~
- (b) ~~one of which~~ at least one of those subsidiary undertakings is a ~~relevant financial services company credit institution or an investment firm;~~ and
- (c) it is not a mixed financial holding company.
- financial institution*
- (1) (in accordance with paragraph 5(c) of Schedule 3 to the Act (EEA Passport Rights: EEA firm) and article 1(5) of the *Banking Consolidation Directive* (Definitions), but not for the purposes of ELM or PRU 8 (Group risk)), an *undertaking*, other than a *credit institution*, the principal activity of which is to acquire holdings or to carry on one or more of the *listed activities* listed in points 2 to 12 of Annex I to the *BCD*, which is a subsidiary of the kind mentioned in article 19 of the *BCD* and which fulfils the conditions in articles 18 and 19 of the *BCD*.
- (2) (for the purposes of ELM and PRU 8 (Group risk) and in accordance with Articles 1(5) (Definitions) and 2(2) (Scope) of the Banking Consolidation Directive);

- (a) an undertaking, other than a credit institution, the principal activity of which is to acquire holdings or to carry on one or more of the listed activities listed in points 2 to 12 of Annex I to the Banking Consolidation Directive; ~~(in ELM) an undertaking other than a credit institution, the principal activity of which is to acquire holdings or to carry on one or more of the activities listed in points 2 to 12 of Annex 1 of the Banking Consolidation Directive.~~
- (b) those institutions permanently excluded by paragraph 2(3) of the Banking Consolidation Directive (Scope), with the exception of the central banks of Member States, but so that, so far as this paragraph (b) applies for the purposes of ELM, it only applies for the purposes of chapter 7 (Consolidated financial supervision) of ELM; and
- (c) (for the purposes of ELM) an asset management company.

*FSA consolidation rule*

(in ELM) the following rules in IPRU:

- (a) 3.3.13R in chapter GN of IPRU(BANK) (as it applies on a consolidated ~~except as it applies to a bank purely on a sole basis);~~
- (b) IPRU(BSOC) 1.2.1R (as it applies on a consolidated ~~except as it applies to a building society purely on a sole basis); and~~
- (c) Chapter 14 of IPRU(INV) ~~5.7.1R;~~
- (d) IPRU(INV) 10.200R(1) to 10.204R;
- (e) IPRU(INV) 13.7.2AR and 13.2.7BR.

*group*

- (1) (except in relation to an ICVC and except for the purposes of PRU 8.1 (Group risk systems and controls requirement)) (as defined in section 421 of the Act (Group)) (in relation to a person ("A")) A and any person who is:  
  - ...
- (2) ...
- (3) (for the purposes of PRU 8.1 (Group risk systems and controls requirement) and in relation to a person "A")) A and any person:
  - (a) who falls into (1);

- (b) who is a member of the same *financial conglomerate* as A;
- (c) who has a *consolidation Article 12(1) relationship* with A;
- (d) who has a *consolidation Article 12(1) relationship* with any *person* in (3)(a);
- (e) who is a *subsidiary undertaking* of a person in (3)(c) or (3)(d); or
- (f) whose omission from an assessment of the risks to A of A's connection to any *person* coming within (3)(a)-(3)(e) or an assessment of the financial resources available to such *persons* would be misleading.

*initial capital*

- (1) (in *ELM*) items coming into stage A of the calculation in *ELM* 2.4.2R (Calculation of initial capital and own funds).
- (2) (for the purposes of the definition of *matched principal dealer*, in accordance with Article 2(24) of the *Capital Adequacy Directive* (Definitions) and with respect to a *firm*) capital that is recognised for the purpose of the *rules* about capital adequacy to which that *firm* is subject but excluding, in accordance with items (1) and (2) of Article 34(2) of the *Banking Consolidation Directive* (General principles), anything that does not fall within the following classes of capital:
  - (a) capital within the meaning of Article 22 of the *Bank Accounts Directive* (Liabilities: Item 9 – Subscribed capital), insofar as it has been paid up, plus share premium accounts but excluding cumulative preferential shares; or
  - (b) reserves within the meaning of Article 23 of the *Bank Accounts Directive* (Liabilities: Item 11 – Reserves) and profits and losses brought forward as a result of the application of the final profit or loss. Interim profits can only be included before a formal decision has been taken only if these profits have been verified by *persons* responsible for the auditing of the accounts and if the amount thereof has been evaluated in accordance with the principles set out in the *Bank Accounts Directive* and is net of any foreseeable charge or dividend.

In the case of a firm subject to the rules in chapter 10 of IPRU(INV), initial capital means initial capital as defined in the Glossary to that chapter.

*parent undertaking*

(in accordance with section 420 of the *Act* (Parent and subsidiary undertaking) and section 258 of the Companies Act 1985 (Parent and subsidiary undertakings))

(a) (in relation to whether an *undertaking*, other than an *incorporated friendly society*, is a parent undertaking and except for the purposes of PRU 8.4 (Cross sector groups), PRU 8.5 (Third country groups), PRU 8 Ann 1R (Capital adequacy calculations for financial conglomerates) and PRU 8 Ann 2R (Prudential rules for third country groups)) an *undertaking* which has the following relationship to another *undertaking* ("S"):

...

(b) (in relation to whether an *incorporated friendly society* is a parent undertaking and except for the purposes of PRU 8.4 (Cross sector groups), PRU 8.5 (Third country groups), PRU 8 Ann 1R (Capital adequacy calculations for financial conglomerates) and PRU 8 Ann 2R (Prudential rules for third country groups)) an *incorporated friendly society* which has the following relationship to a *body corporate* ("S"):

...

(c) (for the purposes of PRU 8.4 (Cross sector groups), PRU 8.5 (Third country groups), PRU 8 Ann 1R (Capital adequacy calculations for financial conglomerates) and PRU 8 Ann 2R (Prudential rules for third country groups) and in relation to whether an *undertaking* is a parent undertaking) an *undertaking* which has the following relationship to another *undertaking* ("S"):

(i) a relationship described in (a) other than (a)(vii); or

(ii) it effectively exercises a dominant influence over S

and so that (ii) applies also for the purpose of PRU 8.1 (Group risk systems and controls requirement).

*sub-group*

~~(in ELM)~~ (in relation to a *person*):

...

## ADDENDUM

### FINANCIAL CONGLOMERATES AND OTHER FINANCIAL GROUPS INSTRUMENT 2004

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex G of this instrument is amended as follows to ensure that correct rule references of SUP 16.7.82R and SUP 16.7.83R are referred to in PRU 8.4.2G:

#### Purpose

8.4.2 G *PRU 8.4* implements the *Financial Groups Directive*. However, material on the following topics is to be found elsewhere in the *Handbook* as follows:

...

(3) material on reporting obligations can be found in ~~SUP 16.7.73R~~ SUP 16.7.82R and ~~SUP 16.7.74R~~ SUP 16.7.83R; and

...

...

Annex I of this instrument is amended as follows to ensure that the correct rule references of SUP 16.7.82R and SUP 16.7.83R are referred to in SUP 7 and SUP 16:

7.3.2 G The *FSA* may seek to vary a *firm's Part IV permission* on its own initiative in certain situations, including the following:

...

(4) If a *firm* is a member of *financial conglomerate* and the *FSA* is implementing supplementary supervision under the *Financial Groups Directive* with respect to that *financial conglomerate* by imposing obligations on the *firm*. Further material on this can be found in *PRU 8.4* (Cross sector groups) and ~~SUP 16.7.73R~~ SUP 16.7.82R and ~~SUP 16.7.74R~~ SUP 16.7.83R (reporting requirements with respect to *financial conglomerates*).

...

#### Reports from groups

16.3.25 G If this chapter requires the submission of a report covering a *group*, a single report may be submitted, and so satisfy the requirements of all *firms* in the *group*. Such a report should contain the information required from all of them, meet all relevant due dates and indicate all the *firms* on whose behalf



it is submitted; if necessary a separate covering sheet should list the *firms* on whose behalf a report is submitted. Nevertheless, the requirement to provide a report, and the responsibility for the report, remains with each *firm* in the *group*. However, reporting requirements that apply to a *firm*, by reason of the *firm* being a member of a *financial conglomerate*, are imposed on only one member of the *financial conglomerate* (see, for example, ~~SUP 16.7.73R~~ SUP 16.7.82R).

...

16.7.5 G Applicable rules and guidance on financial reports (see SUP 16.7.1G)

Firm category	Applicable rules and guidance
<i>Bank, other than an EEA bank with permission for cross border services only</i>	<del>SUP 16.7.7R - SUP 16.7.15R</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
<i>Building society</i>	<del>SUP 16.7.16R - SUP 16.7.19R</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
...	
<i>Securities and futures firm</i> (Note 1)	<del>SUP 16.7.22R - SUP 16.7.34G</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
<i>Investment management firm</i>	<del>SUP 16.7.35R - SUP 16.7.41R</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
<i>Personal investment firm</i>	<del>SUP 16.7.42G - SUP 16.7.53G</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
...	
<i>ELMI</i>	<del>SUP 16.7.64R - SUP 16.7.66R</del> <del>SUP 16.7.73R - SUP 16.7.74R</del> <u>SUP 16.7.82R - SUP 16.7.83R</u>
...	

...

After ~~SUP 16.7.72R~~ SUP 16.7.81G, insert the following new rules, ~~SUP 16.7.73R~~ and ~~16.7.74R~~ SUP 16.7.82R and SUP 16.7.83R:

Financial conglomerates

- 16.7.7382 R (1) A *firm* that is a member of a *financial conglomerate* must submit financial reports to the *FSA* in accordance with the table in SUP 16.7.7483R if:
- (a) it is at the head of an *FSA regulated EEA* ~~EEA~~ *financial conglomerate*; or
  - (b) its *Part IV permission* contains a relevant *requirement*.
- (2) In (1)(b), a relevant *requirement* is one which:
- (a) applies SUP 16.7.7483R to the *firm*; or
  - (b) applies SUP 16.7.7483R to the *firm* unless the *mixed financial holding company* of the *financial conglomerate* to which the *firm* belongs submits the report required under this *rule* (as if the *rule* applied to it).
- 16.7.7483 R Table Financial reports from a member of a financial conglomerate (see SUP 16.7.7382R)

...

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(PROFESSIONAL INDEMNITY INSURANCE FOR PROFESSIONAL FIRMS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 149 (Evidential provisions);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 August 2004.

**Amendments to the Interim Prudential sourcebook for investment businesses**

- D. The Interim Prudential sourcebook for investment businesses is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Professional Indemnity Insurance for Professional Firms) Instrument 2004.

By order of the Board  
15 July 2004

## Annex

### Amendment to the Interim Prudential sourcebook for investment businesses

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 2.3 Professional Indemnity Insurance

2.3.1 R A *firm* must effect and maintain at all times adequate professional indemnity insurance cover for all the business activities which it carries on, or for which it is responsible.

- 2.3.2 ~~E~~  
G (1) ~~To effect and maintain adequate professional indemnity insurance cover a *firm* should obtain cover which is at least equivalent to the requirements of its *designated professional body* which were in force immediately before commencement.~~
- (2) ~~Compliance with (1) may be relied upon by the FSA as tending to establish compliance with *IPRU(INV)* 2.3.1.~~
- (3) ~~Contravention of (1) may be relied upon by the FSA as tending to establish contravention of *IPRU(INV)* 2.3.1.~~ In assessing the adequacy of a *firms'* professional indemnity insurance cover for the purposes of *IPRU(INV)* 2.3.1R, the *FSA* may have regard to a *firm's* compliance with the professional indemnity insurance requirements of its *designated professional body* in force at the time.

**IDENTIFICATION OF CONTRACTS OF INSURANCE INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 August 2004.

**Amendments to the Authorisation manual**

- C. The Authorisation manual is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Identification of Contracts of Insurance Instrument 2004.

By order of the Board  
15 July 2004

## Annex

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

AUTH App 5.3.6 G ~~The FSA has consulted (in CP150 (The Authorisation manual—consultation on draft guidance on the identification of contracts of insurance)) on draft~~ Guidance describing how the FSA identifies contracts of insurance is in AUTH App 6 (Guidance on the Identification of Contracts of Insurance).

...

After AUTH Appendix 5 insert the following new appendix:

AUTH App 6. Guidance on the Identification of Contracts of Insurance

6.1 Application

6.1.1 G This chapter is relevant to any *person* who needs to know what activities fall within the scope of the *Act*.

6.2 Purpose of guidance

6.2.1 G The purpose of this *guidance* is to set out:

(1) at AUTH App 6.5 the general principles; and

(2) at AUTH App 6.6 the range of specific factors;

that the FSA regards as relevant in deciding whether any arrangement is a contract of insurance.

6.2.2 G This *guidance* includes (at AUTH App 6.7) a number of examples, showing how the factors have been applied to reach conclusions with respect to specific categories of business. Further examples may be published from time-to-time.

6.3 Background

6.3.1 G The business of effecting or carrying out contracts of insurance is subject to prior *authorisation* and regulation by the FSA. (There are some limited exceptions to this requirement, for example, for breakdown insurance.)

- 6.3.2 G The *Regulated Activities Order*, which sets out the activities for which *authorisation* is required, does not attempt an exhaustive definition of a ‘contract of insurance’. Instead, it makes some specific extensions and limitations to the general common law meaning of the concept. For example, it expressly extends the concept to fidelity bonds and similar contracts of guarantee, which are not contracts of insurance at common law, and it excludes certain *funeral plan contracts*, which would generally be contracts of insurance at common law. Similarly, the *Exemption Order* excludes certain trade union provident business, which would also be insurance at common law. One consequence of this is that common law judicial decisions about whether particular contracts amount to ‘insurance’ or ‘insurance business’ are relevant in defining the scope of the *FSA’s authorisation* and regulatory activities, as they were under predecessor legislation.
- 6.3.3 G The Courts have not fully defined the common law meaning of ‘insurance’ and ‘insurance business’, since they have, on the whole, confined their decisions to the facts before them. They have, however, given useful guidance in the form of descriptions of contracts of insurance.
- 6.3.4 G The best established of these descriptions appears in the case of *Prudential v. Commissioners of Inland Revenue* [1904] 2 KB 658. This case, read with a number of later cases, treats as insurance any enforceable contract under which a ‘provider’ undertakes:
- (1) in consideration of one or more payments;
  - (2) to pay money or provide a corresponding benefit (including in some cases services to be paid for by the provider) to a ‘recipient’;
  - (3) in response to a defined event the occurrence of which is uncertain (either as to when it will occur or as to whether it will occur at all) and adverse to the interests of the recipient.
- 6.4 Limitations of this guidance
- 6.4.1 G Although what appears below is the *FSA’s* approach, it cannot state what the law is, as that is a matter for the Courts. Accordingly, this *guidance* is not a substitute for adequate legal advice on any transaction.
- 6.4.2 G The list of principles and factors is not closed and this *guidance* by no means covers all types of insurance-like business.
- 6.4.3 G The *FSA* will consider each case on its facts and on its merits.
- 6.4.4 G In some cases transactions with the same commercial purpose or economic effect may be classified differently, ie some as insurance and some as non-insurance.
- 6.5 General principles

- 6.5.1 G The starting point for the identification of a contract of insurance is the case of *Prudential v. Commissioners of Inland Revenue* [1904] 2 KB 658, from which the description set out in *AUTH* App 6.3.4G is drawn. Any contracts that fall outside that description are unlikely to be contracts of insurance.
- 6.5.2 G The *FSA* will interpret and apply the description in *AUTH* App 6.3.4G in the light of applicable legislation and common law, including case law.
- 6.5.3 G In particular, if the common law is unclear as to whether or not a particular contract is a contract of insurance, the *FSA* will interpret and apply the common law in the context of and in a way that is consistent with the purpose of the *Act* as expressed in the *FSA*'s statutory objectives.
- 6.5.4 G The *FSA* will apply the following principles of construction to determine whether a contract is a contract of insurance.
- (1) In applying the description in *AUTH* App 6.3.4G, more weight attaches to the substance of the contract, than to the form of the contract. The form of the contract is relevant (see *AUTH* App 6.6.8G (3) and (4)) but not decisive of whether a contract is a contract of insurance: *Fuji Finance Inc. v. Aetna Life Insurance Co. Ltd* [1997] Ch. 173 (C.A.).
  - (2) In particular, the substance of the provider's obligation determines the substance of the contract: *In re Sentinel Securities* [1996] 1 WLR 316. Accordingly, the *FSA* is unlikely to treat the provider's or the customer's intention or purpose in entering into a contract as relevant to its classification.
  - (3) The contract must be characterised as a whole and not according to its 'dominant purpose' or the relative weight of its 'insurance content': *Fuji Finance Inc. v. Aetna Life Insurance Co. Ltd* [1997] Ch. 173 (C.A.).
  - (4) Since only contracts of marine insurance and certain contracts of insurance effected without consideration are required to be in writing, a contract of insurance may be oral or may be expressed in a number of documents.
- 6.6 The factors
- 6.6.1 G Contracts under which the provider has an absolute discretion as to whether any benefit is provided on the occurrence of the uncertain event, are not contracts of insurance. This may be the case even if, in practice, the provider has never exercised its discretion so as to deny a benefit: *Medical Defence Union v. Department of Trade and Industry* [1979] 2 W.L.R. 686. The degree of discretion required and the matters to which it must relate are illustrated in *AUTH* App 6.7.1G (Example 1: discretionary medical schemes).



- 6.6.2 G The ‘assumption of risk’ by the provider is an important descriptive feature of all contracts of insurance. The ‘assumption of risk’ has the meaning in (1) and (3), derived from the case law in (2) and (4) below. The application of the ‘assumption of risk’ concept is illustrated in *AUTH* App 6.7.2G (Example 2: disaster recovery business).
- (1) Case law establishes that the provider's obligation under a contract of insurance is an enforceable obligation to respond (usually, by providing some benefit in the form of money or services) to the occurrence of the uncertain event. This *guidance* describes the assumption of that obligation as the ‘assumption’ by the provider of (all or part of) the insured risk. ‘Transfer of risk’ has the same meaning in this *guidance*.
  - (2) The case law referred to in (1) is *Prudential v. Commissioners of Inland Revenue* [1904] 2 KB 658, read with *Hampton v. Toxteth Co-operative Provident Society Ltd* [1915] 1 Ch. 721 (C.A.), *Department of Trade and Industry v. St Christopher Motorists Assoc. Ltd* [1974] 1 All E.R. 395, *Medical Defence Union v. Department of Trade and Industry* [1979] 2 W.L.R. 686 and *Wooding v. Monmouthshire and South Wales Mutual Indemnity Soc. Ltd* [1939] 4 All E.R. 570 (H.L.).
  - (3) The *FSA* recognises that there is a line of case law in relation to *long-term insurance business* that establishes that a contract may be a contract of insurance even if, having effected that contract, the provider ‘trades without any risk’. The *FSA* accepts that the insurer's risk of profit or loss from insurance business is not a relevant descriptive feature of a contract of insurance. But in the *FSA*'s view that is distinct from and does not undermine the different proposition in (1).
  - (4) The case law referred to in (3) is *Flood v. Irish Provident Assurance Co. Ltd* [1912] 2 Ch. 597 (C.A.), *Fuji Finance Inc. v. Aetna Life Insurance Co. Ltd* [1995] Ch. 122, *Re Barrett; Ex parte Young v. NM Superannuation Pty Ltd*, (1992) 106 A.L.R. 549, *Fuji Finance Inc. v. Aetna Life Insurance Co. Ltd* [1997] Ch. 173 (C.A.).
- 6.6.3 G Contracts, under which the amount and timing of the payments made by the recipient make it reasonable to conclude that there is a genuine pre-payment for services to be rendered in response to a future contingency, are unlikely to be regarded as insurance. In general, the *FSA* expects that this requirement will be satisfied where there is a commercially reasonable and objectively justifiable relationship between the amount of the payment and the cost of providing the contract benefit.
- 6.6.4 G Contracts under which the provider undertakes to provide periodic maintenance of goods or facilities, whether or not any uncertain or adverse event (in the form of, for example, a breakdown or failure) has occurred, are unlikely to be contracts of insurance.

- 6.6.5 G Contracts under which, in consideration for an initial payment, the provider stands ready to provide services on the occurrence of a future contingency, on condition that the services actually provided are paid for by the recipient at a commercial rate, are unlikely to be regarded as insurance. Contrast *AUTH* App 6.7.21G (Example 7: solicitors' retainers) with *AUTH* App 6.7.22G (Example 8: time and distance cover).
- 6.6.6 G The recipient's payment for a contract of insurance need not take the form of a discrete or distinct premium. Consideration may be part of some other payment, for example the purchase price of goods (*Nelson v. Board of Trade* (1901) 17 T.L.R. 456). Consideration may also be provided in a non-monetary form, for example as part of the service that an employee is contractually required to provide under a contract of employment (*Australian Health Insurance Assoc. Ltd v. Esso Australia Pty Ltd* (1993) 116 A.L.R. 253).
- 6.6.7 G Under most commercial contracts with a *customer*, a provider will assume more than one obligation. Some of these may be insurance obligations, others may not. The *FSA* will apply the principles in *AUTH* App 6.5.4G in the way described in (1) to (3) to determine whether the contract is a contract of insurance.
- (1) If a provider undertakes an identifiable and distinct obligation that is, in substance an insurance obligation as described in *AUTH* App 6.5.4G, then, other things being equal, the *FSA* is likely to find that by undertaking that obligation the provider has effected a contract of insurance.
  - (2) The presence of an insurance obligation will mean that the contract is a contract of insurance, whether or not that obligation is 'substantial' in comparison with the other obligations in the contract.
  - (3) The presence of an insurance obligation will mean that the contract is a contract of insurance, whether or not entering into that obligation forms a significant part of the provider's business. The *FSA* generally regards a provider as undertaking an obligation 'by way of business' if he takes on an obligation in connection with or for the purposes of his core business, to realise a commercial advantage or benefit.
- 6.6.8 G The following factors are also relevant.
- (1) A contract is more likely to be regarded as a contract of insurance if the amount payable by the recipient under the contract is calculated by reference to either or both of the probability of occurrence or likely severity of the uncertain event.
  - (2) A contract is less likely to be regarded as a contract of insurance if it requires the provider to assume a speculative risk (ie a risk carrying the possibility of either profit or loss) rather than a pure risk (ie a risk of loss only).

- (3) A contract is more likely to be regarded as a contract of insurance if the contract is described as insurance and contains terms that are consistent with its classification as a contract of insurance, for example, obligations of the utmost good faith.
- (4) A contract that contains terms that are inconsistent with obligations of good faith may, therefore, be less likely to be classified as a contract of insurance; however, since it is the substance of the provider's rights and obligations under the contract that is more significant, a contract does not cease to be a contract of insurance simply because the terms included are not usual insurance terms.

6.7 Examples

Example 1: discretionary medical schemes

- 6.7.1 G Medical schemes under which an employer operates or contributes to a fund, from which the employee has a right to a benefit (for example, a payment) on the occurrence of a specified illness or injury, are likely to be insurance schemes. This will be the case whether the employee makes any contribution to the fund, or the scheme is funded by the employer as an emolument. The scheme would not be insurance, however, if the employer has an absolute discretion whether or not to provide any benefit to the employee. Absolute discretion requires, for example, that the employer has an unfettered discretion both as to whether the employee will receive a benefit and as to the amount of that benefit. The absolutely discretionary nature of the benefits should also be clear from the terms of the scheme and any literature published about or in relation to it. If these requirements are met, it may not be relevant that, in practice, the employer has never refused to meet a valid claim under the scheme.

Example 2: disaster recovery business

- 6.7.2 G The disaster recovery provider sets up and maintains a range of IT and related facilities (PABX etc). The disaster recovery contracts so far considered by the *FSA* give the recipient, subject to certain conditions including an up front payment, priority access to all or a specified part of these facilities if a 'disaster' causes the failure of a similar business system on which the recipient relies. The provider sells access to the same facilities to a number of different recipients, both for use in response to 'disasters' and, more usually, for use in testing and refining the recipient's ability to switch to alternative systems in the event of a disaster.

- 6.7.3 G In principle, a significant part of disaster recovery business could potentially fall within the description of a contract of insurance set out in *AUTH* App 6.3.4G. The provider undertakes, in consideration of a payment, to provide the recipient with services (alternative facilities) in response to a defined event (a disaster), which is adverse to the interests of the recipient and the occurrence of which is uncertain. The risk dealt with under the disaster recovery contract is a pure risk (see *AUTH* App 6.6.8G(2)) and, at least at the commencement of the contract, the provider assumes that risk, within the terms of *AUTH* App 6.6.2G.
- 6.7.4 G However, the disaster recovery contracts considered by the *FSA* had two key features.
- (1) Priority access to facilities in the event of a disaster was expressed to be on a ‘first come, first served’ basis. The contracts provided expressly that if the facilities needed by recipient A were already in use, following an earlier invocation by recipient B, the provider’s obligation to recipient A was reduced to no more than an obligation of ‘best endeavours’ to meet A’s requirements. The entry into additional contracts of this kind did not increase the probability that the provider’s existing resources would be inadequate to meet all possible claims. The terms of the contract were such that there was no pattern of claims that would cause the provider to have to pay claims from its own resources.
  - (2) In general, the contracts were priced so that the total consideration collected from the recipient over the life of the contract bore a reasonable and justifiable relationship to the commercial cost of the services actually provided to the recipient (see *AUTH* App 6.6.5G). This was achieved, for example, by post-invocation charges levied according to the actual usage of services.
- 6.7.5 G Based on these features, the *FSA* reached the conclusion, with which the other terms of the contracts were consistent (*AUTH* App 6.6.8G (3)), that these disaster recovery contracts were not contracts of insurance.
- 6.7.6 G An important part of the conclusion in *AUTH* App 6.7.5G was that, although the provider assumed a risk at the outset of the contract, looking at the contract as a whole and interpreting the common law in the context of the *FSA*’s objectives (see *AUTH* App 6.6.2G) there was no relevant assumption of risk.
- (1) The presence or absence of an assumption of risk is an important part of the statutory rationale for the prudential regulation of insurance.

- (2) In *Medical Defence Union v. Department of Trade and Industry* [1979] 2 W.L.R. 686, the Court accepted that since there was no common law definition of a contract of insurance, the meaning of the term ‘fell to be construed in its context according to the general law’. The Court recognised that in deciding whether a contract was a contract of insurance for the purposes of the Insurance Companies Act 1974, the ‘context’ included the purpose of the regulatory statute.
- (3) Accordingly, when the common law is unclear, the *FSA* will assess the desirability of regulating a particular contract as insurance in the light of the statutory objectives in the *Act*. The *FSA* will use that assessment as an indicator of whether or not a sufficient assumption of risk is present for the contract to be classified as a contract of insurance at common law.
- (4) In the case of disaster recovery contracts, the fact that there was no pattern of claims that would cause the provider to have to pay claims from its own resources led the *FSA* to conclude that there was no relevant assumption of risk by the disaster recovery provider.

Example 3: manufacturers' and retailers' warranties

- 6.7.7 G Under a simple manufacturer’s or retailer’s warranty the purchase price of the goods includes an amount, in consideration of which the manufacturer undertakes an obligation (the warranty) to respond (without further expense to the purchaser) to specified defects in the product that emerge within a defined time after purchase. When the warranty operates, the manufacturer or retailer provides repairs or replacement products in response to a defined event (the emergence of a latent defect in the product), which is adverse to the interests of the purchaser and the occurrence of which is uncertain. In summary, therefore, a simple manufacturer’s or retailer’s warranty is an identifiable and distinct obligation that is similar to and capable of being described as an insurance obligation in substance under *AUTH* App 6.3.4G.
- 6.7.8 G Notwithstanding *AUTH* App 6.7.7G, the *FSA*’s view is that an obligation that is of the same nature as a seller's or supplier's usual obligations as regards the quality of the goods or services is unlikely to be an insurance obligation in substance.
- 6.7.9 G The *FSA* is unlikely to classify a contract containing a simple manufacturer’s or retailer’s warranty as a contract of insurance, if the *FSA* is satisfied that the warranty does no more than crystallise or recognise obligations that are of the same nature as a seller's or supplier's usual obligations as regards the quality of the goods or services.

- 6.7.10 G For the purpose of *AUTH* App 6.7.9G, an obligation is likely to be of the same nature as the seller's or supplier's usual obligations as regards the quality of goods or services if it is an obligation of the seller to the buyer, assumed by the seller in consideration of the purchase price, which:
- (1) implements, or bears a reasonable relationship to, the seller's statutory or common law obligations as regards the quality of goods or services of that kind; or
  - (2) is a usual obligation relevant to quality or fitness in commercial contracts for the sale of goods or supply of services of that kind.

Example 4: separate warranty transactions and extended warranties

- 6.7.11 G It follows from *AUTH* App 6.7.10G that the *FSA* is unlikely to be satisfied that an obligation in a contract of sale or supply is of the same nature as the seller's or supplier's usual obligations as regards the quality of goods or services, if that obligation has one or more of the following features:
- (1) it is assumed by a person other than the seller or supplier (a 'third party'); or
  - (2) it is significantly more extensive in content, scope or duration than a seller's usual obligations as to the quality of goods or services of that kind.
- 6.7.12 G Other things being equal, the *FSA* is likely to classify a contract of sale containing a warranty that has one or more of the features in *AUTH* App 6.7.11G as a contract of insurance. The features in *AUTH* App 6.7.11G (1) and (2) typically distinguish a 'third party' warranty and an 'extended warranty' from a 'simple' manufacturer's or retailer's warranty.
- 6.7.13 G If a warranty is provided by a third party, the *FSA* will usually treat this as conclusive of the fact that there are different transactions and an assumption or transfer of risk. This conclusion would not usually depend on whether the provider is (or is not) a part of the same group of companies as the manufacturer or retailer. But it will be the third party (who assumes the risk) that is potentially effecting a contract of insurance.
- 6.7.14 G A manufacturer or retailer may undertake a warranty obligation to his customer in a separate contract with the customer, distinct from the contract of sale or supply of goods or services. The *FSA* will examine the separate contract to see if it is a contract of insurance. But the mere existence of a separate warranty contract is unlikely to be conclusive by itself.

- 6.7.15 G A manufacturer or retailer may undertake an obligation to ensure that the customer becomes a party to a separate contract of insurance in respect of the goods sold. This would include, for example, a contract for the sale of a freezer, with a simple warranty in relation to the quality of the freezer, but also providing insurance (underwritten by an *insurer* and in respect of which the customer is the *policyholder*) covering loss of frozen food if the freezer fails. The *FSA* is unlikely to treat a contract containing an obligation of this kind as a contract of insurance. However, the manufacturer or retailer may be in the position of an intermediary and may be liable to regulation in that capacity.
- 6.7.16 G The *FSA* distinguishes the contract in *AUTH* App 6.7.15G from a contract under which the manufacturer or retailer assumes the obligation to provide the customer with an indemnity against loss or damage if the freezer fails, but takes out insurance to cover the cost of having to provide the indemnity to the customer. The obligation to indemnify is of a different nature from the seller's or supplier's usual obligations as regards the quality of goods or services and is an insurance obligation. By assuming it, other things being equal, the manufacturer or retailer effects a contract of insurance. The fact that the manufacturer or retailer may take out insurance to cover the cost of having to provide the indemnity is irrelevant.

Example 5: typical warranty schemes administered by motor dealers

- 6.7.17 G The following are examples of typical warranty schemes operated by motor dealers. Provided that, in each case, the *FSA* is satisfied that the obligations assumed by the dealer are not significantly more extensive in content, scope or duration than a dealer's usual obligations as to the quality of motor vehicles of that kind, the *FSA* would not usually classify the contracts embodying these transactions as contracts of insurance.
- (1) The dealer gives a verbal undertaking to the purchaser that during a specified period (usually 3 months) he will rectify any fault occurring with the vehicle. No money changes hands, and the dealer is responsible for meeting the warranty obligation.
  - (2) The dealer undertakes warranty obligations to his customer. The warranty obligations are either included in the contract for the sale of the vehicle or are set out in a separate contract between dealer and customer at the time of sale. The dealer administers his own warranty scheme and does not employ a separate company (for example a subsidiary) to run the scheme. In the event of a fault, the purchaser must contact the dealer, who is responsible for meeting the warranty obligation. The dealer decides whether or not to put money aside to meet potential claims.

- (3) The dealer purchases proprietary warranty booklets issued by an administration company. These booklets contain 'terms and conditions' under which the dealer undertakes warranty obligations to the customer. The dealer sells these 'products' to his customer under a separate contract or inflates the price of the vehicle to include them as part of the sale of the vehicle. The administration company administers any claims that arise. The financial arrangements are that the dealer charges his customer for the warranty, passing a fee to the administration company for the purchase of the booklet and any administration relating to the processing of claims. The dealer retains all monies (less administration fee) received from the sale of the warranties and keeps any surplus after claims have been paid. The dealer is responsible for meeting the warranty obligation.
- (4) The dealer undertakes warranty obligations to his customer. The warranty obligations are either included in the contract for the sale of the vehicle or are set out in a separate contract between dealer and customer at the time of sale. The dealer employs an administration company to handle all the claims and associated administrative work. The administration company usually has access to a bank account, funded by the dealer and specifically set aside to meet warranty claims. The administration company authorises and pays warranty claims from the bank account in accordance with the dealer's instructions. The dealer ultimately decides on the amount of claims payable from this account and retains all surplus monies. The dealer is responsible for meeting the warranty obligation.

#### Example 6: tax investigation schemes

- 6.7.18 G When self-assessment for income tax was first introduced, a number of providers set up schemes connected with their tax accounting and tax advisory services. In consideration of an annual fee, the provider undertakes to deal with any enquiries or investigations that the Inland Revenue might launch into the self-assessment that the provider completes for the recipient. The event covered by these schemes (an investigation) is both uncertain and adverse to the interests of the recipient, who would, if the scheme were not in place, have to devote resources to dealing with the investigation. Accordingly, these schemes fall within the description of a contract of insurance (see *AUTH* App 6.3.4G).



- 6.7.19 G Some providers argued that these schemes amount to nothing more than a ‘manufacturer’s warranty’ of their own work, within the scope of *AUTH* App 6.7.7G (Example 3: manufacturers’ and retailers’ warranties). However, the Inland Revenue is expected to make a significant number of random checks of self-assessment forms, irrespective of the quality of the work done by the provider. These random checks are also covered by the schemes. The *FSA* concluded, therefore, that these schemes were not analogous to manufacturers’ warranties and that the better view was that they were contracts of insurance.

Example 7: solicitors' retainers

- 6.7.20 G A contract under which a provider undertakes, in consideration of an initial payment, to stand ready to provide, or to procure the provision of, legal services on the occurrence of an uncertain event (for example, if the recipient is sued), is capable of being construed as a contract of insurance (see *AUTH* App 6.3.4G). Indeed, *legal expenses* insurance is commonplace.
- 6.7.21 G If, however, a contract of this kind were structured so that the recipient was charged at a commercial rate for any legal services in fact provided, the *FSA*’s approach will be to treat the arrangement as non-insurance. This is principally because, by taking on obligations of this kind, the provider does not assume a relevant risk (see *AUTH* App 6.7.6G). The position might be different if the solicitor carries the additional obligation to pay for alternative legal services to be provided if the solicitor is unable to act. In that case, the *FSA*’s approach will be to examine all the elements of the contract to determine whether the substance of the solicitor’s obligation (see *AUTH* App 6.5.4G(2)) is to insure, or to give legal advice for a fee.

Example 8: contracts providing for ultimate repayment of any indemnity (‘time and distance cover’)

- 6.7.22 G A contract under which a provider agrees to meet a specified obligation on behalf of the recipient (for example an obligation to pay for the re-purchase of shares or to meet a debt) immediately that obligation falls due, subject to later reimbursement by the recipient, would be a contract of insurance if in all other respects it fell within the description of such contract (see *AUTH* App 6.3.4G). This is principally because the provider assumes the risk that an immediate payment will be required and, depending on the terms of the contract, may also assume the risk that the recipient will be unable to make future repayments (see *AUTH* App 6.6.2G).

**COMPLAINTS SOURCEBOOK (MORTGAGE AND GENERAL INSURANCE  
TRANSITIONAL COMPLAINTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance);
  - (4) section 226 (Compulsory jurisdiction);
  - (5) section 229 (Awards);
  - (6) section 234 (Industry funding);
  - (7) paragraph 13 of schedule 17 (Authority's procedural rules); and
  - (8) articles 9 and 12 of the Financial Services and Markets Act 2000 (Transitional Provisions) (Complaints Relating to General Insurance and Mortgages) Order 2004 (SI 2004/454).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 31 October 2004.

**Amendments to the Disputes resolution: Complaints sourcebook**

- D. The Dispute resolution: Complaints sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Complaints Sourcebook (Mortgage and General Insurance Transitional Complaints) Instrument 2004.

By order of the Board  
15 July 2004

Amended by Addendum  
17 August 2004

## Annex A

### Amendments to the Disputes resolution: Complaints sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Transitional provisions

(1)	Material provision to which transitional applies	(3)	(4) Transitional provision	Transitional provision: dates in force	(6) Handbook provision coming into force
...					
<u>10</u>	<u>DISP 1</u>	<u>R</u>	<p><u>Where, at the <i>relevant commencement date</i>, a <i>firm</i> is still dealing with a complaint that is capable of being referred to the <i>Financial Ombudsman Service</i> as a <i>relevant transitional complaint</i>:</u></p> <p>(1) <u>it may continue to try to resolve the complaint in accordance with the complaints procedures that applied previously; but</u></p> <p>(2) <u>it must, within eight weeks of the <i>relevant commencement date</i>, send the complainant a response which satisfies <i>DISP 1.4.5R</i>, unless <i>DISP 1.4.3AR</i> or <i>DISP 1.4.9R</i> applies.</u></p>	<p><u>31 October 2004 (for a complaint to which the <i>MCAS Scheme</i> applied immediately before that date)</u></p> <p><u>14 January 2005 (for a complaint to which the <i>GISC Facility</i> applied immediately before that date)</u></p>	<u>31 October 2004</u>
<u>11</u>		<u>G</u>	<p><u><i>DISP TP10</i> recognises that where a <i>firm</i> has already received, but only partly completed the handling of, a complaint which is capable of becoming a <i>relevant</i></u></p>		

			<u>transitional complaint, it may not always be practicable to handle the complaint in accordance with DISP 1 after the relevant commencement date.</u>		
--	--	--	---	--	--

...

1.1.5R Except as otherwise specified, references to a "complaint" in this chapter include a complaint which is capable of becoming a *relevant new complaint* or a relevant transitional complaint.

...

1.3.2R *DISP 1.4 – DISP 1.6* also apply to any complaints that are capable of becoming *relevant new complaints* or relevant transitional complaints, unless *DISP 1.3.3R* applies.

...

1.3.4G Under the *Ombudsman Transitional Order* and the *Mortgage and General Insurance Complaints Transitional Order*, a complaint received by a *firm*, either before or after *commencement*, relating to an act or omission relating to business which was not a regulated activity at the time of the matter complained of is capable of becoming a *relevant new complaint* or a *relevant transitional complaint*. A *firm* is expected to handle such complaints in accordance with *DISP 1*. However, where a *firm* has already received, but only partly completed the handling of, such a complaint by *commencement*, *DISP 1.4.6R* recognises that this may not always be practicable.

...

Complaints being dealt with at commencement

1.4.6R Where, at *commencement*, a *firm* is still dealing with a complaint that is capable of being referred to the *Financial Ombudsman Service* as a *relevant new complaint*:

- (1) ~~it may continue to try to resolve the complaint in accordance with its pre-*commencement* complaints procedures; but~~
- (2) ~~it must, within eight weeks of *commencement*, send the complainant a response which satisfies *DISP 1.4.5R*, unless *DISP 1.4.3AR* or *DISP 1.4.9R* applies. [deleted]~~

...

2.1.3R A reference in this chapter to a "complaint":

- (1) includes part of a complaint; and
- (2) under the *Compulsory Jurisdiction* includes all or part of a *relevant new complaint* and all or part of a relevant transitional complaint.

...

Complaints (other than relevant new complaints or relevant transitional complaints)

2.2.1G The following conditions will need to be satisfied before a complaint (other than a *relevant new complaint* or relevant transitional complaint) can be dealt with ...

...

#### Relevant transitional complaints

2.2.2AG (1) Article 2 of the Mortgage and General Insurance Complaints Transitional Order provides that (subject to certain modifications) the Compulsory Jurisdiction applies to a *relevant transitional complaint*, provided that:

- (a) the act or omission is that of a person ("R") who, at the time of that act or omission, was subject to a former scheme;
- (b) R was an authorised person on or after the relevant commencement date;
- (c) the act or omission occurred in the carrying on by R of an activity to which that former scheme applied; and
- (d) the complainant is eligible and wishes to have the complaint dealt with under the new scheme.

(2) For the purposes of (1)(d), the Mortgage and General Insurance Complaints Transitional Order enables the *Ombudsman*, if he considers it appropriate, to treat the complainant as eligible if he would have been entitled to refer an equivalent complaint to the *former scheme* in question immediately before the *relevant commencement date*.

(3) The Mortgage and General Insurance Complaints Transitional Order enables *relevant transitional complaints* to be handled, so far as possible, under the *Financial Ombudsman Service* procedures, but provides for the *rules* of the former schemes to apply or be taken into account in certain circumstances.

...

2.3.1R ...

- (2) ... or where the *firm* or *VJ participant* has not objected to the *Ombudsman* considering the complaint.

...

2.4.2G *Eligible complainants* are those falling within one of the classes of *person* specified in *DISP 2.4.3R*; and

...

or, in relation to *relevant complaints*, those specified in the *Ombudsman Transitional Order* or the *Mortgage and General Insurance Complaints Transitional Order* (see *DISP 2.4.14G*, ~~and~~ *DISP 2.4.15G*, *DISP 2.4.15AG*, *DISP 2.4.15BG* and *DISP App 1.3.1G*).

...

2.4.14G In respect of a *relevant new complaint* or a *relevant transitional complaint*, where the complainant is not eligible in accordance with *DISP 2.4*, article 3(3) of the *Ombudsman Transitional Order* and article 2(3) of the *Mortgage and General Insurance Complaints Transitional Order* provides that the *Ombudsman* may, nonetheless, if he considers it appropriate...

...

2.4.15AG Article 2(4) of the *Mortgage and General Insurance Complaints Transitional Order* provides that, in the case of a *relevant transitional complaint*, where the *former scheme* in question is the *GISC facility*, a complainant is not to be treated as an *eligible complainant* unless:

- (1) he is an individual; and
- (2) he is acting otherwise than solely for the purposes of his business.

2.4.15BG Article 2(5) of the *Mortgage and General Insurance Complaints Transitional Order* provides that, in the case of a *relevant transitional complaint*, where the *former scheme* in question is the *MCAS scheme*, a complainant is not to be treated as an *eligible complainant* if:

- (1) the complaint does not relate to a breach of the Mortgage Code published by the Council of Mortgage Lenders;
- (2) the complaint concerns physical injury, illness, nervous shock or their consequences; or
- (3) the complainant is claiming a sum of money that exceeds £100,000.

...

2.6.3AG Under article 2 of the *Mortgage and General Insurance Complaints Transitional Order*, the *Ombudsman* can also consider a *relevant transitional complaint* under the *Compulsory Jurisdiction* where it relates to an act or omission of a *firm* which was, immediately before the *relevant commencement date*, subject to a *former scheme*, provided that:

- (1) the act or omission occurred in the carrying on by that *firm* of an activity to which that *former scheme* applied; and
- (2) the complainant is eligible and wishes to have the complaint dealt with under the new scheme.

...

3.1.4R Except as otherwise specified, references in this chapter to a "complaint" include:

- (1) a *relevant new complaint* and a *relevant transitional complaint*; and
- (2) part of a complaint or a *relevant new complaint* or a *relevant transitional complaint*.

...

3.1.6G The *Ombudsman Transitional Order* and the *Mortgage and General Insurance Complaints Transitional Order* provides, with some exceptions (see *DISP 2.2.2G* and *DISP 2.2.2AG* (scope of Compulsory Jurisdiction and Relevant transitional complaints), *DISP 2.3.2G* (time limits), *DISP 2.4.14G* and *DISP 2.4.15R* (*eligible complainant*) and *DISP 3.8.2G* and *DISP 3.8.2AG* (determinations) for *relevant new complaints* and *relevant transitional complaints* to be determined in accordance with the requirements of the *Financial Ombudsman Service*.

...

3.3.2AG Under article 4(2) of the *Mortgage and General Insurance Complaints Transitional Order*, the *Ombudsman*, in deciding whether a *relevant transitional complaint* is to be dismissed without consideration of its merits, must take into account whether an equivalent complaint would have been so dismissed under the *former scheme* in question, as it had effect immediately before the *relevant commencement date*.

...

3.8.2AG In determining, in relation to a *relevant transitional complaint*, what is fair and reasonable in all the circumstances of the case and what amount (if any) constitutes fair compensation for the purposes of section 229(2)(a) of the *Act*, the *Ombudsman* is required, under article 5(2) of the *Mortgage and General Insurance Complaints Transitional Order*, to take into account what determination might have been expected to be made under the *former scheme* in question and what amount (if any) might have been expected to have been awarded or recommended by way of compensation under that scheme, in relation to an equivalent complaint dealt with under the *former scheme* immediately before the *relevant commencement date*.

...

3.9.4AG In determining, in relation to a *relevant transitional complaint*, what amount (if any) constitutes fair compensation for the purposes of section 229(2)(a) of the *Act*, the *Ombudsman* is required under article 5(2) of the *Mortgage and General Insurance Complaints Transitional Order* to take into account what amount (if

any) might have been expected to have been awarded or recommended by way of compensation under that scheme, in relation to an equivalent complaint dealt with under the former scheme immediately before the relevant commencement date.

...

3.10.2G Under article 11 of the *Ombudsman Transitional Order* and article 11 of the *Mortgage and General Insurance Complaints Transitional Order*, any information held by any *person* responsible for the operation of a *former scheme* in connection with the operation of a *former scheme* may be disclosed by that *person* (after commencement or, as the case may be, the relevant commencement date) to *FOS Ltd* or to an *Ombudsman* without contravening any restriction on disclosure of that information (imposed by statute or otherwise) to which that *person* was subject. But *FOS Ltd* or the *Ombudsman* is subject to any restrictions on disclosure (and exceptions) which would have applied to the former holder of that information.

3.10.3G Article 11 of the *Ombudsman Transitional Order* and article 11 of the *Mortgage and General Insurance Complaints Transitional Order* does not, however, prevent the application of section 31(4A) of the Data Protection Act 1998. ...



## Annex B

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

<i>former scheme</i>	<p>(1) <u>(except in relation to a <i>relevant transitional complaint</i>)</u> any of the following:</p> <p>(a) ...</p> <p>...</p> <p>(h) ...;</p> <p>(2) <u>(in relation to a <i>relevant transitional complaint</i>)</u></p> <p>(a) <u>the <i>GISC facility</i>; or</u></p> <p>(b) <u>the <i>MCAS scheme</i>.</u></p>
<u><i>GISC facility</i></u>	<u>The Dispute Resolution Facility established by the General Insurance Standards Council.</u>
<u><i>MCAS scheme</i></u>	<u>Mortgage Code Arbitration Scheme.</u>
<u><i>Mortgage and General Insurance Complaints Transitional Order</i></u>	<u>The Financial Services and Markets Act 2000 (Transitional Provisions)(Complaints Relating to General Insurance and Mortgages) Order 2004 (SI 2004/454)</u>
<u><i>relevant commencement date</i></u>	<p><u>(as defined in article 1 of the <i>Mortgage and General Insurance Complaints Transitional Order</i>):</u></p> <p>(a) <u>in relation to a complaint which relates to an activity to which, immediately before 14 January 2005, the <i>GISC Facility</i> applied, the beginning of 14 January 2005;</u></p> <p>(b) <u>in relation to a complaint which relates to an activity to which, immediately before 31 October 2004, the <i>MCAS scheme</i> applied, the beginning of 31 October 2004.</u></p>

<i>relevant complaint</i>	<p>(1) (in DISP) a <i>relevant existing complaint</i> or a <i>relevant new complaint</i> or a <i>relevant transitional complaint</i>.</p> <p>(2)...</p>
<i>relevant transitional complaint</i>	<p><u>(in accordance with the <i>Mortgage and General Insurance Complaints Transitional Order</i>) a complaint referred to the <i>Financial Ombudsman Service</i> after the <i>relevant commencement date</i> which relates to an act or omission occurring before that date if:</u></p> <p>(a) <u>the act or omission is that of a <i>person</i> ("R") who, at the time of that act or omission, was subject to a <i>former scheme</i>;</u></p> <p>(b) <u>R was an <i>authorised person</i> on or after the <i>relevant commencement date</i>;</u></p> <p>(c) <u>the act or omission occurred in the carrying on by R of an activity to which that <i>former scheme</i> applied; and</u></p> <p>(d) <u>the complainant is eligible and wishes to have the complaint dealt with under the <i>new scheme</i>.</u></p>

## ADDENDUM

### COMPLAINTS SOURCEBOOK (MORTGAGE AND GENERAL INSURANCE TRANSITIONAL COMPLAINTS) INSTRUMENT 2004

Annex A to this instrument is amended by the insertion of the underlined text and the deletion of the text that is struck through.

#### Transitional provisions

(1)	(2) Material provision to which transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
...					
<del>1013</del>	<del>DISP</del> <u>DISP</u> 1	R	Where, at the <i>relevant commencement date</i> ...	...	31 October 2004
<del>1114</del>		G	<u>DISP TP</u> <del>1013R</del> recognises that...		

**COMPLAINTS AGAINST THE FSA SCHEME (AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) (a) paragraphs 7 and 8 of Schedule 1;  
(b) section 157(1) (Guidance); and
  - (2) (a) article 2(2) of the Financial Services and Markets Act 2000 (Commencement No.4 and Transitional Provisions) Order 2001 (SI 2001/2364); and  
(b) article 18 of the Financial Services and Markets Act 2000 (Transitional Provisions) (Ombudsman Scheme and Complaints scheme) Order 2001 (SI2001/2326).

**Commencement**

- B. This instrument comes into force on 1 October 2004.

**Amendments to the Complaints against the FSA sourcebook**

- C. The Complaints against the FSA sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Complaints against the FSA Scheme (Amendment) Instrument 2004.

By order of the Board 15 July 2004

**Annex Amendments to the Complaints against the FSA sourcebook**

In this Annex underlining indicates new text and striking through indicates deleted text.

Complaints against the FSA Transitional

provisions TP 1 Transitional Provisions

Complaints against the FSA

COAF 1 There are no transitional provisions in COAF. However, COAF  
2 (Transitional Complaints Scheme) is itself a separate Transitional  
Complaints Scheme covering complaints against the FSA or  
PIA, IMRO or SFASFA in respect of matters arising before  
the date that section 19 (the general prohibition) of the Act  
comes into force.

2 Table: Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to		Transitional provision	Transitional	Handbook
	which the			provision:	provision:
	transitional			dates in	coming
	provision applies			force	into force
1	Every provision in COAF	G	The FSA and the <i>Complaints Commissioner</i> will continue to treat complaints received before 1 October 2004 in accordance with COAF as in force before amendment by the <i>Complaints against the FSA Scheme (Amendment) Instrument 2004</i> .	From 1 October 2004 for eighteen months	3 September 2001

1.1 Introduction ...

1. 1.1.2 G The *complaints scheme* provides that there may be two distinct stages for each complaint. In the first stage, the FSA itself will investigate any complaint that meets the requirements of the *complaints scheme* (see COAF 1.4 (Coverage and scope of the scheme)) and take whatever action to resolve the matter it thinks appropriate. A complaint will normally only proceed to the second stage if the complainant is dissatisfied with the FSA's determination of his complaint or how it has been handled. This second stage consists of investigation of the complaint by the *Complaints Commissioner*, followed, wherever he finds for the complainant, by his recommendation to the FSA on the form of redress, if any, that is appropriate in the circumstances.

.1.1.3 G (1) ...

(2) ....

(3) Each provision in the *complaints scheme* is, consistent with the style and format of the Handbook, identified by the letter "G". It nevertheless constitutes a definitive

statement of the *complaints scheme* which the *FSA* is required to maintain.

...

1.1.5 G In this *complaints scheme*, “complaint” means any expression of dissatisfaction about the manner in which the *FSA* has carried out, or failed to carry out, its functions under the *Act* other than its legislative functions.

...

## 1.2 Application

1. 1.2.1 G Anyone directly affected by the way in which the *FSA* has carried out its functions, or anyone acting directly on such a *person’s* behalf, may bring a complaint under the *complaints scheme*, provided the complaint meets the requirements of the *complaints scheme* (see *COAF* 1.4 (Coverage and scope of the scheme)). This includes *firms* and *issuers*issuers of *listed securities*listed securities and any *customer* or prospective *customer*, whether an individual or a *body corporate*, or *market counterparty*. Groups, such as trade associations, may bring a complaint under the *complaints scheme* where they themselves have been directly affected by the *FSA’s* actions or inactions. Groups may also bring complaints on behalf of one or more named members that have been directly affected by the *FSA’s* actions or inactions, but cannot bring complaints on behalf of their members generally if it is not apparent that all of the group’s members have been directly affected.

2. 1.2.2 G The *complaints scheme* applies in relation to complaints made about the way in which the *FSA* has carried out, or failed to carry out, its functions

under the *Act*. The *FSA* is also applying the main elements of the *complaints scheme* in respect of complaints against the *FSA* arising in connection with the exercise of its functions under previous legislation and in respect of complaints made against *PIA*, *IMRO* and *SFA*. Those arrangements are set out in the *transitional complaints scheme*.

## 1.3 The Complaints Commissioner

1.3.1 G (1) ...

(2) In appointing the *Complaints Commissioner*, the *FSA* is advised by an appointment panel comprising the Deputy Chairman of the *FSA*, the Chairmen of the Practitioner and Consumer Panels *Consumer Panels* established under sections 9 and 10 of the *Act* and another person who is independent of the *FSA*.

...

1. 1.3.3 G The *FSA* will provide remunerate the *Complaints Commissioner* and will provide him with sufficient financial and other resources to allow him to fulfil his role under the *complaints scheme* properly equip him with suitable accommodation and staff. No member of the *Complaints Commissioner’s* staff may be an employee of, or perform any duties for, the *FSA*.

2. 1.4 Coverage and scope of the scheme

1.4.1 G (1) ...

~~.(2) Because the *complaints scheme* is concerned with complaints about the way in which the FSA has discharged its functions, it does not cover complaints about the actions of the *Financial Ombudsman Service* or the *Financial Services Compensation Scheme*. [deleted]~~

.(3) To be eligible to make a complaint under the *complaints scheme*, a *person* (see COAF 1.2.1G) must be seeking a remedy, (which for this purpose may include an apology, see COAF 1.5.5G) in respect of some inconvenience, distress or loss which the *person* has suffered as a result of being directly affected by the FSA's actions or inaction.

Exclusions from the scheme

1.4.2 G Each of the following is excluded from the *complaints scheme*:

- .(1) ...
- .(2) ...; and
- (3) ...; and

. (4) complaints about the actions, or inactions, of the *Financial Ombudsman Service* or the *Financial Services Compensation Scheme*.

Circumstances under which the FSA will not investigate

1.4.2A G The FSA will not investigate a complaint under the *complaints scheme* which it reasonably considers amounts to no more than dissatisfaction with the FSA's general policies or with the exercise of, or failure to exercise, a discretion where no unreasonable, unprofessional or other misconduct is alleged.

Complaints that are more appropriately dealt with in another way ~~Alternative remedies~~

1.4.3 G The FSA will not investigate a complaint under the *complaints scheme* which it reasonably considers: (1) could have been, or would be, more appropriately dealt with in another way (for example by referring the matter to the *Tribunal* or by the institution of other legal proceedings); or

~~(2) amounts to no more than dissatisfaction with the FSA's general policies or with the exercise of discretion where no unreasonable, unprofessional or other misconduct is alleged.~~

Investigations that may be deferred

1.4.4 G ...

~~Certain complaints to be in writing~~

1.4.5 G (1) ~~A complaint made orally by a consumer will be investigated by the FSA. If the complaint cannot be resolved quickly, the FSA will write to the complainant inviting him to confirm its understanding of the complaint.~~

~~(2) Other persons complaining orally will be asked to confirm their complaint in writing (this includes in electronic form), and the FSA will not normally investigate a complaint until the complainant has done so.[deleted]~~

...

## 1.5 Procedure

The FSA's initial response to complaints Telling complainants how the Complaints Scheme works

1.5.1 G The FSA will acknowledge a complaint within five working days of receipt. It will, in response to a each complaint made in a *durable medium*, send to theeach complainant a leaflet, in a *durable medium*, explaining how the *complaints scheme* works, including details of his right to refer the complaint to the *Complaints Commissioner* if he is dissatisfied with the way in which the FSA has dealt with it (see COAF 1.5.56G ).

The FSA's initial analysis of complaints

1.5.1A G On receiving a complaint, the FSA will determine whether it can be dealt with under the *complaints scheme* and whether it can be dealt with under the 'fast track' complaints handling procedure (see COAF 1.5.1DG).

1.5.1B G Where the FSA does not investigate a complaint under the *complaints scheme*, either because the FSA considers it to be outside of the scope of the *complaints scheme* or for another reason described in COAF (see COAF 1.2 (Application) and COAF 1.4 (Coverage and scope of the scheme)), the FSA will write to the complainant explaining why this is the case and informing him of his right to ask the *Complaints Commissioner* to review the decision. The FSA will do this within four weeks of receiving the complaint or, where COAF 1.5.1GG(1) applies, within four weeks of the complainant notifying the FSA that he is dissatisfied with the way his complaint has been handled.

Asking for information in writing

1.5.1C G (1) A complaint made orally by a *consumer* will be investigated by the FSA. However, if the FSA requires clarification from the complainant as to the nature or scope of the complaint, the FSA may either invite the complainant to confirm or clarify the details of the complaint, or it may communicate its understanding of the nature or scope of the complaint to the *consumer*, in a *durable medium*.

. (2) Other *persons* complaining orally will be asked to confirm their complaint in a *durable medium*.

. (3) The FSA may ask the complainant to explain what remedy he is seeking or to provide any factual information that supports his complaint in a *durable medium*.

.(4) The FSA may not be able to progress its investigation of a complaint until it has received the information described in (1) to (3), as it needs to understand from the complainant what the complaint is about if it is to investigate it properly.



'Fast track' complaints handling procedure

1.5.1D G (1) The FSA will use a 'fast track' procedure for investigating a complaint where it believes the complaint:

.(a) is of low impact from the perspective of both the complainant and the FSA (for example, it is about a minor administrative mistake); and

.(b) can be dealt with within five *business days* of the FSA first receiving communication of the complaint, in a way that the FSA believes remedies any adverse effect on the complainant.

(2) If, after initiating the 'fast track' complaints handling procedure for a particular complaint, the FSA then considers that the complaint does not meet the criteria in (1), it will then deal with it as described at COAF 1.5.1HG.

1.5.1E G The 'fast track' procedure will involve the complaint being dealt with under the *complaints scheme* by the area of the FSA most closely concerned with the matter complained of.

1.5.1F G For all complaints dealt with under the 'fast track' procedure, the FSA will advise the complainant of his right to refer his complaint to the FSA's Company Secretariat if he believes the complaint has not been resolved or is otherwise dissatisfied with the way it has been dealt with.

Handling of 'fast track' complaints referred to the Company Secretariat

1.5.1G G (1) If the complainant refers his complaint to the FSA's Company Secretariat, the FSA will acknowledge this complaint within five *business days* of receiving this referral.

(2) The FSA will review the complaint, at this point, to make sure that it falls within the scope of the *complaints scheme*. If the FSA considers that the complaint is outside the *complaints scheme*, it will follow the procedures in COAF 1.5.1BG. Otherwise, it will handle the complaint in accordance with COAF 1.5.2G.

'Non-fast track' complaints: the FSA's initial response

1.5.1H G Where a complaint is not suitable for the 'fast track' complaints handling procedure, the FSA will acknowledge it within five *business days* of receipt and will deal with it in accordance with COAF 1.5.2G.

Stage 1: Investigation of complaints by the FSA

1. 1.5.2 G The FSA will arrange for an initial investigation by its own staff of any complaint which is a complaint under the terms of the *complaints scheme* and which does not come within satisfies the provisions of COAF 1.4.1G to COAF 1.4.6G. That investigation will be carried out by a suitably senior member of staff who has not previously been involved in the matter complained of, with a view to resolving the matter to the complainant's satisfaction. The FSA will seek to resolve the complaint as quickly as possible.—

2. 1.5.3 G The FSA will seek to resolve the complaint as quickly as possible. The FSA will either complete aim to ensure that all investigations are completed within eight weeks. If it has not completed the investigation of a complaint within four weeks, or it will write to the complainant within this time setting out a reasonable timescale within which it plans to deal with the complaint. If the FSA has not already confirmed whether or not the complaint will be admitted to the complaints scheme, the FSA will include this informationthe FSA will write to the complainant reporting ~~that fact.~~

What are the possible outcomes for the complainant?

1. 1.5.4 G If the FSA concludes that a complaint is well founded, it will tell the complainant what it proposes to do to remedy the matters of complaint complained of.

2. 1.5.5 G Remedying a well founded complaint may include offering the

complainant an apology, taking steps to rectify an error or, if appropriate, the offer of a compensatory payment on an ex-gratia basis. If the FSA decides not to uphold or to reject a complaint, it will give its reasons for doing so to the complainant, and will inform the complainant of his right to ask the Complaints Commissioner to review the FSA's decision.

1.5.6 G Complainants who are dissatisfied with the outcome of an investigation, or who are dissatisfied with the FSA's progress in investigating a complaint, may refer the matter to the *Complaints Commissioner*, who may decide will consider whether or not to carry out his own investigation.

When will the If the FSA does not investigate a complaint, will the Complaints Commissioner investigate a complaint that the FSA has not investigated? do so?

1. 1.5.7 G When the FSA has told a complainant in writing that it will not investigate his complaint, as provided for by COAF 1.5.1AG, it will also notify the Complaints Commissioner of this fact. Within ten working days of ~~receiving a complaint, the FSA will notify the Complaints Commissioner of each complaint which it decides not to investigate and will inform the complainant that it has done so.~~ The Complaints Commissioner will not review the FSA's decision unless the complainant requests this. Where the complainant does request this, tThe Commissioner will, after considering any representations from the complainant and the FSA, then decide whether the complaint falls within the scope of the *complaints scheme* and, if so, whether to conduct an investigation.

2. 1.5.8 G (1) If a complaint is referred or notified to the *Complaints Commissioner* before the FSA has had the opportunity to conduct or complete an investigation, the *Complaints Commissioner* will consider whether it would be desirable to allow the FSA that opportunity before conducting his own investigation.

(2) Paragraph (1) also applies to a complaint received by the Complaints Commissioner when he is conducting a Stage 2 investigation into another complaint from the same complainant.

...

## Stage 2: Conduct of investigations by the *Complaints Commissioner*

1.5.10 G The *Complaints Commissioner* may conduct an investigation in whatever manner he thinks appropriate including obtaining, at the *FSA*'s expense, such external resources as may be reasonable. In considering what is appropriate, the *Complaints Commissioner* will take into account the need to ensure that complaints are dealt with fairly, quickly and cost effectively.

1.5.10A G In performing his functions in accordance with the *complaints scheme*, the *Complaints Commissioner* must at all times act independently of the *FSA*. ...

1.5.18 G The *Complaints Commissioner* may, if he thinks it appropriate, recommend that the *FSA* remedy the matters complained of, as described in *COAF* 1.5.5G. take either or both of the following steps:

- ~~(1) remedy the matters of complaint; or~~
- ~~(2) make a compensatory payment to the complainant. ...~~

### Responding to the Complaints Commissioner

1.5.24 G In deciding how it should respond to a report from the *Complaints Commissioner*, the *FSA* will, as well as having regard to its statutory objectives and the considerations set out in section 2(3) or 73(1) of the *Act*, normally take into account the following:

- .(1) ...
- .(2) ...
- .(3) whether what has gone wrong is at the operational or administrative level (rather than in relation to matters of policy or where the *FSA*'s ~~actions have necessarily had to reflect a balancing of conflicting interests and complex issues~~);

- (4) ... ..

### Annual Reports

1.6.2 G The *Complaints Commissioner* will each year submit a report to the *FSA* Board, for publication.;

.(1) a report on investigations concluded by him during the 12-month period ending 31 March. The report may include information concerning trends in the subject matter of complaints and on the general lessons which he considers the *FSA* should learn; and

.(2) information on his activities during that year, including such matters as the approach he adopted to handling different types of complaint and the extent to which he has met his service standards for dealing with complaints. (The *Complaints Commissioner* will set these standards himself.)

### Transitional complaints scheme ...

2.1.5 G (1) Where the *FSA* is required to make a particular arrangement as part of the *transitional complaints scheme*, this is recognised in the following text by use of

the word 'must'. In contrast, where a provision in the *transitional complaints scheme* states that someone "will" do something, this denotes that the *FSA* is committing itself or the *Complaints Commissioner* to some action which, though not specifically required, is nevertheless viewed as necessary to give effect to the intentions of the *Act*.

- (2) Each provision in the *transitional complaints scheme* is, consistent with the style and format of the *Handbook*, identified by the letter "G". It nevertheless constitutes a definitive statement of the *transitional complaints scheme* which the *FSA* is maintaining.

...

#### 2.1.9 G In this *transitional complaints scheme*:

(1) "complaint" means any expression of dissatisfaction about the manner in which the *FSA* has carried out, or failed to carry out, its statutory functions (other than its legislative functions) and about the manner in which *PIA*, *IMRO* or *SFA* have carried out their functions arising in connection with the Financial Services Act 1986 (other than their functions of making rules and issuing guidance);

(2) ...

(3) ... ..

## 2.2 Application

1. 2.2.1 G Anyone directly affected by the way in which the *FSA*, *PIA*, *IMRO* or *SFA* has carried out their functions, or anyone acting directly on such a *person's* behalf, may bring a complaint under the *transitional complaints scheme*, provided the complaint meets the requirements of the *transitional complaints scheme* (see *COAF* 2.3 (Coverage and scope of the scheme)). This includes *firms* and issuers of listed securities and any customer or prospective customer, whether an individual or a body corporate, or market counterparty. Groups, such as trade associations, may bring a complaint under the *transitional complaints scheme* where they themselves have been directly affected by the *FSA's* actions or inactions. Groups may also bring complaints on behalf of one or more named members that have been directly affected by the *FSA's* actions or inactions, but cannot bring complaints on behalf of their members generally if it is not apparent that all of the group's members have been affected.

2. 2.3 Coverage and scope of the scheme

2.3.1 G (1) ...

(2) The *transitional complaints scheme* does not cover complaints about ~~the actions of the Financial Ombudsman Service, the Financial Services Compensation Scheme, the Investors' Compensation Scheme or of any independent complaints investigation body established by *PIA*, *IMRO* or *SFA*.~~[deleted]

(3) ...

(4) To be eligible to make a complaint under the *transitional complaints scheme*, a *person* (see *COAF* 2.2.1G) must be seeking a remedy (which for this purpose may include an apology, see *COAF* 2.4.5G) in respect of some inconvenience, distress or loss which the

person has suffered as a result of being directly affected by the actions or inaction of the *FSA, PIA, IMRO* or *SFA*.

#### Exclusions from the scheme

2.3.2 G Each of the following is excluded from the *transitional complaints scheme*:

(1) ...

...

(4) ....; and

(5) complaints about the actions, or inactions, of the *Financial Ombudsman Service*, the *Financial Services Compensation Scheme*, the Investors' Compensation Scheme or of any independent complaints investigation body established by *PIA, IMRO* or *SFA*.

#### Circumstances under which the FSA will not investigate

2.3.2A G The *FSA* will not investigate a complaint under the *transitional complaints scheme* which it reasonably considers amounts to no more than dissatisfaction with the general policies of the *FSA* or of *PIA, IMRO* or *SFA* or with the exercise of a discretion by any such body where no unreasonable, unprofessional or other misconduct is alleged.

#### Complaints that are more appropriately dealt with in another way Alternative remedies

2.3.3 G The *FSA* will not investigate a complaint under the *transitional complaints scheme* which it reasonably considers: (1) could have been, or would be, more appropriately dealt with in another way (for example by referring the matter to the Financial Services Tribunal or to the committees, tribunals and appeal bodies or to any successor tribunal of *PIA, IMRO* or *SFA* or by the institution of other legal proceedings); or  
(2) ~~amounts to no more than dissatisfaction with the general policies of the *FSA* or of *PIA, IMRO* or *SFA* or with the exercise of discretion by any such body where no unreasonable, unprofessional or other misconduct is alleged.~~

#### Investigations that may be deferred

2.3.4 G ...

#### ~~Certain complaints to be in writing~~

2.3.5G (1) ~~— A complaint made orally by a consumer will be investigated by the *FSA*. If the complaint cannot be resolved quickly, the *FSA* will write to the complainant inviting him to confirm its understanding of the complaint.~~

~~(2) Other persons complaining orally will be asked to confirm their complaint in writing (this includes in electronic form) and the *FSA* will not normally investigate a complaint until the complainant has done so.[deleted]~~

...

2.4 Procedure

## The FSA's initial response to complaints

2.4.1 G The FSA will acknowledge a complaint within five *business days* working days of receipt. and will deal with it in accordance with COAF 2.4.2G-2.4.4G. Where the complaint is in a durable medium, the FSA It will send each complainant a leaflet, in a *durable medium*, explaining how the *transitional complaints scheme* works, including details of his right to refer the complaint to the *Complaints Commissioner* if he is dissatisfied with the way in which the FSA has dealt with it (see COAF 2.4.6G).

2.4.1A G Where the FSA does not investigate a complaint under the *transitional complaints scheme*, either because the FSA considers it to be outside of the scope of the *complaints scheme* or for another reason described in COAF (see COAF 2.2 (Application) and COAF 2.3 (Coverage and scope of the scheme)), the FSA will write to the complainant explaining why this is the case and informing him of his right to ask the *Complaints Commissioner* to review the decision. The FSA will do this within four weeks of receiving the complaint.

### Putting complaints in writing

2.4.1B G (1) A complaint made orally by a consumer will be investigated by the FSA. However, if the FSA requires further clarification from the complainant as to the nature or scope of the complaint, the FSA may either invite the complainant to confirm or clarify the details of the complaint, or it may communicate its understanding of the nature or scope of the complaint to the consumer, in a durable medium.

. (2) Other persons complaining orally will be asked to confirm their complaint in a durable medium.

. (3) The FSA may ask the complainant to explain what remedy he is seeking or to provide any factual information that supports his complaint in a durable medium.

. (4) The FSA may not be able to progress its investigation of a complaint until it has received the information described in (1) to (3), as it needs to understand from the complainant what the complaint is about if it is to investigate it properly.

### Stage 1: Investigation of complaints by the FSA

1. 2.4.2 G The FSA will arrange for an initial investigation by its own staff of any complaint which is a complaint under the terms of the *transitional complaints scheme* and which does not come within satisfies the provisions of COAF 2.3.21G to COAF 2.3.56G. That investigation will be carried out by a suitably senior member of staff who has not previously been involved in the matter complained of, with a view to resolving the matter to the complainant's satisfaction. The FSA will seek to resolve the complaint as quickly as possible.

2. 2.4.3 G The FSA will seek to resolve the complaint as quickly as possible. The FSA will either complete aim to ensure that all investigations are completed within eight weeks. If it has not completed the investigation of a complaint within four weeks, or it will write to the complainant within this time setting out a reasonable timescale within which it plans to deal with the complaint. If the FSA has not already confirmed whether or not the complaint will be admitted to the *complaints scheme*, the FSA will include this information the FSA will write to

the complainant reporting ~~that fact~~.

What are the possible outcomes for the complainant?

1. 2.4.4 G If the *FSA* concludes that a complaint is well founded it will tell the complainant what it proposes to do to remedy the matters of complaint complained of.
2. 2.4.5 G Remedying a well-founded complaint may include offering the complainant an apology and taking steps to rectify an error. If the *FSA* decides not to uphold to reject a complaint, it will give its reasons for doing so to the complainant, and will inform the complainant of his right to ask the *Complaints Commissioner* to review the *FSA*'s decision.
3. 2.4.6 G Complainants who are dissatisfied with the outcome of an investigation, or who are dissatisfied with the *FSA*'s progress in investigating a complaint, may refer the matter to the *Complaints Commissioner*, who may decide will consider whether or not to carry out his own investigation.

When will the If the *FSA* does not investigate a complaint, will the *Complaints Commissioner* investigate a complaint that the *FSA* has not investigated?do so?

2.4.7 G When the *FSA* has told a complainant in writing that it will investigate his complaint, as provided for by *COAF* 2.4.1BG, it will also notify the *Complaints Commissioner* of this fact. Within ten working days of receiving a complaint, the *FSA* will notify the *Complaints Commissioner* of each complaint which it decides not to investigate and will inform the complainant that it has done so. The *Complaints Commissioner* will not review the *FSA*'s decision unless the complainant requests this. Where the complainant does request this, Tthe *Commissioner* will, after considering any representations from the complainant and the *FSA*, then decide whether the complaint falls within the scope of the *transitional complaints scheme* and, if so, whether to conduct an investigation.

- 2.4.8 G (1) If a complaint is referred or notified to the *Complaints Commissioner* before the *FSA* has had the opportunity to conduct or complete an investigation, the *Complaints Commissioner* will consider whether it would be desirable to allow the *FSA* that opportunity before conducting his own investigation;
- (2) Paragraph (1) also applies to a complaint received by the *Complaints Commissioner* when he is conducting a Stage 2 investigation into another complaint by the same complainant.

...

Stage 2: Conduct of investigations by the *Complaints Commissioner*

2.4.10 G The *Complaints Commissioner* may conduct an investigation in whatever manner he thinks appropriate including obtaining, at the *FSA*'s expense, such external resources as may be reasonable. In considering what is appropriate, the *Complaints Commissioner* will take into account the need to ensure that complaints are dealt with fairly, quickly and cost effectively.

2.4.10A G In performing his functions in accordance with the *transitional complaints*

*scheme*, the *Complaints Commissioner* must at all times act independently of the *FSA*, *PIA*, *IMRO* and *SFA*.

...

#### Responding to the Complaints Commissioner

2.4.22 G The *FSA* must, in any case where the *Complaints Commissioner* has reported that a complaint is well founded or where he has criticised the *FSA*, *PIA*, *IMRO* or *SFA* in his report, inform the *Complaints Commissioner* and the complainant of the steps which it proposes to take by way of response.

...

#### Annual Reports

2.5.2 G The *Complaints Commissioner* will each year submit a report to the *FSA* Board, for publication:

. (1) a report on investigations concluded by him during the 12-month period ending 31 March. The report may include information concerning trends in the subject matter of complaints and on the general lessons which he considers the *FSA* should learn; and

.(2) information on his activities during that year, including such matters as the approach he adopted to handling different types of complaint and the extent to which he has met his service standards for dealing

with complaints. (The *Complaints Commissioner* will set these standards himself.)



**HANDBOOK INTERPRETATION INSTRUMENT 2004**

**Commencement**

- A. This instrument comes into force on 1 August 2004.

**Amendments to the General provisions**

- B. The General provisions are amended in accordance with Annex A to this instrument.

**Amendments to other modules**

- C. The Threshold Conditions, the Credit unions sourcebook and the Recognised Investment Exchanges and Recognised Clearing Houses sourcebook are amended in accordance with Annex B to this instrument.

**Citation**

- D. This instrument may be cited as the Handbook Interpretation Instrument 2004.

Made under the authority of the Board

Mark Threipland  
Chief Counsel, EU and Handbook  
General Counsel's Division  
15 July 2004

## ANNEX A

### Amendments to GEN

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 2.1.5      D      This chapter applies to every *person* to whom a direction or requirement in the *Handbook* (~~that is, a provision with the status letter 'D' in the margin or heading~~) applies as if the *rules* in this chapter were part of that direction or requirement.
- ...
- 2.2.5      G      ~~Paragraphs 18 to 31~~ Chapter 6 of the Reader's Guide contains an explanation of the significance of the status letters R, D, P, C, E and G, and includes further information on *evidential provisions*.

## ANNEX B

### Amendments to other modules

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Amendments to the Threshold Conditions (COND)

2.1.1     ~~G~~ D     ....

...

2.2.1     ~~P~~ D     ...

...

2.2A.1   ~~G~~ D     ...

...

2.3.1     ~~P~~ D     ...

...

2.4.1     ~~P~~ D     ...

...

2.5.1     ~~P~~ D     ...

...

2.6.1     ~~G~~ D     ...

#### Amendments to the Credit unions sourcebook (CRED)

Insert the following as CRED 2.4.12 G:

2.4.12     G           The letter D is also used to indicate non-*FSA* legislative material, namely directly applicable EU and UK materials, such as directives, statutes and regulations. In such cases, the source material is clearly indicated.

#### Amendments to the Recognised Investment Exchanges and Recognised Clearing Houses sourcebook (REC)

1.2.2     G           (1)     Most of the provisions in this sourcebook are marked with a G (to indicate *guidance*) or an R (to indicate a *rule*). ~~In addition, there are q~~ Quotations from statute or statutory instruments which are not marked with ~~any~~ the letter "D" unless they form part of a piece of guidance. For

~~a **A** discussion of the status of provisions marked with a letter, see Chapter 6 of the Reader's Guide, and advice on all aspects of the structure, format and use of all parts of the Handbook (including this sourcebook), is included in the Reader's Guide.~~

2.2.1	<u>PD</u>	...
2.3.1	<u>PD</u>	...
2.3.2	<u>PD</u>	...
2.4.1	<u>PD</u>	...
2.4.2	<u>PD</u>	...
2.5.1	<u>PD</u>	...
2.5.2	<u>PD</u>	...
2.6.1	<u>PD</u>	...
2.6.2	<u>PD</u>	...
2.7.1	<u>PD</u>	...
2.7.2	<u>PD</u>	...
2.8.1	<u>PD</u>	...
2.8.2	<u>PD</u>	...
2.9.1	<u>PD</u>	...
2.9.2	<u>PD</u>	...
2.10.1	<u>PD</u>	...
2.10.2	<u>PD</u>	...
2.11.1	<u>PD</u>	...
2.11.2	<u>PD</u>	...
2.12.1	<u>PD</u>	...
2.12.2	<u>PD</u>	...
2.12.3	<u>PD</u>	...
2.13.1	<u>PD</u>	...
2.13.2	<u>PD</u>	...

2.14.1	<u>PD</u>	...
2.14.2	<u>PD</u>	...
2.15.1	<u>PD</u>	...
2.15.2	<u>PD</u>	...
2.16.1	<u>PD</u>	...
2.16.2	<u>PD</u>	...
2.17.2	<u>PD</u>	...
2.17.3	<u>PD</u>	...
6.3.2	<u>PD</u>	...

**INTERIM PRUDENTIAL SOURCEBOOK FOR BANKS (AMENDMENT NO 6)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 November 2004.

**Amendments to the Interim Prudential sourcebook for Banks**

- C. The Interim Prudential sourcebook for Banks is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Banks (Amendment No 6) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Interim Prudential sourcebook for Banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(BANK)), Volume 2, Chapter SE (Securitisation and Asset Transfer) as follows:

#### 1.3 ~~[deleted]~~Notification policy

6 ~~[deleted]~~A bank should give prior notification to the FSA when it proposes to act in any of the primary roles, either solely or jointly with one or more other parties. This should take place in reasonable time to allow the FSA to consider the proposal and raise any concerns that it may have.

- a) ~~The responsibility for achieving supervisory non-objection to a proposal rests with the bank itself.~~

...

#### 6.3 Additional policy relating to asset packages

...

6 ...

(g)~~[deleted]~~—The name of a company used as a vehicle for a scheme should not include the name of the performer of the primary role nor imply any connection with it.

- a) ~~Where the bank acts in a primary role, this also applies to members of the consolidated group.~~

...

#### 9.6.2 Treatment for first loss

13 The originating bank may make a choice of either deducting the amount of the credit enhancement from capital or including the assets within their risk weighted asset ratio under normal rules as if there had been no securitisation. The choice should be made at the outset, and maintained for the duration of the credit enhancement facility and be advised to the FSA. Where the credit enhancement is permanently reduced through the remittance of funds to the originator, and without recourse to the originator thereafter, the amount deducted from capital can be reduced accordingly.

9.6.3 Treatment for second loss

- 14 An originator providing a second loss facility (in an acceptable form) should deduct the amount of the facility from capital. Where the credit enhancement is permanently reduced through the remittance of funds to the originator, and without recourse to the originator thereafter, the amount deducted from capital can be reduced accordingly.

...

9.7.2 Treatment for first loss

- 16 First loss credit enhancement facilities provided by a sponsor or repackager should be deducted from capital. Where the credit enhancement is permanently reduced through the remittance of funds to the sponsor or repackager, and without recourse to the sponsor or repackager thereafter, the amount deducted from capital can be reduced accordingly.



**INTERIM PRUDENTIAL SOURCEBOOK FOR BANKS (AMENDMENT NO 7)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 November 2004.

**Amendments to the Interim Prudential sourcebook for Banks**

- C. The Interim Prudential sourcebook for Banks is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Banks (Amendment No 7) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Interim Prudential sourcebook for banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(BANK), Volume 2, Chapter LS as follows:

4.4 Definitions relevant to both components

4.4.1 *The stock of sterling liquid assets*

...

9 The stock of *sterling liquid assets* consists of:

...

- (e) sterling international bonds issued by certain EEA government and ~~or~~ ~~certain~~ international financial institutions, where they have been issued into Euroclear or Clearstream settlement systems;
- (f) Euro-denominated bonds issued by certain EEA governments and ~~or~~ ~~certain~~ international financial institutions, where they have been issued into Euroclear or Clearstream settlement systems and where they are eligible for use in ESCB monetary policy operations;
- (g) a range of Euro-denominated securities, where they are issued by the central governments and central banks of certain ~~the~~ EEA countries, where they are eligible for use in ESCB monetary policy operations, and where the relevant central bank of a country participating in EMU has agreed to act as a bank's custodian under the Correspondent Central Banking Model (CCBM);
  - a) Detailed lists of the bonds described in (d), (e), (f) and (g) above can be found on the Bank of England's website under OMO on the 'Eligible Securities' page (~~www.bankofengland.co.uk/eligsec.htm~~ www.bankofengland.co.uk/markets/money/eligiblesecurities.htm).
  - b) The FSA will automatically ~~extend~~ update the list of bonds that it considers banks may include in their stock of sterling liquid assets in line with the Bank of England's programme of ~~extending~~ reviewing its eligible securities ~~as outlined in the Bank's announcement of October 1998.~~
    - i) ~~This announcement (and other announcements)~~ All relevant announcements can be found on the Bank of England's website.
    - ii) The Bank of England will update its lists of eligible securities regularly.

...

**MULTILATERAL DEVELOPMENT BANK DEFINITION (AMENDMENT)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 October 2004.

**Amendments to the Handbook**

- D. The modules of the FSA's Handbook listed in column (1) are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Interim Prudential sourcebook for Banks (IPRU(BANK))	Annex A
Interim Prudential sourcebook for Building Societies (IPRU(BSOC))	Annex B
Interim Prudential sourcebook for Investment Businesses (IPRU(INV))	Annex C
Glossary of definitions	Annex D

**Citation**

- E. This instrument may be cited as the Multilateral Development Bank Definition (Amendment) Instrument 2004.

By order of the Board  
16 September 2004

## Annex A

### Amendments to the Interim Prudential sourcebook for Banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(BANK), Volume 1, Chapter BC Section 3.2.4 paragraph 6(a) as follows:

(a) asset items constituting claims on ~~multilateral development banks~~ multilateral development banks as defined in the Handbook Glossary and claims guaranteed by or collateralised by the securities issued by these institutions;

a) ~~[deleted] The following institutions, as set out in The Banking Consolidation Directive (formerly the SRD) and subsequent amendments, are considered as multilateral development banks:~~

- ~~i) African Development Bank (AfDB);~~
- ~~ii) Asian Development Bank (AsDB);~~
- ~~iii) Caribbean Development Bank (CDB);~~
- ~~iv) Council of Europe Development Bank~~
- ~~v) European Bank for Reconstruction and Development (EBRD);~~
- ~~vi) European Investment Bank (EIB);~~
- ~~vii) European Investment Fund (EIF);~~
- ~~viii) Inter American Development Bank (IADB);~~
- ~~ix) Inter American Investment Corporation (IAIC);~~
- ~~x) International Bank for Reconstruction and Development (IBRD) including International Finance Corporation (IFC); and~~
- ~~xi) Nordic Investment Bank (NIB).~~

...

Amend IPRU(BANK), Volume 1, Chapter TI Section 5.2 paragraph 4(b) as follows:

(b) it is a security issued by, or fully collateralised by claims on, a multilateral development bank as defined in the Handbook Glossary ~~listed in the Solvency Ratio Directive.~~

~~a) For the list of qualifying multilateral development banks, see the relevant chapter.~~

Amend IPRU(BANK), Volume 1, Chapter TI paragraph 46G (as inserted by the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004) as follows:

46 G A debt security is a *qualifying debt security* if:

(1)...

(2) it is issued by, or fully guaranteed by:

(a)...

(b) a multilateral development bank ~~listed in 3.2.4 of chapter BC~~ as defined in the Handbook Glossary;

...

## **Annex B**

### **Amendments to the Interim Prudential sourcebook for Building Societies**

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(BSOC), Volume 1, Annex 1B, 1B.4.1 (6) as follows:

Securities issued or guaranteed by multilateral development banks as defined in the Handbook Glossary (~~International Bank for Reconstruction and Development, International Finance Corporation, Inter-American Development Bank, Asian Development Bank, African Development Bank, Caribbean Development Bank, European Investment Bank, European Bank for Reconstruction and Development, Nordic Investment Bank, Council of Europe Resettlement Fund, European Investment Fund and Inter-American Investment Corporation~~).

## Annex C

### Amendments to the Interim Prudential sourcebook for Investment Businesses

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(INV), Chapter 3 (Financial resources for Securities and Futures Firms which are not Investment Firms) Appendix 35 Part 2 as follows:

#### PART 2

##### List of Supranational Organisations

a multilateral development bank;

~~The African Development Bank;~~

~~The Asian Development Bank;~~

The Bank for International Settlements;

~~The Caribbean Development Bank;~~

The Council of Europe;

Euratom (The European Atomic Energy Community);

Eurofina (The European Company for Financing of Railroad Rolling Stock);

~~The European Bank for Reconstruction and Development;~~

The European Coal and Steel Community;

The European Economic Community;

~~The European Investment Bank;~~

~~The Inter-American Development Bank;~~

~~The International Bank for Reconstruction and Development (World Bank);~~

~~The International Finance Corporation;~~

The International Monetary Fund.;

~~The Nordic Investment Bank.~~

...

Amend IPRU(INV), Chapter 5 (Interim Prudential Requirements for Former IMRO Firms), Appendix 1 as follows:

*exempt exposure* means an exposure:

...

(1) secured by marketable securities provided that such collateral exceeds the market value of the *exposure* by 150 per cent in the case of transactions relating to shares and by 50 per cent in relation to debt securities issued by a *credit institution*, a *member state* regional or local authority; or a multilateral development bank ~~the EIB, the IBRD, the IFC, the IADB, the Asian and African Development Banks, the Council of Europe Resettlement Fund, the Nordic Investment Bank and the Caribbean Development Bank.~~

Amend IPRU(INV), Chapter 10 (Financial resources for Securities and Futures Firms which are Investment Firms), Appendix 1 as follows:

*multilateral development bank* means ~~African Development Bank, Asian Development Bank, Caribbean Development Bank, Council of Europe Resettlement Fund, European Bank for Reconstruction and Development, European Investment Bank, Inter American Development Bank, International Finance Corporation, International Bank for Reconstruction and Development (IBRD) and Nordic Investment Bank (NIB);~~

...

*qualifying debt security* means a debt security which –

(1) (a) ...

(b) is issued or fully guaranteed by –

...

(vii) one of the following organisations -

- a multilateral development bank;
- ~~The African Development Bank;~~
- ~~The Asian Development Bank;~~
- The Bank for International Settlements;
- ~~The Caribbean Development Bank;~~
- The Council of Europe;
- Euratom (European Atomic Energy Community);
- Eurofina (European Company for Financing of Railroad Rolling Stock);
- ~~The European Bank for Reconstruction and Development;~~
- The European Coal and Steel Community;
- The European Economic Community;
- ~~The European Investment Bank;~~
- ~~The Inter American Development Bank;~~
- ~~The International Bank for Reconstruction and Development (World Bank);~~
- ~~The International Finance Corporation;~~
- The International Monetary Fund;
- ~~The Nordic Investment Bank;~~

Amend IPRU(INV), Chapter 10 (Financial resources for Securities and Futures Firms which are Investment Firms), Appendix 35 Part 2 as follows:

## **PART 2**

### **List of Supranational Organisations**

a multilateral development bank;

~~The African Development Bank;~~

~~The Asian Development Bank;~~

The Bank for International Settlements;

~~The Caribbean Development Bank;~~

The Council of Europe;

Euratom (The European Atomic Energy Community);

Eurofina (The European Company for Financing of Railroad Rolling Stock);

~~The European Bank for Reconstruction and Development;~~

The European Coal and Steel Community;

The European Economic Community;

~~The European Investment Bank;~~

~~The Inter American Development Bank;~~

~~The International Bank for Reconstruction and Development (World Bank);~~

~~The International Finance Corporation;~~

The International Monetary Fund;

~~The Nordic Investment Bank.~~



Amend IPRU(INV), Chapter 13 (Financial Resource Requirements for Personal Investment Firms) Appendix 13(1) as follows:

*qualifying debt security* a debt security which –

(a) ...

(iv) one of the following organisations:

- ~~a *multilateral development bank*;~~
- ~~The African Development Bank;~~
- ~~The Asian Development Bank;~~
- ~~The Caribbean Development Bank;~~
- ~~The Council of Europe;~~
- ~~The European Bank for Reconstruction and Development;~~
- ~~The European Investment Bank;~~
- ~~The Inter-American Development Bank;~~
- ~~The International Bank for Reconstruction and Development (World Bank);~~
- ~~The International Finance Corporation;~~
- ~~The Nordic Investment Bank;~~

...

## Annex D

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend the following definition as shown:

*multilateral development bank*      ~~(in ELM)~~ any of the following:  
African Development Bank (AfDB)  
Asian Development Bank (ASB)  
Caribbean Development Bank (CDB)  
Council of Europe Development Bank  
European Bank for Reconstruction & Development (EBRD)  
European Investment Bank (EIB)  
European Investment Fund (EIF)  
Inter-American Development Bank (IADB)  
Inter-American Investment Corporation (IAIC)  
International Bank for Reconstruction & Development (IBRD) including International Financial Corporation (IFC)  
Multilateral Investment Guarantee Agency (MIGA)  
Nordic Investment Bank (NIB)

**INTERIM PRUDENTIAL SOURCEBOOK FOR BUILDING SOCIETIES  
(AMENDMENT NO 8) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 November 2004.

**Amendments to the Interim Prudential sourcebook for Building Societies**

- C. The Interim Prudential sourcebook for Building Societies is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Building Societies (Amendment No 8) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Interim Prudential sourcebook for Building Societies

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend IPRU(BSOC), Volume 1, Chapter 10, Chapter SE (Securitisation and Asset Transfers) as follows

#### 1.3 ~~[deleted]~~Notification Policy

6 ~~[deleted]~~A bank should give prior notification to the FSA when it proposes to act in any of the primary roles, either solely or jointly with one or more other third parties. This should take place in reasonable time to allow the FSA to consider the proposal and raise any concerns that it might have.

- a) ~~The responsibility for achieving supervisory non-objection to a proposal rests with the bank itself.~~

...

#### 6.3 Additional policy relating to asset packages

...

6 ...

(g) ~~[deleted]~~—The name of a company used as a vehicle for a scheme should not include the name of the performer of the primary role nor imply any connection with it.

- a) ~~Where the bank acts in a primary role, this also applies to members of the consolidated group.~~

...

#### 9.6.2 Treatment for first loss

13 The originating bank may make a choice of either deducting the amount of the credit enhancement from capital or including the assets within their risk weighted asset ratio under normal rules as if there had been no securitisation. The choice should be made at the outset, and maintained for the duration of the credit enhancement facility and be advised to the FSA. Where the credit enhancement is permanently reduced through the remittance of funds to the originator, and without recourse to the originator thereafter, the amount deducted from capital can be reduced accordingly.

### 9.6.3 Treatment for second loss

- 14 An originator providing a second loss facility (in an acceptable form) should deduct the amount of the facility from capital. Where the credit enhancement is permanently reduced through the remittance of funds to the originator, and without recourse to the originator thereafter, the amount deducted from capital can be reduced accordingly.

...

### 9.7.2 Treatment for first loss

- 16 First loss credit enhancement facilities provided by a sponsor or repackager should be deducted from capital. Where the credit enhancement is permanently reduced through the remittance of funds to the sponsor or repackager, and without recourse to the sponsor or repackager thereafter, the amount deducted from capital can be reduced accordingly.

**INTERIM PRUDENTIAL SOURCEBOOK FOR INVESTMENT BUSINESSES  
(AMENDMENT NO 10) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power); and
  - (2) section 156 (General supplementary powers).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 November 2004.

**Amendments to the Interim Prudential sourcebook for Investment Businesses**

- D. The Interim Prudential sourcebook for Investment Businesses is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Interim Prudential Sourcebook for Investment Businesses (Amendment No 10) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Interim Prudential sourcebook for Investment Businesses

In this Annex, underlining indicates new text and striking through indicates deleted text.

Chapter 5, Appendix 1

#### GLOSSARY OF TERMS FOR CHAPTER 5 (FORMER IMRO FIRMS)

The following words or terms throughout Chapter 5 are to have the meanings given to them below if not inconsistent with the subject or context. If a defined term does not appear in the Chapter 5 glossary below, the definition ~~appearing in the Glossary~~ appearing in the *Glossary* applies.

...

*otc derivative* means interest rate and foreign exchange contracts covered by Annex ~~III~~ II to the ~~Solvency Ratio Directive~~ Banking Consolidation Directive and off balance sheet contracts based on equities which are not traded on a *recognised* or *designated investment exchange* or other exchange where they are subject to daily margin requirements, excluding any foreign exchange contract with an original maturity of 14 calendar days or less.

...

Chapter 13, Appendix 13(1)

...

#### Appendix 13 (1) Defined terms for Chapter 13

...

Category A firm a *personal investment firm* which is an *ISD investment firm*.

...

Category A2 firm a *Category A firm* whose *permission* does not include *dealing in investments as principal*; and which is not subject to a requirement preventing the holding or controlling of client money or custody assets.

Category A3 firm a *Category A firm* whose *permission* includes only *arranging* transactions in *investments, advising on investments* and ~~if applicable~~ *managing investments* but which is subject to a requirement not to hold or control client money or custody assets.

...

Category B2 firm a *Category B firm* whose *permission* does not include *dealing as principal*; and is not subject to a requirement preventing the holding or controlling of client money or custody assets.

Category B3 firm a *Category B firm* whose *permission* includes only *arranging* transactions in *life policies* and other insurance contracts, *advising on investments* and receiving and transmitting, on behalf of investors, orders in relation to *securities* and *units in collective investment schemes*; but which is subject to a requirement not to hold or control client money or custody assets.



**DISTANCE MARKETING DIRECTIVE (AMENDMENT) INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1)
    - (a) section 118(8) (Market abuse);
    - (b) section 138 (General rule-making power);
    - (c) section 139(1) and (4) (Miscellaneous ancillary matters);
    - (d) section 145 (Financial promotion rules);
    - (e) section 147 (Control of information rules);
    - (f) section 149 (Evidential provisions);
    - (g) section 156 (General supplementary powers);
    - (h) section 157(1) (Guidance);
    - (i) section 247 (Trust scheme rules); and
  - (2)
    - (a) regulation 6(1) of the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228);
    - (b) regulation 3 of the Electronic Commerce Directive (Financial Services and Markets Act 2000) Regulations 2002 (SI 2002/1775); and
    - (c) regulation 2 of the Financial Services and Markets Act 2000 (Fourth Motor Insurance Directive) Regulations 2002 (SI 2002/2706).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 9 October 2004.

**Amendments to the Handbook**

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Conduct of Business sourcebook (COB)	Annex A
Client Assets sourcebook (CASS)	Annex B
Credit Unions sourcebook (CRED)	Annex C
Electronic Commerce Directive sourcebook (ECO)	Annex D
Professional Firms sourcebook (PROF)	Annex E
Glossary of definitions	Annex F

**Citation**

- E. This instrument may be cited as the Distance Marketing Directive (Amendment) Instrument 2004.

By order of the Board  
16 September 2004

Amended by Addendum  
19 October 2004

## Annex A

### Amendment to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. The text shown amended is the text in COB, as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39). Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not struck through or underlined.

Transitional provisions TP 4

...

COB 5

...

Table: COB TR6: Distance Marketing Directive transitional rules (applicable to all firms)

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
-----	---	-----	-------------------------------	---	--

...					
3		R	<p>When an <i>insurer effects or carries out, or a firm manages the underwriting capacity of a Lloyd's syndicate as a managing agent at Lloyd's in relation to, a non-investment insurance contract</i> which is a <i>distance contract</i>, then either:</p> <p>(1) the <i>Distance Marketing Regulations</i> (<del>other than regulation 2(3)</del>) apply as if the <i>insurer or firm</i> was an <i>unauthorised person</i>; or</p> <p>...</p> <p><u>Delayed amendment of the Handbook for distance contracts</u></p>	From 9 October 2004 until 14 January 2005	
4	<u>Handbook</u>	R	<p>(1) <u>The amendments to the Handbook made by the Distance Marketing Directive Instrument 2004 and the Distance Marketing (Amendment) Instrument 2004 do not apply to a firm unless it has elected to comply with them.</u></p> <p>(2) <u>An election under (1) is irrevocable. The firm must make a record of the election and retain it for 6 years from 31 October 2004.</u></p>	From 9 October 2004 until 31 October 2004	<u>Already in force</u>

...

1.3.5 G *Firms* are reminded that the definition of *inter-professional business* does not include:

...

(3) ...;

(4) *corporate finance business*;

(4)(5) concluding a *distance contract* with a *retail customer*.

...

1.6.2 R Table Provisions of COB applied to stock lending activity  
This table belongs to COB 1.6.1R

COB	Subject
...	
<u>2.6</u>	<u>General provisions related to distance marketing, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i></u>
6.7	Cancellation and withdrawal, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i>
...	

...

1.6.4 R Table Provisions of COB applied to corporate finance business  
This table belongs to COB 1.6.3R

COB	Subject
...	
<u>2.6</u>	<u>General provisions related to distance marketing, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i></u>
<u>6.4.25R</u>	<u>Entering into a <i>distance contract</i> to accept deposits, but (a) as if <i>corporate finance business</i> was <i>accepting deposits</i> and (b) only in relation to <i>distance contracts</i> concluded with <i>retail customers</i></u>
6.7	Cancellation and withdrawal, but only in relation to <i>distance contracts</i> concluded with <i>retail customers</i>
...	

...

#### Distance contract

1.10.4 G not used

(1) To be a *distance contract*, a contract must be concluded under an 'organised distance sales or service-provision scheme' run by the contractual provider of the service who, for the purpose of the contract, makes exclusive use (directly or through an intermediary) of one or more *means of distance communication* up to and including the time at

which the contract is concluded. The expression 'organised distance sales or service-provision scheme' is not defined in the DMD, but:

- (a) recital 15 of the DMD states that contracts negotiated at a distance involve the use of *means of distance communication* which are used as part of such a scheme not involving the simultaneous physical presence of the supplier and the consumer; and
- (b) recital 18 of the DMD states that the expression is intended to exclude services provided on a strictly occasional basis and outside a commercial structure dedicated to the conclusion of *distance contracts*.

(2) So, in the FSA's view, this means that:

- (a) the *firm* must have put in place facilities designed to enable a *retail customer* to deal with it exclusively at a distance, such as facilities for a *retail customer* to deal with it purely by *post*, telephone, fax or the Internet. If a *firm* normally operates face-to-face and has no facilities in place enabling a *retail customer* to deal with it customarily by distance means, the DMD will not apply. A one-off transaction effected exclusively by distance means to meet a particular contingency or emergency will not be a *distance contract*; and
- (b) there must have been no simultaneous physical presence of the *firm* and the other party to the contract throughout the offer, negotiation and conclusion of the contract. So, for example, contracts offered, negotiated and concluded over the Internet, through a telemarketing operation or by *post* will normally be *distance contracts*. A *retail customer* may visit the local office of the *firm* in the course of the offer, negotiation or conclusion of the contract with that *firm*. Wherever, in the literal sense, there has been "simultaneous physical presence" of the *firm* and the *retail customer* at the time of such a visit, any ensuing contract will not be a *distance contract*.

...

#### Application of parts of the Distance Marketing Regulations

1.10.7 G *COB* implements most of the *Distance Marketing Directive* for *distance contracts* concluded by *firms*, the making or performance of which constitutes, or is part of, *designated investment business* or *accepting deposits*. However, certain aspects of the *Distance Marketing Directive* are implemented by provisions of the *Distance Marketing Regulations*, which apply in addition to *COB*, in particular:

- (1) regulation ~~4~~12 (Automatic cancellation of an attached distance contract) on which there is guidance in *COB* 6.7.51AG; and

(2) regulation ~~13~~14 (Payment by cards).

1.11 Application of COB in relation to deposits

1.11.1 G Table: Application of rules in COB in relation to deposits

Delete the existing table and replace with the following:

COB	Subject matter	Application for cash deposit ISAs	Application for other deposits
2.5.5 R	Exclusion of liability	√ ( <i>distance contract only</i> )	√ ( <i>distance contract only</i> )
2.6	General provisions related to distance marketing	√ ( <i>distance marketing only</i> )	√ ( <i>distance marketing only</i> )
3.5.5R to 3.5.7R 3.8.4R to 3.8.5E	Financial promotions	√	√
3.8.8R, 3.8.11R, 3.8.15R	Specific non-real time financial promotions	√ (if the <i>financial promotion</i> relates to a <i>structured deposit</i> )	√ (if the <i>financial promotion</i> relates to a <i>structured deposit</i> )
3.9.6R(1), 3.9.7AR and 3.9.8R	Direct offer financial promotions	√	X
6.1.4R, 6.1.5R, 6.2.2R, 6.4.13R, 6.5.2R(2), 6.5.3R, 6.5.42R	Product disclosure	√	X
6.4.25R	Pre-contract information when entering into a <i>distance contract</i> for <i>accepting deposits</i>	X	√ ( <i>distance contract only</i> )
6.4.27R to 6.4.31R	Exemptions for telephone sales; certain other <i>means of distance communication</i> ; and successive operations	√ ( <i>distance contract and other telephone sales only</i> )	√ ( <i>distance contract only</i> )

6.7.7R(1), 6.7.17R, 6.7.18R, 6.7.21R	Cancellable contracts	X	√ (distance contract only)
6.7.7R(3)	Cancellable contracts	√	X
6.7.10R(2), 6.7.10AR, 6.7.11R	Cancellation period	√	√ (distance contract only)
6.7.42R to 6.7.48R	Exercising the right to cancel	√	√ (distance contract only)
6.7.51R to 6.7.53R	Effects of, and obligations on, cancellation	√	√ (distance contract only)
Note:			
(1) Those <i>rules</i> marked with "X" do not apply; those marked with "√" do apply.			
(2) This Table lists rules imposing obligations. It does not list all application <i>rules</i> , exemptions, transitional <i>rules</i> or <i>guidance</i> .			

#### Exemption for firms which follow the Banking Code Guidance

1.11.2 R ~~[deleted]~~ (1) The *rules* in COB 1.11.3R do not apply in relation to *accepting deposits*, to a *firm* which subscribes to the "Guidance for subscribers" to the Banking Code (the 'Banking Code Guidance') issued by the British Banker's Association, the Building Societies Association and the Association for Payment Clearing Services [edition in force on 9 October 2004].

(2) In relation to a *firm* in (1) the provisions of the Banking Code Guidance in COB 1.11.3R apply as if they were *rules*.

1.11.3 R ~~[deleted]~~ Table: This table belongs to COB 1.11.2R(2)

(1) COB rules which do not apply	(2) Equivalent provisions of the Banking Code Guidance
COB 2.5 (Exclusion of liability)	[references in the Code which correspond to relevant COB rules to be added when settled]
COB 2.6 (General provisions related to distance contracts)	
COB 3.9.6R(2) and 3.9.8R (Direct offer financial promotions: cash	



deposit ISAs)	
<del>COB 6.1 to 6.5 (Key features)</del>	
<del>COB 6.7 (Cancellation and withdrawal)</del>	

...

- 2.5.1 R (1) This section (~~other than COB 2.5.5R~~) applies to a *firm* that conducts *designated investment business*.
- (2) This section (~~other than COB 2.5.3R and COB 2.5.4R~~) also applies to a *firm* which enters into a *distance contract to accept deposits* with a *retail customer*.

...

Limits on the exclusion of liability: designated investment business

- 2.5.3 R A *firm* must not, in any written or oral communication in connection with *designated investment business*, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability it may have to a *customer* (which for these purposes includes a *retail customer*) under the *regulatory system*.
- 2.5.4 R A *firm* must not, in any written or oral communication to a *private customer* in connection with *designated investment business*, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability not referred to in COB 2.5.3R unless it is reasonable for it to do so.

...

Limits on the exclusion of liability: distance contracts to accept deposits

- 2.5.5 R A *firm* must not, in any written or oral communication to a *retail customer* in connection with a *distance contract to accept deposits* with a *retail customer*, seek to exclude or restrict, or to rely on any exclusion or restriction of, any duty or liability it may have to a *retail customer* under COB (~~but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)~~).

...

## 2.6 General provisions related to distance ~~contracts~~ marketing

Application

- 2.6.1 R This section applies to a *firm* which:
- (1) conducts *designated investment business* with or for a *retail customer* ~~in relation to a distance contract~~;

- (2) ~~enters into a distance contract to accept~~ a deposits ~~with~~ from a retail customer (but see *COB 1.11.2R* (Exemption for firms which follow the *Banking Code Guidance*)).

...

#### Unsolicited services

- 2.6.3 R (1) Subject to *COB 2.6.4R*, a *firm* must not:
- (1a) ~~advise on, arrange, enter into or conduct any designated investment business in relation to a distance contract with~~ supply a service to a retail customer without a prior request on his part, when the supply of such service includes a request for immediate or deferred payment; or
  - (2b) enforce any obligations against a *retail customer* in the event of unsolicited supplies of such services, the absence of reply not constituting consent.
- (2) Paragraph (1) applies in relation to designated investment business, and accepting deposits, under an organised distance sales or service-provision scheme run by the firm or by an intermediary, who, for the purpose of that supply, makes exclusive use of one or more means of distance communication up to and including the time at which the services are supplied.

...

- 3.2.3 R (1) To the extent that a *financial promotion* relates to:
- (a) a *deposit*; or
  - (b) ...
- only *COB 3.1* to *COB 3.5* and *COB 3.8.4R* to *COB 3.8.6G* and *COB 3.14* apply, unless the *financial promotion* relates to a *cash deposit ISA* in which case *COB 3.9.6R(1)*, *COB 3.9.7AR* and *COB 3.9.8R* also apply; and
- (2) ...

...

- 3.9.3 G Table: Location of the provisions applicable to *direct offer financial promotions*

This table belongs to *COB 3.9.2G*

...  
(3) Direct offer financial promotions: general requirements *COB 3.9.6R to COB 3.9.7R*

(3A) Contractual terms and conditions for distance contracts *COB 3.9.7AR*

...  
(9) Information to be contained in direct offer financial promotions regarding:

...  
(d) ~~cancellation rights~~ EIS or non-packaged products, ISAs or PEPs with no right of withdrawal *COB 3.9.21R to COB 3.9.22G*

...

#### Cash deposit ISAs

3.9.8 R A direct offer financial promotion relating to a cash deposit ISA must contain the information required by *COB 6.5.42R(1) to (8)* and *COB App 1* (but see *COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance)*).

...

#### Authorised professional firms

4.2.3 G ...  
(3) the *Distance Marketing Regulations* may apply and require the provision of pre-contractual information in certain circumstances (see *PROF 5.4*).

...

#### COB 4 Annex 1R

1 Table: Circumstances in which the terms of business requirement in *COB 4.2.5R* does not apply and conditions for using the exemption (R)

This table belongs to *COB 4.2.5R*

	Exempted type of firm or transaction or event:	Conditions for using the exemption:
(1)	Voice telephony communications	<p>...</p> <p>(b) if the <i>customer</i> gives his explicit consent to receiving only limited information about the <i>terms of business</i>, the <i>firm</i> must in good time before the <i>retail customer</i> is bound by a contract or offer on the telephone, provide the <i>customer</i> with <u>at least</u> the following information:</p> <p>...</p> <p>(c) if the customer does not give his explicit consent to receiving <del>only the</del> limited information <del>in (b)</del>, and the parties wish to proceed by telephone, the firm must in good time before the retail customer is bound by a contract or offer on the telephone, provide all of the information required by COB App 1 orally to the customer; and</p> <p>...</p>

...

COB 4 Annex 2E

1 Table Content of terms of business provided to a customer: general requirements

This table belongs to  
COB 4.2.11E

A <i>firm's terms of business</i> (including a <i>client agreement</i> ) provided to a <i>customer</i> should, where relevant, include some provision about:	
...	
(15)	<i>Customer's</i> understanding of risk When a <i>firm</i> chooses to fulfil its obligations under COB 5.4.3R (Requirement for risk warnings) in the <i>terms of business</i> in relation to any of the following:
	...
	<u>(f) a security or an investment trust savings scheme which satisfies the conditions specified in COB 3.8.9G(6);</u>
	the relevant risk warning.
...	

...

- 5.3.3 G *Firms* are reminded of the requirements of COB 3.9.76R (Direct offer financial promotions: general requirements) a *direct offer financial promotion* must make it clear that, if a *private customer* is in any doubt about the suitability of the agreement which is the subject of the promotion, he should contact the *firm*, or an *independent intermediary* if the *firm* does not offer *advice*.

...

- 6.1.1AB R In COB 6.1 to COB 6.5, references to a *private customer* include, in relation to the conclusion of a *distance contract*, a *retail customer*.

...

#### Quality and production of key features

- 6.1.5 R A *firm* must ensure that any *key features* or information document it produces in relation to a packaged product or cash deposit ISA is in writing, whether in printed hard copy or in electronic format, and:

- (1) ...

...

#### Medium for provision of key features

- 6.2.2 R The *key features* or information which the *rules* in COB 6.1, COB 6.2 and COB 6.4 require a *firm* to provide to a *private customer* in relation to a packaged product or cash deposit ISA must be provided by the *firm* in a *durable medium*.

...

6.2.7 R When a *firm* sells, *personally recommends* or arranges the sale of a *life policy* to a *private customer*, the *private customer* must be provided with appropriate *key features* before the *private customer* completes an application for the *policy*, subject to *COB 6.2.9R* (Sales through intermediaries) and *COB 6.4.27R to COB 6.4.31R* (telephone sales and other exemptions).

...

6.2.12 R ...

(2) If (1)(a) to (c) apply, then, subject to *COB 6.4.27R to COB 6.4.31R* (telephone sales and other exemptions), if the contract is to be a *distance contract* with a *retail customer*, the *retail customer* must be provided with details of such changes in a *durable medium* in good time before the contract is concluded.

...

#### Variations to existing life policies

6.2.16 R ...

(2) ... ;  
in a *durable medium* by the *firm* personally recommending, arranging or effecting the variation in good time before it is put into effect, unless *COB 6.2.19R* (sales through intermediaries) or *COB 6.4.27R to COB 6.4.31R* (telephone sales and other exemptions) applies.

...

6.2.18 R When a policyholder applies to vary a *policy* issued before 1 January 1995 (or is *personally recommended* to do so) and the variation of the *policy* gives rise to a right to cancel under *COB 6.7.7R*, information must be given to the policyholder by the *firm* that is *personally recommending*, arranging or effecting the variation before it is put into effect, unless *COB 6.2.19R* or *COB 6.4.27R to COB 6.4.31R* (telephone sales and other exemptions) applies. The *firm* must:

(1) ...

...

#### Schemes

6.2.22 R When a *firm* sells, *personally recommends* or arranges for the sale of

a *scheme* to a *private customer*, unless *COB* 6.2.24R (exceptions) or *COB* 6.4.27R to *COB* 6.4.31R (telephone sales and other exemptions) applies, the *private customer* must be provided with *key features* for the *scheme* before the *private customer* completes an application for the *scheme holding*.

...

#### Income withdrawals

- 6.4.8 R When a *firm personally recommends*, arranges or effects *income withdrawals* to or for a *private customer*, the *customer* must be provided with *key features* in good time before the *customer* signs any form of application or authority electing to make those withdrawals, whether that election is made with *advice on investments* or on an execution-only basis, unless *COB* 6.4.10R to *COB* 6.4.12R ~~apply~~ or *COB* 6.4.27R to *COB* 6.4.31R (telephone sales and other exemptions) applies.

...

#### Cash Deposit ISAs

- 6.4.13 R When a *firm* manages, *personally recommends* or sells a *cash deposit ISA* to a *private customer* that *customer* must be provided with the information specified in *COB* 6.5.42R in good time before the *customer* is bound by the transaction, unless *COB* 6.4.27R to *COB* 6.4.31R (telephone sales and other exemptions) applies (~~but see *COB* 1.11.2R (Exemption for firms which follow the Banking Code Guidance)~~)).

...

#### Stakeholder pension schemes

- 6.4.15 R When a *firm* sells, manages, *personally recommends* or arranges the sale of a *stakeholder pension scheme* to or for a *private customer*, the *firm* must, subject to *COB* 6.4.18R and unless *COB* 6.4.27R to *COB* 6.4.31R (telephone sales and other exemptions) applies, provide the *private customer* with *key features* before the *private customer* completes an application for the *stakeholder pension scheme*.

...

#### Entering into a distance contract for accepting deposits (other than a cash deposit ISA)

- 6.4.25 R (1) A *retail customer* must be provided with all the contractual terms and conditions and the information in *COB* App 1 in a *durable medium* in good time before he is bound by a *distance contract* or offer under which the *firm* will *accept deposits*

(other than a cash deposit ISA, for which see COB 6.5.42R), unless an exemption in (2), (3), (4) or (5) COB 6.4.27R to COB 6.4.31R (telephone sales and other exemptions) applies.

~~(2) Exemption: telephone sales~~

~~The exemption in COB 6.4.27R applies in the case of voice telephony communications (References to a 'customer' in that those rules should be read as references to a 'retail customer').~~

~~(3) Exemption: certain other means of distance communication~~

~~This exemption applies, if the contract is concluded at the retail customer's request using a means of distance communication (other than telephone) which does not enable provision of the contractual terms and conditions and the information in accordance with (1). In that case, the firm must provide it to the retail customer in a durable medium immediately after the conclusion of the distance contract.~~

~~(4) Exemption: successive or separate operations under an initial service agreement~~

~~This exemption applies if the firm has an initial service agreement with the retail customer and the contract is in relation to a successive operation or a separate operation of the same nature under that agreement (see COB 1.10.2G (1)).~~

~~(5) Exemption: other successive or separate operations~~

~~This exemption applies if:~~

~~(a) the firm has no initial service agreement with the retail customer;~~

~~(b) the firm has performed an operation with the retail customer within the last year; and~~

~~(c) the contract is in relation to a successive operation or separate operation of the same nature (see COB 1.10.2G (2)).~~

6.4.26 G ~~[deleted] There is a further exemption for those firms which subscribe to the Banking Code Guidance (see COB 1.11.2R).~~



~~Provision of key features or other information in relation to a telephone call~~ Exemption: telephone sales

6.4.27 R (1) ...

(b) provided the *customer* gives his explicit consent to receiving only limited information, may proceed on the basis of at least the following oral information only:

...

(2) If the *customer* does not give his explicit consent to receiving ~~only the limited information in (1)(b)~~, and the parties wish to proceed by telephone, the *firm* must prior to the conclusion of the contract provide all of the information required by *COB* App 1 orally to the *customer*.

...

(4) ~~If the service relates to a tax-exempt policy issued by a friendly society, the firm may send an abbreviated key features in accordance with COB 6.5.43R (Friendly Society tax-exempt policies).~~

6.4.28 G *Firms* are reminded of the requirements in *COB* 3.8.21G (Real time financial promotions) and *COB* 3.10 (Unsolicited real time financial promotions) in relation to telephone calls that may fall within the definition of a *financial promotion*. *Firms* are also reminded that in relation to a stakeholder pension scheme COB 6.4.16R continues to apply.

Exemption: certain other means of distance communication

6.4.29 R This exemption applies where this chapter requires *key features* or other information to be provided in relation to a *distance contract*, if the *distance contract* is concluded at the *customer's* request using a *means of distance communication* (other than telephone) which does not enable provision of the information in a *durable medium* before the *customer* is bound by the contract or offer. In that case, the *firm* must provide *key features* or other information to the *customer* in a *durable medium* immediately after the conclusion of the contract.

Exemption: successive or separate operations under an initial service agreement

6.4.30 R This exemption applies where this chapter requires *key features* or other information to be provided in relation to a *distance contract*, if the *firm* has an initial service agreement with the *customer* and the contract is in relation to a successive operation or a separate operation of the same nature under that agreement (see *COB* 1.10.2G (1)).

Exemption: other successive or separate operations

6.4.31 R This exemption applies where this chapter requires *key features* or other information to be provided in relation to a *distance contract*, if:

- (1) the *firm* has no initial service agreement with the *customer*;
- (2) the *firm* has performed an operation for the *customer* within the last year; and
- (3) the contract is in relation to a successive operation or separate operation of the same nature (see *COB 1.10.2G (2)*).

...

General

6.5.2 R A *firm* must ensure, unless *COB 6.5.3R* applies, that:

- (3) the information document or abbreviated form of *key features* it produces:
  - (a) relating to *friendly society tax exempt policies*, ~~or *traded life policies*~~, ~~or *broker funds*~~, contains the applicable information specified in *COB 6.4.43R-~~COB 6.4.454R~~*;
  - (b) relating to *broker funds* contains the applicable information in *COB 6.4.45R*;
- (4) ...;
- (5) ...; and
- ...
- (6) all:
  - (a) *key features*; and
  - (b) abbreviated *key features* mentioned at *COB 6.5.2R(3)(a)* above.

it produces in relation to a *distance contract* with a *retail customer* include or are accompanied by all the contractual terms and conditions and the information in *COB App 1* except to the extent that they are separately provided to the *retail customer* in a *durable medium* at the same time in good time before the *retail customer* is bound by the contract or offer.

...

6.5.41 G ~~[deleted] *COB 6.5.42R* does not apply to a *cash deposit ISA* offered by a *bank* or *building society* which subscribes to the Banking Code Guidance (see *COB 1.11.2R*).~~

6.5.42 R If *COB 6.4.13R(+)* applies, for a *cash deposit ISA*, the *private customer*

must be given the following information (in accordance with *COB* 6.4.13R) and, in relation to a *distance contract* with a *retail customer*, all the contractual terms and conditions and the information in *COB* App 1 in place of *key features*:

...

Friendly Society tax exempt policies

6.5.43 R Where a *private customer* buys a *tax-exempt policy* issued by a *friendly society*, or agrees to make additional contributions to such a *policy*, the *firm* may, where there is a right to cancel under *COB* 6.7 (Cancellation and withdrawal), issue an abbreviated form of *key features* containing the following details ~~and, in relation to a *distance contract* with a *retail customer*, all the contractual terms and conditions and the information required under *COB* App 1:~~

...

(3) ...; ~~and~~

(4) ...; and

(5) in relation to a *distance contract* with a *retail customer*, all the contractual terms and conditions and the information in *COB* App 1.

...

6.7.2 G *COB* 6.7 (Cancellation and withdrawal) does not act to cancel *distance contracts* entered into by an *appointed representative* as principal to provide intermediation services to a *retail customer*. Regulations 89 (Right to cancel) to 1213 (Payment for services provided before cancellation) of the *Distance Marketing Regulations* may apply instead (see regulation 4(53)).

...

6.7.5 G Cancellable investment agreements.  
This table belongs to *COB* 6.7.4G

Cancellable investment agreements			
	Post-sale right to cancel?	Pre-sale right to withdraw ?	Maximum period of reflection (but see <i>COB</i> 6.7.11R)

<b>Cancellable investment agreements</b>			
<b>A. Contracts where the right arises regardless of means of sale.</b>			
<i>Appropriate personal pension (APP)</i>	Yes <sup>5,6</sup>	No	30 days
<i>Cash deposit ISA</i>	Yes <sup>5,6</sup>	No	14 days
<i>Life policy (including pension policy, pension annuity or within ISA)</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<i>Personal pension contract</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<i>Stakeholder pension scheme (SHP)</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<i>Certain variations of existing life policies, pension contracts and SHPs</i>	Yes <sup>1,5,6</sup>	No <sup>1</sup>	30 days <sup>2</sup>
<b>B. Contracts where the right arises only if advice is given or if sold by distance contract.</b>			
<i>Units in an AUT, recognised scheme or ICVC (within an ISA or PEP)</i> (1) if sold by <i>distance contract</i> ; (2) if sold otherwise with advice	No Yes <sup>4</sup>	No No <sup>4</sup>	14 days
<i>ISA or PEP not mentioned in any other row</i>  (1) if sold by <i>distance contract</i> (2) if sold otherwise with advice	Yes <sup>5,6</sup> No	No Yes <sup>3</sup>	14 days 7 days

<b>Cancellable investment agreements</b>			
<i>Units in an AUT, recognised scheme or ICVC (outside an ISA or PEP)</i>			
(1) if sold by <i>distance contract</i>	No	No	
(2) if sold otherwise with advice	Yes	No	14 days
<i>EIS</i>			
(1) if sold by <i>distance contract</i>	Yes <sup>5,6</sup>	No	14 days
(2) if sold otherwise with advice	No	Yes <sup>3</sup>	7 days
<b>C. Contracts where the right arises for distance contracts only</b>			
<i>Distance contract to accept deposits</i>	Yes <sup>5,6</sup>	No	14 days
<i>Distance contract not mentioned in another row the making or performance of which constitutes, or is part of, designated investment business</i>	Yes <sup>5,6,7</sup>	No	14 days
Notes:			
1. For a <i>pension annuity</i> or <i>pension transfer</i> (and a relevant variation), the <i>firm</i> can, in certain circumstances, choose to <u>provide the right to cancel, in whole or part, through a operate a pre-sale right to withdraw in COB 6.7.19R instead of a post-sale right to cancel (see COB 6.7.14R(2)).</u> A <i>firm</i> may offer a <u>pre-sale right to withdraw</u> , even where there is no right to cancel.			
2. <del>[Deleted] The period is at least 14 days if the option of pre-sale withdrawal is offered.</del>			
...			

...

Post-sale right to cancel

6.7.7 R A retail customer has a right to cancel:

...

- (3) a contract for a *cash deposit ISA*, unless the right to cancel is disapplied for a *distance contract* by case 15 of row 2 to COB 6.7.17R (but see COB 1.11.2R (Exemption for firms which follow the Banking Code Guidance));

- (4) a variation of a *life policy, pension contract* or *stakeholder pension scheme* for which a right to cancel applies under *COB 6.7.23R* and *COB 6.7.26AR*.

...

6.7.9 G ...

- (2) A *product provider* or operator of a *stakeholder pension scheme* (~~see *COB 6.7.2G*~~) may be unsure whether any of the situations in row 2 of *COB 6.7.17R* applies to the contract in question. In such circumstances the *product provider* or operator of a *stakeholder pension scheme* may find it convenient to contract with an intermediary for the provision of documentary evidence needed to confirm the status of *customers*. However, the responsibility for ensuring compliance with the *cancellation rules* remains with the *product provider* or operator of a *stakeholder pension scheme*.

...

Right to cancel a stakeholder pension scheme

- 6.7.12 R (1) A *retail customer* who has entered into a contract for a *stakeholder pension scheme* has a right to cancel, unless the right to cancel is disapplied for a *distance contract* by case 15 of row 2 to *COB 6.7.17R*.

...

Pre-sale right to withdraw

6.7.14 R A *retail customer* has a right to withdraw an offer to enter into:

- (1) an *EIS, ISA* or *PEP*:
- (a) following *advice on investments*;
  - (b) which is not a *distance contract*;
  - (c) unless a right to cancel is offered under *COB 6.7.7R(3)*, *COB 6.7.15R* or *COB 6.7.17R*; and
  - (d) subject to cases 8 and 9 of row 2 *COB 6.7.17R*

~~(unless a right to cancel is offered for an *ISA* or *PEP* under *COB 6.7.7R(3)*, *COB 6.7.15R* or *COB 6.7.17R* and subject to cases 8 and 9 of row 2 *COB 6.7.17R*)~~ an *EIS, ISA* or *PEP*, following *advice on investments*; the right to withdraw procedures are that the offer made by the *customer* to enter into the contract cannot be accepted by the *firm* until at least seven days after the offer is made; or

- (2) a *pension annuity* or a *pension transfer* (or a relevant variation), ~~if a right to cancel has been replaced by a right to withdraw under case 4(a) or 7(a) of row 2, COB 6.7.15R, case 12 of row 2, COB 6.7.17R, COB 6.7.23R (3), or COB 6.7.26AR (2); the~~ to the extent that the right to cancel is provided through a right to withdraw ~~under the~~ procedures ~~are~~ set out in COB 6.7.19R.

6.7.15 R Cancellable contracts and exceptions – life  
This table belongs to COB 6.7.7R(1).

<b>Cancellable contracts and exceptions – life</b>	
<i>Long-term insurance contracts</i> which a <i>retail customer</i> has a right to cancel under COB 6.7.7R(1) (subject to row 2):	
...	
Row 2	<p>There is no right to cancel where any one or more of the following cases applies:</p> <p>...</p> <p>4. <i>pension policy</i> or <i>stakeholder pension scheme</i> funded (wholly or in part) from payments derived from:</p> <p>(a) a <i>pension transfer</i>, <del>for which</del> <u>to the extent that</u> the right to cancel is <del>replaced by</del> <u>provided through</u> the right to withdraw (see COB 6.7.14R(2)), using the cancellation substitute in COB 6.7.19R; or</p> <p>...</p> <p>7. <i>pension annuity</i> that is:</p> <p>(a) due to commence within a year and a day of the contract, <del>for which</del> <u>to the extent that</u> the right to cancel is <del>replaced by</del> <u>provided through</u> the right to withdraw (see COB 6.7.14R(2)), using the cancellation substitute in COB 6.7.19R; or</p> <p>...</p>

...

6.7.17 R Cancellable contracts and exceptions – non-life  
This table belongs to COB 6.7.7R (1) and COB 6.7.14R (1)

<b>Cancellable contracts and exceptions – non-life</b>	
Contracts which a <i>retail customer</i> has a right to cancel under <i>COB</i> 6.7.7R(1) (subject to row 2):	
...	
Row 2	<p>There is no right to cancel where any one or more of the following cases applies:</p> <p>...</p> <p>12. <i>pension contract</i> or <i>stakeholder pension scheme</i> funded (wholly or in part) from payments derived from a <i>pension transfer</i> <del>for which a</del> <u>to the extent that the</u> right to cancel is <del>replaced by</del> <u>provided through</u> a right to withdraw (see <i>COB</i> 6.7.14R(2)) using the cancellation substitute in <i>COB</i> 6.7.19R;</p> <p>...</p>

...

#### 6.7.19 R Cancellation substitute

This table belongs to *COB* 6.7.14R(2), cases 4(a) and 7(a) of row 2 to *COB* 6.7.15R, ~~and~~ case 12 of row 2 to *COB* 6.7.17R, *COB* 6.7.23(3) and *COB* 6.7.26A(2).

<b>Cancellation substitute</b>	
The <i>retail customer's</i> right to cancel under <i>COB</i> 6.7.7R(1) or (4) is <del>replaced</del> <u>provided through</u> (see note 2) <del>by the</del> <u>a</u> right to withdraw only if:	
1.	The <i>firm</i> has supplied (or has reasonably relied upon another <i>firm</i> to supply) to the <i>retail customer</i> , at least <del>30</del> <u>14</u> days <del>in the case of a life policy and 14 days in any other case</del> before the contract is concluded, a written notice (see note 1) which prominently states:
(a)	that the <i>retail customer</i> has <del>that</del> <u>a specified</u> period <del>within</del> which to consider his pension options;
(b)	the dates at which the period begins and ends (which must be, in the case of a <i>pension transfer</i> , before the transfer has been irrevocably effected);
(c)	the pension options available (for example, the <i>open-market option</i> in relation to a <i>pension annuity</i> );
(d)	the steps the <i>retail customer</i> must take in order to exercise a particular pension option;
(e)	that the <i>retail customer</i> is entitled to <i>key features</i> and is advised to check with the <i>firm</i> if it has not been received;
(f)	the cost of any advice given to the <i>retail customer</i> in relation to the transaction; and



<b>Cancellation substitute</b>	
2.	The <i>firm</i> has taken sufficient steps (or has reasonably relied upon the same <i>firm</i> as in 1. to take those steps) to ensure that the <i>customer</i> has been informed and made fully aware of the potential advantages and disadvantages of proceeding and has had an opportunity to consider all other possible alternatives.
Notes:	
1. The notice must be issued separately or feature prominently as part of the application form or <i>suitability letter</i> supplied to the <i>customer</i> .	
2. <u>Where the <i>retail customer's</i> right to cancel is provided through a right to withdraw of less than 30 days, a further right to cancel of at least 30 days less the right to withdraw period must be provided in accordance with these <i>rules</i> so that the total period provided is at least 30 days.</u>	

...

- 6.7.26A R (1) If a *customer* who is an individual varies an existing *pension scheme* by exercising an option to make *income withdrawals*, he has a right to cancel that first variation, ~~unless the right to cancel is replaced by the right to withdraw under (2).~~
- (2) ~~The customer's right to cancel under (1) is replaced by the right to withdraw if the firm follows the procedures in COB 6.7.19R~~  
A firm may use the cancellation substitute in COB 6.7.19R in relation to the right to cancel in (1) .

...

#### Automatic cancellation of an attached distance contract

- 6.7.51A G Regulation ~~411~~12 (Automatic cancellation of an attached distance contract) of the *Distance Marketing Regulations*, has the effect that when notice of cancellation is given in relation to a contract, that notice also operates to cancel any attached distance financial services contract which does not fall within one of the exceptions to the right to cancel in regulation ~~4011~~, unless the *retail customer* gives notice that cancellation of the main contract is not to operate to cancel the attached contract. So, for example, the attached contract will not be cancelled if the price of the service depends on fluctuations in the financial market outside the *firm's* control or if performance of the contract has been fully completed by both parties at the consumer's express request.

#### Obligations on cancellation

- 6.7.52 R ...

...

#### Shortfall ~~where there is a right to cancel a non-distance contract~~

6.7.54 R Subject to *COB* 6.7.56R, the *firm* is entitled under *COB* 6.7.52R(2)(b) to charge the *retail customer* for the market loss (that is, *shortfall*), calculated in accordance with *COB* 6.7.58R, which the firm would incur in cancelling any contract specified in *COB* 6.7.57R.

6.8.12 R ...subject to *COB* 6.8.13 and ~~*COB* 6.8.13A~~ provide the individual with:

...

6.8.13A R ~~[deleted] *COB* 6.8.12R does not apply if the contract is a *distance contract* with a *retail customer* who is not present in the *United Kingdom*.~~

## Annex B

### Amendments to the Client Assets sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 2.5.5 E (1) In the case of a *private customer*, the appropriate terms and conditions referred to in *CASS 2.5.4R* include those specified in ~~*COB 4.2.15E(19)*~~ *4 Annex 2E(18)* (Content of terms of business provided to a customer: stock lending).

...

...

- 2.5.11 G The *stock lending* requirements in ~~*COB 4.2.15E(19)*~~ *4 Annex 2E(18)* also apply to *safe custody investments* held collectively on behalf of a *firm's customers* in any *custody* or settlement system. If the *custody* or settlement system operates an 'automatic' *stock lending* programme, the *firm* should maintain a separate account or be able to demonstrate that it maintains adequate systems to differentiate between the *safe custody investments* of those *customers* who have not consented to *stock lending activity* through that programme from the *designated investments* of those that have consented.

## Annex C

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. The text shown amended is the text in CRED, as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39).

...

#### Exemptions

- 11.4.5 G The exemptions referred to in *CRED* 11.4.3G are set out in *COB* 6.4.~~25~~27R to *COB* 6.4.31R. They are relevant:
- (1) where the contract is concluded by telephone and the *retail customer* gives explicit consent to receiving a more limited range of information. *COB* 6.4.27R(1) sets out the information to be provided in such cases. Full information has to be provided, in a *durable medium*, immediately after conclusion of the *distance contract* (*COB* 6.4.~~25~~27R(2));
  - (2) where a means of communication (other than telephone) is used which does not enable provision of the required information in a *durable medium* before conclusion of the contract; in this case full information must also be provided in a *durable medium* immediately after conclusion of the *distance contract* (*COB* 6.4.~~25~~27R(3));
  - (3) where there is an initial service agreement and the contract is in relation to a successive or separate operation of the same nature under that agreement, or there is no initial service agreement and the contract is in relation to a successive or separate operation of the same nature and is being performed no more than one year from the date of performance of the last operation (*COB* 6.4.30R to *COB* 6.4.31R; and see *COB* 1.10.2G).
- 11.4.6 G The other provisions in *COB* which relate to the disclosure requirements and are of relevance to *credit unions* entering into a *distance contract* for *accepting deposits* are in *COB* 2.6 (General provisions related to distance contracts). ~~*COB* 1.11.2R (Exemption for firms which follow the Banking Code Guidance) would be relevant if a *credit union* came within its scope and subscribed to the Banking Code Guidance.~~

## Annex D

### Amendments to the Electronic Commerce sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. The text shown amended is the text in ECO, as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39).

1.2.45A R ...

...

1.2.5AB R ...

...

1.2.12 E Table: Provision of essential information to consumers in direct offer financial promotions. This table belongs to ECO 1.2.6E(1)(c).

COB rule	Description
<del>COB 3.9.76R(52)(a)</del> , as regards the information in <u>COB App 1.1.1R(6) and (7)</u>	<del>Direct offer financial promotions: particular information required</del> <u>Required information for certain direct offer financial promotions</u>
<del>COB 3.9.12R(1)</del>	Execution-only dealing services
<del>COB 3.9.15R(1)</del>	Investments which can fluctuate in value
<del>COB 3.9.18R</del>	Life policies
<del>COB 3.9.21R(1)(a)</del> <u>3.9.6R(2)(a)</u> , as regards the information in <u>COB App 1.1.1R(17)</u>	Cancellation rights
<del>COB 3.9.21R(1)(c)</del>	<del>Cancellation rights</del>
<del>COB 3.9.23R</del>	Charges for regulated collective investment schemes

## Annex E

### Amendments to the Professional Firms sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. The text shown amended is the text in PROF, as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39).

#### 5.4 Application of the Distance Marketing Regulations

- 5.4.1 R (1) In addition to those provisions of the *Distance Marketing Regulations* which apply directly (see COB 1.10.7G), an authorised professional firm must, with respect to its *non-mainstream regulated activities*, comply with regulations ~~67 to 1011~~, ~~14 to 15(2)~~ and ~~16 to 2015~~ of the *Distance Marketing Regulations*, and ~~†~~Those regulations have effect to cancel *distance contracts* the making or performance of which by such firms constitutes a *non-mainstream regulated activity*.
- (2) Paragraph (1) does not apply in relation to regulations ~~67 to 78~~ and ~~14 to 15(2)~~15 if the *designated professional body* of the *authorised professional firm* has rules equivalent to those regulations and:
- (a) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and
  - (b) the *authorised professional firm* is subject to those rules in the form in which they have been approved.

## Annex F

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text in the Glossary, as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39).

Amend the following definition as shown:

<i>Distance Marketing Regulations</i>	The Financial Services (Distance Marketing) Regulations 2004 (SI 2004/ <u>2095</u> ).
---------------------------------------	---

**ADDENDUM**

**DISTANCE MARKETING DIRECTIVE (AMENDMENT) INSTRUMENT 2004**

In this Addendum, underlining indicates new text and striking through indicates deleted text.

Annex A of this instrument is amended as follows:

....

6.1.1BA R In *COB* 6.1 to *COB* 6.5, references to a *private customer* include, in relation to the conclusion of a *distance contract*, a *retail customer*.

...

...

General

6.5.2 R A *firm* must ensure, unless *COB* 6.5.3R applies, that:

- (3) the information document or abbreviated form of *key features* it produces:
  - (a) relating to *friendly society tax exempt policies*, or *traded life policies*, contains the applicable information specified in *COB* ~~6.4.5.43R~~-*COB* ~~6.4.5.44R~~;
  - (b) relating to *broker funds* contains the applicable information in *COB* ~~6.4.5.45R~~;

... ..

...

...

6.7.19 R Cancellation substitute

...

<b>Cancellation substitute</b>
...
Notes:
1. The notice must be issued separately or feature prominently as part of <del>the application form or suitability letter</del> <u>another document</u> supplied to the <i>customer</i> .
...

...



**CONDUCT OF BUSINESS SOURCEBOOK  
(AMENDMENT NO 18) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Conduct of Business sourcebook.
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force as follows:
  - (1) Annex A comes into force on 1 January 2005; and
  - (2) Annex B comes into force on 1 October 2004.

**Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Conduct of Business Sourcebook (Amendment No 18) Instrument 2004.

By order of the Board  
16 September 2004

## Annex A

### Amendments to COB

In this Annex, underlining indicates new text and striking through indicates deleted text.

8.2.10 E Table: Periodic statements – timing and content

This table belongs to *COB 8.2.7E*.

Periodic statements: timing and content				
...				
Adequate information	(3)	A <i>periodic statement</i> should contain:		
		(a)	(i)	the information set out in <i>COB 8.2.11E</i> ;
			(ii)	if applicable, the additional information in <i>COB 8.2.12E</i> , <i>COB 8.2.13E</i> , <i>COB 8.2.14E</i> , <i>COB 8.2.15E</i> and <i>COB 8.2.17E</i> ( <u>but the information set out in <i>COB 8.2.17E</i> need only be provided once in any period not exceeding 12 months</u> ); and
			(iii)	...

...

8.2.17 E Table: Periodic statements – additional information required for a structured capital at risk product

This table belongs to *COB 8.2.10E*~~(3)~~~~(a)~~~~(ii)~~.

Additional information required when a <i>firm sells, advises on or communicates or approves a financial promotion</i> relating to a <i>structured capital-at-risk product</i> to a <i>person who is a private customer</i> , or manages the relevant assets of the issuer of a <i>structured capital-at-risk product</i> , <u>or acts as an <i>investment manager</i> where the <i>investments</i> managed include <i>structured capital-at-risk products</i></u>
....

## Annex B

### Amendments to the Glossary

In this Annex, underlining indicates new text.

Amend the following definition as shown:

*pension transfer* a transaction resulting from a decision made, with or without advice from a *firm*, by a *customer* who is an individual, to transfer deferred benefits from:

(a) an *occupational pension scheme*; or

(b) an *individual pension contract* providing fixed or guaranteed benefits that replaced similar benefits under a *defined benefits pension scheme*; or

(c) (in *COB 6.7 (Cancellation and withdrawal)*) a *stakeholder pension scheme* or a *personal pension scheme*)

to a *stakeholder pension scheme* or to a *personal pension scheme* (including a self-invested *personal pension scheme*), or to any deferred annuity policy (including a *pension buy-out contract*) where the eventual benefits depend in whole or in part on investment performance in the period up to the *intended retirement date*.

**INSURANCE: CONDUCT OF BUSINESS SOURCEBOOK  
(AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Insurance: Conduct of Business Sourcebook.
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial and Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force on 14 January 2005.

**Amendments to the Insurance: Conduct of Business sourcebook**

- D. The Insurance: Conduct of Business sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Insurance: Conduct of Business Sourcebook (Amendment) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

The amendments shown to ICOB 4.7.1R and ICOB 8.4.1R are to the text as amended by the Distance Marketing Directive Instrument 2004 (FSA 2004/39).

#### ICOB Transitional Rules

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: date in force	(6) Handbook provision: coming into force
1	Every <i>rule</i> in <i>ICOB</i> unless the context otherwise requires and subject to any more specific transitional provision relating to the matter.	R	If the application of any provision in <i>ICOB</i> is dependent on the occurrence of a series of events, some of which occur before, and some of which occur <u>on or</u> after 14 January 2005, the provision applies with respect to the events that occur <u>on or</u> after 14 January 2005.	14 January 2005 – 15 July 2005	14 January 2005
2		G	For example, if a <i>firm</i> were to <i>advise</i> a <i>customer</i> before 14 January 2005 to <i>buy</i> a <i>non-investment insurance contract</i> , the <i>firm</i> would not be required to comply with the provisions relating to <i>personal recommendations</i> in <i>ICOB</i> 4 if the <i>customer</i> were to <i>buy</i> the <i>non-investment insurance contract</i> <u>on or</u> after 14 January 2005. However, if the <i>firm</i> were to repeat the <i>personal recommendation</i> to the		

			<i>customer on or after 14 January 2005, those provisions in <i>ICOB 4</i> would apply.</i>		
...					
4	<i>ICOB 4.4</i>	G	Where, before 14 January 2005, an <i>insurance intermediary</i> makes a <i>personal recommendation</i> to a <i>customer</i> of a specific <i>non-investment insurance contract</i> , or <i>arranges</i> for the <i>customer</i> to enter into a <i>non-investment insurance contract</i> , but the contract is concluded <u>on or</u> after that date, the <i>insurance intermediary</i> will need to provide the <i>customer</i> with a statement of demands and needs in accordance with <i>ICOB 4.4.1R</i>		
...					
8	<u><i>ICOB 4.2.4G(1)</i></u>	<u>G</u>	<u>Until 31 May 2005, the reference in <i>ICOB 4.2.4G(1)</i> to the initial disclosure document set out in <i>ICOB 4 Ann 1G</i> includes an initial disclosure document which complies with <i>ICOB 4 Ann 1G</i> in the <i>Insurance: Conduct of Business Sourcebook Instrument 2004 (FSA 2004/06)</i>.</u>	<u>14 January 2005 – 31 May 2005</u>	<u>Already in force</u>

...

Customer to be treated as retail customer when contract covers him in both a private and business capacity

1.2.6A R      If an *insurance intermediary* or an *insurer* is dealing with a *customer* who is an individual in relation to a *non-investment insurance contract* or a *distance non-investment mediation contract* which would cover him in both a private and business capacity, the *insurance intermediary* or an *insurer* must comply with *ICOB* as if the *customer* were a *retail customer*.

...

1.2.8R      Where an *insurance intermediary* carries on *insurance mediation activities* for *commercial customers* in relation to *contracts of large risks* where the risk is located within the *European Economic Area*, the only provisions of *ICOB* that apply are:

- (1)      *ICOB* 5.4.5R (Provision of a policy document to commercial customers); and
- (2)      *ICOB* 5.4.8R and *ICOB* 5.4.9G (Group policies sold to commercial customers); ~~and~~
- (3)      ~~*ICOB* 7.6 (Motor vehicle liability insurers: claims representatives).~~

...

1.2.9A G      A provision in *ICOB* that applies to an *insurer* when acting as *product provider* or as a *motor vehicle liability insurer* applies where relevant in relation to *contracts of large risks* where the risk is located within the *European Economic Area*.

...

UK establishments – Exemption for insurers and managing agents

- 1.3.2A R
- (1)      Notwithstanding *ICOB* 1.3.1R, this *rule* sets out circumstances in which some or all of the *rules* in *ICOB* are disapplied for an *insurer* or a *managing agent* in relation to any *non-investment insurance contract* provided, or which may be provided, by it (or in the case of a *managing agent*, by *members* for whom it acts).
  - (2)      *ICOB* does not apply if:
    - (a)      the intermediary (whether or not an *insurance intermediary*) in contact with the *customer* is not established in the *United Kingdom*; and
    - (b)      the *customer* is not *habitually resident* in, and, if applicable, the *State of the risk* is outside, an *EEA State*.
  - (3)      A *rule* in *ICOB* which goes beyond the minimum required by Community legislation does not apply if the *customer* is *habitually resident* in (and, if applicable, the *State of the risk* is) an *EEA State*

other than the *United Kingdom*, to the extent that the *EEA State* in question imposes measures of like effect .

...

IMD passported activities

- 1.3.10 R
- (1) In addition to *ICOB 1.3.1R*, the provisions in *ICOB 1.3.11R* apply to the *passported activities* carried on by a *UK firm* under the *IMD* from a *branch* elsewhere in the *EEA* unless the *Host State regulator* imposes measures which implement articles 12 and 13 of the *IMD* for those activities.
  - (2) Notwithstanding *ICOB 1.3.1R*, the provisions in *ICOB* which implement articles 12 and 13 of the *IMD* do not apply to a *UK firm* providing *cross border services* in another *EEA State* under the *IMD*, except that:
    - (a) the provisions in *ICOB 1.3.11R* apply if the *Host State regulator* does not impose minimum measures which implement articles 12 and 13 of the *IMD* for those activities; and
    - (b) the other provisions in *ICOB* relating to articles 12 and 13 of the *IMD* apply unless the *Host State regulator* imposes measures of like effect for those activities.
  - (3) In addition to *ICOB 1.3.1R*:
    - (a) the provisions in *ICOB 1.3.11R* do not apply to an *incoming EEA firm* carrying on *passported activities* under the *IMD* from a *branch* in the *United Kingdom* if the *firm's Home State regulator* imposes minimum measures which implement articles 12 and 13 of the *IMD* for these activities;
    - (b) the provisions in *ICOB 1.3.11R* apply to an *incoming EEA firm* providing *cross border services* in the *United Kingdom* if the *firm's Home State regulator* does not impose minimum measures which implement articles 12 and 13 of the *IMD* for those activities; and
    - (c) the other provisions in *ICOB* relating to articles 12 and 13 of the *IMD* (beyond the minimum required to implement these articles) apply to an *incoming EEA firm* providing *cross-border services* in the *United Kingdom*, unless the *firm's Home State regulator* imposes measures of like effect for those activities.

1.3.11 R      The provisions referred to in *ICOB 1.3.10R* are:



- (1) ICOB 4.2.2R to 4.2.8R, ICOB 4.2.11R, ICOB 4.2.14R and ICOB 4.2.20R;
- (2) ICOB 4.3;
- (3) ICOB 4.4 (except ICOB 4.4.7R); and
- (4) ICOB 4.8.1R.

1.3.12 G

- (1) The provisions in ICOB 1.3.11R are the minimum provisions required for the implementation of articles 12 and 13 of the IMD.
- (2) The effect of ICOB 1.3.10R is to apply these minimum provisions to firms in respect of their insurance mediation activities passported under the IMD if other EEA States have not implemented articles 12 and 13 of the IMD for those activities.
- (3) Firms are reminded that insurers have passporting rights under the Insurance Directives but not under the IMD, and so ICOB 1.3.10R does not apply to insurers.

...

1.6.1G

- (1) ...
- (2) *ICOB 8.5 (Cancellation requirements) does not apply to a distance non-investment mediation contract entered into by an appointed representative itself to provide insurance mediation activity services to a retail customer. Regulation 89 (Right to cancel) to 1213 (Payment for services provided before cancellation) of the Distance Marketing Regulations apply instead (see regulation 4(5)). See also ICOB 1.7.3G (2)(e), (f) and (g) (4) (guidance on when a distance non-investment mediation contracts is concluded).*
- (3) ...

1.7.2G

- ...
- (1) Regulation 112 (Automatic cancellation of an attached distance contract); and
- (2) Regulation 1314 (Payment cards).

1.7.3G

- ...
- (1) Retail customer
  - (a) ...

- (b) Examples of individuals who would be regarded as *retail customers* include:
  - (i) ...; and
  - (ii) private individuals acting in personal or other family circumstances, for example, as trustee of a family trust; and.
  - (iii) ~~a customer who buys a non-investment insurance contract that covers him in both a private and business capacity, for example motor insurance for a driving instructor which also provides cover for social and domestic use, or insurance taken out by a sole trader which provides cover for him in both a private and business capacity.~~

...

2.7.1 R During the course of a *distance contract* with a *retail customer*, the making of which constitutes or is part of a *non-investment insurance contract*:

- (1) ...
- (2) the *firm* must comply with the *retail customer's* request to change the *means of distance communication* used, unless this is incompatible with the *non-investment insurance contract* concluded or the service being provided by the *firm*.

2.7.2 R A *firm* must ensure that information provided to a *retail customer* before the conclusion of a *distance contract* about his contractual obligations under that contract conforms with the contractual obligations that would be imposed on him under the law applying if the contract were concluded.

...

2.9 Communications with customers

2.9.1 R Where a *non-investment insurance contract* is effected jointly, the information required by any *rule* in *ICOB* may be sent only to the first-named *customer*.

...

4.2.2R ...

- (3) (a) ...
- (b) If *Provided* the *customer* gives his explicit consent to receiving only limited ~~disclosure~~ information, the *insurance intermediary* ~~must provide the *customer* with~~ may proceed on the basis of at least the following information:

...

- (c) If the *customer* does not give his explicit consent to receiving limited information, and the parties wish to proceed by telephone, the *insurance intermediary* must prior to the conclusion of the contract provide all of the information required by *ICOB 4.2.8R* orally to the *customer*.

4.2.8R Table: Information to be provided before conclusion of the contract or immediately after conclusion of the contract

This table belongs to *ICOB 4.2.2R*

...
(9) That the <i>customer</i> may be entitled to compensation from the <del><i>compensation scheme</i></del> <u>The compensation arrangements should the <i>insurance intermediary</i> be unable to meet its liabilities.</u>

...

4.4.4AG Where a *firm* has not made a *personal recommendation* and provides *key features* as an alternative to a *policy summary* under *ICOB 5.5.4R*, that constitutes provision of a statement of demands and needs.

...

4.6.1R Before the conclusion of a *non-investment insurance contract*, or at any other time, an *insurance intermediary* that conducts *insurance mediation activities* for a *commercial customer* must, if that *commercial customer* asks, promptly disclose the *commission* that he and any *associate* of his receives in connection with the *non-investment insurance contract* in question, in cash terms or, to the extent it cannot be indicated in cash terms, the basis for the calculation of the *commission*, in a *durable medium*.

...

4.6.7G In considering any disclosure of *commission* under *ICOB 4.6.1R*, an *insurance intermediary* should include all forms of remuneration from any arrangements he may have for remuneration in connection with the *non-investment insurance contract* (including arrangements for sharing profits, for payments relating to the volume of sales, and for payments from premium finance companies in connection with arranging finance for a *non-investment insurance contract*).

4.6.8G An example of a situation where the *commission* could not be stated in cash terms under *ICOB 4.6.1R* is where the *insurance intermediary* is remunerated under a profit share arrangement or any other similar arrangement under which the *insurance intermediary* may receive a non-fixed amount not specific to any particular *non-investment insurance contract*. The *commission*, to the

extent it cannot be indicated in cash terms, should instead be indicated by showing the basis of its calculation.

...

- 4.7.1R (1) Subject to *ICOB 4.7.2R*, an *insurance intermediary* or an *insurer* must not, ~~in relation to a *non-investment insurance contract* that is a *distance contract*:~~
- (1)(a) ~~advise on, arrange, enter into, carry out or assist in the administration and performance of such a contract for supply a service to a *retail customer* without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or~~
- (2)(b) ...
- (2) Paragraph (1) applies in relation to *insurance mediation activities and insurance business*, in relation to *non-investment insurance contracts* under an organised distance sales or service-provision scheme run by the *firm* or by an intermediary, who, for the purpose of that supply, makes exclusive use of one or more *means of distance communication* up to and including the time at which the services are supplied.

...

- 4.8.1 R (1) ~~All~~ Except as provided in (2), the information provided to customers in accordance with this chapter by a *firm* must:
- (a) ~~(if the *customer* is in the *United Kingdom*) be in English, unless the *customer* requests it to be, and the *firm* agrees to it being, in another language; or~~
- (b) ~~(if the *customer* is in another *EEA State*) be in an official language of that *EEA State*.~~
- (2) If a *customer* requests all the information provided to him in accordance with this chapter to be, and the *firm* agrees to it being, in another language then the information may be in that language.

...

ICOB 4 Ann 1G

...

---

**4 What will you have to pay us for our services? [Note 15]**

---

A fee [of £ [ ] ] [for] [list the types of services provided for *non-investment insurance contracts*]. [Note 15]

No fee [for] [list the types of services provided for *non-investment insurance contracts*].

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

...

---

## 7 What to do if you have a complaint [Note 16]

---

...

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 26] [Note 26A]

---

## 8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 16] [Note 27] [Note 27A]

---

...

[or] [Note 28] [Note 29]

...

The following notes do not form part of the IDD.

...

Note 9 – this is the list required by *ICOB* 4.2.14R. This sentence is required only where a *firm* selects this service option.

...

Note 15 – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, the *insurance intermediary* should insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* and *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'. If the *firm* is offering more than one type of service in connection with *non-investment insurance contracts*, the *firm* may aggregate the *fees* over all the services provided, and (if that is the case) identify the services for which there is no *fee*.

...

Note 20 – the *insurance intermediary* should insert a short, plain language description of the business for which it has permission which relates to the service it provides in relation to non-investment insurance contracts.

...

Note 26A – if the IDD is provided by an authorised professional firm which is exclusively carrying on non-mainstream regulated activities, the authorised professional firm should delete this sentence and refer to the alternative complaints handling arrangements.

...

Note 27A - when a firm which is not a participant firm provides the IDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained.

...

Note 29 – where the insurance intermediary provides a service in relation to a contract which covers both a compulsory class of insurance and a class of insurance which is not compulsory, it should indicate the level of compensation that applies to each class.

...

- 5.2.3R (1) ...
- (2) Unless (3) applies, if an insurer operates from an establishment maintained by it in the United Kingdom but the intermediary does not, is not authorised, is a firm selling connected contracts, or is an authorised professional firm carrying on non-mainstream regulated activities, the insurer is responsible for the provision of the information in ICOB 5.2.9R to the customer, where the non-investment insurance contract relates to a customer habitually resident in the EEA, subject to ICOB 5.2.5R, as well as for the content and production of it.
- (3) If an insurer operates from an establishment maintained by it in the United Kingdom, but the intermediary does not, and the customer is habitually resident outside the EEA, ICOB 5 does not apply to the insurer.

- 5.2.4G (1) ICOB 5.2.3R(2) makes the insurer responsible for the content, production and provision of information to customers dealing through:
- (1)(a) intermediaries in the United Kingdom who do not have Part IV permission (for example, travel agents selling connected contracts, exempt professional firms and intermediaries who do not have an establishment in the United Kingdom); or
- (2)(b) firms selling connected contracts; or

- ~~(3)(c)~~ *authorised professional firms carrying on non-mainstream regulated activities.*
- (2) The insurer is not responsible for the content, production or provision of information to customers outside the EEA unless the insurer is acting as the insurance intermediary in contact with the customer.
- 5.2.5R (4) If an *insurer* deals with an intermediary who operates from an establishment in the *United Kingdom* but does not need to be *authorised*, who is a *firm* selling *connected contracts*, or who is an *authorised professional firm* carrying on *non-mainstream regulated activities*, despite *ICOB 5.2.3R(2)* the *insurer* need not produce or provide:
- ~~(a)~~ (1) a *policy summary*; and
- ~~(b)~~ (2) in respect of a distance sale, the directive-required information at *ICOB 5.5.20R(16)* to (21).
- (2) ~~If the insurer deals with an intermediary who does not operate from an establishment maintained by the intermediary in the United Kingdom, despite ICOB 5.2.3R(2) the insurer need not produce or provide a policy summary.~~
- ...
- 5.2.10A G Where any rule in this chapter refers to information about fees to be provided to customers, the fees so mentioned are all fees throughout the distribution chain between the insurer and the customer and which are payable by the customer in addition to the premium.
- ...
- 5.2.11A R An insurer may agree with an insurance intermediary that the insurance intermediary will be responsible for producing and providing to the retail customer the price and payment information referred to in ICOB 5.5.20R (17)(b) to (f).
- ...
- 5.3.6R (1) ...
- (e) information about the claims handling process (*ICOB 5.3.9R* to *ICOB 5.3.11G*); ~~and~~
- (f) information, where applicable, about cancellation rights (*ICOB 5.3.12R* to *ICOB 5.3.14G*); and

(g) information, where applicable, about the extent and level of compensation cover and how further information can be obtained about compensation arrangements, if not already included in (a).

(2) The following exemptions from (1) apply:

(a) Telephone sales

If a *non-investment insurance contract* is concluded by telephone, ~~and provided the retail customer gives his explicit consent to receiving only the limited information specified in (i) to (ix) below, an insurance intermediary must give may proceed on the basis of at least this the following information to the retail customer orally before the conclusion of the contract:~~

...

If the retail customer does not give his explicit consent to receiving limited information, and the parties wish to proceed by telephone, the insurance intermediary must prior to the conclusion of the contract provide all of the information required by (1) orally to the retail customer.

(b) ...

5.3.7G ~~[deleted]If the retail customer does not give explicit consent to receiving only limited information before conclusion of the contract in accordance with ICOB 5.3.6R(2)(a), the exemption at ICOB 5.3.6R(2)(a) does not apply and the information in ICOB 5.3.6R(1) must be provided to the retail customer in a durable medium before conclusion of the contract.~~

...

#### Group policies sold to retail customers

5.3.29R When an insurance intermediary sells a group policy to a retail customer the terms of which provide for persons, other than the retail customer who concludes the non-investment insurance contract, to become policyholders, the insurance intermediary must, promptly after the conclusion of the contract:

(1) provide a policy document and a policy summary containing the information in ICOB 5.5.5R except ICOB 5.5.5R(6) (cross-references to the policy document) to the retail customer;

(2) inform the retail customer that he should:



- (a) provide the *policy summary* containing the information in (1) to each *policyholder* who is capable of being a *retail customer*; and
  - (b) inform each *policyholder* that a copy of the *policy document* is available on request; and
  - (3) if the *policy* replaces a previous *group policy*, inform the *retail customer* that he should inform each *policyholder* who is capable of being a *retail customer* of any changes to the information in the *policy summary*.
- 5.3.30G
- (1) The *policyholder* referred to in *ICOB 5.3.29R* is a *person* who has rights under the *policy* to make a *claim* on the *insurance undertaking* of the *policy* (as distinct from a *person* who can only make a *claim* on, for example, his employer or on trustees in respect of the *policy* (see *ICOB 1.2.15R* and *ICOB 1.2.16G*). Such a *policyholder* will typically be a *retail customer* under *ICOB*.
  - (2) The *policy summary* information to be provided to *policyholders* in accordance with *ICOB 5.3.29R(2)* can be provided in any form, for example, on an employer's intranet, in a staff handbook or in a separate booklet, providing it is in writing.
- ...
- 5.4.8R
- When an *insurance intermediary* sells a *group policy* to a *commercial customer* the terms of which provide for *persons*, other than the *commercial customer* who concludes the *non-investment insurance contract*, to become *policyholders*, the *insurance intermediary* must, promptly after the conclusion of the contract:
- (1) provide a *policy document* and a *policy summary* containing the information in *ICOB 5.5.5R* except *ICOB 5.5.5R(6)* (cross-references to the *policy document*) to the *commercial customer* (but a *policy summary* need not be supplied if there is no *policyholder* who would be a *retail customer*);
  - (2) where a *policy summary* is provided, inform the *commercial customer* that he should:
    - (a) provide the *policy summary* containing the information in (1) to each *policyholder* who is capable of being a *retail customer*; and
    - (b) inform ~~them~~ each *policyholder* that a copy of the *policy document* is available on request; and
  - (3) where a *policy summary* is provided, if the *policy* replaces a previous *group policy*, inform the *commercial customer* that he should inform

each *policyholder* who is capable of being a *retail customer* of any changes to the information in the *policy summary*.

...

5.5.4R A *firm* may provide *key features* that meet the requirements of COB 6 on the content of the *key features*, instead of a *policy summary*. The *key features* must include the information required in ICOB 5.5.5R(6), (10) and (13) (cross-references from significant and unusual exclusions or limitations to related sections of the *policy document*, a telephone number or address for notification of *claims* and the key facts logo), in addition to that required by COB 6, but this rule does not require a *firm* to meet the requirements of COB 6.5.12R or COB 6.5.38R.

...

5.5.14A R Where an exact amount, required to be included in a statement of price in accordance with ICOB 5.5.14R, cannot be indicated, the statement of price must show the basis for calculation of the amount enabling the *retail customer* to verify it.

5.5.14B G A *firm* may only show the basis of calculation (in accordance with ICOB 5.5.14AR) if it is not possible to show an exact amount. So ICOB 5.5.14AR will not apply where, for example, a creditor insurance *policy* is financed by means of a loan agreement and it is possible to state the total amount payable in accordance with the requirements under the Consumer Credit Act 1974 to show the total price. In such cases ICOB 5.5.14R(3) requires the interest payable on the *premium* to be stated, and ICOB 5.5.14R(6) requires the total price to be stated.

...

5.5.15AG If the *non-investment insurance contract* contains optional elements of cover, the requirements of ICOB 5.5.14R also apply to each optional element of cover.

...

5.5.21R ~~[deleted]Where a *non-investment insurance contract* is effected jointly, the information required by ICOB 5.5.20R may be sent only to the first named *customer*.~~

...

6.1.5R This chapter does not apply to the following contracts:

...

- (5) a *general insurance contract* that is not a *distance contract* sold by an intermediary who is an *unauthorised person* (except where the intermediary is an *appointed representative*);

...

...

6.4.2G

(1) Regulation ~~11~~12 (Automatic cancellation of an attached distance contract) of the *Distance Marketing Regulations* has the effect that, when notice of cancellation is given in relation to a contract, that notice also operates to cancel any attached contract which is also a distance financial services contract which does not fall within one of the exceptions to the right to cancel in Regulation 11 (Exceptions to the right to cancel) of the *Distance Marketing Regulations*, unless the *retail customer* gives notice that cancellation of the main contract is not to operate to cancel the attached contract. So the attached contract will not be cancelled if the price of the service depends on fluctuations in the financial market outside the *firm's* control or if performance of the contract has been fully completed by both parties at the *retail customer's* express request. Whether a contract will be "attached" to the main contract will depend on the circumstances in each case. Regulation ~~11(1)(b)~~ 12(1) provides that the contract will be attached if any of the following conditions are satisfied:

- (a) it has been entered into in ~~accordance~~ compliance with a term of the main contract;
- (b) the main contract is financed or to be financed by the contract;
- (c) the main contract is a debtor-creditor-supplier agreement within the meaning of the Consumer Credit Act 1974 and the contract is to be financed by the main contract;
- ~~(e)~~(d) the *retail customer* has entered into the contract ~~for a purpose related to~~ to induce the supplier to enter into the main contract;  
or
- ~~(d)~~(e) performance of the contract requires performance of the main contract.

...

8.3.6R

(1) (a) ...

(b) ~~If~~ Provided the *retail customer* gives his explicit consent to receiving only limited ~~disclosure~~ information, the *insurance intermediary* ~~must~~ may proceed on the basis of at least the ~~prior to the conclusion of the *distance non-investment mediation contract* on the telephone,~~ provide the *retail customer* with the following information:

...

If the *retail customer* does not give his explicit consent to receiving limited information, and the parties wish to proceed by telephone, the *insurance intermediary* must prior to the conclusion of the contract provide all of the information required by *ICOB* 8.3.1R orally to the *retail customer*.

...

- 8.4.1R (1) Subject to *ICOB* 8.4.2R, an *insurance intermediary* must not, ~~in relation to a *distance non-investment mediation contract*:~~
- (1)(a) ~~advise on, arrange, enter into, carry out or assist in the administration and performance of such a contract for supply a service to a *retail customer* without a prior request on his part, when the supply of such a service includes a request for immediate or deferred payment; or~~
- (2)(b) ...
- (2) Paragraph (1) applies in relation to *insurance mediation activities in relation to distance non-investment mediation contracts under an organised distance sales or service-provision scheme run by the firm or by an intermediary, who, for the purpose of that supply, makes exclusive use of one or more means of distance communication up to and including the time at which the services are supplied.*

**MORTGAGES: CONDUCT OF BUSINESS SOURCEBOOK  
(AMENDMENT NO 2) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers listed in Schedule 4 to the Mortgages: Conduct of Business sourcebook.
- B. The rule-making powers listed in that Schedule are specified for the purpose of section 153(2) (Rule-making instruments) of the Financial Services and Markets Act 2000.

**Commencement**

- C. This instrument comes into force on 31 October 2004.

**Amendments to the Mortgages: Conduct of Business sourcebook**

- D. The Mortgages: Conduct of Business sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Mortgages: Conduct of Business Sourcebook (Amendment No 2) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Mortgages: Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### MCOB Transitional Provisions

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
6	<i>MCOB 3.6</i>	R	<p>(1) Providing it does not state or imply that protections under the Consumer Credit Act 1974 apply, a <i>non-real time qualifying credit promotion</i> communicated:</p> <p>(a) in a directory (or similar publication) that is updated annually;</p> <p>(b) otherwise than in (a);</p> <p>on or after 31 October 2004 <del>that was first communicated</del> <u>where the deadline for submission for communication was</u> before that date will be in compliance with the rules in <i>MCOB 3.6</i> if it satisfies the</p>	<p>(1)(a) From <u>the later of 31 October 2004 or the date of first communication</u>, for one year;</p> <p>(1)(b) From 31 October 2004 until 31 January 2005.</p>	31 October 2004

			advertising requirements under the Consumer Credit Act 1974.  ...		
...					
<u>8</u>		<u>R</u>	<p>A reference to:</p> <p>(a) <u>an initial disclosure document in MCOB 4 Ann 1R or MCOB 8 Ann 1R; or</u></p> <p>(b) <u>an illustration in MCOB 5 Ann 1R or MCOB 9 Ann 1R;</u></p> <p><u>includes an initial disclosure document or illustration which complies with the rules in the Mortgages: Conduct of Business Sourcebook Instrument 2003, as amended by the Mortgages: Conduct of Business Sourcebook (Amendment) Instrument 2004.</u></p>	<p><u>From 31 October 2004 until 31 May 2005</u></p>	<p><u>31 October 2004</u></p>

...

2.2.3R In any communication to a *customer*, a *firm* must:

...

- (3) describe any *regulated lifetime mortgage contract* as a 'lifetime mortgage' and not use any other expression to describe such a mortgage or omit that description from the name given to any product that meets the definition.

...

2.2.5G *Firms* are reminded that they should follow the relevant ~~rules~~ rules in COB 5 and COB 6 relating to advice and disclosure on *investments* if they are *advising the customer on an investment (such as an ISA) such as an annuity linked to a regulated lifetime mortgage contract or an ISA used as a repayment vehicle.*

...

- 2.3.6R (1) *A firm* must not operate a system of giving or offering inducements to a *mortgage intermediary* or any other third party whereby the value of the inducement increases if the *mortgage intermediary* or third party, such as a packager, exceeds a target set for the amount of business referred (for example, a volume override).
- (2) *A firm* must not solicit or accept an inducement whereby the value of the inducement increases if the *firm* exceeds a target set for the amount of business referred.

...

2.7.5R *A firm* must ensure that information provided to a *retail customer* before the conclusion of a *distance contract* about his contractual obligations under that contract conform with the contractual obligations that would be imposed on him under the law applying if the contract were concluded.

#### Unsolicited services

- 2.7.6R (1) *A firm* must not:
- (a) supply a service to a *retail customer* without a prior request on his part, when this activity includes a request for immediate or deferred payment; or
  - (b) enforce any obligations against a *retail customer* in the event of unsolicited supplies of services, the absence of a reply not constituting consent.
- (2) Paragraph (1) applies in relation to *advising on, arranging or entering into a regulated mortgage contract* under an organised distance sales or service-provision scheme run by the *firm* or by an intermediary, who, for the purpose of that supply, makes exclusive use of one or more *means of distance communication* up to and including the time at which the services are supplied.



...

3.6.9R A *non-real time qualifying credit promotion* must:

- (1) describe any *early repayment charge* as an 'early repayment charge' and not use any other expression to describe such charges;
- (2) describe any *higher lending charge* as a 'higher lending charge' and not use any other expression to describe such charges; ~~and~~
- (3) not contain the 'key facts' logo unless it is required by a *rule*; and
- (4) describe any *regulated lifetime mortgage contract* as a 'lifetime mortgage' and not use any other expression to describe such a mortgage.

...

4.1.2R Table: This table belongs to *MCOB 4.1.1R*

(1) Category of firm	(2) Applicable section
<i>mortgage lender</i>  ...	whole chapter except <i>MCOB 4.56</i> and <i>MCOB 4.67</i>

...

4.1.5R In relation to a *regulated lifetime mortgage contract* or a home reversion scheme, this chapter *MCOB 4* is ~~replaced~~ modified by *MCOB 8* (Lifetime mortgages: advising and selling standards).

...

4.4.7R ...

- (2) Provided that the telephone call in (1) has not led the *firm* to conclude that the *customer* is ineligible for any of its *regulated mortgage contracts*, and that the *customer* has provided his contact details, the *firm* must send the *customer* a copy of the initial disclosure document required by *MCOB 4.4.1R*(~~4~~) in the form set out in *MCOB 4 Ann 1R* or *MCOB 4 Ann 2R* and any other information required to be provided, in a *durable medium* within five *business days* of the telephone call (see also *MCOB 4.5.2R*(2)(b) for the equivalent requirement in relation to *distance mortgage mediation contracts*).

...

4.5.2R If the initial contact of a kind in *MCOB 4.4.1R(1)* is with a *retail customer* with a view to concluding a *distance mortgage mediation contract*, a *firm* must:

...

(2) Exemption: telephone sales

(a) This exemption applies if the service is being provided on the telephone and the *customer* wishes to enter into a contract with the *firm*. Provided Subject to the customer gives giving his explicit consent to receiving only limited disclosure information, the firm must, prior to the conclusion of the contract on the telephone, may proceed provide the customer with on the basis of at least the following information in addition to the information in *MCOB 4.4.7R(1)*:

...

(aa) If the customer does not give his explicit consent to receiving limited information, and the parties wish to proceed by telephone, the firm must, prior to the conclusion of the contract, provide orally to the customer all of the information required by (1).

(b) Where (a) or (aa) applies, the *firm* must send the *retail customer* without delay and, at the latest immediately after a contract is concluded, the information in *MCOB 4 Ann 3R* and any other information required to be provided in accordance with *MCOB 4* required by (1), in a *durable medium*.

...

~~Unsolicited services~~

4.5.4R Subject to *MCOB 4.5.5R*, a *firm* must not:

(1) ~~advise on, arrange, or enter into, a distance mortgage mediation contract with a retail customer, without a prior request on his part, when the supply of such service includes a request for immediate or deferred payment; or~~

(2) ~~enforce any obligation against a retail customer in the event of unsolicited supplies of such services, the absence of a reply not constituting consent.~~

4.5.5R ~~*MCOB 4.5.4R* does not apply for a tacit renewal of a distance contract.~~

...

4.9.1AG Firms are reminded that in accordance with MCOB 1.2.3R, they should either comply in full with MCOB or comply with all tailored provisions in MCOB that relate to business loans. Therefore, a firm may only follow the tailored provisions in MCOB 4.9 if it also follows all other tailored provisions in MCOB.

...

4 Ann 1R

Initial disclosure document ("IDD")

R

1 Table:

This Annex belongs to ~~MCOB~~ MCOB 4.4.1R(1)

...

---

## **7 What to do if you have a complaint [Note 18]**

---

...

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 22A]

---

## **8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 18] [Note 23] [Note 24]**

---

...

The following notes do not form part of the IDD

...

Note 9 - this sentence is required only where a firm selects this service option. It may also be omitted if a the firm chooses to list all of the lenders it offers mortgages from instead of the text "a limited number of lenders", in the previous line, so long as the firm offers all of the mortgages generally available from each lender.

...

Note 12 – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer*, it must insert a plain language explanation of this (see specimen for a plain

language example). If the *firm* will pay over to the *customer* any commission the *firm* receives, it may refer to that fact here.

...

Note 14 - if, in section 4, it has been indicated that there will be 'No fee' or that any *fee* will be payable only if the mortgage completes, section 5 may be omitted altogether, and the following sections re-numbered accordingly.

...

Note 21 – insert a short, plain language description of the business for which the *firm* has *permission* in relation to *regulated mortgage contracts*.

...

Note 22A – if the IDD is provided by an authorised professional firm which is exclusively carrying on non-mainstream regulated activities, the authorised professional firm should delete this sentence and refer to the alternative complaints handling arrangements.

...

Note 24 - when a *firm* which is not a *participant firm* provides the IDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained.

...

5.1.3R ...

- (2) In relation to further advances and other variations, MCOB 5 is modified by MCOB 7 (Disclosure at start of contract and after sale) ~~applies in place of MCOB 5~~, regardless of whether they are variations to an existing *regulated mortgage contract*, or are such that they involve the *customer* entering into a new *regulated mortgage contract*.
- (3) In relation to a *regulated lifetime mortgage contract*, MCOB 5 is modified by MCOB 9 (Lifetime mortgages: product disclosure) ~~applies in place of MCOB 5~~.

...

5.6.18R ...

- (3) If the amount on which the *illustration* is based includes the amount that the *customer* wants to borrow plus insurance premiums or insurance-related charges (other than a *higher lending charge* ~~or where the premium is repaid over a term of 12 months or less and no interest is charged on the premium~~) that have been added to the loan:
  - (a) except where (b) applies, this section must include the following text... "plus £[insert amount of premium or charges, or both, to

be added to the loan] for insurance [premiums] [and] [charges] that will be added to the loan – see Section 9 for details."; or

(b) where there are other insurance premiums or insurance-related charges, or both, that the *customer* must pay that have not been added to the loan, this section must include the following text ...: "plus £[insert amount of premium or charges, or both, to be added to the loan] for insurance [premiums] [and] [charges] that will be added to the loan. These and any additional insurance [premiums] [and] [charges] that you need to pay are shown in Section 9."

(4) If the amount on which the *illustration* is based..., Section 3 of the *illustration* must include the following text after the loan amount from *MCOB* 5.6.6R(2): "No fees have been added to this amount but the fees you need to pay are shown in Section 8. For details of any insurance charges, see Section 9."

(5) If the *regulated mortgage contract* on which the *illustration* is based has no charges or payments that must be paid by the *customer* (~~that is, there are no fees to pay in Section 8~~), and no insurance premiums are being added to the loan, ...

...

5.6.42R Section 6 of the *illustration* must contain the following information:

...

(2) the assumed start date that has been used in the *illustration* to estimate the number of payments to be charged at given interest rates ~~must be stated using the following text: "This illustration assumes that the mortgage will start on [insert assumed start date]."~~;

...

5.6.65R The following text must be included at the end of Section 7 'Are you comfortable with the risks?': "The FSA's information sheet 'You can afford your mortgage now, but what if...?' will help you consider the risks. You can get a free copy from [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer), or by calling 0845 ~~606 1234~~ 456 1555."

...

5.6.70R ...

(2) If the *customer* has asked for any fees to be added to the loan, this ~~should~~ must be stated alongside each fee.

...

5.6.82R ...

(2) If the ~~customer~~ *customer* has asked to add any insurance premiums or insurance-related charges to the amount borrowed in accordance with *MCOB 5.6.18R(3)*, the *illustration* must state that this is the case.:

(a) ~~the insurance premiums must be included in Section 3; and~~

(b) ~~the following text must be used in Section 9:~~

~~"The annual insurance premium will be added to your mortgage account and increase the amount you owe. You can pay this premium in full by [insert details of the period of time that the *customer* will have to pay the premium in full before interest is charged on the insurance premium e.g. 'by the end of the month in which the *regulated mortgage contract* starts'] at no extra cost, otherwise interest will be charged at [insert details of the applicable interest rate e.g. 'the same rate as your mortgage' or 'the standard variable rate which is currently x%']."~~

...

5.6.129R If the *regulated mortgage contract* is a *shared appreciation mortgage*, *MCOB 5.6* applies to the *illustration* with the following amendments:

(1) Section 4 'Description of this mortgage' must contain the following additional information and text in this order after the details required by *MCOB 5.6.25R* to *MCOB 5.6.29R*:

...

(f) include this text after the cash examples in (c) (or, if applicable, after the cash examples in (d) or (e)): "This is not an indication of how the actual value of your property may change.";

...

...

5.6.145R The following text must be included at the end of Section 7 'Are you comfortable with the risks?': "The FSA's information sheet 'You can afford your mortgage now, but what if...?' will help you consider the risks. You can get a free copy from [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer), or by calling 0845 ~~606 1234~~ 456 1555."

...

5.7.1AG *Firms* are reminded that, in accordance with *MCOB 1.2.3R*, they should either comply in full with *MCOB* or comply with all tailored provisions in *MCOB*

that relate to business loans. Therefore, a *firm* may only follow the tailored provisions in *MCOB* 5.7 if it also follows all other tailored provisions in *MCOB*.

...

5 Ann 1R

The illustration: table of contents, prescribed text and prescribed section headings and subheadings.

...

13. Using a mortgage intermediary

...

<b>[...] Where can you get more information about mortgages?</b>
The FSA publishes useful guides on choosing a mortgage. These are available free through its website <a href="http://www.fsa.gov.uk/consumer">www.fsa.gov.uk/consumer</a> or by calling 0845 <del>606 1234</del> <u>456 1555</u> . The website also provides Comparative Tables to help you shop around.

...

6.1.4R In relation to a *regulated lifetime mortgage contract*, this chapter, *MCOB* 6, is ~~replaced~~ modified by *MCOB* 9 (Lifetime mortgages; – product disclosure).

...

6.7.1AG *Firms* are reminded that in accordance with *MCOB* 1.2.3R, they should either comply in full with *MCOB* or comply with all tailored provisions in *MCOB* that relate to business loans. Therefore, a *firm* may only follow the tailored provisions in *MCOB* 6.7 if it also follows all other tailored provisions in *MCOB*.

...

7.1.8R In relation to a *regulated lifetime mortgage contract*, this chapter *MCOB* 7 is ~~replaced~~ modified by *MCOB* 9 (Lifetime mortgages; – product disclosure).

...

7.2.1G ...

(2) Where a *firm* provides services to a *customer* in relation to a further advance, rate switch, or addition or removal of a party to the variation ~~of~~ a *regulated mortgage contract*, this chapter also requires that the

*customer* is provided with an *illustration* to make clear the price and features associated with that variation.

...

7.7.1AG Firms are reminded that in accordance with MCOB 1.2.3R, they should either comply in full with MCOB or comply with all tailored provisions in MCOB that relate to business loans. Therefore, a firm may only follow the tailored provisions in MCOB 7.7 if it also follows all other tailored provisions in MCOB.

8.3.3R Table Table of modified cross-references to other rules:

...

Subject	Rule or guidance	Reference in rule or guidance	To be read as a reference to:
...			
Initial disclosure requirements	<i>MCOB</i> 4.4.3G	<i>MCOB</i> 4	<i>MCOB</i> 4 as modified by <i>MCOB</i> 8
<u>Initial disclosure requirements where initial contact is by telephone (for regulated lifetime mortgage contracts only)</u>	<u><i>MCOB</i> 4.4.7R(2)</u>	<u><i>MCOB</i> 4 Ann 1R</u>	<u><i>MCOB</i> 8 Ann 1R</u>
Additional disclosure for <i>distance mortgage mediation contracts</i>	<i>MCOB</i> 4.5	<u><i>MCOB</i> 4</u>	<u><i>MCOB</i> 4 as modified by <i>MCOB</i> 8</u>
...			

8 Ann 1R

Initial disclosure document ("IDD")



R

1 Table:

This annex belongs to *MCOB* 4.4.1R (as modified by *MCOB* 8) and *MCOB* 8.4.1R.

...

---

## **7 What to do if you have a complaint [Note 19]**

---

...

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [The Financial Ombudsman Service does not consider complaints about home reversion schemes]. [Note 3] [Note 23A]

---

## **8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 19] [Note 24] [Note 25]**

---

...

The following notes do not form part of the IDD.

...

Note 10 - this sentence is required only where a *firm* selects this service option. It may also be omitted if a ~~the~~ *firm* chooses to list all of the companies it offers products from instead of the text "a limited number of companies", in the previous line, so long as the *firm* offers all of the products generally available from each company.

...

Note 13 – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer*, it must insert a plain language explanation of this (see specimen for a plain language example). If the *firm* will pay over to the *customer* any commission the *firm* receives, it may refer to that fact here.

...

Note 15 - if, in section 4, it has been indicated that there will be 'No fee' or that any *fee* will be payable only if the product completes, section 5 may be omitted altogether, and the following sections re-numbered accordingly.

...

Note 22 – insert a short, plain language description of the business for which the *firm* has *permission* in relation to *regulated lifetime mortgage contracts*.

...

Note 23A – if the IDD is provided by an *authorised professional firm* which is exclusively carrying on non-mainstream regulated activities, the *authorised professional firm* should delete this sentence and refer to the alternative complaints handling arrangements. It should also omit the information required under Note 3.

...

Note 25 - when a *firm* which is not a *participant firm* provides the IDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained. It should also omit the information required under Note 3.

...

- 9.4.10R (1) In estimating a term under MCOB 9.4.6R(5) a *firm* must:
- (a) use the following mortality table: ~~the PA92 (male or female as appropriate) pensioners' 1991-94 table amounts, projected forward to 2010 from the Continuous Mortality Investigation Reports 16 and 17, PMA92(C=2010) and PFA92(C=2010) for males and females respectively, derivable from the Continuous Mortality Investigation Report 17 published by the Institute of Actuaries and the Faculty of Actuaries in 1998 and 1999 respectively; and~~

...

- 9.4.21R ...
- (4) If the amount on which the *illustration* is based includes the amount that the *customer* wants to borrow plus insurance premiums or insurance-related charges (other than a *higher lending charge* ~~or where the premium is repaid over a term of 12 months or less and no interest is charged on the premium~~) that have been added to the loan or amount to be drawn down:
    - (a) except where (b) applies, this section must include the following text... "plus £[insert amount of premium or charges, or both, to be added to the loan] for insurance [premiums] [and] [charges] that will be added to the loan [or amount drawn down] – see Section 12 for details."; or
    - (b) where there are other insurance premiums or insurance-related charges, or both, that the *customer* must pay that have not been added to the loan, this section must include the following text ... "plus £[insert amount of premium or charges, or both, to be added to the loan] for insurance [premiums] [and] [charges] that will be added to the loan [or amount drawn down]. These and

any additional insurance [premiums] [and] [charges] that you need to pay are shown in Section 12."

- (5) If the amount on which the *illustration* is based ..., Section 4 of the *illustration* must include the following text after the loan amount from *MCOB* 9.4.13R(1): "No fees have been added to this amount but the fees you need to pay are shown in Section 11. For details of any insurance charges, see Section 12.".
- (6) If the *regulated lifetime mortgage contract* on which the *illustration* is based has no charges ~~or payments~~ that must be paid by the *customer* (~~that is there are no fees to pay in Section 11~~), and no insurance premiums are being added to the loan, ...

...

9.4.39R Section 8 of the *illustration* must contain the following information:

...

- (2) the assumed start date that has been used in the *illustration* to estimate the number of payments to be charged at given interest rates ~~must be stated using the following text: "This illustration assumes that the lifetime mortgage will start on [insert assumed start date]."~~;

...

...

9.4.51R The table showing the projection in the section headed "Projection of roll-up of interest" should show annual details in columns under the following headings:

...

- (4) "Interest charged at [insert percentage(s)] ~~per year~~": this must be the interest charge for the year in question, ...

...

...

9.4.69R ...

- (2) If the *customer* has asked for any fees to be added to the loan ~~amount~~, this ~~should~~ must be stated alongside each fee.

9.4.81R ...

(2) If the *customer* has asked to add any insurance premiums or insurance-related charges to the amount borrowed in accordance with *MCOB 9.4.21R(4)*, the *illustration* must state that this is the case.:

(a) ~~the insurance premium(s) must be included in Section 4; and~~

(b) ~~the following text must be used in Section 12:~~

~~"The annual insurance premium will be added to your lifetime mortgage account and increase the amount you owe. You can pay this premium in full by [insert details of the period of time that the *customer* will have to pay the premium in full before interest is charged on the insurance premium e.g. 'by the end of the month in which the lifetime mortgage starts'] at no extra cost, otherwise interest will be charged at [insert details of the applicable interest rate e.g. 'the same rate as your lifetime mortgage' or 'the standard variable rate which is currently x%']."~~

...

9.4.130R If the *regulated lifetime mortgage contract* is a *shared appreciation mortgage*, *MCOB 9.4* applies to the *illustration* with the following modifications:

(1) Section 5 'Description of this mortgage' must contain the following additional information and text in this order after the details required by *MCOB 9.4.24R* to *MCOB 9.4.29R*:

...

(f) include this text after the cash examples in (c) (or, if applicable, after the cash examples in (d) or (e)): 'This is not an indication of how the actual value of your home may change.'

...

...

9 Ann 1R

The illustration: table of contents, prescribed text and prescribed section headings and subheadings.

...

<b>1. About this information</b>
...
The FSA provides useful information on lifetime mortgages and other ways of releasing

...

equity from your home in a booklet called 'Raising money from your home'. You can get this free through the FSA website [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer) or by calling 0845 606 1234 456 1555.

...

12.3.4R Before:

...

- (3) changing all or part of a *regulated mortgage contract* from one ~~type of~~ interest rate to another; ...

...

12.6.2G *Firms* are also reminded that in accordance with *MCOB* 1.2.3R, they should either comply in full with *MCOB* or comply with all tailored provisions in *MCOB* that relate to business loans.

...

13.7.2G *Firms* are reminded that in accordance with *MCOB* 1.2.3R, they should either comply in full with *MCOB* or comply with all tailored provisions in *MCOB* that relate to business loans. Therefore, a *firm* may only follow the tailored provisions in *MCOB* 13.7, if it also follows all other tailored provisions in *MCOB*.

**INSURANCE MEDIATION AND MORTGAGE MEDIATION, LENDING AND  
ADMINISTRATION (MISCELLANEOUS AMENDMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 59 (Approval for particular arrangements);
  - (2) section 138 (General rule-making power);
  - (3) section 139 (Miscellaneous ancillary matters);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157 (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as indicated in this table:

Annex A	31 October 2004 (in part) and 14 January 2005 (in part) (see note)
Annex B	14 January 2005
Annex C	31 October 2004 (in part) and 14 January 2005 (in part) (see note)
Annex D	31 October 2004 (in part) and 14 January 2005 (in part) (see note)
Annex E	14 January 2005
Note - to the extent that a provision relates to any regulated activity in relation to a long-term care insurance contract or a regulated mortgage activity, it comes into force on 31 October 2004. Otherwise it comes into force on 14 January 2005.	

**Amendments to the Handbook**

- D. The Authorisation manual is amended in accordance with Annex A to this instrument.
- E. The Supervision manual is amended in accordance with Annex B to this instrument.
- F. The Integrated Prudential sourcebook is amended in accordance with Annex C to this instrument.
- G. The Interim Prudential sourcebook for Investment Businesses is amended in accordance with Annex D to this instrument.
- H. The Training and Competence sourcebook is amended in accordance with Annex E to this instrument.

**Citation**

- I. This instrument may be cited as the Insurance Mediation and Mortgage Mediation, Lending and Administration (Miscellaneous Amendments) Instrument 2004.

By order of the Board  
16 September 2004

## Annex A

### Amendments to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Mortgages: Conduct of Business Sourcebook (Consequential Amendments to the Handbook) Instrument 2003 (FSA 2003/72) and the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (FSA 2004/01).)

#### AUTH 5 Annex 3

Table: G

<u>SUP 12 (Appointed representatives)</u>	<u>SUP 12 (Appointed representatives)</u>
Applies only if the <i>firm</i> has <i>permission</i> to carry on <i>designated investment business, <u>insurance mediation activity</u> or <u>mortgage mediation activity</u></i> and wishes to appoint, or has appointed, an <i>appointed representative (SUP 12.1.1R(1))</i> .	As column (2).

...

#### AUTH Appendix 4

4.3.8 G It follows that whether or not any particular *person* may be carrying on a *regulated mortgage activity* ‘by way of business’ will depend on his individual circumstances. However, some typical examples where the applicable business test would be likely to be satisfied are where a *person*:

- (1) enters into one or more *regulated mortgage contracts* as lender in the expectation of receiving interest or another form of payment that would enable him to profit from his actions ~~or recover the cost of taking them;~~

...

...

4.4.1 G Article 61(3)(a) of the *Regulated Activities Order* defines a *regulated mortgage contract* as a contract which, at the time it is entered into, satisfies the following conditions:

...

- (2) the contract provides for the obligation of the borrower to repay is to be secured by a first legal mortgage on land (other than timeshare accommodation) in the *United Kingdom*; and

...

#### Provision of credit

4.4.1A G (1) Article 61(3)(c) of the *Regulated Activities Order* states that credit includes a cash loan and any other form of financial accommodation. Although 'financial accommodation' has a potentially wide meaning, its scope is limited by the terms used in the definition of a *regulated mortgage contract* set out in *AUTH* App 4.4.1G. Whatever form the financial accommodation may take, article 61(3)(a) envisages that it must involve an obligation to repay on the part of the individual who receives it.

- (2) In the *FSA's* view, an obligation to repay implies the existence, or the potential for the existence, of a debt owed by the individual to whom the financial accommodation is provided (the 'borrower') to the person who provides it (the 'lender'). Consequently, for any facility under which any form of financial accommodation is being provided, the test is whether it allows for the possibility that the person providing the financial accommodation may be placed in a position where he becomes a creditor of the individual to whom he is providing it. An example of this would be the issue of a guarantee by a bank to a third party for an individual customer (such as a rent guarantee or a performance bond) where the guarantee is secured on a first legal charge over the customer's residential property. In the *FSA's* view, this would amount to a *regulated mortgage contract* as the customer would owe a debt to the bank in the event that the bank had to pay the third party under the guarantee.

...

4.4.8 G The requirement that at least 40% of the land area be used as or in connection with a dwelling means that 'buy to let' loans secured on the property to be let ~~are will usually be excluded, unless~~ However, such loans will not be excluded if:

- (1) the lessee is a 'related person' to the borrower. This will be the case ~~e~~Even if the borrower subsequently takes possession of the property, the loan will still not become a *regulated mortgage contract*, as the conditions set out in *AUTH* App 4.4.1G(1) to (3) were not satisfied at the outset of the contract (see *AUTH* App 4.4.3G); or
- (2) at the time the contract is entered into, the borrower has a real intention to use the land as, or in connection with, a dwelling (for example a member of the British Forces Posted Overseas who buys a property in the *United Kingdom* intending to live there on his return but which he lets out in the meantime).



...

4.4.12 G A number of products, however, are excluded from the definition, such as:

...

- (3) so-called 'home reversion schemes', under which a property owner (usually an older person) sells some or all of his interest in the property in return for a lump sum (usually a proportion of the value of the property sold) and a right to reside at the property for the rest of his life. (It should be noted, however, that the Treasury announced in May 2004 that 'home reversion schemes' are to be regulated by the FSA and that it would be introducing legislation to this effect.)

...

Exclusion: article 25A(1)(b) ~~and (2)~~ arrangements made in the course of administration by authorised person

4.5.9 G Article 29A of the *Regulated Activities Order* excludes from ~~both~~ article 25A(1)(b) (which covers making arrangements for another person to vary the terms of a regulated mortgage contract) ~~and (2)~~ certain activities of an *unauthorised person* who is taking advantage of the exclusion from *administering a regulated mortgage contract* in article 62 (Exclusion: arranging administration by authorised persons) (see *AUTH* App 4.8.4G).

...

4.6.30 G The main exclusion from *advising on regulated mortgage contracts* relates to advice given ...

...

- (2) enter as borrower ~~into~~ into regulated mortgage contracts ~~regulated mortgage contracts or vary the terms of~~ or vary the terms of regulated mortgage contracts entered into by such persons as the borrower.

...

...

4.13.1 G Certain named persons are exempted by the *Exemption Order* from the need to obtain *authorisation*. The following bodies are exempt ...

...

- (3) ~~housing associations or other bodies corporate~~ registered social landlords in Scotland within the meaning of the Housing (Scotland) Act 2001 ~~by Scottish Homes~~ (paragraph 48(2)(b) of the Schedule to the *Exemption Order*) but not their subsidiaries;

...

...

- 4.17.15 G Articles 90 and 91 of the *Regulated Activities Order* include provisions that have the effect of removing from CCA regulation *financial promotions* about *qualifying credit*. Such promotions will not, therefore, be subject to Part IV of the CCA, ~~the Consumer Credit (Advertisements) Regulations 1989 and the Consumer Credit (Content of Quotations) and Consumer Credit (Advertisements) (Amendment) Regulations 1999~~ or regulations made under that Part.

...

#### AUTH Appendix 5

...

- 5.11.6 G (1) The removal of the exclusion for *groups* and *joint enterprises* in article 69 of the *Regulated Activities Order* (Groups and joint enterprises) may have implications for ~~companies~~ a company providing services for:
- (1a) other members of its *group*; or
  - (2b) other participants in a *joint enterprise* of which it is a participant.
- (2) Such *companies* might typically provide risk or treasury management or administration services which may include *regulated activities* relating to a *contract of insurance*. If so, such *companies* will need *authorisation* or exemption if they conduct the activities by way of business (see AUTH App 5.4 (The business test) generally and (3) and (4)). This is unless another exclusion applies.
- (3) In the FSA's view, particular issues arise in applying the by way of business test to group companies. Recital 11 of the Insurance Mediation Directive states that the Directive should apply to persons whose activity consists in providing insurance mediation services to third parties for remuneration. This suggests that the Directive is intended to apply only where the service is provided to a third party. The expression 'third party' is not defined in the Directive. The FSA considers that a group company that is providing services solely for the benefit of other group companies would not normally be regarded as providing services to a third party. The FSA also considers that, as a result, a group company providing services solely for the benefit of other group companies should not normally be regarded as satisfying the requirement that it be remunerated for providing insurance mediation services to third parties. Were a group company to be remunerated other than by another group company, however, the situation may be different. For example, if the group company receives commission from an insurer or broker, that fact would tend to suggest that the company has been rewarded

for providing a service to the insurer or broker. In the FSA's view, it is appropriate to apply this principle to a *group* as defined in section 421 (Group) of the Act.

- (4) The FSA considers that similar principles to those applied to a group company in (2) may be applied to the participants in a joint enterprise. This would be where one participant in the joint enterprise is providing services solely for the benefit of another participant and for the purposes of the joint enterprise. This extends to any person in the same group as a participant in a joint enterprise and who provides insurance mediation services to one or more participants for the purposes of or in connection with the joint enterprise.

...

- 5.11.9 G Article 67 excludes from the activities of *dealing as agent, arranging (bringing about) deals in investments, making arrangements with a view to transactions in investments, and assisting in the administration and performance of a contract of insurance* and *advising on investments*, any activity which:

...

...

- 5.11.16 G Article 72D (Large risks contracts where risk situated outside the EEA) provides an exclusion for large risks situated outside the *EEA*. Broadly speaking, these are risks relating to:

...

- (3) ~~risks relating to~~ land vehicles, fire and natural forces, property damage, motor vehicle liability where the *policyholder* is a business of a certain size;
- (4) ~~certain financial loss where the *policyholder* is a business of a certain size.~~

For a fuller definition ...

...

- 5.13.4 G Table: insurance mediation activities able to be carried on by an appointed representative. This table belongs to AUTH App 5.13.3G.

Type of insurance contract	Regulated activities an appointed representative can carry on
<i>General insurance contract</i>	<ul style="list-style-type: none"> <li>• <i>Dealing in investments as agent;</i></li> <li>• <i>Arranging;</i></li> <li>• <i>Assisting in the administration and performance of a contract of insurance;</i></li> <li>• <i>Advising on investments; and</i></li> <li>• <i>Agreeing to carry on these regulated activities.</i></li> </ul>
<i>Pure protection contract</i>	<ul style="list-style-type: none"> <li>• <u><i>Dealing in investments as agent (but only where the contract is not a long-term care insurance contract);</i></u></li> <li>• <i>Arranging;</i></li> <li>• <u><i>Assisting in the administration and performance of a contract of insurance;</i></u></li> <li>• <i>Advising on investments; and</i></li> <li>• <i>Agreeing to carry on these regulated activities.</i></li> </ul>
<i>Life policy (note that this already has effect prior to 14 January 2005)</i>	<ul style="list-style-type: none"> <li>• <i>Arranging;</i></li> <li>• <u><i>Assisting in the administration and performance of a contract of insurance;</i></u></li> <li>• <i>Advising on investments; and</i></li> <li>• <i>Agreeing to carry on these regulated activities.</i></li> </ul>

...

5.14.5 G In addition to certain named *persons* exempted by the *Exemption Order* from the need to obtain *authorisation*, the following bodies are exempt ...

...

(3) ~~housing associations or other bodies corporate~~ registered social landlords in Scotland within the meaning of the Housing (Scotland) Act 2001 ~~by Scottish Homes~~ but not their subsidiaries;

...

...

5.16 Meaning of insurance mediation

5.16.1 G *AUTH* App 5.16.2G sets out the text of article 2.3 of the *Insurance Mediation Directive*. ...

## Annex B

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (2004/01) and Annex D of the Appointed Representatives Instrument 2004 (2004/09).)

What the governing functions include

...

- 10.6.3A G *PRU 9.1.3R provides that an insurance intermediary, other than a sole trader, must allocate to a director or senior manager the responsibility for the firm's insurance mediation activity. PRU 9.1.4R(1) provides that the firm may allocate this responsibility to one or more of the persons performing a governing function (other than the non-executive director function).*

...

Business for which an appointed representative is exempt

- 12.2.7 G (1) The *Appointed Representatives Regulations* are made by the Treasury under section 39(1) of the *Act*. These regulations describe, among other things, the business for which an *appointed representative* may be exempt, which is business which comprises any of:
- (a) *dealing in investments as agent* (article 21 of the *Regulated Activities Order*) where the transaction relates to a *pure protection contract* (but only where the contract is not a *long-term care insurance contract*) ~~or general insurance contract;~~

...

- (f) *assisting in the administration and performance of a contract of insurance* (article 39A of the *Regulated Activities Order*) ~~where the activity relates to a general insurance contract;~~

...

- 12.2.8 G ...

- (2) The permitted scope of appointment of an *introducer appointed representative* does not include in particular:

...

- (c) *assisting in the administration and performance of a contract of insurance* ~~where the transaction relates to a general insurance contract;~~ or

...

...

12.5.2 G ...

(2) Under the *Appointed Representative Regulations*, an *appointed representative* is treated as representing other counterparties if, broadly, it:

...

(d) *assists in the administration and performance of a contract of insurance* (article 39A of the *Regulated Activities Order*) ~~where the activity relates to a general insurance contract;~~

...

...

12.7.7 R (1)

If:

(a) (i) the scope of appointment of the *appointed representative* is extended to cover *insurance mediation activities* for the first time; and

~~(b)~~ (ii) the *appointed representative* is not included on the *Register* as carrying on *insurance mediation activities* in another capacity; ~~and~~ or

~~(c)~~ (b) the scope of appointment of an *appointed representative* ceases to include *insurance mediation activity*;

the *appointed representative's principal* must give written notice to the *FSA* of that change before the *appointed representative* begins to carry on *insurance mediation activities* under the contract (see *SUP 12.4.9G*) or as soon as the scope of appointment of the *appointed representative* ceases to include *insurance mediation activity*.

## Annex C

### Amendments to the Integrated Prudential sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (2004/01).)

- 9.1.4 R The *firm* may allocate the responsibility for its *insurance mediation activity* under *PRU 9.1.3R* to an *approved person* (or *persons*) performing:
- (1) a *governing function* (other than the *non-executive director function*);  
or  
...
- 9.1.5 G (1) Typically an *insurance intermediary* will appoint a *person* performing a *governing function* (other than the *non-executive director function*) to direct its *insurance mediation activity*. Where this responsibility is allocated to a *person* performing another function, the *person* performing the *apportionment and oversight function* with responsibility for the apportionment of responsibilities under *SYSC 2.1.1R* must ensure that the *firm's insurance mediation activity* under *PRU 9.1.3R* is appropriately allocated.
- (2) ...
- (3) In the case of a *sole trader*, the *sole trader* will be responsible for the *firm's insurance mediation activity*, whether or not he is himself a *person approved to perform the sole trader function*.
- ...
- 9.1.7 G The *FSA* will specify in the *FSA Register* the name of the *persons* to whom the responsibility for the *firm's insurance mediation activity* has been allocated under *PRU 9.1.3R* by inserting after the relevant *controlled function* the words “(insurance mediation)”. In the case of a *sole trader*, the *FSA* will specify in the *FSA Register* the name of the *sole trader* as the 'contact person' in the *firm*.
- ...
- 9.2.8 G The minimum *limits of indemnity* for a *A firm* whose *Part IV permission* covers more than one *regulated activity* within the scope of this section ~~will need to comply with~~ is the higher of the *limits of indemnity* as set out in *PRU*

9.2.13R and the *limits of indemnity* as set out in *PRU 9.2.15R*. If the *firm* opts for a single comparable guarantee to finance the claims which might arise as a result of both activities, the provisions set out in *PRU 9.2.1R(3)* apply. ~~professional indemnity insurance requirements for each of these activities. However, this does not necessarily mean that the *firm* should purchase two or more separate *contracts of insurance*. It could, for example, purchase one contract that covers all of its activities, but which contains separate *limits of indemnity* and excesses for each individual activity.~~

Minimum limits of indemnity: insurance ~~intermediary~~ mediation activity

...

9.2.13 R ~~In relation to *insurance mediation activity*, If the *firm* is an *insurance intermediary*, then~~ the minimum *limits of indemnity* referred to in *PRU 9.2.10R(2)* are:

...

...

Minimum limits of indemnity: mortgage ~~intermediary~~ mediation activity

9.2.15 R ~~In relation to *mortgage mediation activity*, If the *firm* is a *mortgage intermediary*, then~~ the minimum *limit of indemnity* referred to in *PRU 9.2.10R(2)* is the higher of 10% of annual income (see *PRU 9.3.42R*) up to £1 million, and:

(1) ...

...

- 9.3.45 G
- (1) The purpose of *PRU 9.3.44R* is to ensure that the capital resources requirement is calculated on the basis only of brokerage and other amounts earned by a *firm* which are its own income.
  - (2) For the purposes of *PRU 9.3.43R* and *PRU 9.3.44R*, a *firm's* annual income includes *commissions* and other amounts the *firm* may have agreed to pay to other *persons* involved in a transaction, such as sub-agents or other intermediaries.
  - (3) A *firm's* annual income does not, however, include any amounts due to another *person* (for example, the product provider) which the *firm* has collected on behalf of that other *person*.



## Annex D

### Amendments to the Interim Prudential sourcebook for Investment Businesses

In this Annex underlining indicates new text and striking through indicates deleted text.

Chapter 13: Financial Resources Requirements for Personal Investment Firms

Appendix 13(1) – Defined terms for Chapter 13

...

Category A3 firm      a *Category A firm* whose *permission* includes only *insurance mediation activity in relation to non-investment insurance contracts, mortgage mediation activity, assisting in the administration and performance of contracts of insurances,* *arranging* transactions in *investments, advising on investments* and, if applicable *managing investments*;

...

Category B3 firm      a *Category B firm* whose *permission* includes only *insurance mediation activity in relation to non-investment insurance contracts, mortgage mediation activity, assisting in the administration and performance of contracts of insurances,* *arranging* transactions in *life policies* and other insurance contracts, *advising on investments* and receiving and transmitting, on behalf of investors, orders in relation to *securities* and units in *collective investment schemes*;

## Annex E

### Amendments to the Training and Competence sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

- 2.1.2 R (1) In relation to *designated investment business*:
- (a) unless (aa) applies, this chapter applies to a *UK domestic firm*...
  - (aa) if the *designated investment business* constitutes *insurance mediation activity*, this chapter applies to a *UK domestic firm* in respect of its *employees* who engage in or oversee activities (to the extent indicated in *TC 2.1.4R*):
    - (i) from an establishment maintained by the *firm* (or its appointed representative) in the *United Kingdom*; or
    - (ii) from a *branch* established in another *EEA State*;  - (b) unless (bb) applies, ~~t~~ This chapter applies to an *overseas firm*...
  - (bb) if the *designated investment business* constitutes *insurance mediation activity*, this chapter does not apply to an *overseas firm* which is an *EEA firm*.
- ...
- (3) In relation to *insurance mediation activities* in respect of *non-investment insurance contracts* carried on with or for a *customer*, this chapter applies to any such activity carried on by a *UK domestic firm*:
- (a) from an establishment maintained by the *firm* (or its appointed representative) in the *United Kingdom*; or
  - (b) from a *branch* established in another *EEA State*.

**AUTHORISATION MANUAL (AMENDMENT NO 7) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 November 2004.

**Amendments to the Authorisation manual**

- C. The Authorisation manual is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Authorisation Manual (Amendment No 7) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendment to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text.

- 8.3.18 G In the case of a decision within the scope of *AUTH*, ~~the FSA's general policy is not normally to publish *final notices* about publications in a way which would disclose confidential information about them or prejudice consumer interests~~ the FSA's policy is to publish relevant details about the decision. The details may include the identity of the applicant or the name of any *person* who is the subject of an application such as an application for approval under section 60 of the *Act*. Other details may include the nature of the application and grounds for the decision. The FSA will seek to publish these details in a way which is fair to the *person* who is named and which is not prejudicial to the interests of consumers.

**COMPENSATION SOURCEBOOK (AMENDMENT NO 3) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 213 (The compensation scheme);
  - (4) section 214 (General);
  - (5) section 216 (Continuity of long-term insurance policies); and
  - (6) section 217 (Insurers in financial difficulties).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 October 2004.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Compensation Sourcebook (Amendment No 3) Instrument 2004.

By order of the Board  
16 September 2004

## Annex

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

3.3.2C R ...

(4) Where a payment is due under (1), FSCS may:

(a) make payments to or on behalf of *eligible claimants* on such terms (including any terms requiring repayment in whole or in part) and on such conditions as it thinks fit (subject to (1)); or

(b) secure that payments (subject to (1)) are made to or on behalf of any such *eligible claimants* by the liquidator, administrator or provisional liquidator by giving him an indemnity covering any such payments or any class or description of such payments.

...

Insurance undertakings in financial difficulties

3.3.3 R (1) The FSCS may take such measures as it considers appropriate for the purpose of safeguarding the rights of *eligible claimants* under *protected contracts of insurance* which are:

...

(b) *Long-term insurance contracts* with a *relevant person* which is an *insurance undertaking* in financial difficulties (see COMP 3.3.6R) but ~~which is not the subject of any of the proceedings listed in COMP 6.3.3R (1) to (5) in respect of which the FSCS is not securing continuity of insurance within COMP 3.3.1R;~~

...

11.2.3 R Where an *eligible claimant* has a *claim* under a *protected contract of insurance* against a *relevant person* that is in administration, provisional liquidation, or liquidation, the FSCS may, ~~unless arrangements have been or are being made to secure continuity of insurance or other measures are being taken to safeguard *eligible claimants* under COMP 3.3:~~

...

**NEW COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK  
(INTRODUCTION OF NORTHERN IRELAND OEICS) (AMENDMENT)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1)
    - (a) section 138 (General rule-making power);
    - (b) section 145 (Financial promotion rules);
    - (c) section 156 (General supplementary powers);
    - (d) section 157(1) (Guidance);
    - (e) section 340 (Appointment); and
    - (f) paragraph 17(1) of Schedule 1 (Fees); and
  - (2) regulation 6 (FSA rules) of The Open-Ended Investment Companies Regulations (Northern Ireland) 2004 (SR 2004/335).
- B. The rule-making powers identified above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 November 2004.

**Amendments to the New Collective Investment Schemes sourcebook**

- D. The New Collective Investment Schemes sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the New Collective Investment Schemes Sourcebook (Introduction of Northern Ireland OEICs) (Amendment) Instrument 2004.

By order of the Board  
16 September 2004

## Annex A

### Amendments to the New Collective Investment Schemes sourcebook

In this Annex underlining indicates new text.

Table: contents of the instrument constituting the scheme

3.2.6 R This table belongs to *COLL* 3.2.4R (Matters which must be included in the instrument constituting the scheme)

...

ICVCs: unit transfers

21 A statement that the *person* designated for the purposes of paragraph 4 of Schedule 4 to the *OEIC Regulations* (Share transfers) or for an ICVC established in Northern Ireland, paragraph 3 of Schedule 4 to the Open-Ended Investment Companies Regulations (Northern Ireland) 2004 (SR 2004/335) is the *person* who, for the time being, is the *ACD* of the *ICVC*.

...

Consequences of commencement of winding up or termination

7.3.6 R (3) ...

(b) if winding up an *ICVC*, publish notice of the commencement of the winding up (if the head office of the *ICVC* is situated in England and Wales or Wales) in the London Gazette, or (if the head office of the *ICVC* is situated in Scotland) in the Edinburgh Gazette or (if the head office of the *ICVC* is situated in Northern Ireland) in the Belfast Gazette.



## Annex B

### Amendment to the Glossary

In this Annex underlining indicates new text.

Amend the following definition as shown:

*OEIC Regulations*      the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228) or for an ICVC established in Northern Ireland, the Open-Ended Investment Companies Regulations (Northern Ireland) 2004 (SR 2004/335).

**INTERIM PRUDENTIAL SOURCEBOOK FOR BUILDING SOCIETIES  
(AMENDMENT NO 9) INSTRUMENT 2004**

**Power exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 July 2005.

**Amendments to the Interim Prudential sourcebook for Building Societies**

- C. The Interim Prudential sourcebook for Building Societies is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Interim Prudential Sourcebook for Building Societies (Amendment No 9) Instrument 2004.

By order of the Board  
20 October 2004

## Annex

### Amendments to the Interim Prudential sourcebook for Building Societies

In this Annex underlining indicates new text.

Amend IPRU(BSOC), Volume 1, Annex 4B, Chapter CD, s7 as follows:

See chs TS and TV	3	Banks may apply to the FSA to include credit derivatives in recognised models under CAD1 and also under <del>CAD2</del> <u>VaR</u> models. Banks may apply for recognition of <del>CAD2</del> <u>VaR</u> models which quantify partial offsets for specific risk positions where there is a maturity or asset mismatch.
	...	
	10	...
See ch TI s5 <u>46G</u>	...	a) For the specific risk position to be treated as a qualifying debt item, the reference asset should meet the standard conditions for a qualifying debt item as defined in the chapter on interest rate position risk.
	17	...
See ch TI s5 <u>46G</u>	...	a) Qualifying debt items are defined in the chapter on interest rate position risk.
	19	...
See ch TI s3 <u>37G</u>	(a)	the underlying and reference assets are issued by the same obligor;
	(b)	the underlying and reference asset specific risk positions meet the matching criteria set out in the chapter on interest rate position risk; and
	...	
See ch TI s6	23	Credit default products do not normally create a general market risk position.
	...	
	29	...
See ch TI s5 <u>46G</u>	a)	Qualifying debt items are defined in the chapter on interest rate position risk.
...		

Amend IPRU(BSOC), Volume 1, Annex 4B, Chapter CD, s8.3 as follows:

- 5 The option ~~carve-out treatment~~ standard method should be used for credit spread options only after consultation with the FSA. Banks should normally apply for recognition of option models covering credit spread options.

...

Amend IPRU(BSOC), Volume 1, s10 Chapter SE, s3.2.2 as follows:

- 4 (b) As a repackager, it sells *investment grade* third party *financial instruments* via its balance sheet to an SPV that then rebundles them and resells them to investors.
- a) In a *repackaging scheme*, the repackager is *not* the original lender and is therefore subject to fewer limitations than an originator.
- b) Where the assets are influenced in credit quality by reference to the repackaging bank, the bank will be regarded as an originator.
- c) For a definition of *investment grade* see the interest rate position risk chapter. Where the securities to be repackaged are not rated, the bank should be able to demonstrate that the asset are of a comparable quality.

See ch  
TI s9  
47G

...

Amend IPRU(BSOC), Volume 1, s10 Chapter SE, s9.3 as follows:

- 5 Securities issued that are deemed to be investment grade by relevant rating agencies, as defined, are deemed not to constitute credit enhancement if there is already sufficient credit enhancement within the terms of this section.

...

Amend IPRU(BSOC), Volume 1, s10 Chapter SE, s11.1 as follows:

- 3 ...
- a) ...
- b) ...
- c) The ability to deal in securities is limited to securities deemed to be of investment grade by a relevant rating agency as defined. Securities below investment grade fall within the definition of credit enhancement as described below.

See s6.2

See s9  
and ch  
TI s9  
47G

**MORTGAGE FIRMS AND INSURANCE INTERMEDIARIES (FEES)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers);
  - (2) section 157(1) (Guidance); and
  - (3) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 31 October 2004 (in part) and 14 January 2005 (in part). To the extent that a provision relates to any regulated activity in relation to a long-term care insurance contract or a regulated mortgage activity, it comes into force on 31 October 2004. Otherwise it comes into force on 14 January 2005.

**Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with Annex A to this instrument.

**Amendments to the Professional Firms sourcebook**

- E. The Professional Firms sourcebook is amended in accordance with Annex B to this instrument.

**Amendments to the Authorisation manual**

- F. The Authorisation manual is amended in accordance with Annex C to this instrument.

**Citation**

- G. This instrument may be cited as the Mortgage Firms and Insurance Intermediaries (Fees) Instrument 2004.

By order of the Board  
20 October 2004

## Annex A

### Amendments to the Supervision manual

In this Annex underlining indicates new text, striking through indicates deleted text.

#### Transitional provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
16	...				
17	<u>SUP 20.4.4R(4)</u>	<u>R</u>	<u>The periodic fee modification set out in SUP 20.4.4R(4) does not apply to the A.2, A.18 and A.19 activity groups until 1 April 2005.</u>	<u>From 31 October 2004 to 31 March 2005</u>	<u>1 April 2002</u>

...

SUP 20 Ann 1R

#### Activity groups, tariff bases and valuation dates applicable

##### Part 1

...

SUP Table:

2

Activity group	Fee-payer falls in the activity group if
...	...
<b>A.13 Advisory arrangers, dealers or brokers (not holding or controlling client money or assets, or both)</b>	<p>(1) it is an <i>authorised professional firm</i> and <b>ALL</b> the <i>regulated activities</i> in its <i>permission</i> are limited to <i>non-mainstream regulated activities</i>;</p> <p><b>OR</b></p> <p>(2) its <i>permission</i>:</p> <p>(a) includes one or more of the following, in relation to one or more <i>designated investments</i>:</p> <ul style="list-style-type: none"> <li>• <i>dealing in investments as agent</i>;</li> <li>• <i>arranging (bringing about) deals in investments</i>;</li> <li>• <i>making arrangements with a view to transactions in investments</i>;</li> <li>• <i>dealing as principal in investments</i> where the activity is carried on as a matched principal broker, <i>oil market participant</i>, <i>energy market participant</i> or <i>local</i>;</li> <li>• <i>advising on investments (except pension transfers and pension opt-outs)</i>;</li> <li>• <i>advising on pension transfers and pension opt-outs</i>;</li> </ul>

	<ul style="list-style-type: none"> <li>• <i>advising on syndicate participation at Lloyd's</i>;</li> </ul> <p>(b) <b>BUT NONE</b> of the following:</p> <ul style="list-style-type: none"> <li>• <i>effecting contracts of insurance</i>;</li> <li>• <i>carrying out contracts of insurance</i>;</li> <li>• <i>safeguarding and administration of assets</i>;</li> <li>• <i>arranging safeguarding and administration of assets</i>;</li> </ul> <p><b>AND</b></p> <p>(c) <b>MUST EITHER</b>, in connection with its <i>designated investment business</i>:</p> <ul style="list-style-type: none"> <li>• have a <i>requirement</i> that prohibits the <i>firm</i> from holding or controlling <i>client money</i>, or both;</li> </ul> <p><b>OR</b></p> <ul style="list-style-type: none"> <li>• if it does not have such a <i>requirement</i>, only holds or controls <i>client money</i> (or both), arising from an agreement under which <i>commission</i> is rebated to a <i>client</i>;</li> </ul> <p>...</p>
...	...

...

## Part 2

This table indicates the tariff base for each fee-block. The tariff base is the means by which we measure the 'amount of business' conducted by a *firm*.

Activity group	Tariff-base
...	...
<b>A.2</b>	<p>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</p> <p><b><u>NUMBER OF MORTGAGES ENTERED INTO AND ADMINISTERED</u></b></p> <p><u>The number of new mortgage contracts entered into;</u></p> <p><b><u>AND</u></b></p> <p><u>The number of mortgage contracts being administered, multiplied by 0.5.</u></p> <p><b><u>Notes:</u></b></p> <p>(1) <u>For 2004/05 and 2005/06 firms have supplied this data on their 'HSF1' or 'variation of permission' application form.</u></p> <p>(2) <u>In this context a "mortgage" means a loan secured by a first charge over residential property in the <i>United Kingdom</i>. For the measure of the number of contracts being administered, each first charge counts as one contract, irrespective of the number of loans involved.</u></p> <p>(3) <u>Mortgages administered include those that the <i>firm</i> administers on behalf of other <i>firms</i>.</u></p>
...	...
<b>A.18</b>	<p>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</p> <p><b><u>ANNUAL INCOME</u></b></p>

	<p>(a) <u>the net amount retained by the <i>firm</i> of all brokerages, fees, commissions and other related income (eg administration charges, overrides, profit shares) due to the <i>firm</i> in respect of or in relation to <i>mortgage mediation activity</i> (or activities which would have been <i>mortgage mediation activity</i> if they had been carried out after 30 October 2004);</u></p> <p><b><u>Plus</u></b></p> <p>(b) <u>for any <i>mortgage mediation activity</i> carried out by the <i>firm</i> for which it receives payment from the lender on a basis other than that in (a), the value of all new mortgage advances resulting from that activity multiplied by 0.004;</u></p> <p><b><u>Plus</u></b></p> <p>(c) <u>if the <i>firm</i> is a <i>mortgage lender</i>, the value of all new mortgage advances which are or would be <i>regulated mortgage contracts</i> if they had been made after 30 October 2004 (other than those made as a result of <i>mortgage mediation activity</i> by another <i>firm</i>), multiplied by 0.004.</u></p> <p><b><u>Notes on annual income:</u></b></p> <p>(1) <u>For 2004/05 and 2005/06 <i>firms</i> have supplied this data on their 'HSF1' or 'variation of permission' application form.</u></p> <p>(2) <u>For the purposes of calculating annual income, "net amount retained" means all the commission, fees, etc. in respect of <i>mortgage mediation activity</i> that the <i>firm</i> has not rebated to customers or passed on to other <i>firms</i> (for example, where there is a commission chain). Items such as general business expenses (eg employees' salaries, overheads) should <b>not</b> be deducted.</u></p> <p>(3) <u>The <i>firm</i> must include in its income calculation, on the same basis as above, earnings from those who will become its <i>appointed representatives</i> immediately after <i>authorisation</i>.</u></p> <p>(4) <u>Reference to a "<i>firm</i>" above also includes reference to any <i>person</i> who carried out activities which would be <i>mortgage mediation activity</i> if they had been carried out after 30 October 2004.</u></p>
A.19	<p>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</p> <p><b><u>ANNUAL INCOME</u></b></p> <p>(a) <u>the net amount retained by the <i>firm</i> of all brokerages, fees, commissions and other related income (eg administration charges, overrides, profit shares) due to the <i>firm</i> in respect of or in relation to <i>insurance mediation activity</i> (or activities which would have been <i>insurance mediation activity</i> if they had been carried out after 13 January 2005) in relation to <i>general insurance contracts</i> or <i>pure protection contracts</i>;</u></p> <p><b><u>Plus</u></b></p> <p>(b) <u>in relation to the activities set out in (a), for any <i>insurance mediation activity</i> carried out by the <i>firm</i> for which it receives payment from the <i>insurer</i> on a basis other than that in (a), the amount of <i>premiums</i> receivable on the <i>contracts of insurance</i> resulting from that activity multiplied by 0.07;</u></p> <p><b><u>Plus</u></b></p> <p>(c) <u>if the <i>firm</i> is an <i>insurer</i>, in relation to the activities set out in (a), the amount of</u></p>



	<p><u>premiums receivable on its contracts of insurance multiplied by 0.07, excluding those contracts of insurance which:</u></p> <p>(i) <u>result from insurance mediation activity by another firm, where a payment has been made by the insurer to the firm under (a); or</u></p> <p>(ii) <u>the insurer reports in, and pays a fee under, the A.4 activity group; or</u></p> <p>(iii) <u>are not general insurance contracts or pure protection contracts.</u></p> <p><b><u>Notes on annual income:</u></b></p> <p>(1) <u>For 2004/05 and 2005/06 firms have supplied this data on their 'HSF1' or 'variation of permission' application form.</u></p> <p>(2) <u>For the purposes of calculating annual income, "net amount retained" means all the commission, fees, etc. in respect of insurance mediation activity that the firm has not rebated to customers or passed on to other firms (for example, where there is a commission chain). Items such as general business expenses (eg employees' salaries, overheads) should <b>not</b> be deducted.</u></p> <p>(3) <u>The firm must include in its income calculation, on the same basis as above, earnings from those who will become its appointed representatives immediately after authorisation.</u></p> <p>(4) <u>Reference to a "firm" above also includes reference to any person who carried out activities which would be insurance mediation activity (in respect of general insurance contracts or pure protection contracts) if they had been carried out after 13 January 2005.</u></p>
...	...

### Part 3

This table indicates the valuation date for each fee-block. A firm can calculate its tariff data by applying the tariff bases set out in Part 2 with reference to the valuation dates shown in this table.

Activity group	Tariff-base
...	...
A.2	<p><del>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</del></p> <p><u>Number of mortgages entered into in the twelve months ending 31 December.</u></p> <p><b><u>AND</u></b></p> <p><u>Number of mortgages being administered on 31 December.</u></p>
...	...
A.18	<p><del>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</del></p> <p><u>Annual income (AI) for the financial year ended in the calendar year ending 31 December.</u></p>
A.19	<p><del>Not applicable. [Note: will be made to come into effect from 31 October 2004.]</del></p> <p><u>Annual income (AI) for the financial year ended in the calendar year ending 31 December.</u></p>
...	...

## Annex B

### Amendments to the Professional Firms sourcebook

In this Annex underlining indicates new text.

PROF 6 Ann 1R

...

Table: Fees payable by Designated Professional Bodies

...

Notes

- (1) The FSA register will include details of exempt professional firms carrying out insurance mediation activity.
- (2) In addition to the periodic fees shown above, the sum of £50,000 will be due from the designated professional bodies, divided between the bodies in proportion to the number of exempt professional firms each has on the FSA register on 14 January 2005. This is a contribution towards the costs of developing this part of the FSA register.
- (3) Each of the designated professional bodies will be invoiced for the appropriate amount in January 2005. The invoices must be paid on or before 28 February 2005.

## Annex C

### Amendments to the Authorisation manual

In this Annex underlining indicates new text.

AUTH 4 Ann 1R

...

#### Part 2 – Complexity Groupings

Straightforward cases

Activity grouping	Description
...	...
<u>A.18</u>	<u>Mortgage lenders, advisers and arrangers (excluding mortgage lenders)</u>
<u>A.19</u>	<u>General insurance mediation</u>

Moderately complex cases

Activity grouping	Description
A.1	<u>E-money issuers only</u>
<u>A.2</u>	<u>Mortgage lenders and administrators</u>
...	...

...

## **PRUDENTIAL REPORTING FOR MARKET RISK BY BANKS INSTRUMENT 2004**

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### **Commencement**

- C. The annexes to this instrument come into force as follows:
- (1) Annexes A and B come into force on 1 November 2004; and
  - (2) Annex C comes into force as follows:
    - (a) (in the case of a firm that under paragraph 1 of Chapter TRANS of IPRU(BANK) is treating the material added to IPRU(BANK) by the Interim Prudential Sourcebook for Banks (Market Risk) Instrument 2004 as being in force) it comes into force on 1 November 2004; and
    - (b) (in other cases) it comes into force on 1 July 2005.

### **Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with the Annexes to this instrument.

### **Citation**

- E. This instrument may be cited as the Prudential Reporting for Market Risk by Banks Instrument 2004.

By order of the Board  
20 October 2004

## **Annex A**

### **Amendments to SUP 16 Ann 1R**

In this Annex, underlining indicates new text and striking through indicates deleted text.

Amend Form BSD3 (Capital Adequacy Return) as follows. The pages of the form that are changed are the cover page and pages 24, 25, 33, 35 and 36 (these are in the position of pages 3 to 8 of this instrument).



# FORM BSD3 - Capital Adequacy Return

Reporting institution \_\_\_\_\_

as at. 

--	--	--

 FSA number \* 

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(eg 31 12 2001)

Unconsolidated/solo consolidated/consolidated - tick as appropriate

Unconsolidated  Solo consolidated  Consolidated

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

Tel No \_\_\_\_\_ Ext \_\_\_\_\_

### Notes on Completion

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA for guidance.
- 2 Complete the return quarterly on an unconsolidated/solo consolidated basis as at end of March, June, September and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (see SUP 8).
- 3 Complete the return half-yearly on a consolidated basis as at end of June and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (see SUP 8).
- 4 Enter amounts to the nearest thousands omitting £000s/€000s. Calculated amounts should be rounded to the nearest thousands, or two decimal places as appropriate.
- 5 For definitions of items, refer to the Guidance Notes
- 6 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 7 Submit within 10 business days for unconsolidated/solo consolidated returns and 20 business days for consolidated returns or 12 and 22 business days respectively for those institutions reporting electronically to:

**The Financial Services Authority**  
**c/o Monetary and Financial Statistics Division**  
**Domestic Banking Statistics (HO-4)**  
**Bank of England**  
**Threadneedle Street**  
**London EC2R 8AH**

- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
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March 2004 January 2005

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

# MARKET RISKS IN THE TRADING BOOK

<b>I STANDARD APPROACH FOREIGN EXCHANGE RISK</b>		Capital Requirement (000)s
B150	For basic approach (from Appendix B-V).....	
B160	For backtesting approach (from Appendix B-V).....	
B170	Additional Capital Charge for Options.....	
B170.1	Using Curve Out.....	
B170.2	Using CAD1 Models Approach.....	
<u>B170.3</u>	<u>Using the standard method</u> .....	
<u>B170.4</u>	<u>Using the hedging method</u> .....	
B180	<b>Total foreign exchange risk requirement</b> .....	

<b>INTEREST RATE POSITION RISK</b>		Amount (000s)	Specific Risk Weights	Capital Requirement (000)s
B190	Specific Risk.....			
B190.1	.....		0.00%	
B190.2	.....		0.25%	
B190.3	.....		1.00%	
B190.4	.....		1.60%	
B190.5	.....		8.00%	
B200	General Market Risk (from Appendix B-VI).....			
B210	Additional Capital Charge for Options:.....			
B210.1	Using Curve Out.....			
B210.2	Using CAD1 Models Approach.....			
<u>B210.3</u>	<u>Using the standard method</u> .....			
<u>B210.4</u>	<u>Using the hedging method</u> .....			
B215	Embedded Interest Rate Risk in Equity Derivatives.....			
B220	<b>Total interest rate position risk requirement</b> .....			

		Capital Requirement (000s)
<b><u>EQUITY POSITION RISK REQUIREMENT</u></b>		
B230	Specific Risk (from Appendix B-VII).....	
B240	General Market Risk (from Appendix B-VII).....	
B250	Additional Capital Charge for Options:.....	
B250.1	Using Carve Out.....	
B250.2	Using CAD1 Models Approach.....	
<u>B250.3</u>	<u>Using the standard method</u> .....	
<u>B250.4</u>	<u>Using the hedging method</u> .....	
B270	<b>Total equity position risk <u>requirement</u></b> .....	

		Capital Requirement (000s)
<b><u>COMMODITY POSITION RISK REQUIREMENT</u></b>		
B280	Commodity position risk (from Appendix B-VIII).....	
B282	Additional Capital Charge for Options:.....	
B282.1	Using Carve Out.....	
B282.2	Using CAD1 Models Approach.....	
<u>B282.3</u>	<u>Using the standard method</u> .....	
<u>B282.4</u>	<u>Using the hedging method</u> .....	
B284	<b>Total commodity position risk <u>requirement</u></b> .....	

		Capital Requirement (000s)
<b>II INTERNAL MODELS APPROACH</b>		
B290	Previous day's value at risk.....	
B300	Average of previous 60 days' value at risk .....	
B310	Multiplication factor (rounded to 2 decimal places and multiplied by 100) .	
B320	Capital requirement for general market risk .....	
B330	Capital surcharge for specific risk .....	
B340	<b>Total capital requirement for risks subject to internal models</b> (items B320 + B330) ....	



## APPENDIX B-V: CAPITAL REQUIREMENT FOR FOREIGN EXCHANGE POSITION RISK REQUIREMENT (000s)

			<b>Column 1</b> Net Overall Long (short) Position (1 = 2 + 3)	<b>Column 2</b> Positions to be treated under basic method	<b>Column 3</b> Positions being treated under backtesting approach
BASE CURRENCY					
Other Currencies					
Belgium/Luxembourg Francs	BE	BELG			
Canadian Dollars	CA	CANA			
Danish Kronor	DK	DENM			
EUROS	ER	EURO			
French Francs	FR	FRAN			
Deutschmarks	DE	RGER			
Irish Pounds	IE	EIRE			
Italian Lire	IT	ITAL			
Japanese Yen	JP	JAPA			
Netherlands Guilders	NL	NETH			
Spanish Pesetas	ES	SPAI			
Swedish Kroner	SE	SWED			
Swiss Francs	CH	SWIT			
Sterling	UK	UKIN			
US Dollars	US	USA			
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.....					
Other Material currencies .....	U9	UNAL			
Other Aggregate Net Long Positions		OTHL			
Other Aggregate Net Short Positions		OTHS			
<b>TOTAL</b>			<b>ZERO</b>		
Higher of aggregate net short/long open positions					
GOLD	GO	GOLD			
.....					
SUM OF GROSS POSITION.....					
CAPITAL REQUIREMENT.....					

**APPENDIX B-VI: CAPITAL REQUIREMENT INTEREST RATE GENERAL MARKET RISK - continued (000s)**

			6	7	8	9	10
			Zone Three Net Short Position	Maturity based approach method (Method one)	Duration based approach method (Method two)	Simplified Maturity Method	Total General Market Interest Rate Risk (7 + 8 + 9)
Australia	AU	AUSL					
Austria	AT	AUSR					
Belgium	BE	BELG					
Brazil	BR	BRAZ					
Canada	CA	CANA					
Denmark	DK	DENM					
EUROS	ER	EURO					
Finland	FI	FINL					
France	FR	FRAN					
Germany	DE	RGER					
Greece	GR	GREE					
Ireland	IE	EIRE					
Italy	IT	ITAL					
Japan	JP	JAPA					
Malaysia	MY	MALA					
Mexico	MX	MEXI					
Netherlands	NL	NETH					
Norway	NO	NORW					
Portugal	PT	PORT					
Singapore	SG	SING					
South Africa	RA	SAFR					
Spain	ES	SPAI					
Sweden	SE	SWED					
Switzerland	CH	SWIT					
Turkey	TR	TURK					
UK	UK	UKIN					
Sterling Index Linked Gilts							
USA	US	USA					
Other Material Countries							
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.....							
Other.....	U9	UNAL					
Non Material Countries	XF	NONM					
TOTAL	.....						

**APPENDIX B-VII: EQUITY POSITION RISK (000s)**

**Gross Positions for Specific Risk**

			1	2	3	4
			Positions attracting 8% specific- Execution risk	Positions attracting 4% specific- Execution risk	Positions attracting 0% specific- Execution risk	Total Gross Equity Positions for specific -Execution risk (1 + 2 + 3)
<b>Positions, including positions in indices, allocated by country</b>						
Australia	AU	AUSL.....				
Belgium	BE	BELG.....				
Canada	CA	CANA.....				
France	FR	FRAN.....				
Germany	DE	RGER....				
Japan	JP	JAPA.....				
Netherlands	NL	NETH.....				
Spain	ES	SPAI.....				
Sweden	SE	SWED....				
Switzerland	CH	SWIT.....				
United Kingdom	UK	UKIN.....				
United States	US	USA.....				
Denmark	DK	DENM....				
Finland	FI	FINL.....				
Greece	GR	GREE.....				
Ireland	IE	EIRE.....				
Italy	IT	ITAL.....				
Luxembourg	LU	LUXE.....				
Portugal	PT	PORT.....				
.....						
.....						
.....						
.....						
.....						
.....						
Other material ctry.	U9	UNAL				
Non material ctry...	XF	NONM				
TOTAL.....						

## Annex B

### Amendments to SUP 16 Ann 2G

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Part 1

#### **BSD3 REPORTING INSTRUCTIONS**

...

#### **BSD3-SECTION B: TRADING BOOK FOR SOLO BANK AND LINE BY LINE CONSOLIDATED ENTITIES**

##### **General Notes**

1 For consolidated returns, the companies to be included in the consolidation should be those agreed between the reporting institution and the FSA in accordance with the FSA's Policy on Consolidated Supervision (Chapter CS (Consolidated supervision) of the FSA Policy Guide/IPRU (BANK)).

1A New market risk provisions were added to IPRU(BANK) in July 2004. They come into force for all banks on 1 July 2005. However banks may choose to apply them before then in accordance with paragraph 1 of chapter TRANS of IPRU(BANK).

If a bank has chosen to apply the new provisions before 1 July 2005 the following applies.

- (1) It should use boxes B170.2-B170.4, B210.2-B210.4, B250.2-B250.4 and B282.2-B282.4 as appropriate.
- (2) It should not use boxes B160, B170.1, B210.1, B250.1 or B282.1.
- (3) It should use these guidance notes in the form that was amended in October 2004 by the Prudential Reporting for Market Risk by Banks Instrument 2004. These amendments are set out in the Annexes to that Instrument. That instrument can be found at [www.fsa.gov.uk/handbook/instruments.html](http://www.fsa.gov.uk/handbook/instruments.html).

If a bank has not chosen to apply the new provisions then, until 1 July 2005, the following applies.

- (4) It should use boxes B160, B170.1-B170.2, B210.1-B210.2, B250.1-B250.2 and B282.1-B282.2 as appropriate.
- (5) It should not use boxes B170.3-B170.4, B210.3-B210.4, B250.3-B250.4 or B283.2-B282.4.

- (6) It should use the form of these guidance notes that does not incorporate the amendments contained in Annex C of the Prudential Reporting for Market Risk by Banks Instrument 2004. This unamended version can be found at:

[http://www.fsa.gov.uk/pubs/other/sup\\_chapter16\\_annex2g.pdf](http://www.fsa.gov.uk/pubs/other/sup_chapter16_annex2g.pdf)

...

## **FORM BSD3 - SECTION B : TRADING BOOK FOR SOLO BANK AND LINE BY LINE**

### **INTERNAL VALIDATIONS**

**Ref No      Item No**

...

17            B170            = ~~B170.1 + B170.2~~ Superseded by validation 37, January 2005

...

21            B210            = ~~B210.1 + B210.2~~ Superseded by validation 38, January 2005

...

25            B250            = ~~B250.1 + B250.2~~ Superseded by validation 39, January 2005

...

31            B282            = ~~B282.1 + B282.2~~ Superseded by validation 40, January 2005

...

37            B170            = B170.1 + B170.2 + B170.3 + B170.4

38            B210            = B210.1 + B210.2 + B210.3 + B210.4

39            B250            = B250.1 + B250.2 + B250.3 + B250.4

40            B282            = B282.1 + B282.2 + B282.3 + B282.4

## **Part 2**

Amend the version of Form BSD3 (Capital Adequacy Return) whose boxes have been completed with references to validation and other items as follows.

The pages of the form that are changed are the cover page and pages 24, 25, 33, 35 and 36 (these are in the position of pages 12 to 17 of this instrument).



# FORM BSD3 - Capital Adequacy Return

Reporting institution \_\_\_\_\_

as at. 

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(eg 31 12 2001)

FSA number \* 

		F	S	A	
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Unconsolidated/solo consolidated/consolidated - tick as appropriate  
 Unconsolidated  Solo consolidated  Consolidated

Knowingly or recklessly giving the FSA information which is false or misleading in a material particular may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.1R and SUP 15.6.3R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. SUP 16.3.10R requires an authorised person to submit reports containing all the information required. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. Any additional information of relevance should be provided by letter direct to the FSA.

I confirm the information in this form is accurate and complete to the best of my knowledge and belief and that I have read the Guidance Notes to this form.

Signature of authorised signatory: \_\_\_\_\_ Date: \_\_\_\_\_

Name: \_\_\_\_\_ Position held: \_\_\_\_\_

*In the event of a query, the FSA or the Bank of England may, in the first instance, contact (block letters please)*

Tel No \_\_\_\_\_ Ext \_\_\_\_\_

**Notes on Completion**

- 1 If you have any difficulty in completing this return, please telephone your normal supervisory contact at the FSA for guidance.
- 2 Complete the return quarterly on an unconsolidated/solo consolidated basis as at end of March, June, September and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (SUP 8).
- 3 Complete the return half-yearly on a consolidated basis as at end of June and December. Institutions wishing to report at dates which coincide with the financial year end should apply to the FSA for a waiver (SUP 8).
- 4 Enter amounts to the nearest thousands omitting £000s/€000s. Calculated amounts should be rounded to the nearest thousands, or two decimal places as appropriate.
- 5 For definitions of items, refer to the Guidance Notes
- 6 To assist with the scanning process, please enter all data neatly within the relevant boxes and do not enter the % symbol in any boxes on this return.
- 7 Submit within 10 business days for unconsolidated/solo consolidated returns and 20 business days for consolidated returns or 12 and 22 business days respectively for those institutions reporting electronically to:

**The Financial Services Authority  
 c/o Monetary and Financial Statistics Division  
 Domestic Banking Statistics (HO-4)  
 Bank of England  
 Threadneedle Street  
 London EC2R 8AH**

- 8 Returns may also be delivered to the Works Gate at the Lothbury entrance of the Bank of England between 9.00am and 5.00pm, Monday to Friday. Envelopes should be clearly addressed as above.

FSA use only	Logged in	Data entered
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March 2004 ~~January~~ 2005

\* For unconsolidated/solo-consolidated entities, this should be the FSA firm reference number. For consolidated reports, this will be the FSA firm reference number of the institution on whom the requirement to report has been placed. This box must be filled in by all reporters (SUP 16.3.7R).

# MARKET RISKS IN THE TRADING BOOK

		Capital Requirement (000)s	
<b>I</b>	<b>STANDARD APPROACH</b>		
	<b>FOREIGN EXCHANGE RISK</b>		
B150	For basic approach (from Appendix B-V).....		B150
B160	For backtesting approach (from Appendix B-V).....		B160
B170	Additional Capital Charge for Options.....		B170
B170.1	Using Curve Out.....		B170.1
B170.2	Using CAD1 Models Approach.....		B170.2
<u>B170.3</u>	<u>Using the standard method</u> .....		<u>B170.3</u>
<u>B170.4</u>	<u>Using the hedging method</u> .....		<u>B170.4</u>
B180	<b>Total foreign exchange risk requirement</b> .....		B180
	<b>INTEREST RATE POSITION RISK</b>	Amount (000s)	Specific Risk Weights Capital Requirement (000)s
B190	Specific Risk.....		B190
B190.1	.....		0.00% B190.1
B190.2	.....		0.25% B190.2
B190.3	.....		1.00% B190.3
B190.4	.....		1.60% B190.4
B190.5	.....		8.00% B190.5
B200	General Market Risk (from Appendix B-VI).....		B200
B210	Additional Capital Charge for Options:.....		B210
B210.1	Using Curve Out.....		B210.1
B210.2	Using CAD1 Models Approach.....		B210.2
<u>B210.3</u>	<u>Using the standard method</u> .....		<u>B210.3</u>
<u>B210.4</u>	<u>Using the hedging method</u> .....		<u>B210.4</u>
B215	Embedded Interest Rate Risk in Equity Derivatives.....		B215
B220	<b>Total interest rate position risk requirement</b> .....		B220



<b><u>EQUITY POSITION RISK REQUIREMENT</u></b>		Capital Requirement (000s)
B230	Specific Risk (from Appendix B-VII).....	B230
B240	General Market Risk (from Appendix B-VII).....	B240
B250	Additional Capital Charge for Options:.....	B250
B250.1	Using Curve Out.....	B250.1
B250.2	Using CAD1 Models Approach.....	B250.2
<u>B250.3</u>	<u>Using the standard method</u> .....	<u>B250.3</u>
<u>B250.4</u>	<u>Using the hedging method</u> .....	<u>B250.4</u>
B270	<b>Total equity position risk <u>requirement</u></b> .....	B270

<b><u>COMMODITY POSITION RISK REQUIREMENT</u></b>		Capital Requirement (000s)
B280	Commodity position risk (from Appendix B-VIII).....	B280
B282	Additional Capital Charge for Options:.....	B282
B282.1	Using Curve Out.....	B282.1
B282.2	Using CAD1 Models Approach.....	B282.2
<u>B282.3</u>	<u>Using the standard method</u> .....	<u>B282.3</u>
<u>B282.4</u>	<u>Using the hedging method</u> .....	<u>B282.4</u>
B284	<b>Total commodity position risk <u>requirement</u></b> .....	B284

<b>II INTERNAL MODELS APPROACH</b>		Capital Requirement (000s)
B290	Previous day's value at risk.....	B290
B300	Average of previous 60 days' value at risk .....	B300
B310	Multiplication factor (rounded to 2 decimal places and multiplied by 100) .	B310
B320	Capital requirement for general market risk .....	B320
B330	Capital surcharge for specific risk .....	B330
B340	<b>Total capital requirement for risks subject to internal models</b> (items B320 + B330) ....	B340

**APPENDIX B-V: CAPITAL REQUIREMENT FOR FOREIGN EXCHANGE POSITION  
RISK REQUIREMENT (000s)**

			Column 1 Net Overall Long (short) Position  (1 = 2 + 3)	Column 2 Positions to be treated under basic method	Column 3 Positions being treated under backtesting approach
BASE CURRENCY	<input type="text"/>	<input type="text"/>			
Other Currencies					
Belgium/Luxembourg Francs	BE	BELG			
Canadian Dollars	CA	CANA			
Danish Kronor	DK	DENM			
EUROS	ER	EURO			
French Francs	FR	FRAN			
Deutschmarks	DE	RGER			
Irish Pounds	IE	EIRE			
Italian Lire	IT	ITAL			
Japanese Yen	JP	JAPA			
Netherlands Guilders	NL	NETH			
Spanish Pesetas	ES	SPAI			
Swedish Kroner	SE	SWED			
Swiss Francs	CH	SWIT			
Sterling	UK	UKIN			
US Dollars	US	USA			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
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.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
.....	<input type="text"/>	<input type="text"/>			
Other Material currencies .....	U9	UNAL			
Other Aggregate Net Long Positions		OTHL			
Other Aggregate Net Short Positions		OTHS			
TOTAL			ZERO		
Higher of aggregate net short/long open positions				NSOP	NSOP
GOLD	GO	GOLD			
.....					
SUM OF GROSS POSITION.....			SUMG	SUMG	SUMG
CAPITAL REQUIREMENT.....			CAPR	CAPR	CAPR

**APPENDIX B-VI: CAPITAL REQUIREMENT INTEREST RATE GENERAL MARKET RISK - continued (000s)**

			6	7	8	9	10
			Zone Three Net Short Position	Maturity based approach method	Duration based approach method	Simplified Maturity Method	Total General Market Interest Rate Risk (7 + 8 + 9)
Australia	AU	AUSL					
Austria	AT	AUSR					
Belgium	BE	BELG					
Brazil	BR	BRAZ					
Canada	CA	CANA					
Denmark	DK	DENM					
EUROS	ER	EURO					
Finland	FI	FINL					
France	FR	FRAN					
Germany	DE	RGER					
Greece	GR	GREE					
Ireland	IE	EIRE					
Italy	IT	ITAL					
Japan	JP	JAPA					
Malaysia	MY	MALA					
Mexico	MX	MEXI					
Netherlands	NL	NETH					
Norway	NO	NORW					
Portugal	PT	PORT					
Singapore	SG	SING					
South Africa	RA	SAFR					
Spain	ES	SPAI					
Sweden	SE	SWED					
Switzerland	CH	SWIT					
Turkey	TR	TURK					
UK	UK	UKIN					
Sterling Index Linked Gilts							
USA	US	USA					
Other Material Countries							
.....							
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.....							
.....							
.....							
.....							
Other.....	U9	UNAL					
Non Material Countries							
TOTAL							

**APPENDIX B-VII: EQUITY POSITION RISK (000s)**

**Gross Positions for Specific Risk**

			1	2	3	4
			Positions attracting 8% specific Execution risk	Positions attracting 4% specific Execution risk	Positions attracting 0% specific Execution risk	Total Gross Equity Positions for specific Execution risk (1 + 2 + 3)
<b>Positions, including positions in indices, allocated by country</b>						
Australia	AU	AUSL.....				
Belgium	BE	BELG.....				
Canada	CA	CANA.....				
France	FR	FRAN.....				
Germany	DE	RGER....				
Japan	JP	JAPA.....				
Netherlands	NL	NETH.....				
Spain	ES	SPAI.....				
Sweden	SE	SWED....				
Switzerland	CH	SWIT.....				
United Kingdom	UK	UKIN.....				
United States	US	USA.....				
Denmark	DK	DENM....				
Finland	FI	FINL.....				
Greece	GR	GREE.....				
Ireland	IE	EIRE.....				
Italy	IT	ITAL.....				
Luxembourg	LU	LUXE.....				
Portugal	PT	PORT.....				
.....						
.....						
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.....						
.....						
.....						
Other material ctry.	U9	UNAL				
Non material ctry...	XF	NONM				
TOTAL.....						

## Annex C

### Further amendments to SUP 16 Ann 2G

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### **BSD3 REPORTING INSTRUCTIONS**

##### **SECTION A: BANKING BOOK**

##### **ASSETS**

...

##### **A462 Aggregate net short open foreign currency position**

Reporting institutions which also complete Section B should not report a number in this item, as the capital requirement for foreign exchange position risk requirement should be calculated via item B180. All other reporting institutions should complete this item. The figure reported here should have a positive sign.

The aggregate net short position (net foreign exchange position) should be calculated in accordance with Chapter FX (Foreign exchange position risk requirement), ~~Section 3, of the FSA Policy Guide/IPRU (BANK)~~ as relevant. The amount reported in item A462 should be equal to Y+g in the notation of the open currency position plus the net gold position as calculated in Chapter FX (Foreign exchange position risk requirement), Section 4.4, of the FSA Policy Guide/IPRU (BANK). However, where fx options business is undertaken, the following adjustments should be made:

- (1) ~~w~~Where the simple curve-out standard or hedging method is used, the options capital charges should be multiplied by 12.5 and added to the net short position, so that the amount. The calculated amount will be reported in item A462. is equal to  $Y+g+12.5*(C+D)$  in the notation of Chapter FX (Foreign exchange risk), Section 4.4, of the FSA Policy Guide/IPRU (BANK).
- (2) ~~where one of the write-off methods is used, the options should not be included in the calculation of the net short position.~~
- (23) ~~w~~Where one of the other options methods are used, banks should consult their supervisor.

~~Institutions whose net open position calculated according to Chapter FX (Foreign exchange risk), Section 3, of the FSA Policy Guide/IPRU (BANK) is less than or equal to 2% of previous period's Large Exposures Capital Base may alternatively calculate their net open position as the difference between the value of foreign currency assets and the value of foreign currency liabilities (regardless of whether the result is long or short), on a consistent basis.~~

The basic method should be used to calculate foreign exchange risk unless the reporting institution is using a VaR model.

...

### **BSD3 - Section B: Trading book for solo bank and line by line consolidated entities**

...

#### **B150-B180 FOREIGN EXCHANGE POSITION RISK**

For more detailed information on the specification of capital for foreign exchange risk, see Chapter FX (Foreign exchange position risk requirement) of ~~the FSA Policy Guide~~/IPRU (BANK).

...

#### **B160 ~~For Backtesting Approach~~**

~~The total capital required for foreign exchange risk treated under the backtesting approach should be reported here. Item B160 should equal the item for the capital requirement for the backtesting method from Appendix B-V (column 3).~~~~[deleted]~~

...

#### **B170.1 ~~Using the Carve Out Approach~~**

~~Banks should report here the capital requirement arising from options on foreign exchange instruments treated under the carve out approach to options.~~~~[deleted]~~

#### **B170.2 Using CAD1 Models (Scenario Matrix/Buffer) Approach**

Banks should report here the capital requirement arising from options on foreign exchange instruments treated under the scenario matrix or buffer approach to options.

#### **B170.3 Using the Standard Method**

Banks should report here the position risk requirement arising from options on foreign exchange instruments treated under the standard method for options.

#### **B170.4 Using the Hedging Method**

Banks should report here the position risk requirement arising from options on foreign exchange that are treated under the hedging method.

#### **B180 Total foreign exchange risk requirement**

...

#### **B190-B220 INTEREST RATE POSITION RISK**

For more detailed information on the specification of capital for interest rate risk, see Chapter TI (Interest rate position risk requirement) of ~~the FSA Policy Guide~~/IPRU (BANK).

#### **B190 Specific Risk**

Report here the sum of individual net position (as defined in Chapter TI (Interest rate position risk requirement) of ~~the FSA Policy Guide~~/IPRU (BANK) within each risk weighted amount. ...

The specific risk weights are:

0.00% Certain Central Government debt instruments;

Debt instruments should be given a 0% specific risk weighting if they are:

- a) ~~they are issued by an issue of, or fully guaranteed by, or fully collateralised by securities issued by a Zone A<sup>+</sup> central governments and, central banks, including or the European Communities; or~~
- b) ~~they are issued by an issue of, or fully guaranteed by, Zone B central governments and central banks with a residual maturity of 1 year or less and are denominated in local currency and funded by liabilities in the same currency.~~

0.25% Qualifying Items debt securities up to 6 months residual maturity

1.00% Qualifying Items debt securities over 6 and up to 24 months residual maturity

1.60% Qualifying Items debt securities over 24 months residual maturity

~~Debt instruments should be treated as qualifying if any of the following conditions apply:~~

- a) ~~they are issued by, or fully guaranteed by, Zone B central governments and central banks with a residual maturity of over 1 year and are denominated in local currency and funded by liabilities in the same currency.~~
- b) ~~They are securities issued by, or fully collateralised by claims on, a multilateral development bank as listed in the Solvency Ratio Directive. The European Commission may amend this list periodically (see SGN Appendix E for more detail).~~
- e) ~~They are issued, guaranteed, endorsed, or accepted, by a credit institution incorporated in a Zone A country (see SGN Appendix C for details of Zone A and B countries);~~
- d) ~~They are issued, or guaranteed, endorsed, or accepted, by a credit institution incorporated in a Zone B country and have a residual maturity of 1 year or less;~~
- e) ~~They are issued, or guaranteed, by an investment firm that is incorporated in a Zone A country and subject to the Capital Adequacy Directive, or to a regime that FSA deems to be CAD equivalent;~~
- f) ~~They are issued, or guaranteed, by an investment firm that is incorporated in a Zone B country and subject to the Capital Adequacy Directive, or to a regime that the FSA deems to be CAD equivalent; and they have a residual maturity of 1 year or less;~~
- g) ~~They are issued by, or guaranteed by, Zone A public sector entities (see SGN23);~~
- h) ~~They are issued by, or guaranteed by, a company whose equity is eligible for 2% equity specific risk weighting.~~
- i) ~~The issue, or an issue of equivalent ranking in a liquidation, or an issue of equivalent ranking in a liquidation of the guarantor, is rated investment grade (or its equivalent for money market obligations), or above and the~~

---

<sup>+</sup>See SGN Appendix C.

~~reporting bank is unaware of any sub-investment grade<sup>2</sup> rating issued by any of the relevant credit rating agencies (see SGN Appendix H for the list of agencies which are considered relevant).~~

A debt security is a qualifying debt security if:

- (1) it attracts zero specific risk under table 44G of Chapter TI of IPRU(BANK); or
- (2) it is issued by, or fully guaranteed by:
  - (a) a Zone B central government or central bank and the security is denominated in the local currency of the issuer; or
  - (b) a multilateral development bank as defined in the Handbook Glossary; or
  - (c) a Zone A public sector entity; or
  - (d) a company whose equity is a constituent of one of the indices making up the FTSE All-World Index; or
  - (e) an issue of, or fully guaranteed by an investment firm or recognised third-country investment firm; or
- (3) it is issued by, fully guaranteed by, endorsed or accepted by:
  - (a) a credit institution incorporated in a Zone A country; or
  - (b) a credit institution incorporated in a Zone B country and the debt security has a residual maturity of one year or less; or
- (4) it is a mortgage backed security which meets the criteria in 7e of section 3.2.5 of Chapter BC of IPRU(BANK); or
- (5) it is rated by at least one of the agencies shown in table 47G of Chapter TI of IPRU(BANK), and every such rating equals or exceeds the corresponding minimum shown in that table.

Convertible securities, such as bonds and preference shares, that are treated as debt instruments should be given a specific risk weighting identical to other debt items for the same issuer as described in the preceding paragraphs. Convertible securities (as defined in Chapter TE (Equity position risk), ~~Section 2, Paragraph 4, of the FSA Policy Guide/IPRU (BANK)~~) should be treated as equities when:

- a) ...
- b) the convertible is trading at a premium of less than 10%, where the premium is defined as the current mark to market value of the convertible less the mark to market value of the underlying equity, expressed as a percentage of the mark to market value of the underlying equity market price of less than 110% of the underlying equity.

---

<sup>2</sup> ~~Chapter BC (Credit risk in the banking book), Section 5, of the FSA Policy Guide/IPRU (BANK) includes a list of the relevant cut off points for investment grade for each relevant ratings agency.~~



Otherwise, a bank may treat equity convertibles as either:-

- a) ~~an equity position based upon conversion of the bond and deducting from capital (by including in item B215) any losses, including accrued interest, that may arise from this “conversion” for the purposes of calculating the capital requirements, but limiting the size of any profits from the “conversion” to the sum of the specific and general risk requirements; or~~ an equity position (by including in item B215), where the bank's equity PRR should be adjusted by making an addition equal to the current value of any loss which the bank would make if it did convert to equity; or a deduction equal to the current value of any profit which the bank would make if it did convert to equity (subject to a maximum reduction equal to the PRR on the notional position underlying the convertible).
- b) a debt item.

...

#### **B210.1 Using the Carve Out Approach**

~~Banks should report here the capital requirement arising from options on interest rate instruments treated under the carve out approach to options (see in Chapter TI (Interest rate position risk), Section 7, of the FSA Policy Guide/IPRU (BANK)).~~[deleted]

#### **B210.2 Using CAD1 Models Approach**

Banks should report here the capital requirement arising from options on interest rate instruments treated under the scenario matrix or buffer approach to options.

#### **B210.3 Using the Standard Method**

Banks should report here the position risk requirement arising from options on interest rate instruments treated under the standard method for options (see Chapter TO of IPRU (BANK)).

#### **B210.4 Using the Hedging Method**

Banks should report here the position risk requirement arising from options or interest rate instruments treated under the hedging method (see Chapter TO of IPRU (BANK)).

#### **B215 Interest Rate Risk on Equity Derivatives**

Reporting institutions should include in this box any interest rate risk arising from equity derivatives (including options) which is not processed via either an approved model or the usual methods for interest rate general market risk (see in Chapter TE (Equity position risk requirement), ~~Section 5, Paragraph 5, of the FSA Policy Guide/IPRU (BANK).~~

...

#### **B220 Total Interest Rate Position Risk Requirement**

This item should be the sum of items B190, B200, B210 and B215.

#### **B230-B270 EQUITY POSITION RISK REQUIREMENT**

...

### **B250.1 ~~Using the Carve Out Approach~~**

~~Banks should report here the capital requirement arising from options on equities treated under the carve out approach to options. [deleted]~~

### **B250.2 Using CAD1 Models Approach**

Banks should report here the capital requirement arising from options on equities treated under the scenario matrix or buffer approach to options.

### **B250.3 Using the Standard Method**

Banks should report here the position risk requirement arising from options on equities treated under the standard method (see Chapter TO of IPRU (BANK)).

### **B250.4 Using the Hedging Method**

Banks should report here the position risk requirement arising from options on equities treated under the hedging method (see Chapter TO of IPRU (BANK)).

### **B270 Total Equity Position Risk Requirement**

This item should be the sum of the capital requirements for specific and general market risk on equities plus any additional capital requirements reported for options.

### **B280 Commodity position risk requirement**

...

### **B282 Additional Capital Charge for Options**

... This item should equal the sum of items ~~B282.1 and B282.2~~, B282.3 and B282.4.

### **~~B282.1 Using the Carve Out Approach~~**

~~Banks should report here the capital requirement arising from options on commodity instruments treated under the carve out approach to options. [deleted]~~

### **B282.2 Using CAD1 Models (Scenario Matrix/Buffer) Approach**

Banks should report here the capital requirement arising from options on commodity instruments treated under the scenario matrix or buffer approach to options.

### **B282.3 Using the Standard Method**

Banks should report here the position risk requirement arising from options on commodity instruments treated under the standard method (see Chapter TO of IPRU (BANK)).

### **B282.4 Using the Hedging Method**

Banks should report here the position risk requirement arising from options on commodity instruments treated under the hedging method (see Chapter TO of IPRU (BANK)).

### **B284 Total commodity position risk requirement**

...

## **APPENDIX B-V: CAPITAL REQUIREMENT FOR FOREIGN EXCHANGE RISK**

...

The net open position in each currency (including gold but excluding the base currency) should be calculated according to Chapter FX (Foreign exchange position)

risk requirement), Section 3, of the FSA Policy Guide/IPRU(BANK). Positions in composite currencies may either be broken down into positions in the component currencies according to the quotas in force, or treated as positions in a separate currency. However, one or other method should be used consistently. Positions in American depository receipts should be treated as positions in the currency of the underlying instrument.

...

Positions in Column 1, other than the balancing item in the base currency, should be allocated to either Column 2 or 3 in line with the agreed policy set out in the Trading Book Policy Statement. (In certain circumstances, it may be appropriate to split the position in one pre-determined currency, with only a proportion included in the backtesting method. Such a treatment should also be agreed in advance with the supervisor).

...

The capital requirement for currency and gold positions included in the backtesting method should be reported at the bottom of column 3 and in item B160. The minimum requirement is 2% of the sum of the higher of net short/long open currency positions and the absolute value of the position in gold in Column 3: the entry at the bottom of Column 3 and in item B160 must be at least as large as this in order for the return to be processed.

From 1 September 1999, only the basic method ~~should be~~ has been used to calculate foreign exchange risk unless the reporting institution ~~is using~~ has used a VaR model. Accordingly, columns 2 and 3 are no longer applicable, as column 1 is the same as column 2.

## **APPENDIX B-VI - CAPITAL REQUIREMENT FOR INTEREST RATE GENERAL MARKET RISK**

Chapter TI (Interest rate position risk requirement) of the FSA Policy Guide/IPRU(BANK) contains three alternative methods that may be used for the calculation of interest rate general market risk. ...

### **Simplified Method: Interest Rate**

Reporting institutions which have chosen to apply the simplified method (Chapter TI (Interest rate position risk requirement), Section 4, of the FSA Policy Guide/IPRU(BANK)) for interest rate risk should report the resultant capital requirement for each currency in the simplified method column. ...

### **Embedded Interest Rate Risk On Equity Derivatives (Including Options)**

~~For general interest rate position risk on equity derivatives, an amount equal to the notional underlying equities may be included in Appendix B-VI as government securities with a coupon below 3% in the currency concerned. Banks should only report in this way if the FSA is satisfied, and has given express written agreement, that sufficient controls are in place to monitor this interest rate exposure and to take account of dividend exposures and liquidity risk. If a bank has an approved interest rate sensitivity model, the interest exposure may be incorporated into that model. Otherwise the embedded interest rate exposures in equity derivatives should be~~

calculated as in Chapter TI (Interest rate position risk requirement) or as in Chapter TE (Equity position risk requirement) of IPRU(BANK) and reported in item B215.

~~Unless otherwise agreed with the FSA, embedded interest rate exposures in equity derivatives should be calculated as in Chapter TE (Equity position risk), Section 5, Paragraphs 5-7, of the FSA Policy Guide/IPRU(BANK) and reported in item B215.~~

## APPENDIX B-VII: EQUITY POSITION RISK

...

### Standard Method

Gross equity positions (including positions in indices) should be reported in Columns 1, 2 or 3 according to the tests and definitions set out in Chapter TE (Equity position risk requirement), Section 4, of the FSA Policy Guide/IPRU(BANK). Under the standard method positions in qualifying equities ~~“highly liquid” stocks which form a “diversified portfolio”~~ for the country concerned should be reported in Column 2. Positions in highly liquid qualifying equity indices which attract a ~~charge for execution~~ zero specific risk charge should be reported in column 3. All other positions should be reported in Column 1. Banks should include any notional equity instruments underlying positions in derivatives, but should exclude positions in ~~“highly liquid”~~ qualifying equity indices, unless they have been broken down into their components for the purpose of offsetting other positions. The capital requirement for specific/~~execution~~ risk calculated from these positions is the total of Column 1 multiplied by 8% plus the total of Column 2 multiplied by 4% plus the total of Column 3 multiplied by 0%. This capital requirement should not be reported in Appendix B-VII, but in item B230. Column 4 is the sum of Columns 1, 2 and 3.

The absolute value (ie disregarding sign) of net equity positions should be reported in ~~columns 5 and 6~~. Banks should include any notional equity instruments, underlying positions in derivatives and also any positions in indices. ~~For “concentrated” positions, ie those which form more than 20% of the total gross equity position for the country concerned, the value of the position in excess of 20% should be reported in Column 5 (disregarding sign), the remainder of the position being included in Column 6. If more than one concentrated position exists within a country portfolio, the reported excess positions should be aggregated without offsetting (ie disregarding sign) or use zone A/B distinction. The concentration test is no longer in use. Therefore column 5 is no longer applicable so column 6 will equal column 7.~~

~~Column 7 is the sum of Columns 5 and 6. The capital requirement for general risk calculated from these positions is the total of amount in Columns 5 and 6 multiplied by 8%. This capital requirement should not be reported in Appendix B-VII, but in item B240.~~

Equity positions arising from underwriting should be included within the gross and net equity positions reported for the relevant country. When discount factors are applied to underwriting positions prior to Working Day Zero and for the subsequent five days, the discounted position should be aggregated with other net equity positions for that country without offsetting (ie disregarding sign). [See Chapter TU (Underwriting in the capital adequacy framework Securities Underwriting) of the FSA Policy Guide/IPRU(BANK) for more details on the treatment of underwriting.]

## Equity Simplified Method

~~Banks which have chosen to apply the simplified method for equity position risk should report gross equity positions either entirely in Column 1 (attracting an 8% charge). Equity index positions should be included in the gross position for the relevant country. The capital requirement for specific risk, which should be reported in item B230, is the total of Column 1 multiplied by 8%.~~

~~Under the simplified method the general risk requirement is calculated in the same way as under the standard method: the capital requirement for general market risk, which should be reported in item B240, is the total of Columns 5 and 6 multiplied by 8%.~~

Banks which have chosen to apply the simplified method for equity position risk should report gross equity positions in either Column 1 (attracting an 8% specific risk charge) or in Column 3 (attracting a 0% specific risk charge). Positions in qualifying equity indices attract a 0% specific risk charge and should be reported in column 3. All other positions attract an 8% specific risk charge and should be reported in column 1. Equity index positions should be included in the gross position for the relevant country. The capital requirement for specific risk calculated from these positions is the total of Column 1 multiplied by 8%, which should be reported in item B230.

Under the simplified method the gross equity positions should be summed, and reported under the relevant country in column 6. Netting of general market risk is not allowed under the simplified equity method. The general market risk requirement which should be reported in item B240 is Column 6 multiplied by 8%.

## APPENDIX B-VIII - COMMODITY POSITION RISK

This section outlines the calculation of capital charges for commodity position risk. For the purposes of this section, a commodity includes any physical or energy product (except gold) product which is or can be traded on a secondary market ~~and positions in respect of contracts whether tangibles or intangibles not covered elsewhere in these reporting instructions.~~ Commodities therefore include agricultural products, base metals, other minerals and various precious metals; however, gold is excluded and is treated as a foreign currency according to the methodology set out under Appendix B-V. ...

### Definition of a single commodity

Capital charges should be calculated for each commodity separately; long and short positions in the same commodity only should be matched (see below) prior to determining the net open position. For the purpose of these calculations, a bank should treat positions in different grades or brands of the same commodity-class as different commodities unless they: ~~specific items may be considered as being elements of the same commodity if:~~

- ~~(a) positions in different sub-categories are deliverable against each other can be delivered against each other; or~~
- ~~(b) positions in commodities which are close substitutes for each other such that price movements over a minimum period of one year can be shown to have a stable and~~

reliable correlation of at least 0.9. have price movements which have exhibited a stable correlation coefficient of at least 0.9 over the last 12 months. The bank should then monitor the correlation on a continuing basis.

Banks may undertake the matching of positions under option (b) above. However they should ~~obtain the prior approval of~~ notify their line supervisor before doing so as set out in Chapter CM, 23G of IPRU(BANK). A bank wishing to treat positions in respect of non-identical items as the same commodity should be able to demonstrate that the correlation is valid and to monitor its continuing validity.

### **Derivative positions**

...

- ~~options and warrants on commodities may be treated under one of two the hedging or standard methods. A simple method, called the carve-out, may be used for portfolios which contain (at most) only a small number of written options or warrants, and providing also they contain only plain vanilla and shorter dated instruments. Banks with larger and/or more complex options portfolios should seek recognition for one of the option risk management models described in Chapter TS (CAD1 models) in the FSA Policy Guide/IPRU(BANK).~~

### **Maturity ladder approach**

...

**Table 1 - Time bands and spread rates**

#### **Time bands and spread rates**

<b>Time band</b>	<b>Spread rate</b>
0-1 month	<del>1.5%</del> <u>3%</u>
1-3 months	<del>1.5%</del> <u>3%</u>
3-6 months	<del>1.5%</del> <u>3%</u>
6-12 months	<del>1.5%</del> <u>3%</u>
1-2 years	<del>1.5%</del> <u>3%</u>
2-3 years	<del>1.5%</del> <u>3%</u>
over 3 years	<del>1.5%</del> <u>3%</u>

Matched long and short positions in each time band should incur a capital charge. When calculating this charge, ~~the sum of matched positions (i.e. both long and short positions)~~ should be multiplied first by the spot price for that commodity and second by the spread rate for that band (~~1.5%~~3%). ...

...

## ONLINE SUBMISSION AND MANDATORY FORMS INSTRUMENT 2004

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 51(3)(a) (Applications under this Part);
  - (2) section 138 (General rule-making power);
  - (3) section 157(1) (Guidance); and
  - (4) section 182(1) (Notification).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### **Commencement**

- C. This instrument comes into force on 1 November 2004.

### **Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with Annexes A and B to this instrument.

### **Citation**

- E. This instrument may be cited as the Online Submission and Mandatory Forms Instrument 2004.

By order of the Board  
20 October 2004

## Annex A

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

- 3.3.2 R A *firm* to which this section applies (see *SUP* 3.1) must:
- (1) ...
  - (2) notify the *FSA*, without delay, on the form in *SUP* 15 Ann 2R (Standing data form), in accordance with the instructions on the form, when it is aware that a vacancy in the office of auditor will arise or has arisen, giving the reason for the vacancy;
  - ...
  - (5) notify the *FSA* of the appointment of an auditor, on the form in *SUP* 15 Ann 2R (Standing data form), in accordance with the instructions on the form, advising the *FSA* of the name and business address of the auditor appointed and the date from which the appointment has effect.
- ...
- 6.3.15 D (1) ~~A If a firm which wishes to apply for a variation of *Part IV* permission, it must ~~do so in writing~~ complete and submit to the *FSA* the form in *SUP* 6 Ann 5D (Variation of permission application form), explaining the variation it seeks.~~
- ...
- 6.3.17 G (1) ~~Subject to *SUP* 6.3.20G, there is no application pack for a variation of *Part IV* permission. Instead, a *firm* should send an application under *SUP* 6.3.15D to its usual supervisory contact at the *FSA*. This application should set out the requirements in *SUP* 6.3.16G in as much detail as possible, together with a detailed description of the reasons and circumstances that have given rise to the request. [deleted]~~
- (2) ~~However, a A firm is ...~~
- ...
- 6.4.5 D (1) ~~If a *firm* wishes to cancel its *Part IV* permission, it must ~~write~~ complete and submit to the *FSA* the form in *SUP* 6 Ann 6D (Cancellation of permission application form) ~~giving the reasons for its application to cancel its *Part IV* permission), and the date on which the *firm* has ceased, or expects to cease, to carry on regulated activities. The *firm* must explain the full circumstances of its application.~~~~



...

- (3) ~~A firm's application for cancellation of Part IV permission must be served in the ways set out in SUP 15.7 (Form and method of notification)-[deleted]~~

...

Insert after SUP 6 Ann 4G the following two new links to forms (the forms are detailed in Annex B):

:

SUP 6 Ann 5D: Variation of permission application form

SUP 6 Ann 6D: Cancellation of permission application form

...

- 8.3.3A G (1) The FSA's preferred method of submission for *waiver* applications is by e-mail or by online submission at [www.fsa.gov.uk](http://www.fsa.gov.uk).

...

- 10.13.3 ~~G~~D A firm ~~should~~ must use Form E ...

...

- 11.3.7 D A notification ("notice of *control*") given to the FSA by a *person* who is acquiring *control* or increasing his *control* over a *firm*, in a way described in SUP 11.4.2R(1) to (4), must:

- (1) in the case of a *controller* or a proposed *controller* who is not an *authorised person*, contain the information required in:

...

- (2) in all other cases, contain the information required in Controllers Form A, sections 1, 5 and 6 (SUP 11 Ann4 D)-; and

- (3) if a notification is not submitted on the relevant form specified in (1) or (2), provide reasons why that form was not used.

...

- 11.3.11 G The FSA, for administrative reasons, expects notifications within SUP 11.3.7D to be given on Controllers Form A or Controllers Form B, as appropriate. If notifications are not made on these forms the applicant must inform FSA of the reasons for not using them. Copies of Controllers Form A and Controllers Form B are available on the FSA's website at [www.fsa.gov.uk](http://www.fsa.gov.uk). ...

...

- 12.7.1 R (1) *A firm* which appoints an *appointed representative* must complete and submit give written notice of the appointment to the FSA the form in SUP 12 Ann 3R (Appointed representative appointment form) in accordance with the instructions on the form and not more than ten *business days* after the date the appointment takes effect.
- (2) ~~*A firm's* notification under (1) must be given to a member of or addressed for the attention of the Authorisation and Approvals Department (Authorisation teams) at the address given in SUP 12.7.5R [deleted]~~

...

- 12.7.4 G (1) ~~*Firms* can obtain a standard notification form from either the FSA website at [www.fsa.gov.uk](http://www.fsa.gov.uk) or by post from the Corporate Authorisation department [Monitoring and Notifications Department<sup>1</sup>].~~
- (2) ~~*A firm's* notice under SUP 12.7.1 R should be returned to the department at the address below. [deleted]~~

...

- 12.7.7 R (1) ~~*A firm* must give written notice on the relevant form to the FSA of~~ Where there is a change in any of the information provided to the FSA under SUP 12.7.1R, a *firm* must complete and submit to the FSA the form in SUP 12 Ann 4R (Appointed representative notification form) in accordance with the instructions on the form and within ten *business days* of a that change being made or, if later, as soon as ~~it~~ the *firm* becomes aware of the change. The Appointed representative notification form notice must state that the information has changed.
- (2) ~~*A firm's* notification under (1) [and (2)<sup>2</sup>] must be given to a member of or addressed for the attention of the Authorisation and Approvals Department (Authorisation teams) [Monitoring and Notifications Department<sup>3</sup>] at the address given in SUP 12.7.5R. [deleted]~~

- 12.7.8 R (1) ~~*A firm* must give written notice to the FSA a~~ As soon as it a *firm* has reasonable grounds to believe that any of the conditions in SUP 12.4.2R or SUP 12.4.6R (as applicable) are not satisfied, or are likely not to be satisfied, in relation to any of its *appointed representatives*, it must complete and submit to the FSA the form in SUP 12 Ann 4R (Appointed representative notification form), in accordance with the instructions on the form.
- (2) ...

<sup>1</sup> Deleted text was due to come into force on 14 January 2005.

<sup>2</sup> Deleted text was due to come into force on 14 January 2005.

<sup>3</sup> Deleted text was due to come into force on 14 January 2005.

- (3) ~~A firm's notification under (1) must be given to a member of or addressed for the attention of the Corporate Authorisation department at the address given in SUP 12.7.5R [deleted]~~

...

12.8.1 R If either the *firm* or the *appointed representative* notifies the other that it proposes to terminate the contract of appointment or to amend it so that it no longer meets the requirements contained or referred to in SUP 12.5 (Contracts: required terms), the *firm* must:

- (1) ~~complete and submit give written notice to the FSA the form in SUP 12 Ann 5R (Appointed representative termination form) in accordance with the instructions on the form and no more than ten business days after the date of the decision to terminate or so amend the contract or, if later, as soon as it becomes aware that the contract is to be or has been terminated or amended;~~
- (2) ~~include in the written notice the reason for the termination or amendment, if the termination or amendment is due to misconduct or the appointed representative is resigning while under investigation by the firm, the FSA, another regulator, a clearing house, an exchange, a designated professional body, or a government body or agency; [deleted]~~
- (3) ~~if relevant, include in the written notice details of action taken by the firm and, if applicable, its outcome; and [deleted]~~
- (4) ~~ensure that the written notice is given to a member of or addressed for the attention of the Corporate Authorisation department at the address given in SUP 12.7.5R.[deleted]~~

...

Insert after SUP 12 Ann 2G the following four new links to forms (the forms are detailed in Annex B):

[SUP 12 Ann 3R: Appointed representative appointment form](#)

[SUP 12 Ann 4R: Appointed representative notification form](#)

[SUP 12 Ann 5R: Appointed representative termination form](#)

...

15.7.1 R A notification required from a *firm* under any *notification rule* must be given in writing, and in English, and must be submitted on the form specified for that notification rule, or if no form is specified, on the form in SUP 15 Ann 3R (Notification form), and must give the *firm's* FSA Firm Reference Number unless:

...

15.7.2 G A *firm* should have regard to the urgency and significance of a matter and, if appropriate, should also notify its usual supervisory contact at the *FSA* by telephone or by other prompt means of communication, before submitting a written notification....

...

15.7.4 R Unless stated in the *notification rule* or on the relevant form (if specified)  
...

15.7.5 R Table: Methods of Notification

...

5. Fax to a fax number for the *firm's* usual supervisory contact at the *FSA* and receiving a successful transmission report for all pages of the notification, followed by delivery by one of methods 1–4 in this table ~~within five business days after the date of the faxed notification~~

6. Online submission via the *FSA's* website at [www.fsa.gov.uk](http://www.fsa.gov.uk).

...

Insert after SUP 15 Ann 1R the following links to forms (the forms are detailed in Annex B):

SUP 15 Ann 2R: Standing data form

SUP 15 Ann 3R: Notification form

...

16.3.9 R Table Method of submission of reports (see SUP 16.3.8R)

...

5. Fax to the number notified by the firm's usual supervisory contact at the *FSA*, ~~followed by submission by one of the methods 1–4 in this table within 5 business days after the date of the faxed submission~~ and receiving a successful transmission report for all pages of the report.

...

16.9.3 R (1) A *firm* must:

(a) submit a report to the *FSA* annually, in the form of an amended copy of the relevant extract from the *FSA Register*, containing the information in (2);

...

...

16.9.5 G ~~The information required by SUP 16.9.3R or SUP 16.9.4R should be provided in the form of an amended copy of the relevant extract from the *FSA Register*. [deleted]~~

...

## **Annex B**

In this Annex underlining indicates new text and striking through indicates deleted text.

The forms referred to in Annex A as detailed in Annex B are set out sequentially below.

SUP 6 Ann 5D: Variation of permission application form

SUP 6 Ann 6D: Cancellation of permission application form

SUP 12 Ann 3R: Appointed representative appointment form

SUP 12 Ann 4R: Appointed representative notification form

SUP 12 Ann 5R: Appointed representative termination form

SUP 15 Ann 2R: Standing data form

SUP 15 Ann 3R: Notification form

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 6 Ann 5D: Variation of permission application form



# Variation of Part IV Permission (VOP)

## Application Form

(September 2004)

Firm name

("The Firm")

FSA reference number

Address

The Financial Services Authority  
Variation of Permission ('VOPs') Team  
Regulatory Decisions Department  
25 The North Colonnade  
Canary Wharf  
London E14 5HS  
United Kingdom  
Telephone +44 (0) 20 7066 1000  
Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

### **Purpose of this form**

This form will help you apply to vary the permission of your firm.

It may look long but it should be relatively straightforward to complete. For the majority of applications, completing this form will make it clear to us (the Financial Services Authority – ‘the FSA’) what you want to do and provide the information we need. However, you may be required to submit further information if necessary.

You should read through this form before you attempt to complete it to ensure that you can vary your permission in the way you want to, you have all the information required and have taken any additional steps necessary.

- **Authorisation and Permission**

Under section 19 of the Financial Services and Markets Act 2000 (FSMA 2000), no firm may carry on a regulated activity in the United Kingdom, or claim to do so, unless the firm is authorised by us or is an exempt person. This is referred to as the general prohibition. It is a serious offence, or ‘breach of the general prohibition’, if a firm conducts regulated activities within the UK and is not authorised or exempt.

When authorising a firm, we give the firm a permission - a “Part IV permission”. This lists all the services covered by FSMA 2000 ('regulated activities') that the firm is allowed to offer. For each of the regulated activities it will say what products ('investment types') the firm can offer in connection with that activity and to which class(es) of client ('customer types').

For example, an IFA’s permission might include:

- Regulated activity: Advising (excluding Pension Transfers/Opt Outs).
- Investment types related to this regulated activity: Certificates representing certain security, Debenture, Government and public security, Life Policy, Rights to or interests in investments (Contract Based Investments), Rights to or interests in investments (Security), Share, Stakeholder pension scheme, Unit, Warrant.
- Clients for this activity and these investment types: Intermediate Customer, Private Customer.

Note that in this example the IFA's permission does not allow it to give advice to Market Counterparties, nor would it be allowed to give advice on products not listed such as futures or Contracts for Difference.

If a firm decides that it wants to undertake a new type of business, extend a business line into a new product or to a new class of people, it must decide if this means that it needs to change its permission. If we do not regulate the business or service (the ‘activity’), then the firm will not need to apply for a change of permission. If we do regulate the activity, then before the firm starts doing the new activity, or starts doing an existing activity with a new investment type or customer type, it must apply to us for a variation of its Part IV permission. We must approve the variation before the firm can start the business. In making this decision, we are required by law to consider whether the firm will continue to meet the minimum standards for authorised firms. These standards are referred to as the Threshold Conditions. These are



detailed in the Threshold Conditions section of the FSA Handbook, which is referred to as COND. You will find this on our website at [www.fsa.gov.uk/vhb/html/cond/CONDtoc.html](http://www.fsa.gov.uk/vhb/html/cond/CONDtoc.html).

If a firm undertakes regulated business that is not covered by its permission, we can take enforcement action against the firm.

Similarly, if a firm ceases a business line or restricts the way it undertakes it in some way, it should consider whether it should remove a regulated activity or change the client types or instruments associated with a regulated activity. A permission should only reflect the activities that a firm undertakes.

- **Limitations and Requirements**

A permission may contain a ‘requirement’. This can restrict the way in which a firm can act in regard to the regulated activities listed. Requirements may be positive or negative, either requiring a firm to take specified action or not to take any action. This may extend to activities which are not regulated.

Some requirements restrict the way a permission can work, so that the firm fits a particular definition of a type of firm referred to in the FSA Handbook e.g. Oil Market Participants, Corporate Finance Firms, Venture Capital Firms. For example a common requirement for Venture Capital Firms is “the firm must not conduct designated investment business other than Venture Capital business”.

A particular regulated activity in the permission may have a ‘limitation’. These enable us to limit the description of a regulated activity as we see appropriate. A limitation may restrict the circumstances in which an activity may be carried out. For example, a common limitation for insurance firms is “the permission to accept deposits is limited to accepting deposits in the course of carrying on insurance business for which the insurer has a permission”.

A firm can apply to have requirements and limitations added, removed or changed.

### **Be aware**

When you vary your permission you must be aware that:

- for certain types of variation you may be charged an application fee, which you must pay even if you withdraw the application or it is refused;
- your FSA periodic fee may increase or decrease;
- you may have to demonstrate how your firm has enhanced its systems and controls to take into account new risks your firm faces by doing new types of business; and
- your firm’s financial category may change, so your financial resource requirements could increase.

You should fully understand how these points will affect your firm before completing this form.

### **Getting help**

If you have problems completing this application form you may find it helpful to consult the FSA Handbook:

- SUP 6.3 and Annex 2 for general information on VOP applications;
- AUTH 2 for information on regulated activities, instruments etc; and

- SUP 20 and AUTH 4.1 for fees.

If this does not resolve your problems then you should discuss the application with your usual supervisory contact at the FSA or seek professional help. If your questions specifically relate to how to complete this form then please contact the VoPs Team at the contact details at the end of this section.

- **Time to process this application**

We will attempt to process your application as quickly as possible. In doing so we will endeavour to meet any relevant dates you notify us of but to help us with this you should make any application in plenty of time. However, please note that we have six months to consider an application for variation of permission once received and deemed complete (see SUP 6.3.35G).

- **Complex variations**

If you are applying to add one of the activities listed in Table 1.2(c) below to your permission then you should be aware that you will be asked to complete further forms and provide more information, including all or part of an Authorisation Pack. This is because these will cause a fundamental change to the way you should run and control your business. You will be advised on this after we receive this application form.

- **Fee Blocks and Fees**

Authorised firms are required to pay annual periodic fees while they are authorised by us. Firms are categorised into groups that conduct similar types of business called Fee-blocks. The Fee-blocks determine the amount of fees that are charged to a firm in a particular category. This allows us to minimise any cross subsidising of one sector to another and ensure that similar businesses are charged fees on a similar basis. It is the regulated activities that determine which Fee-blocks a firm is in. This means that varying your permission can change the annual periodic fees that a firm pays.

Typically, the permission granted to an Independent Financial Adviser would cause the firm to be allocated to fee-blocks A.12 or A.13.

- **A.12** – Advisers, arrangers, dealers, brokers (holding and/or controlling client money and/or client assets).
- **A.13** – Advisers, arrangers, dealers, brokers (NOT holding and/or controlling client money and/or client assets).

Changing investment types and / or client types should not affect the Fee-blocks a firm is in but changing a requirement may. For example, removing a requirement to restrict the business of a firm to corporate finance will change a firm's fees.

### **Variation of Permission Application fees**

Your firm will have to pay an application fee if the variation you are applying for brings you into one of the Fee-blocks listed below for the first time. This is not refundable if you do not go ahead with the variation or if we refuse the variation. You do not have to pay a fee if you do not enter one of the fee blocks below. The questions in this form will help you determine whether you need to pay an application fee.

### **Table 1.2 - Variation of permission application fee**

This table is taken from AUTH 4, Annex 1R.

**(a) Straightforward (£1,000)**

<b>New Fee Block</b>	<b>Descriptions</b>
A.3	Friendly societies
A.4	Friendly societies
A.12	Advisory arrangers, dealers or brokers (holding or controlling client money and/or assets)
A.13	Advisory arrangers, dealers or brokers (not holding or controlling client money and/or assets)
A.14	Corporate finance advisers

**(b) Moderately complex (£2,500)**

<b>New Fee Block</b>	<b>Descriptions</b>
A.1	E-money issuers only
A.5	Managing agents at Lloyd's
A.7	Fund Managers (holding or controlling client money and/or assets)
A.9	Operators, trustees and depositaries of collective investment schemes
A.10	Firms dealing as principal

**(c) Complex (£12,500)**

<b>New Fee Block</b>	<b>Descriptions</b>
A.1	Deposit acceptors (excluding e-money issuers and credit unions)
A.3	Firms conducting insurance activities subject only to prudential regulation (excluding friendly societies)
A.4	Firms conducting insurance activities subject to both prudential and conduct of business regulation (excluding friendly societies)

**Changes to periodic fees**

If your firm is granted an additional permission or extends an existing permission during the course of a year, which takes you into a different Fee-block, then the periodic fees that you will be charged in future years will change. Also, an additional periodic fee will also be charged for the current year. The exact amount payable for the current year will depend on the date in our financial year when the permission is changed. The fee is a set proportion of the full annual periodic fee. The proportions payable are set out in Table 1.3 below.

**Table 1.3 - Proportion of full periodic fee payable for part-year authorisations**

<b>Quarter in which the permission is changed</b>	<b>• Proportion payable</b>
1 April to 30 June inclusive	100%
1 July to 30 September inclusive	75%
1 October to 31 December inclusive	50%

1 January to 31 March inclusive	25%
---------------------------------	-----

If a firm reduces or renounces its permission or recognition during our financial year, then we will give no refund of periodic fees.

If a firm formally applies to vary its permission before the start of a new fee period (1 April each year), and the permission is reduced within three months of the start of the new fee period, we will not charge a fee for any fee-block that applied to the firm before the variation took effect.

SUP 20 Annex 1 R ([www.fsa.gov.uk/vhb/html/SUP/SUP20Annex1.html](http://www.fsa.gov.uk/vhb/html/SUP/SUP20Annex1.html)) contains the fee rules and may be used for detailed information on Fee-blocks. You will find further information at [www.fsa.gov.uk/fees](http://www.fsa.gov.uk/fees) .

### **Instructions for submission**

When completed, submit this application form by post to:

Variation of Permission ('VoPs') Team  
Regulatory Decisions Department  
The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

**If you are requesting multiple variations, for example adding more than one activity, please copy the relevant section for each change as appropriate. Please note that all questions marked with an asterisk (\*) are mandatory and must be answered.**

- 1 Contact Name for this application  \*
- 2 Contact's Details:
  - a Position in the firm  \*
  - b Daytime telephone number  \*
  - c E-mail address
  - d Individual reference number (IRN), if applicable
- 3 If you have a specific target date for a decision on this application enter it here:  /  /

We will attempt to process your application as quickly as possible and, if feasible, endeavour to meet this date. However, we have six months to consider an application once received and deemed complete (See SUP 6.3.35G).

**Change Client Money Requirement**

**Section Ba**

**Answer this question if you are requesting to hold or control client money or assets or to cease doing so, otherwise consider Section Bb.**

We (the FSA) require firms that hold and/or control client money or assets to follow the Client Assets Sourcebook (CASS). You should read and be aware of your obligations under CASS.

- A1 New Client Money Requirement (please tick one):
  - Hold and Control Client Money
  - Control but not hold Client Money
  - Not hold and not control Client Money
  - Hold and control client money in respect of non-investment insurance contracts (Insurance Mediation activities only)
- A2 If you are applying to cease to hold client money then you must include a report from your auditors confirming that you have done this and it has either been paid back to the clients concerned or transferred to another entity that is authorised to hold it.
- A3 What type of account will your firm use to hold Client Money? (please tick one)

- Statutory Trust
- Non Statutory Trust
- Risk Transfer
- Not Applicable (Please explain why below):

- |           |  | Yes                      | No                       | N/A                      |
|-----------|--|--------------------------|--------------------------|--------------------------|
| <b>A4</b> | Is the account held at an approved bank? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

If you have answered 'Not Applicable' or 'No', please explain why below:

- |           |  | Yes                      | No                       | N/A                      |
|-----------|--|--------------------------|--------------------------|--------------------------|
| <b>A5</b> | Does this bank meet the requirements imposed under CASS 4.3? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

If you have answered 'Not Applicable' or 'No', please explain why below:

- |           |  | Yes                      | No                       | N/A                      |
|-----------|--|--------------------------|--------------------------|--------------------------|
| <b>A6</b> | Have you read and understood the Client Money rules that you are required to abide by? | <input type="checkbox"/> | <input type="checkbox"/> | <input type="checkbox"/> |

If you have answered 'Not Applicable' or 'No', please explain why below:

**Answer this question if you are requesting to add a new requirement, otherwise consider Section Bc.**

Please select **either** a standard requirement from Appendix A (attached to this form), or enter a non-standard requirement. Please also explain why you would like the new requirement to be added.

**B1** Standard Requirement:

If applicable, please enter the reference number and short description of the requirement that is being applied for (see Appendix A):

Ref Number      Short description

Ref Number	Short description

**B2** Non-Standard Requirement **hererer:**

**B3** Please explain why you would like this new requirement to be added:

\*

## Change Requirement

## Section Bc

Answer this question if you are requesting a change to an existing requirement, otherwise consider Section Bd.

Please state the current requirement that you wish to change:

\*

**C1** Please detail the change to the above requirement:

\*

**C2** Please explain why you would like this requirement to be changed:

\*

## Delete Requirement

## Section Bd

Answer this question if you are requesting to delete an existing requirement, otherwise consider Section Be.

Please state the current requirement that you wish to delete:

\*

**D1** Please explain why you would like this requirement to be deleted:

\*



Answer this question if you are requesting regulated activities to be added to your permission, otherwise consider Section Bf.

Please select a new activity, its associated customer types and investment types, and explain why you would like the new activity to be added.

**E1** Please choose an Activity Category and an Activity

<b>Activity Category</b>	<b>Activities</b>	
<b>Insurance Business</b>	<input type="checkbox"/> <i>Effecting contracts of insurance</i>	<input type="checkbox"/> <i>Carrying out contracts of insurance</i>
<b>Accepting Deposits</b>	<input type="checkbox"/> <i>Accepting Deposits</i>	<input type="checkbox"/>
<b>Designated Investment Business</b>	<input type="checkbox"/> <i>Establishing, operating or winding up a regulated collective investment scheme</i>	<input type="checkbox"/> <i>Establishing, operating or winding up an un-regulated collective investment scheme</i>
	<input type="checkbox"/> <i>Acting as trustee of an authorised unit trust scheme</i>	<input type="checkbox"/> <i>Acting as the depository or sole director of an open-ended investment company</i>
	<input type="checkbox"/> <i>Establishing, operating or winding up a stakeholder pension scheme</i>	<input type="checkbox"/> <i>Dealing in investments as principal</i>
	<input type="checkbox"/> <i>Arranging safeguarding and administration of assets</i>	<input type="checkbox"/> <i>Safeguarding and administration of assets (without arranging)</i>
	<input type="checkbox"/> <i>Managing Investments</i>	<input type="checkbox"/> <i>Advising on pension transfers and pension opt-outs</i>
	<input type="checkbox"/> <i>Sending dematerialised instructions</i>	<input type="checkbox"/> <i>Causing dematerialised instructions to be sent</i>
	<input type="checkbox"/> <i>Dealing in investments as agent</i>	<input type="checkbox"/> <i>Arranging (bringing about) deals in investments</i>
	<input type="checkbox"/> <i>Making arrangements with a view to transactions in investments</i>	<input type="checkbox"/> <i>Advising on investments (except pension transfers and pension opt-outs)</i>
	<input type="checkbox"/> <i>Agreeing to carry on a regulated activity</i>	<input type="checkbox"/>
	<b>The Lloyd's Market</b>	<input type="checkbox"/> <i>Advising on syndicate participation at Lloyd's</i>
<input type="checkbox"/> <i>Arranging (bringing about) deals in investments</i>		<input type="checkbox"/> <i>Making arrangements with a view to transactions in investments</i>
<input type="checkbox"/> <i>Agreeing to carry on a regulated activity</i>		<input type="checkbox"/>
<b>Funeral Plan Providers</b>	<input type="checkbox"/> <i>Entering as provider into a funeral plan contract</i>	<input type="checkbox"/> <i>Agreeing to carry on a regulated activity</i>
<b>Regulated Mortgages</b>	<input type="checkbox"/> <i>Advising on regulated mortgage contracts</i>	<input type="checkbox"/> <i>Arranging (bringing about) regulated mortgage contracts</i>

		<i>Making arrangements with a view to regulated mortgage contracts</i>	<input type="checkbox"/>	<i>Entering into regulated mortgage contracts (mortgage lending)</i>	<input type="checkbox"/>
		<i>Administering regulated mortgage contracts</i>	<input type="checkbox"/>	<i>Agreeing to carry on a regulated activity</i>	<input type="checkbox"/>
<b>Insurance Mediation</b>	<input type="checkbox"/>	<i>Dealing in investments as agent</i>	<input type="checkbox"/>	<i>Arranging (bringing about) deals in investments</i>	<input type="checkbox"/>
		<i>Making arrangements with a view to transactions in investments</i>	<input type="checkbox"/>	<i>Advising on investments (except pension transfers and pension opt-outs)</i>	<input type="checkbox"/>
		<i>Agreeing to carry on a regulated activity</i>	<input type="checkbox"/>	<i>Assisting in administration of insurance</i>	<input type="checkbox"/>

**E2** Please choose the customer types associated with the new activity

All	<input type="checkbox"/>	Intermediate Customer	<input type="checkbox"/>	Market Counterparty	<input type="checkbox"/>
Private Customer	<input type="checkbox"/>	Retail Customer (insurance mediation only)	<input type="checkbox"/>	Commercial Customer (insurance mediation only)	<input type="checkbox"/>
Customer (regulated mortgages only)	<input type="checkbox"/>				

**E3** Please choose the investment types associated with the new activity

**Insurance business**

Accident	<input type="checkbox"/>	Sickness	<input type="checkbox"/>	Land Vehicles	<input type="checkbox"/>
Railway rolling stock	<input type="checkbox"/>	Aircraft	<input type="checkbox"/>	Ships	<input type="checkbox"/>
Goods in transit	<input type="checkbox"/>	Fire and natural forces	<input type="checkbox"/>	Damage to property	<input type="checkbox"/>
Motor vehicle liability	<input type="checkbox"/>	Aircraft liability	<input type="checkbox"/>	Liability of ships	<input type="checkbox"/>
General liability	<input type="checkbox"/>	Credit	<input type="checkbox"/>	Suretyship	<input type="checkbox"/>
Miscellaneous financial loss	<input type="checkbox"/>	Legal Expenses	<input type="checkbox"/>	Assistance	<input type="checkbox"/>
Life and annuity	<input type="checkbox"/>	Marriage and birth	<input type="checkbox"/>	Linked long-term	<input type="checkbox"/>
Permanent health	<input type="checkbox"/>	Tontines	<input type="checkbox"/>	Capital redemption	<input type="checkbox"/>
Pension fund management	<input type="checkbox"/>	Collective insurance	<input type="checkbox"/>	Social insurance	<input type="checkbox"/>

**Accepting deposits**

Deposit	<input type="checkbox"/>
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**Designated Investment Business**

Share	<input type="checkbox"/>	Debenture	<input type="checkbox"/>	Government or public security	<input type="checkbox"/>
Warrant	<input type="checkbox"/>	Certificate representing certain security	<input type="checkbox"/>	Unit	<input type="checkbox"/>
Stakeholder pension scheme	<input type="checkbox"/>	Rights to interests in investment – security	<input type="checkbox"/>	Option (excluding a commodity option and an option on commodity futures)	<input type="checkbox"/>
Commodity future	<input type="checkbox"/>	Contract for differences (excluding a spread bet and a rolling spot forex contract)	<input type="checkbox"/>	Spread Bet	<input type="checkbox"/>
Rolling spot forex contract	<input type="checkbox"/>	Life policy	<input type="checkbox"/>	Rights to interests in investment – contractually based investment	<input type="checkbox"/>

**The Lloyd’s Market**

Membership of a Lloyd's syndicate	<input type="checkbox"/>	Underwriting capacity of a Lloyd's syndicate	<input type="checkbox"/>	Rights to interests in investment	<input type="checkbox"/>
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**Funeral Plan Providers**

Funeral plan contract

**Regulated Mortgages**

Regulated mortgage contract

**Insurance Mediation**

Non-investment insurance contract

**E4** Please detail any limitation(s) you would like to add to this activity:

**E5** Please explain why you would like to add this activity:

\*

**Answer this question if you are requesting to delete an activity, otherwise consider Section Bg.**

Please state the activity and activity category that you wish to delete:

• Activity: \*

• Activity Category: \*

**F1** Please explain why you would like this activity to be deleted:

\*

**Answer this question if you are requesting to change a customer type, otherwise go to Section Bh.**

Please state the activity and activity category that you wish to change the customer type for:

- Activity: \*

- Activity Category: \*

Amendments to customer types may affect your exemption status under DISP 1.1.7R, Dispute Resolution: Complaints and COMP 13.3.1, Compensation: Funding. This is particularly relevant if you are adding or removing the customer type 'private'. Please ensure you notify your normal supervisory contact in writing of any changes to your status under this exemption that this variation of permission may cause.

**G1** Current Customer type(s) (please tick as appropriate):

All	<input type="checkbox"/>	Intermediate Customer	<input type="checkbox"/>	Market Counterparty	<input type="checkbox"/>
Private Customer	<input type="checkbox"/>	Retail Customer (insurance mediation only)	<input type="checkbox"/>	Commercial Customer (insurance mediation only)	<input type="checkbox"/>
Customer (regulated mortgages only)	<input type="checkbox"/>				

**G2** Please select your new customer types:

All	<input type="checkbox"/>	Intermediate Customer	<input type="checkbox"/>	Market Counterparty	<input type="checkbox"/>
Private Customer	<input type="checkbox"/>	Retail Customer (insurance mediation only)	<input type="checkbox"/>	Commercial Customer (insurance mediation only)	<input type="checkbox"/>
Customer (regulated mortgages only)	<input type="checkbox"/>				

**G3** Please explain why you wish to change the customer type:

**Answer this question if you are requesting to change/add/delete a limitation, otherwise consider Section Bi.**

Please state the activity and activity category that you wish to change the customer type for:

- Activity:  \*

- Activity Category:  \*

- New limitations - for each limitation, please enter the details of the new limitation in the box provided. (If you require more than one limitation to be added to this activity, please copy this sheet and attach to this application).

- Change/deletion of current limitations – please detail the limitation that you wish to change or delete. (If you require more than one limitation to be added to this activity, please copy this sheet and attach to this application.)

- Do you wish to:  Delete this limitation  
 Change this limitation (please detail the change below)

- Please explain why you would like this limitation to be changed:

 \*

Answer this question if you are requesting changes to investment types, otherwise go to Section C.

Please state the activity and activity category that you wish to change the customer type for:

Activity: \*

Activity Category: \*

Please select the current investment types and new investment types you wish to be associated with this activity:

	Current Inv Type	New Inv Type		Current Inv Type	New Inv Type		Current Inv Type	New Inv Type
Accident	<input type="checkbox"/>	<input type="checkbox"/>	Sickness	<input type="checkbox"/>	<input type="checkbox"/>	Land Vehicles	<input type="checkbox"/>	<input type="checkbox"/>
Railway rolling stock	<input type="checkbox"/>	<input type="checkbox"/>	Aircraft	<input type="checkbox"/>	<input type="checkbox"/>	Ships	<input type="checkbox"/>	<input type="checkbox"/>
Goods in transit	<input type="checkbox"/>	<input type="checkbox"/>	Fire and natural forces	<input type="checkbox"/>	<input type="checkbox"/>	Damage to property	<input type="checkbox"/>	<input type="checkbox"/>
Motor vehicle liability	<input type="checkbox"/>	<input type="checkbox"/>	Aircraft liability	<input type="checkbox"/>	<input type="checkbox"/>	Liability of ships	<input type="checkbox"/>	<input type="checkbox"/>
General liability	<input type="checkbox"/>	<input type="checkbox"/>	Credit	<input type="checkbox"/>	<input type="checkbox"/>	Suretyship	<input type="checkbox"/>	<input type="checkbox"/>
Miscellaneous financial loss	<input type="checkbox"/>	<input type="checkbox"/>	Legal Expenses	<input type="checkbox"/>	<input type="checkbox"/>	Assistance	<input type="checkbox"/>	<input type="checkbox"/>
Life and annuity	<input type="checkbox"/>	<input type="checkbox"/>	Marriage and birth	<input type="checkbox"/>	<input type="checkbox"/>	Linked long-term	<input type="checkbox"/>	<input type="checkbox"/>
Permanent health	<input type="checkbox"/>	<input type="checkbox"/>	Tontines	<input type="checkbox"/>	<input type="checkbox"/>	Capital redemption	<input type="checkbox"/>	<input type="checkbox"/>
Pension fund management	<input type="checkbox"/>	<input type="checkbox"/>	Regulated mortgage contract	<input type="checkbox"/>	<input type="checkbox"/>	Collective insurance	<input type="checkbox"/>	<input type="checkbox"/>
Social insurance	<input type="checkbox"/>	<input type="checkbox"/>	Deposit	<input type="checkbox"/>	<input type="checkbox"/>	Membership of a Lloyd's syndicate	<input type="checkbox"/>	<input type="checkbox"/>
Underwriting capacity of a Lloyd's syndicate	<input type="checkbox"/>	<input type="checkbox"/>	Rights to interests in investment	<input type="checkbox"/>	<input type="checkbox"/>	Share	<input type="checkbox"/>	<input type="checkbox"/>
Debenture	<input type="checkbox"/>	<input type="checkbox"/>	Government or public security	<input type="checkbox"/>	<input type="checkbox"/>	Warrant	<input type="checkbox"/>	<input type="checkbox"/>
Certificate representing certain security	<input type="checkbox"/>	<input type="checkbox"/>	Unit	<input type="checkbox"/>	<input type="checkbox"/>	Stakeholder pension scheme	<input type="checkbox"/>	<input type="checkbox"/>

Rights to interests in investment – security	<input type="checkbox"/>	<input type="checkbox"/>	Option (excluding a commodity option and an option on commodity futures)	<input type="checkbox"/>	<input type="checkbox"/>	Commodity future	<input type="checkbox"/>	<input type="checkbox"/>
Contract for differences (excluding a spread bet and a rolling spot forex contract)	<input type="checkbox"/>	<input type="checkbox"/>	Spread Bet	<input type="checkbox"/>	<input type="checkbox"/>	Rolling spot forex contract	<input type="checkbox"/>	<input type="checkbox"/>
Life policy	<input type="checkbox"/>	<input type="checkbox"/>	Funeral plan contract	<input type="checkbox"/>	<input type="checkbox"/>	Rights to interests in investment – contractually based investment	<input type="checkbox"/>	<input type="checkbox"/>
Non-investment insurance contract	<input type="checkbox"/>	<input type="checkbox"/>						

Please explain why you would like to change the investment types:

\*



Varying your permission can generate a variation of permission application fee and vary your periodic fees.

If an application fee is due, you are required to pay the fee before your application is considered. **This fee is non-refundable. You will not be invoiced for the application fee.**

#### Fee Blocks

- A1 Deposit acceptors
- A1 E-money issuers only
- A2 Mortgage lenders and administrators
- A3 Firms conducting insurance activities subject only to prudential regulation
- A3 Friendly Societies
- A4 Firms conducting insurance activities subject to both prudential and conduct of business regulation
- A4 Friendly Societies
- A5 Managing agents at Lloyd's
- A6 The Society of Lloyd's
- A7 Fund managers
- A9 Operators, trustees and depositories of collective investment schemes (CIS)
- A10 Firms dealing as principal
- A12 Advisers, arrangers, dealers, brokers (holding and/or controlling client money and/or client assets)
- A13 Advisers, arrangers, dealers, brokers (NOT holding and/or controlling client money and/or client assets)
- A14 Corporate finance advisers
- A18 Mortgage lenders, advisers and arrangers
- A19 General Insurance mediation

4 Which fee block(s) are you currently in?

5 Which fee block(s) will your firm be in after the variation?

6 Application fee payable: (see Table 1.2 of the notes at front of application form for assistance)

£

**All application fees must be paid by cheque within 5 business days of the date this form is submitted. We can only consider your application once we have received your application fee as well as the form.**

Please make the cheque payable to The Financial Services Authority, with your firm reference number and name written on the back, and send it to us with the form.

7 I confirm that the firm is ready and willing to pay the application fee (please tick to confirm)

Adding certain regulated activities will require you to have certain approved persons to perform Controlled Functions. You must have identified these people and ensured that they are competent to undertake the required functions.

Similarly, removing some activities may require you to remove Controlled Functions.

You should consider this before continuing with your application. If you require further help with this please call the Approved Persons Helpline on 0207 066 0019 or e-mail [iva@fsa.gov.uk](mailto:iva@fsa.gov.uk). The Controlled Functions that relate directly to activities are:

<b>Regulated Activity</b>	<b>CF</b>	<b>Controlled Function</b>
Advising on investments (except pension transfers and pension opt-outs)	CF21	Investment adviser
There is no single activity that covers this function. Ceasing business will require you to remove these approved persons and commencing this business will require you to have this controlled function.	CF22	Investment adviser (trainee)
	CF23	Corporate Finance adviser
Advising on pension transfers and pension opt-outs	CF24	Pension transfer specialist
Advising on syndicate participation at Lloyd's	CF25	Advisor on syndicate participation at Lloyd's
Dealing in investments as agent	CF26	Customer trading
Managing investments	CF27	Investment management

**Controlled functions required** Yes No

Will the change require new approved persons or additional controlled functions for existing approved persons in relation to the application? See SUP 6.3.8G.

Yes No N/A

**8a** Have you submitted the required Approved Person 'Form A' application form?

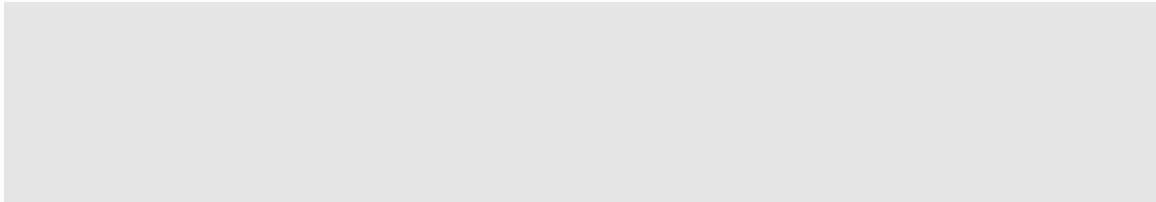
**8b** If you have answered 'Not Applicable' or 'No', please explain why below:

**8c** Please provide the names of applicant(s) for the new controlled functions:

**Controlled functions no longer required** Yes No N/A

**9a** The changes that you have requested may result in current controlled functions no longer being required. The FSA will now remove the specific functions from the profiles of the relevant approved persons. Do you accept this?

**9b** If you have answered 'Not Applicable' or 'No', please explain why below:



**Person responsible for insurance intermediation**

Every firm that carries on insurance mediation business must appoint an approved person who will be responsible for insurance mediation at the firm. This responsibility must be allocated to a director or senior manager (or in the case of a sole trader, to himself) performing:

- a governing function; or
- the apportionment and oversight function; or
- the significant management (other business operations) function.

The person will appear on the FSA Register as the person responsible for insurance mediation at the firm, and any appointed representatives that carry on insurance mediation activity on behalf of the firm. The FSA Register is a public record of all authorised firms and appointed representatives and lists the main contact name for each firm. Note that responsibility for insurance mediation is not a controlled function. This means that an approved person application will not be required if an existing approved person will take on this responsibility.

**10** If applicable, what is the name of the individual that the firm has appointed to be responsible for insurance mediation?

Title

Forename

Surname

**Please consult the chapter of AUTH specified or other parts of the Handbook referred to and then confirm whether you can apply for the variation by answering the following questions. If you cannot confirm this then you must not continue with the application or commence new business.**

	Yes	No	N/A
<b>11</b> Applicants seeking to carry on insurance business: Do you comply with the provisions of AUTH 3.12?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

If you answer 'No' to this question, please contact your normal supervisory contact to discuss this.

	Yes	No	N/A
<b>12a</b> Applicants seeking to carry on the regulated activity or accepting deposits: Do you comply with the provisions of AUTH 3.13 in that the applicant, under threshold condition 1 (legal status), is a firm which is either a body corporate or a partnership?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

**12b** If you have answered 'No', please explain why below:

	Yes	No	N/A
<b>13a</b> Applicants seeking to establish, operate or wind up a stakeholder pension scheme: Do you comply with the provisions of AUTH 3.16?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

**13b** If you have answered 'No', please explain why below:

	Yes	No	N/A
<b>14a</b> Applicants seeking to establish a collective investment scheme or to act as a manager of a regulated collective investment scheme: Do you comply with the provisions of AUTH 3.17?	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>

**14b** If you have answered 'No', please explain why below:

The threshold conditions represent the minimum conditions that a firm is required to satisfy, and continue to satisfy, to be given and to retain Part IV permission. The firm must satisfy the FSA that all of these conditions will continue to be met if the application is granted. Details of the various prudential categories are noted below. For any change in your prudential requirements, you need to be able to meet the requirements now. **Note: we may ask you for evidence in support of your answers.**

#### **Prudential Categories for Non Investment Business Firms**

<b>IPRU Sourcebook</b>	<b>Ref</b>
Bank	B
Building Society	BS
Friendly Society	FS
Insurer	INS

#### **Prudential Categories for Investment Business Firms**

<b>IPRU(INV) Chapter</b>	<b>Sub Category in Chapter</b>	<b>Ref</b>
2 – Professional Firms	N/A	PROF
3 – Securities and Futures Firms (not Investment Firms)	Corporate Finance	NI-CF
	Venture Capital	NI-VC
	Arranger	NI-ARR
	Agency Broker	NI-AB
	Financial Bookmaker	NI-FB
	Non clearing Floor Member	NI-NCFM
	Broadscope	NI-BRA
	Local	LOCAL
	EMP	EMP
	OMP	OMP
4 – Lloyd’s Firms	N/A	LLOYD
5 – Investment Management Firms	N/A	IM
6 – Service Companies	N/A	SC
10 – Securities and Futures Firms (Investment Firms)	ISD A	ISD-A
	ISD B	ISD-B
	ISD C	ISD-C
	ISD D	ISD-D
	ISD Corporate Finance	ISD-CF
	ISD Branch	ISD-BRA
13 – Personal Investment Firms	A1	PI-A1
	A2	PI-A2
	A3	PI-A4
	B1	PI-B1
	B2	PI-B2
	B3	PI-B3

Media Firm

N/A

Media

**16** What is your firm's current prudential category?

**17** If the application is granted, what prudential category will your firm be in?

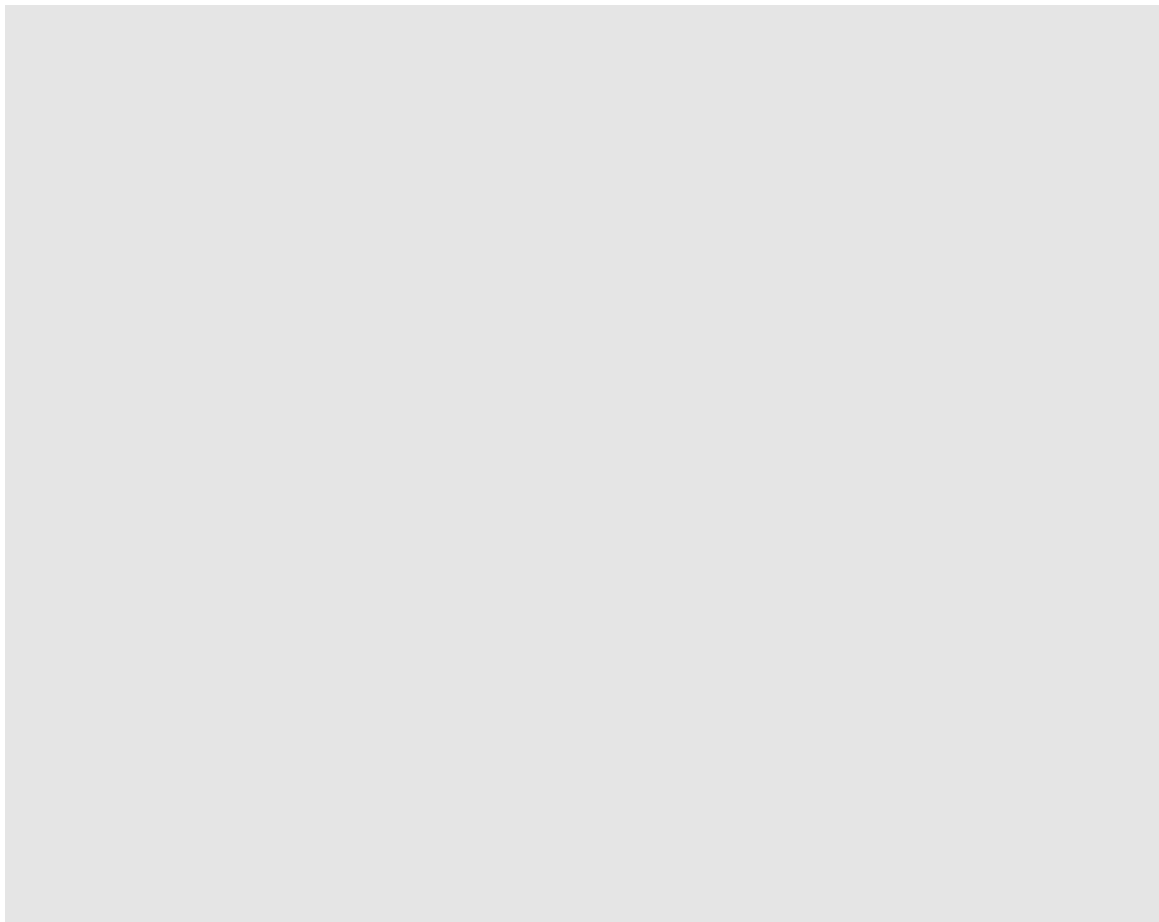
**18** Please detail the change in your financial requirements in the box below:

Yes No N/A

**19** Please confirm that your firm meets these new requirements:

The threshold conditions represent the minimum conditions that a firm is required to satisfy, and continue to satisfy, to be given and to retain Part IV permission. The firm must satisfy the FSA that all of these conditions will continue to be met if the application is granted.

- 20** If the Application is granted, enter in the box below how your firm will continue to meet the Systems and Controls required (see SYSC) – detail any enhancements you have made.

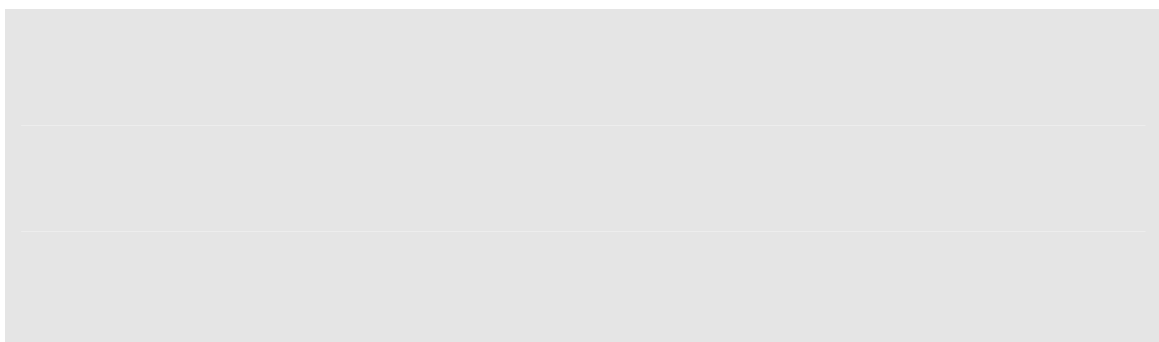


Yes    No    N/A

- 21a** Is your firm ready, willing and organised to comply with the relevant prudential, Conduct of Business and other regulatory requirements? See COND, especially 1.2.2G.

- 21b** If you have answered 'Not Applicable' or 'No', please explain why below:



If your firm is connected with a firm regulated outside the UK but within the European Economic Area (EEA), the FSA is required by s.49 of the Financial Services and Markets Act (FSMA) to consult with the appropriate EEA regulator.

Yes      No

**22** Is your firm connected with a firm regulated outside the United Kingdom but in the EEA?           

**23** If you have answered 'Yes', please enter each connection below

**23a**      Name of EEA Regulated Firm      Firm's main contact at EEA regulator      Name of EEA Regulator

Name of EEA Regulated Firm	Firm's main contact at EEA regulator	Name of EEA Regulator



Yes No N/A

**24** Is your firm **currently** an Authorised Professional Firm?  
(e.g. a firm of solicitors or accountants)

If you have answered 'yes', please complete the remainder of this section, otherwise continue to the next section.

**25** Please confirm that the current practice of your firm's profession (i.e. not including regulated activities) remains the main business of your firm.

**26a** If this variation of permission is approved, will you still be an Authorised Professional Firm as defined by the scale or nature of the activities that your firm seeks to carry on?

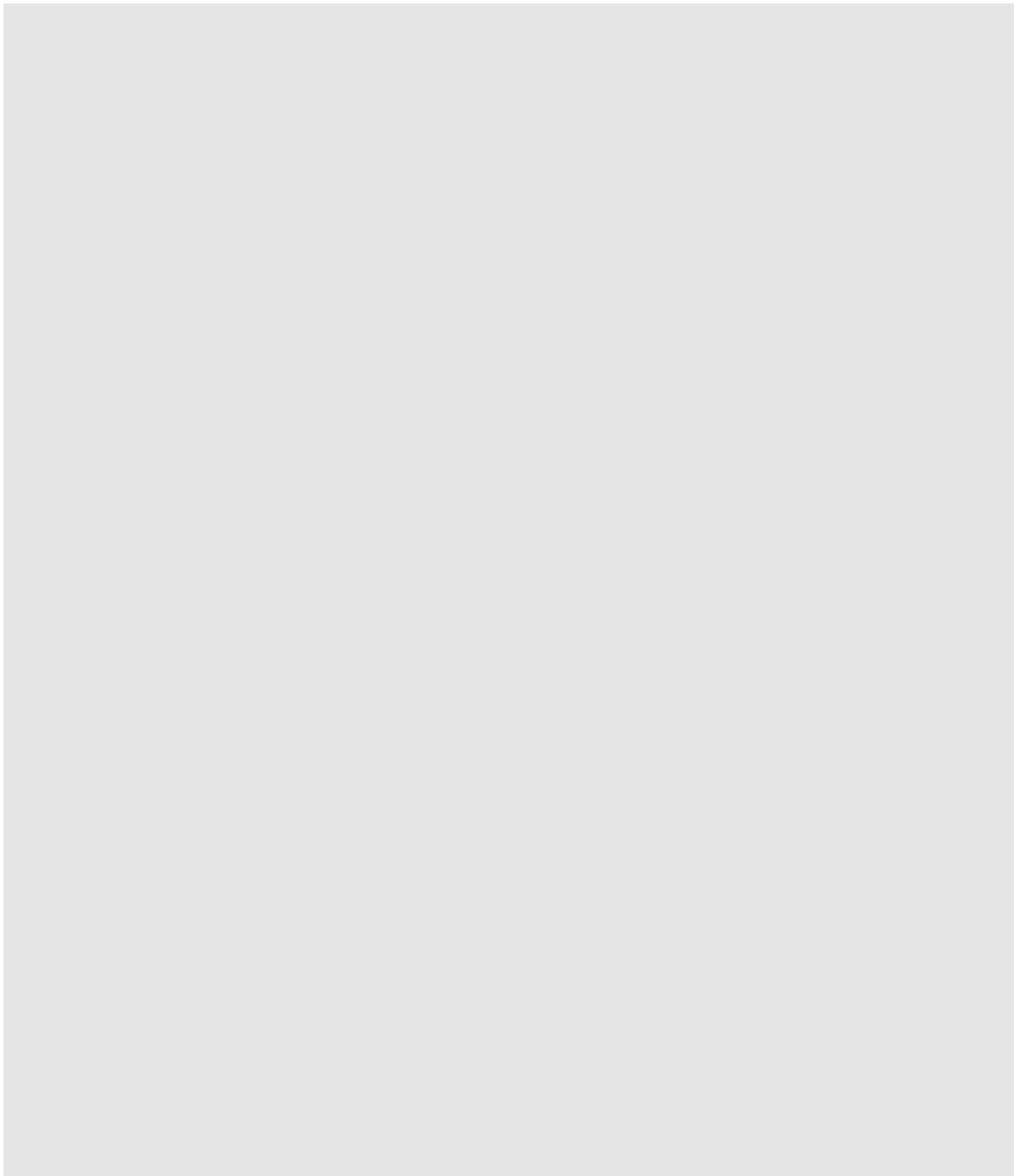
**26b** If no, do you confirm that you understand and will be able to comply with the new prudential requirements that will apply to your firm?

Please note that we are likely to contact you for further information and to discuss the firm's future status and Handbook obligations.

**26c** If you have answered 'No' to question 26b, please explain why below:

- 27 If there is any other information you think we should know when determining the application. Please enter it below or attach it as a document.

**Note that the FSA may ask you for additional information to support this application after you have submitted this form. For example, if you are undertaking insurance business or wish to start undertaking insurance business, you may later be asked to send a scheme of operation to support your application.**



### Warning

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R require an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA just because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

### Data Protection

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

### Declaration

By submitting this application form

- I/we confirm that the information in this application is accurate and complete to the best of my/our knowledge and belief and that I/we have taken all reasonable steps to ensure that this is the case.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the application pack. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date

Name of first signatory<sup>4</sup>

Position<sup>5</sup> of first signatory

Individual Registration Number

Signature

Name of second signatory

Position of second signatory

Individual Registration Number

Signature

## Appendix A – Standard Requirements

Ref	Short description	Requirement (full narrative)
1	Regulated activities incidental only.	The firm must not carry on the specified REGULATED ACTIVITIES otherwise than in an incidental manner in the course of the provision by it of professional services (that is, services

<sup>4</sup> For a sole trader, the signature of the principal is required.

For a limited company, the signature of two directors or one director and the company secretary is required.

For a partnership, the signature of at least one partner is required.

<sup>5</sup> e.g. Director, Partner or Sole Trader.

		which do not consist of REGULATED ACTIVITIES)
2	Only rights to/interests in permitted investments	The firm may carry on a REGULATED ACTIVITY in relation to rights to or interests in investments only where those investments are themselves of a type permitted for that REGULATED ACTIVITY
3	No actions to stabilise market price	The firm must not act in any way to stabilise the market price of any investment.
4	No pension transfer or opt out	The firm must not carry on any business relating to a PENSION TRANSFER or OPT OUT.
5	May hold/control client money if rebated commission	The general requirement not to hold or control CLIENT MONEY does not apply if the CLIENT MONEY arises from an agreement under which commission is rebated to the client.
6	No speculative foreign exchange dealings.	The firm must not undertake a permitted activity in respect of speculative foreign exchange dealings.
7	May control money if settlement through a mandate.	The general requirement not to hold or control CLIENT MONEY does not restrict the firm from controlling CLIENT MONEY if it arises from an agreement under which the firm effects settlement through a mandate or otherwise.
8	No CORPORATE FIN. BUSINESS unless non-mainstream	The firm must not carry on any CORPORATE FINANCE BUSINESS that is a REGULATED ACTIVITY unless it is a NON-MAINSTREAM REGULATED ACTIVITY.
9	Not to act as Broker Fund Adviser	The firm must not operate as a BROKER FUND ADVISER
10	Version 1 credit union.	The firm must only operate as a version 1 credit union.
11	Corporate finance business only.	The firm must not conduct designated investment business other than corporate finance business.
12	The firm must not act as an ISA manager.	The firm must not act as an ISA manager.
13	Activities only in respect of long term insurance.	The firm may only carry on listed activities in respect of the investments specified for the purpose of its long term insurance business.
14	Venture Capital Business Only	The firm must not conduct designated investment business other than Venture Capital business.
15	Derivatives as incidental services only.	The firm must not carry on a permitted activity concerning the sale of an option (including a commodity option), future (including commodity future) or contract for difference (including spread bet or rolling spot forex contract), except where the activity is incidental to services to a particular client.
16	Pensions T/O-O only in designated circumstances	The firm must not effect or advise on PENSION TRANSFERS or PENSION OPT-OUTS except in one or more of the designated circumstances
17	DERIVATIVES only during corporate finance	The firm must not carry on regulated activities in relation to DERIVATIVES otherwise than in the course of carrying on CORPORATE FINANCE business (excluding the activities forming paragraph (b) of the definition of CORPORATE FINANCE business)
18	Must not establish etc. UCIS with DERIVATIVES	The firm must not establish, operate or wind up an Unregulated Collective Investment Scheme in relation to DERIVATIVES
19	The firm must not undertake any regulated activity	The firm must not undertake any regulated activity.
20	Corporate finance only (except managing invest.)	In respect of each regulated activity for which the firm holds a Part IV permission, excluding managing investments, the activity is limited to corporate finance business only.

21	Not to promote AUTS via tied sales force	The firm must not promote authorised unit trust schemes to Private Customers through a tied sales force.
22	Not to promote ICVCs via tied sales force	The firm must not promote authorised ICVCs (Investment Companies with Variable Capital) to Private Customers through a tied sales force.
23	Restricted to re-insurance.	The firm must restrict all insurance business to reinsurance activities.
24	Not to promote Invest. Trusts via tied sales force	The firm must not promote Investment Trust Savings Schemes to Private Customers through a tied sales force.
25	Oil Market Participant	The firm must not conduct designated investment business which is not an oil market activity.
26	Not to dispose of company's/client's assets	Not to dispose or otherwise deal with the Company's or any client's assets held in the United Kingdom or elsewhere without prior approval of FSA.
27	Marketing limited to the Firm's own funds	The firm must not promote any unregulated collective investment schemes which it does not manage itself or act as advisor.
28	Energy Market Participant	The firm must not conduct designated investment business other than energy market activity.
29	Promote only own managed UCIS	The firm must not promote any unregulated collective investment schemes which it does not manage itself.
30	Not to guarantee a participant's performance	The firm must not guarantee, or otherwise accept responsibility for, the performance of a participant's obligations in arrangements made by the firm in carrying on regulated activities.
31	The firm must not undertake any regulated activity	The firm must not undertake any regulated activity and  To preserve all documents relating to the firm's conduct of regulated activities.
32	No split capital investment trust business	To exclude split capital closed end funds and zero dividend preference shares from the firm's scope of permission.
33	corporate finance or venture capital only	The firm must not conduct designated investment business other than corporate finance business or venture capital business
34	No sales to pvte cstmers thru tied sales force	Firm is required to ensure that sales to Private Customers are not carried out through a tied sales force
35	Requirement to comply with IPRU (INV) 5	Requirement to comply with IPRU (INV) 5
36	Private customers for regulated CIS only	The firm may only conduct regulated activities for private customers which are regulated collective investment schemes.
37	No split capital investment trust business	The firm must not transact any Split Capital Investment Trust Business
38	EIS mktng not through tied sales force	The Firm is required to ensure that Enterprise Investment Scheme marketing to Private Customers is not to take place through a tied sales force.

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 6 Ann 6D: Cancellation of permission application form



# Cancellation of Part IV Permission - Application Form

(September 2004)

Firm name

("The Firm")

FSA reference number

Address

**(Please return form to:)**

The Financial Services Authority  
Cancellations Team  
Regulatory Decisions Department  
25 The North Colonnade  
Canary Wharf  
London E14 5HS  
United Kingdom

Telephone +44 (0) 20 7066 1000

Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

## NOTES

Please note that before completing this form to cancel all of your firm's regulated activities, you may find it helpful to discuss your proposed application with your usual supervisory contact at the FSA.

You should ensure that all relevant information and confirmations are included in the form. If not, your application will be delayed whilst we seek the outstanding information and/or confirmations. Ultimately your application will be refused if the outstanding information and/or confirmations are not provided.

For more complex applications e.g. involving banks or insurance companies, we may request some additional information, in which case we will send a separate schedule.

**N.B.** an inwardly passporting EEA firm that is applying to cancel a top-up permission should only deal with matters in relation to that top-up permission in this form.

If you want to cancel some but not all of the regulated activities of your firm's permission then you should use the relevant Variation of Permission form to vary your firm's permission. Where a firm may require a long period in which to wind down (run off) its business, it is usually appropriate for the firm to apply to vary its permission before commencing the wind down. Please contact your normal supervisory contact to discuss your options.

To enable the FSA to process this application for the cancellation of your firm's Part IV permission, i.e. of all of its regulated activities, your firm should have taken the appropriate steps and be able to answer YES to each question below.

	Yes	No
• Have you notified all your firm's clients of its intention to cancel its permission and how this will affect them? (See SUP 6.4.11)	<input type="checkbox"/>	<input type="checkbox"/>
• Are your firm's fees paid up to date? (See SUP 6.4.22)	<input type="checkbox"/>	<input type="checkbox"/>
• Have all of your firm's regulatory returns been submitted up to date? (See SUP 6.4.9 & 16)	<input type="checkbox"/>	<input type="checkbox"/>
• Have you already informed your firm's approved persons of this application for cancellation?	<input type="checkbox"/>	<input type="checkbox"/>
• Can you confirm that there are no unsatisfied or undischarged complaints against the firm that have not been fully dealt with in accordance with your firm's complaints procedures? (See SUP 6.4.10 & 22)	<input type="checkbox"/>	<input type="checkbox"/>
• If your firm's carrying on of regulated activities has not already ceased, will your firm cease to do so within the next 6 months? (See SUP 6.4.3)	<input type="checkbox"/>	<input type="checkbox"/>
If you and the firm are not able to answer YES to all the questions above, you should NOT be making this application.		



**Personal Details**

**Section A**

- 1 Contact Name for this application \*
  
- 2 Contact's Details:
  - a Position in the firm \*
  - b Daytime telephone number \*
  - c E-mail address
  - d Individual reference number (IRN), if applicable

\* Denotes a mandatory field

**Application Details Part 1**

**Section B1**

3 On behalf of The Firm, I/we, the undersigned, hereby apply to cancel the Firm's Part IV permission and declare that:

The firm has ceased conducting all regulated activities from:     /     /

**OR**

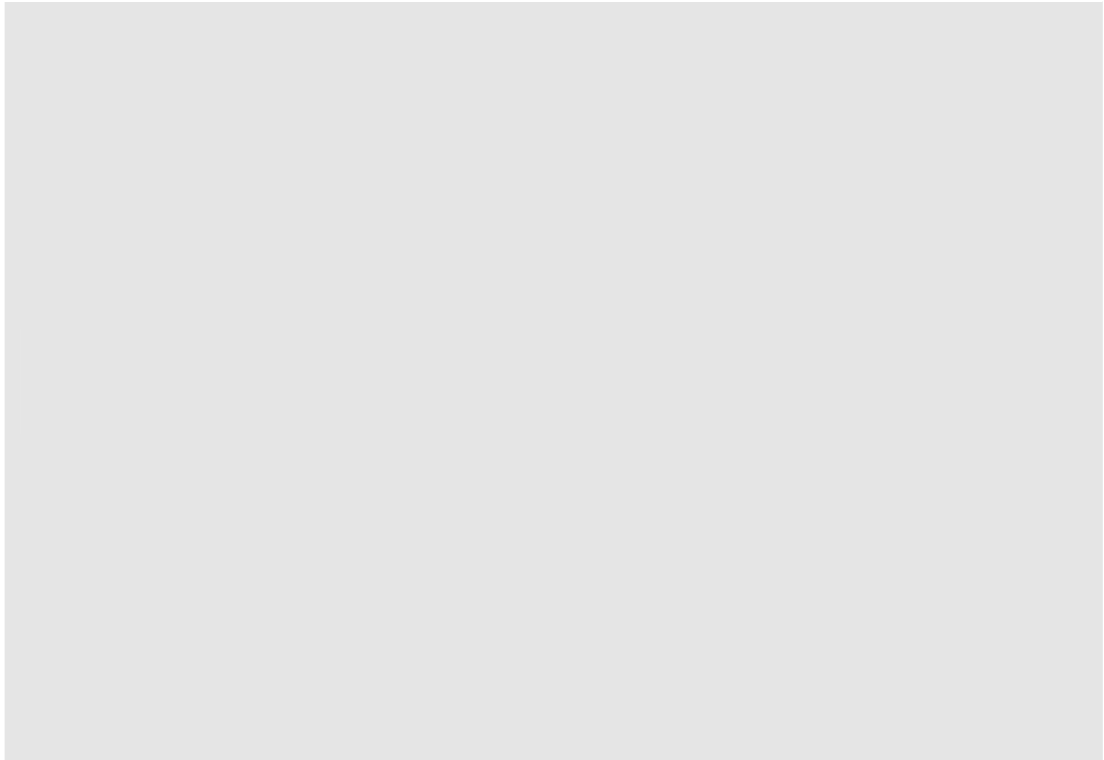
The firm will cease conducting all regulated activities from:     /     /

Please note that all regulated activities must cease no later than six months from the date of any application to cancel Part IV permissions (see SUP 6.4.3 G).

If you do not intend to cease regulated activities within the next six months, you should NOT apply at this stage.

4 What are your firm's reason(s) for cancellation (please tick as appropriate):

- (a) Ceased to carry on regulated activities
- (b) Proposing only to be authorised through:
  - Association of Chartered Certified Accountants
  - Institute of Chartered Accountants in England and Wales
  - Institute of Chartered Accountants in Scotland
  - Law Society
  - Law Society of Scotland
- (c) Business transferred to another regulated firm
- (d) Joining a network
- (e) Merging with another regulated firm
- (f) To become an appointed representative of another regulated firm
- (g) Firm never carried on regulated activities
- (h) Non-availability of professional indemnity insurance cover
- (i) Cost of professional indemnity insurance cover
- (j) Other (please provide details)



- Yes    No
- 5 Is there any information, relating to the withdrawal of individual approved persons performing controlled functions, of which the FSA should be aware?

Please provide details:

- 6 **Does your firm hold or control client money or assets?**    
 We may ask you for an auditor's report. Please refer to SUP 6.4.15G, 6.4.16G and 6.4.17G.  
 All client money/client deposits/discharged custody assets and any other property belonging to clients must be repaid before cancellation can proceed. Please refer to SUP 6.2.22 (2)G.

- 7 **Are any of your firm's clients being transferred to another firm that is regulated by the FSA?**

7a If 'Yes', number of firms to whom business is being transferred \_\_\_\_\_

Please complete Section B2a for each firm to whom business is being transferred.

(If there is more than one transferee firm, please copy this page and attach to the form)

- Name of firm to which business is being transferred  \*
- a) On what date do you propose to transfer this business?  /  /  \*
- Yes  No
- b) Is this firm currently authorised?
- (If not, it must be authorised before the transfer takes place. You can find out whether a firm is authorised by checking the FSA Register on our website))
- If yes, please enter its FSA reference number
- c) Address of Firm
- d) If no, please enter the date on which it is expected to become authorised  /  /
- e) Principal compliance contact at firm  \*

\* Denotes a mandatory field

- | 8 | Does your firm:   | Yes                      | No                       |
|---|---|--------------------------|--------------------------|
|   | (i) undertake corporate finance business;               | <input type="checkbox"/> | <input type="checkbox"/> |
|   | (ii) have any investment agreements;                    | <input type="checkbox"/> | <input type="checkbox"/> |
|   | (iii) manage any Collective Investment Schemes;         | <input type="checkbox"/> | <input type="checkbox"/> |
|   | (iv) have any outstanding subordinated loan agreements? | <input type="checkbox"/> | <input type="checkbox"/> |

If you answer yes to any of the above, by signing this Form you will be declaring that, by the date of cancellation, in respect of:

Q8 (i) all mandates have been or will be transferred;

Q8 (ii) your firm has terminated or will be terminating all agreements;

Q8 (iii) schemes managed by the firm have been or will be wound up; and

Q8 (iv) all such loan agreements have been or will be terminated (See SUP 6 Annex 4 G: table 3)

---

**9 a) Pensions: Selling or advising between 29 April 1988 and 30 June 1994**

Tick as appropriate:

The firm did not undertake the business of pension selling or advising between 29 April 1988 and 30 June 1994.

The firm did undertake the business of pension selling or advising between 29 April 1988 and 30 June 1994 and has completed its review as specified by the rules and guidance issued by the PIA and the FSA.

The firm did undertake the business of pension selling or advising between 29 April 1988 and 30 June 1994 and has not completed its review (as specified by the rules and guidance issued by the PIA and the FSA) and has therefore been in contact with the FSA and carried out all the actions required.

**b) Free Standing Voluntary Contributions ('FSAVCs'): Advising or arranging between 29 April 1988 and 15 August 1999.**

Tick as appropriate:

The firm did not undertake the business of advising or arranging FSAVCs between 29 April 1988 and 15 August 1999.

The firm did undertake the business of advising or arranging FSAVCs between 29 April 1988 and 15 August 1999 and has completed its review as specified by the rules and guidance issued by the PIA and the FSA.

The firm did undertake the business of advising or arranging FSAVCs between 29 April 1988 and 15 August 1999 and has not completed its review (as specified by the rules and guidance issued by the PIA and the FSA) and has therefore been in contact with the FSA and carried out all the actions required.

**Note: Please only apply to cancel once the resolution of all Pension review and/or FSAVC review issues are near completion.**

### Warning

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

### Data Protection

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

### Declaration

By signing this application form

- I/we confirm that this information is accurate and complete to the best of my knowledge and belief.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date

Name of first signatory<sup>6</sup>

Position<sup>7</sup> of first signatory

Individual Registration Number

Signature

Name of second signatory

Position of second signatory

Individual Registration Number

Signature

<sup>6</sup> For a sole trader, the signature of the principal is required. For any other firm, the signature of two directors or of two partners, as appropriate, is required.

<sup>7</sup> e.g. Director, Partner or Sole Trader.

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 12 Ann 3R: Appointed representative appointment form





# Add an Appointed Representative Form

Notification under SUP 12.7.1R

(September 2004)

*Firm name (i.e. the principal firm)*

("The Firm")

FSA reference number

Address

**Please return the form to:**

Authorisation & Approvals Department  
The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS  
United Kingdom  
Telephone +44 (0) 20 7066 1000  
Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

## NOTES

This form should be used to notify the FSA of a new appointed representative to the firm.

### Personal Details

### Section A

1 Contact Name for this form

\*

2 Contact's Details:

a Position in the *firm*

\*

b Daytime telephone number

\*

c E-mail address

d Individual reference number (IRN), if applicable

### New Appointed Representative Details

### Section B

1 Name of the appointed representative

\*

2 Address of the appointed representative

\*

Postcode:

3 Trading name(s) of the appointed representative, if different to the name given in question 1 above

4 Telephone number of the appointed representative

5 Fax number of the appointed representative

6 Email address of the appointed representative

7 Website address of the appointed representative

8 Legal status of the appointed representative \*

Private Limited Company

Public Limited Company

Partnership

Limited Partnership

Limited Liability Partnership

Unincorporated Association

Sole Trader

Other, please specify below

9 Date of commencement of agreement with your firm

Yes No

10 Is the appointed representative an introducer appointed representative? \*

11 Will the appointed representative undertake insurance mediation? \*

If question 11 is answered "yes", you must complete the 3 fields immediately below:

Name of main contact for FSA register

Title

Forename(s)

Surname

Yes No

12 Will the appointed representative undertake regulated mortgage activities? \*

13 Will the appointed representative undertake designated investment business activities? \*

**Warning**

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

**Data Protection**

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

**Declaration**

By submitting this notification

- I/we confirm that this information is accurate and complete to the best of my knowledge and belief and that I have taken all reasonable steps to ensure that this is the case.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date

Name of signatory

Position in firm

Individual Registration Number (if applicable)

Signature

The attached form or its equivalent is the form detailed in Annex B for SUP 12 Ann 4R:  
Appointed representative notification form



## Appointed Representative - Change Details

Notification under SUP 12.7.7R

(September 2004)

*Firm name (i.e. the principal  
firm)*

("The Firm")

FSA reference number

Address

**Please return this form to:**

Authorisation & Approvals Department  
The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS  
United Kingdom  
Telephone +44 (0) 20 7066 1000  
Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

## NOTES

This form should be used to change the details of an existing appointed representative.

**N.B. if all the changes made on the form do not take effect from the same date, you should use more than one form for each set of changes that take effect on the same date.**

### Personal Details

### Section A

1 Contact Name for this form

 \*

2 Contact's Details:

a Position in the *firm*

 \*

b Daytime telephone number

 \*

c E-mail address

d Individual reference number (IRN), if applicable

What is the name of the Appointed Representative whose details are to be amended?

\*

What is this Appointed Representative's Firm Reference Number? (If not known, this can be found on the FSA Register on our website at [www.fsa.gov.uk](http://www.fsa.gov.uk))

\*

Yes

**1 a. Do you wish to suspend** the appointed representative?

If 'Yes', please give the reasons for this:

If you have any additional information to add to the reason above please attach it to this form.

Yes

**b. Do you wish to reinstate** the appointed representative?



Yes

2 Do you wish to change the name of the appointed representative?

If 'Yes', what is the new name of the appointed representative?

\*

Yes

3a Do you wish to change the legal status of the appointed representative?

If 'Yes', What is the new legal status of the appointed representative?

Private Limited Company

Public Limited Company

Partnership

Limited Partnership

Limited Liability Partnership

Unincorporated Association

Sole Trader

Other, please specify below

Yes No N/A

3c Has the name change been approved by Companies House?

Note that if the appointed representative is a UK registered company or LLP, the name of the appointed representative can only be change if the change has already been approved by Companies House.

Yes

4 Do you wish to change the address of the appointed representative?

If 'Yes', please enter the new address:

\*

Postcode:

Yes

5 Do you wish to change the trading name(s) of the appointed representative?

If 'Yes', please provide details below. If you wish to amend a trading name please delete this name and add the new one below:

Please detail the trading name(s) to be deleted Please detail the trading name(s) to be added below:  
below:

--	--

Yes

6 Do you wish to change the telephone number of the appointed representative?

If 'Yes', please enter the new telephone number:  \*

Yes

7 Do you wish to change the fax number of the appointed representative?

If 'Yes', please enter the new fax number:  \*

Yes

8 Do you wish to change the Email address of the appointed representative?

If 'Yes', please enter the new email address  \*

Yes

9 Do you wish to change the website address of the appointed representative?

If 'Yes', please enter the new website address:  \*

Yes No

10 Is the appointed representative currently an introducer appointed representative?

Do you wish to change this? Please provide details below:

Yes No

11 Does the appointed representative undertake insurance mediation?

Do you wish to change this? Please provide details below:

Yes No

Do you wish to change the details of the Main Contact for the FSA register for this appointed representative?

If 'Yes', please give the new details:

Title

Forename(s)

Surname

Yes No

12 Does the appointed representative undertake regulated mortgage activities?

Do you wish to change this? Please provide details below:

Yes No

13 Does the appointed representative undertake designated investment business activities?

Do you wish to change this? Please provide details below:

14 Please enter the date on which these changes take effect:  /  /  \*

**Warning**

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

**Data Protection**

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

**Declaration**

By submitting this notification

- I/we confirm that this information is accurate and complete to the best of my knowledge and belief and that I have taken all reasonable steps to ensure that this is the case.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date

Name of signatory

Position in *firm*

Individual Registration Number (if applicable)

Signature

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 12 Ann 5R: Appointed representative termination form



# Appointed Representative - Termination

Notification under SUP 12.8.1

(September 2004)

*Firm name (i.e. the principal firm)*

("The Firm")

FSA reference number

Address

**Please return this form to :**

Authorisation & Approvals Department  
The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS  
United Kingdom  
Telephone +44 (0) 20 7066 1000  
Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

## NOTES

This form should be used to notify the FSA of the termination of an existing appointed representative arrangement

**Personal Details**

**Section A**

**1** Contact Name for this form

\_\_\_\_\_ \*

**2** Contact's Details:

**a** Position in the *firm*

\_\_\_\_\_ \*

**b** Daytime telephone number

\_\_\_\_\_ \*

**c** E-mail address

\_\_\_\_\_

**d** Individual reference number (IRN), if applicable

\_\_\_\_\_





Reason For Termination:

Resignation/end of contract

Terminated by principal

If the reason for termination is Termination by Principal please give further details below:

If you have any additional information to add to the reason above please attach it to this form.

Date of Termination:

/ /

Please use this section if you wish to terminate one appointed representative. If you wish to terminate more than one appointed representative but for different reasons please copy this section as appropriate and attach to the form.

In order to terminate an appointed representative please complete the following details:

Please enter the name of the appointed representative:

 \*

Please enter the FRN of the appointed representative:

Please enter the postcode of the appointed representative:

Reason For Termination:

Resignation/end of contract

Terminated by principal

If the reason for termination is Termination by Principal please give further details below:

If you have any additional information to add to the reason above please attach it to this form.

Date of Termination:

 / /

**Warning**

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

**Data Protection**

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

**Declaration**

By submitting this notification

- I/we confirm that this information is accurate and complete to the best of my knowledge and belief and that I have taken all reasonable steps to ensure that this is the case.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date

Name of signatory

Position in *firm*

Individual Registration Number (if applicable)

Signature

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 15 Ann 2R: Standing data form



## Standing Data

**To update firm name and trading names, website address, accounting reference date, auditors, locum, contacts and addresses.**

(September 2004)

Firm name

("The Firm")

FSA firm reference number

Address

**(Please return the form, marked for the attention of the Firm Contact Centre, to:)**

The Financial Services Authority

25 The North Colonnade

Canary Wharf

London E14 5HS

United Kingdom

Telephone +44 (0) 20 7066 1000

Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

## NOTES

This form should be used to update your firm name and trading name(s), website address, accounting reference date, auditors, locum, contacts and addresses.

### Personal Details

### Section A

1 Contact Name for this application

 \*

2 Contact's Details:

a Position in the firm

 \*

b Daytime telephone number

 \*

c E-mail address

d Individual reference number (IRN), if applicable

### Change Full Name of Firm

### Section B

If you wish to advise FSA of a change to the firm's name please enter the following details, otherwise proceed to Section C1.

**Note:** this section is not intended to be used by firms that are covered by Industrial & Provident, Friendly Society, Credit Union or Building Society legislation. These firms should contact the FSA's Mutuals Team.

Current Legal Status:

(a) Private Limited Company

(b) Public Limited Company

(c) Limited Liability Partnership

(d) Limited Partnership

(e) Sole Trader

(f) Unlimited Liability Company

(g) Partnership

(h) Other, please specify below

1 New full name of firm

 \*

- 2 Please enter the date on which the change becomes effective  /  /
- Yes No N/A
- 3 Has the change requested been approved by Companies House?

**If your firm is a UK registered limited company (including PLC), limited partnership (if registered at Companies House), limited liability partnership or unlimited liability company, you should only make a change to your firm name if the change has already been approved by Companies House**

If you have answered 'Not Applicable', please explain why below:

- 4 I confirm that the change requested does not constitute a change of legal status

## Add New Trading Name(s)

## Section C1

If you wish to add a new trading name of the firm please enter the following details, otherwise please proceed to Section C2:

- 1 New Trading Name  \*
- 1a Please enter the date on which the change becomes effective  /  /  \*
- 2 New Trading Name  \*
- 2a Please enter the date on which the change becomes effective  /  /  \*
- 3 New Trading Name  \*
- 3a Please enter the date on which the change becomes effective  /  /  \*
- 4 New Trading Name  \*
- 4a Please enter the date on which the change becomes effective  /  /  \*

## Delete Current Trading Name(s)

## Section C2

If you wish to delete a trading name of the firm please enter the following details, otherwise please proceed to Section D:

- 1 Trading name to be deleted  \*
- 1a Please confirm when the trading name must cease:  /  /  \*
- 1b I confirm that the above trading name will not be used by the firm from the date indicated above.
- 2 Trading name to be deleted  \*
- 2a Please confirm when the trading name must cease:  /  /  \*
- 2b I confirm that the above trading name will not be used by the firm from the date indicated above.
- 3 Trading name to be deleted  \*
- 3a Please confirm when the trading name must cease:  /  /  \*
- 3b I confirm that the above trading name will not be used by the firm from the date indicated above.
- 4 Trading name to be deleted  \*
- 4a Please confirm when the trading name must cease:  /  /  \*
- 4b I confirm that the above trading name will not be used by the firm from the date indicated above.



If you wish to change the contact details of the Complaints Officer or Primary Compliance Contact please enter the following details, otherwise please proceed to Section E1:

**Please note that this will not change your approved person records. If you want to change these records, please use the appropriate Approved Persons Form.**

Please indicate which contact this change applies to. If you wish to change the details for both please copy this form and record the details for each on separate forms, unless the details are the same.

(a) Complaints Officer  (b) Primary Compliance Contact

1 Title  \*

2 Forename(s)  \*

3 Surname  \*

4 Job Title

5 Email address

6 Phone number. This must be a direct dialled number.  \*

7 Fax Number

8 Please enter the date on which the change becomes effective.  /  /  \*

9 Address  \*

Postcode:

10 If you would also like the contact details of the following to be changed, please tick the appropriate boxes. This will amend the contact details in line with the changes recorded above.

Complaints Contact  Primary Compliance Contact

## Change of Address

## Section E1

1. Please indicate which of the following this change applies to. If you wish to change the details for more than one of the following please copy this form and record the details for each on separate forms, unless the details are the same.

- (a) Registered Office  (b) Principal Place of Business   
(c) Billing Address  (d) Publication Address   
(e) Head Office

Please enter the new address details:

2 Address

\*

Postcode:

3 Telephone number.

\*

4 Fax Number

5 Email address

6 Please enter the date on which the change becomes effective.

/  /  \*

7 **Contact Address Details**

- (a) Complaints Address  (b) Principal Compliance Address

## Change of Other Address

## Section E2

1. Please indicate which of the following this change applies to. If you wish to change the details for more than one of the following please copy this form and record the details for each on separate forms, unless the details are the same.

- (a) 3<sup>rd</sup> Party Administration  (b) Actuary   
(c) Customer Services  (d) EEA Branch Address   
(e) Firm Association Branch  (f) IVAD Contact Address

(g) Professional Advisor

Please enter the new address details:

2 Address

\*

Postcode:

3 Telephone number.

\*

4 Fax Number

5 Email address

6 Please enter the date on which the change becomes effective.

/ / \*

## Change of Accounting Reference Date

## Section F

1 Please enter the following details to change your accounting reference date:

(a) Current Accounting Reference Date (dd/mm)  \*

(b) New Accounting Reference Date (dd/mm)  \*

2 What accounting periods will result from the change? The new accounting reference date that you have entered could result in several different periods depending on whether you want to extend or reduce your periods and which period is the first period affected.

Although the FSA may accept accounting periods of up to 18 months, SUP 16.3.18G advises firms that accounting periods longer than 15 months may be deemed unacceptable as this may hinder the timely provision of relevant and important information to the FSA. If a firm wishes to have an accounting period of longer than 18 months (sole traders and certain partnerships), the firm must apply to the FSA in writing.

Please detail the start and end dates for the current accounting period and the two following periods below:

(a) Current Period  \*

(b) Next Period  \*

(c) Next Period 2  \*

**Note the change that you have requested will result in a change to your reporting timetable.**

3 I confirm the change requested above and that it is correctly represented by the accounting periods listed.

## Change of Website Address

## Section G

Please enter the new website address:

1 Website (format – www.fsa.gov.uk):

## Change Auditor Details

## Section H1

Please enter the following details to change your Auditor's details:

1 Firm name  \*

2 Address

Grey rectangular input field with an asterisk (\*) in the top right corner. The text "Postcode:" is centered near the bottom.

3 Telephone number.

Grey rectangular input field with an asterisk (\*) in the top right corner.

4 Fax Number

Grey rectangular input field.

5 Email address

Grey rectangular input field.

6 Effective date

Grey rectangular input field with pre-filled slashes (/ /) and an asterisk (\*) in the top right corner.

**Change Locum Details** **Section H2**

For details of the FSA’s requirements for locum arrangements, see AUTH 3.9.10(2)G.  
Please enter the following details to change your Locum’s details:

1 Title

Grey rectangular input field.

2 Forename(s)

Grey rectangular input field.

3 Surname

Grey rectangular input field.

4 Firm name

Grey rectangular input field with an asterisk (\*) in the top right corner.

5 Address

Grey rectangular input field with an asterisk (\*) in the top right corner. The text "Postcode:" is centered near the bottom.

6 Telephone number.

Grey rectangular input field with an asterisk (\*) in the top right corner.

7 Fax Number

8 Email address

6 Effective date

**Warning**

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

**Data Protection**

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

**Declaration**

By submitting this application form

- I/we confirm that the information contained in this form is accurate and complete to the best of my knowledge and belief and that I have taken all reasonable steps to ensure that this is the case.
- I am/we are aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- I/we confirm that, for those questions that do not require supporting evidence, the records which demonstrate the firm's compliance with the rules in relation to the questions will be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in enforcement action.

Date

Name of first signatory<sup>8</sup>

Position<sup>9</sup> of first signatory

Individual Reference Number (IRN)

Signature

Name of second signatory<sup>1</sup>

Position<sup>2</sup> of second signatory

Individual Reference Number (IRN)

Signature

<sup>8</sup> For a sole trader, the signature of the principal is required.  
 For a limited company, the signature of two directors or one director and the company secretary is required.  
 For a partnership, the signature of at least one partner is required.  
<sup>9</sup> e.g. Director, Partner or Sole Trader.

The attached form or its online equivalent (if any) is the form detailed in Annex B for SUP 15 Ann 3R: Notification form





<b>Notifications Form</b>	

(September 2004)

Firm name

("The Firm")

FSA reference number

Address

**(Please return the form, marked for the attention of your normal supervisory contact, to:)**

The Financial Services Authority

25 The North Colonnade

Canary Wharf

London E14 5HS

United Kingdom

Telephone from UK: 0845 606 9966 (locals call rates)

from Overseas: +44 20 7066 1000

Facsimile +44 (0) 20 7066 1099

Registered as a Limited Company in England and Wales No 1920623. Registered Office as above.

1 Contact Name for this form \*

2 Contact's Details:

a Position in the firm \*

b Daytime telephone number \*

c E-mail address [please complete where possible]

d Individual reference number (IRN), if applicable

There are circumstances where a firm must disclose information to the FSA in a timely manner including:

- where a particular rule has been breached;
- where it fails to satisfy a threshold condition;
- where a matter occurs which could have a significant adverse impact on a firm, including its ability to provide adequate services to a customer; and
- where a particular notifiable event may have occurred

A consolidated summary of some of the notification rules is in the FSA Handbook, Schedule 2 of the Supervision Manual (SUP). Also Principles for Businesses (No 11) requires a firm to disclose appropriately any information of which the FSA would reasonable expect notice. Other notification requirements are listed in Schedule 2 of many of the other FSA Manuals within the Handbook. This form allows you to make any of these notifications.

3 To help us process your notification efficiently, please select one or more of the categories below by ticking the appropriate box and then giving details in Section 4:

**Finance/capital issues**

For example:

- breach of capital requirements;
- excess in allowed large exposures requirements;
- qualification in audited annual accounts (financial issue);
- insolvency, bankruptcy or winding up; and
- company to be struck off by Companies House.

<b>Client money issues</b>	<input type="checkbox"/>
For example: <ul style="list-style-type: none"> <li>• negative client money account; and</li> <li>• notifiable issue in client assets report.</li> </ul>	
<b>Professional indemnity insurance (PII) cover</b>	<input type="checkbox"/>
For example: <ul style="list-style-type: none"> <li>• cover not renewed;</li> <li>• cover exhausted; and</li> <li>• cover does not meet FSA requirements.</li> </ul>	
<b>Complaints, including a decision not to pay a FOS award</b>	<input type="checkbox"/>
<ul style="list-style-type: none"> <li>• Any complaints received that could have a significant impact on a firm's financial resources</li> <li>• A decision not to pay a Financial Ombudsman Service (FOS) award.</li> <li>• A firm's inability to pay a consumer</li> </ul>	
<b>Fraud, error or other irregularities</b>	<input type="checkbox"/>
For example: <ul style="list-style-type: none"> <li>• fraud on the firm (actual or attempted);</li> <li>• fraud by staff (actual or attempted); and</li> <li>• money laundering issues.</li> </ul>	
<b>Litigation/disciplinary issues, including civil, criminal or disciplinary proceedings against the firm or any of its representatives.</b>	<input type="checkbox"/>
<b>Other rules breaches (not included above).</b>	<input type="checkbox"/>
<b>Other notification requirements (not relating to a rule breach).</b>	<input type="checkbox"/>

This form does not cover

- changes to standing data (e.g. change of firm name, address, contact details, website, auditor, accounting reference date). These changes need to be made via the FSA Standing data form; or
- whistle blowing (i.e. revealing a suspected wrongdoing in an organisation). In these circumstances you should email [whistle@fsa.gov.uk](mailto:whistle@fsa.gov.uk), write in or phone us (020 7066 9200). Please see our website for more details <http://www.fsa.gov.uk/whistle/>

Yes No

4 Has the Notifiable event occurred?

4a If selected 'Yes', what date did the event occur (record last applicable date)?  /  /

4b If selected 'No', what is the probability of the event occurring?

5 If this notification is about a specific rule, threshold condition and/or principle, please record its reference if known:

6 What are the details of the notification?

7 What (if any) is the impact of the notification?

Yes No N/A

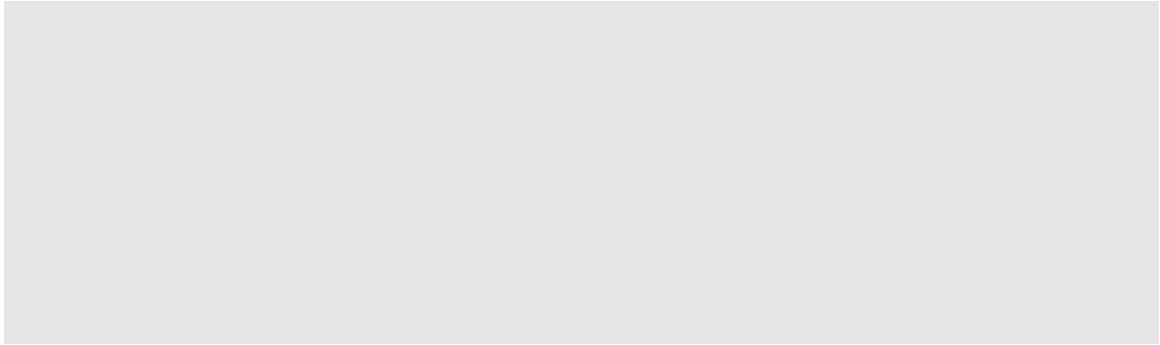
8 If relevant, have you resolved the issue?

8a If answered 'Yes'. When did you resolve the issue (end date)?

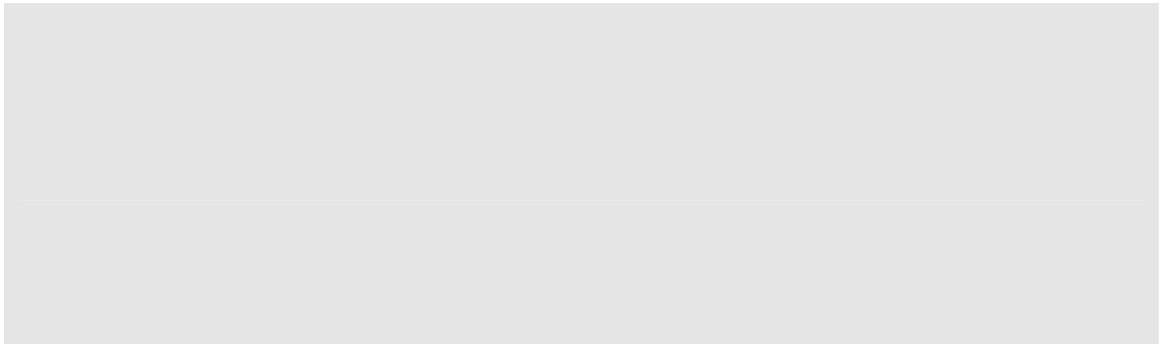
/ /

How was the issue resolved?

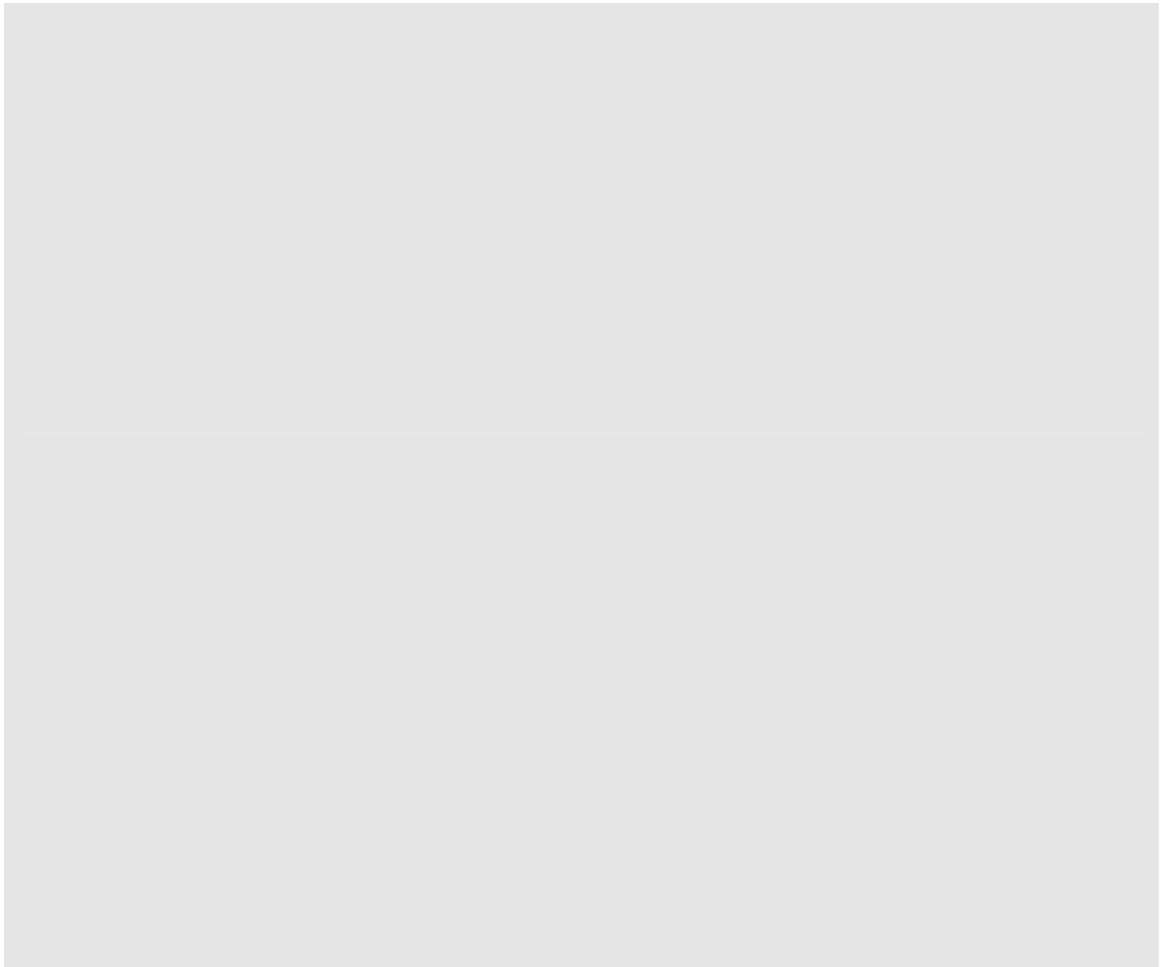
**8b** If answered 'No', what action (if any) will you be taking?



**8c** If answered 'Not applicable', please explain why below:



**9** If you have any additional information to add to this form, please enter it below or attach it as a document.



**Warning**

Knowingly or recklessly giving the FSA information, which is false or misleading in a material particular, may be a criminal offence (sections 398 and 400 of the Financial Services and Markets Act 2000). SUP 15.6.4R requires an authorised person to take reasonable steps to ensure the accuracy and completeness of information given to the FSA and to notify the FSA immediately if materially inaccurate information has been provided. Contravention of these requirements may lead to disciplinary sanctions or other enforcement action by the FSA. It should not be assumed that information is known to the FSA merely because it is in the public domain or has previously been disclosed to the FSA or another regulatory body. If you are not sure whether a piece of information is relevant, please include it anyway.

**Data Protection**

For the purposes of complying with the Data Protection Act, the personal information in this form will be used by the Financial Services Authority to discharge its statutory functions under the Financial Services and Markets Act 2000 and other relevant legislation. It will not be disclosed for any other purposes without the permission of the applicant.

**Declaration**

By submitting this application form

- I/we confirm that this information is accurate and complete to the best of my knowledge and belief and that I have taken all reasonable steps to ensure that this is the case.
- I/we am aware that it is a criminal offence knowingly or recklessly to give the FSA information that is false or misleading in a material particular.
- Some questions do not require supporting evidence. However, the records, which demonstrate the applicant firm's compliance with the rules in relation to the questions, must be available to the FSA on request.
- I/we will notify the FSA immediately if there is a significant change to the information given in the form. If I/we fail to do so, this may result in a delay in the application process or enforcement action.

Date	<input type="text"/>
Name of first signatory <sup>10</sup>	<input type="text"/>
Position <sup>11</sup> of first signatory	<input type="text"/>
Individual Registration Number	<input type="text"/>
Signature	<input type="text"/>
Name of second signatory	<input type="text"/>
Position of second signatory	<input type="text"/>
Individual Registration Number	<input type="text"/>
Signature	<input type="text"/>

<sup>10</sup> For a sole trader, the signature of the principal is required.  
 For a limited company, the signature of two directors or one director and the company secretary is required.  
 For a partnership, the signature of at least one partner is required.

<sup>11</sup> e.g. Director, Partner or Sole Trader.

## INTEGRATED REGULATORY REPORTING INSTRUMENT 2004

### **Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### **Commencement**

- C. This instrument comes into force on 1 April 2005.

### **Amendments to the Supervision Manual (Reporting and Audit Requirements) Instrument 2004 (FSA 2004/29)**

- D. The commencement of certain provisions introduced by the Supervision Manual (Reporting and Audit Requirements) Instrument 2004 (FSA 2004/29) is suspended until the Financial Services Authority by subsequent instrument provides for the commencement of these provisions. The affected amendments are set out in Annex A to this instrument.

### **Amendments to the Electronic Reporting Requirements and Standing Data Instrument 2004 (FSA 2004/30)**

- E. The commencement of certain provisions introduced by the Electronic Reporting Requirements and Standing Data Instrument 2004 (FSA 2004/30) is suspended until the Financial Services Authority by subsequent instrument provides for the commencement of these provisions. The affected provisions are set out in Annex B to this instrument.

### **Amendments to the Supervision manual**

- F. The Supervision manual is amended in accordance with Annex C to this instrument.

### **Amendments to the Dispute resolution: Complaints sourcebook**

- G. The Dispute resolution: Complaints sourcebook is amended in accordance with Annex D to this instrument.

### **Citation**

- H. This instrument may be cited as the Integrated Regulatory Reporting Instrument 2004.

By order of the Board  
20 October 2004



**Annex A**  
**Amendments to the Supervision Manual (Reporting and Audit Requirements)**  
**Instrument 2004 (FSA 2004/29)**

The commencement of the following provisions made in Part 3 of Annex A of the Supervision Manual (Reporting and Audit Requirements) Instrument 2004 (FSA 2004/29) is suspended until the Financial Services Authority by subsequent instrument provides for the commencement of these provisions.

The provisions whose commencement is suspended are:

1. *SUP 16.1.3 R*: insertion into the table of:

...		
<i>SUP 16.7</i>	....	
	<i>Insurer</i> <i>Friendly society</i>	<i>SUP 16.7.73 R to SUP 16.7.75 R</i>
	...	

2. *SUP 16.7.2 G*: amendments made to this guidance

3. *SUP 16.7.5 G*: insertion into the table of:

...	
<i>Insurer</i> <i>Friendly society</i>	<i>SUP 16.7.73 R to SUP 16.7.75 R</i>
...	

4. Amendments made to:

- a. *SUP 16.7.8 R*
- b. *SUP 16.7.10 R*
- c. *SUP 16.7.12 R*
- d. *SUP 16.7.17 R*
- e. *SUP 16.7.21 R*
- f. *SUP 16.7.25 R*
- g. *SUP 16.7.27 R*
- h. *SUP 16.7.29 R*

- i. *SUP* 16.7.33 R
  - j. *SUP* 16.7.36 R
  - k. *SUP* 16.7.58 R
  - l. *SUP* 16.7.63 R
  - m. *SUP* 16.7.63A G
  - n. *SUP* 16.7.66 R
5. Insertion of the following new provisions:
- a. *SUP* 16.7.73 R
  - b. *SUP* 16.7.74 R
  - c. *SUP* 16.7.75 R

## Annex B

### Amendments to the Electronic Reporting Requirements and Standing Data Instrument 2004 (FSA 2004/30)

The commencement of the following provisions introduced by the Electronic Reporting Requirements and Standing Data Instrument 2004 (FSA 2004/30) is suspended until the Financial Services Authority by subsequent instrument provides for the commencement of these provisions.

The provisions whose commencement is suspended are:

1. *SUP* 16.10.4 R (2)
2. The following provisions of *SUP* 16 Annex 16R
  3. Country of incorporation
  11. Whether the *firm* is an "*ISD investment firm*"
  12. *Firm* types
  13. *Passported activities*
3. All of *SUP* 16 Annex 17R

## Annex C

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

#### Part 1: Amendments to SUP Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
12B	<del>SUP 16.7.7R;</del> <del>SUP 16.7.9R;</del> <del>SUP 16.7.11R;</del> <del>SUP 16.7.16R;</del> <del>SUP 16.7.20R;</del> <del>SUP 16.7.24R;</del> <del>SUP 16.7.26R;</del> <del>SUP 16.7.28R;</del> <del>SUP 16.7.35R;</del> <del>SUP 16.7.54R;</del> <del>SUP 16.7.57R;</del> <del>SUP 16.7.62R;</del> <del>SUP 16.7.65R;</del> <del>SUP</del>	<b>R</b>	<p>(1) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-yearly basis, and the <i>firm</i> has:</p> <p style="padding-left: 20px;">(a) annual income of less than £5m but more than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity</i> and <del><i>retail investment activity</i></del> <u>its permitted activities as a personal investment firm</u>, and</p> <p style="text-align: center;">...</p> <p>(2) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-yearly basis, and the <i>firm</i> has:</p> <p style="padding-left: 20px;">(a) annual income of less than £5m but more than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity</i> and <del><i>retail investment activity</i></del> <u>its permitted activities as a personal investment firm</u>, and</p> <p style="text-align: center;">...</p> <p>(4) Where a <i>rule</i> in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a half-yearly basis, and the <i>firm</i> has:</p> <p style="padding-left: 20px;">(a) annual income of less than £60,000 in total from <i>insurance mediation activity, mortgage mediation activity</i> and <del><i>retail investment activity</i></del> <u>its permitted activities as a personal investment firm</u>, and</p> <p style="padding-left: 20px;">(b) an <i>accounting reference date</i> which falls between 31 December 2004 <del>1 January</del></p>	From 1 April 2005	1 April 2005

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
	<del>16.7.73R;</del> SUP 16.7.76R SUP 16.7.79R SUP 16.7.80R		<p><del>2005 and 30<sup>1</sup> December 2005</del> the relevant <i>rule</i> must be read as requiring the first return to be provided in accordance with <del>SUP TR 12DR.</del></p> <p>the relevant <i>rule</i> must be read as requiring the first return to be provided in accordance with <u>SUP TR 12DR.</u></p> <p>(5) Where a rule in SUP 16.7 requires a <i>firm</i> to submit information using the <i>RMAR</i> on a quarterly basis, and the firm has an <u>accounting reference date</u> which falls between 31 December 2004 and 30 December 2005 the <i>relevant rule</i> must be read as requiring the first return to be provided with <u>SUP TR 14B.</u></p>					
12C		<b>R</b>	If SUP TR 12B R (1) - (3) applies, the <i>firm's</i> first return must be provided as follows:					
			<i>Accounting reference date</i>	Reporting period starts	Reporting period ends	Return to be provided		
			...	...	....	...		
			<u>31 December 2004</u>	<u>1 April 2005</u>	<u>30 June 2005</u>	<u>30 business days after the period end</u>		
			Between <del>31 December 2004</del> <u>1 January 2005</u> and 31 March 2005	1 April 2005	6 months after <u>the accounting reference date</u> within 2005	30 <i>business days</i> after period end		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
12D		<b>R</b>	(1) If <i>SUP</i> TR 12B R (4) applies, the <i>firm's</i> first return must be provided as follows:					
			<i>Accounting reference date</i>	Reporting period starts	Reporting period ends	Return to be provided		
			<u>31 December 2004</u>	<u>1 April 2005</u>	<u>30 June 2005</u>	<u>30 business days after period end</u> (Note 1)		
			Between <del>31 December 2004</del> <u>1 January 2005</u> and 31 March 2005	1 April 2005	6 months after <u>the accounting reference date</u> within 2005	30 <i>business days</i> after period end (Note 1)		
			Between 1 April 2005 and 29 June 2005	the <del>business day</del> following <u>the accounting reference date</u> within 2005	6 months after <u>the accounting reference date</u> within 2005	30 <i>business days</i> after period end (Note 1)		
			...	...	...	...		
			Between 30 September 2005 and 30	<u>The day after 6 months preceding the</u>	...	...		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			December 2005	<i>accounting reference date</i> within 2005				
12E		<b>R</b>	(2) If <i>SUP</i> TR 12B R(4) applies, the <i>firm's</i> second return must be provided as follows:					
			<u><i>Accounting reference date</i></u>	<u><i>Reporting period starts</i></u>	<u><i>Reporting period ends</i></u>	<u><i>Return to be provided</i></u>		
			Between 30 June 2005 and 29 September 2005	the <i>business day</i> following the <u><i>accounting reference date</i></u> within 2005	6 months after the <u><i>Accounting reference date</i></u> within 2005	...		
14B		<b>R</b>	If <i>SUP</i> TR 12B R (5) applies, the <i>firm's</i> first return must be provided as follows:					
			<u><i>Accounting reference date</i></u>	<u><i>Reporting period starts</i></u>	<u><i>Reporting period ends</i></u>	<u><i>Return to be provided</i></u>		
			<u>31 December 2004</u>	<u>1 April 2005</u>	<u>30 June 2005</u>	<u>30 <i>business days</i> after period end</u>		
			<u>Between 1 January 2005 and 31 March</u>	<u>1 April 2005</u>	<u>6 months after the <i>accounting reference date</i> within</u>	<u>30 <i>business days</i> after period</u>		

(1)	(2)	(3)	(4)				(5)	(6)
	Material to which the transitional provision applies		Transitional provision				Transitional provision: dates in force	Handbook provision: coming into force
			<u>2005</u>		<u>2005</u>	<u>end</u> (Note 2)		
			<u>Between 1 April 2005 and 29 June 2005</u>	<u>The day following the accounting reference date within 2005</u>	<u>3 months after the accounting reference date within 2005</u>	<u>30 business days after period end</u> (Note 2)		
			<u>Between 30 June 2005 and 29 September 2005</u>	<u>1 April 2005</u>	<u>Accounting reference date within 2005</u>	<u>30 business days after period end</u> (Note 2)		
			<u>Between 30 September 2005 and 30 December 2005</u>	<u>The day after 6 months preceding the accounting reference date within 2005</u>	<u>3 months preceding the accounting reference date within 2005</u>	<u>30 business days after period end</u> (Note 3)		
14C	<u>16.10.4</u>	<b>R</b>	<u>A firm whose accounting reference date falls between 1 April 2005 and 30 June 2005 (inclusive) need not comply with SUP 16.10.4 R until its accounting reference date in 2006.</u>				<u>1 April 2005 – 30 June 2005</u>	<u>1 April 2005</u>
14D	<u>16.11.3</u>	<b>R</b>	<u>The report under SUP 16.11.3 R (1) for the quarter 1 April to 30 June 2005, together with the report for the quarter 1 July to 30 September 2005 must be submitted within 20 business days after the end of the 1 July -30 September 2005 quarter.</u>				<u>1 April 2005 – 30 June 2005</u>	<u>1 April 2005</u>



Note 2 = Sections A, B, C, D, E of the *RMAR* should be reported for the 3 months to the reporting end date.

Note 3 = This should only cover sections A, B, C, D, E of the *RMAR*

**Part 2: Amendments to SUP 16**

16.1.3 R

(1) Section(s)	(2) Categories of firm to which section applies	(3) Applicable rules and guidance
...		
<i>SUP 16.7</i>	....	
	<p>A <i>firm</i> not subject to other reporting requirements in <i>SUP 16.7.1-16.7.75</i>:</p> <p>...</p> <p>(2) which is a <i>retail investment firm</i> <i>personal investment firm</i></p>	<p><i>SUP 16.7.76 R</i> to <i>SUP 16.7.81 G</i></p>
	...	

...

16.3.2 G ...

(7) ~~Confirmation~~ Verification of *standing data* (*SUP 16.10*); and ...

...

16.3.9 R (6) Online submission via the *FSA's* website at [www.fsa.gov.uk](http://www.fsa.gov.uk)

...

16.7.5 G Table Applicable rules and guidance on reports (see *SUP 16.7.1G*)

Firm Category	Applicable rules and guidance
....	
<p>A <i>firm</i> not subject to other reporting requirements in <i>SUP 16.7.1-16.7.75</i>:</p> <p>...</p> <p>(b) which is a <i>retail investment firm</i> <i>personal investment firm</i></p>	<p><i>SUP 16.7.76 R</i> to <i>SUP 16.7.81 G</i></p>

...

16.7.6B G The *RMAR* is relevant to the reporting requirements of personal investment firms and firms carrying on insurance mediation activity, mortgage mediation activity or retail investment activity. ...

16.7.6C R Where reference is made in SUP 16.7 to adequate information relating to the following activities:

(1) a personal investment firm; or

(2) the following activities:

(a) insurance mediation activity; or

(b) mortgage mediation activity; or

(c) retail investment activity;

this includes ...

...

16.7.54 R (1) An *authorised professional firm* must submit an annual questionnaire ... unless:

(a) its only *regulated activities* are one or more of:

(i) insurance mediation;

(ii) mortgage mediation;

(iii) retail investment;

(iv) mortgage lending;

(v) mortgage administration; or

(b) its "main business" as determined by IPRU (INV) 2.1.2 R (3) is advising on, or arranging deals in, packaged products, or managing investments for private customers.

(e)

16.7.54A R Table

Report	Return (Note 1)	Frequency	Due date
Adequate information relating to the following activities: (1) ....	...	...	...

(4) <u>advising on, or arranging deals in, packaged products, or managing investments for private customers where these activities are the authorised professional firm's "main business" as determined by IPRU (INV) 2.1.2 R (3)</u>			
---	--	--	--

...

16.7.76 R Replace the reference in paragraph (b) to "*retail investment firm*" with "*personal investment firm*".

16.7.77 R Table

Insert new text as underlined:

Report	Return (Note 1)	Frequency	Due date
Adequate information relating to: <u>(1) a personal investment firm; or</u> <u>(2) the following activities:</u>  <u>(a) insurance mediation activity;</u>  <u>(b) ...</u>  <u>(c) ...</u>	...	...	...
...			
If the <i>firm</i> is a <i>mortgage lender</i> or <i>mortgage administrator</i> , annual report and audited accounts.	N/A	Annually	3 months after the <i>firm's</i> <i>accounting reference date</i>
<u>Consolidated supervision return (note 5)</u>		<u>Half yearly</u>	<u>4 months after end of relevant 6-month period</u>
<u>Annual accounts of the mixed-activity holding company (Note 6)</u>		<u>Annually</u>	<u>As soon as available after year-end</u>

...

Note 5 = This report is only required from a category A1, A2 or A3 *personal investment firm* if it is a member of a *group*, and it is subject to consolidated

supervision as set out in IPRU (INV) Chapter 14.

Note 6 = This report is only required from a category A1, A2 or A3 *personal investment firm* if its ultimate parent is a *mixed-activity holding company*

...

16.10 ~~Confirmation~~ Verification of standing data

...

Requirement to check accuracy of standing data and to report changes to the FSA

16.10.4 R ...

(3) If any *standing data* is incorrect, the *firm* must give the corrected *standing data* to ~~the firm's usual supervisory contact at the FSA,~~ by electronic mail using the appropriate form submitted in accordance with instructions on that form.

16.10.5 G The *standing data* is made available to the *firm* when the *firm* logs into the appropriate section of the FSA website. The *firm* should check the *standing data* and send any corrections to the FSA. ~~If there are no errors, the firm will be asked to signal this by pressing the appropriate button on the web page.~~ The FSA's preferred method of receiving corrections to *standing data* is by the online forms available at the FSA's website.

...

16.10.7 G For the purpose of SUP 16.10.4 R (3), the appropriate form will be determined by the *standing data* to be corrected. Appropriate forms will include (but are not limited to) the form in SUP 15 Ann 2R (standing data form) and the form in SUP 15 Ann 3R (notification form).

...

16.11 Product Sales Data Reporting

Application

16.11.1 R This ~~chapter~~ section applies to a firm which is a *mortgage lender*; or ...

...

Purpose

16.11.2 G (1) The purpose of this ~~chapter~~ section is to set out the requirements for *firms* in the retail mortgage, investment, and *pure protection contract* markets specified in SUP 16.11.1 R to report individual product sales data to the FSA. ...

...

16.11.8 R The data report must refer both to transactions undertaken by the *firm* and to transactions undertaken by an intermediary which has dealt directly with the customer ~~*firm*~~ on the *firm's* behalf.

16.11.8 G Where the *operator* of a *collective investment scheme* receives business from a *firm* which operates a nominee account, the data report in respect of those transactions submitted by the *operator* should treat those transactions as transactions undertaken by the *operator* with the *firm*.  
A

...

SUP 16 Ann 18A R Retail Mediation Activities Return ('RMAR')

Insert as the first question before SECTION A of the RMAR the following question:

What is the *firm's regulated business revenue* in the most recent *financial year*?

Amend the following pages of the RMAR making the underlined insertions and the struck through deletions. All amendments have been highlighted in grey to facilitate easy identification of the changes to the RMAR. Changes to cell reference numbers should be ignored (they will not be visible on the online form).

**SECTION A: Balance sheet**

**Fixed assets**

Intangible assets	RR0076
Tangible assets	RR0077
Investments	RR0078
<b>TOTAL FIXED ASSETS</b>	<b>RR0079</b>

**Current assets**

Stocks	RR0081
Debtors	RR0082
Investments held as current assets	RR0083
Cash at bank and in hand	RR0084
<u>Other assets</u>	RR0086a
<b>TOTAL CURRENT ASSETS</b>	<b>RR0086</b>

**Liabilities: amounts falling due within one year**

Bank loans and overdrafts	RR0088
Other liabilities falling due within one year	RR0089

TOTAL AMOUNTS FALLING DUE WITHIN ONE YEAR **RR0090**

**Net current assets**

**RR0091**

**Total assets less current liabilities**

**RR0092**

**Other liabilities falling due after more than one year**

**RR0093**

**Provisions for liabilities and charges**

**RR0094**

**Net assets**

**RR0095**

**Memo: guarantees provided by firm**

**RR0096**

**Memo: personal net assets**

**RR0097**

**Memo: Goodwill**

**RR0098**

**Capital and reserves**

**Capital account (incorporated businesses excluding Limited Liability Partnerships)**

Ordinary share capital	RR0100
Preference share capital	RR0101
Share premium account	RR0102
Profit and Loss account	RR0103
Other reserves	RR0104
<b>TOTAL CAPITAL AND RESERVES</b>	<b>RR0105</b>

Was the firm's last annual accounts audit report qualified? Yes / No  
**RR0117**

**Capital account (unincorporated businesses and Limited Liability Partnerships)**

Sole trader/Partners' capital account/Members' capital	RR0119
Sole trader/Partners' current account/Other Reserves	RR0120
<b>TOTAL CAPITAL AND RESERVES</b>	<b>RR0121</b>

**SECTION B: Profit and Loss account**

**B1: Regulated Business Revenue**

	Commissions		Fees	Other income (reg activities)	Regulated business revenue
	Gross	Net			
Regulated mortgage contracts	RR0125	RR0126	RR0127	RR0128	RR0129
Non-investment insurance	RR0131	RR0132	RR0133	RR0134	RR0135
Retail investments	RR0137	RR0138	RR0139	RR0140	RR0141
<b>TOTAL</b>	<b>RR0143</b>	<b>RR0144</b>	<b>RR0145</b>	<b>RR0146</b>	<b>RR0147</b>

**B2: Other P&L**

<u>Income from other regulated activities</u>	RR0148c	
Other Revenue (income from non-regulated activities)	RR0149	
<b>TOTAL REVENUE</b>	RR0150	PL20 + PL24
<b>TOTAL EXPENDITURE</b>	RR0156	
Profit/(Loss) on ordinary activities before taxation	RR0157	PL22 less PL23
Profit/(Loss) on extraordinary activities before taxation	RR0157a	
Taxation	RR0158	
Profit/(Loss) for the period before dividends and appropriations	RR0159	(PL24 + PL25) – PL26
Dividends and other appropriations	RR0160	
Retained Profit	RR0161	PL27 less PL28



**SECTION C: Client money and assets**

Have any notifiable issues been raised in relation to client money or other assets, either in the firm's last client assets audit report or elsewhere, that have not previously been notified to the FSA?

Yes / No

RR0174

How is your client account(s) set up (tick all that apply)?

	Risk Transfer	Segregated Trusts	
		Statutory	Non-statutory
Non-investment insurance	RR0176	RR0177	RR0178
Retail investments		RR0178a	

~~If not risk transfer:~~

	Non-investment insurance		Retail investments
	Statutory	Non-statutory	Statutory
Client money credit total as at reporting date	RR0181	RR0182	RR0182a
Client money debit total as at reporting date	RR0184	RR0185	RR0185a
Net client money balance as at reporting date	RR0187	RR0188	RR0188a

If non-statutory, has auditor's confirmation of systems and controls been obtained?

Yes / No

RR0189

Is any client money invested (other than on deposit)?

Yes / No

RR0190

Do you hold client money for business undertaken by an AR?

Yes / No

RR0191

Does the firm hold any client assets (other than client money)?

Mortgage	Non-investment	
	insurance	Retail investments
RR0193	RR0194	RR0195

## SECTION D1: Regulatory Capital

Is the firm exempt from these capital requirements in relation to any of its retail mediation activities?

	Non- investment insurance	Retail investments
<b>Mortgage</b>		
RR0198	RR0199	RR0200

### Mortgage and non-investment insurance

Base requirement  
5% of annual income (firms holding client money)  
2.5% of annual income (firms not holding client money)

Client money	Non-client money
RR0202	RR0203
RR0205	
	RR0206

### Capital requirement (higher of above)

RR0207	RR0208
--------	--------

Other FSA capital requirements (if applicable)  
Additional capital requirements for PII (if applicable)

RR0210
RR0211

### TOTAL CAPITAL REQUIREMENT

RR0212	(RC8 or RC9) + RC10 + RC11
--------	----------------------------

### TOTAL CAPITAL RESOURCES

RR0213	See notes
--------	-----------

### TOTAL CAPITAL EXCESS/DEFICIT

RR0214	RC13 less RC12
--------	----------------

### Eligible capital (mortgage and non-investment insurance)

#### Incorporated firms

Share capital  
Audited reserves  
Interim net profits (audited)  
Interim net profits (not audited)  
Revaluation reserves  
Eligible subordinated loans  
**less** Investments in own shares  
**less** Intangible assets  
**less** interim net losses  
TOTAL CAPITAL RESOURCES

RR0228
RR0229
RR3231
RR3232
RR0233
RR0234
RR0235
RR0236
RR0237
RR0238

RC27 + RC28 + RC29 + RC31  
+ RC32 less RC33 less RC34  
less RC35

#### Unincorporated firms

Capital of a sole trader or partnership  
Eligible subordinated loans  
Personal assets not needed to meet non-business liabilities  
**less** Intangible assets  
**less** interim net losses  
**less** excess of drawings over profits for a sole trader or p'ship  
TOTAL CAPITAL RESOURCES

RR0240
RR0245
RR0246
RR0247
RR0248
RR0249
RR0250

RC37 + RC38 + RC39 less  
RC40 less RC41 less RC42

### IPRU(INV) requirements for personal investment firms (retail investment activities only)

Category of personal investment firm under IPRU(INV)

RR0215a
---------

### Own funds requirement

RR0216	A
--------	---

### Own funds

RR0217	B
--------	---

### Surplus/deficit of own funds

RR0218	C
--------	---

Additional own funds requirement for PII (if applicable)

RR0219
--------

Other FSA capital requirements (if applicable)

RR0219a
---------

### Adjusted net current assets requirement (if applicable)

RR0220	D
--------	---

Adjusted net current assets (if applicable)

RR0221	E
--------	---

Surplus/deficit (if applicable)

RR0222	F
--------	---

### Expenditure based requirement (if applicable)

RR0223	G
--------	---

Adjusted Capital/liquid capital (if applicable)

RR0224	H
--------	---

Surplus/deficit (if applicable)

RR0225	I
--------	---

**SECTION E: PII Self-Certification**

Is the firm exempt from the PII requirements in respect of any regulated activities? (tick as appropriate)

Mortgage advising/arranging	Non-inv insurance advising/arranging/dealing/assisting	Retail investment advising/arranging
RR0358	RR0359	RR0360

If not exempt, has the firm renewed its PII cover since the last reporting date?

RR0362	RR0363	RR0364
--------	--------	--------

Have any of the data items below changed since the last reporting date (or since you last notified the FSA of any changes)?

RR0366	RR0367	RR0368
--------	--------	--------

If any of the data items have changed, Please complete amend the following fields section as appropriate, in relation to each applicable PII policy:

What activities are covered by the policy?

Mortgage advising/arranging	RR0371
Non-inv insurance advising/arranging/dealing/assisting	RR0372
Retail investment advising/arranging	RR0373
Is the cover compliant?	RR0374
Annual premium	RR0375
Limit of Indemnity - single claim/aggregate	RR0376
Policy excess	RR0377
Increased excess(es) for specific business types	RR0378
Policy exclusion(s) for specific business types	RR0379
Renewal date	RR0380
Insurer name	RR0381

Amount of additional capital required for increased excess(es) (where applicable, total amount for all PII policies)

RR0383

**Personal investment firms only:**

Total amount of additional own funds required for policy exclusion(s)

RR0384

Total of additional own funds required

RR0386

Total of readily realisable own funds

RR0387

Excess/deficit of readily realisable own funds

RR0388

Y/N

Does the firm have any other PII policies?

RR0389

## SECTION F: Threshold conditions

### Adequate resources

Does the firm have adequate resources in relation to its regulated activities?

RR0392

### Close links

Are you exempt from close links reporting requirements?

RR0394

If not, have there been changes to your close links since the FSA was last informed?

RR0395

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

RR0396

### Approved persons

Have there been changes to your approved persons' details since the FSA was last informed?

RR0398

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

RR0399

### Controllers

Are you exempt from the controllers reporting requirements?

RR0401

If not, have there been changes to your controllers or to the percentage of shares or voting power in the firm held by any of them since the FSA was last informed?

RR0402

If yes, on what date did the changes take effect?  
(if no notification has been made, please notify us separately of the changes)

RR0403

**SECTION G: Training and Competence**

	Mortgages		Advising on non-investment insurance (retail customers)	Retail investments		Total
	advising	arranging		advising	arranging	
Total number of all staff						RR0405
Of which:						
Number of staff that give advice	RR0407		RR0408		RR0409	RR0410
<u>Number of staff that give advice (Full time equivalent)</u>						RR410a
Number of staff that supervise others to give advice	RR0412		RR0413		RR0414	RR0415
Number of advisers that have been assessed as competent	RR0417		RR0418		RR0419	RR0420
Number of advisers that have passed approved appropriate examinations	RR0422				RR0423	RR0424
Number of advisers that have left since the last reporting date	RR0426		RR0427		RR0428	RR0429
Number of staff that take private customers through stakeholder pension scheme decision trees					RR0431	RR0432
Number of staff that supervise non-advised sales of lifetime mortgages		RR0434				RR0435
Number of staff that design filtering questions for non-advised sales of lifetime mortgages		RR0437				RR0438

**SECTION H: COB Data**

**Sources of business:** please tick all that apply, or confirm here that there have been no changes since the last reporting date. no changes  
RR0441

	Mortgage	Non-inv insurance (except reinsurance)	Retail investments
Marketing lists	RR0444	RR0443	RR0445
Referrals from non-authorized introducers	RR0448	RR0447	RR0449
Referrals from intermediaries	RR0452	RR0451	RR0453
Telephone sales	RR0456	RR0455	RR0457
Cold calling	RR0460	RR0459	RR0461
Sales visits	RR0464	RR0463	RR0465
Postal sales	RR0468	RR0467	RR0469
Direct offer financial promotions	RR0472	RR0471	RR0473
Repeat customers	RR0476	RR0475	RR0477
Internet Sales	RR0480	RR0479	RR0481
Other	RR0484	RR0483	RR0485

**Advertising**  
Does your firm approve financial promotions and/or qualifying credit promotions? RR0489   RR0488   RR0490

**Types of advertising:** please tick all that apply, or confirm here that there have been no changes since the last reporting date. no changes  
RR0492

	Mortgage	Non-inv insurance (except reinsurance)	Retail investments
Newspaper	RR0495	RR0494	RR0496
Magazine	RR0499	RR0498	RR0500
T.V.	RR0503	RR0502	RR0504
Radio	RR0507	RR0506	RR0508
Internet	RR0511	RR0510	RR0512
Other	RR0515	RR0514	RR0516

Do you use one or more lists or panels of preferred product providers? y/n  
RR0517a

	Mortgage	Non-inv insurance (except reinsurance)	Retail investments
If yes, indicate the applicable types of business	RR0517b	RR0517c	RR0517d

What (if known) is the total number of providers on the panel(s)? RR0521a  
How often (if known) are the panel(s) reviewed? RR0522a

**General COB data**

Do regulated activities form the core business of the firm? RR0526  
If not, specify type of core business: RR0527

Do you give independent advice? Mortgage   Non-inv insurance   Retail inves  
RR0528   RR0528a   RR0528b

**Clawed back commission (retail investment firms only)**

Clawed back commission by: Number   RR0531  
Value   RR0532

**Complaints**

Does the firm have complaints handling procedures? y/n  
RR0534a

**Monitoring of Appointed Representatives ('ARs')**

Number of ARs registered with the firm RR0542  
Of which, number of 'secondary' ARs RR0543  
Of which, number of introducer ARs RR0544  
Number of advisers within ARs RR0545

(Only firms that have ARs)  
Does the firm have appropriate systems and procedures to ensure that the activities of its ARs are effectively monitored and controlled? RR0546

Number of ARs that have been subject to monitoring visits by the firm during the reporting period. RR0547

Number of ARs that have been subject to file reviews by the firm during the reporting period. RR0548

Number of ARs that have been subject to financial checks by the firm during the reporting period. RR0549

Has any other monitoring of ARs by the firm taken place? RR0550

**SECTION I: supplementary product sales data**

**(i) non-investment insurance contracts - product information**

1 Please indicate in column **A** each product type where the firm has advised or arranged transactions for retail customers during the reporting period

Please indicate in column **B** where the firm's retail-business for retail customers in the product type formed more than

40% by premium of all of its retail non-investment insurance activities.

**(ii) non-investment insurance chains**

3 Total non-investment insurance premium derived from retail customers

RR0556

4 Of this business, please indicate in column **C** the products where retail sales were passed up a chain and in column **D** where this business is significant\*

\*significant is where premium collected from being in a chain for this product amounts to

- 1) more than 40% of the premium collected for all non-investment insurance activities with retail customers, or
- 2) more than 40% of premium collected for all retail business in this product

6 Please also indicate in column **E** where the firm has dealt directly with the retail customer within the chain

**(iii) dealing as agent**

If you **deal as agent** for non-investment insurance contracts:  
Please provide:

7 Number of sales to retail customers during the reporting period where the firm dealt as agent

RR0564

8 Premium paid by retail customers during the reporting period where the firm dealt as agent

RR0565

9 Of the total of these sales, please indicate in column **F** the products where the firm dealt as agent and in column **G** where this business is significant\*.

\*significant is where premium collected from dealing as agent in this product amounts to

- 1) more than 40% of the premium collected for all non-investment insurance activities with retail customers, or
- 2) more than 40% of premium collected for all retail business in this product

**(iv) claims handling**

If you **assist** in the administration and performance of contracts of insurance:  
Please provide:

11 Number of claims handled on behalf of customers during the reporting period

RR0572

**(v) Lloyd's brokers - product sales data**

	Retail	Commercial	Reinsurance	Total
12 % of regulated business revenue	RR0672	RR0673	RR0674	100%

Round to nearest 20% and ensure figures add to 100%

Product types:	A y/n	B y/n	C y/n	D y/n	E y/n	F y/n	G y/n
Private motor	RR0575	RR0576	RR0577	RR0578	RR0579	RR0580	RR0581
Household	RR0583	RR0584	RR0585	RR0586	RR0587	RR0588	RR0589
Creditor - Payment protection	RR0591	RR0592	RR0593	RR0594	RR0595	RR0596	RR0597
Travel	RR0599	RR0600	RR0601	RR0602	RR0603	RR0604	RR0605
Personal accident - sickness	RR0607	RR0608	RR0609	RR0610	RR0611	RR0612	RR0613
Legal expenses	RR0615	RR0616	RR0617	RR0618	RR0619	RR0620	RR0621
Private Medical Insurance (PMI)	RR0623	RR0624	RR0625	RR0626	RR0627	RR0628	RR0629
Critical illness	RR0631	RR0632	RR0633	RR0634	RR0635	RR0636	RR0637
Private Health Insurance (PHI)	RR0639	RR0640	RR0641	RR0642	RR0643	RR0644	RR0645
Life assurance (or term assurance)	RR0647	RR0648	RR0649	RR0650	RR0651	RR0652	RR0653
HealthCare cash plan	RR0655	RR0656	RR0657	RR0658	RR0659	RR0660	RR0661
Extended warranty (motor only)	RR0663	RR0664	RR0665	RR0666	RR0667	RR0668	RR0669

SUP 16 Ann 18B G Notes for completion of the Retail Mediation Activities Return ('RMAR')

...

Introduction: general notes on the RMAR

...

Application of RMAR sections

6 ...

(c) *firms* (defined as *retail investment firms*) that have *private customers*, and have *permission* to carry on the following activities in relation to *retail investments*:

- *Advising on investments*;
  - *Arranging (bringing about) deals in investments*;
  - *Making arrangements with a view to transactions in investments*;
- and

(d) *personal investment firms*.

...

7 ~~Many of the *firms* conducting the above *regulated activities* also have the *permission* to carry on other *regulated activities*, including for example *mortgage lending and administration*, *managing investments* or *dealing in investments as agent*. These *firms* are required to complete the RMAR in addition to other data requirements.~~

Firms conducting *mortgage lending* or *mortgage administration* (including those that carry on an activity that is treated as *arranging in COB* - see *MCOB 1.2.12*) that also conduct the above activities are required to complete the *RMAR* in addition to other data requirements.

8 ~~However, not all *firms* are required to complete all sections of the RMAR. Certain data requirements will be duplicated because of the separate reporting requirements imposed in relation to other *regulated activities*. Broadly, a *firm* that has the *permission* to carry on other *regulated activities* will not be subject to our proposed data requirements for financial reporting (RMAR sections A, B, C, D & E) or *threshold conditions* (section F), as we would expect to be collecting similar information as part of the data requirements for these other activities. For details, see *SUP 16.7*.~~

However, these *firms* are not required to complete all sections of the *RMAR*. Certain data requirements will be de-duplicated because of the separate reporting requirements imposed in relation to other regulated activities in the form of the *MLAR*. Broadly, a *firm* that has the *permission* to carry on *mortgage lending* or *mortgage administration activities* will not be subject to our proposed data requirements for financial reporting in the *RMAR* (*RMAR*



sections A, B, C, D & E). For details, see *SUP 16.7*.

EEA Firms

9 In accordance with the relevant directives, ... The same applies to *incoming EEA firms* providing *cross border services* only, pursuant to the *ISD*.

...

NOTES FOR COMPLETION OF THE RMAR

...

Section C: Client money and assets

...

Note 3: firms should complete all applicable fields.

Section C: guide for completion of individual fields

...	
Client money credit total as at reporting date	This should be the total of credits on the <i>firm's client money</i> account(s) as at the current date of return. <u>These should be taken from the <i>firm's</i> ledgers.</u>
Client money debit total as at reporting date	This should be the total of any debits on the <i>firm's client money</i> account(s) as at the current date of return. <u>These should be taken from the <i>firm's</i> ledgers.</u>
Net client money balance as at reporting date	This should be the aggregate balance on the <i>firm's client money</i> account(s). ( <del>The reporting of this figure should not be taken to mean that firms are permitted to offset an overdrawn client bank account against one that is in credit.</del> )
...	

...

Section D: Regulatory Capital

'Higher of' requirements

...

(iii) other *personal investment firms*, and *firms* that are subject to *PRU*, but are also subject to *IPRU(INV)* or *CRED* (see below). These additional capital

requirements are not calculated as part of the RMAR.

...

Section D1: guide for completion of individual fields

...	
Eligible capital (mortgage and non-investment insurance)	
Incorporated firms	
Share capital	<del>As reported in section A</del> <u>Share capital in section A which is eligible for inclusion as regulatory capital</u>
Audited reserves	These are the audited accumulated profits retained by the <i>firm</i> ... Reserves also include gifts of capital, for example, from a <i>parent undertaking</i> . <del>If Any</del> <u>reserves that have not been audited this field should not be zero included.</u>
Interim net profits (audited)	Interim net profits should be audited by the <i>firm's</i> external auditor, net of tax or anticipated dividends and other appropriations <u>to be included as capital</u> . <del>Normally this will mean that they form a proportion of the firm's P&amp;L account in field BS24, but if no audit has been undertaken during the reporting period it should be a nil return.</del>
...	
<b>Less</b> interim net losses	<del>Interim net losses should be calculated in relation to the period following the date at which the capital resources are being calculated</del> <u>reported where they have not already been incorporated into audited reserves.</u> The figures do not have to be audited to be included.
Unincorporated firms	
...	
<b>Less</b> interim net losses	<del>Interim net losses should be calculated in relation to the period following the date as at which the capital resources are being calculated</del> <u>reported where they have not already been incorporated.</u> The figures do not have to be audited to be included.
...	..

...

Section E: guide for completion of individual fields

...	
Excess/deficit of readily realisable own funds	<del>This field will automatically calculate the excess or deficit, i.e. In this field, enter the result of the 'total of additional own funds required' less the 'total of readily realisable own funds'</del>

...

Section H: guide for completion of individual fields

...	
How often (if known) are the panel(s) reviewed?	<p>If the <i>firm</i> compiles its own panel(s), you should state the frequency with which the panel or list is reviewed and amended as appropriate, e.g. quarterly. <u>The frequency should be given in months eg if panels are reviewed quarterly, fill in "3".</u></p> <p>If separate panels are reviewed with differing frequencies, you should state the least frequent.</p> <p>It is acceptable to leave this field blank if, for example, the <i>firm</i> uses a panel or panels compiled by a product provider or packager firm.</p>

...

Section I: supplementary product sales data

...

Sub-heading: (i) non-investment insurance product information

In this section *firms* are asked for aggregate data on their ~~non-investment insurance~~ advising and arranging activities ~~(with~~ for non-investment insurance contracts with retail customers). The information required is an indication of the product types in which the *firm* has been active during the reporting period, and a further indication of how significant this activity is (i.e. whether it forms more than 40% by premium of all the *firm's* retail non-investment insurance activities).

...

Section I: guide for completion of individual fields

(i) non-investment insurance product information	
...	
Please indicate in column	You should state 'yes' in column B for each relevant

B where the firm's retail business in the product type formed more than 40% by premium of all of its non-investment insurance activities.	product based on an estimate of the percentage of business. If you think the product might account for more than 40% of business but are not sure, you should state 'yes'.
(ii) non-investment insurance chains	
Total non-investment insurance premium derived from retail customers	You should state here the total of premiums <u>paid payable</u> by <i>retail customers</i> during the reporting period in relation to non-investment insurance products.
...	
(iii) dealing as agent	
...	
Premium paid by retail customers during the reporting period where the firm dealt as agent	You should state here the total value of premiums <del>from policyholders</del> <u>payable</u> by <i>retail customers</i> during the reporting period <del>whether annual or one-off</del> —where the <i>firm</i> has dealt as agent of a product provider (i.e. with delegated authority). <del>For regular premium business, annualised figures should be used.</del>
...	

...

*SUP 16* Ann 19A R Mortgage Lending and Administration Return ('MLAR')

Amend the following pages of the MLAR making the underlined insertions and the struck through deletions. All amendments have been highlighted in grey to facilitate easy identification of the changes to the MLAR.

**D(1) LENDING : Business flows & rates**

(£000's)

D(1)

	<i>Balance at end of previous quarter</i>	<i>Advances made in quarter</i>	<i>Repayment of principal</i>	<i>Write offs in quarter</i>	<i>Other debits/ (credits) and transfers (net)</i>	<i>Balance at end of quarter (a)</i>	<i>Of which: Loans excluding overdrafts</i>	<i>Overdrafts</i>	<i>Overdrafts Aggregate of credit limits</i>
<b>D1 Loans: Advances/Repayments</b>									
Residential lending to individuals :									
D1.1 Regulated									
D1.2 Non regulated									
D1.3 Other secured loans									
D1.4 TOTAL Secured loans									

a) Column 6 = Col 1 + Col 2 - Col 3 - Col 4 + Col 5

**Transactions in quarter included in D1 [column 5]**

**Balance at end quarter on loan**

	<i>Loans acquired</i>	<i>Loans sold</i>	<i>Loans securitised</i>	<i>Other</i>	<i>Total (b)</i>	<i>assets subject to non-recourse funding</i>
<b>D2 Loans: Book movements</b>						
Residential lending to individuals :						
D2.1 Regulated						
D2.2 Non regulated						
D2.3 Other secured loans						
D2.4 TOTAL Secured loans						

(b) D1 column [5] = D2[Col 1 - Col 2 - Col 3 + Col 4]

**Balances at end of quarter**

**Interest rates at end of quarter (to 2 decimal places)**

	<i>TOTAL £000s</i>	<i>Of which at :</i>		<i>Of which at :</i>			<i>Weighted average nominal annual rate on</i>			
		<i>Fixed rates</i>	<i>Variable rates</i>	<i>less than 2% above BBR</i>	<i>2 &lt; 3% above BBR</i>	<i>3 &lt; 4% above BBR</i>	<i>4% or more above BBR</i>	<i>all balances</i>	<i>balances at fixed rates</i>	<i>balances at variable rates</i>
		<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>£000s</i>	<i>%</i>	<i>%</i>	<i>%</i>
<b>D3 Loans: Interest rates</b>										
Residential loans to individuals: Regulated										
D3.1 Total book										
D3.2 Advances in quarter										
Residential loans to individuals: Non Regulated										
D3.3 Total book										
D3.4 Advances in quarter										
Other secured loans:										
D3.5 Total book										
D3.6 Advances in quarter										
All secured loans:										
D3.7 Total book										
D3.8 Advances in quarter										

	<i>Commitments outstanding at end of previous quarter</i>	<i>Commitments made since end of previous quarter</i>	<i>Cancellations in quarter</i>	<i>Advances made in quarter (a)</i>	<i>Other debits/(credits) and transfers (net)</i>	<i>Commitments outstanding at end of quarter</i>
D4 Loans: <b>Commitments</b>						
Residential lending to individuals						
D4.1 Regulated						
a) House purchase	_____	_____	_____	_____	_____	_____
b) Remortgage	_____	_____	_____	_____	_____	_____
c) Other	_____	_____	_____	_____	_____	_____
d) TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.2 Non regulated						
a) House purchase	_____	_____	_____	_____	_____	_____
b) Remortgage	_____	_____	_____	_____	_____	_____
c) Other	_____	_____	_____	_____	_____	_____
d) TOTAL	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.3 Other secured loans	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>
D4.4 TOTAL Secured loans	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>	<input type="text"/>

a) Entries should agree with relevant items in Column 2 of D1.

		Regulated loans				Non regulated loans				All loans			
		Gross advances in quarter		Balances outstanding		Gross advances in quarter		Balances outstanding		Gross advances in quarter		Balances outstanding	
		Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount
E3	<b>By credit history</b>												
E3.1	Impaired credit history												
E3.2	Other												
E3.3	TOTAL												
E4	<b>By payment type</b>												
E4.1	Repayment (capital & interest)												
E4.2	Interest only												
E4.3	Combined												
E4.4	Other												
E4.5	TOTAL												
E5	<b>By drawing facility</b>												
E5.1	Loans with extra drawing facility :												
	a) Loans including unused facility												
	b) Unused facility												
	c) Net loans (a - b)												
E5.2	Loans with no extra drawing facility												
E5.3	TOTAL												
E6	<b>By purpose</b>												
E6.1	House Purchase:												
	Owner occupation												
	a) FTB's												
	b) Other												
E6.2	Buy to let												E6.2
E6.3	Further Advance												
	Remortgage:												
E6.4	Own borrowers												
E6.5	From other lenders												
E6.6	Lifetime Mortgage												E6.6
E6.7	Other												
E6.8	TOTAL												

**G0 Do you need to complete tables G and H ?**

If you have a mortgage lenders permission, and only administer your own on-balance sheet loan book, and do not have any off-balance sheet loans to administer, **then** please tick this box ( and do not complete the rest of this section).

**Otherwise**, please complete sections G1 and G2, and table H in your capacity as a loan administrator.

**G1 Mortgage contracts administered at end of quarter:**

**As PRINCIPAL administrator**

**As OTHER administrator**

**Residential loans to individuals**

**Residential loans to individuals**

*Regulated loans      Non regulated loans      All loans*

*Regulated loans      Non regulated loans      All loans*

G1.1 Number of loans administered for :

a) Firms with a mortgage lender's permission	_____	_____	_____
b) Other firms	_____	_____	_____
c) SPVs	_____	_____	_____
d) Total	<input type="text"/>	<input type="text"/>	<input type="text"/>


G1.2 Balance outstanding on loans administered for :

a) Firms with a mortgage lender's permission	_____	_____	_____
b) Other firms	_____	_____	_____
c) SPVs	_____	_____	_____
d) Total	<input type="text"/>	<input type="text"/>	<input type="text"/>




Residential loans to individuals administered for third parties

G2	Lenders for whom mortgage administration was being carried out at end of quarter	<u>Details of lender</u>		<u>Balances outstanding at end of quarter</u>			<u>Administrator Status</u>
		<i>FSA firm reference (if available)</i>	<i>Name of firm</i>	<i>Regulated loans £000's</i>	<i>Non regulated loans £000's</i>	<i>All loans £000's</i>	<i>Indicate whether acting as "Principal" or "Other"</i>
G2.1	Firms with a mortgage lenders permission : [ top 5 only ]	1	-----	-----	-----	-----	-----
		2	-----	-----	-----	-----	-----
		3	-----	-----	-----	-----	-----
		4	-----	-----	-----	-----	-----
		5	-----	-----	-----	-----	-----
G2.2	Other firms : [ top 5 only ]	1	-----	-----	-----	-----	-----
		2	-----	-----	-----	-----	-----
		3	-----	-----	-----	-----	-----
		4	-----	-----	-----	-----	-----
		5	-----	-----	-----	-----	-----
G2.3	SPVs: [ top 5 only ]	1	-----	-----	-----	-----	-----
		2	-----	-----	-----	-----	-----
		3	-----	-----	-----	-----	-----
		4	-----	-----	-----	-----	-----
		5	-----	-----	-----	-----	-----

...

SUP 16 Ann 19B G      NOTES FOR COMPLETION OF THE MORTGAGE LENDING  
AND ADMINISTRATION RETURN ('MLAR')

Contents

...

[Version ~~10 March~~ October 2004]

...

INTRODUCTION: GENERAL NOTES ON RETURN

...

2.      Overview of reporting requirements

...

Commencement and transitional provisions

The *MLAR* sections on **Arrears** (tables F and H) are not required to be submitted as part of a *firm's* first *MLAR* submission ~~(if that first submission is in respect of the *firm's* first financial quarter starting on or after 1 April 2005; but this concession does not apply however to firms that are subject to delayed implementation of *MLAR* in 2006)~~. They should however be included in all subsequent quarterly submissions. A *firm* may of course submit these sections from the outset, but is not obliged to do so.

...

4.      Regulated mortgage contracts and the wider mortgage market

...

(ii)    Residential loans to individuals

...

It is lending to individuals secured by mortgage on land and buildings where the lender has either a first or second (or subsequent) charge, where at least 40% of the land and buildings is used for residential purposes, and where the premises are for occupation by either the borrower (or dependant), or any other third party (e.g. it includes 'buy to let' lending to individuals).

Only loans where there is a one-to-one correspondence between the loan and a specific security should be included within 'residential loans to individuals'. Do not include here any residential loans to individuals that are part of a 'business loans' type package (involving multiple loans and multiple securities, where there is no one-to-one correspondence between a loan and a specific security), but report them under 'other

secured lending'.

**Regulated mortgage contracts** are therefore a subset of this market category.

Examples of **non-regulated mortgage contracts** which fall under the wider category of residential loans to individuals include: buy-to-let loans and other types of loan where the property is not for use by the borrower (or qualifying dependants); and residential loans to individuals where the lender does not have a first charge. In the case where a lender takes a first and a second charge over the same residential property (for different purposes) we consider that generally the loan secured by the first charge will be a regulated mortgage contract, but that the loan secured by the second charge will invariably not and should be reported as non-regulated.

It is important, therefore, to separate this category from all other forms of secured lending.

(iii) Other secured lending

This covers all other forms of lending secured on land and buildings in the United Kingdom. Primarily it covers secured lending to corporate bodies (including to housing associations), but it also includes lending to individuals which, although being secured on land and buildings, is not deemed to be residential (e.g. the residential element is less than 40%). A corporate body for this purpose is any entity other than an individual.

It also includes any residential lending to an individual that forms part of a 'business loan' type package. These arrangements between a lender and a borrower are usually offered by a lender's specialist business or corporate lending departments. They typically involve a number of loans secured against a range of securities including the borrower's residential property, business premises and the business itself. Such packages involve no specific one-to-one correspondence between a single loan and a single security, and instead the lender assesses loan cover against the basket of securities in the package. Given the business nature of this type of lending, it would therefore be misleading to try and classify some or all of the loan elements in such cases to any part of 'residential lending to individuals', and hence all such lending should be reported under 'other secured lending'. This is for MLAR reporting purposes only; the actual categorisation or treatment for MCOB purposes remains unchanged.

...

8. Loans made before 31 October 2004

(i) Classifying the 'back book'

Loans made before 31 Oct 2004 fall into the following categories:

- residential loans to individuals (see Introduction, section 4(ii)) which should be classified as non-regulated (eg as at A3.3, and D1.2 etc)
- other secured loans (see Introduction, section 4(iii)) and shown for example at A3.4, D1.3 etc
- other loans (see Guidance for A3.5)

The approach to classification for pre-31 Oct 2004 loans will, of necessity, need to be a pragmatic one. We do not for example envisage the need to look at individual

paper loan files. Rather, we expect that a firm will apply its knowledge of its various loan books, products & their characteristics, to come up with some realistic allocation rules. This will then enable the firm to apply some automatic process to its computerised loan records, and thereby classify individual loans into each of the relevant categories used in the MLAR. Such a process may not be perfect, and it may result in a few loans being wrongly allocated, but it will be sufficient for the purpose. In many cases, there will be further transactions in relation to this type of loan in the period immediately following 31 October 2004, and this event will provide an opportunity for the loan classification to be re-assessed, and if necessary, revised.

(ii) Specific treatment of residential loans to individuals

Any loans made before 31 October 2004, ...

... causes it to be formally treated as a regulated contract.

(iii) Further advances on loans made before 31 October 2004

We cannot be prescriptive about whether, after the onset of mortgage regulation, a further advance (or any other variation) to a pre-31 October 2004 mortgage will have the effect of creating a new *regulated mortgage contract*. Our perimeter guidance (at AUTH App 4.4.13G) considers the effect of variations to contracts entered into before the onset of mortgage regulation. Whether a variation amounts to creating a new contract will depend on each lender's individual mortgage documentation. This documentation will differ, possibly significantly, between firms. Each lender will need to review its existing documentation and take a view on the scope that this provides for making changes.

In practice this means that:

- if the lender can make a further advance without creating a new contract, then the further advance should be added to the original loan and the combined loan treated as a single loan for MLAR reporting. This combined loan should be reported as 'non-regulated';
- if making a further advance creates a new contract, (and this further advance is a *regulated mortgage contract*) then the correct reporting approach will be determined as follows:
  - (a) where the original loan was made before 31 October 2004, but would otherwise satisfy the specific requirements of a *regulated mortgage contract*, the original loan and further advance may be treated as one for MLAR reporting, being shown as "Regulated" under "Residential loans to individuals";
  - (b) where the original loan did not satisfy the defined conditions of a *regulated mortgage contract* at the time it was entered into, the old loan and further advance will be treated as two separate loans for most aspects of MLAR reporting, the former being 'unregulated' while the latter will be reported as 'regulated'. However, for the LTV & Income Multiple analysis, while the firm should only show the amount of the further advance in the relevant "cell", the "cell" should be determined

by using the total amount of the loan (old loan + further advance) when deciding which LTV band and which Income Multiple band are applicable;

- (c) where the lender decides to combine the original loan and the further advance to create a single new contract that is a *regulated mortgage contract*, this should be reported as 'regulated'.

...

## SECTION D1: LENDING – BUSINESS FLOWS AND RATES

...

### D1 Loans: Advances/Repayments – Transactions (columns)

**Advances made in quarter** should include:

...

but should exclude:

...

- (h) sundry debits, i.e. any items not approved and not included in commitments, e.g. insurance debits, fines, insurance guarantees, valuation fees, arrangement fees etc. (unless formally treated as part of loan, that is where such amounts are repaid over the period of the loan);

- (i) any movements on overdrafts.

**Repayment of principal** should include:

...

but should exclude:

...

- (g) *investment* receipts temporarily posted to mortgage accounts;:

- (h) any movement in overdrafts.

...

**Other debits/(credits) and transfers (net) include:**

- (i) ... or change in status of loan from/to regulated/non-regulated etc);:

- (j) all movements on overdrafts (that is, net change in overdraft balances), other than write-offs.

NB Balances on loan books acquired/sold/securitised should be as at the date of the relevant event.

### **Overdraft analysis (final 3 columns of D1):**

The term “overdraft” here and in other columns of D1, is used to cover two types of revolving credit facilities: overdrafts and credit cards.

The balance at end of quarter in column 6 is further analysed into loan balances excluding overdrafts and, separately, balances on overdrafts.

The final column in D1 represents the sum total, across all overdraft accounts included in the penultimate column, of the individual credit limits on each such overdraft.

...

D3 Loans: Interest rates

Basis

Interest rates in this table are **nominal annual rates** charged to the *customer* on loan accounts excluding overdrafts (as defined in D1). They should ignore ...

This provides an analysis of weighted average interest rates for the loan assets reported ~~in the final~~ under 'Loans excluding overdrafts' in column 7 of D1 above. 'Interest rates at end of quarter' (columns 4, 5, and 6 of section D3) ...

...

D4 Loans: ~~e~~Commitments (columns)

Commitments made since end of previous quarter should include:

- (a) the aggregate of formally agreed advances (whether or not the mortgage offer has been accepted by the prospective borrower), including amounts recommended for retention, all instalment elements, and further advances;

but should exclude:

...

- (f) sundry debits, e.g. insurance debits, fines, insurance guarantees, valuation fees, arrangement fees etc (unless formally treated as part of the loan, that is where such amounts are repaid over the period of the loan). ~~premiums (unless additional to the loan), insurance of contents etc.~~

...

### **Advances made in quarter**

This refers to the same amount as covered under ‘advances in quarter’ in section D1 above.

### **Other debits/(credits) and transfers (net)**

This is unlikely to be needed on a routine basis. It is intended to cover less frequent events such as loan commitments acquired on merger with another firm or acquisition

of a loan book; or transferred on sale of a package of loans; or where 'commitments outstanding' need adjusting for reasons not attributable to other columns.

## SECTION E: RESIDENTIAL LOANS TO INDIVIDUALS - Income Multiples & LTV

...

### E3-6 Balances outstanding

Covers balances at end of the quarter. Relevant sub-totals should agree with corresponding balances shown ~~in the final columns~~ under 'Loans excluding overdrafts' in column 7 of D1.

...

### E3 Credit History

This seeks to categorise lending in terms of a borrower's previous credit history, as measured at the point when the new advance is made. For these purposes, it is only necessary to establish a borrower's credit history at a single point in time, i.e. at the time of making the loan. In practice this will usually be done at the 'offer' stage of making a loan. It is not intended that credit history should be reassessed after the loan has been made. However, if a further advance is made, then it will be necessary to re-assess.

In particular ...

(i) ...

(ii) ...

However, if there is subsequently a further advance on the loan (and which will be reported under 'Gross advances' in E3), this is an occasion to re-assess the borrower's credit history. At that stage, the total amount of the loan (including further advance) should be classified under 'Balances outstanding' on the basis of the credit history as determined at the time of making the further advance. This means that the further advance and total loan amount will be reported on a consistent basis.

### E3.1 Impaired credit history

...

**NB** In (i) to (v), *firms* should ignore whether the borrower has subsequently paid off arrears, or has satisfied/discharged a CCJ or IVA or bankruptcy.

In the case of loans involving **two or more borrowers**, the impaired credit test is whether any one of the borrowers individually meets any of the five listed impaired credit conditions.

...

E5 By drawing facility

These are loans which include ..., **but not** those arising only in relation to previous overpayments).

The drawing facility category is also meant to indicate a facility that is only exercisable by the borrower (e.g. via a cheque book, on line transaction or on demand). It would therefore not apply to situations where a loan is merely subject to retentions or stage payments, since the borrower does not have a draw-down option that he can exercise.

...

E6.1/2 House purchase

.... where the tenure of the main borrower immediately before this advance was not owner-occupier) and those to other buyers.

E6.2 Buy to let (BTL)

Such loans typically involve the borrower purchasing a residential property with the intention of letting it out on a rental basis.

The majority of BTL loans will be those used by the borrower to acquire a property with the intention of letting it on a commercial basis to unrelated third parties. That is to persons, who in relation to the borrower, are not 'related persons' (where 'related persons' are those set out in subsections (A), (B) and (C) of section 4 (iv) of the Introduction). These BTL loans are not regulated mortgage contracts and hence should be shown in columns 5 to 8 of E6.2 under 'Non regulated loans'.

However, where a BTL loan is used by the borrower to acquire a residential property that will be occupied by a related person, such a loan will normally be a regulated mortgage contract (providing it satisfies the other requirements of a regulated mortgage contract) and should therefore be shown in columns 1 to 4 of E6.2 under 'Regulated loans'. An example of such a loan is where a parent buys a house or flat for use by a student son or daughter, with a plan to take in other students on a rental basis.

Further advances and remortgages on any BTL loans should be included within E6.2.

E6.3 Further advance

...

The underlying purpose of the further advance ...; or as a 'drawdown' on a flexible mortgage.

However, further advances on existing buy to let loans, and on lifetime mortgage loans should instead be reported against E6.2 and E6.6 respectively.



## E6.4/5 Re-mortgage

Loans where the borrower is not moving house but ... even if it is larger than the existing loan.

Re-mortgages from another lender are well understood, and need no further comment.

But a 're-mortgage' by one of a firm's existing borrowers (i.e. 'own borrower' in E6.4) will not always be transacted in exactly the same way by different lenders. The following comments are designed to provide some illustrative examples, and indicate how the actual transaction between lender and borrower should be reported:

- **Example 1:** borrower changes from variable rate to fixed rate, with loan amount unchanged, at say £100k. Some lenders' systems formally treat this as a redemption and a new loan advance which is reportable under "advances" in D1 (in which case report as "re-mortgage" under this analysis of advances in E6), but other lenders treat it as an interest variation and not as a new advance (so not included in advances in D1 or E).
- **Example 2:** borrower changes from variable rate to fixed rate and takes out additional loan at the same time, say extra £25k on top of existing £100k. Some lenders will treat as a redemption of £100k and a new advance of £125k (in which case the £125k is a re-mortgage), but others may treat as two loans (with first loan regarded as just subject to an interest rate variation, and the extra loan as a "further advance").
- It is recognised that practices vary among lenders when it comes to further advances or re-mortgages. What is important is that the actual transaction between the lender and the borrower is reflected in the MLAR.
- Thus if a firm genuinely treats the advance of new money as a further advance (perhaps setting up a second sub account), then that should be reported as such (e.g. at E6.3)
- However if the old loan is formally replaced with a new loan (at the same or increased size) and this is reported in "advances" in D1, then the new loan should similarly be reported in E, and in E6.4 shown as "re-mortgage".

**NB** However, re-mortgages on existing buy to let loans, and on *lifetime mortgage* loans, should instead be reported against E6.2 and E6.6 respectively.

E6.6 Lifetime mortgages

**(i) Regulated loans: Lifetime mortgages (columns 1 to 4)**

This is a specific type of *regulated mortgage contract*, ...

(c) ...

- (vi) the *mortgage lender* exercises its legal right to take possession of the mortgaged land under the terms of the contract.

**(ii) Non-regulated loans: 'Lifetime mortgage' (columns 5 to 8)**

Loans to be included under these columns include:

- loans having broadly similar characteristics to those set out in (i)(a), (b) and (c) above, but which were advanced before 31 October 2004. Such loans will usually have been known as 'equity release loans';
- loans made after 31 October 2004, which whilst not satisfying the full criteria needed to be classed as a *regulated mortgage contract* (e.g. since a second but not a first charge is taken), nonetheless match the characteristics set out in (i)(a), (b) and (c) above.

**(iii) Further advances and re-mortgages on any of the loans described in (i) and (ii) above, should be included within E6.6**

...

SECTION F: LENDING - ARREARS ANALYSIS

Introduction

The guidance notes in this section serve two purposes: they provide guidance for

- (i) items **F1 to F5** shown in MLAR table F.

For these sections, the analysis of lending refers to on-balance sheet loan assets only, but excluding overdrafts (ie as included ~~in the final column~~ under 'Loans excluding overdrafts' in column 7 of section D1 of table D)

The responsibility for completing table F lies with the authorised lender, irrespective of whether the lender administers the loans itself or out-sources the administration elsewhere. The information should therefore appear as part of the lender's MLAR.

- (ii) items **H1 to H5** shown in MLAR table H.

For these sections, which cover reporting of arrears by *firms* with a *mortgage administrator's* activity, the analysis should include arrears in respect of the types of residential loans to individuals set out in the guidance notes for table G, but only where the firm is acting as 'principal administrator'. For *guidance* on items H1 to H5 see ...

...

- 6.2 The amount to be entered on the return is a percentage to 2 decimal places. Given the limitation described in 6.1 (ii), it cannot exceed 100%.

...

## SECTION G: MORTGAGE ADMINISTRATION – BUSINESS PROFILE

### Introduction

...

You should also note, however, ... then you should not complete this section of the *MLAR*.

### **‘Principal’ and ‘Other’ Administrators**

Because of the extent of specialisation and separation of activities in the provision of mortgage lending and administration services, we need to identify whether a firm that is authorised as a *mortgage administrator* is acting for MLAR purposes as a ‘principal administrator’ or as an ‘other administrator’:

- **Principal administrator:** this is where your firm is authorised to undertake a *mortgage administrator’s* activity, and is exercising that activity on behalf of either a lender or other firm that is not itself authorised to undertake a *mortgage administrator’s* activity;
- **Other administrator:** this is where your firm (although authorised to undertake a *mortgage administrator’s* activity) is undertaking loan administration for either a lender or other firm which itself is also authorised to undertake a *mortgage administrator’s* activity. In this situation, your firm is not regarded as the ‘principal administrator’, and you are merely acting on behalf of an authorised *mortgage administrator*.

- G1 Mortgage contracts administered at end quarter

#### **Where your firm is acting as Principal administrator (columns 1-3)**

Collects data on mortgage contracts administered as at the end of the quarter, ...

- G1.2 Outstanding balance on loans

...

The total (all loans) is the sum of *regulated mortgage contracts* and non-regulated loans.

#### **Where your firm is acting as Other administrator (columns 4-6)**

Record under these columns all of the mortgage contracts administered at the end of the quarter where you are not acting as a principal administrator.

...

G2 Lenders for whom mortgage administration was being carried out at quarter end

Collects data only on the top five lenders for each category by value ..., over and above the top five listed in each category.)

The analysis required in G2 covers all mortgage administration activity undertaken by your firm, irrespective of whether your firm is acting as a 'principal' or 'other' administrator. The final column of the analysis, however, asks you to indicate your status for each firm listed, namely whether acting as 'Principal' or as 'Other' administrator.

...

#### SECTION H: MORTGAGE ADMINISTRATION – Arrears Analysis

...

H1- Guidance on arrears items

H5 The *guidance* for these items is provided in section F of these guidance notes, where items H1 to H5 correspond to items F1 to F5.

The arrears analysis is of loan balances excluding overdrafts, as is used in section F.

...

SUP 16 Ann 20G

Products covered by the reporting requirements in SUP 16.11

This is the *guidance* referred to in SUP 16.11.6G.

~~SUP 16.11.3R requires certain firms to report product sales data. For reporting purposes, a reportable sale applies where the~~ A reportable sale is when a new contract has been made and the premium has been paid. A reportable sale does not include a policy renewal, a policy top-up, or any alteration to an existing policy.

Part 1 Products

...

Table 1 – RETAIL INVESTMENTS

Relevant products include:

<u>Unit in a Regulated unit trust scheme/OEIC</u>
---

...

Reporting fields

...

(c) Mortgages

...

Data reporting field	Illustrative code (where applicable)	Notes
...		
Employment status of main borrower	F = full time E = employed S = self employed R = retired O = other	Applies to main borrower only  Only 1 code can be entered
...		

...

3. OPTIONAL REPORTING FIELDS

The following data items are not currently mandatory reporting fields. ~~Firms are not obliged to report these items within the data report if the data is not readily available.~~

However, without this information, we will not be able to identify individual incorrect transactions. A firm would need to trawl through all submitted transactions until they could match the original transaction details and thus, correct and resubmit the information to us. These data items are essential for the smooth running of the regulatory reporting process both from the FSA's and the firm's perspective and because we understand that these data items are generally available to firms it is our intention to make these data items mandatory in due course. In the interim, we would encourage firms to build these extra items into their PSD reporting systems.

Data reporting field	Illustrative code (where applicable)	Notes
...		
<u>Product sale reference</u>	<u>free text field</u>	<u>This can be any unique number such as the policy/account number but must be a number that the a firm can use to trace the original transaction information.</u>
<u>Date sale of product</u>	<u>DD/MM/YYYY</u>	<u>Enter date</u>

concluded		
-----------	--	--

...

*SUP* Schedule 2 – Notification Requirements

Table 2

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
SUP 16.10.4 R	<u>Verification</u> <del>Confirmation</del> of <i>standing data</i> items	<del>Confirmation</del> of accuracy of <del><i>standing data</i></del> or correction of inaccuracies <u>in <i>standing data</i></u>	<i>Accounting reference date</i>	30 <i>business days</i> after <i>accounting reference date</i>
...				

## Annex D

### Amendments to the Dispute Resolution: Complaints sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

DISP Table: Transitional Provisions table

1

(1)	(2)	(3)	(4)				(5)	(6)
	Material to which the transitional provision applies		Transitional provision				Transitional provision: dates in force	Handbook provision: coming into force
...								
12	<i>DISP</i> 1.5.4R	<b>R</b>	If transitional provision 11R applies, the <i>firm's</i> first and second report must be provided as follows:					
			Accounting reference date	Reporting period starts	Reporting period ends	Report to be provided		
			Between 1 January 2005 and 31 March 2005	1 <sup>st</sup> report: 1 April 2005	<i>6 months</i> after <u>the</u> <i>accounting reference date</i> within 2005	30 <i>business days</i> after period end		
				2 <sup>nd</sup> report: <u>the day</u> after the <u>end of the</u> <u>1<sup>st</sup> reporting period</u> <i>6 months</i> after the <i>business day</i> following the	<u>the</u> <i>accounting reference date</i> within 2006			

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
				<i>accounting reference date within 2005</i>				
			Between 1 April 2005 and 30 June 2005	1 <sup>st</sup> report: 1 April 2005	<i>6 months after the accounting reference date within 2005</i>	30 business days after period end		
				2 <sup>nd</sup> report: <i>the day after the end of the 1<sup>st</sup> reporting period the business day following the accounting reference date within 2005</i>	<i>6 months after the accounting reference date within 2006</i>			
			Between 1 July 2005 and 30 September 2005	1 <sup>st</sup> report: 1 April 2005	<i>the accounting reference date within 2005</i>	30 business days after period end		
				2 <sup>nd</sup> report: <i>the day business day following</i>	<i>6 months after the business day accounting</i>			



(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision				(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
				the accounting reference date within 2005	reference date within 2005			
			Between 1 October 2005 and 31 December 2005	1 <sup>st</sup> report: 1 April 2005	<del>6 months preceding</del> the accounting reference date within 2005	30 business days after period end		
				2 <sup>nd</sup> report: the day <i>business day</i> following <del>6 months preceding</del> the accounting reference date within 2005	<u>6 months after the business day</u> accounting reference date within 2005			
...								

**COMPLAINTS AND COMPENSATION SOURCEBOOKS (MORTGAGE AND  
GENERAL INSURANCE INTERMEDIARIES FUNDING OF THE OMBUDSMAN  
AND COMPENSATION SCHEMES) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 213 (The compensation scheme);
  - (4) section 214 (General);
  - (5) section 223 (Management expenses); and
  - (6) section 234 (Industry funding).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) The amendments in Annexes A, B and C come into force on 31 October 2004;
  - (2) The amendments in Annex D come into force on 14 January 2005.

**Amendments to the Dispute resolution: Complaints sourcebook**

- D. The Dispute resolution: Complaints sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Compensation sourcebook**

- E. The Compensation sourcebook is amended in accordance with Annexes B and D to this instrument.

**Amendments to the Glossary**

- F. The Glossary is amended in accordance with Annex C to this instrument.

**Citation**

- G. This instrument may be cited as the Complaints and Compensation Sourcebooks (Mortgage and General Insurance Intermediaries Funding of the Ombudsman and Compensation Schemes) Instrument 2004.

By order of the Board  
20 October 2004

## Annex A

### Amendments to the Dispute Resolution: Complaints sourcebook

In this Annex, underlining indicates new text.

DISP Table Transitional Provisions table

1

(1)	(2)	(3)	(4)	(5)	(6)
	Material provision to which transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision coming into force
	...				
<u>15</u>	<u>DISP 5.5.1R</u>	<u>R</u>	A <i>firm</i> which falls within <i>industry block 16</i> or <i>17</i> needs to provide a statement to the <i>FSA</i> by the end of <u>February 2005</u> only if it is providing the <i>FSA</i> with a statement of the total amount of <u>relevant business</u> .	<u>31 October 2004</u> to <u>28 February 2005</u> for <i>firms</i> falling in <i>industry block 16</i>  <u>14 January 2005</u> to <u>28 February 2005</u> for <i>firms</i> falling in <i>industry block 17</i>	<u>31 October 2004</u>
<u>16</u>	<u>DISP 5.5.1R</u>	<u>G</u>	In respect of the year <u>2005/06</u> , the <i>FSA</i> will already have a statement of the total amount of the <i>firm's</i> annual income as part of the <i>firm's</i> application for a <i>Part IV permission</i> or to vary a <i>Part IV permission</i> . There is thus no need for a <i>firm</i> to repeat this information if it decides not to report annual income for <u>relevant business</u> in accordance with <u>DISP TP 15R</u> .	<u>31 October 2004</u> to <u>28 February 2005</u> for <i>firms</i> falling in <i>industry block 16</i>  <u>14 January 2005</u> to <u>28 February 2005</u> for <i>firms</i> falling in <i>industry block 17</i>	<u>31 October 2004</u>

...

5.4.10 R For the purpose of *DISP 5.4*, references to *relevant business* for a firm which falls in *industry block 16 or 17* and which so elects under part 2 of *DISP 5 Ann 1R*, are references to the *firm's* total amount of annual income reported in accordance with Part 2 of *SUP 20 Ann 1R*.

...

5.5.1 R (4) For the purpose of *DISP 5.5.1R*, references to *relevant business* for a firm which falls in *industry block 16 or 17* and which so elects under part 2 of *DISP 5 Ann 1R*, are references to the *firm's* total amount of annual income reported in accordance with Part 2 of *SUP 20 Ann 1R*.

DISP 5 Ann 1R

...

2 Table: ~~Table:~~ fee tariffs for industry blocks

Industry block	Tariff base	General levy payable by firm
...		
<u>16 – Mortgage lenders, advisers and arrangers (excluding firms in blocks 13, 14 &amp; 15)</u>	<u>Either annual income reported in accordance with Part 2 of SUP 20 Ann 1R from relevant business or the firm's total annual income reported in accordance with Part 2 of SUP 20 Ann 1R</u>	<u>No levy is payable for 2004/2005</u>
<u>17 – General insurance mediation (excluding firms in blocks 13,14 &amp; 15)</u>	<u>Either annual income reported in accordance with Part 2 of SUP 20 Ann 1R from relevant business or the firm's total annual income reported in accordance with Part 2 of SUP 20 Ann 1R</u>	<u>No levy is payable for 2004/2005</u>

## Annex B

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text.

COMP Table: Transitional Provisions Table

1

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional Provision	(5) Transitional provision: dates in force	(6) Handbook Provisions coming into force
...					
<u>10</u>	<u>COMP 5.7.1R, 13.4.7BR and 13.6.9BR</u>	<u>R</u>	<u>Rules not in effect.</u>	<u>31 October 2004 to 13 January 2005</u>	<u>31 October 2004</u>
<u>11</u>	<u>COMP 13.4.1R, 13.4.19R, 13.5.6R, 13.5.8R, 13.6.1R and 13.6.6R</u>	<u>R</u>	<u>With regard to <i>contribution group A.18 – Mortgage lenders, advisers and arrangers, the management expenses levy and compensation costs levy</i> for 2005/2006 may also take account of expenditure in the period 31 October 2004 to 31 March 2005.</u>	<u>31 October 2004 to 31 March 2006</u>	<u>31 October 2004</u>
<u>12</u>	<u>COMP 13.4.1R, 13.4.19R, 13.5.6R, 13.5.8R, 13.6.1R and 13.6.6R</u>	<u>R</u>	<u>With regard to <i>contribution group A.19 – General insurance mediation, the management expenses levy and compensation costs levy</i> for 2005/2006 may also take account of expenditure in the period 14 January 2005 to 31 March 2005.</u>	<u>14 January 2005 to 31 March 2006</u>	<u>31 October 2004</u>

<u>13</u>	<u>COMP 13.6.7 (4) 13.6.9A R and 13.6.11R(2)</u>	<u>R</u>	For the period 31 October 2004 to 31 March 2006 the tariff base will be the annual income (relating to the relevant <i>contribution group</i> ) reported in accordance with note 3 to <i>AUTH 4 Ann 2</i> or, if the <i>firm</i> prefers, that amount of its annual income which is attributable to business conducted with <i>eligible claimants</i> but only if the <i>firm</i> notifies <i>FSCS</i> of the amount by 28 February 2005.	<u>31 October 2004 to 31 March 2006</u>	<u>31 October 2004</u>
<u>14</u>	<u>COMP 13.6.7(5), 13.6.9B R and 13.6.11R(2)</u>		For the period 14 January 2005 to 31 March 2006 the tariff base will be the annual income (relating to the relevant <i>contribution group</i> ) reported in accordance with note 3 to <i>AUTH 4 Ann 2</i> or, if the <i>firm</i> prefers, that amount of its annual income which is attributable to business conducted with <i>eligible claimants</i> but only if the <i>firm</i> notifies <i>FSCS</i> of the amount by 28 February 2005.	<u>14 January 2005 to 31 March 2006</u>	<u>31 October 2004</u>

...

5.7.1 R *Protected non-investment insurance mediation* is an *insurance mediation activity* where the *investment* concerned is a *non-investment insurance contract* which is not a *reinsurance contract*, provided that the condition in *COMP 5.7.2R* is satisfied.

...

13.4.7A R The *FSCS* must not require a *participant firm* in the mortgage advice and arranging *sub-scheme* to pay a share of a *compensation costs levy* allocated to that *sub-scheme* in any financial year of the *compensation scheme*, to the extent that:

- (1) the share in question; plus
- (2) all previous amounts paid by the *firm* as its share of *compensation costs levies* allocated to that *sub-scheme* in that financial year;

amounts to more than 0.8% of the *participant firm's annual eligible income*.

13.4.7B R The *FSCS* must not require a *participant firm* in the general insurance mediation *sub-scheme* to pay a share of a *compensation costs levy* allocated to that *sub-scheme* in any financial year of the *compensation scheme*, to the extent that:

- (1) the share in question; plus
- (2) all previous amounts paid by the *firm* as its share of *compensation costs levies* allocated to that *sub-scheme* in that

financial year;  
amounts to more than 0.8% of the participant firm's annual eligible income.

...  
 13.6.7 R ...

- (3) ... ;  
 (4) the mortgage advice and arranging sub-scheme, the FSCS must use the contribution group and tariff base set out in the table in COMP 13.6.9AR;  
 (5) the general insurance mediation sub-scheme, the FSCS must use the contribution group and tariff base set out in the table in COMP 13.6.9BR.

...  
13.6.9AR Table: the contribution groups and tariff bases for the mortgage advisers and arrangers (see COMP 13.6.7R(4))

<u>SUB-SCHEME</u>	<u>CONTRIBUTION GROUP (REFERENCE S TO A1, A2 ETC ARE TO THE FSA FEE BLOCKS)</u>	<u>LEGAL BASIS FOR ACTIVITY (references to articles are to articles of the Regulated Activities Order)</u>	<u>TARIFF BASE</u>
<u>Mortgage advice and arranging</u>	<u>A.18 – Mortgage lenders, advisers and arrangers</u>	<u>Any of the following: (a) arranging (bringing about) regulated mortgage contracts; (b) making arrangements with a view to regulated mortgage contracts; (c) advising on regulated mortgage contracts; (d) agreeing to carry on a regulated activity which is within any of the above; and (e) the activities of a mortgage lender which would be arranging but for article 28A of the Regulated Activities Order (Arranging contracts to which the arranger is a party).</u>	<u>annual eligible income</u>

13.6.9B R Table: the contribution groups and tariff bases for the general insurance intermediaries (see COMP 13.6.7R(5))

<u>SUB-SCHEME</u>	<u>CONTRIBUTION GROUP (REFERENCES TO A1, A2 ETC ARE TO THE FSA FEE BLOCKS)</u>	<u>LEGAL BASIS FOR ACTIVITY (references to articles are to articles of the <i>Regulated Activities Order</i>)</u>	<u>TARIFF BASE</u>
<u>General insurance mediation</u>	<u>A.19 – General insurance mediation</u>	<u>Any of the following in relation to a <i>non-investment insurance contract</i>: (a) <i>dealing in investments as agent</i>; (b) <i>arranging (bringing about) deals in investments</i>; (c) <i>making arrangements with a view to transactions in investments</i>; (d) <i>assisting in the administration and performance of a contract of insurance</i>; (e) <i>advising on investments</i>; and (f) <i>agreeing to carry on a regulated activity which is within any of the above</i>.</u>	<u><i>annual eligible income</i></u>



## Annex C

### Amendment to the Glossary of definitions

In this Annex underlining indicates new text and strikethrough indicates deleted text.

Insert the following new definition in the appropriate alphabetical position:

*annual eligible income* (in *COMP*) the annual income (as described in Part 2 of *SUP* 20 Ann 1R) for the *firm's* last financial year preceding the date for submission of the information under COMP16.6.11R attributable to the relevant *contribution group*; or if the *firm* prefers, that amount of that annual income attributable to business conducted with *eligible claimants*, but only if the *firm* notifies *FSCS* of the amount in accordance with *FSCS* reporting requirements.

Amend the following definition as shown:

*sub-scheme* one of the ~~three~~ sub-schemes to which the *FSCS* allocates liabilities for *compensation costs* , as described in *COMP* 13.6.7R.

## Annex D

### Amendments to the Compensation sourcebook

In this Annex new sections of text are being inserted, so the place where the change will be made is indicated and the text is not struck through or underlined.

Insert the following new rule after *COMP* 3.2.3 R

- 3.2.4 R The *FSCS* may also pay compensation to a *firm*, who makes a claim in connection with *protected non-investment insurance mediation* on behalf of its *customers*, if the *FSCS* is satisfied that:
- (1) each *customer* has borne a *shortfall* in *client money* held by the *firm* caused by a *secondary pooling event* arising out of the *failure* of a broker or *settlement agent* which is a *relevant person in default*;
  - (2) the *customers* in respect of which compensation is to be paid satisfy the conditions set out in *COMP* 3.2.2R(1);
  - (3) the *customers* do not have a *claim* against the *relevant person* directly, nor a claim against the *firm*, in respect of the same loss;
  - (4) the *customers* would have been paid compensation by *FSCS* if the *customers* had a *claim* for their share of the *shortfall*, and if the *firm* were the *relevant person*; and
  - (5) the *firm* has agreed, on such terms as the *FSCS* thinks fit, to pay, or credit the accounts of, without deduction, each relevant *customer* in (1), that part of the compensation equal to the *customer's* financial loss, subject to the limits in *COMP* 10.2.

...

Insert the following new rule after *COMP* 6.3.7G:

- 6.3.8 R Claims arising under *COMP* 3.2.4R
- 6.3.8 R For the purposes of *COMP* 6.3 a claim made by a *firm* under *COMP* 3.2.4R is to be treated as if it were a *protected claim* against the *relevant person*.

...

Insert the following new rule after *COMP* 7.2.6G

- 7.2.7 R (1) For the purposes of compensation paid under *COMP* 3.2.4R, *FSCS* may require any *firm* (including, but not limited to, the claimant *firm*) to assign to *FSCS* any rights the *firm* may have to claim against the *relevant person* in relation to the amount of the *shortfall* in *client money* arising out of the *failure* of the *relevant person*.
- (2) A *firm* required by *FSCS* to assign its rights in (1), must assign those rights as requested, unless it has a reasonable

excuse for not doing so.

...

Insert the following new rule after *COMP* 10.2.8R

Claims arising under *COMP* 3.2.4R

- 10.2.9 R If a *firm* has a claim under *COMP* 3.2.4R, the *FSCS* must treat the share of the *shortfall* of each *customer* as if it were a *protected claim* for the purposes of calculating the limits of compensation payable, within *COMP* 10.2, in relation to that *customer*.

...

Insert the following new rule after *COMP* 12.6.11R

Claims arising under *COMP* 3.2.4R

- 12.6.12 R If a *firm* has a claim under *COMP* 3.2.4R, the *FSCS* must treat each *customer* of the *firm* as having the claim for the purposes of calculating compensation within *COMP* 12.

**COMPENSATION SOURCEBOOK (AMENDMENT NO 4) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 213 (The compensation scheme);
  - (4) section 214 (General); and
  - (5) section 223 (Management expenses).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C This instrument comes into force immediately.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Compensation Sourcebook (Amendment No 4) Instrument 2004.

By order of the Board  
20 October 2004

## Annex

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

#### COMP 13 Ann 1R: Management Expenses Levy Limit

1 This table belongs to *COMP* 13.5.2R

**2 Table**

Period	Limit on total of all management expenses levies attributable to that period (£)
1 December 2001 to 31 March 2002	£4,209,000
1 April 2002 to 31 March 2003	£13,228,000
1 April 2003 to 31 March 2004	£13,319,000
1 April 2004 to 31 March 2005	<del>£12,548,000</del> <u>£17,590,000</u>

**CREDIT UNIONS SOURCEBOOK (AMENDMENT NO 6) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 1 January 2005.

**Amendments to the Credit Unions sourcebook**

- C. The Credit Unions sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Credit Unions Sourcebook (Amendment No 6) Instrument 2004.

By order of the Board  
20 October 2004

## Annex

### Amendments to the Credit Unions sourcebook

In this annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section of text is being inserted, the place where it goes is indicated and it is not underlined.

2.7.1 G ... Where a word or phrase which is shown in italics in one part of the text appears without italics in another part, it is meant to be given, where un-italicised, its ordinary natural meaning. See CRED 13 Annex 1A G 1(2) on the meaning of "credit union".

...

13.2.1 G Registration and becoming *authorised* as a *credit union* are two distinct statutory processes. The Credit Unions Act 1979 sets out the statutory requirements for registration and the *Act* sets out the statutory requirements relating to *authorisation*. Section 1 of the Credit Unions Act 1979 as amended (see CRED 13 Ann 1B G) provides that a credit union may not be registered unless it has applied to the FSA for a *Part IV permission to accept deposits*...

...

13.4.1 G (1) For registration, applicants must demonstrate to the satisfaction of the *FSA* that the statutory conditions set out in section 1 of the Credit Unions Act 1979 will be fulfilled. *CRED 13 Ann 1G* contains a table listing these statutory conditions.

(a) One of the conditions is that the objects of the credit union are those, and only those, of a credit union. The objects are set out in full in ~~the table~~ CRED 13 Ann 1B G. ...

(b) Another condition is that admission to membership of the credit union is restricted to persons who fulfil an appropriate membership qualification ("AMQ") and that in consequence a common bond exists among the members (see CRED 13 Ann 1A G – CRED 13 Ann 1C G).

...

Requirements of Registration

- 1 Table The requirements of registration under the Industrial and Provident Societies Act 1965, as set out in the Credit Unions Act 1979 and referred to in *CRED* 13.4.1G.

REQUIREMENT	SECTION OF THE RELEVANT ACTS
That the objects of the society are those, and only those of a credit union	Credit Unions Act 1979, s.1(2)(a)
<del>The objects of a credit union are:</del>	
<del>See <u>CRED 13 Ann 1B G Section 1 of the Credit Unions Act 1979 (as amended).</u></del>	Credit Unions Act 1979, s.1(3)
<del>the promotion of thrift among the members of the society by the accumulation of their savings</del>	
<del>the promotion of thrift among the members of the society by the accumulation of their savings</del>	Credit Unions Act 1979, s.1(3)
<del>the creation of sources of credit for the benefit of the members of the society at a fair and reasonable rate of interest</del>	Credit Unions Act 1979, s.1(3)
<del>the use and control of the members' savings for their mutual benefit</del>	Credit Unions Act 1979, s.1(3)
<del>the training and education of the members in the wise use of money and in the management of their financial affairs</del>	Credit Unions Act 1979, s.1(3)
That admission to membership of the society is restricted to individuals all of whom fulfil a specific qualification which is appropriate to a credit union (and that in consequence a "common bond" exists between members).	Credit Unions Act 1979, s.1(2)(b)
<del>The appropriate membership qualifications ("AMQs") for a credit union are:</del>	
<del>See <u>CRED 13 Ann 1B G Section 1 of the Credit Unions Act 1979 (as amended) - CRED 13 Ann 1C G Qualifications approved by the FSA (and the Registry of Friendly Societies).</u></del>	Credit Unions Act 1979, s.1(4)(a)
<del>following a particular occupation</del>	
<del>residing in a particular locality</del>	Credit Unions Act 1979, s.1(4)(b)
<del>being employed in a particular locality</del>	Credit Unions Act 1979, s.1(4)(c)
<del>being employed by a particular employer</del>	Credit Unions Act 1979, s.1(4)(d)
<del>being a member of a bona fide organisation or being otherwise associated with other members of the society for a purpose other than that of forming a society to be</del>	Credit Unions Act 1979, s.1(4)(e)



<p>registered as a credit union residing in or being employed in a particular locality</p>	<p>Credit Unions Act 1979, s.1(4)(f)</p>
<p>and such other qualifications as are for the time being approved by the FSA</p>	<p>Credit Unions Act 1979, s.1(4)</p>
<p>The following qualifications (in addition to those set out in section 1(4) of the Credit Unions Act 1979) have been approved by the FSA or its predecessor, the Registry of Friendly Societies:</p>	
<p>being currently in receipt of a continuing and regular contractual payment arising from employment by a particular employer</p>	<p>Credit Unions Act 1979, s.1(4)</p>
<p>being currently in receipt of a continuing and regular contractual payment arising from employment by particular employers in a particular area</p>	<p>Credit Unions Act 1979, s.1(4)</p>
<p>being currently in receipt of a continuing and regular payment arising from participation in the provision of a public service of a particular nature, or of particular services associated with such participation</p>	<p>Credit Unions Act 1979, s.1(4)</p>
<p>residing in a particular locality, or being a member of a bona fide organisation or group of organisations (or otherwise having a continuing and active association with one or more of such organisations) existing within that locality for a purpose other than that of forming a society to be registered as a credit union</p>	<p>Credit Unions Act 1979, s.1(4)</p>
<p>That the rules of the credit union are in a form as agreed by the FSA and provide for all matters required by the legislation.</p>	<p>Credit Unions Act 1979, s.4(1) and Schedule 1</p>
<p>That the registered office of the credit union is in Great Britain.</p>	<p>Credit Unions Act 1979, s.1(1)(c)</p>
<p><u>See CRED 13 Ann 1B G Section 1 of the Credit Unions Act 1979 (as amended).</u></p>	<p><u>Credit Unions Act 1979, s.1(1)(c)</u></p>

After CRED 13 Annex 1 G insert the following new annexes: CRED 13 Annex 1A G, CRED 13 Annex 1B G and CRED 13 Annex 1C G as follows:

## **CRED 13 Annex 1A G**

### **Common bond**

#### **Application**

1. (1) This Annex is relevant to:
  - (a) societies (typically known as “study groups”) seeking registration as credit unions (see *CRED* 13 Ann 1A G 1(2)); and
  - (b) credit unions seeking to amend their membership qualifications.
- (2) When the term “credit union” is in italics, its definition is in the *Glossary* to the *FSA Handbook*, which reads: “a body corporate registered under the Industrial and Provident Societies Act 1965 as a credit union in accordance with the Credit Unions Act, which is an *authorised person*”. When the term is not in italics, it may also refer to a credit union that does not have permission to take deposits, but is merely registered, or is a study group or other association seeking to be registered as a credit union. The term is only intended to refer to a credit union in Great Britain, not one in Northern Ireland.

#### **Introduction**

2. (1) This Annex relates to section 1 of the Credit Unions Act 1979 (see *CRED* 13 Ann 1B G). It explains how the *FSA* exercises its statutory function of satisfying itself before registration that a common bond exists among the members of a credit union.
- (2) These are the key points covered by this Annex:
  - (a) the need for a common bond is fundamental to the regulatory regime for credit unions;
  - (b) an “appropriate membership qualification” does not necessarily create a common bond;
  - (c) the *FSA* has adopted the following policy for the geographical extent of terms limiting membership qualifications:
    - (i) “locality” is comparable in extent to a principal tier of local government (for example: a single city, London borough or county); and

- (ii) “area” is comparable in extent to a single administrative region (for example: Scotland, Wales, North-East England or London);
- (d) a membership qualification based on association between members may be combined with another qualification set out in section 1(4) of the Credit Unions Act 1979 (for example, residing in or being employed in a particular locality - see *CRED* 13 Ann 1B G) but not with additional qualifications created under that subsection;
- (e) common bonds cannot be infinitely extended, so the *FSA* has adopted the policy of using the following presumptions for or against the existence of a common bond for different numbers of persons eligible for membership:
  - (i) up to 100,000 – there is a presumption for the common bond (if supported by a statutory declaration – see *CRED* 13 Ann 1A G 2(2)(g));
  - (ii) from 100,000 to 1 million – there is no presumption either way: the credit union has to make a case; and
  - (iii) over 1 million – there is a presumption against the common bond: the credit union will have to have particularly strong arguments to succeed in making a case;
- (f) the common bond is not a franchise, so:
  - (i) when deciding whether to approve a common bond, the *FSA* will not take into account whether the proposed area overlaps the area of another credit union; and
  - (ii) it is not necessary for a credit union to demonstrate an intention to service the whole of its common bond area;
- (g) (i) three members and the secretary of a credit union may make a statutory declaration that as a result of the qualification for admission to membership, a common bond exists between the members (but the *FSA* may require other evidence – see *CRED* 13 Ann1A 7(2)(b));
  - (ii) there is a special form for this purpose;
  - (iii) a statutory declaration is made under the provisions of the Statutory Declarations Act 1835 and must be signed before a solicitor or commissioner for oaths or notary public or justice of the peace;

- (iv) it is a criminal offence knowingly or wilfully to make a false statutory declaration, and an offender may be imprisoned or fined or both.

### **Statutory function**

- 3. A credit union may be registered if the *FSA* is satisfied (among other things) that admission is restricted to persons who fulfil an “appropriate membership qualification”, in consequence of which a “common bond” exists among the members (sections 1(1)(a) and 1(2)(b) of the Credit Unions Act 1979 (*CRED* 13 Ann 1B G)).

### **Handbook material**

- 4. *DEC* 1.2.8G – *DEC* 1.2.10G provide guidance on who within the *FSA* makes decisions under section 1 of the Credit Unions Act 1979. It is possible for such decisions to be taken to judicial review. *CRED* 13 (Registration and authorisation) is concerned with the registration and authorisation of credit unions.

### **What is a common bond?**

- 5. (1) The Credit Unions Act 1979 provides for the registration of credit unions under the Industrial and Provident Societies Act 1965 (the Act under which bona fide co-operatives are registered).
- (2) Credit unions are only allowed to have the objects set out in section 1(3) of the Credit Unions Act 1979 (see *CRED* 13 Ann 1B G). They are thus restricted to providing services to their members, not to the public at large.
- (3) Membership of a credit union must be restricted by an “appropriate membership qualification” that creates a common bond (section 1(2)(b) of the Credit Unions Act 1979 - see *CRED* 13 Ann 1B G and *CRED* 13 Ann 1C G).
- (4) It is apparent from the Parliamentary debates on the Credit Unions Act 1979 that persons who had a common bond were envisaged as having some degree of shared identity, a sense of belonging or a collective interest. The *FSA* considers that the bond should be sufficient to encourage members to do some or all of the following:
  - (a) play an active role in the credit union (for example, by volunteering);
  - (b) save regularly; and
  - (c) repay loans promptly.

The sense of obligation to save and repay among the members of credit unions would be greater than among persons dealing with an ordinary commercial provider.

- (5) The decision whether or not a common bond exists is made under the Credit Unions Act 1979, so the basis for the *FSA*'s decision will be confined to criteria under that Act, and prudential issues will not be directly involved. However, in discharging its responsibilities under the *Act*, the *FSA* will need to satisfy itself that the credit union will meet or continue to meet the *threshold conditions* and not put its members' funds at risk. These issues will be considered in a risk-based manner when the *FSA* decides whether or not to give a credit union permission to accept deposits. Section 1 of the Credit Unions Act 1979 as amended (see *CRED* 13 Ann 1B G) provides that a credit union may not be registered unless it has applied to the *FSA* for such permission, and the *FSA* shall not register a credit union unless it proposes to give the credit union permission. The *FSA* may give the credit union an opportunity of withdrawing an application for registration if it considers that it will not be able to grant authorisation. Prudential issues will also be considered separately when a credit union seeks to amend its membership qualification.
- (6) It is important that a credit union should not admit to membership any person who does not share the common bond; that is any person who is ineligible under the credit union's membership qualification. *CRED* 13 Ann 2G provides further guidance about the consequences of admitting ineligible persons.

### **What is an “appropriate membership qualification”?**

6. (1) “Appropriate membership qualifications” are such qualifications as “residing in a particular locality”, “being employed by a particular employer” and “being a member of a bona fide organisation”. Some of the qualifications were included when the Credit Unions Act 1979 was passed; others have been added to that Act by Deregulation and other Orders; and others have been approved by the *FSA*, or its predecessor, the Registry of Friendly Societies. A full list of “appropriate membership qualifications” is given in *CRED* 13 Ann 1B G (Section 1 of the Credit Unions Act 1979, as amended) and *CRED* 13 Ann 1C G (Qualifications approved by the *FSA* (and the Registry of Friendly Societies)). The *FSA* has power to approve further qualifications.
- (2) The membership of a credit union is made up of the following types of member:
  - (a) directly qualifying member – who fulfils the “appropriate membership qualification”;
  - (b) indirectly qualifying member (“family member”) - who lives in the same household as, and is a relative of, a directly qualifying member; and

- (c) non-qualifying member – who joined the credit union as a directly or indirectly qualifying member, but has ceased to be so.

Further guidance on eligibility for membership of a credit union is given in *CRED 13 Ann 2G*.

- (3) The two concepts of the “appropriate membership qualification” and the “common bond” are often treated in the credit union sector as though they were interchangeable, but this is not the case. The “appropriate membership qualification” exists as the basis for creating the common bond: thus, the “appropriate membership qualification” may be viewed as the cause and the “common bond” the effect. But the fact that there is an “appropriate membership qualification” does not necessarily mean that there will be a “common bond”.
- (4) For registration to be possible, both the “appropriate membership qualification” and the “common bond” have to be in place. On examining the “appropriate membership qualification”, the *FSA* could in theory infer from it the existence of a “common bond” (section 1(5)(b) of the Credit Unions Act 1979 – see *CRED 13 Ann 1B G*) without a statutory declaration or further evidence. However, the *FSA* is unlikely to be able to make this inference for any but the smallest of population pools – see *CRED 13 Ann 1A 7(2)*.
- (5) Since the Regulatory Reform (Credit Unions) Order 2003, it is possible for a credit union to adopt a membership qualification combining association and one of the other qualifications set out in section 1(4)(a), (b), (c), (d) or (f) of the Credit Unions Act 1979, as amended (without the need for the *FSA* to approve an additional qualification for each combination, under the power in the tailpiece to that subsection – see *CRED 13 Ann 1B G*). For example, a credit union may now adopt a membership qualification under which some members reside in the locality (but do not belong to a bona fide organisation there) and other members belong to a bona fide organisation in the locality (but do not reside there). However, a credit union cannot combine association and one of the qualifications approved by the *FSA* or Registry of Friendly Societies (see *CRED 13 Ann 1C G* and *CRED 13 Ann 1A G 10(2)*); nor may the qualifications in section 1(4)(a), (b), (c), (d) or (f) of the Credit Unions Act 1979, as amended, be combined with each other (see *CRED 13 Ann 1B G*).

- (6) Having chosen an “appropriate membership qualification” from the list, it has always been possible for a credit union to impose within its registered rules an additional requirement upon members. This is the effect of the words in section 1(2)(b) of the Credit Unions Act 1979 see *CRED* 13 Ann 1B G: “whether or not any other qualifications are also required by the rules”. Thus it has always been possible to adopt a requirement that each member of the credit union must both reside and belong to a bona fide organisation in the locality. Under such a qualification, neither a person who merely resides (but does not belong to the organisation), nor one who merely belongs to the organisation (but does not reside) may join the credit union.
- (7) *CRED* 13 Ann 1C G lists the qualifications approved by the *FSA* (or its predecessor, the Registry of Friendly Societies). The *FSA* has power, as previously mentioned, to approve further qualifications.

**What has the FSA to decide?**

- 7. (1) In relation to membership, the *FSA* has to be satisfied on two counts:
  - (a) there is an “appropriate membership qualification” ; and
  - (b) in consequence of the “appropriate membership qualification”, a common bond exists.

It is a two-stage process: the first stage is factual (a question of technical validity); the second is judgemental (and potentially subjective).

- (2) If it considers it proper in the circumstances of the case, the *FSA* may:
  - (a) infer the existence of a common bond from the appropriate membership qualification (but see *CRED* 13 Ann 1A G 6(4)); or
  - (b) rely on a statutory declaration (by 3 members and the secretary of the credit union or prospective credit union – see *CRED* 13 Ann 1A 2(2)(g)) that a common bond exists (section 1(5) of the Credit Unions Act 1979 – see *CRED* 13 Ann 1B G). Even where a statutory declaration is given, the *FSA* may require other evidence to support the credit union’s (or prospective credit union’s) contention that there is a common bond.

**Meaning of “locality ” in “appropriate membership qualifications ” based on residence**

- 8 (1) Although several of the “appropriate membership qualifications” (see *CRED* 13 Ann 1B G - *CRED* 13 Ann 1C G) use the term “locality”, it is not defined by the Credit Unions Act 1979. Historically, the Registry of Friendly Societies took a fairly restrictive view of its meaning, but the *FSA* is taking a broader one, drawing on case law and other statutory uses of that term.

- (2) The *FSA*'s working definition is that a "locality" is a natural geographical or administrative unit, comparable in size (but not limited to) the principal tier of local government in Great Britain, that is unitary authorities or county councils. The justification for this is that the common provision of "local" public services is currently made at this level.
- (3) So the *FSA* will generally accept that "locality" extends up to the area covered by such local authorities, and so may cover such areas as single cities, London boroughs or counties. If larger areas were proposed, the onus would lie with credit unions to demonstrate that they still constituted a "locality". Even if a geographical or administrative area satisfies the criteria for being a "locality", that does not mean that there will be a common bond (see *CRED* 13 Ann 1A G 2(2)(b) and 11(1)–(5)).

**Meaning of "area " in "appropriate membership qualifications " based on employment**

9. The "appropriate membership qualification" based on employment in *CRED* 13 Ann 1C G uses the term "area", but this is not defined in the Credit Unions Act 1979. The *FSA* accepts that the term "area" is potentially much larger in scope than "locality", and that it could extend up to the size of a single standard administrative region within Great Britain. So, for example, Scotland, Wales, the North-East of England or Greater London could be regarded as "areas" for the purpose of this "appropriate membership qualification". To be acceptable, it is not necessary for the boundary proposed by a credit union to coincide with an actual standard administrative region.

**Regulatory Reform (Credit Unions) Order 2003 and associational "appropriate membership qualification"**

10. (1) The "appropriate membership qualification" in section 1(4)(e) of the Credit Unions Act 1979 is that of "being a member of a bona fide organisation or being otherwise associated with other members of the society for a purpose other than that of forming a society to be registered as a credit union". So the members must be associated through something other than the credit union. The stronger the character of the association between the individuals, the more likely it is to form the basis for the existence of a common bond.



- (2) As a result of the Regulatory Reform (Credit Unions) Order 2003, it is now possible for a credit union to adopt a membership qualification combining association and one of the other qualifications set out in section 1(4)(a), (b), (c), (d) or (f) of the Credit Unions Act 1979, as amended (without the need for the *FSA* to approve an additional qualification for each combination, under the power in the tailpiece to that subsection - see *CRED 13 Ann 1B G* and *CRED 13 Ann 1A G 6(5)*). However, it is not possible for a credit union to combine association and one of those qualifications specifically approved by the *FSA* or its predecessor, the Registry of Friendly Societies - see *CRED 13 Ann 1C G* and *CRED 13 Ann 1A G 6(5)*, nor may the qualifications in section 1(4)(a), (b), (c), (d) or (f) of the Credit Unions Act 1979, as amended, be combined with each other. This means that a single credit union may be properly formed for persons who:
- (a) live or work in a locality; or
  - (b) associate with the residents and workers (through, for example, attending a religious centre in the locality).
- (3) However, it is still necessary to establish that the qualifications establish a common bond: this may be difficult if there is no shared identity between the members qualifying under the different qualifications (even where the population pool is below 100,000 – *CRED 13 Ann 1A G 11(3)*).

**Overall size of population pool for “appropriate membership qualifications”**

11. (1) It is in the nature of the common bond that the concept cannot be infinitely expanded: the larger the eligible population pool covered by an “appropriate membership qualification”, the weaker or less plausible will be the existence of a common bond.
- (2) It is not practical to expect credit unions to operate on the basis that members will be fully acquainted with each other, but there has to be some mutual identification, and some point at which this ceases to have a significant effect.
- (3) The Registry of Friendly Societies (a predecessor of the *FSA*) adopted 100,000 as an indicative maximum for the size of the residential population in a common bond area. The *FSA* has further developed that thinking through its decisions in subsequent cases. For full transparency, the indicative bands currently used by the *FSA* are set out below:
- (a) where an “appropriate membership qualification” covers a pool of up to 100,000 people eligible to be members:
    - (i) there is a presumption in favour of the existence of a common bond; and

- (ii) the *FSA* will (provided the “appropriate membership qualification” is technically valid and there are no unusual features) generally accept a simple explanation of the nature of the common bond, together with a statutory declaration (but see *CRED* 13 Ann 1A G 10(3)).
- (b) where an “appropriate membership qualification” covers a pool of between 100,000 and 1 million eligible people:
  - (i) there is no presumption in favour of the existence of a common bond; and
  - (ii) the *FSA* expects the credit union to make a positive, convincing case, marshalling all the information relevant to establishing that a common bond exists among the members.
- (c) where an “appropriate membership qualification” covers a pool of more than 1 million eligible people:
  - (i) there is a presumption that the common bond is so dilute as to be meaningless; but
  - (ii) it is open to a credit union to make a submission to convince the *FSA* that a common bond exists among the members: but its arguments would have to be particularly strong for it to succeed in making a case.
- (4) The *FSA*’s decision whether or not to accept the existence of a common bond (for a new or prospective credit union) is made on an individual basis. So decisions (whether made by the *FSA* or its predecessor, the Registry of Friendly Societies) create no binding precedent that a population pool of a given size is acceptable for a particular “appropriate membership qualification”.
- (5) Given the range of “appropriate membership qualification” and the different populations covered, it is not possible to be prescriptive about the information necessary to show that a common bond is real. In general, it has been the experience of the Registry of Friendly Societies and the *FSA* that it is fairly straightforward to make a plausible case for the existence of a common bond where the “appropriate membership qualification” is based on employment by a single employer. For residential qualifications, applicants should draw on their local knowledge to identify those elements, geographical and social that create a sense of cohesion. For a qualification based on living or working in a particular locality, the applicants might wish to identify the ways in which workers from outside the area become involved in the activities of the residential community.

- (6) The size thresholds set out above apply to the number of persons eligible for membership under any “appropriate membership qualification”, not just ones based on residence.

### **Overlapping common bond areas**

12. A common bond area cannot be regarded legally as a franchise, giving exclusive rights of access to a particular area or pool of potential members. The *FSA* recognises the value of consolidation in providing stronger entities, but there is no justification in current legislation for refusing the registration of a new credit union in an area already served by existing credit unions, nor even for consulting them: the *FSA's* decision on registration is based only on the criteria in the Credit Unions Act 1979 (see *CRED* 13 Ann 1A G 5(5)). In the absence of express statutory support, it would be wrong for the *FSA* to act in a manner that could be construed as anti-competitive. So the *FSA* will not refuse registration on the grounds of overlap, nor will it undertake to consult credit unions whose common bond area may be overlapped by a later registration.

### **Servicing whole of area**

13. Since the common bond is not a franchise, the *FSA* will not expect a credit union to service fully the whole of its area or population pool. But where the “appropriate membership qualification” covers a large population pool, the inference is that the bond is likely to be weaker, and there will need to be more justification. An intention to service only part of the area does not help to establish whether or not the “appropriate membership qualification” establishes a common bond for the area as a whole.

### **Mergers**

14. (1) The Credit Unions Act 1979 allows credit unions to merge, either by amalgamation (where a new credit union is created and the constituents cease to exist) or by transfer of engagements (where the credit union transferring its engagements ceases to exist, but the enlarged credit union accepting the engagements continues).
- (2) For either of these procedures to be practicable in individual cases:
  - (a) the merged credit union will need to have an “appropriate membership qualification” that creates a “common bond”; and
  - (b) members of the constituent credit unions will need to be eligible for membership of the merged credit union.
- (3) So in individual cases:

- (a) it might not be possible for the merged credit union to adopt an “appropriate membership qualification” (for example, the new catchment area required for the merger of two residential credit unions might not qualify under the definition of “locality” – see *CRED 13 Ann 1A G 8(1)-(3)*);
- (b) even though each credit union seeking to merge has a “common bond” among its own members, this does not necessarily mean that there would be a common bond among all the members of the merged credit union (for example, too large a population pool might be produced by the merger – see *CRED 13 Ann 1A G 11(1)*).

**What information does a credit union need to provide in support of a common bond application?**

15 Table

<b>Population pool</b>	<b>Information needed</b>
Up to 100,000	Statutory declaration Simple explanation of common bond (subject to <i>CRED 13 Ann 1A G 10(3)</i> )
100,000 to 1 million	Convincing case that common bond exists
Over 1 million	Evidence to rebut presumption against existence of common bond (special factors generating particular interaction in this population pool, despite its large size and the dilution normally expected in such circumstances)

## CRED 13 Annex 1B D

### Section 1 of the Credit Unions Act 1979 (as amended)

1. Registration as a credit union
  - (1) Subject to ... sections 2(1) and 7(1) of the Industrial and Provident Societies Act 1965 (in this Act referred to as “the 1965 Act”), a society may be registered under that Act if:
    - (a) it is shown to the satisfaction of the Authority that the conditions specified in subsection (2) below are fulfilled;
    - (b) the rules of the society comply with section 4(1) [of this Act];
    - (c) the place which under those rules is to be the society’s registered office is situated in Great Britain;
    - (d) the society has made an application to the Authority for Part IV permission under section 40 of the Financial Services and Markets Act 2000 (in this Act referred to as “the 2000 Act” to accept deposits; and
    - (e) the Authority is satisfied that, once registered under the 1965 Act, the society will satisfy, and continue to satisfy, the *threshold conditions* set out in Schedule 6 to the 2000 Act in relation to the regulated activity of accepting deposits; and a society which is so registered by virtue of this section shall be registered as, and is in this Act referred to as, a “credit union”.
  - (1A) The Authority shall not issue an acknowledgement of registration under section 2(3) of the 1965 Act to a credit union unless it also proposes to give that society permission under Part IV of the 2000 Act to accept deposits.
  - (2) The conditions referred to in subsection (1)(a) above are –
    - (a) that the objects of the society are those, and only those, of a credit union; and
    - (b) that as a result of any provision of the rules, admission to membership of the society meets the requirement specified in subsection (3A) or (3B) below (whether or not any other qualifications for admission to membership are also required by the rules) and that in consequence, a common bond exists between members of the society.
  - (3) The objects of a credit union are –

- (a) the promotion of thrift among the members of the society by the accumulation of their savings;
  - (b) the creation of sources of credit for the benefit of the members of the society at a fair and reasonable rate of interest;
  - (c) the use and control of the members' savings for their mutual benefit; and
  - (d) the training and education of the members in the wise use of money and in the management of their financial affairs.
- (3A) The requirement specified in this subsection is that admission to membership of the society is restricted to persons all of whom fulfil the same specific qualification for admission to membership, being a qualification specified in, or approved under, subsection (4) below as being appropriate to a credit union.
- (3B) The requirement specified in this subsection is that admission to membership of the society is restricted to persons each of whom fulfils either –
- (a) the qualification for admission to membership specified by paragraph (e) of subsection (4) below as being appropriate to a credit union; or
  - (b) the same specific qualification for admission to membership, being a qualification which is so specified in paragraph (a), (b), (c), (d) or (f) of that subsection.
- (4) The qualifications for admission to membership which are appropriate to a credit union are –
- (a) following a particular occupation;
  - (b) residing in a particular locality;
  - (c) being employed in a particular locality;
  - (d) being employed by a particular employer;
  - (e) being a member of a bona fide organisation or being otherwise associated with other members of the society for a purpose other than that of forming a society to be registered as a credit union;
  - (f) residing in or being employed in a particular locality;
- and such other qualifications as are for the time being approved by the Authority.

- (5) In ascertaining whether a common bond exists between the members of a society, the Authority –
- (a) may, if it considers it proper in the circumstances of the case, treat as sufficient evidence of the existence of a common bond a statutory declaration which is given by three members and the secretary of the society, and is to the effect that a common bond exists
  - (b) may, if it considers it proper in the circumstances of the case, treat the fact that admission to membership is restricted as mentioned in subsection (2)(b) above as sufficient evidence of the existence of a common bond.
- (6) For the purposes of this Act, if the rules of a credit union so provide, a person shall be treated as fulfilling a qualification for admission to membership stated in those rules if he is a member of the same household as, and is a relative of, another person who is a member of the credit union and fulfils that qualification directly.

In section 1 of the Credit Unions Act 1979, the *FSA* is referred to as "the Authority".

## CRED 13 Annex 1C D

### Qualifications approved by the FSA (and the Registry of Friendly Societies)

1. The following qualifications (in addition to those set out in section 1(4) of the Credit Unions Act 1979) have been approved by the *FSA* (and the Registry of Friendly Societies ("RFS")):
  - (1) being currently in receipt of a continuing and regular contractual payment arising from employment by a particular employer;  
RFS: 25 February 1994
  - (2) being currently in receipt of a continuing and regular contractual payment arising from employment by particular employers in a particular area;  
RFS: 6 October 1994
  - (3) being currently in receipt of a continuing and regular payment arising from participation in the provision of a public service of a particular nature, or of particular services associated with such participation;  
RFS: 22 May 1998
  - (4) residing in a particular locality, or being a member of a bona fide organisation or group of organisations (or otherwise having a continuing and active association with one or more of such organisations) existing within that locality for a purpose other than that of forming a society to be registered as a credit union;  
RFS: 15 November 1999
  - (5) being employed by an undertaking in a particular group of employers (and for this purpose "group" has the same meaning as in section 421 of the Financial Services and Markets Act 2000).  
FSA 1 January 2005
2. Section 421 of the *Act*:
  - (1) In this *Act* "group", in relation to a person ("A"), means A and any person who is-
    - (a) a parent undertaking of A;
    - (b) a subsidiary undertaking of A;
    - (c) a subsidiary undertaking of a parent undertaking of A;
    - (d) a parent undertaking of a subsidiary undertaking of A;
    - (e) an undertaking in which A or an undertaking mentioned in



paragraph (a), (b), (c) or (d) has a participating interest;

- (f) if A or an undertaking mentioned in paragraph (a) or (d) is a building society, an associated undertaking of the society; or
  - (g) if A or an undertaking mentioned in paragraph (a) or (d) is an incorporated friendly society, a body corporate of which the society has joint control (within the meaning of section 13(9)(c) or (cc) of the Friendly Societies Act 1992).
- (2) "Participating interest" has the same meaning as in Part VII of the Companies Act 1985 or Part VIII of the Companies (Northern Ireland) Order 1986; but also includes an interest held by an individual which would be a participating interest for the purposes of those provisions if he were taken to be an undertaking.
- (3) "Associated undertaking" has the meaning given in section 119(1) of the Building Societies Act 1986.

## **CRED Appendix 2**

### **2.1 Detailed contents of CRED**

#### **2.1.1 Table**

### **13 Registration and Authorisation**

...

Ann 1 Requirements of Registration [table]

Ann 1A Common bond

Ann 1B Section 1 of the Credit Unions Act 1979 (as amended)

Ann 1C Qualifications approved by the FSA (and the Registry of Friendly Societies)

Ann 2 Eligibility for membership of a credit union

**LISTING RULES (AUDITORS' RESPONSIBILITIES IN RELATION TO THE  
COMBINED CODE) INSTRUMENT 2004**

**Powers Exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000:
- (1) section 74 (The official list);
  - (2) section 96 (Obligations of issuers of listed securities); and
  - (3) paragraph 1 of Schedule 7.

**Commencement**

- B. This instrument comes into force on 1 November 2004.

**Amendments to the Listing Rules**

- C. The Listing Rules are amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Listing Rules (Auditors' Responsibilities in relation to the Combined Code) Instrument 2004.

By order of the Board  
20 October 2004

## Annex

### Amendments to the Listing Rules

In this annex underlining indicates new text, and striking through indicates deleted text.

Amend Chapter 12 of the Listing Rules detailing the application of the Combined Code in listing rule 12.43A as set out below:

Corporate governance and director's remuneration

...

12.43A...

...

Requirements of auditors

A company's statement under 12.43A(b) must be reviewed by the auditors before publication ~~only~~ insofar as it relates to Code provisions C1.1, C.2.1, C3.1, C3.2, C3.3, C3.4, C3.5, C3.6 and C.3.7 ~~A.1.2, A.1.3, A.6.1, A.6.2, D.1.1, D.2.1 and D.3.1~~ of the Combined Code.

The scope...

## INTERIM PERMITTED MORTGAGE INTERMEDIARIES INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the powers and related provisions in:
- (1) article 4(1) of the Financial Services and Markets Act 2000 (Transitional Provisions) (Mortgages) Order 2004 (SI No 2004/2615) (“the Order”); and
  - (2) the following sections of the Financial Services and Markets Act 2000 (“the Act”):
    - (a) section 138 (General rule-making power);
    - (b) section 145 (Financial promotion rules);
    - (c) section 149 (Evidential provisions);
    - (d) section 156 (General supplementary powers);
    - (e) section 157(1) (Guidance);
    - (f) section 213 (The compensation scheme); and
    - (g) section 214 (General)
- B. Article 4(2) of the Order is relevant to the exercise of the powers set out in paragraph A(2) above because it provides that sections 155 (Consultation) and 157(3) (Guidance) of the Act do not apply to the rules and guidance set out in this instrument.
- C. The provisions listed above relevant to making rules are specified for the purposes of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- D. This instrument comes into force on 31 October 2004.

### Citation

- E. This instrument may be cited as the Interim Permitted Mortgage Intermediaries Instrument 2004.
- F. The Annex to this instrument may be cited as the Directions, rules and guidance for Interim Permitted Mortgage Intermediaries.

Made under the authority of the Board and under article 4 of the Order

Clive Briault  
Managing Director, Retail Markets

29 October 2004

## Annex

### Directions, rules and guidance for Interim Permitted Mortgage Intermediaries

In this annex, new provisions relevant to interim permitted mortgage intermediaries (“IPMI”) are being introduced and they are not underlined.

#### 1. Handbook and other requirements for Interim Permitted Mortgage Intermediaries

##### 1.1 Application and purpose

1.1.1 R *IPMI* applies to *interim permitted mortgage intermediaries*.

1.1.2 G The purpose of *IPMI* is:

- (1) to make *rules* relating to disclosure of their regulated status by *interim permitted mortgage intermediaries*;
- (2) to direct, in accordance with article 4(1) of the *Mortgages Transitional Order*, that certain provisions of the *Handbook* that would otherwise apply to *interim permitted mortgage intermediaries*:
  - (a) are not to apply; or
  - (b) are to apply to them as modified in *IPMI*; and
- (3) to give ancillary *guidance* to *interim permitted mortgage intermediaries* as to the application of the *Handbook* to them.

##### 1.2 Disclosure of interim permitted mortgage intermediary status

1.2.1 G *IPMI* 1.2 makes special provision for *interim permitted mortgage intermediaries* in place of *GEN* 1.2 (Referring to approval by the FSA). The purpose is to prevent *clients* being misled about the extent to which the *FSA* has approved a *firm's* affairs.

1.2.2 D The *FSA* directs that *GEN* 1.2 (Referring to approval by the *FSA*) does not apply to an *interim permitted mortgage intermediary*.

1.2.3 R (1) Unless required to do so under the *regulatory system*, an *interim permitted mortgage intermediary* must ensure that neither it, nor anyone acting on its behalf claims, in a public statement or to a *client*, expressly or by implication, that its affairs, or any aspect of them, have the approval of the *FSA* or that it is an *authorised person* for the purposes of the *Act*.

- (2) Paragraph (1) does not apply to statements by or on behalf of an *interim permitted mortgage intermediary* who is an *interim authorised mortgage person* that explain, in a way that is fair, clear and not misleading, that:
- (a) the *firm* is an *interim permitted mortgage intermediary*;
  - (b) the *firm's approved persons* are deemed to be approved by the *FSA* for the purposes of section 59 of the *Act* (Approval for particular arrangements) pending determination of the *firm's* application for authorisation;
  - (c) the *firm* has been given express written approval by the *FSA* in respect of a specific aspect of the *firm's* affairs.
- (3) Paragraph (1) does not apply to any statement by or on behalf of an *interim permitted mortgage intermediary* who is not an *interim authorised mortgage person* that explains, in a way that is fair, clear and not misleading, that:
- (a) the *firm* is an *authorised person*;
  - (b) as appropriate:
    - (i) the *firm* has *permission* to carry on a specific activity; or
    - (ii) the *firm* has *interim permission* to carry out a specific activity;
  - (c) as appropriate:
    - (i) one or more of the *firm's approved persons* has been approved by the *FSA* for the purposes of section 59 of the *Act* (Approval for particular arrangements); or
    - (ii) one or more of the *firm's approved persons* is deemed to be approved by the *FSA* for the purposes of section 59 of the *Act* (Approval for particular arrangements) pending determination of the *firm's* application for *permission*; or
  - (d) the *firm* has been given express written approval by the *FSA* in respect of a specific aspect of the *firm's* affairs.
- (4) Paragraph (1) applies with respect to the carrying on of both *regulated activities* and *unregulated activities*.

## Required disclosures

- 1.2.4 R (1) An *interim permitted mortgage intermediary* who is an *interim authorised mortgage person* and who, in order to comply or to provide evidence of complying with a provision (including a provision mentioned in *IPMI 1.2.6R*) of the *Handbook*, discloses that he is authorised or regulated by the *FSA*, must also disclose that he is authorised or regulated on an interim basis only.
- (2) An *interim permitted mortgage intermediary* who, in the course of carrying on *mortgage mediation activity*, discloses that he is authorised or regulated by the *FSA*, must as part of that disclosure, and with equal prominence, disclose that the *FSCS* does not apply to any *mortgage mediation activity* that he undertakes.
- 1.2.5 E (1) An *interim permitted mortgage intermediary* should, in the circumstances mentioned in *IPMI 1.2.4R*, disclose that:
- (a) he is 'interim authorised under the Financial Services and Markets Act 2000' or 'interim regulated by the Financial Services Authority' or 'regulated by the Financial Services Authority as an interim authorised person' or use words to that effect; and
- (b) 'no compensation will be available from the Financial Services Compensation Scheme in the event that we are unable to meet our obligations under our mortgage business' or use words to that effect.
- (2) Compliance with (1) may be relied on as tending to establish compliance with *IPMI 1.2.4R*.
- (3) Contravention of (1) may be relied on as tending to establish contravention of *IPMI 1.2.4R*.
- 1.2.6 R Table Non-exhaustive list of provisions about status disclosure

This table belongs to *IPMI 1.2.4R*.

Provision	Topic
<i>MCOB 4.4.1R(1)(c)</i>	Initial disclosure requirements
<i>MCOB 4 Ann 1R</i>	
<i>MCOB 4 Ann 2R</i>	
<i>MCOB 8.4.1R</i>	Initial disclosure requirements for <i>lifetime mortgages</i> and <i>home reversion schemes</i>
<i>MCOB 8 Ann 1R</i>	



### 1.3 Application of the handbook to interim permitted mortgage intermediaries

- 1.3.1 G The *Mortgages Transitional Order* provides broadly that *interim permitted mortgage intermediaries* are to be treated, unless otherwise provided, as *authorised persons* for the purposes of the *Act* and of any provision made under the *Act* (see paragraph 5 of the Schedule to the *Mortgages Transitional Order*). As a result, the *Handbook* applies to *interim permitted mortgage intermediaries* and any *regulated activity* for which they are seeking *permission* is *regulated activity* for the purposes of the *Handbook*.
- 1.3.2 G Annex 4G to *MCOB 1* contains a list of the parts of the *Handbook* and their application to *mortgage intermediaries*. This annex is also relevant to *interim permitted mortgage intermediaries*, with the modifications set out in *IPMI 1.3.3G*.
- 1.3.3 G Table Modifications to *MCOB 1 Ann 4G* where the firm concerned is an interim permitted mortgage intermediary

This table belongs to *IPMI 1.3.2G*.

Part of Handbook	Extent of modification
Statements of Principle and Code of Practice for Approved Persons ( <i>APER</i> )	Under article 3 of the <i>Mortgages Transitional Order</i> , special provision is made for <i>approved persons</i> carrying on controlled functions for <i>interim permitted mortgage intermediaries</i> .
General provisions ( <i>GEN</i> )	<i>GEN 1.2</i> (Referring to approval by the <i>FSA</i> ) does not apply to <i>interim permitted mortgage intermediaries</i> : see <i>IPMI 1.2.2D</i> . Instead, <i>IPMI 1.2.3R</i> makes provision about <i>interim permitted mortgage intermediaries</i> referring to approval by the <i>FSA</i> or <i>authorisation</i> for the purposes of the <i>Act</i> .
Mortgages: Conduct of Business ( <i>MCOB</i> )	<p>(1) This applies.</p> <p>(2) <i>IPMI 1.2.4R</i> makes special provision for required status disclosure by <i>interim permitted mortgage intermediaries</i>.</p> <p>(3) Paragraph 6 of the Schedule to the <i>Mortgages Transitional Order</i> provides broadly that an <i>interim permitted mortgage intermediary</i> is not authorised for the purposes of sections 21(1) (Restrictions on financial promotion) and 25(2)(a)</p>

	<p>(Contravention of section 21) unless the communication invites an agreement the making or performance of which constitutes a <i>controlled activity</i> corresponding to a <i>regulated activity</i> covered by his <i>interim mortgage permission</i>.</p>
<p>Authorisation manual (<i>AUTH</i>)</p>	<p>(1) Paragraph 2 of the Schedule to the <i>Mortgages Transitional Order</i> provides that for the purposes of section 20 (Authorised persons acting without permission) a person's <i>interim mortgage permission</i> is treated as having been given to him under Part IV of the <i>Act</i>.</p> <p>(2) Paragraph 3 of the Schedule to the <i>Mortgages Transitional Order</i> provides that an applicant's <i>interim mortgage permission</i> is to be disregarded for the purposes of sections 38(2) (Exemption orders), 40(2) (Application for permission), 42 (Giving permission), 43 (Imposition of requirements) and 44(1), (4) and (5) (Variation etc. at request of authorised person) of the <i>Act</i>.</p> <p>(3) Under article 3 of the <i>Mortgages Transitional Order</i>, special provision is made for <i>approved persons</i> carrying on controlled functions for <i>interim permitted mortgage intermediaries</i>.</p> <p>(4) The Schedule to the <i>Mortgages Transitional Order</i> provides broadly that <i>interim permitted mortgage intermediaries</i>:</p> <p>(a) are to be treated, unless otherwise provided, as <i>authorised persons</i> for the purposes of the <i>Act</i> (see paragraph 5); and</p>

	(b) may still be <i>appointed representatives</i> (and hence may be treated as exempt from the <i>general prohibition</i> as a result of section 39(1) for the purposes of section 42(3)(a) of the <i>Act</i> (see paragraph 7).
Supervision manual ( <i>SUP</i> )	See notes (2), (3) and (4)(b) to <i>AUTH</i> which are relevant to <i>SUP 6</i> , <i>SUP 7</i> , <i>SUP 10</i> and <i>SUP 12</i> .
Compensation sourcebook ( <i>COMP</i> )	This does not apply:  (1) to an <i>interim permitted mortgage intermediary</i> who is an <i>interim authorised mortgage person</i> ; and  (2) to an <i>interim permitted mortgage intermediary</i> who is not an <i>interim authorised mortgage person</i> in respect of his <i>mortgage mediation activities</i> .

1.3.4 D The *FSA* directs that any special application or disapplication provisions in the *Handbook* are to apply to *interim permitted mortgage intermediaries* as nearly as possible as if the application for *permission* which gives rise to the *interim mortgage permission* has been granted in the terms applied for, including as if the *requirements* and *limitations* applied for (or otherwise required to give effect to the terms of the application) have already been included in that *permission*.

1.3.5 D The *FSA* directs that *COMP*:

- (1) does not apply to an *interim authorised mortgage person*;
- (2) does not apply to an *interim permitted mortgage intermediary* who is not an *interim authorised mortgage person* in respect of his *mortgage mediation activities*.

1.3.6 R In *COMP*, *relevant person* does not include:

- (1) an *interim authorised mortgage person*;
- (2) in respect of his *mortgage mediation activities*, an *interim permitted mortgage intermediary* who is not an *interim authorised mortgage person*.

- 1.3.7 G Where the *FSA* has given an *interim permitted mortgage intermediary* a *waiver* from a provision of the *Handbook*, the terms of that *waiver* are to be taken into account in determining the provisions of the *Handbook* that apply to that *interim permitted mortgage intermediary*.

## 2. Interpretation

### 2.1 GEN and Glossary apply

- 2.1.1 R The General provisions (*GEN*) of the *Handbook* and the *Glossary* made under the *Act* apply in the interpretation of *IPMI*, unless *IPMI* 1.2.2D applies.
- 2.1.2 R The terms in *IPMI* 2.1.3R are also defined for the purposes of *IPMI*.
- 2.1.3 R Terms defined for the purposes of *IPMI*

This table belongs to *IPMI* 2.1.2R.

Defined expression	Definition
<i>interim authorised mortgage person</i>	an <i>interim permitted mortgage intermediary</i> who is an <i>authorised person</i> only because he has an <i>interim mortgage permission</i> .
<i>interim mortgage permission</i>	a <i>Part IV permission</i> conferred by article 2 of the <i>Mortgages Transitional Order</i> .
<i>interim permitted mortgage intermediary</i>	a person who has an <i>interim mortgage permission</i> .
<i>IPMI</i>	Directions, rules and guidance for Interim Permitted Mortgage Intermediaries forming the Annex to the Interim Permitted Mortgage Intermediaries Instrument 2004 (FSA 2004/84).
<i>Mortgages Transitional Order</i>	The Financial Services and Markets Act 2000 (Transitional Provisions) (Mortgages) Order 2004 (SI 2004/2615).

**CHANGING ACCOUNTING FRAMEWORK INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) 138 (General rule-making power);
  - (2) 141 (Insurance business rules);
  - (3) 156 (General supplementary powers);
  - (4) 157 (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) the amendments to SUP 16 Annex 18BG in Annex E, Part 2 come into force on 1 April 2005;
  - (2) all other amendments come into force on 1 January 2005.

**Amendments to the Handbook**

- D. The modules of the FSA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Interim Prudential sourcebook for Banks (IPRU(BANK))	Annex A
Interim Prudential sourcebook for Friendly Societies (IPRU(FSOC))	Annex B
Interim Prudential sourcebook for Insurers (IPRU(INS))	Annex C
Interim Prudential sourcebook for Investment Businesses (IPRU(INV))	Annex D
Supervision manual (SUP)	Annex E, Parts 1 and 2
Electronic Money sourcebook (ELM)	Annex F
Glossary of definitions	Annex G

**Citation**

- E. This instrument may be cited as the Changing Accounting Framework Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### Amendments to the Interim Prudential sourcebook for Banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Volume 2, LE LARGE EXPOSURES

...

#### 5 KEY DEFINITIONS: COUNTERPARTY

...

#### 5.3 Connected counterparties

...

9 *Parties connected to a bank* comprise:

(a) ...

(b) ~~associated companies~~ as defined by Financial Reporting Standard 9 or by International Accounting Standard 28;

...

#### Volume 2, VA VALUATION

...

#### 2 GENERAL POLICY ON VALUATION

...

5 The form and content of a bank's statutory financial statements are governed by:

(a) the Companies Act 1985, as amended by the Companies Act 1985 (Bank Accounts) Regulations 1991 ('BAR'), which implemented the EU Bank Accounts Directive, and the Companies Act 1985 (International Accounting Standards and Other Accounting Amendments) Regulations 2004 (SI 2004/to follow), which made arrangements for the use of *international accounting standards* (see definition in the *Glossary*) by companies and implemented the accounting Modernisation Directive (2003/51/EC) of 18 June 2003;

a) ...

(b) accounting standards comprising statements of standard accounting practice ('SSAPs') and financial reporting standards ('FRSs') or, where applicable, *international accounting standards*; and

a) SSAPs, ~~and~~ FRSs and *international accounting standards* focus on particular accounting issues and apply to the generality of companies.

(c) ...

a) Because ~~the SSAPs and FRSs~~ accounting standards apply to the generality of companies and not to banks specifically, they do not cover the accounting treatment of instruments and transactions peculiar to banks. SORPs issued by the BBA seek to plug this gap by codifying best banking industry practices.

...

## Volume 2, CS CONSOLIDATED SUPERVISION

...

### 4 SCOPE OF CONSOLIDATION

...

#### 4.3 Companies to be consolidated

3 Consolidation then extends to all relevant financial companies within that domain: that is the *parent company*; its *subsidiaries*; and companies in which the parent or its subsidiaries have a *participation*.

a) ...

b) ~~[deleted] The notion of *subsidiary* is also normally extended to cover a company over which the parent or one of its subsidiaries exercises *dominant influence*. The criteria used to determine whether dominant influence exists are those provided by the contemporary UK accounting standards.~~

i) ~~— The relevant accounting standard is FRS2, Accounting for Subsidiary Undertakings.~~

c) ...

...

## Volume 2, PN PROVISIONING POLICY STATEMENTS

...

### 2 THE FSA'S BASIC APPROACH TO PROVISIONING

1 The *FSA* regards the prudent valuation of assets and the establishment of provisions as of fundamental importance. The *FSA* expects contingent liabilities and anticipated losses to be recognised in accordance with accepted accounting standards (as embodied in the Statements of Standard Accounting Practice and Financial Reporting Standards or, where applicable, *international accounting standards* (see definition in the *Glossary*)).

## Annex B

### Amendments to the Interim Prudential sourcebook for Friendly Societies

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Chapter 7

#### DEFINITIONS

##### Part I Definitions

##### 7.1

Insert the following definition in the appropriate alphabetical position:

international accounting standards means the international accounting standards, within the meaning of EC Regulation No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, adopted from time to time by the European Commission in accordance with that Regulation.

...

#### Appendix 5

#### LIABILITY VALUATION RULES

...

##### Rates of interest

##### 10.

- (5A) For variable interest investments that are equity *shares* in *companies* subject to, or drawing up accounts as if subject to, legislation implementing the *Accounts Directives*, or which draw up a set of accounts in accordance with ~~International Accounting Standards Committee accounting standards~~ international accounting standards or US generally accepted accounting practice, the yield on an asset, subject to (7A), must be the ratio to the value of the asset of- ...
- (5B) ...
- (5C) For the purposes of (5B), the issuing *company's* profits after taxation from its ordinary activities for the relevant financial year must be derived from accounts drawn up in accordance with legislation implementing the *Accounts Directives* or, if accounts are not drawn up in accordance with the *Accounts Directives*, from accounts drawn up in accordance with ~~International Accounting Standards Committee accounting standards~~ international accounting standards or US generally accepted accounting practice.



## Annex C

### Amendments to the Interim Prudential sourcebook for Insurers

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Volume 1, Chapter 9 FINANCIAL REPORTING

##### Part I

##### ACCOUNTS AND STATEMENTS

...

##### Audit and auditor's report

9.35

(2) For the purposes of the *Accounts and Statements Rules* –

(a) ...

(i) the references to the *profit and loss account* contained in the definition of 'individual accounts' in section 226~~(1)~~A of that Act and article 234(1) of that Order, respectively, included references to the revenue account; and

...

#### Volume 1, Chapter 11 DEFINITIONS

##### PART I

##### DEFINITIONS

11.1

Insert the following definition in the appropriate alphabetical position:

Term or phrase	Definition
...	
<u><i>international accounting standards</i></u>	<u>has the meaning given in the <i>Glossary of the FSA Handbook</i>.</u>

## Annex D

### Amendments to the Interim Prudential sourcebook for Investment Businesses

In this Annex, underlining indicates new text and striking through indicates deleted text.

### 3 Chapter 3: Financial resources for Securities and Futures Firms which are not Investment Firms

...

#### APPENDIX 1 – GLOSSARY OF TERMS FOR IPRU(INV) 3

...

<i>audited annual financial statements</i>	means statements drawn up in accordance with Schedule 4 to the Companies Act 1985 <u>or, where applicable, international accounting standards</u> as at the <i>firm's annual accounting reference date</i> together with an <i>auditor's report</i> thereon;
--	--

...

### Interim Prudential Requirements for Former IMRO Firms

#### 5 CHAPTER 5: FINANCIAL RESOURCES

...

#### APPENDIX 1 (INTERPRETATION)

#### GLOSSARY OF TERMS FOR CHAPTER 5 (FORMER IMRO FIRMS)

Term	Meaning
...	
<i>contingent liability</i>	<del>has the meaning in FRS 12 which states that it is: ...</del>
...	
<i>parent</i>	means any parent undertaking as defined in section 258 of the Companies Act 1985 <del>or paragraph 14 of Financial Reporting Standard No 2</del> and any undertaking which effectively exercises a dominant influence over another undertaking.
...	

**10 Chapter 10: Financial resources for Securities and Futures Firms which are Investment Firms**

...

**APPENDIX 1 – GLOSSARY OF TERMS FOR IPRU(INV) 10**

...

*audited annual financial statements* means statements drawn up in accordance with Schedule 4 to the Companies Act 1985 or, where applicable, international accounting standards as at the *firm's annual accounting reference date* together with an *auditor's report* thereon;

...

*parent* means any parent undertaking as defined in section 258 of the Companies Act 1985 ~~or paragraph 14 of Financial Reporting Standard No.2~~ and any undertaking which effectively exercises a dominant influence over another undertaking;

...

**Chapter 13: Financial Resource Requirements for Personal Investment Firms**

...

**APPENDIX 13 (1)**

**Defined terms for Chapter 13**

...

*market value* the market value as determined in accordance with ~~United Kingdom~~ generally accepted accounting practice.

## Annex E

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Part 1

#### Amendments taking effect on 1 January 2005

#### SUP 16 Annex 2G Form BSD3 REPORTING INSTRUCTIONS

...

#### APPENDIX A-IV - CURRENT YEAR'S PROFIT & LOSS ACCOUNT

...

#### 80 Dividends/share of profits from subsidiary and associated companies

Reporting institutions reporting on an unconsolidated basis should include the dividends from other group companies only, together with the revaluation of any investment in subsidiaries or associates if equity accounting; those reporting on a consolidated basis should include only the share of profits from associates ~~companies according to the normal convention of accounting as currently set out in Financial Reporting Standard 9, "Accounting for the Results of Associated Entities"~~.

...

#### SUP 16 Annex 2G Supervisory Guidance Notes (SGN)

...

Closely related counterparties

#### 12 ...

An undertaking (~~as defined in Financial Reporting Standard 2, Paragraph 14~~) is the parent undertaking of another undertaking (a subsidiary undertaking) if any of the following (from section 2598, Companies Act 1985) apply....

Connected counterparties

#### 13 Parties connected to the reporting institution comprise:-

(i) ...

(ii) associates ~~companies as defined in the Statement of Standard Accounting Practice 1 (SSAP1) Financial Reporting Standard 9 (FRS 9) or in International Accounting Standard 28 (IAS 28);~~

...

**SUP 16 Annex 4G Form MFS 1 GUIDANCE NOTES**

**BUILDING SOCIETY: MONTHLY STATEMENT**

**INTRODUCTION: GENERAL NOTES ON THE RETURN**

...

**7(ii) Foreign currencies**

...Societies should apply the same accounting treatment as for the published accounts having regard to SSAP 20 or IAS 21.

...

**SUP 16 Annex 4G Form QFS 1 GUIDANCE NOTES**

**BUILDING SOCIETY: QUARTERLY STATEMENT**

**INTRODUCTION: GENERAL NOTES ON THE RETURN**

...

**8(iii) Foreign currencies**

...Societies should apply the same accounting treatment as for the published accounts having regard to SSAP 20 or IAS 21.

...

**SUP 16 Annex 4G Form AFS 1 GUIDANCE NOTES**

**BUILDING SOCIETY: ANNUAL STATEMENT**

**INTRODUCTION: GENERAL NOTES ON THE RETURN**

...

**8(ii) Foreign currencies**

...Societies should apply the same accounting treatment as for the published accounts having regard to SSAP 20 or IAS 21.

...

**SUP Ann 10R : Securities and Futures Firms' Reporting Forms and Requirements Applying to their Completion**

...

**Section 6: Securities and futures firms: Form and content of reports**

...

3 Table Audited Annual Financial Statements

...

1.1.2 A firm's audited annual financial statements must be drawn up in accordance with Schedule 4 of the Companies Act 1985 or, where applicable, international accounting standards as at the firm's accounting reference date.

4	Table	Accounting policies for financial reporting statements and audited annual financial statements
---	-------	--

**General rule**

- 1.1.3 (1) Unless otherwise provided in the *rules*, and subject to (2) below, a *firm* must determine amounts included in respect of items shown in a *firm*'s financial reporting statements and audited annual financial statements in accordance with this rule and the accounting principles and rules which the *firm* would apply if it were drawing up financial statements under the Companies Act 1985 including those accounting principles and rules contained in the United Kingdom Statements of Standard Accounting Practice (SSAPs) and Financial Reporting Standards (FRSs) or, where applicable, *international accounting standards* effective at the relevant time.

...

**SUP 16 Annex 11G Section 4**

**Guidance on the completion of LEM Forms for securities and futures firms which are ISD firms**

**1 SUMMARY OF REPORTING REQUIREMENTS**

(1)...

(2) The amount at risk

The amount of risk should, with certain exceptions ... unless an alternative format is indicated within these reporting instructions.

~~Completion of the return should be in accordance with UK accepted accounting standards and practice subject to the paragraph above.~~

## Part 2

### Amendments taking effect on 1 April 2005

#### SUP 16 Ann 18BG NOTES FOR COMPLETION OF THE RETAIL MEDIATION ACTIVITIES RETURN (RMAR)

##### Introduction: general notes on the RMAR

...

##### Accounting Principles

15. The following principles should be adhered to by *firms* in the submission of financial information (sections A to E).

- (a) Unless a rule requires otherwise, amounts to be reported within the *firm's* balance sheet and profit and loss account should be determined in accordance with:
  - (i) ...
  - (ii) UK generally accepted accounting practice (UK GAAP). ~~This is set out in the Financial Reporting Standards and Statements of Standard Accounting Practice issued or adopted by the Accounting Standards Board; or, where applicable, international accounting standards;~~

## Annex F

### Amendments to the Electronic Money sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

5 Systems and controls

5.5 Rules for making calculations

...

Accounting policy for the ELM financial rules

5.5.2 R Except as otherwise provided for in *ELM*, and subject to *ELM 5.5.3R*, a *firm* must determine amounts included in the calculations required by the *ELM financial rules* in accordance with the accounting principles and rules which the *firm* would apply if it were drawing up financial statements under the Companies Act 1985 including those accounting principles and rules contained in the United Kingdom Statements of Standard Accounting Practice (SSAPs) and Financial Reporting Standards (FRSs) or, where applicable, *international accounting standards* effective at the relevant time.



## Annex G

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

...	
<i><u>international accounting standards</u></i>	<u>means the international accounting standards, within the meaning of EC Regulation No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards, adopted from time to time by the European Commission in accordance with that Regulation.</u>
...	
<i>market value</i>	The market value as determined in accordance with <del>United Kingdom</del> generally accepted accounting practice.

**ENLARGEMENT OF EU (DEFINITION OF ZONE A) INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power); and
  - (2) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 January 2005.

**Amendments to the Handbook**

- D. The modules of the FSA’s Handbook of rules and guidance listed in Column (1) below are amended in accordance with the Annexes to this instrument listed in Column (2).

(1)	(2)
Interim Prudential sourcebook for Investment Businesses (IPRU(INV))	Annex A
Interim Prudential sourcebook for Banks (IPRU(BANK))	Annex B
Interim Prudential sourcebook for Building Societies (IPRU(BSOC))	Annex C
Supervision manual (SUP)	Annex D
Glossary of definitions	Annex E

**Citation**

- E. This instrument may be cited as the Enlargement of EU (Definition of Zone A) Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### Amendments to the Interim Prudential sourcebook for Investment Businesses

In this Annex underlining indicates new text and striking through indicates deleted text.

Chapter 3: Financial resources for Securities and Futures Firms which are not Investment Firms

#### APPENDIX 1 – GLOSSARY OF TERMS FOR IPRU(INV) 3

...

*EEA State*

means ~~(in accordance with paragraph 8 of Schedule 3 to the Act (EEA Passport Rights)) a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992, as it has effect for the time being; as at 21 June 2001, the following are the EEA States: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden and the United Kingdom; see definition of EEA State in the Glossary;~~

...

*zone A*

means ~~any country which is a full member of the OECD or has concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow, provided it has not rescheduled its external sovereign debt to official or commercial bank creditors in the previous five years (Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany (including any pre-unification claims on East Germany), Greece, Hungary, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Portugal, Saudi Arabia, South Korea, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States, the Channel Islands, Gibraltar, Bermuda and the Isle of Man) see definition of Zone A country in the Glossary; and~~

...

Chapter 5: Financial Resources  
APPENDIX 1 (INTERPRETATION)  
GLOSSARY OF TERMS FOR CHAPTER 5 (FORMER IMRO FIRMS)

...

*EEA State*

means (in accordance with paragraph 8 of Schedule 3 to the *Act* (EEA Passport Rights)) a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992, as it has effect for the time being; as at 21 June 2001, the following are the *EEA States*: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden and the United Kingdom; see definition of *EEA State* in the *Glossary*;

...

*zone a country*

means a country which is a member of the *OECD*, or which has negotiated special lending arrangements with the IMF.

**Note:** Countries which currently fall within this definition are Australia, Austria, Belgium, Bermuda, Canada, Denmark, Finland, France, Germany, Gibraltar, Greece, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, The Netherlands, New Zealand, Norway, Portugal, Saudi Arabia, Spain, Sweden, Switzerland, Turkey, *UK*, Channel Islands, Isle of Man and United States.

**Note:** For the purpose of determining whether a bank is in a *zone a* or *zone b* country, the place of incorporation is the relevant factor to be considered rather than the location of the branch. see definition of *Zone A country* in the *Glossary*

...

Chapter 10: Financial resources for Securities and Futures Firms which are Investment Firms  
APPENDIX 1 – GLOSSARY OF TERMS FOR IPRU(INV) 10

...

*EEA State*

means (in accordance with paragraph 8 of Schedule 3 to the *Act* (EEA Passport Rights)) a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992, as it has effect for the time being; as at 21 June 2001, the following are the *EEA States*: Austria, Belgium, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Italy, Liechtenstein, Luxembourg, the Netherlands, Norway, Portugal, Spain, Sweden and the United Kingdom; see definition of *EEA State* in the *Glossary*;

...

*Zone A*

~~means any country which is a full member of the *OECD* or has concluded special lending arrangements with the IMF associated with the IMF's General Arrangements to Borrow, provided it has not rescheduled its external sovereign debt to official or commercial bank creditors in the previous five years (Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany (including any pre-unification claims on East Germany), Greece, Hungary, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Portugal, Saudi Arabia, South Korea, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States, the Channel Islands, Gibraltar, Bermuda and the Isle of Man)see definition of Zone A country in the Glossary; and~~

...

...

## Annex B

### Amendments to the Interim Prudential sourcebook for Banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

Volume 1, Adequacy of Capital, Specific banking book treatments, BC Credit risk in the banking book, Section 3 Risk Weighting Framework: On Balance Sheet

...

#### 3.2.8 Zone A/ Zone B countries

10

~~The term “*Zone A*” covers full members of the Organisation for Economic Co-operation and Development (OECD), and those countries which have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the IMF’s General Agreement to Borrow (GAB), provided they have not rescheduled their external sovereign debt, to official or private sector creditors, in the previous five years. This group of countries is extended automatically to include any new countries which join the OECD, provided they meet the rescheduling criterion, from the date of their submission. *one A countries* now comprise: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany (including pre-reunification claims on East Germany), Greece, Hungary, Iceland, Ireland, Italy, Japan, South Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Saudi Arabia, Spain, Sweden, Switzerland, Turkey, United Kingdom, and USA. For the definition of *Zone A country* see the *Glossary*~~

...

## Annex C

### Amendments to the Interim Prudential sourcebook for Building Societies

In this Annex underlining indicates new text and striking through indicates deleted text.

#### 1 SOLVENCY

##### Annex 1G Definitions of Zone A and Zone B Countries

###### *1G.1.1*

~~Member States of the European Community and all other countries which are full members of the Organisation for Economic Co-operation and Development (OECD) and those countries which have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the Fund's General Arrangements to Borrow (GAB). Any country which reschedules its external sovereign debt is however, precluded from Zone A for a period of 5 years. Zone A countries currently comprise Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany (including pre-unification claims on East Germany), Greece, Hungary, Iceland, Ireland, Italy, Japan, South Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Saudi Arabia, Spain, Sweden, Switzerland, Turkey, United Kingdom and USA. For the definition of Zone A country see the Handbook Glossary.~~

...

...

## Annex D

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

SUP 16 Annex 2G: Guidance notes on completion of banks' reporting forms (including validations)

Supervisory Guidance Notes (SGN)

...

Appendix C

Zone A/Zone B countries

~~The term “Zone A” covers full members of the OECD and those countries which have concluded special lending arrangements with the IMF associated with the IMF’s General Arrangements to Borrow, provided they have not rescheduled their external sovereign debt to official or commercial bank creditors in the previous five years. At present, these countries comprise:~~

~~Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Saudi Arabia, Spain, South Korea, Sweden, Switzerland, Turkey, United Kingdom and United States.~~

For the definition of *Zone A country* see the *Glossary*.

...

Appendix D

Central banks (central monetary institutions)

...

Bulgaria	Bulgarian Foreign Trade Bank
Poland	Bank Handlowy w Warszawie (non-UK offices only)

Reporting institutions may however classify ~~FTBs as Zone B banks~~ the Bulgarian FTB as a Zone B bank and the Polish FTB as a Zone A bank, if they so wish, and should notify the FSA if they do so.

European Union

...

Belgium	Banque Nationale de Belgique, SA
<u>Cyprus</u>	<u>Central Bank of Cyprus</u>
<u>Czech Republic</u>	<u>Czech National Bank (Ceská Národní Banka)</u>
Denmark and Greenland	Danmarks Nationalbank
<u>Estonia</u>	<u>Bank of Estonia (Eesti Pank)</u>
Finland	Suomen Pankki - Finlands Bank

...



Greece	Bank of Greece
<u>Hungary</u>	<u>National Bank of Hungary (Magyar Nemzeti Bank)</u>
Ireland	Central Bank and Financial Services Authority of Ireland
Italy	Banca d'Italia
	Ufficio Italiano dei Cambi
<u>Latvia</u>	<u>Bank of Latvia (Latvijas Banka)</u>
<u>Lithuania</u>	<u>The Bank of Lithuania (Lietuvos Bankas)</u>
Luxembourg	Institut Monétaire Luxembourgeois
<u>Malta</u>	<u>Central Bank of Malta</u>
Netherlands	De Nederlandsche Bank NV
<u>Poland</u>	<u>National Bank of Poland (Narodowy Bank Polski)</u>
Portugal	Banco de Portugal
<u>Slovakia, the Republic of</u>	<u>National Bank of Slovakia (Národná Banka Slovenska)</u>
<u>Slovenia</u>	<u>Banka Slovenije</u>
Spain	Banco de España
...	
Other Western Europe	
...	
Croatia	National Bank of Croatia
<del>Cyprus</del>	<del>Central Bank of Cyprus</del>
Gibraltar	The Commissioner of Currency
...	
Macedonia	National Bank of Macedonia
<del>Malta</del>	<del>Central Bank of Malta</del>
Norway	Norges Bank
<del>Slovenia</del>	<del>Banka Slovenije</del>
...	
Other OECD countries	
...	
Canada	Bank of Canada
<del>Czech Republic</del>	<del>Czech National Bank (Ceská Národní Banka)</del>
<del>Hungary</del>	<del>National Bank of Hungary (Magyar Nemzeti Bank)</del>
Iceland	Central Bank of Iceland (Sedlabanki Islands)
...	
Mexico	Banco de Mexico SA
<del>Poland</del>	<del>National Bank of Poland (Narodowy Bank Polski)</del>
New Zealand	Reserve Bank of New Zealand
United States	Federal Reserve System (comprising the Federal Reserve Board and 12 Federal Reserve banks)
Eastern Europe	
...	
Bulgaria	National Bank of Bulgaria (Bulgarska Narodna Banka)
	Bulgarian Foreign Trade Bank
<del>Estonia</del>	<del>Bank of Estonia (Eesti Pank)</del>
Georgia	National Bank of Georgia
Kazakhstan	National State Bank of Kazakhstan
<u>Kirgizstan (Kyrgyzstan)</u>	<u>National Bank of Kyrgyzstan</u>

<del>Latvia</del>	<del>Bank of Latvia (Latvijas Banka)</del>
<del>Lithuania</del>	<del>The Bank of Lithuania (Lietuvos Bankas)</del>
<del>...</del>	
<del>Russia</del>	<del>Central Bank of the Russian Federation</del>
<del>Slovakia, the Republic of</del>	<del>National Bank of Slovakia (Národná Banka Slovenska)</del>
<del>Tajikistan</del>	<del>National Bank of Tajikistan</del>
<del>...</del>	

## Annex E

### Amendments to the Glossary

In this Annex underlining indicates new text and striking through indicates deleted text.

...

~~*Zone A country*~~

~~any *EEA State* and any other country which is a full member of the *OECD* and any country which has concluded special lending arrangements with the International Monetary Fund associated with the Fund's General Arrangements to Borrow.~~

*Zone A country*

(a) any *EEA State*;

(b) all other countries which are full members of the *OECD*; and

(c) those countries which have concluded special lending arrangements with the International Monetary Fund (IMF) associated with the Fund's general arrangements to borrow (GAB).

save that any country falling with (a), (b) or (c) which reschedules its external sovereign debt is precluded from Zone A for a period of five years.

**INTEGRATED PRUDENTIAL SOURCEBOOK (INSURERS AND OTHER  
AMENDMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 141 (Insurance business rules);
  - (3) section 149 (Evidential provisions);
  - (4) section 150(2) (Actions for damages);
  - (5) section 156 (General supplementary powers); and
  - (6) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) PRU 8.3.15R in Annex J comes into force on 31 December 2006;
  - (2) subject to (3), the remainder of this instrument comes into force on 31 December 2004;
  - (3) paragraph E below comes into force on 1 December 2004.

**Amendments to the Integrated Prudential sourcebook**

- D. The Integrated Prudential sourcebook is amended:
- (1) by inserting new chapters or sections of chapters, as listed in column (1) of the following table, in accordance with the Annexes to this instrument listed in column (2):

(1)	(2)
PRU 1.2	Annex A
PRU 1.3	Annex B
PRU 1.4	Annex C
PRU 2	Annex D
PRU 3	Annex E
PRU 4	Annex F
PRU 5	Annex G
PRU 6	Annex H
PRU 7	Annex I
PRU 8.3	Annex J

- (2) in accordance with Annex K to this instrument.

**Revocation**

- E. Annex E to the Financial Conglomerates and Other Financial Groups Instrument 2004 is revoked.

**Citation**

- F. This instrument may be cited as the Integrated Prudential Sourcebook (Insurers and Other Amendments) Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### PRU 1.2

In this Annex, all the text is new and is not underlined.

#### 1.2 Adequacy of financial resources

##### Application

- 1.2.1 R This section applies to an *insurer* unless *PRU 1.2.7R* applies.
- 1.2.2 R (1) In relation to *liquidity risk* only, this section applies to a *firm* in *PRU 1.2.3R* unless *PRU 1.2.7R* applies.
- (2) *Liquidity risk* includes the systems, processes and resources required by this section in respect of *liquidity risk*.
- 1.2.3 R The *firms* referred to in *PRU 1.2.2R(1)* are:
- (1) a *building society*;
- (2) a *bank* or an *own account dealer* (other than a *venture capital firm*) that is a *UK firm*;
- (3) an *incoming EEA firm* which:
- (a) is a *full BCD credit institution*; and
- (b) has a *branch* in the *United Kingdom*;
- (4) an *overseas firm* which is a *bank* or an *own account dealer* (other than a *venture capital firm*) but which is not:
- (a) an *incoming EEA firm*; or
- (b) a *lead-regulated firm*;
- (5) an *overseas firm* which:
- (a) is a *bank*;
- (b) is a *lead-regulated firm*;
- (c) is not an *incoming EEA firm*; and
- (d) has a *branch* in the *United Kingdom*.
- 1.2.4 R For a *firm* described in *PRU 1.2.3R(3)* or *PRU 1.2.3R(5)*, this section applies only with respect to the *branch*.

- 1.2.5 R This section applies to an *incoming EEA firm* only to the extent that the relevant matter is not reserved by the relevant *Single Market Directive* to the *firm's Home State regulator*.
- 1.2.6 R If a *firm* carries on:
- (1) *long-term insurance business*; and
  - (2) *general insurance business*;
- this section applies separately to each type of business.
- 1.2.7 R This section does not apply to:
- (1) a *non-directive friendly society*; or
  - (2) a *Swiss general insurer*; or
  - (3) an *EEA-deposit insurer*; or
  - (4) a *UCITS qualifier*; or
  - (5) an *ICVC*; or
  - (6) an *incoming EEA firm* (unless *PRU 1.2.3R* applies); or
  - (7) an *incoming Treaty firm*.
- 1.2.8 G The *guidance* in *PRU 1.2* is drafted with respect to a *firm* to which *PRU 1.2* and the other provisions of *PRU* referred to in *PRU 1.2* apply in full. The *guidance* in *PRU 1.2* is also applicable to a *firm* that falls into *PRU 1.2.2R*. However the *guidance* in *PRU 1.2*, as it applies to such a *firm*, should be read accordingly. In particular, the *guidance* in *PRU 1.2* only applies to such a *firm* in respect of *liquidity risk*.
- 1.2.9 G In the case of an *incoming EEA firm* that is a *full BCD credit institution* and of an *overseas firm* that is a *lead-regulated firm*, *PRU 1.2* only applies to its *United Kingdom branch*. However, as a *branch* is not itself a legal entity separate from the rest of a *firm*, this restriction does not mean that the rest of the *firm* can necessarily be left out of account when considering compliance with *PRU 1.2*. For example, the availability of the *branch's* liquidity resources may be affected by general liquidity problems in the *firm*. Likewise, there may be liquidity resources elsewhere in the *firm* that are available to meet liquidity problems in the *branch*.
- 1.2.10 G One factor that may affect the degree to which it is necessary to take into account the *firm* as a whole is the extent to which the *firm* manages the liquidity of the *branch* on an autonomous basis, or includes the *branch* within integrated liquidity management of the *firm* as a whole. In the latter case, for instance, the requirement in *PRU 1.2.35R* to carry out scenario analyses may be satisfied by the *firm* meeting similar requirements set by the regulator in its home country in respect of the *firm* as whole, provided that the *firm* separately identifies the impacts on the *United Kingdom branch* of the scenarios analysed. However, in the case of a *full BCD*

*credit institution*, the application of *PRU 1.2* is further restricted by *PRU 1.2.5R*.

- 1.2.11 G The scope of application of *PRU 1.2* is not restricted to *firms* that are subject to the relevant EC Directives. It applies, for example, to *pure reinsurers*.
- 1.2.12 G The adequacy of a *firm's* financial resources needs to be assessed in relation to all the activities of the *firm* and the risks to which they give rise.
- 1.2.13 G The requirements in *PRU 1.2* apply to a *firm* on a solo basis.

#### Purpose

- 1.2.14 G This section amplifies *Principle 4*, under which a *firm* must maintain adequate financial resources. It is concerned with the adequacy of the financial resources which a *firm* needs to hold in order to be able to meet its liabilities as they fall due. These resources include both capital and liquidity resources. *PRU 2* sets out provisions relating to the adequacy of *capital resources*. *PRU 5* contains provisions relating to liquidity.
- 1.2.15 G This section therefore introduces *rules* requiring a *firm* to identify and assess risks to its being able to meet its liabilities as they fall due, how it intends to deal with those risks, and the amount and nature of financial resources the *firm* considers necessary. These assessments should be documented so that they can be easily reviewed by the *FSA* as part of the *FSA's* assessment of the adequacy of *capital resources*.
- 1.2.16 G This section also introduces *rules* requiring a *firm* to carry out appropriate stress tests and scenario analyses for the risks it has previously identified and to establish the amount of financial resources needed in each of the circumstances and events considered in carrying out the stress tests and scenario analyses.
- 1.2.17 G The adequacy of a *firm's capital resources* needs to be assessed both by the *firm* and the *FSA*. This is done, by the *FSA*, through comparing the *firm's capital resource requirements* with its *capital resources* and by review of a *firm's* processes and systems for assessing capital needs, the results of the *firm's* assessments, and other information available to the *FSA* on the risks faced by the *firm*.

#### Outline of other related provisions

- 1.2.18 G *PRU 2.1* sets out the minimum *capital resources requirements* for a *firm*. *PRU 2.2* sets out how *capital resources* are defined and measured for the purpose of meeting the requirements of *PRU 2.1*.
- 1.2.19 G *PRU 2.3* sets out detailed *guidance* on how *firms* could assess the adequacy of their *capital resources* both to comply with the *rules* set out in this section and to enable the *FSA* to assess better whether the minimum *capital resources requirements* of *PRU 2.1* are appropriate. The more thorough, objective, and prudent a *firm's* capital assessment is and can be demonstrated as being, the more reliance the *FSA* will be able to place on the results of that assessment. The *FSA* will consider the appropriateness of the *firm's* capital assessment to establish the level of *capital resources* the *firm* needs. This may result in the *FSA's* assessment of a *firm's*



*capital resources* needs being lower or higher than would otherwise be the case.

1.2.20 G *PRU 5.1* sets out general systems and controls provisions for *liquidity risk*.

1.2.21 G *PRU 1.4* sets out *rules* and *guidance* on the establishment and maintenance of systems and controls.

#### Main Requirements

1.2.22 R A *firm* must at all times maintain overall financial resources, including *capital resources* and liquidity resources, which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.

1.2.23 G The liabilities referred to in *PRU 1.2.22R* include contingent and prospective liabilities that a *firm* has potentially incurred. It therefore excludes liabilities that might arise from transactions that a *firm* has not entered into and which it could avoid, for example, by ceasing to trade. It includes liabilities or costs that arise as a consequence of strategies other than continuing as a going concern. It also includes claims that could be made against a *firm*, which ought to be paid in accordance with fair treatment of *customers*, even if such claims could not be legally enforced.

1.2.24 G A *firm* should therefore make its assessment of adequate financial resources on realistic valuation bases for assets and liabilities taking into account the actual amounts and timing of cash flows under realistic adverse projections. This does not require a *firm* to hold financial resources sufficient to ensure that any particular margin of financial resources is maintained under such adverse projections.

1.2.25 G Risks may be addressed through holding capital to absorb losses that unexpectedly materialise. The ability to pay liabilities as they fall due also requires liquidity. Therefore, in assessing the adequacy of a *firm's* financial resources, both capital and liquidity needs should be considered. *PRU 5.1.86E* is an *evidential provision* relating to *PRU 1.2.22R* concerning *contingency funding plans*. A *firm* should also consider the quality of its financial resources such as the loss-absorbency of different types of capital and the time required to liquidate different types of asset.

1.2.26 R A *firm* must carry out regular assessments of the adequacy of its financial resources using processes and systems which comply with *PRU 1.2.27R*.

1.2.27 R The processes and systems required by *PRU 1.2.26R* must be proportionate to the nature, scale and complexity of the *firm's* activities.

1.2.28 G *PRU 1.2.27R* amplifies the requirement in *SYSC 3.2.6R*.

1.2.29 G The processes and systems are required for a *firm's* internal assessment of the adequacy of its financial resources. The appropriateness of the internal process, and the degree of involvement of senior management in the process, will be taken into account by the *FSA* when reviewing a *firm's* assessment as part of the *FSA's* own assessment of the adequacy of a *firm's* financial resources. The processes and systems should ensure that the assessment of the adequacy of a *firm's* financial resources is reported to its senior management as often as is necessary. In addition,

a *firm* would be expected to reassess the adequacy of its financial resources should the *firm* experience some material change to the nature or scale of its activities.

- 1.2.30 G The assessments undertaken by *firms in run-off* may not need to be as comprehensive or frequent compared to a *firm* not in run off since this may better reflect the reduced nature and complexity of its business and reduced access to new capital. Whilst a *firm in run-off* will still need to carefully monitor the progress of the run off, a more comprehensive assessment may only be appropriate on commencement of the run off or when considering a reduction in capital through the payment of a dividend or other capital distribution or if the *firm's* circumstances change materially.
- 1.2.31 R The processes and systems required by *PRU 1.2.26R* must enable the *firm* to identify the major sources of risk to its ability to meet its liabilities as they fall due, including the major sources of risk in each of the following categories:
- (1) credit risk;
  - (2) *market risk*;
  - (3) *liquidity risk*;
  - (4) operational risk; and
  - (5) insurance risk.
- 1.2.32 G In *PRU 1.2.31R*:
- (1) operational risk refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events; and
  - (2) insurance risk refers to the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities.
- 1.2.33 R The processes and systems required by *PRU 1.2.26R* must enable the *firm* to carry out an assessment of how it intends to deal with each of the major sources of risk identified in accordance with *PRU 1.2.31R*.
- 1.2.34 G Certain risks such as systems and controls weaknesses may not be adequately addressed by, for example, holding additional capital and a more appropriate response would be to rectify the weakness. In such circumstances, the amount of financial resources required to address these risks, which may not be adequately addressed by holding additional capital, will be zero. However, a *firm* must, in accordance with *PRU 1.2.37R*, document the approaches taken to manage these risks.
- 1.2.35 R For each of the major sources of risk identified in accordance with *PRU 1.2.31R*, the *firm* must carry out stress tests and scenario analyses that are appropriate to the nature of those major sources of risk, as part of which the *firm* must:
- (1) take reasonable steps to identify an appropriate range of realistic adverse

circumstances and events in which the risk identified crystallises; and

- (2) estimate the financial resources the *firm* would need in each of the circumstances and events considered in order to be able to meet its liabilities as they fall due.
- 1.2.36 G Stress tests and scenario analyses should be carried out at least annually. A *firm* should, however, consider whether the nature of the major sources of risks identified by it in accordance with *PRU* 1.2.31R and their possible impact on its financial resources suggest that such tests and analyses should be carried out more frequently. For instance, a sudden change in the economic outlook may prompt a *firm* to revise the parameters of some of its stress tests and scenario analyses. Similarly, if a *firm* has recently become exposed to a particular sectoral concentration, it may wish to add some stress tests and scenario analyses in order to reflect that concentration. *PRU* 5.1.61E is an *evidential provision* relating to *PRU* 1.2.35R concerning scenario analysis in relation to *liquidity risk*.
- 1.2.37 R A *firm* must make a written record of its assessment of the adequacy of its financial resources, including:
- (1) the major sources of risk identified in accordance with *PRU* 1.2.31R;
  - (2) how it intends to deal with those risks; and
  - (3) details of the stress tests and scenario analyses carried out and the resulting financial resources estimated to be required in accordance with *PRU* 1.2.35R.
- 1.2.38 R A *firm* must retain the records of its assessment of the adequacy of its financial resources for at least three years.
- 1.2.39 G Where a *firm* follows the *guidance* set out in *PRU* 2.3.35G to *PRU* 2.3.48G and assesses the adequacy of the *capital resources requirement (CRR)* in its particular circumstances as a basis for deciding what financial resources are adequate, it should include this in the documentation produced in accordance with *PRU* 1.2.37R.

#### Stress tests and scenario analyses

- 1.2.40 G A large part of the process of managing a *firm* is based on an understanding of the expected outcomes of its business operations and outside events and the normal variation about these expected outcomes. To gain a comprehensive view of the risks being run by a *firm*, an analysis of extreme events is also needed. Such analysis may take the form of stress tests and scenario analyses. For example, a *firm* may normally expect interest rates to increase or decrease by 1 or 2 percentage points due to normal variations in economic conditions. However, in some extreme circumstances, interest rates may change by a much greater amount. The use of stress tests and scenario analyses can give a *firm's* management a better understanding of the *firm's* true exposure in extreme circumstances.
- 1.2.41 G Stress testing typically refers to shifting the values of individual parameters that affect the financial position of a *firm* and determining the effect on the *firm's*

business.

- 1.2.42 G Scenario analysis typically refers to a wider range of parameters being varied at the same time. Scenario analyses often examine the impact of catastrophic events on the *firm's* financial position, for example, simultaneous movements in a number of risk categories affecting all of a *firm's* business operations such as business volumes, investment values and interest rate movements.
- 1.2.43 G Scenarios generally could also be considered under three broad categories. For example, changes to the business plan, scenarios that involve changes in business cycles and those relating to extreme events. The scenarios can be derived in a variety of ways including stochastic models, analysis of historic experience or a repetition of an historical event. Scenarios can be developed with varying degrees of precision and depth.
- 1.2.44 G Both stress tests and scenario analyses can be undertaken by *firms* to further a better understanding of the vulnerabilities that they face under extreme conditions. They are based on the analysis of the impact of unlikely, but not impossible, events. These events can be financial, operational, legal or relate to any other risk that might have an economic impact on the *firm*.
- 1.2.45 G *PRU 1.2.35R* requires a *firm*, as part of carrying out stress tests and scenario analyses, to take reasonable steps to identify an appropriate range of realistic circumstances and events in which a risk would crystallise. In particular:
- (1) a *firm* need only carry out stress tests and scenario analyses in so far as the circumstances or events are reasonably foreseeable, that is to say, their occurrence is not too remote a possibility; and
  - (2) a *firm* should also take into account the relative costs and benefits of carrying out the stress tests and scenario analyses in respect of the circumstances and events identified.
- 1.2.46 G The purpose of stress tests and scenario analyses is to test the adequacy of overall financial resources. Scenarios need only be identified, and their impact assessed, in so far as this facilitates that purpose. In particular, the nature, depth and detail of the analysis depend, in part, upon the *firm's* capital strength and the robustness of its risk prevention and risk mitigation measures.
- 1.2.47 G Both stress testing and scenario analyses are prospective analysis techniques, which seek to anticipate possible losses that might occur if an identified risk crystallises. In applying them, a *firm* needs to decide how far forward to look. This should depend upon:
- (1) how quickly it would be able to identify events or changes in circumstances that might lead to a risk crystallising resulting in a loss; and
  - (2) after it has identified the event or circumstance, how quickly and effectively it could act to prevent or mitigate any loss resulting from the risk crystallising and to reduce exposure to any further adverse event or change in circumstance.

- 1.2.48 G The time horizon over which stress tests and scenario analysis would need to be carried out for the *market risk* arising from the holding of *investments*, for example, should depend upon:
- (1) the extent to which there is a regular, open and transparent market in those assets, which would allow fluctuations in the value of the *investment* to be more readily and quickly identified; and
  - (2) the extent to which the market in those assets is liquid (and would remain liquid in the changed circumstances contemplated in the stress test or scenario analysis) which would allow the *firm*, if needed, to sell its holding so as to prevent or reduce exposure to future price fluctuations.
- 1.2.49 G In identifying scenarios, and assessing their impact, a *firm* should take into account, where material, how changes in circumstances might impact upon:
- (1) the nature, scale and mix of its future activities; and
  - (2) the behaviour of *counterparties*, and of the *firm* itself, including the exercise of choices (for example, options embedded in financial instruments or *contracts of insurance*).
- 1.2.50 G In determining whether it would have adequate financial resources in the event of each identified realistic adverse scenario, a *firm* should:
- (1) only include financial resources that could reasonably be relied upon as being available in the circumstances of the identified scenario; and
  - (2) take account of any legal or other restriction on the purposes for which financial resources may be used.
- 1.2.51 G A *firm* should consider conducting stress tests and scenario analyses which enable it to assess its exposure not only in its current position in the economic and business cycles, but also the possible changes in the cycles which might be expected over, say, the next three to five years.
- 1.2.52 G A *firm* may consider scenarios in which expected future profits will provide capital reserves against future risks. However, it would only be appropriate to take into account profits that can be foreseen with some certainty as arising before the risk against which they are being held could possibly arise. In estimating future reserves, a *firm* should deduct future dividend payment estimates from projections of future profits.
- 1.2.53 G A *firm* may substitute for traditional stress tests and scenario analyses more sophisticated modelling techniques and this approach is acceptable providing major risks are identified and the modelling has the effect of calculating the effect on a *firm's* financial position where the risks crystallise or are assumed to crystallise with a particular probability.
- 1.2.54 G Additional *guidance* on stress tests and scenario analyses for the assessment of *capital resources* is available in *PRU 2.3*.

- 1.2.55 G Additional *guidance* in relation to stress tests and scenario analysis for *liquidity risk* is available in *PRU 5.1.58G* to *PRU 5.1.62G*.

## Annex B

### PRU 1.3

In this Annex, all the text is new and is not underlined.

#### 1.3 Valuation

##### Application

- 1.3.1 R *PRU 1.3* applies to an *insurer*, unless it is:
- (1) a *non-directive friendly society*; or
  - (2) an *incoming EEA firm*; or
  - (3) an *incoming Treaty firm*.
- 1.3.2 G The scope of application of *PRU 1.3* is not restricted to *firms* that are subject to relevant EC directives. It applies, for example, to *pure reinsurers*.
- 1.3.3 R (1) *PRU 1.3* applies to a *firm* in relation to the whole of its business.
- (2) Where a *firm* carries on both *long-term insurance business* and *general insurance business*, *PRU 1.3* applies separately to each type of business.

##### Purpose

- 1.3.4 G *PRU 1.3* sets out, for the purposes of *PRU*, *rules* and *guidance* as to how a *firm* should recognise and value assets, liabilities, equity and income statement items. Except where a *rule* in *PRU* makes different provision, *PRU 1.3* applies whenever a *rule* in *PRU* refers to the value or amount of an asset, liability, equity or income statement item

##### General requirements: accounting principles to be applied

- 1.3.5 R Except where a *rule* in *PRU* provides for a different method of recognition or valuation, whenever a *rule* in *PRU* refers to an asset, liability, equity or income statement item, a *firm* must, for the purpose of that *rule*, recognise the asset, liability, equity or income statement item and measure its value in accordance with:
- (1) the *insurance accounts rules*, or the Friendly Societies (Accounts and Related Provisions) Regulations 1994;
  - (2) Financial Reporting Standards and Statements of Standard Accounting Practice issued or adopted by the Accounting Standards Board; and
  - (3) Statements of Recommended Practice, issued by industry or sectoral bodies recognised for this purpose by the Accounting Standards Board;

as applicable to the *firm* (or as would be applicable if the *firm* were a company with its head office in the *United Kingdom*).

- 1.3.6 G *PRU* 1.3.5R provides that unless a *rule* in *PRU* provides for a different method of recognition or valuation, the applicable provisions of the Companies Act 1985, the Companies Act (Northern Ireland) Order 1986 or the Friendly Societies (Accounts and Related Provisions) Regulations 1994, as supplemented by Financial Reporting Standards, Statements of Standard Accounting Practice, and Statements of Recommended Accounting Practice, should be used to determine the recognition and valuation of assets, liabilities, equity and income statement items for the purposes of *PRU*, including:
- (1) whether, and when, to recognise or de-recognise an asset or liability;
  - (2) the amount at which to value an asset, liability, equity or income statement item;
  - (3) which description to place on an asset, liability, equity or income statement item.
- 1.3.7 G In particular, unless an exception applies, *PRU* 1.3.5R should be applied for the purposes of *PRU* to determine how to account for:
- (1) netting of amounts due to or from the *firm*;
  - (2) the securitisation of assets and liabilities (see also *PRU* 1.3.8G);
  - (3) leased tangible assets;
  - (4) assets transferred or received under a *sale and repurchase* or *stock lending* transaction; and
  - (5) assets transferred or received by way of initial or variation margin under a *derivative* or similar transaction.
- 1.3.8 G Where assets or liabilities are securitised, *PRU* 1.3.5R only permits de-recognition where Financial Reporting Standard 5 permits either de-recognition or the linked presentation. However, the *FSA* will consider granting a *waiver* to permit de-recognition in other circumstances provided that the *firm* can demonstrate that securitisation has effectively transferred risk
- 1.3.9 G Specific provisions for the methods and assumptions to be used by a *firm* in calculating its *mathematical reserves* are made in *PRU* 7.3.
- 1.3.10 G *PRU* 1.3.5R implements the requirements of Articles 23.3(viii) and 24.2(iv) of the *Consolidated Life Directive*. These articles require assets of a *firm* that are managed on its behalf by a *subsidiary undertaking* to be taken into account for the purposes of determining the *firm's admissible assets* and its assets in excess of concentration limits. The application of *PRU* 1.3.5R will result in such assets remaining on the balance sheet of the *firm*.



## Investments, derivatives and quasi-derivatives

- 1.3.11 R Subject to *PRU* 1.3.31R, for the purposes of *PRU*, a *firm* must apply *PRU* 1.3.12R to *PRU* 1.3.30R in order to determine how to account for:
- (1) *investments* that are, or amounts owed arising from the disposal of:
    - (a) *debt securities*, bonds and other money- and capital-market instruments; or
    - (b) loans; or
    - (c) *shares* and other variable yield participations; or
    - (d) *units* in *UCITS schemes*, *non-UCITS retail schemes*, *recognised schemes* and any other *collective investment scheme* that invests only in *admissible assets* (including any *derivatives* or *quasi-derivatives* held by the scheme); and
  - (2) *derivatives* and *quasi-derivatives*.

## Marking to market

- 1.3.12 R Wherever possible, a *firm* must use mark to market in order to measure the value of the *investments* referred to in *PRU* 1.3.11R. Marking to market is valuation at readily available close out prices from independent sources.
- 1.3.13 G For the purposes of *PRU* 1.3.12R, examples of readily available close out prices include exchange prices, screen prices, or quotes from several independent reputable brokers.
- 1.3.14 R When marking to market, a *firm* must use the more prudent side of bid/offer price unless the *firm* is a significant market maker in a particular position type and it can close out at the mid-market price.

## Marking to model

- 1.3.15 R Where marking to market is not possible, a *firm* must use mark to model in order to measure the value of the *investments* referred to in *PRU* 1.3.11R. Marking to model is any valuation which has to be benchmarked, extrapolated or otherwise calculated from a market input.
- 1.3.16 R When the model used is developed by the *firm*, that model must be:
- (1) based on appropriate assumptions which have been assessed and challenged by suitably qualified parties independent of the development process; and
  - (2) independently tested, including validation of the mathematics, assumptions, and software implementation.
- 1.3.17 R A *firm* must ensure that its senior management are aware of the positions which are subject to mark to model and understand the materiality of the uncertainty this

creates in the reporting of the performance of the business of the *firm* and the risks to which it is subject.

- 1.3.18 R A *firm* must source market inputs in line with market prices so far as possible and assess the appropriateness of the market inputs for the position being valued and the parameters of the model on each valuation date.
- 1.3.19 R A *firm* must use generally accepted valuation methodologies for particular products where these are available.
- 1.3.20 R A *firm* must establish formal change control procedures, hold a secure copy of the model, and periodically use that model to check valuations.
- 1.3.21 R A *firm* must ensure that its risk management functions are aware of the weakness of the models used and how best to reflect those in the valuation output.
- 1.3.22 R A *firm* must periodically review the model to determine the accuracy of its performance.
- 1.3.23 G Examples of periodical review are assessing the continued appropriateness of the assumptions and comparison of actual close out values to model inputs.

#### Independent price verification

- 1.3.24 R In addition to marking to market or marking to model, a *firm* must perform independent price verification. This is the process by which market prices or model inputs are regularly verified for accuracy and independence.
- 1.3.25 G For independent price verification, where independent pricing sources are not available or pricing sources are more subjective, for example, only one available broker quote, prudent measures such as valuation adjustments may be appropriate.

#### Valuation adjustments or reserves

- 1.3.26 R A *firm* must establish and maintain procedures for considering valuation adjustments or reserves. These procedures must be compliant with the requirements set out in *PRU* 1.3.29R.
- 1.3.27 R A *firm* using third-party valuations, or marking to model, must consider whether valuation adjustments are necessary.
- 1.3.28 R A *firm* must consider the need for establishing reserves for less liquid positions and, on an ongoing basis, review their continued appropriateness in accordance with the requirements set out in *PRU* 1.3.29R.
- 1.3.29 R The requirements referred to in *PRU* 1.3.26R and *PRU* 1.3.28R are:
  - (1) a *firm* must consider the following adjustments or reserves: unearned credit spreads, close-out costs, operational risks, early termination, investing and funding costs, future administrative costs and, where appropriate, model risk; and

- (2) a *firm* must consider several factors when determining whether a valuation reserve is necessary for less liquid items. These factors include the amount of time it would take to hedge out the position/risks within the position; the average and volatility of bid/offer spreads; the availability of market quotes (number and identity of market makers); and the average and volatility of trading volumes.

1.3.30 R If the result of establishing adjustments or reserves under *PRU* 1.3.26R to *PRU* 1.3.29R is a valuation which differs from the fair value determined in accordance with Financial Reporting Standards issued or adopted by the Accounting Standards Board, a *firm* must reconcile the two valuations.

Shares in, and debts due from, related undertakings

1.3.31 R *PRU* 1.3.11R does not apply to *shares* in, and *debts* due from, a *related undertaking* that is:

- (1) a *regulated related undertaking*; or
- (2) an *ancillary services undertaking*; or
- (3) any other *subsidiary undertaking*, the *shares* of which a *firm* elects to value in accordance with *PRU* 1.3.35R.

1.3.32 G The effect of *PRU* 1.3.31R is that *shares* in, and *debts* due from, *related undertakings* of the types referred to are not valued on a mark to market basis. As a result, *debts* due from these *undertakings*, and *shares* in *related undertakings* which are *ancillary services undertakings*, are valued at their accounting book value in accordance with *PRU* 1.3.5R. *Shares* in *related undertakings* referred to in *PRU* 1.3.31R(1) or (3) are valued in accordance with *PRU* 1.3.33R to *PRU* 1.3.38R.

1.3.33 R Except where the contrary is expressly stated in *PRU*, whenever a rule in *PRU* refers to *shares* held in, and *debts* due from, an *undertaking* referred to in *PRU* 1.3.31R(1) or *PRU* 1.3.31R(3), a *firm* must value the *shares* held in accordance with *PRU* 1.3.35R.

1.3.34 R In relation to *shares* in, and *debts* due from, an *undertaking* referred to in *PRU* 1.3.31R(1), *PRU* 1.3.33R does not apply for the purposes of *PRU* 2.2.78R and *PRU* 8.3.

1.3.35 R For the purposes of *PRU* 1.3.33R, the value of the *shares* held in an *undertaking* referred to in *PRU* 1.3.31R(1) or *PRU* 1.3.31R(3) is the sum of:

- (1) the regulatory surplus value of that *undertaking*; less
- (2) for the purposes of *PRU* 2.2.90R, the book value of the total investments in the tier one capital resources and tier two capital resources of that *undertaking* by the *firm* and its *related undertakings*; or
- (3) for other purposes in *PRU*, the sum of:

- (a) the book value of the investments by the *firm* and its *related undertakings* in the tier two capital resources of the *undertaking*; and
  - (b) if the *undertaking* is an *insurance undertaking*, its ineligible surplus capital and any restricted assets of the *undertaking* which have been excluded under *PRU* 8.3.41R(1).
  
- 1.3.36 R For the purposes of *PRU* 1.3.35R(1), the regulatory surplus value of an *undertaking* referred to in *PRU* 1.3.31R(1) or *PRU* 1.3.31R(3) is, subject to *PRU* 1.3.37R, the sum of:
  - (1) the tier one capital resources of the *undertaking*; plus
  - (2) the tier two capital resources of the *undertaking*; less
  - (3) the individual capital resources requirement of the *undertaking*.
  
- 1.3.37 R (1) Subject to *PRU* 1.3.38R, for the purposes of *PRU* 1.3.36R, only the relevant proportion of the:
  - (a) tier one capital resources of the *undertaking*;
  - (b) tier two capital resources of the *undertaking*;
  - (c) individual capital resources requirement of the *undertaking*;
 is to be taken into account.
  - (2) In (1), the relevant proportion is the proportion of the total number of *shares* issued by the *undertaking* held, directly or indirectly, by the *firm*.
  
- 1.3.38 R If the individual capital resources requirement of an *undertaking* in *PRU* 1.3.31R(1) that is a *subsidiary undertaking* exceeds the sum of its tier one capital resources and tier two capital resources, the full amount of the items referred to in *PRU* 1.3.37R(1) are to be taken into account for the purposes of *PRU* 1.3.36R.
  
- 1.3.39 R For the purposes of *PRU* 1.3.35R to *PRU* 1.3.38R:
  - (1) in relation to an *undertaking* referred to in *PRU* 1.3.31R(1):
    - (a) individual capital resources requirement has the meaning given by *PRU* 8.3.34R;
    - (b) the following expressions are to be construed in accordance with *PRU* 8.3.37R:
      - (i) tier one capital resources; and
      - (ii) tier two capital resources;
    - (c) ineligible surplus capital has the meaning given by *PRU* 8.3.67R;

(2) in relation to an *undertaking* referred to in PRU 1.3.31R(3), the following expressions are to be construed as if that *undertaking* were an *insurance holding company*:

- (a) individual capital resources requirement;
- (b) tier one capital resources; and
- (c) tier two capital resources.

- 1.3.40 G PRU 1.3.35R to PRU 1.3.39R set out several different valuation bases for a *firm's shares* in *related undertakings*. The regulatory surplus value (defined in PRU 1.3.36R) measures the *related undertaking's* own capital surplus or deficit. This is used: (i) in PRU 1.3.35R as a basis for calculating the impact on the *firm's* position of its investments in *related undertakings*; and (ii) in PRU 8.3 as a starting point for the calculation of ineligible surplus capital.
- 1.3.41 G PRU 1.3.35R determines how, for the purposes of the solo capital adequacy calculation of a *firm*, that *firm's capital resources* should be adjusted to take into account its investments in *related undertakings*.
- 1.3.42 G The *rules* that specify how, for the purposes of the adjusted solo capital calculation, a *firm* must incorporate its *related undertakings* into its *capital resources* and *capital resources requirement* are set out in PRU 8.3.

Community co-insurance operations: general insurance business

- 1.3.43 R Where a *relevant insurer* determines the amount of a liability in order to make provision for outstanding *claims* under a *Community co-insurance operation*, then, if the *leading insurer* has informed the *relevant insurer* of the amount of the provision made by the *leading insurer* for such *claims*, the amount determined by the *relevant insurer*:
- (1) must be at least as great as the amount of the provision made by the *leading insurer*; or
  - (2) in a case where it is not the practice in the *United Kingdom* to make such provision separately, must be sufficient, when all liabilities are taken into account, to include provision at least as great as that made by the *leading insurer* for such *claims*;

due regard being had in either case to the proportion of the risk covered by the *relevant insurer* and by the *leading insurer* respectively.

## Annex C

### PRU 1.4

In this Annex, all the text is new and is not underlined.

#### 1.4 Prudential risk management and associated systems and controls

##### Application

1.4.1 R *PRU 1.4* applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

1.4.2 R *PRU 1.4* applies to:

- (1) an *EEA-deposit insurer*; and
- (2) a *Swiss general insurer*;

only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

##### Purpose

1.4.3 G *PRU 1.4* sets out some *rules* and *guidance* on the establishment and maintenance of systems and controls for the management of a *firm's* prudential risks. A *firm's* prudential risks are those that can reduce the adequacy of its financial resources, and as a result may adversely affect confidence in the financial system or prejudice *consumers*. Some key prudential risks are credit, market, liquidity, operational, insurance and group risk.

1.4.4 G The purpose of *PRU 1.4* is to serve the *FSA's regulatory objectives* of consumer protection and market confidence. In particular, this section aims to reduce the risk that a *firm* may pose a threat to these *regulatory objectives*, either because it is not prudently managed, or because it has inadequate systems to permit appropriate senior management oversight and control of its business.

1.4.5 G Both adequate financial resources and adequate systems and controls are necessary for the effective management of prudential risks. A *firm* may hold financial resources to help alleviate the financial consequences of minor weaknesses in its systems and controls (to reflect possible impairments in the accuracy or timing of its identification, measurement, monitoring and control of certain risks, for example). However, financial resources cannot adequately compensate for significant weaknesses in a *firm's* systems and controls that could fundamentally undermine its ability to control its affairs effectively.

##### How to interpret PRU 1.4

- 1.4.6 G *PRU 1.4 is designed to amplify Principle 3 (Management and control) which requires that a firm take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems. PRU 1.4 is also designed to be complementary to SYSC 2, SYSC 3 and SYSC 3A in that it contains some additional rules and guidance on senior management arrangements and associated systems and controls for firms that could have a significant impact on the FSA's objectives in a prudential context.*
- 1.4.7 G In addition to supporting *PRIN* and *SYSC*, *PRU 1.4* lays the foundations for the more specific *rules* and *guidance* on the management of credit, market, liquidity, operational, insurance and group risks that are in *PRU 3.1*, *PRU 4.1*, *PRU 5.1*, *PRU 6.1*, *PRU 7.1* and *PRU 8.1* respectively. Many of the elements raised here in general terms are expanded upon in these sections.
- 1.4.8 G Appropriate systems and controls for the management of prudential risk will vary from *firm* to *firm*. Therefore most of the material in *PRU 1.4* is *guidance*. In interpreting this *guidance*, a *firm* should have regard to its own particular circumstances. Following from *SYSC 3.1.2G*, this should include considering the nature, scale and complexity of its business, which may be influenced by factors such as:
- (1) the diversity of its operations, including geographical diversity;
  - (2) the volume and size of its transactions; and
  - (3) the degree of risk associated with each area of its operation.
- 1.4.9 G The *guidance* contained within this section is not designed to be exhaustive. When establishing and maintaining its systems and controls a *firm* should have regard not only to other parts of the *Handbook*, but also to material that is issued by other industry or regulatory bodies.

#### The role of systems and controls in a prudential context

- 1.4.10 G In a *prudential context*, a *firm's* systems and controls should provide its senior management with an adequate means of managing the *firm*. As such, they should be designed and maintained to ensure that senior management is able to make and implement integrated business planning and risk management decisions on the basis of accurate information about the risks that the *firm* faces and the financial resources that it has.

#### The prudential responsibilities of senior management and the apportionment of those responsibilities

- 1.4.11 G Ultimate responsibility for the management of prudential risks rests with a *firm's governing body* and relevant *senior managers*, and in particular with those individuals that undertake the *firm's governing functions* and the *apportionment and oversight function*. In particular, these responsibilities should include:
- (1) overseeing the establishment of an appropriate business plan and risk management strategy;
  - (2) overseeing the development of appropriate systems for the management of prudential risks;

- (3) establishing adequate *internal controls*; and
- (4) ensuring that the *firm* maintains adequate financial resources.

The delegation of responsibilities within the firm

- 1.4.12 G Although authority for the management of a *firm's* prudential risks is likely to be delegated, to some degree, to individuals at all levels of the organisation, overall responsibility for this activity should not be delegated from its *governing body* and relevant *senior managers*.
- 1.4.13 G Where delegation does occur, a *firm* should ensure that appropriate systems and controls are in place to allow its *governing body* and relevant *senior managers* to participate in and control its prudential risk management activities. The *governing body* and relevant *senior managers* should approve and periodically review these systems and controls to ensure that delegated duties are being performed correctly.

Firms subject to risk management on a group basis

- 1.4.14 G Some *firms* organise the management of their prudential risks on a stand-alone basis. In some cases, however, the management of a *firm's* prudential risks may be entirely or largely subsumed within a whole *group* or *sub-group* basis.
- (1) The latter arrangement may still comply with the *FSA's* prudential policy on systems and controls if the *firm's governing body* formally delegates the functions that are to be carried out in this way to the *persons* or bodies that are to carry them out. Before doing so, however, the *firm's governing body* should have explicitly considered the arrangement and decided that it is appropriate and that it enables the *firm* to meet the *FSA's* prudential policy on systems and controls. The *firm* should notify the *FSA* if the management of its prudential risks is to be carried out in this way.
  - (2) Where the management of a *firm's* prudential risks is largely, but not entirely, subsumed within a whole *group* or *sub-group* basis, the *firm* should ensure that any prudential issues that are specific to the *firm* are:
    - (a) identified and adequately covered by those to whom it has delegated certain prudential risk management tasks; or
    - (b) dealt with by the *firm* itself.



- 1.4.15 G Any delegation of the management of prudential risks to another part of a *firm's group* does not relieve it of responsibility for complying with the *FSA's* prudential policy on systems and controls. A *firm* cannot absolve itself of such a responsibility by claiming that any breach of the *FSA's* prudential policy on systems and controls is effected by the actions of a third party *firm* to whom the *firm* has delegated tasks. The risk management arrangements are still those of the *firm*, even though personnel elsewhere in the *firm's group* are carrying out these functions on its behalf. Thus any references in *PRU* to what a *firm*, its personnel and its management should and should not do still apply, and do not need any adjustment to cover the situation in which risk management functions are carried out on a *group-wide* basis.
- 1.4.16 G Where it is stated in *PRU* that a particular task in relation to a *firm's* systems and controls should be carried out by a *firm's governing body* this task should not be delegated to another part of its *group*. Furthermore, even where the management of a *firm's* prudential risks is delegated as described in *PRU* 1.4.14G, responsibility for its effectiveness and for ensuring that it remains appropriate remains with the *firm's governing body*. The *firm's governing body* should therefore keep any delegation under review to ensure that delegated duties are being performed correctly.

#### Business planning and risk management

- 1.4.17 G Business planning and risk management are closely related activities. In particular, the forward-looking assessment of a *firm's* financial resources needs, and of how business plans may affect the risks that it faces, are important elements of prudential risk management. A *firm's* business planning should also involve the creation of specific risk policies which will normally outline a *firm's* strategy and objectives for, as appropriate, the management of its market, credit, liquidity, operational, insurance and group risks and the processes that it intends to adopt to achieve these objectives. *PRU* 1.4.18R to *PRU* 1.4.25G set out some *rules and guidance* relating to business planning and risk management in a *prudential context* (see also *SYSC* 3.2.17G, which states that a *firm* should plan its business appropriately).
- 1.4.18 R A *firm* must take reasonable steps to ensure the establishment and maintenance of a business plan and appropriate systems for the management of prudential risk.
- 1.4.19 R When establishing and maintaining its business plan and prudential risk management systems, a *firm* must document:
- (1) an explanation of its overall business strategy, including its business objectives;
  - (2) a description of, as applicable, its policies towards market, credit (including provisioning), liquidity, operational, insurance and group risk (that is, its risk policies), including its appetite or tolerance for these risks and how it identifies, measures or assesses, monitors and controls these risks;

- (3) the systems and controls that it intends to use in order to ensure that its business plan and risk policies are implemented correctly;
  - (4) a description of how the *firm* accounts for assets and liabilities, including the circumstances under which items are netted, included or excluded from the *firm's* balance sheet and the methods and assumptions for valuation;
  - (5) appropriate financial *projections* and the results of its stress testing and scenario analysis (see *PRU 1.2 Adequacy of financial resources*); and
  - (6) details of, and the justification for, the methods and assumptions used in financial *projections* and stress testing and scenario analysis.
- 1.4.20 G The prudential risk management systems referred to in *PRU 1.4.18R* and *PRU 1.4.19R* are the means by which a *firm* is able to:
- (1) identify the prudential risks that are inherent in its business plan, operating environment and objectives, and determine its appetite or tolerance for these risks;
  - (2) measure or assess its prudential risks;
  - (3) monitor its prudential risks; and
  - (4) control or mitigate its prudential risks.
- PRU 5.1.78E* is an *evidential provision* relating to *PRU 1.4.18R* concerning risk management systems in respect of *liquidity risk* arising from substantial exposures in foreign currencies.
- 1.4.21 G A *firm* should consider the relationship between its business plan, risk policies and the financial resources that it has available (or can readily access), recognising that decisions made in respect of one element may have consequences for the other two.
- 1.4.22 G A *firm's* business plan and risk management systems should be:
- (1) effectively communicated so that all *employees* and contractors understand and adhere to the procedures related to their own responsibilities;
  - (2) regularly updated and revised, in particular when there is significant new information or when actual practice or performance differs materially from the documented strategy, policy or systems.
- 1.4.23 G The level of detail in a *firm's* business plan and its approach to the design of its risk management systems should be appropriate to the scale and complexity of its operations, and the nature and degree of risk that it faces.
- 1.4.24 G A *firm's* business plan and systems documentation should be accessible to the *firm's* management in line with their respective responsibilities and, upon request, to the *FSA*.

- 1.4.25 G *PRU 1.4.19R(5)* requires a *firm* to *document* its financial projections and the results of its stress testing and scenario analysis. Such financial projections, stress tests and scenario analysis should be used by a *firm's governing body* and relevant *senior managers* when deciding upon how much risk the *firm* is willing to accept in pursuit of its business objectives and how risk limits should be set. Further *rules* and *guidance* on stress testing and scenario analysis are outlined in *PRU 1.2* (Adequacy of financial resources) and *PRU 5.1* (Liquidity risk systems and controls).

Internal controls: introduction

- 1.4.26 G *Internal controls* should provide a *firm* with reasonable assurance that it will not be hindered in achieving its objectives, or in the orderly and legitimate conduct of its business, by events that may reasonably be foreseen. More specifically in a *prudential context*, *internal controls* should be concerned with ensuring that a *firm's* business plan and risk management systems are operating as expected and are being implemented as intended. The following *rule* (*PRU 1.4.27R*) reflects the importance of *internal controls* in a *prudential context*.
- 1.4.27 R A *firm* must take reasonable steps to establish and maintain adequate *internal controls*.
- 1.4.28 G The precise role and organisation of *internal controls* can vary from *firm* to *firm*. However, a *firm's internal controls* should normally be concerned with assisting its *governing body* and relevant *senior managers* to participate in ensuring that it meets the following objectives:
- (1) safeguarding both the assets of the *firm* and its *customers*, as well as identifying and managing liabilities;
  - (2) maintaining the efficiency and effectiveness of its operations;
  - (3) ensuring the reliability and completeness of all accounting, financial and management information; and
  - (4) ensuring compliance with its internal policies and procedures as well as all applicable laws and regulations.
- 1.4.29 G When determining the adequacy of its *internal controls*, a *firm* should consider both the potential risks that might hinder the achievement of the objectives listed in *PRU 1.4.28G*, and the extent to which it needs to control these risks. More specifically, this should normally include consideration of:
- (1) the appropriateness of its reporting and communication lines (see *SYSC 3.2.2G*);
  - (2) how the delegation or contracting of functions or activities to *employees*, *appointed representatives* or other third parties (for example *outsourcing*) is to be monitored and controlled (see *SYSC 3.2.3G* to *SYSC 3.2.4G*, *PRU 1.4.12G* to *PRU 1.4.16G* and *PRU 1.4.33G*; additional *guidance* on the management of *outsourcing* arrangements is also provided in *SYSC 3A.9*);
  - (3) the risk that a *firm's employees* or contractors might accidentally or deliberately breach a *firm's* policies and procedures (see *SYSC 3A.6.3G*);

- (4) the need for adequate segregation of duties (see *SYSC 3.2.5G* and *PRU 1.4.30G* to *PRU 1.4.33G*);
- (5) the establishment and control of risk management committees (see *PRU 1.4.34G* to *PRU 1.4.37G*);
- (6) the need for risk assessment and the establishment of a risk assessment function (see *SYSC 3.2.10G* and *PRU 1.4.38G* to *PRU 1.4.41G*); and
- (7) the need for internal audit and the establishment of an internal audit function and audit committee (see *SYSC 3.2.15G* to *SYSC 3.2.16G* and *PRU 1.4.42G* to *PRU 1.4.45G*).

Internal controls: segregation of duties

- 1.4.30 G The effective segregation of duties is an important internal control in the *prudential context*. In particular, it helps to ensure that no one individual is completely free to commit a *firm's* assets or incur liabilities on its behalf. Segregation can also help to ensure that a *firm's governing body* receives objective and accurate information on financial performance, the risks faced by the *firm* and the adequacy of its systems. In this regard, a *firm* should ensure that there is adequate segregation of duties between *employees* involved in:
- (1) taking on or controlling risk (which could include risk mitigation);
  - (2) risk assessment (which includes the identification and analysis of risk); and
  - (3) internal audit.
- 1.4.31 G In addition, a *firm* should normally ensure that no single individual has unrestricted authority to do all of the following:
- (1) initiate a transaction;
  - (2) bind the *firm*;
  - (3) make payments; and
  - (4) account for it.
- 1.4.32 G Where a *firm* is unable to ensure the complete segregation of duties (for example, because it has a limited number of staff), it should ensure that there are adequate compensating controls in place (for example, frequent review of an area by relevant *senior managers*).
- 1.4.33 G Where a *firm* outsources a *controlled function*, such as *internal audit*, it should take reasonable steps to ensure that every individual involved in the performance of this service is independent from the individuals who perform its external audit. This should not prevent services from being undertaken by a *firm's* external auditors provided that:
- (1) the work is carried out under the supervision and management of the *firm's* own internal staff; and
  - (2) potential conflicts of interest between the provision of external audit services and the provision of *controlled functions* are properly managed.

Internal controls: risk management committees

- 1.4.34 G In many *firms*, especially if there are multiple business lines, it is common for the *governing body* to delegate some tasks related to risk control and management to committees such as asset and liability committees (ALCO), credit risk committees and market risk committees.
- 1.4.35 G Where a *firm* decides to create one or more risk management committee(s), adequate *internal controls* should be put in place to ensure that these committees are effective and that their actions are consistent with the objectives outlined in *PRU* 1.4.28G. This should normally include consideration of the following:
- (1) setting clear terms of reference, including membership, reporting lines and responsibilities of each committee;
  - (2) setting limits on their authority;
  - (3) agreeing routine reporting and non-routine escalation procedures;
  - (4) agreeing the minimum frequency of committee meetings; and
  - (5) reviewing the performance of these risk management committees.
- 1.4.36 G The decision to delegate risk management tasks, along with the terms of reference of the committees and their performance, should be reviewed periodically by the *firm's governing body* and revised as appropriate.
- 1.4.37 G The effective use of risk management committees can help to enhance a *firm's internal controls*. In establishing and maintaining its risk management committees, a *firm* should consider:
- (1) their membership, which should normally include relevant *senior managers* (such as the head of group risk, head of legal, and the heads of market, credit, liquidity and operational risk, etc.), business line managers, risk management personnel and other appropriately skilled people, for example, actuaries, lawyers, accountants, IT specialists, etc.;
  - (2) using these committees to:
    - (i) inform the decisions made by a *firm's governing body* regarding its appetite or tolerance for risk taking;
    - (ii) highlight risk management issues that may require attention by the *governing body*;
    - (iii) consider risk at the firm-wide level and, within delegated limits, to determine the allocation of risk limits and financial resources across business lines;
    - (iv) consider how exposures may be unwound, hedged, or otherwise mitigated, as appropriate.

Internal controls: risk assessment

- 1.4.38 G Risk assessment is the process through which a *firm* identifies and analyses (using both qualitative and quantitative methodologies) the risks that it faces. A *firm's* risk assessment activities should normally include consideration of:
- (1) its total exposure to risk at the firm-wide level (that is, its exposure across business lines and risk categories);
  - (2) capital allocation and the need to calculate risk weighted returns for different business lines;

- (3) the potential correlations that can exist between the risks in different business lines; this should also include looking for risks to which a *firm's* business plan is particularly sensitive, such as interest rate risk, or multiple dealings with the same *counterparty*;
  - (4) the use of stress tests and scenario analysis;
  - (5) whether there are risks inherent in the *firm's* business that are not being addressed adequately;
  - (6) the risk adjusted return that the *firm* is achieving; and
  - (7) the adequacy and timeliness of management information on market, credit, insurance, liquidity, operational and group risks from the business lines, including risk limit utilisation.
- 1.4.39 G In accordance with SYSC 3.2.10G a *firm* should consider whether it needs to set up a separate *risk assessment function* (or functions) that is responsible for assessing the risks that the *firm* faces and advising its *governing body* and *senior managers* on them.
- 1.4.40 G Where a *firm* does decide that it needs a separate *risk assessment function*, the *employees* or contractors that carry out this function should not normally be involved in risk taking activities such as business line management (see PRU 1.4.30G to PRU 1.4.33G on the segregation of duties).
- 1.4.41 G A summary of the results of the analysis undertaken by a *firm's risk assessment function* (including, where necessary, an explanation of any assumptions that were adopted) should normally be reported to relevant *senior managers* as well as to the *firm's governing body*.
- Internal audit
- 1.4.42 G A *firm* should ensure that it has appropriate mechanisms in place to assess and monitor the appropriateness and effectiveness of its systems and controls. This should normally include consideration of:
- (1) adherence to and effectiveness of, as appropriate, its market, credit, liquidity, operational, insurance, and group risk policies;
  - (2) whether departures and variances from its documented systems and controls and risk policies have been adequately documented and appropriately reported, including whether appropriate pre-clearance authorisation has been sought for material departures and variances;
  - (3) adherence to and effectiveness of its accounting policies, and whether accounting records are complete and accurate;
  - (4) adherence to and effectiveness of its management reporting arrangements, including the timeliness of reporting, and whether information is comprehensive and accurate; and
  - (5) adherence to *FSA rules* and regulatory prudential standards.
- 1.4.43 G In accordance with SYSC 3.2.15G and SYSC 3.2.16G, a *firm* should consider whether it needs to set up a dedicated *internal audit function*.
- 1.4.44 G Where a *firm* decides to set up an *internal audit function*, this function should provide independent assurance to its *governing body*, audit committee or an appropriate *senior manager* of the integrity and effectiveness of its systems and controls.

- 1.4.45 G In forming its judgements, the *person* performing the *internal audit function* should test the practical operation of a *firm's* systems and controls as well as its accounting and risk policies. This should include examining the adequacy of supporting records.
- Management information
- 1.4.46 G Many individuals, at various levels of a *firm*, need management information relating to their activities. However, *PRU 1.4.47G* to *PRU 1.4.50G* concentrates on the management information that should be available to those at the highest level of a *firm*, that is, the *firm's governing body* and relevant *senior managers*. In so doing *PRU 1.4.47G* to *PRU 1.4.50G* amplifies *SYSC 3.2.11G* to *SYSC 3.2.12G* (which outlines the *FSA's* high level policy on senior management information) by providing some additional *guidance* on the management information that should be available in a *prudential context*.
- 1.4.47 G The role of management information should be to help a *firm's governing body* and *senior managers* to understand risk at a firm-wide level. In so doing, it should help them to:
- (1) determine whether a *firm* is prudently managed with adequate financial resources;
  - (2) make the decisions that fall within their ambit (for example, the high level business plans, strategy and risk tolerances of the *firm*); and
  - (3) oversee the execution of tasks for which they are responsible.
- 1.4.48 G A *firm* should consider what information needs to be made available to its *governing body* and *senior managers*. Some possible examples include:
- (1) firm-wide information such as the overall profitability and value of a *firm* and its total exposure to risk;
  - (2) reports from committees to which the *governing body* has delegated risk management tasks, if applicable;
  - (3) reports from a *firm's internal audit* and *risk assessment functions*, if applicable, including exception reports, where risk limits and policies have been breached or systems circumvented;
  - (4) financial projections under expected and abnormal (that is, stressed) conditions;
  - (5) reconciliation of actual profit and loss to previous financial projections and an analysis of any significant variances;
  - (6) matters which require a decision from the *governing body* or *senior managers*, for example a significant variation to a business plan, amendments to risk limits, the creation of a new business line, etc;
  - (7) compliance with *FSA rules* and regulatory prudential standards;
  - (8) risk weighted returns; and
  - (9) liquidity and funding requirements.
- 1.4.49 G The management information that is provided to a *firm's governing body* and *senior managers* should have the following characteristics:
- (1) it should be timely, its frequency being determined by factors such as:

- (a) the volatility of the business in which the *firm* is engaged (that is, the speed at which its risks can change);
  - (b) any time constraints on when action needs to be taken; and
  - (c) the level of risk that the *firm* is exposed to, compared to its available financial resources and tolerance for risk;
- (2) it should be reliable, having regard to the fact that it may be necessary to sacrifice a degree of accuracy for timeliness; and
  - (3) it should be presented in a manner that highlights any relevant issues on which those undertaking *governing functions* should focus particular attention.
- 1.4.50 G The production of management and other information may require the collation of data from a variety of separate manual and automated systems. In such cases, responsibility for the integrity of the information may be spread amongst a number of operational areas. A *firm* should ensure that it has appropriate processes to validate the integrity of its information.

Record keeping

- 1.4.51 G *SYSC 3.2.20R* requires a *firm* to take reasonable care to make and retain adequate records. The following policy on record keeping supplements *SYSC 3.2.20R* by providing some additional *rules* and *guidance* on record keeping in a *prudential context*. The purpose of this policy is to:
- (1) facilitate the prudential supervision of a *firm* by ensuring that adequate information is available regarding its past/current financial situation and business activities (which includes the design and implementation of systems and controls); and
  - (2) help the *FSA* to satisfy itself that a *firm* is operating in a prudent manner and is not prejudicing the interests of its *customers* or market confidence.
- 1.4.52 G In addition to the record keeping requirements in *PRU*, a *firm* should remember that it may be obliged, under other applicable laws or regulations, to keep similar or additional records.
- 1.4.53 R (1) A *firm* must make and regularly update accounting and other records that are sufficient to enable the *firm* to demonstrate to the *FSA*:
- (a) that the *firm* is financially sound and has appropriate systems and controls;
  - (b) the *firm's* financial position and exposure to risk (to a reasonable degree of accuracy); and
  - (c) the *firm's* compliance with the *rules* in *PRU*.
- (2) The records in (1) must be retained for a minimum of three years, or longer as appropriate.
- 1.4.54 G A *firm* should be able to make available the records described in *PRU 1.4.53R* within a reasonable timeframe when requested to do so by the *FSA*.



- 1.4.55 G The *FSA* recognises that not all records are specific to a particular point in time. As such, while it may be appropriate to update some records on a daily or continuous basis, for example expenditure and details of certain transactions, it may not be appropriate to update other records as regularly as this, for example those relating to its business plan and risk policies. A *firm* should decide how regularly it should update particular records.
- 1.4.56 G A *firm* should decide which records it needs to hold, noting that compliance with *PRU* 1.4.53R does not require it to hold records on every single aspect of its activities. Some specific *guidance* on the types of records that a *firm* should hold is set out in each of the risk specific sections on systems and controls (see *PRU* 3.1, *PRU* 4.1, *PRU* 5.1, *PRU* 6.1, *PRU* 7.1 and *PRU* 8.1).
- 1.4.57 G In deciding which records to hold, a *firm* should also take into account that failure to keep adequate records could make it harder for it to satisfy the *FSA* that it is compliant with the *rules* in *PRU*, and to defend any enforcement action taken against it.
- 1.4.58 G A *firm* should keep the records required in *PRU* in an appropriate format and language (in terms of format this could include holding them on paper or in electronic or some other form). However, whatever format or language a *firm* chooses, *SYSC* 3.2.20R requires that records be capable of being reproduced on paper and in English (except where they relate to business carried on from an establishment situated in a country where English is not an official language).
- 1.4.59 G In accordance with *SYSC* 3.2.20R, a *firm* should retain the records that it needs to comply with *PRU* 1.4.53R for as long as they are relevant for the purposes for which they were made.
- 1.4.60 R A *firm* must keep the *records* required in *PRU* 1.4.53R in the *United Kingdom*, except where:
- (1) they relate to business carried on from an establishment in a country or territory that is outside the *United Kingdom*; and
  - (2) they are kept in that country or territory.
- 1.4.61 R When a *firm* keeps the records required in *PRU* 1.4.53R outside the *United Kingdom*, it must periodically send an adequate summary of those records to the *United Kingdom*.
- 1.4.62 G Where a *firm* outsources the storage of some or all of its records to a third party service provider, it should ensure that these records are readily accessible and can be reproduced within a reasonable time period. The *firm* should also ensure that these records are stored in compliance with the *rules* and *guidance* on record keeping in *PRU*. Additional *guidance* on the management of *outsourcing* agreements is provided in *SYSC* 3A.
- 1.4.63 G A *firm* may rely on records that have been produced by a third party (for example, another *group* company or an external agent, such as an outsource service provider). However where the *firm* does so it should ensure that these records are readily accessible and can be reproduced within a reasonable time period. The *firm* should also ensure that these records comply with the *rules* and *guidance* on record keeping in *PRU*.

- 1.4.64 G In accordance with SYSC 3.2.21G, a *firm* should have adequate systems and controls for maintaining the security of its records so that they are reasonably safeguarded against loss, unauthorised access, alteration or destruction.

## Annex D

### PRU 2

In this Annex, all the text is new and is not underlined.

- 2.1 Calculation of capital resources requirements
- Application
- 2.1.1 R *PRU 2.1* applies to an *insurer* unless it is:
- (1) a *non-directive friendly society*; or
  - (2) a *Swiss general insurer*; or
  - (3) an *EEA-deposit insurer*; or
  - (4) an *incoming EEA firm*; or
  - (5) an *incoming Treaty firm*.
- 2.1.2 G The scope of application of *PRU 2.1* is not restricted to *firms* that are subject to the relevant EC Directives. It applies, for example, to *pure reinsurers*.
- 2.1.3 R (1) *PRU 2.1* applies to a *firm* in relation to the whole of its business, except where a particular provision provides for a narrower scope.
- (2) Where a *firm* carries on both *long-term insurance business* and *general insurance business*, *PRU 2.1* applies separately to each type of business.
- 2.1.4 G The adequacy of a *firm's capital resources* needs to be assessed in relation to all the activities of the *firm* and the risks to which they give rise.
- 2.1.5 G The requirements in *PRU 2.1* apply to a *firm* on a solo basis.
- Purpose
- 2.1.6 G *Principle 4* requires a *firm* to maintain adequate financial resources. *PRU 2* sets out provisions that deal specifically with the adequacy of that part of a *firm's* financial resources that consists of *capital resources*. The adequacy of a *firm's capital resources* needs to be assessed both by the *firm* and the *FSA*. Through its *rules*, the *FSA* sets minimum *capital resources requirements* for *firms*. It also reviews a *firm's* own assessment of its capital needs, and the processes and systems by which that assessment is made, in order to see if the minimum *capital resources requirements* are appropriate (see *PRU 2.3.2G* to *PRU 2.3.3G*).
- 2.1.7 G This section (*PRU 2.1*) sets *capital resources requirements* for a *firm*. *PRU 2.2* sets out how, for the purpose of this, the amounts or values of capital, assets and liabilities are to be determined. More detailed *rules* relating to capital, assets and liabilities are also set out in the following chapters and sections:
- PRU 1.3* Valuation;
  - PRU 3* Credit risk;
  - PRU 4* Market risk;
  - PRU 5* Liquidity risk;
  - PRU 6* Operational risk;
  - PRU 7* Insurance risk; and
  - PRU 8* Group risk.
- PRU 2.1* and *PRU 2.2* include appropriate cross-references to these chapters and sections.
- 2.1.8 G *PRU 2.1* implements minimum EC standards for the *capital resources* required to be held by a *firm* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC) or the *First Non-Life Directive* (73/239/EEC) as amended.

## Main requirements

- 2.1.9 R (1) A *firm* must maintain at all times *capital resources* equal to or in excess of its *capital resources requirement (CRR)*.  
(2) A *firm* which is a *participating insurance undertaking* and, in relation to its own *group capital resources*, is in compliance with *PRU 8.3.9R*, is deemed to comply with (1).
- 2.1.10 R A *firm* must comply with *PRU 2.1.9R* separately in respect of both its *long-term insurance business* and its *general insurance business*.
- 2.1.11 G In order to comply with *PRU 2.1.10R*, a *firm* carrying on both *general insurance business* and *long-term insurance business* will need to allocate its *capital resources* between its *general insurance business* and *long-term insurance business* so that the *capital resources* allocated to its *general insurance business* are equal to or in excess of its *CRR* for its *general insurance business* and the *capital resources* allocated to its *long-term insurance business* are equal to or in excess of its *CRR* for its *long-term insurance business*. Whereas *long-term insurance assets* cannot be used towards meeting a *firm's CRR* for its *general insurance business*, surplus general insurance assets may be used towards meeting the *CRR* for its *long-term insurance business* (see *PRU 7.6.30R* to *PRU 7.6.32G*). *PRU 7.6* sets out the detailed requirements for the separation of *long-term* and *general insurance business*.
- 2.1.12 G *Firms* commonly use different terminology for the various *PRU* requirements. For example, the *MCR* is traditionally known as the required minimum margin.
- 2.1.13 G The *FSA* may impose a higher capital requirement than the minimum requirement set out in this section as part of the *firm's Part IV permission*. (See *PRU 2.3*).
- Calculation of the *CRR*
- 2.1.14 R The *CRR* for any *firm* carrying on *general insurance business* is equal to the *MCR* in *PRU 2.1.21R*.
- 2.1.15 R The *CRR* for any *firm* to which this *rule* applies (see *PRU 2.1.16R* and *PRU 2.1.17R*) is the higher of:  
(1) the *MCR* in *PRU 2.1.22R*; and  
(2) the *ECR* in *PRU 2.1.34R*.
- 2.1.16 R Subject to *PRU 2.1.17R*, *PRU 2.1.15R* applies to a *firm* carrying on *long-term insurance business*, other than:  
(1) a *non-directive mutual*;  
(2) a *firm* which has no *with-profits insurance liabilities*; and  
(3) a *firm* which has *with-profits insurance liabilities* that are, and at all times since 31 December 2004 (the coming into force of *PRU 2.1.15R*) have remained, less than £500 million.
- 2.1.17 R *PRU 2.1.15R* also applies to a *firm* of a type listed in *PRU 2.1.16R(3)* if:  
(1) the *firm* makes an election that *PRU 2.1.15R* is to apply to it; and  
(2) that election is made by written notice given to the *FSA* in a way that complies with the requirements for written notice in *SUP 15.7*.

- 2.1.18 G The effect of *PRU 2.1.16R(3)* is that a *firm* to which *PRU 2.1.15R* applies because it has *with-profits insurance liabilities* of £500 million or more, will continue to be subject to *PRU 2.1.15R* even if its *with-profits insurance liabilities* fall below £500 million. However, if that happens, it may apply for a *waiver* from *PRU 2.1.15R* under section 148 of the *Act*. In exercising its discretion under section 148 of the *Act*, the *FSA* will have regard (among other factors) to whether there has been a material and permanent change to the *firm's* business and to the prospects of it continuing to have *with-profits insurance liabilities* of less than £500 million.
- 2.1.19 G A *firm* that has always had *with-profits insurance liabilities* of less than £500 million since *PRU 2.1.15R* came into force may wish to “opt in” to *PRU 2.1.15R* and therefore become a *realistic basis life firm*. By doing so, it becomes obliged to calculate a *with-profits insurance capital component* (see *PRU 2.1.34R* and *PRU 7.4*), but it also becomes entitled to certain modifications to the way that a *firm* is required to calculate its *mathematical reserves* (see *PRU 7.3.46R* and *PRU 7.3.76R*). The *firm* is also then required to report its liabilities on a realistic basis (see *IPRU(INS)* rule 9.31R(b)). In order to “opt in”, the *firm* must make an election under *PRU 2.1.17R* that *PRU 2.1.15R* is to apply to it. If a *firm* that has elected to calculate and report its *with-profits insurance liabilities* on a realistic basis subsequently decides that it no longer wishes to do so, it may seek to “opt out” by applying for a *waiver* from *PRU 2.1.15R* under section 148 of the *Act*. In exercising its discretion under section 148 of the *Act*, the *FSA* will have regard (among other factors) to whether there has been a material and permanent change to the *firm's* business and to whether it continues to have *with-profits insurance liabilities* of less than £500 million.
- 2.1.20 R The *CRR* for a *firm* carrying on *long-term insurance business*, but to which *PRU 2.1.15R* does not apply, is equal to the *MCR* in *PRU 2.1.22R*.
- Calculation of the *MCR*
- 2.1.21 R For a *firm* carrying on *general insurance business*, the *MCR* in respect of that business is the higher of:
- (1) the *base capital resources requirement* for *general insurance business* applicable to that *firm*; and
  - (2) the *general insurance capital requirement*.
- 2.1.22 R For a *firm* carrying on *long-term insurance business*, the *MCR* in respect of that business is the higher of:
- (1) the *base capital resources requirement* for *long-term insurance business* applicable to that *firm*; and
  - (2) the sum of:
    - (a) the *long-term insurance capital requirement*; and
    - (b) the *resilience capital requirement*.
- 2.1.23 G The *MCR* gives effect to the EC Directive minimum requirements. For *general insurance business*, the EC Directive minimum is the higher of the *general insurance capital requirement* and the relevant *base capital resources requirement*. For *long-term insurance business*, the EC Directive minimum is the higher of the *long-term insurance capital requirement* and the *base capital resources requirement*. The *base capital resources requirement* is the minimum guarantee fund for the purposes of article 29(2) of the *Consolidated Life Directive* (2002/83/EC) and article 17(2) of the *First Non-Life Directive* (73/239/EEC) as amended. The *resilience capital requirement* is an *FSA* requirement that is additional to the EC minimum requirement for *long-term insurance business*.
- 2.1.24 G The calculation of the *resilience capital requirement* is set out in *PRU 4.2*.

Calculation of the base capital resources requirement

2.1.25 R The amount of a *firm's base capital resources requirement* is set out in Table 2.1.26R.

2.1.26 R Table: Base capital resources requirement

Firm type			Amount: Currency equivalent of
<i>General insurance business</i>			
	<i>Liability insurer (classes 10-15)</i>	<i>Directive mutual</i>	€2.25 million
		<i>Non-directive insurer</i>	€300,000
		<i>Overseas firm</i>	€1.5 million
		<i>Other</i>	€3 million
	<i>Other insurer</i>	<i>Directive mutual</i>	€1.5 million
		<i>Non-directive insurer (classes 1 to 8, 16 or 18)</i>	€225,000
		<i>Non-directive insurer (classes 9 or 17)</i>	€150,000
		<i>Overseas firm</i>	€1 million
		<i>Other</i>	€2 million
<i>Long-term insurance business</i>			
	<i>Mutual</i>	<i>Directive</i>	€2.25 million
		<i>Non-directive</i>	€600,000
	<i>Overseas firm</i>		€1.5 million
	<i>Any other insurer</i>		€3 million

2.1.27 R (1) Subject to (2) and (3), the amount of the *base capital resources requirement* specified in the last column of the table in *PRU 2.1.26R* for a *firm* which is not a *non-directive insurer* will increase each year, starting on the review date of 20 September 2005 (and annually after that), by the percentage change in the European index of consumer prices (comprising all EU member states, as published by Eurostat) from 20 March 2002, to the relevant review date, rounded up to a multiple of €100,000.

(2) In any year, if the percentage change since the last increase is less than 5%, then there will be no increase.

(3) The increase will take effect 30 days after the EU Commission has informed the European Parliament and Council of its review and the relevant percentage change.

2.1.28 G Any increases in the *base capital resources requirement* referred to in *PRU 2.1.27R* will be published on the *FSA* website.

2.1.29 R For the purposes of the *base capital resources requirement*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union.

Calculation of the general insurance capital requirement

- 2.1.30 R A *firm* must calculate its *general insurance capital requirement* as the highest of:
- (1) the *premiums amount*;
  - (2) the *claims amount*; and
  - (3) the *brought forward amount*.
- 2.1.31 G The calculation of each of the *premiums amount*, *claims amount* and *brought forward amount* is set out in *PRU 7.2*.
- Calculation of the long-term insurance capital requirement
- 2.1.32 R A *firm* must calculate its *long-term insurance capital requirement* as the sum of:
- (1) the *insurance death risk capital component*;
  - (2) the *insurance health risk capital component*;
  - (3) the *insurance expense risk capital component*; and
  - (4) the *insurance market risk capital component*.
- 2.1.33 G The calculation of each of the capital components is set out in *PRU 7.2*.
- Calculation of the ECR
- 2.1.34 R For a *firm* carrying on *long-term insurance business*, the *ECR* in respect of that business is the sum of:
- (1) the *long-term insurance capital requirement*;
  - (2) the *resilience capital requirement*; and
  - (3) the *with-profits insurance capital component*.
- 2.1.35 G Details of the *resilience capital requirement* and the *with-profits insurance capital component* are set out in *PRU 4.2* and *PRU 7.4* respectively.
- Monitoring requirements
- 2.1.36 R A *firm* must at all times monitor whether it is complying with *PRU 2.1.9R* and be able to demonstrate that it knows at all times whether it is complying with that *rule*.
- 2.1.37 G For the purposes of *PRU 2.1.36R*, a *firm* should have systems in place to enable it to be certain whether it has adequate *capital resources* to comply with *PRU 2.1.9R* at all times. This does not necessarily mean that a *firm* needs to measure the precise amount of its *capital resources* and its *CRR* on a daily basis. A *firm* should, however, be able to demonstrate the adequacy of its *capital resources* at any particular time if asked to do so by the *FSA*.
- 2.1.38 R A *firm* must notify the *FSA* immediately of any breach, or expected breach, of *PRU 2.1.9R*.

- 2.2 Capital resources
- Application
- 2.2.1 R *PRU 2.2* applies to an *insurer* unless it is:
- (1) a *non-directive friendly society*; or
  - (2) a *Swiss general insurer*; or
  - (3) an *EEA-deposit insurer*; or
  - (4) an *incoming EEA firm*; or
  - (5) an *incoming Treaty firm*.
- Purpose
- 2.2.2 G *PRU 2.1* sets out minimum *capital resources requirements* for a *firm*. This section (*PRU 2.2*) sets out how, for the purpose of these requirements, *capital resources* are defined and measured. *PRU 2.2* also implements minimum EC standards for the composition of *capital resources* required to be held by a *firm* undertaking business that falls within the scope of the *Consolidated Life Directive* (2002/83/EC) or the *First Non-Life Directive* (73/239/EEC) as amended.
- Principles underlying the definition of capital resources
- 2.2.3 G The *FSA* has divided its definition of capital into categories, or tiers, reflecting differences in the extent to which the capital instruments concerned meet the purpose and conform to the characteristics of capital listed in *PRU 2.2.5G*. The *FSA* generally prefers a *firm* to hold higher quality capital that meets the characteristics of permanency and loss absorbency that are features of *tier one capital*. Capital instruments falling into *core tier one capital* can be included in a *firm's* regulatory capital without limit. Typically, other forms of capital are either subject to limits (see *PRU 2.2.16R* to *PRU 2.2.26R*) or, in the case of some specialist types of capital, may only be included with the express consent of the *FSA* (which takes the form of a *waiver* under section 148 of the *Act*).
- 2.2.4 G Details of the individual components of capital are set out in *PRU 2.2.14R*.
- Tier one capital
- 2.2.5 G *Tier one capital* typically has the following characteristics:
- (1) it is able to absorb losses;
  - (2) it is permanent;
  - (3) it ranks for repayment upon winding up after all other debts and liabilities; and
  - (4) it has no fixed costs, that is, there is no inescapable obligation to pay dividends or interest.
- 2.2.6 G The forms of capital that qualify for *tier one capital* are set out in *PRU 2.2.14R* and include, for example, *share* capital, reserves, verified interim net profits and, for a *mutual*, the *initial fund* plus permanent members' accounts. *Tier one capital* is divided into *core tier one capital*, perpetual non-cumulative *preference shares*, and *innovative tier one capital*.
- Upper and lower tier two capital
- 2.2.7 G *Tier two capital* includes forms of capital that do not meet the requirements for permanency and absence of fixed servicing costs that apply to *tier one capital*. *Tier two capital* includes, for example:
- (1) capital which is perpetual (that is, has no fixed term) but cumulative (that is, servicing costs cannot be waived at the issuer's option, although they may be deferred – for example cumulative *preference shares*); perpetual capital instruments may be included in *upper tier two capital*; and



- (2) capital which is not perpetual (that is, it has a fixed term) and which may also have fixed servicing costs that cannot generally be either waived or deferred, for example subordinated debt. Such capital should normally be of a medium to long-term maturity (that is, an original maturity of at least five years). Dated capital instruments are included in *lower tier two capital*.

Deductions from capital

- 2.2.8 G Deductions should be made at the relevant stage of the calculation of *capital resources* to reflect capital that may not be available to the *firm* or assets of uncertain value, for example, holdings of intangible assets and assets that are inadmissible for a *firm*.
- 2.2.9 G A full list of deductions from *capital resources* is shown in PRU 2.2.14R.
- Calculation of capital resources
- 2.2.10 G *Capital resources* can be calculated either as the total of eligible assets less foreseeable liabilities (which is the approach taken in the *Insurance Directives*) or by identifying the components of capital. Both calculations give the same result for the total amount of *capital resources*. The approach taken in this section has been to specify the components of capital and the relevant deductions. This is set out in PRU 2.2.14R. This approach is the same as that used for the calculation of *capital resources* for *banks, building societies* and *investment firms*. A simple example, showing the reconciliation of the two methods, is given in PRU 2.2.11G.
- 2.2.11 G Table: Approaches to calculating capital resources

Liabilities		Assets	
Borrowings	100	Admissible assets	350
Ordinary <i>shares</i>	200	Intangible assets	100
Profit and loss account and other reserves	100	Other inadmissible assets	100
Perpetual subordinated debt	150		
Total	<u>550</u>	Total	<u>550</u>
Calculation of <i>capital resources</i> : eligible assets less foreseeable liabilities			
Total assets		550	
less intangible assets		(100)	
less inadmissible assets		(100)	
less liabilities (borrowings)		(100)	
<i>Capital resources</i>		<u>250</u>	
Calculation of <i>capital resources</i> : components of capital			
Ordinary <i>shares</i>		200	
Profit and loss account and other reserves		100	
Perpetual subordinated debt		150	
less intangible assets		(100)	
less inadmissible assets		(100)	
<i>Capital resources</i>		<u>250</u>	

- 2.2.12 R A *firm* must calculate its *capital resources* for the purpose of *PRU* in accordance with *PRU* 2.2.14R, subject to the limits in *PRU* 2.2.16R to *PRU* 2.2.26R.
- 2.2.13 G Where *PRU* 2.2.14R refers to related text, it is necessary to refer to that text in order to understand fully what is included in the descriptions of capital items and deductions set out in the table.
- 2.2.14 R Table: Capital resources (see *PRU* 2.2.12R)

	Related text	Included in the calculation of capital resources
		A ✓ denotes that the item is included in the calculation of a <i>firm's capital resources</i> ; a ✗ denotes that the item is not included in the calculation of a <i>firm's capital resources</i> .
<b>(A) Core tier one capital:</b>		
<i>Permanent share capital</i>	<i>PRU</i> 2.2.36R	✓
Profit and loss account and other reserves	<i>PRU</i> 2.2.76R and 2.2.77R	✓
<i>Share</i> premium account	None	✓
Externally verified interim net profits	<i>PRU</i> 2.2.82R	✓
Positive valuation differences	<i>PRU</i> 2.2.78R	✓
Fund for future appropriations	None	✓
<b>(B) Perpetual non-cumulative preference shares</b>		
Perpetual non-cumulative <i>preference shares</i>	<i>PRU</i> 2.2.50R	✓
<b>(C) Innovative tier one capital</b>		
<i>Innovative tier one instruments</i>	<i>PRU</i> 2.2.52R to 2.2.75R	✓
<b>(D) Total tier one capital before deductions = A + B + C</b>		
<b>(E) Deductions from tier one capital:</b>		
Investments in own <i>shares</i>	None	✓
Intangible assets	<i>PRU</i> 2.2.84R	✓
Amounts deducted from <i>technical provisions</i> for discounting and other negative valuation differences	<i>PRU</i> 2.2.78R to 2.2.81R	✓
<b>(F) Total tier one capital after deductions = D – E</b>		
<b>(G) Upper tier two capital:</b>		

	Related text	Included in the calculation of capital resources
Perpetual cumulative <i>preference shares</i>	<i>PRU</i> 2.2.101R	✓
Perpetual subordinated debt	<i>PRU</i> 2.2.101R	✓
Perpetual subordinated securities	<i>PRU</i> 2.2.101R	✓
(H) Lower tier two capital		
Fixed term <i>preference shares</i>	<i>PRU</i> 2.2.108R	✓
Fixed term subordinated debt	<i>PRU</i> 2.2.108R	✓
Fixed term subordinated securities	<i>PRU</i> 2.2.108R	✓
(I) Total tier two capital = G + H		
(J) Positive adjustments for related undertakings		
<i>Related undertakings that are regulated related undertakings (other than insurance undertakings)</i>	<i>PRU</i> 2.2.90R	✓
(K) Total capital after positive adjustments for regulated related undertakings that are not insurance undertakings but before deductions = F + I + J		
(L) Deductions from total capital		
Inadmissible assets	<i>PRU</i> 2.2.86R & <i>PRU</i> 2 Ann 1R	✓
Assets in excess of <i>market risk</i> and <i>counterparty</i> limits	<i>PRU</i> 3.2.22R	✓
<i>Related undertakings that are ancillary services undertakings</i>	<i>PRU</i> 2.2.89R	✓
Negative adjustments for <i>related undertakings that are regulated related undertakings (other than insurance undertakings)</i>	<i>PRU</i> 2.2.90R	✓
(M) Total capital after deductions = K – L		
(N) Other capital resources*:		
Unpaid <i>share</i> capital or, in the case of a <i>mutual</i> , <i>unpaid initial funds</i> and calls for supplementary contributions	<i>PRU</i> 2.2.126G to <i>PRU</i> 2.2.128G	✗
<i>Implicit items</i>	<i>PRU</i> 2 Ann 2G	✗
(O) Total capital resources after deductions = M + N		
* Items in section (N) of the table can be included in <i>capital resources</i> if subject to a <i>waiver</i> under section 148 of the <i>Act</i> .		

Limits on the use of different forms of capital

- 2.2.15 G As the various components of capital differ in the degree of protection that they offer the *firm* and its *customers*, restrictions are placed on the extent to which certain types of capital are eligible for inclusion in a *firm's capital resources*. These restrictions are set out in *PRU 2.2.16R* to *PRU 2.2.26R*.
- 2.2.16 R At least 50% of a *firm's MCR* must be accounted for by the sum of:  
(1) the amount calculated at stage A of the calculation in *PRU 2.2.14R*; and  
(2) notwithstanding *PRU 2.2.20R(1)*, the amount calculated at stage B of the calculation in *PRU 2.2.14R*;  
less the amount calculated at stage E of the calculation in *PRU 2.2.14R*.
- 2.2.17 R A *firm* carrying on *long-term insurance business* must meet the higher of:  
(1)  $\frac{1}{3}$  of the *long-term insurance capital requirement*; and  
(2) the *base capital resources requirement*;  
with the sum of the items listed at stages A, B, G and H less the sum of the items listed at stage E in *PRU 2.2.14R*.
- 2.2.18 R A *firm* carrying on *general insurance business* must meet the higher of:  
(1)  $\frac{1}{3}$  of the *general insurance capital requirement*; and  
(2) the *base capital resources requirement*;  
with the sum of the items listed at stages A, B, G and H less the sum of the items listed at stage E in *PRU 2.2.14R*.
- 2.2.19 G The purposes of the requirements in *PRU 2.2.16R* to *2.2.18R* are to comply with the *Insurance Directives'* requirement that *firms* maintain a *guarantee fund* of higher quality *capital resources* items and to ensure that at least 50% of the *firm's capital resources* needed to meet its *MCR* provide maximum loss absorbency to protect the *firm* from insolvency.
- 2.2.20 R In relation to a *firm's tier one capital resources* calculated at stage F of the calculation in *PRU 2.2.14R*:  
(1) at least 50% must be accounted for by *core tier one capital*; and  
(2) no more than 15% may be accounted for by *innovative tier one capital*.
- 2.2.21 G The purpose of the requirement in *PRU 2.2.20R(1)* is to ensure that at least 50% of the *firm's tier one capital resources* (net of *tier one capital* deductions) is met by *core tier one capital* which provides maximum loss absorbency on a going concern basis to protect the *firm* from insolvency. Although a perpetual non-cumulative *preference share* is in legal form a *share*, it behaves in many ways like a perpetual fixed interest debt instrument. Within the 50% limit on non-*core tier one capital*, *PRU 2.2.20R(2)* places a further sub-limit on the amount of *innovative tier one capital* that a *firm* may include in its *tier one capital resources*. This limit is necessary to ensure that most of a *firm's tier one capital* comprises items of capital of the highest quality.
- 2.2.22 G The amount of any capital item excluded from a *firm's tier one capital resources* under *PRU 2.2.20R* may form part of its *tier two capital resources* subject to the limits in *PRU 2.2.23R*.
- 2.2.23 R Subject to *PRU 2.2.24R*, a *firm* must exclude from the calculation of its *capital resources* the following:  
(1) the amount (if any) by which *tier two capital resources* exceed the amount calculated at stage F of the calculation in *PRU 2.2.14R*; and  
(2) the amount (if any) by which *lower tier two capital resources* exceed 50% of the amount calculated at stage F of the calculation in *PRU 2.2.14R*.
- 2.2.24 R At least 75% of a *firm's MCR* must be accounted for by the sum of:

- (1) the amount calculated at stage A plus stage B less stage E of the calculation in *PRU 2.2.14R*; and
- (2) the amount calculated at stage G of the calculation in *PRU 2.2.14R*.
- 2.2.25 G *PRU 2.2.23R* and *PRU 2.2.24R* give effect to the *Insurance Directives'* requirements that a *firm's tier two capital resources* must not exceed its *tier one capital resources* and that no more than 25% of a *firm's "required solvency margin"* should consist of *lower tier two capital resources*.
- 2.2.26 R A *firm* that carries on both *long-term insurance business* and *general insurance business* must apply the limits in *PRU 2.2.16R* to *PRU 2.2.24R* separately for each type of business.
- Characteristics of tier one capital
- 2.2.27 R A *firm* may not include a *share* in, or another investment in, or external contribution to the capital of, that *firm* in its *tier one capital resources* unless it complies with the following conditions:
- (1) it is included in one of the categories in *PRU 2.2.28R*;
- (2) it is not excluded by any of the *rules* in *PRU 2.2*; and
- (3) it complies with the conditions set out in *PRU 2.2.29R*.
- 2.2.28 R The categories referred to in *PRU 2.2.27R(1)* are:
- (1) *permanent share capital*;
- (2) a perpetual non-cumulative *preference share*; and
- (3) an *innovative tier one instrument*.
- 2.2.29 R Subject to *PRU 2.2.30R*, an item of capital in a *firm* complies with *PRU 2.2.27R(3)* if:
- (1) it is issued by the *firm*;
- (2) it is fully paid and the proceeds of issue are immediately and fully available to the *firm*;
- (3) it:
- (a) cannot be redeemed at all or can only be redeemed on a winding up of the *firm*; or
- (b) complies with the conditions in *PRU 2.2.38R* and *PRU 2.2.39 R*;
- (4) any *coupon* is either non-cumulative or, if it is cumulative, it complies with *PRU 2.2.40R*;
- (5) it is able to absorb losses to allow the *firm* to continue trading and in the case of an *innovative tier one instrument* it complies with *PRU 2.2.56R* to *PRU 2.2.58R*;
- (6) it ranks for repayment upon winding up no higher than a *share* of a company incorporated under the Companies Act 1985 or the Companies (Northern Ireland) Order 1986 (whether or not it is such a *share*);
- (7) the *firm* has the right to choose whether or not to pay a *coupon* on it in cash at any time;
- (8) the description of its characteristics used in its marketing is consistent with the characteristics required to satisfy *PRU 2.2.29R(1)* to (7).
- 2.2.30 R (1) An item of capital does not comply with *PRU 2.2.27R(3)* if the issue of that item of capital by the *firm* is connected with one or more other transactions which, when taken together with the issue of that item, could produce the effect described in (2).
- (2) The effect referred to in (1) is a reduction in the economic benefit intended to be conferred on the *firm* by the issue of the item of capital which means that the item of capital no longer displays all of the characteristics set out in *PRU 2.2.29R(1)* to (8).

- 2.2.31 R An item of capital does not comply with *PRU 2.2.29R(5)* if the holder of that item does not bear losses to at least the same degree as the holder of a *share* of a company incorporated under the Companies Act 1985 or the Companies (Northern Ireland) Order 1986 (whether or not it is such a *share*).
- 2.2.32 G *PRU 2.2.29R(2)* is stricter than the Companies Act definition of fully paid, which only requires an undertaking to pay.
- 2.2.33 G An item of capital does not comply with *PRU 2.2.29R(8)* if it is marketed as a capital instrument that would only qualify for a lower level of capital or on the basis that investing in it is like investing in a *lower tier two instrument*. For example, an undated capital instrument should not be marketed as a dated capital instrument if the terms of the capital instrument include an option by the issuer to redeem the capital instrument at a specified date in the future.
- 2.2.34 G For the purposes of *PRU 2.2.30R*, examples of connected transactions might include guarantees or any other side agreement provided to the holders of the capital instrument by the *firm* or a connected party or a related transaction designed, for example, to enhance their security or to achieve a tax benefit, but which may compromise the loss absorption capacity or permanence of the original capital item.
- 2.2.35 R A *firm* may not include a *share* in its *tier one capital resources* unless (in addition to complying with the other relevant *rules* in *PRU 2.2*):
- (1) (in the case of a *firm* that is a company as defined in the Companies Act 1985 or the Companies (Northern Ireland) Order 1986) it is “called-up *share* capital” within the meaning given to that term in that Act or, as the case may be, that Order; or
  - (2) (in the case of any other *firm*) it is:
    - (a) in economic terms; and
    - (b) in its characteristics as capital (including loss absorbency, permanency, ranking for repayment and fixed costs);
 substantially the same as called-up *share* capital falling into (1).
- Core tier one capital: permanent share capital
- 2.2.36 R *Permanent share capital* means an item of capital which (in addition to satisfying *PRU 2.2.29R*) meets the following conditions:
- (1) it is:
    - (a) an ordinary *share*; or
    - (b) a *members' contribution*; or
    - (c) part of the *initial fund* of a *mutual*;
  - (2) any *coupon* on it is not cumulative, and the *firm* has both the right to choose whether or not to pay a *coupon* and the right to choose the amount of that *coupon*; and
  - (3) the terms upon which it is issued do not permit redemption and it is otherwise incapable of being redeemed to at least the degree of an ordinary *share* issued by a company incorporated under the Companies Act 1985 or the Companies (Northern Ireland) Order 1986 (whether or not it is such a *share*).

- 2.2.37 G *PRU 2.2.36R* has the effect that the *firm* should be under no obligation to make any payment in respect of a *tier one instrument* if it is to form part of its *permanent share capital* unless and until the *firm* is wound up. A *tier one instrument* that forms part of *permanent share capital* could not therefore count as a liability before the *firm* is wound up. The fact that relevant company law permits the *firm* to make earlier repayment does not mean that the *tier one instruments* are not eligible. However, the *firm* should not be required by any contractual or other obligation arising out of the terms of that capital to repay *permanent share capital*. Similarly a *tier one instrument* may still qualify if company law allows dividends to be paid on this capital, provided the *firm* is not contractually or otherwise obliged to pay them. There should therefore be no fixed costs.
- Basic rules about redemption and cumulative coupons
- 2.2.38 R In relation to a perpetual non-cumulative *preference share* which is redeemable, a *firm* may not include it in its *tier one capital resources* unless its contractual terms are such that:
- (1) it is redeemable only at the option of the *firm*; and
  - (2) the *firm* cannot exercise that redemption right:
    - (a) on or before the fifth anniversary of its date of issue;
    - (b) unless it has given notice to the *FSA* in accordance with *PRU 2.2.72R*; and
    - (c) unless at the time of exercise of that right it complies with *PRU 2.1.9R* and will continue to do so after redemption.
- 2.2.39 R In relation to an *innovative tier one instrument* which is redeemable and which, either:
- (1) is or may become subject to a *step-up*; or
  - (2) satisfies *PRU 2.2.54R(2)*;
- a *firm* may not include it in its *tier one capital resources* unless it complies with the conditions in *PRU 2.2.38R*, except that in *PRU 2.2.38R(2)(a)*, "fifth anniversary" is replaced by "tenth anniversary".
- 2.2.40 R A *potential tier one instrument* with a cumulative *coupon* complies with *PRU 2.2.29R(4)* only if any such *coupon* must, if deferred, be paid by the *firm* in the form of *permanent share capital*.
- 2.2.41 G *PRU 2.2.38R* does not apply to *permanent share capital* because no item of capital that is either redeemable or that has a cumulative *coupon* can be *permanent share capital*.
- Further guidance on redemption
- 2.2.42 G The *rules* in *PRU 2.2* about redemption of *potential tier one instruments* fall into three classes:
- (1) *rules* defining whether a *firm's potential tier one instruments* are eligible for inclusion in its *tier one capital resources* at all;
  - (2) *rules* defining whether a *firm's potential tier one instruments* are eligible for inclusion in its *permanent share capital*; and
  - (3) *rules* defining whether a *firm's potential tier one instruments* must be classified as *innovative tier one instruments*.
- 2.2.43 G The *rules* about redemption that are relevant to deciding whether a *firm's potential tier one instruments* are eligible for inclusion in its *tier one capital resources* at all are as follows.
- (1) *PRU 2.2.29R(3)* and *PRU 2.2.39R* have the following provisions.

- (a) Any capital instrument that is redeemable at the option of the holder cannot form part of a *firm's tier one capital resources*. Instead, if it is redeemable at all, a capital instrument should only be redeemable at the option of the *firm*.
  - (b) A redemption right should be exercisable no earlier than the fifth anniversary of the date of issue. However, if an instrument is an *innovative tier one instrument* which is subject to a *step-up* or any other economic incentive to redeem, any such redemption should be exercisable no earlier than the tenth anniversary.
  - (c) Any redemption proceeds should be payable only in cash or in *shares*.
  - (d) The terms of the capital instrument should provide that any redemption right should not be exercised unless and until the *firm* has given the notice to the *FSA* required under *PRU 2.2.72R*.
  - (e) Any redemption right should not be exercisable unless both before and after the redemption the *firm* complies with *PRU 2.1.9R* (which requires that a *firm* has sufficient *capital resources* to meet its *capital resources requirement*).
- (2) Under *PRU 2.2.70R*, a *firm* should not include a *potential tier one instrument* that is redeemable in whole or in part in *permanent share capital* in its *tier one capital resources* unless the *firm* has:
    - (a) sufficient *permanent share capital* or sufficient authority to issue *permanent share capital* (and the authority to allot it) to meet any redemption obligations that have become due; and
    - (b) a prudent reserve of *permanent share capital* or sufficient authority to issue *permanent share capital* (and the authority to allot it) to meet possible future redemption obligations.
  - (3) *PRU 2.2.65R* contains limits on the amount of *permanent share capital* that may be issued on a redemption of a *potential tier one instrument* redeemable in *permanent share capital*.
- 2.2.44 G The *rules* defining whether a *firm's potential tier one instruments* are eligible for inclusion in its *permanent share capital* are to be found in *PRU 2.2.36R*. As far as redemption is concerned, it says that the capital instrument should be no more capable of being redeemed than a *share* under the Companies Act 1985 or the Companies (Northern Ireland) Order 1986. *PRU 2.2.38R* (which sets out the basic rules for redemption) does not apply to *permanent share capital* as a redeemable *potential tier one instrument* should not be included in *permanent share capital*.
- 2.2.45 G The *rules* about redemption that are relevant to deciding whether a *firm's potential tier one instruments* should be classified as *innovative tier one instruments* are as follows.
- (1) Under *PRU 2.2.53R*, a redeemable *potential tier one instrument* is always treated as an *innovative tier one instrument* if the redemption proceeds are payable otherwise than in cash.
  - (2) Under *PRU 2.2.54R*, any feature of a *tier one instrument* that in conjunction with a call would make a *firm* more likely to redeem it or to have an incentive to do so will make it an *innovative tier one instrument*.
  - (3) Under *PRU 2.2.62R* a *step-up* coupled with a right of redemption results in a *potential tier one instrument* being treated as an *innovative tier one instrument*.

Further guidance on coupons



- 2.2.46 G The *rules* in PRU 2.2 about the *coupons* payable on *potential tier one instruments* fall into the same three classes that apply to the *rules* on redemption, as set out in PRU 2.2.42G.
- 2.2.47 G The *rules* about *coupons* that are relevant to deciding whether a *firm's potential tier one instruments* are eligible for inclusion in its *tier one capital resources* at all are as follows.
- (1) Under PRU 2.2.29R(4) and PRU 2.2.40R, any deferred cumulative *coupon* should only be payable in *permanent share capital*. If a cumulative *coupon* is payable on a *potential tier one instrument* in another form, it should not be included in the *firm's tier one capital resources*.
  - (2) Under PRU 2.2.29R(7), the *firm* has the right not to pay a *coupon* in cash at any time.
  - (3) PRU 2.2.63R says that a *potential tier one instrument* that may be subject to a *step-up* that potentially exceeds defined limits should not be included in the *firm's tier one capital resources*. PRU 2.2.64R says that any *step-up* should not arise before the tenth anniversary of the date of issue if it is to be included in the *firm's tier one capital resources*.
  - (4) The provisions of PRU 2.2.70R summarised in PRU 2.2.43G(2) also apply to the payment of *coupons*.
- 2.2.48 G PRU 2.2.36R(2) says that a capital instrument on which a cumulative *coupon* is payable must not be included in a *firm's permanent share capital*. The payment of a *coupon* must be purely discretionary.
- 2.2.49 G The *rules* about *coupons* that are relevant to deciding whether a *firm's potential tier one instruments* should be classified as *innovative tier one instruments* are as follows:
- (1) Under PRU 2.2.60R a *potential tier one instrument* with a cumulative *coupon* is an *innovative tier one instrument*.
  - (2) Under PRU 2.2.40R a *potential tier one instrument* with a *coupon* that if deferred must be paid in *permanent share capital* is an *innovative tier one instrument*.
  - (3) Under PRU 2.2.62R a *step-up* coupled with a right of redemption by the *firm* results in a *potential tier one instrument* being treated as an *innovative tier one instrument*.
- Perpetual non-cumulative preference shares
- 2.2.50 R A perpetual non-cumulative *preference share* may be included at stage B of the calculation in PRU 2.2.14R if:
- (1) it complies with PRU 2.2.29R, PRU 2.2.35R and PRU 2.2.38R;
  - (2) any *coupon* on it is not cumulative, and the *firm* has the right to choose whether or not to pay a *coupon* in all circumstances;
  - (3) it is not excluded from *tier one capital resources* by any of the *rules* in PRU 2.2; and
  - (4) it is not an *innovative tier one instrument*.
- 2.2.51 G Perpetual non-cumulative *preference shares* should be perpetual and redeemable only at the *firm's* option. Any feature that, in conjunction with a call, would make a *firm* more likely to redeem perpetual non-cumulative *preference shares* would normally result in classification as an *innovative tier one instrument*. Such features would include, but not be limited to, a *step-up*, bonus *coupon* on redemption or redemption at a premium to the original issue price of the *share*.
- Innovative tier one instruments: general rules

- 2.2.52 R If an item of capital is stated to be an *innovative tier one instrument* by the rules in *PRU 2.2*, it cannot be included in stages A or B of the calculation in *PRU 2.2.14R*.
- 2.2.53 R If a *tier one instrument* is redeemable at the option of the *firm*, it is an *innovative tier one instrument* unless it is redeemable solely in cash.
- 2.2.54 R If a *tier one instrument*:
- (1) is redeemable; and
  - (2) is issued on terms that are (or its terms are amended and the amended terms are) such that a reasonable *person* would (judging at or around the time of issue or amendment) think that:
    - (a) the *firm* is likely to redeem it; or
    - (b) the *firm* is likely to have a substantial economic incentive to redeem it;
 that *tier one instrument* is an *innovative tier one instrument*.
- 2.2.55 G Any feature that in conjunction with a call would make a *firm* more likely to redeem a *tier one instrument* would normally result in classification as *innovative tier one capital resources*. *Innovative tier one instruments* include but are not limited to those incorporating a *step-up* or principal stock settlement.
- Innovative tier one instruments: loss absorbency
- 2.2.56 R A capital instrument may only be included in *innovative tier one capital resources* if a *firm's* obligations under the instrument either:
- (1) do not constitute a liability (actual, contingent or prospective) under section 123(2) of the Insolvency Act 1986; or
  - (2) do constitute such a liability but the terms of the instrument are such that:
    - (a) any such liability is not relevant for the purposes of deciding whether:
      - (i) the *firm* is, or is likely to become, unable to pay its debts; or
      - (ii) its liabilities exceed its assets;
    - (b) a creditor (including, but not limited to, a holder of the instrument) is not able to petition for the winding up or administration of the *firm* on the grounds that the *firm* is or may become unable to pay any such liability; and
    - (c) the *firm* is not obliged to take into account such a liability for the purposes of deciding whether or not the *firm* is, or may become, insolvent for the purposes of section 214 of the Insolvency Act 1986 (wrongful trading).
- 2.2.57 G The effect of *PRU 2.2.56R* is that if a *potential tier one instrument* does constitute a liability, this should only be the case when the *firm* is able to pay that liability but chooses not to do so. As *tier one capital resources* must be undated, this will generally only be relevant on a solvent winding up of the *firm*.
- 2.2.58 R A *firm* wishing to issue an *innovative tier one instrument* must obtain an opinion from Queen's Counsel, or where the opinion relates to the law of a jurisdiction outside the *United Kingdom*, from a lawyer in that jurisdiction of equivalent status, confirming that the criteria in *PRU 2.2.29R(5)* and *PRU 2.2.31R* are met.
- 2.2.59 G The holder should agree that the *firm* has no liability (including any contingent or prospective liability) to pay any amount to the extent to which that liability would cause the *firm* to become insolvent if it made the payment or to the extent that its liabilities exceed its assets or would do if the payment were made. The terms of the capital instrument should be such that the *directors* can continue to trade in the best interests of the senior creditors even if this prejudices the interests of the holders of the instrument.

Innovative tier one instruments: Coupons

- 2.2.60 R A *tier one instrument* with a cumulative *coupon* which complies with PRU 2.2.40R is an *innovative tier one instrument*.
- 2.2.61 G An item of capital does not fall into PRU 2.2.60R merely because a *firm* has come under an obligation to pay a particular *coupon* in *permanent share capital* where that obligation is the result of a voluntary election by the holder or the *firm* to be paid the *coupon* in that form. Thus, for example, if a shareholder of a *firm* is allowed to elect to be paid a dividend in the form of a conventional scrip dividend, that does not make the *share* into an *innovative tier one instrument*.
- Innovative tier one instruments and other tier one instruments: step-ups
- 2.2.62 R If:
- (1) a *potential tier one instrument* is or may become subject to a *step-up*; and
  - (2) that *potential tier one instrument* is redeemable at any time (whether before, at or after the time of the *step-up*);
- that *potential tier one instrument* is an *innovative tier one instrument*.
- 2.2.63 R If a *potential tier one instrument* is or may become subject to a *step-up*, a *firm* must not include it in its *tier one capital resources* if the amount of the *step-up* exceeds or may exceed;
- (1) 100 basis points; and
  - (2) 50% of the *initial credit spread*.
- 2.2.64 R A *firm* must not include a *potential tier one instrument* that is or may become subject to a *step-up* in its *tier one capital resources* if the *step-up* can arise earlier than the tenth anniversary of the date of issue of that item of capital.
- Innovative tier one instruments: principal stock settlement
- 2.2.65 R A *firm* must not include a *potential tier one instrument* that is redeemable in whole or in part in *permanent share capital* in its *tier one capital resources* if:
- (1) the conversion ratio as at the date of redemption may be greater than the conversion ratio as at the time of issue by more than 200%; or
  - (2) the issue or market price of the conversion instruments issued in relation to one unit of the original capital item (plus any cash element of the redemption) may be greater than the issue price (or, as the case may be, market price) of that original capital item.
- 2.2.66 R In PRU 2.2.65R to PRU 2.2.69R:
- (1) the original capital item means the capital item that is being redeemed; and
  - (2) the conversion instrument means the *permanent share capital* issued on its redemption.
- 2.2.67 R In PRU 2.2.65R to PRU 2.2.69R, the conversion ratio means the ratio of:
- (1) the number of units of the conversion instrument that the *firm* must issue to satisfy its redemption obligation (so far as it is to be satisfied by the issue of conversion instruments) in respect of one unit of the original capital item; to
  - (2) one unit of the original capital item.
- 2.2.68 R In PRU 2.2.65R, the conversion ratio as at the date of issue of the original capital item is calculated as if the original capital item were redeemable at that time.
- 2.2.69 R If the conversion instruments or the original capital item are subdivided or consolidated or subject to any other occurrence that would otherwise result in like not being compared with like, the conversion ratio calculation in PRU 2.2.65R must be adjusted accordingly.
- Requirement to have sufficient unissued stock
- 2.2.70 R (1) This *rule* applies to a *potential tier one instrument* of a *firm* where either:
- (a) the redemption proceeds; or
  - (b) any *coupon* on that capital item;

can be satisfied by the issue of another *tier one instrument*.

- (2) A *firm* may only include an item of capital to which this *rule* applies in its *tier one capital resources* if the *firm* has authorised and unissued *tier one instruments* of the kind in question (and the authority to issue them):
- (a) that are sufficient to satisfy all such payments then due; and
  - (b) are of such amount as is prudent in respect of such payments that could become due in the future.

Notifying the *FSA* of the issue and redemption of tier one instruments

2.2.71 R A *firm* must not include any perpetual non-cumulative *preference shares* or *innovative tier one instruments* in its *tier one capital resources* for the purpose of *PRU 2.2* unless it has notified the *FSA* of its intention at least one month before it first includes them.

2.2.72 R A *firm* must not redeem any *tier one instrument* that it has included in its *tier one capital resources* for the purpose of *PRU 2.2* unless it has notified the *FSA* of its intention at least one month before it does so.

Non standard capital instruments

2.2.73 G There may be examples of capital instruments that, although based on a standard form, contain structural features that make the rules in *PRU 2.2* difficult to apply. In such circumstances, a *firm* may seek individual *guidance* on the application of those *rules* to the capital instrument in question. See *SUP 9* for the process to be followed when seeking individual *guidance*.

Step-ups

2.2.74 R In relation to a *tier one instrument*, a *step-up* means any change in the *coupon* rate on that instrument that results in an increase in the amount payable at any time, including a change already provided in the original terms governing those payments.

A *step-up*:

- (1) includes (in the case of a fixed rate) an increase in that *coupon* rate;
- (2) includes (in the case of a floating rate calculated by adding a fixed amount to a fluctuating amount) an increase in that fixed amount;
- (3) includes (in the case of a floating rate) a change in the identity of the benchmark by reference to which the fluctuating element of the *coupon* is calculated that results in an increase in the absolute amount of the *coupon*;
- (4) does not include (in the case of a floating rate) an increase in the absolute amount of the *coupon* caused by fluctuations in the fluctuating figure by reference to which the absolute amount of the *coupon* floats.

2.2.75 R Where a *rule* in *PRU 2.2* says that a particular treatment applies to an item of capital that is subject to a *step-up* of a specified amount, the question of whether that *rule* is satisfied must be judged by reference to the cumulative amount of all *step-ups* since the issue of that item of capital rather than just by reference to a particular *step-up*.

Profit and loss account and other reserves

2.2.76 R Negative amounts, including any interim net losses, must be deducted from *tier one capital resources*.

2.2.77 R Dividends must be deducted from reserves as soon as they are declared.

Valuation differences

2.2.78 R Valuation differences are all differences between the valuation of assets and liabilities as valued in *PRU* and the valuation that the *firm* uses for its external financial reporting purposes, except valuation differences which are dealt with elsewhere in *PRU 2.2.14R*. The sum of these valuation differences must either be added to (if positive) or deducted from (if negative) a *firm's capital resources* in accordance with *PRU 2.2.14R*.

- 2.2.79 G Additions to and deductions from *capital resources* will arise from the application of asset and liability valuation and admissibility rules (see *PRU 1.3*, *PRU 2.2.86R* and *PRU 2 Ann 1R*). Downward adjustments include *discounting of technical provisions* for *general insurance business* (which is optional for financial reporting but not permitted for regulatory valuation – see *PRU 2.2.80R* to *PRU 2.2.81R*). Details of valuation differences relating to *technical provisions* and liability adjustments for *long-term insurance business* are set out in *PRU 7.3*. In particular, contingent loans or other arrangements which are not valued as a liability under *PRU 7.3.79R(2)* result in a positive valuation difference.
- 2.2.80 R *PRU 2.2.81R* applies to a *firm* that carries on *general insurance business*, except a *pure reinsurer*, and which *discounts* or reduces its *technical provisions* for *claims* outstanding to take account of its investment income as permitted by Article 60(1)(g) of the *Annual Accounts Directive*.
- 2.2.81 R A *firm* of a kind referred to in *PRU 2.2.80R* must deduct from its *capital resources* the difference between the undiscounted *technical provisions* or *technical provisions* before deductions as disclosed in the notes on the accounts, and the discounted *technical provisions* or *technical provisions* after deductions. This adjustment must be made for all *general insurance business classes*, except for risks listed under *classes 1* and *2*. For *classes* other than *1* and *2*, no adjustment needs to be made in respect of the discounting of annuities included in *technical provisions*.
- Externally verified interim net profits
- 2.2.82 R Externally verified interim net profits are interim profits verified by a *firm's* external auditors after deduction of tax, declared dividends and other appropriations.
- 2.2.83 G The *FSA* may request a *firm* to provide it with a copy of the external auditor's opinion on whether the interim profits are fairly stated.
- Intangible assets
- 2.2.84 R A *firm* must deduct from its *tier one capital resources* the value of intangible assets.
- 2.2.85 G Intangible assets include goodwill, capitalised development costs, brand names, trademarks and similar rights, and licences.
- Inadmissible assets
- 2.2.86 R For the purposes of *PRU 2.2.14R*, a *firm* must deduct from total *capital resources* the value of any asset which is not an *admissible asset* as listed in *PRU 2 Ann 1R*.
- 2.2.87 G *PRU 2.2.86R* does not apply to intangible assets which must be deducted from *tier one capital resources* under *PRU 2.2.84R*.
- 2.2.88 G The list of *admissible assets* has been drawn with the aim of excluding assets:
- (1) for which a sufficiently objective and verifiable basis of valuation does not exist; or
  - (2) whose realisability cannot be relied upon with sufficient confidence; or
  - (3) whose nature presents an unacceptable custody risk; or
  - (4) the holding of which may give rise to significant liabilities or onerous duties.
- Adjustments for related undertakings
- 2.2.89 R A *firm* must deduct from its *capital resources* the value of its investments in each of its *related undertakings* that is an *ancillary services undertaking*.

- 2.2.90 R In relation to each of its *related undertakings* that is a *regulated related undertaking* (other than an *insurance undertaking*) a *firm* must add to (if positive), at stage J in *PRU 2.2.14R*, or deduct from (if negative), at stage L in *PRU 2.2.14R*, its *capital resources* the value of its *shares* in that *undertaking* calculated in accordance with *PRU 1.3.35R*.
- 2.2.91 G For the purposes of *PRU 2.2.89R*, investments must be valued at their accounting book value in accordance with *PRU 1.3.5R*.
- 2.2.92 G *Related undertakings* which are also *insurance undertakings* are not included in *PRU 2.2.90R* because a *firm* that is a *participating insurance undertaking* is subject to the requirements of *PRU 8.3*.
- Additional requirements for a tier one or tier two instrument issued by a firm carrying on with-profits insurance business
- 2.2.93 R A *firm* carrying on *with-profits insurance business* must, in addition to the other requirements in respect of *capital resources* elsewhere in *PRU 2.2*, meet the following conditions before a capital instrument can be included in the *firm's capital resources*:
- (1) the *firm* must manage the *with-profits fund* so that discretionary benefits under a *with-profits insurance contract* are calculated and paid disregarding, insofar as is necessary for its *customers* to be treated fairly, any liability the *firm* may have to make payments under the capital instrument;
  - (2) the intention to manage the *with-profits fund* on the basis set out in *PRU 2.2.93R(1)* must be disclosed in the *firm's Principles and Practices of Financial Management*; and
  - (3) no amounts, whether interest, principal, or other amounts, must be payable by the *firm* under the capital instrument if the *firm's* assets would then be insufficient to enable it to declare and pay under a *with-profits insurance contract* discretionary benefits that are consistent with the *firm's* obligations under *Principle 6*.
- 2.2.94 G The purpose of *PRU 2.2.93R* is to achieve practical subordination of capital instruments if they are to qualify as capital resources to the liabilities a *firm* has to *with-profits policyholders*, including liabilities which arise from the regulatory duty to treat *customers* fairly in setting discretionary benefits. (*Principle 6* (Customers' interests) requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly.) It is not sufficient for a capital instrument to be subordinated to such liabilities only on winding up of the *firm* because such *liabilities to policyholders* may have been reduced by the inappropriate use of management discretion to enable funds to be applied in repaying subordinated capital instruments before winding up proceedings commence.
- 2.2.95 G *PRU 2.2.93R* is an additional requirement to all other rules in *PRU 2.2* concerning the eligibility of a capital instrument to count as a component of a *firm's capital resources*. Subordinated debt instruments will be the main type of capital instrument to which this *rule* is relevant, including both *upper tier two* (undated) and *lower tier two* (dated) subordinated debt instruments. Subordinated debt instruments which are issued by a *related undertaking* are not intended to be covered by this *rule* and may be included in *group capital resources* as appropriate if the other eligibility criteria are met.

- 2.2.96 G *PRU 2.2.29R(8) and PRU 2.2.108R(10) contain provisions concerning the marketing of a capital instrument. In relation to a firm to which PRU 2.2.93R applies, in order to comply with PRU 2.2.29R(8) and PRU 2.2.108R(10), it should draw to the attention of subscribers the risk that payments may be deferred or cancelled in order to operate the with-profits fund so as to give priority to the payment of discretionary benefits to with-profits policyholders.*
- 2.2.97 G (1) *Upper tier two instruments must meet the requirements of PRU 2.2.101R(3) which goes beyond the requirement in PRU 2.2.93R(3) since it requires a firm to have the option to defer payments in all circumstances, not just if necessary to treat customers fairly. However, for lower tier two instruments, PRU 2.2.93R(3) represents an additional requirement since a failure to pay amounts of interest or principal on a due date must not constitute an event of default under PRU 2.2.108R(2) for firms carrying on with-profits insurance business.*
- (2) *For firms which are realistic basis life firms compliance with PRU 2.2.93R(3) would usually be achieved if the capital instrument provides that no amounts will be payable under it unless the firm's capital resources exceed its capital resources requirement. However, such firms should ensure that the terms of the capital instrument refer to FSA capital resources requirements in force from time to time, including the current realistic reserving requirements and are not restricted to former minimum capital requirements based only on the Insurance Directives' required minimum margin of solvency. For firms which are not realistic basis life firms, compliance with PRU 2.2.93R(3) will probably require specific reference to be made to treating customers fairly in the terms of the capital instrument.*
- Tier two capital
- 2.2.98 G *Tier two capital resources is split into upper and lower tiers. The principal distinction between upper and lower tier two capital is that perpetual instruments may be included in upper tier two capital whereas dated instruments, such as fixed term preference shares and dated subordinated debt, are included in lower tier two capital.*
- 2.2.99 G *Tier two capital instruments are capital instruments that combine the features of debt and equity in that they are structured like debt, but exhibit some of the loss absorption and funding flexibility features of equity.*
- Upper tier two capital
- 2.2.100 G *Examples of capital instruments which may be eligible to count in upper tier two capital resources include the following:*
- (1) *perpetual cumulative preference shares;*
- (2) *perpetual subordinated debt; and*
- (3) *other instruments that have the same economic characteristics as (1) or (2).*
- 2.2.101 R *A capital instrument must meet the following conditions before it can be included in a firm's upper tier two capital resources:*
- (1) *it must meet the general conditions described in PRU 2.2.108R;*
- (2) *it must have no fixed maturity date;*
- (3) *the contractual terms of the instrument must provide for the firm to have the option to defer any interest payment in cash on the debt; and*
- (4) *the contractual terms of the instrument must provide for the loss-absorption capacity of the debt and unpaid interest, whilst enabling the firm to continue its business.*

- 2.2.102 R A capital instrument does not meet *PRU 2.2.101R(4)* unless it meets *PRU 2.2.103R* and *PRU 2.2.105R*.
- 2.2.103 R A capital instrument may only be included in *upper tier two capital resources* if a *firm's* obligations under the instrument either:
- (1) do not constitute a liability (actual, contingent or prospective) under section 123(2) of the Insolvency Act 1986; or
  - (2) do constitute such a liability but the terms of the instrument are such that:
    - (a) any such liability is not relevant for the purposes of deciding whether:
      - (i) the *firm* is, or is likely to become, unable to pay its debts; or
      - (ii) its liabilities exceed its assets;
    - (b) a creditor (including but not limited to a holder of the instrument) is not able to petition for the winding up or administration of the *firm* on the grounds that the *firm* is or may become unable to pay any such liability; and
    - (c) the *firm* is not obliged to take into account such a liability for the purposes of deciding whether or not the *firm* is, or may become, insolvent for the purposes of section 214 of the Insolvency Act 1986 (wrongful trading).
- 2.2.104 G The effect of *PRU 2.2.103R* is that if an *upper tier two instrument* does constitute a liability, this should only be the case when the *firm* is able to pay that liability but chooses not to do so. As *upper tier two capital resources* must be undated, this will generally only be relevant on a solvent winding up of the *firm*.
- 2.2.105 R A *firm* wishing to issue an *upper tier two instrument* other than a perpetual cumulative *preference share* must obtain an opinion from Queen's Counsel, or where the opinion relates to the law of a jurisdiction outside the *United Kingdom*, from a lawyer in that jurisdiction of equivalent status, confirming that the criteria in *PRU 2.2.101R(4)* are met.
- 2.2.106 G For the purpose of *PRU 2.2.103R(2)(b)* above, the holder should agree that the *firm* has no liability (including any contingent or prospective liability) to pay any amount to the extent to which that liability would cause the *firm* to become insolvent if it made the payment or to the extent that its liabilities exceed its assets or would do if the payment were made. The terms of the capital instrument should be such that the *directors* can continue to trade in the best interests of the senior creditors even if this prejudices the interests of the holders of the instrument.
- Lower tier two capital
- 2.2.107 G Capital instruments that meet the general conditions described in *PRU 2.2.108R* may be included in *lower tier two capital resources*.
- General conditions for eligibility as tier two capital
- 2.2.108 R A capital instrument must not form part of the *tier two capital resources* of a *firm* unless it meets the following conditions:
- (1) the claims of the creditors must rank behind those of all unsubordinated creditors;
  - (2) the only events of default must be non-payment of any amount falling due under the terms of the capital instrument or the winding-up of the *firm*;
  - (3) the remedies available to the subordinated creditor in the event of non-payment or other breach of the written agreement or instrument must be limited to petitioning for the winding-up of the *firm* or proving for the debt and claiming in the liquidation of the *firm*;
  - (4) any events of default and any remedy described in (3) must not prejudice the matters in (1) and (2);



- (5) in addition to the requirement about repayment in (1), the debt must not become due and payable before its stated final maturity date (if any) except on an event of default complying with (2);
  - (6) the debt agreement or terms of the capital instrument are governed by the law of England and Wales, or of Scotland or of Northern Ireland;
  - (7) to the fullest extent permitted under the laws of the relevant jurisdictions, creditors must waive their right to set off amounts they owe the *firm* against subordinated amounts included in the *firm's capital resources* owed to them by the *firm*;
  - (8) the terms of the capital instrument must be set out in a written agreement that contains terms that provide for the conditions set out in (1) to (7);
  - (9) the debt must be unsecured and fully paid up;
  - (10) the description of its characteristics used in its marketing is consistent with the characteristics required to satisfy (1) to (9); and
  - (11) the *firm* has obtained a properly reasoned external legal opinion stating that the requirements in (1) to (10) have been met.
- 2.2.109 G For the purposes of *PRU 2.2.108R(5)* the debt agreement or terms of the instrument should not contain any clause which might require early repayment of the debt (e.g. cross default clauses, negative pledges and restrictive covenants). A cross default clause is a clause which says that the loan goes into default if any of the borrower's other loans go into default. It is intended to prevent one creditor being repaid before other creditors, e.g. obtaining full repayment through the courts. A negative pledge is a clause which puts the loan into default if the borrower gives any further charge over its assets. A restrictive covenant is a term of contract that directly, or indirectly, could lead to early repayment of the debt. Some covenants, e.g. relating to the provision of management information or ownership restrictions, are likely to comply with *PRU 2.2.108R(5)* as long as monetary redress is ruled out, or any payments are covered by the subordination and limitation of remedies clauses (that is, if damages are unpaid, the only remedy is to petition for a winding up).
- 2.2.110 G The purpose of *PRU 2.2.108R(7)* is to ensure that all of the *firm's* assets are available to *customers* ahead of subordinated creditors. The waiver should apply both before and during liquidation.
- 2.2.111 R *PRU 2.2.108R(6)* does not apply if the *firm* has obtained a properly reasoned external legal opinion confirming that the same degree of subordination has been achieved under the law that governs the debt and the agreement as that which would have been achieved under the laws of England and Wales, Scotland, or Northern Ireland.
- 2.2.112 G An item of capital does not comply with *PRU 2.2.108R(10)* if it is marketed as a capital instrument that would only qualify for a lower level of capital or on the basis that investing in it is like investing in a lower tier capital instrument. For example, an undated capital instrument should not be marketed as a dated capital instrument if the terms of the capital instrument include an option by the issuer to redeem the capital instrument at a specified date in the future.
- 2.2.113 R (1) An item of capital does not comply with *PRU 2.2.101R* or *PRU 2.2.108R* if the issue of that item of capital by the *firm* is connected with one or more other transactions which, when taken together with the issue of that item, could produce the effect described in (2).

- (2) The effect referred to in (1) is a reduction in the economic benefit intended to be conferred on the *firm* by the issue of the item of capital which means that the item of capital no longer displays all of the characteristics set out in *PRU 2.2.101R* or *PRU 2.2.108R*.
- 2.2.114 G For the purposes of *PRU 2.2.113R*, examples of connected transactions might include guarantees or any other side agreement provided to the holders of the capital instrument by the *firm* or a connected party or a related transaction designed, for example, to enhance their security or to achieve a tax benefit, but which may compromise the loss absorption capacity or permanence of the original capital item.
- 2.2.115 G The *FSA* is more concerned that the subordination provisions listed in *PRU 2.2.108R* should be effective than that they should follow a particular form. The *FSA* does not, therefore, prescribe that the loan agreement should be drawn up in a standard form.
- 2.2.116 R A *firm* must not amend the terms of the debt and the documents referred to in *PRU 2.2.108R(8)* unless:
- (1) at least one month before the amendment is due to take effect, the *firm* has given the *FSA* notice in writing of the proposed amendment and the *FSA* has not objected; and
  - (2) that notice includes confirmation that the legal opinions referred to in *PRU 2.2.108R(11)* and, if applicable, *PRU 2.2.105R* and *PRU 2.2.111R*, continue in full force and effect in relation to the terms of the debt and documents, notwithstanding any proposed amendment.
- 2.2.117 R A *firm* must notify the *FSA* of its intention to repay a *tier two instrument* at least six months before the date of the proposed repayment (unless the *firm* intends to repay an instrument on its contractual repayment date) providing details of how it will meet its *capital resources requirement* after such repayment.
- Step-ups
- 2.2.118 R In relation to a *tier two instrument*, a *step-up* in a *coupon* rate means:
- (1) (in the case of a fixed rate) an increase in that rate;
  - (2) (in any other case) any change in the way that the interest or other payment is calculated that may result in an increase in the amount payable at any time, including a change already provided in the original terms governing those payments.
- 2.2.119 R Where a *tier two instrument* is subject to one or more *step-ups*, the first date that a *step-up* can take effect must be treated, for the purposes of this section, as the instrument's final maturity date if its actual maturity date occurs after that, unless the effect of the *step-up* or *step-ups* is to increase the *coupon* rate at which payments are to be made by no more than:
- (1) 50 basis points in the first ten years of the life of the debt; or
  - (2) 100 basis points over the whole life of the debt.
- 2.2.120 R A *firm* may not include in its *tier two capital resources* a capital instrument the terms of which provide for a *step-up* in the first five years after issue.
- 2.2.121 R Where a *step-up* arises through a change from paying a *coupon* on a debt instrument to paying a dividend on a *share* issued in settlement of the *coupon*, then any cost to the *firm* arising from the tax treatment of the dividend may be excluded.

- 2.2.122 G Debt instruments containing embedded options, e.g. issues containing options for the interest rate after the *step-up* to be at a margin over the higher of two (or more) reference rates, or for the interest rate in the previous period to act as a floor, may affect the funding costs of the borrower and imply a *step-up*. In such circumstances, a *firm* may wish to seek individual *guidance* on the application of the *rules* relating to *step-ups* to the capital instrument in question. See *SUP 9* for the process to be followed when seeking individual *guidance*.
- Other conditions for eligibility as lower tier two capital
- 2.2.123 R A capital instrument may be included in *lower tier two capital resources* only if it has an original maturity of at least five years or, where it has no fixed maturity date, notice of repayment of not less than five years has been given.
- 2.2.124 R In its final five years to maturity, for the purposes of calculating the amount of a *lower tier two instrument* which may be included in a *firm's capital resources*, the principal amount must be amortised on a straight line basis.
- 2.2.125 G *PRU 2.2.124R* applies both to a *tier two instrument* with a fixed maturity and to a *tier two instrument* with no fixed maturity but where the *firm* has given five years' notice of repayment.
- Unpaid share capital or initial funds and calls for supplementary contributions
- 2.2.126 G Unpaid *share capital* or, in the case of a *mutual*, *unpaid initial funds* and calls for supplementary contributions are excluded from the *capital resources* of a *firm* except to the extent allowed in a *waiver* under section 148 of the *Act*.
- 2.2.127 G Subject to a *waiver*, under the *Insurance Directives* a maximum of one half of unpaid *share capital* or, in the case of a *mutual*, one half of the *unpaid initial fund* may be included in a *firm's capital resources*, once the paid-up part amounts to 25% of that *share capital* or fund, up to 50% of total *capital resources*.
- 2.2.128 G In the case of a *mutual* carrying on *general insurance business* and subject to a *waiver*, calls for supplementary contributions within the *financial year* may only be included in a *firm's capital resources* up to a maximum of 50% of the difference between the maximum contributions and the contributions actually called in, subject to a limit of 50% of total *capital resources*. In the case of a *mutual* carrying on *long-term insurance business*, the *Consolidated Life Directive* does not permit calls for supplementary contributions to be included in a *firm's capital resources*.

## 2.3 Individual Capital Assessment

### Application

2.3.1 R *PRU 2.3* applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) a *Swiss general insurer*; or
- (3) an *EEA-deposit insurer*; or
- (4) an *incoming EEA firm*; or
- (5) an *incoming Treaty firm*.

### Purpose

2.3.2 G *Principle 4* requires a *firm* to maintain adequate financial resources. *PRU 2* sets out provisions that deal specifically with the adequacy of that part of a *firm's* financial resources that consists of *capital resources*. The adequacy of a *firm's* *capital resources* needs to be assessed both by the *firm* and the *FSA*. In *PRU 2.1*, the *FSA* sets minimum *capital resources requirements* for *firms*. It also reviews a *firm's* own assessment of its capital needs, and the processes and systems by which that assessment is made, in order to see if the minimum *capital resources requirements* are appropriate. *PRU 1.2* contains *rules* requiring a *firm* to identify and assess risks to its being able to meet its liabilities as they fall due, to assess how it intends to deal with those risks and to quantify the financial resources it considers necessary to mitigate those risks. To meet these requirements, a *firm* should consider the extent to which capital is an appropriate mitigant for the risks identified and assess the amount and quality of capital required. In accordance with *PRU 1.2.37R*, these assessments must be documented so that they can be easily reviewed by the *FSA* as part of the *FSA's* assessment of the adequacy of the *firm's* *capital resources*.

2.3.3 G This section (*PRU 2.3*) sets out *guidance* on how *firms* should assess the adequacy of their *capital resources*, both to comply with the *rules* in *PRU 1.2* and to enable the *FSA* better to assess whether the minimum *capital resources requirements* in *PRU 2.1* are appropriate. This section also requires *firms* carrying on *general insurance business* to calculate their *ECR*. The *ECR* for *firms* carrying on *general insurance business* is an indicative measure of the *capital resources* that a *firm* may need to hold based on risk sensitive calculations applied to its business profile. For *realistic basis life firms*, the *ECR* forms part of the calculation of the *firm's* *capital resources requirement* (see *PRU 2.1.15R*). The *ECR* for such *firms* requires the calculation of a *with-profits insurance capital component* (see *PRU 7.4*) that supplements the *mathematical reserves* so as to ensure that a *firm* holds adequate financial resources for the conduct of its *with-profits insurance business*. In the case of *firms* carrying on *general insurance business* and *realistic basis life firms*, the *FSA* will use the *ECR* as a benchmark for its consideration of the appropriateness of the *firm's* own capital assessment. For *firms* where an *ECR* is not calculated the *MCR* will provide a benchmark for the *firm's* own capital assessment. For *firms* generally, the more thorough, objective and prudent a *firm's* capital assessment is and can be demonstrated as being, the more reliance the *FSA* will be able to place on the results of that assessment. The *FSA* will consider the appropriateness of the *firm's* capital assessment to establish the level of *capital resources* the *firm* needs. This may result in the *FSA's* assessment of a *firm's* *capital resources* needs being lower or higher than would otherwise be the case.

2.3.4 G There are two main purposes of this section:

- (1) to enable *firms* to understand the issues which the *FSA* would expect to see assessed and the systems and processes which the *FSA* would expect to see in operation for capital adequacy assessments by the *firm* to be regarded as thorough, objective and prudent; and
- (2) to enable *firms* to understand the *FSA*'s approach to assessing whether the minimum *capital resources requirements* of *PRU 2.1* are appropriate and what action may be taken if the *FSA* concludes that those requirements are not appropriate to a *firm*'s circumstances.

Main requirements and guidance

- 2.3.5 G In making an assessment of capital adequacy, the *FSA* requires *firms* to identify the major risks they face and, where capital is appropriate to mitigate those risks, to quantify how much (and what type) of capital is appropriate. To do this, the *FSA* expects *firms* to conduct stress tests and scenario analyses in respect of each risk. For each risk the *firm* will then be able to estimate a range of probable outcomes and hence capital required to absorb losses which might arise. A *firm* must document the results of each of the stress tests and scenario analyses undertaken and should also document, as part of the details of those tests and analyses, the key assumptions including the aggregation of the results.
- 2.3.6 G The assessment which a *firm* makes should be based upon its future business plans and projections. This is the main area where the *firm*'s assessment may diverge from its prescribed *capital resources requirement* which, necessarily, is based upon historic data.
- 2.3.7 G In assessing the quality and the amount of *capital resources* projected to be available to meet its projected *capital resources requirement*, a *firm* should consider the timing of its liabilities to repay existing capital together with the prospects for raising new capital in the scenarios considered.
- 2.3.8 G The *FSA* may ask for the results of a *firm*'s assessment to be provided to it together with a description of the processes by which the assessment has been made, the range of results from each stress test or scenario analysis performed and the main assumptions made. The *FSA* may also carry out a more detailed examination of the details of the *firm*'s processes and calculations.
- 2.3.9 G Based upon this information and other information available to the *FSA*, the *FSA* will consider whether the *capital resources requirement* applicable to the *firm* is appropriate. Where relevant, the *firm*'s *ECR* will be a key input to the *FSA*'s assessment of the adequacy of the *firm*'s *capital resources*.
- 2.3.10 R A *firm* carrying on *general insurance business*, other than a *non-directive insurer*, must calculate the amount of its *ECR*.
- 2.3.11 R A *firm* to which *PRU 2.3.10R* applies must calculate its *ECR* in respect of its *general insurance business* as the sum of:
- (1) the *asset-related capital requirement*; and
  - (2) the *insurance-related capital requirement*; less
  - (3) the *firm*'s *equalisation provisions*.
- 2.3.12 G Details of the calculation of the *asset-related capital requirement* are set out in *PRU 3.3.10R* to *3.3.16R*. Details of the calculation of the *insurance-related capital requirement* are set out in *PRU 7.2.76R* to *7.2.79R*.
- 2.3.13 G Where the *FSA* considers that a *firm* will not comply with *PRU 1.2.22R* (adequate financial resources, including *capital resources*) by holding the *capital resources* required by *PRU 2.1*, the *FSA* may give the *firm* individual *guidance* advising it of the amount and quality of *capital resources* which the *FSA* considers it needs to hold in order to meet that *rule*.

- 2.3.14 G The individual *guidance* will be given taking into consideration *capital resources* consistent with a 99.5% confidence level over a one year timeframe or, if appropriate to the *firm's* business, an equivalent lower confidence level over a longer timeframe. *Firms* should therefore prepare an individual capital assessment on the same basis. Throughout whatever timeframe is adopted by *firms*, *firms* should ensure that their projected assets are, and will continue to be, sufficient, to enable their projected liabilities to be paid, and it would be reasonable for *firms* to test that this is the case at the end of each year of the timeframe. *Firms* may also wish to make estimates of capital adequacy using other assumptions for their own internal purposes and are free to do so if they so choose.
- 2.3.15 G If a *firm* considers that the individual *guidance* is inappropriate to its circumstances, then the *firm* should inform the *FSA* that it does not intend to follow that *guidance*. Informing the *FSA* of such an intention would be expected if a *firm* is to comply with *Principle 11* (relations with regulators).
- 2.3.16 G The *FSA* expects most disagreements about the adequacy of capital will be resolved through further analysis and discussion. The *FSA* may consider the use of its powers under section 166 of the *Act* (Reports by skilled persons) to assist in such circumstances. If the *FSA* and the *firm* still do not agree on an adequate level of capital, then the *FSA* may consider using its powers under section 45 of the *Act* to, on its own initiative, vary a *firm's Part IV permission* so as to require it to hold capital in accordance with the *FSA's* view of the capital necessary to comply with *PRU 1.2.22R*. *SUP 7* provides further information about the *FSA's* powers under section 45.
- 2.3.17 G Where a *firm* or the *FSA* considers that the *capital resources requirements* of *PRU 2.1* require the holding of more capital than is needed for the *firm* to comply with *PRU 1.2.22R* then the *firm* may apply to the *FSA* for a *waiver* of the requirements in *PRU 2.1* under section 148 of the *Act*. This section sets out the factors which the *FSA* will consider in deciding whether to grant such a *waiver* request, and if so, the terms and extent of any modification to the *rules* in *PRU 2.1*. In addition to the statutory tests under section 148, these will include the thoroughness, objectivity, and prudence of a *firm's* own capital assessment and the extent to which the *guidance* in this section has been followed. The *FSA* will not grant a *waiver* that would cause a breach of the minimum capital requirements under the *Insurance Directives*.
- Stress and scenario requirement
- 2.3.18 G *PRU 1.2.35R* requires a *firm* to carry out stress tests and scenario analyses for each of the sources of risk identified in accordance with *PRU 1.2.31R*. Using each of the risk categories set out in *PRU 1.2.31R*, 2.3.19G to 2.3.34G set out the factors that a *firm* should consider. *PRU 2 Ann 3G* provides a practical illustration of how a small *firm* carrying on *general insurance business* might undertake this analysis.
- Factors to consider when assessing credit risk
- 2.3.19 G Credit risk refers to the risk of loss if another party fails to perform its obligations or fails to perform them in a timely fashion.
- 2.3.20 G In assessing potential credit risk events that may affect the *firm's* solvency, a *firm* should allow for:
- (1) the financial effect of non-payment of *reinsurance*, considering the likelihood both of non-payment of outstanding *claims* and for the fact that *reinsurance* cover purchased for underwritten risks may not be effective (that is, offsetting potential liabilities); and

- (2) the financial effect of non-payment of *premium* debtors such as intermediaries and *policyholders*.
- 2.3.21 G Some further areas to consider in developing the credit risk stress tests and scenario analyses might include:
- (1) the adequacy of the *reinsurance* programme and whether it is appropriate for the risks selected by the *firm* and adequately takes account of the underwriting and business plans of the *firm* generally;
  - (2) the collapse of a *reinsurer* or several *reinsurers* on the *firm's reinsurance* programme and the subsequent impact this may have on the *firm's* outstanding *reinsurance* recoveries and *IBNR* recoveries;
  - (3) a deterioration in the creditworthiness of the *firm's reinsurers*, intermediaries or other *counterparties*;
  - (4) the degree of credit concentration. For example, the degree to which a *firm* is exposed to a single *counterparty* or *group*;
  - (5) the degree of concentration of exposure to *reinsurers* of particular rating grades;
  - (6) the prospect of *reinsurance* rates increasing substantially or *reinsurance* being unavailable;
  - (7) any existing or possible future disputes relating to *reinsurance* contracts on a pessimistic basis and the extent that they are not already reflected in the value attributed to the *reinsurances*;
  - (8) greater losses from bad debts than anticipated;
  - (9) deterioration in the extent and quality of *collateral*; and
  - (10) guarantees given by the *insurer* of the performance of others, whether under *contracts of insurance* or otherwise.
- Factors to consider when assessing market risk
- 2.3.22 G *Market risk* includes the risks that arise from fluctuations in values of, or income from, assets or in interest or exchange rates.
- 2.3.23 G In assessing potential *market risk* events that may affect the *firm's* solvency, a *firm* should allow for:
- (1) reduced market values of *investments*;
  - (2) variation in interest rates and the effect on the market value of *investments*;
  - (3) a lower level of investment income than planned; and
  - (4) the possibility of *counterparty* defaults.
- 2.3.24 G Some further areas to consider in developing the *market risk* scenario might include:
- (1) the possibility of a severe economic or market downturn or upturn leading to adverse interest rate movements affecting the *firm's* investment position;
  - (2) unanticipated losses and defaults of issuers;
  - (3) price shifts in asset classes, and their impact on the entire portfolio;
  - (4) inadequate valuation of assets;
  - (5) the direct impact on the portfolio of currency devaluation, as well as the effect on related markets and currencies;
  - (6) extent of any mismatch of assets and liabilities, including reinvestment risk;
  - (7) the impact on the portfolio value of a dramatic change in the spread between a market index of interest rates and the risk-free interest rates; and
  - (8) the extent to which market moves could have non-linear effects on values, such as *derivatives*.
- Factors to consider when assessing liquidity risk
- 2.3.25 G In accordance with *PRU 1.2.31R* a *firm* should consider the major sources of risk,

- including *liquidity risks*, and assess its response should each risk materialise.
- 2.3.26 G *PRU 5.1* (liquidity risk systems and controls) contains evidential provisions and *guidance* on how *firms* should meet *PRU 1.2.22R* for liquidity purposes.
- (1) *PRU 5.1.61E* states that a scenario analysis in relation to *liquidity risk* required under *PRU 1.2.35R* should include a cash-flow projection for each scenario tested, based on reasonable estimates of the impact of that scenario on the *firm's* funding needs and sources.
  - (2) *PRU 5.1.86E* states that a *firm* should have a contingency funding plan for taking action to ensure, so far as it can, that in each of the scenarios tested under *PRU 1.2.35R(2)*, it would still have sufficient liquid financial resources to meet liabilities as they fall due.
- 2.3.27 G When assessing *liquidity risk*, the *firm* should consider the extent of mismatch between assets and liabilities and the amount of assets held in highly liquid, marketable forms should unexpected cashflows lead to a liquidity problem. The price concession of liquidating assets is a prime concern when assessing such *liquidity risk* and should be built into any assessment of capital adequacy.
- 2.3.28 Some further areas to consider in developing the *liquidity risk* scenario might include:
- (1) any mismatching between expected asset and liability cash flows;
  - (2) the inability to sell assets quickly;
  - (3) the extent to which the *firm's* assets have been pledged;
  - (4) the cash-flow positions generally of the *firm* and its ability to withstand sharp, unexpected outflows of funds via *claims*, or an unexpected drop in the inflow of *premiums*; and
  - (5) the possible need to reduce large asset positions at different levels of market liquidity, and the related potential costs and timing constraints.
- Factors to consider when assessing operational risk
- 2.3.29 G Operational risk refers to the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.
- 2.3.30 G A *firm* may wish to refer to *SYSC 3A* and *PRU 6.1* when carrying out its operational risk assessment.
- 2.3.31 G Examples of some issues that a *firm* might want to consider include:
- (1) the likelihood of fraudulent activity occurring that may impact upon the financial or operational aspects of the *firm*;
  - (2) the obligation a *firm* may have to fund a pension scheme for its employees;
  - (3) the technological risks that the *firm* may be exposed to regarding its operations. For example, risks relating to both the hardware systems and the software utilised to run those systems;
  - (4) the reputational risks to which the *firm* is exposed. For example, the impact on the *firm* if the *firm's* brand is damaged resulting in a loss of *policyholders* from the underwriting portfolio;
  - (5) the marketing and distribution risks that the *firm* may be exposed to. For example, the dependency on intermediary business or a *firm's* own sales force;
  - (6) the impact of legal risks. For example a non-insurance related legal action being pursued against the *firm*;
  - (7) the management of employees – for instance staff strikes, where dissatisfied staff may withdraw goodwill and may indulge in fraud or acts giving rise to reputational loss;



- (8) the resourcing of key functions such as the risk management function by staff in appropriate numbers and with an appropriate mix of skills such as underwriting, claims handling, accounting, actuarial and legal expertise.
- 2.3.32 G A *firm* may consider that investigation of operational weaknesses and corrective action is a better response than holding capital and may consider that a certain degree of operational risk is within its pre-defined risk tolerance. However, until the *firm* corrects any identified deficiencies a *firm* should consider capital as a (interim) response to the risk.
- Factors to consider when assessing insurance risk
- 2.3.33 G As a result of the differences between the nature of *general* and *long-term insurance business*, some aspects of the risk assessment vary depending on the type of business written. In assessing potential insurance risk events that may affect the *firm's* solvency, *general* and *long-term insurance business firms* should:
- (1) analyse the potential for catastrophic losses, including both risk and event losses, the cost of reinstatement *premiums* and any possible *reinsurance* exhaustion; and
  - (2) determine the likelihood of any other feature of insurance risk that may lead to a variation in projected outcomes.
  - (3) *Firms* carrying on *general insurance business* should in addition:
    - (a) analyse the potential for *claims* reserves to deteriorate beyond the current reserving level; and
    - (b) determine the effect of loss ratios being higher than planned by analysing historic loss ratio experience and volatility.
  - (4) *Firms* carrying on *long-term insurance business* should in addition:
    - (a) analyse the potential for *mathematical reserves* subsequently to prove inadequate compared with the current reserving level; and
    - (b) determine the effect of *claims* experience being more costly than planned by analysing historic *claims* experience, volatility and trends in experience.
- 2.3.34 G Some further areas to consider in developing the insurance risk scenario might include:
- (1) For underwriting risks, *general insurance business* and *long-term insurance business firms*:
    - (a) the adequacy of the *firm's* pricing. For example, the *firm* should be able to satisfy itself that it can charge adequate rates, taking into account the business and the risk profile of different products, the business environment (e.g. *premium* cycle-non-life) and its own internal profit targets;
    - (b) the uncertainty of *claims* experience;
    - (c) the dependence on intermediaries for a disproportionate share of the *insurer's premium* income; the effects of a high level of uncertainty in pricing in new or emerging underwriting markets due to a lack of information needed to enable the *insurer* to make a proper assessment of the price of the risk; the geographical mix of the portfolio or whether any geographical or jurisdictional concentrations exist;
    - (d) the appropriateness of *policy* wordings;
    - (e) the risk of mis-selling, for example, the number of complaints or disputed *claims*; and
    - (f) the tolerance for expense reserve variations or variations in expenses (including indirect costs).

- (2) For *firms* carrying on *general insurance business*, in addition:
  - (a) the length of tail of the *claims* development and latent *claims*; and
  - (b) the effects of rapid growth or decline in the volume of the underwriting portfolio.
- (3) For *firms* carrying on *long-term insurance business*, in addition:
  - (a) the uncertainty of future investment returns;
  - (b) the effects of rapid growth or decline in the volume and nature of new business written; and
  - (c) the ability of *firms* to adjust *premium* rates or charges for some products.
- (4) For reserving and *claims* risks, both *general insurance business* and *long term insurance business firms*:
  - (a) the frequency and size of large *claims*;
  - (b) possible outcomes relating to any disputed *claims*, particularly where the outcome is subject to legal proceedings;
  - (c) the ability of the *firm* to withstand catastrophic events, increases in unexpected exposures, latent *claims* or aggregation of *claims*;
  - (d) the possible exhaustion of *reinsurance* arrangements, both on a per risk and per event basis;
  - (e) social changes regarding an increase in the propensity to claim and to sue; and
  - (f) other social, economic and technological changes.
- (5) For *firms* carrying on *general insurance business*:
  - (a) the adequacy and uncertainty of the technical *claims* provisions, such as outstanding *claims*, *IBNR* and *claims* handling expense reserves;
  - (b) the adequacy of other underwriting provisions, such as the provisions for *unearned premium* and unexpired risk reserves;
  - (c) the appropriateness of catastrophe models and underlying assumptions used, such as possible maximum loss (PML) factors used;
  - (d) unanticipated legal judgements and legal change with retrospective effect specifically with regard to the *claims* reserves; and
  - (e) the effects of inflation.
- (6) For *firms* carrying on *long-term insurance business*:
  - (a) the adequacy and sensitivity of the *mathematical reserves* to variations in future experience, including:
    - (i) the risk that investment returns differ from those assumed in the reserving assumptions;
    - (ii) the risk of variations in mortality, morbidity and persistency experience and in the exercise of options under contracts;
    - (iii) the rates of taxation applied, in particular where there is uncertainty over the tax treatment; and
  - (b) unanticipated legal judgements and legal change with retrospective effect specifically with regard to the impact on *mathematical reserves*.

Other assessments of the adequacy of capital resources

- 2.3.35 G *Firms* must assess the adequacy of their financial resources and this will entail an assessment of both *capital resources* and liquidity resources. The stress tests and scenario analyses which a *firm* must carry out will assist with both assessments.

- However, *firms* may also find it helpful to approach their assessment of capital in another way.
- 2.3.36 G *Firms* may also wish to carry out an additional assessment to inform their view as to whether their *capital resources* are adequate. The additional assessment is to consider the extent to which the *capital resources requirement (CRR)* produces adequate capital for a *firm's* particular circumstances. In considering this, *firms* that are required to calculate an *Enhanced Capital Requirement (ECR)* may wish to note that the *ECR* as calculated is based upon the assumptions that a *firm's* business is well diversified, well managed with assets matching its liabilities and good controls, and stable with no large, unusual, or high risk transactions. *Firms* may find it helpful to assess the extent to which their actual business differs from these assumptions and therefore what adjustments it might be reasonable to make to the *CRR* or *ECR* to arrive at an adequate level of *capital resources*.
- 2.3.37 G *Firms* may find it helpful for their own assessment process if they also consider divergences from the assumptions described in *PRU 2.3.36G* under the headings set out below. These are the areas which the *FSA* considers when forming its view of the adequacy of a *firm's capital resources*.
- Business risk factors:
- (1) *market risk*;
  - (2) securitisation risk;
  - (3) residual risk;
  - (4) concentration risk;
  - (5) high impact, low probability events; and
  - (6) cyclical and capital planning.
- Control risk factors:
- (1) systems and controls.
- 2.3.38 G *Market risk*: a *firm* should assess its exposure to those elements of *market risk* that are not captured by the *CRR*. In doing so, *firms* may wish to use stress tests to determine the impact on their balance sheets of an appropriate move in market conditions. The results of this test should then be used by the *firm* to determine its *market risk*.
- 2.3.39 G *Securitisation risk*: a *firm* should assess its exposure to risks transferred through the securitisation of assets should those transfers fail for whatever reason. For instance, *firms* may contemplate two broad types of securitisation: 'embedded value securitisation' – the transfer of the value emerging from an existing block of business to bondholders; and 'risk transfer securitisation' – the purchase of protection against catastrophic risks to the *insurer* through the issuance of bonds whose repayment is contingent upon the non-occurrence of such risks. In either case, *firms* should consider the effect on their financial position of a failure of such complex arrangements to operate as anticipated or the values and risks transferred not emerging as expected.
- 2.3.40 G *Residual risk*: a *firm* should assess its exposure to the residual risks that may result from the partial performance or failure of risk mitigation techniques for reasons that are unconnected with their intrinsic value. This could result from (for example): ineffective documentation, a delay in payment or the inability to realise payment from a guarantor in a timely manner. Given that residual risks can always be present, *firms* should assess the appropriateness of their *capital resources requirement* against their assumptions for the risk mitigation measures that they may have in place.
- 2.3.41 G *Concentration risk*: a *firm* should assess and monitor its exposure to: sector,

- geographic, liability and asset concentrations, as well as granularity. The *FSA* considers that concentrations in these areas increase the *firm's* credit risk and where the *firm* identifies concentrations then they should consider the adequacy of the *capital resources requirement*. For instance, *firms* should monitor concentrations of exposure to particular *reinsurers* and ensure that they are aware of the implications of several of their *reinsurers* failing at the same time.
- 2.3.42 G High impact, low probability events: *firms* should consider stress tests and scenario analyses which are realistic – that is not too remote a possibility. However, should a *firm* decide to enter into a high impact, low probability transaction, the *firm* should satisfy itself that it has sufficient financial resources to meet its resulting financial obligation in the event the single risk materialises. For instance, a *firm* should not accept individual risks in circumstances where, if that single risk materialised, the *claim* arising would exceed the financial resources available to the *firm*.
- 2.3.43 G A *firm* should also consider the value of the financial obligation arising where the risks from a combination of high impact, low probability transactions that the *firm* has entered into materialise at the same time. A *firm* should ensure that in no circumstances would a combination of any consequent *claims* materially exceed the financial resources available to it.
- 2.3.44 G Cyclical and capital planning: a *firm's capital resources requirement* may vary as business cycles and economic conditions fluctuate over time. *Firms* should be aware that a deterioration in business or economic conditions could require them to raise capital or alternatively to contract their businesses at a time when market conditions are most unfavourable to raising capital. Such an effect is known as procyclicality.
- 2.3.45 G To reduce the impact of cyclical effects, *firms* should look to build-up capital levels through the course of an upturn in business and economic cycles to ensure that they have sufficient capital available to protect themselves against adverse conditions.
- 2.3.46 G To assess its expected capital requirements over the economic and business cycles, a *firm* may wish to project forward its financial position taking account of its business strategy and expected growth under a range of environmental assumptions. Projections over a three to five year period would be appropriate in most circumstances. *Firms* may then calculate their projected *capital resources requirement* and assess whether that requirement could be met from expected financial resources.
- 2.3.47 G Systems and controls: a *firm* may decide to hold additional *capital resources* to mitigate weaknesses in its overall control environment. Weaknesses might be indicated by the following:
- (1) a failure by the *firm* to complete an assessment of its systems and controls in line with *SYSC* 3.1 (Systems and Controls) and *PRU* 1.4;
  - (2) a failure by the *firm's* senior management to approve its financial results; and
  - (3) a failure by the *firm* to consider an analysis of relevant internal and external information on its business and control environment.
- 2.3.48 G In considering any systems and control weaknesses and their effect on the adequacy of the *capital resources requirement*, a *firm* may wish to be able to demonstrate to the *FSA* that all the issues identified in *SYSC* 3.2 (Areas covered by systems and controls) have been considered; and that appropriate plans and procedures exist to deal adequately with adverse scenarios.

Capital models

- 2.3.49 G A *firm* may approach its assessment of adequate *capital resources* by developing a model for some or all of its business risks. Where such a model captures some of the risks identified in accordance with *PRU* 1.2.31R then this will usually satisfy the requirement to perform stress tests in respect of those risks. However, the assumptions required to aggregate risks modelled and the confidence levels adopted should be considered by the *firm's* senior management. A *firm* should also consider whether any risks are not captured by the model and also the extent to which systems and control risks are not incorporated in the model.
- 2.3.50 G A *firm* should not expect the *FSA* to accept as adequate any particular model that it develops or that the results from the model are automatically reflected in any individual *guidance* given to the *firm* for the purpose of determining adequate *capital resources*. However, the *FSA* will take into account the results of any sound and prudent model when giving individual *guidance* or considering applications for a *waiver* under section 148 of the *Act* of the *capital resources requirement* in *PRU* 2.1. This section sets out the types of issues the *FSA* would consider before giving individual *guidance* or granting a *waiver* based on the results of a model.
- 2.3.51 G There is no prescribed modelling approach for how a *firm* develops its internal model. However, *firms* should be able to demonstrate:
- (1) the extent of use of the internal capital model within the *firm's* capital management policy;
  - (2) that sound and appropriate risk-management techniques are employed and are embedded in the daily operations and financial resources requirements of the *firm*;
  - (3) that all material risks to which the *firm* is exposed have been adequately addressed by quantitative and qualitative means as appropriate;
  - (4) the confidence levels set and whether these are linked to the *firm's* corporate strategy;
  - (5) the time horizons set for the different types of business that the *firm* undertakes;
  - (6) the extent of historic data used and back testing carried out; and
  - (7) whether sufficient accuracy and validation in the internal capital model has been undertaken.
- Quantitative factors
- 2.3.52 G The *firm's* model should be based on an appropriate probability of insolvency over an appropriate time period. A *firm* should be able to demonstrate the selected probability of insolvency and time horizon it has derived and explain why these are appropriate for its business.
- 2.3.53 G Good models will have as inputs (in addition to the specific examples given under the stress and scenario guidance):  
For both *firms* carrying on *general insurance business* and *long-term insurance business*:
- (1) assumed future investment returns. In particular, assumptions for future interest rates (to the extent that they impact on interest income on funds on deposit, price of and yield on fixed stock that may be purchased in future and interest income on variable interest rate assets), equity prices, dividend income, property prices, property rental income and inflation. The assumptions should take account of likely volatility and historic volatility in interest rates and asset prices;

- (2) five-year predictions as to *premium* rates in each homogeneous category of business taking account of the effect of underwriting cycles;
- (3) predictions of exposures written in each homogeneous category of business in the next five years;
- (4) predictions of *premium* volume and expected growth under a five year business plan;
- (5) expenses and commission;
- (6) catastrophic events, aggregations of *claims* and *claims* affecting more than one *class* of business;
- (7) inflation in terms of how it might affect future *claims*, non-settled *claims* that have occurred to date, future expenses, future *reinsurance* costs and future investment returns;
- (8) *reinsurance* programmes in place, allowing for changing term conditions, reinstatements and loss experience features;
- (9) estimates of non-recovery of *reinsurance* and other debtors taking account of the financial strength of each *reinsurance* or other *counterparty*; and
- (10) foreign exchange movements.

For *firms* carrying on *general insurance business* in particular:

- (11) frequency and severity of *claims* (including costs associated with *claims* such as professional fees) for each homogeneous category of business, allowing for any impact of future social, legal and inflationary effects (especially concerning price, earnings, medical and *claims*) on future *claims* costs;
- (12) settlement patterns of *claims* and *reinsurance* recoveries for each homogeneous category of business (including occurred and future *claims*);
- (13) unintended coverage of risks; and
- (14) correlation between these risks.

For *firms* carrying on *long-term insurance business* in particular:

- (15) projected *claims* experience for each homogeneous category of business allowing for trends in mortality/ morbidity experience;
- (16) assumptions for future *policyholder* actions such as lapsing or surrendering a *policy*, ceasing to pay *premiums* or choosing to exercise an option under the contract; and
- (17) for business where management has discretion over the level of benefits or charges, assumptions about management reactions to changes in economic conditions and consequent changes to the benefits or charges.

- 2.3.54 G The *FSA* places credence in approaches to financial models to aid the assessment of capital adequacy which involve the production of a Dynamic Financial Analysis (“DFA”) model. These models transform each element in the financial projection into a statistical distribution with a range of possible outcomes, and are therefore stochastic. They would generally incorporate a suitable economic model integrated into the DFA model and linked into the generation of insurance related assumptions. The model would, as far as possible, cover all risks and all areas of business. The future time period over which projections are made should be determined with reference to the type of insurance business written, the asset profile and the insurance cycle. It may be appropriate to consider several different time periods.
- 2.3.55 G Due regard should also be given to the historical experience of both the *firm* and the wider relevant industry and market when assigning values to the above inputs.
- 2.3.56 G The values assigned to each of the above inputs should be derived either

stochastically, by assuming the value of an item can follow an appropriate probability distribution and by selecting appropriate values at the tail of the distribution, or deterministically, using appropriate prudent assumptions. For *long-term insurance business* which includes options or guarantees that change in value significantly in certain economic or demographic circumstances, a stochastic approach would normally be appropriate.

## Annex 1R

### Admissible assets in insurance

- (1) Investments that are, or amounts owed arising from the disposal of:
  - (a) *debt securities*, bonds and other money and capital market instruments;
  - (b) loans;
  - (c) *shares* and other variable yield participations;
  - (d) *units* in *UCITS schemes*, *non-UCITS retail schemes*, *recognised schemes* and any other *collective investment scheme* that invests only in *admissible assets* (including any *derivatives* or *quasi-derivatives* held by the scheme);
  - (e) land, buildings and immovable property rights;
  - (f) an *approved derivative* or *quasi-derivative* transaction that satisfies the conditions in *PRU 4.3.5R* or an *approved stock lending* transaction that satisfies the conditions in *PRU 4.3.36R*.
- (2) Debts and claims
  - (a) debts owed by *reinsurers*, including *reinsurers' shares of technical provisions*;
  - (b) *deposits* with and debts owed by *ceding undertakings*;
  - (c) debts owed by *policyholders* and *intermediaries* arising out of direct and *reinsurance* operations (except where overdue for more than 3 months and other than *commission* prepaid to agents or *intermediaries*);
  - (d) for *general insurance business* only, claims arising out of salvage and subrogation;
  - (e) for *long-term insurance business* only, advances secured on, and not exceeding the *surrender value* of, *long-term insurance contracts* issued by the *insurer*;
  - (f) tax recoveries;
  - (g) claims against *compensation funds*.
- (3) Other assets
  - (a) tangible fixed assets, other than land and buildings;
  - (b) cash at bank and in hand, *deposits* with *credit institutions* and any other bodies authorised to receive *deposits*;
  - (c) for *general insurance business* only, *deferred acquisition costs*;
  - (d) accrued interest and rent, other accrued income and prepayments;
  - (e) for *long-term insurance business* only, reversionary interests.



## Annex 2G

### Guidance on applications for waivers relating to implicit items

#### Implicit items under the Act

1. *PRU 2.2.14R* does not permit *implicit items* to be included in the calculation of a *firm's capital resources*, except subject to a *waiver* under section 148 of the *Act*. Article 27(4) of the *Consolidated Life Directive* states that *implicit items* can be included in the calculation of a *firm's capital resources*, within limits, provided that the supervisory authority agrees. Certain *implicit items*, however, are not eligible for inclusion beyond 31 December 2009 (see paragraph 5). The *FSA* may be prepared to grant a *waiver* from *PRU 2.2.14 R* to allow *implicit items*, in line with the purpose of the *Consolidated Life Directive*, and provided the conditions as set out in article 27(4) of the *Consolidated Life Directive* are met. Such a *waiver* would allow an *implicit item* to count towards the *firm's capital resources* available to count against its *capital resources requirement (CRR)* set out for *realistic basis life firms* in *PRU 2.1.15R* and for *regulatory basis only life firms* in *PRU 2.1.20R*. Where a *firm* applies for an *implicit item waiver* the *firm* may also apply for a *waiver* from *PRU 2.2.16R*, which requires at least 50% of a *firm's MCR* to be covered by *core tier one capital* and perpetual non-cumulative *preference shares*. Under *PRU 2.2.17R* a *firm* must meet the *guarantee fund* from the sum of the items listed at stages A, B, G and H less the sum of the items listed at stage E of *PRU 2.2.14R*. *PRU 2.2.17R* addresses the requirement in article 29(1) of the *Consolidated Life Directive* that *implicit items* should be excluded from capital eligible to cover the *guarantee fund*. Where an *implicit items waiver* is granted, an *implicit item* may potentially count as either *tier one* or *tier two capital*, but not *core tier one capital*. *PRU 2.2.20R* requires that at least 50 % of a *firm's tier one capital resources* must be accounted for by *core tier one capital*.
2. Under section 148 of the *Act*, the *FSA* may, on the application of a *firm*, grant a *waiver* from *PRU*. There are general requirements that must be met before any *waiver* can be granted. As explained in *SUP 8*, the *FSA* may not give a *waiver* unless the *FSA* is satisfied that:
  - (1) compliance by the *firm* with the *rules* will be unduly burdensome, or would not achieve the purpose for which the *rules* were made; and
  - (2) the *waiver* would not result in undue risk to *persons* whose interests the *rules* are intended to protect.
3. The *FSA* will assess compliance with the requirements in the light of all the relevant circumstances. This will include consideration of the costs incurred by compliance with a particular *rule* or whether a *rule* is framed in a way that would make compliance difficult in view of the *firm's* circumstances. For example, the *firm* may demonstrate that if an *implicit item* were not allowed, the *firm* would either have to suffer increased (and unwarranted) costs in injecting further *capital resources* or operate with a lower equity backing ratio (see case studies in paragraph 43). Even if a *firm* can demonstrate a case for an *implicit item waiver*, it should not assume that the *FSA* will grant the *waiver* requested, or that any *waiver* will be granted for the full

amount of the *implicit item* which could be granted, as set out in this annex. The *FSA* will consider each application on its own merits, and taking into account all relevant circumstances, including the financial situation and business prospects of the *firm*.

4. *Implicit items* are economic reserves which are contained within the *long-term insurance business* provisions. Article 27(4) of the *Consolidated Life Directive* identifies three types of *implicit item*, in respect of: future profits, *zillmerisation* and hidden reserves. This annex is intended to amplify the *guidance* in *SUP 8* relating to the granting of *waivers* for *implicit items* and to provide *guidance* on other aspects. Whilst this *guidance* applies to applications for *waivers* for *implicit items* generally, for a *realistic basis life firm*, to the extent that an *implicit item* is allocated to a *with-profits fund*, this *guidance* relates to *implicit items* for the purposes of determining the *regulatory value of assets* (see *PRU 7.4.24R*).
5. The *Consolidated Life Directive* (reflecting the changes introduced by the *Solvency I Directive*) requires member states to end a *firm's* ability to take into account future profits *implicit items* by (at the latest) 31 December 2009. Until then, the maximum amount of the *implicit item* relating to future profits permitted under the *Consolidated Life Directive* is limited to 50% of the product of the estimated annual profits and the average period to run (not exceeding six years) on the *policies* in the portfolio. The *Consolidated Life Directive* further limits the maximum amount of these economic reserves that can be counted to 25% of the lesser of the available solvency margin and the required solvency margin. The changes introduced by the *Solvency I Directive* take effect for financial years beginning on or after 1 January 2004. However, the *Consolidated Life Directive* allows for a transitional period of five years, which runs from 20 March 2002 (the publication date of the *Solvency I Directive*), for *firms* to become fully compliant with these new requirements. *Firms* will need to consider the potential impact of these changes when engaging in future capital planning. When applying for an *implicit item waiver* a *firm* should provide the *FSA* with a plan showing how the *firm* intends to maintain its capital adequacy over the period to 31 December 2009. *Firms* should also be aware that the *FSA* will typically only grant *waivers* for a maximum of 12 months.

#### Future Profits

6. The future profits *implicit item* allows *firms* to take credit for margins in the *mathematical reserves* to the extent that these are expected to emerge from in force business. The future profit from in force business should be assessed, in the first instance, on prudent assumptions, to demonstrate that there is an 'economic reserve'. Having demonstrated that it exists, the amount should be limited to an amount calculated using a formula that takes into account the actual profit which has emerged over the last five years (see paragraph 28).

#### Zillmerisation

7. *Zillmerisation* is an allowance for acquisition costs that are expected, under prudent assumptions, to be recoverable from future *premiums*. *Firms* can make a direct adjustment to their reserves for *zillmerisation*, subject to the *rules* on *mathematical reserves*. However, where no such adjustment has been made, the *FSA* will consider an application for a *waiver* to take into account an *implicit item*.

## Hidden reserves

8. Hidden reserves are reserves resulting from the underestimation of assets (other than *mathematical reserves*).

## Process for applying for a waiver, including limits applicable when a waiver is granted

9. This annex sets out the procedures to be followed and the form of calculations and data which should be submitted by *firms* to the *FSA*. This *guidance* should also be read in conjunction with the general requirements relating to the *waiver* process described in *SUP 8*. The *FSA* expects that applications for *waivers* in respect of future profits and *zillmerising* will not normally be considered to pass the “not result in undue risk to persons whose interests the *rules* are intended to protect” test unless the relevant criteria set out in this *guidance* have been satisfied and an application for such a *waiver* may require further criteria to be satisfied for this test to be passed. As set out below, *waivers* in respect of either *zillmerising* or hidden reserves will not normally be given except in very exceptional circumstances.

## Timing

10. A *long-term insurer* may apply to the *FSA* for a *waiver* in respect of *implicit items*. A *waiver* will not apply retrospectively (see *SUP 8.3.6G*). Consequently, applications intended for a particular accounting reference date will normally need to be made well before that reference date. Applications by *firms* must be made to the *FSA* in writing and include the relevant details specified under *SUP 8.3.3D*. Given the uncertainty in predicting the future, *waivers* will normally be granted for a maximum of 12 months at a time and any further applications will need to be made accordingly.
11. The information that will be required to enable an application to be considered as set out below, should normally include a demonstration of how the *capital resources requirement* is to be met, with and without the *waiver*. Clearly, up-to-date information may not be available before the *financial year-end*. In some cases information from the previous year-end’s *return* may be used, as long as any known significant changes in the structure of the *firm*, or the assumptions used, have been taken into account.
12. If the application for a *waiver* is granted, when a *firm* submits its next *return* the amount of the *implicit item* shown should not exceed that supported by the *firm’s* calculations as at the valuation date. In the event that the amount of the future profits item calculated by the *firm* based on these updated assumptions is less than the amount calculated at the time of the *firm’s* *waiver* application, the lower figure should be used in the *return*.
13. An *implicit item* in respect of *zillmerising* or hidden reserves is related to the basis on which liabilities or assets have been valued. In the case of hidden reserves, as explained below, the granting of a *waiver* will be dependent on the overall *capital resources* of the *firm*. *Waivers* in respect of these *implicit items* will, therefore, only be made in relation to the position shown in a particular set of *returns* and it will be essential for *firms* to submit applications to the *FSA* well in advance of the latest date for the submission of the relevant *return*.

14. *Waivers* may be withdrawn by the *FSA* at any time (e.g. where the *FSA* considers the amount in respect of which a *waiver* has been given can no longer be justified). This may be as a result of changes in the *firm's* position or as a result of queries arising on scrutiny of the *returns*.

#### Information to be submitted

15. An application for a *waiver* (which includes an application for an extension to or other variation of a *waiver*) should be prepared using the standard application form for a *waiver* (see *SUP 8 Ann 2D*). In addition, the application should be accompanied by full supporting information to enable the *FSA* to arrive at a decision on the merits of the case. In particular, the application should state clearly the nature and the amounts of the *implicit items* that a *firm* wishes to count against its *capital resources requirement* and the treatment it proposes to adopt in counting the *implicit items* towards the *firm's capital resources*. Furthermore, the application should demonstrate that in allowing for *implicit items* there has been no double counting of future margins and that the basis for valuing such margins is prudent.
16. The *FSA* recognises that the assessment of the insurance *technical provisions* reflects the contractual obligations of the *firm*. *Implicit items* are therefore margins over and above an economic assessment in these *technical provisions* only. Non-contractual “constructive” obligations arising from a *firm's* regulatory duty to treat *customers* fairly e.g. regarding future terminal bonuses, are not fully captured by the *technical provisions*. A *firm* must instead be satisfied that it has sufficient *capital resources* at all times to meet its obligations under *Principle 6*. The granting of a *waiver* for an *implicit item* does not in any way detract from this requirement and a *firm* will need to be satisfied that this condition is still met.
17. As a minimum, applications for a future profits *implicit item* should be supported by the information contained in Forms 13, 14, 18, 19, 40, 41, 42, 48, 49, the answers to questions 1 to 12 of the abstract of the valuation report, Appendix 9.4 of *IPRU(INS)*, the abstract of the valuation report for the realistic valuation, Appendix 9.4A of *IPRU(INS)* and Forms 51, 52, 53, 54 and 58. For a *zillmerisation implicit item*, only those items noted above forming part of the abstract valuation report will normally be needed. Applications for a *waiver* in respect of a hidden reserves *implicit item* will normally be considered only if accompanied by the information which is contained in the annual regulatory *returns*. In particular, the balance sheet forms, *long-term insurance business* revenue accounts, and abstract of the valuation report as set out in Appendices 9.1, 9.3 and 9.4 of *IPRU(INS)* should be provided. This is not to say that a full regulatory *return* must be provided in the specified format, simply that the information contained in these forms should be provided. Where appropriate, the information may be summarised.
18. The following supporting information relating to the calculation of the amounts claimed should be supplied for each type of *implicit item* in respect of which a *waiver* is sought:

Future profits: in addition to information related to the prospective calculation and retrospective calculation described below, the profits reported in each of the last five *financial years* up to the date of the most recent available valuation under *rule 9.4* of

*IPRU(INS)* which has been submitted to the *FSA* prior to, or together with, the application, and the amounts and nature of any exceptional items left out of account; the method used for calculating the average period to run and the results for each of the main categories of business, both before and after allowing for premature termination (where the calculation has been made in two stages); and the basis on which this allowance has been made.

*Zillmerising*: the categories of contracts for which an item has been calculated and the percentages of the *relevant capital sum* in respect of which an adjustment has been made.

Hidden reserves: particulars, with supporting evidence, of the undervaluation of assets for which recognition is sought.

#### Continuous monitoring by firms

19. *Firms* should take into account any material changes in financial conditions or other relevant circumstances that may have an impact on the level of future profits that can prudently be taken into account. *Firms* should also re-evaluate whether an application to vary an *implicit item waiver* should be made whenever circumstances have changed. In the event that circumstances have changed such that an amendment is appropriate, the *firm* must contact the *FSA* as quickly as possible in accordance with *Principle 11*. (See *SUP 8.5.1R*). In this context, the *FSA* would expect notice of any matter that materially impacts on the *firm's* financial condition, or any *waivers* granted.

#### Future profits - factors to take into account when submitting calculations to support waiver applications

20. Where an application is made in respect of a *firm* which has separate *with-profits funds* and *non-profit funds*, the *firm* should ensure that the *capital resources requirement* in respect of the *non-profit fund* is not covered by future profits attributable to *policyholders* arising in the *with-profits fund*. Furthermore, for a *realistic basis life firm* the amount of the *implicit item* allocated to each *with-profits fund* should be calculated separately, as the amount allocated to each *with-profits fund* will be taken into consideration in the calculation of the *with-profits insurance capital component* (see *PRU 7.4.24R*)
21. *Firms* need to assess prospective future profit (i.e. how much can reasonably be expected to arise) and compare this to maximum limits (in article 27(4) of the *Consolidated Life Directive*), which relate to past profits.

#### Future profits - prospective calculation

22. The application for a *waiver* should be supported by details of a prospective calculation of future profits arising from in-force business. The information supplied to the *FSA* should include a description of the method used in the calculation and of the assumptions made, together with the results arising. From 31 December 2009 at the latest, future profits *implicit items* will no longer be permitted under the *Consolidated Life Directive*. Where a *firm* first applies for an *implicit items waiver* after *PRU 2.2* comes into effect, under the prospective calculation a *firm* should only take into

consideration future profits that are expected to emerge in the period up to 31 December 2009. *Implicit item waivers* granted before *PRU 2.2* comes into effect will continue to operate under the terms of those *waivers*, but an application to vary the terms of such a *waiver*, for example to extend the effective period, is an application for a new *waiver* for which a *firm* should usually only take into consideration future profits that are expected to emerge in the period up to 31 December 2009.

#### Assumptions

23. The assumptions made should be prudent, rather than best estimate, assumptions of future experience (that is, the prudent assumptions should allow for the fair market price for assuming that risk including associated expenses). In particular, it would not normally be considered appropriate for the projected return on any asset to be taken to be higher than the risk-free yield (that is, assessed by reference to the yield arrived at using a model of future risk free yields properly calibrated from the forward gilts market). It may also be appropriate to bring future withdrawals into account on a suitably prudent basis. For *with-profits business*, the assumptions for future investment returns should not capitalise future bonus loadings except where the *with-profits policyholders* share in risks other than the investment performance of the fund. Furthermore, the rate at which future profits are discounted should include an appropriate margin over a risk free rate of return. Calculations should also be carried out to demonstrate that the prospective calculation of the future profits arising from the in-force business supporting the application for the *implicit item* would be sufficient to support the amount of the *implicit item* under each scenario described for use in determining the *resilience capital requirement* – where the *waiver* relates to an *implicit item* allocated to more than one fund, this should be demonstrated separately for that element of the *implicit item* allocated to each fund. For an *implicit item* allocated to a *with-profits fund*, proper allowance should be made for any shareholder transfers to ensure that the *implicit item* is not supported by future profits which will be required to support those transfers. To the extent, if any, that future profits are dependent on the levying of explicit expense related charges (for example as in the case of unit-linked business) the documentation submitted should include a demonstration of the prudence of the assumptions made as to the level at which future charges will be levied and expenses incurred.

Other limitations on the extent to which waivers for implicit items will be granted to a realistic basis life firm

24. Where a *waiver* in respect of an *implicit item* is granted to a *realistic basis life firm* additional limits may apply by reference to a comparison of *realistic excess capital* and *regulatory excess capital* including allowance for the effect of the *waiver*. Where the *waiver* relates to an *implicit item* allocated partly or entirely to a *with-profits fund*, the *waiver* will contain a limitation to the effect that the *regulatory excess capital* for that *with-profits fund*, allowing for the effect of the *waiver*, may not exceed that fund's *realistic excess capital*. This limitation will apply on an ongoing basis so that, for example, in the case of an *implicit item* allocated to a *with-profits fund*, the amount of the *implicit item* would be limited to zero whenever the *regulatory excess capital* exceeded the *realistic excess capital* of that fund.

Other charges to future profits

25. To avoid double counting, no account should be taken of any future surplus arising from assets corresponding to explicit items which have been counted towards the *capital resources requirement* such as shareholders funds, surplus carried forward or investment reserves. Deductions should be made in the calculation of future surpluses for the impact of any other arrangements which give rise to a charge over future surplus emerging (e.g. financial *reinsurance* arrangements, subordinated loan capital or contingent loan agreements). Deductions should also be made to the extent that any credit has been taken for the purposes of *PRU 7.4.45R(2)(c)* for the present value of future profits relating to non-profit business written in a *non-profit fund*. The information supplied to the *FSA* should identify the amount and reason for any adjustments made to the calculation of the prospective amount of future profits.
26. The *firm* should confirm to the *FSA* that the calculations have been properly carried out and that there are no other factors that should be taken into account.

#### Future profits - retrospective calculation

#### Overriding limit

27. The maximum amount of the *implicit item* relating to future profits permitted under the *Consolidated Life Directive* is 50% of the product of the estimated annual profit and the average period to run (not exceeding six years (ten years during the transitional period referred to in paragraph 5)) on the *policies* in the portfolio. Article 27(4) of the *Consolidated Life Directive* also imposes a further limit on the amount of the *implicit item* equal to 25% of the lower of:
  - (1) the *firm's capital resources*; and
  - (2) the higher of its *base capital resources requirement* for long-term insurance business and its *long-term insurance capital requirement*.

Once the transitional period set out in article 71(1) of the *Consolidated Life Directive* has expired in 2007 (see paragraph 5), the *FSA* will not allow a *waiver* for more than the amount permitted by article 27(4) of the Directive.

#### Definition of profits

28. The estimated annual profit should be taken as the average annual surplus arising in the *long-term insurance fund* over the last five *financial years* up to the date of the most recent available valuation which has been submitted to the *FSA* prior to, or together with, the application. For this purpose, deficiencies arising should be treated as negative surpluses. Where a *firm's financial year* has altered, the surplus arising in a period falling partly outside the relevant five year period should be assumed to accrue uniformly over the period in question for the purpose of estimating the profits arising within the five year period. When there has been a transfer of a block of business into the *firm* (or out of the *firm*) during the period, the impact of the transfer will need to be taken into account to reflect the remaining portfolio.

29. Where a *firm* has been carrying on *long-term insurance business* for less than 5 years, the total profits made during the past five years should be taken to be the aggregate of any surpluses that have arisen during the period in which *long-term insurance business* has been carried on less any deficiencies that may have arisen during that period. The resulting total should still be divided by five to obtain the estimated annual profit.

#### Exceptional items

30. Substantial items of an exceptional nature should be excluded from the calculation of the estimated annual profit. Such items include profits arising from an exceptional change in the value at which assets are brought into account, where this is not reflected in a similar change in the amount of the liabilities, and profits arising from a change in the overall valuation approach between one year and another. An exceptional loss (i.e. a reduction of an exceptional nature in the surplus arising) may be excluded from the calculation only to the extent that it can be set against a profit or profits up to the amount of the loss and arising from a similar cause. It is not intended, however, that any adjustment should be made for the effect on surplus of a net strengthening of reserves for costs associated with an expansion of the business or for special capital expenditure, such as the purchase of computer systems.

#### Double counting

31. The inclusion of investment income arising from the assets representing the explicit components of *capital resources* (as part of the estimated annual profit for the purpose of determining the future profits *implicit item*) would result in double-counting. If those assets were required to meet the effects of adverse developments, this would automatically result in the cessation of the contribution to profits from the associated investment income. It would clearly not be appropriate for the *FSA* to grant a *waiver* which would enable a *firm* to meet the *capital resources requirement* on the basis of counting both the capital values of the assets and the value of the income flow which they can be expected to generate.
32. The definition of the estimated annual profit as the surplus arising in the *long-term insurance fund* ensures that any contribution to surplus arising from transfers from the profit and loss account, including investment income on shareholders' assets, is not included in the estimated annual profit. Thus double-counting should not arise in respect of shareholders' assets. Double-counting may arise, however, in respect of the investment income from the assets representing the explicit components of *capital resources* carried within the *long-term insurance fund* (e.g. surplus carried forward or investment reserves), but the amount of such investment income is not separately identified in the *return*.
33. Where there is reason to suspect that the elimination of any such double-counting would reduce a *firm's capital resources* to close to or below the required level, or would otherwise be significant, the *FSA* will request this information with a view to taking account of this factor in determining the amount of the *implicit item*. Additional information concerning investment income should be furnished with an application for a *waiver*, if a *firm* believes that any double-counting would fall into one of the categories mentioned above.



#### Average period to run

34. The average number of years remaining to run on *policies* should be calculated on the basis of the weighted average of the periods for individual *contracts of insurance*, using as weights the actuarial present value of the benefits payable under the contracts. A separate weighted average should be calculated for each of the various categories of contract and the results combined to obtain the weighted average for the portfolio as a whole. Approximate methods of calculation, which the *firm* considers will give results similar to the full calculation, will be accepted. In particular, the *FSA* will normally accept the calculation of an average period to run for a specific category of contract on the basis of the average valuation factor for future benefits derived from data contained in the abstract of the valuation report in the regulatory *returns*. A *firm* will be asked to demonstrate the validity of the method adopted only where an abnormal distribution of the business in force gives grounds for doubt about its accuracy.
35. Calculations will normally be requested only for the main categories of *insurance business*, accounting for not less than 90% of the *mathematical reserves*, except where there are grounds for expecting that the exclusion of certain categories of *policies* under this provision might have a significant effect on the resulting average period to run. Detailed calculations will not be required where a *waiver* is sought in respect of a low multiple of the annual profits, well within the average period to run for the *firm*.
36. Where, for a particular category of business, a method of valuation is used which does not involve the calculation of the value of future benefits and which is significant for the *firm* in question, the calculation of the average period to run should be based on estimates of the value of future benefits.

#### Premature termination of contracts

37. Allowance should be made for the premature termination of *contracts of insurance*, based on the actual experience of the *firm* over the last five years, or other appropriate period, and taking into account specific features of contracts such as options which can be expected to lead to premature termination (e.g. guaranteed surrender values on income bonds written as *long-term insurance contracts* and option dates on flexible whole-life contracts). The adjustment should be made separately for each of the main categories of business. The use of industry-wide rates of termination will be acceptable where a *firm* is satisfied that this will result in sufficient allowance being made having regard to the *firm's* own experience. Methods of calculation that involve a degree of approximation will be permitted.
38. For certain types of contract, where the period left to run is most naturally defined as the term to a fixed maturity or expiry date, the allowance for premature termination should also take into account terminations resulting from death.

#### Overall limit

39. The overall average period left to run calculated as described above should be limited to a maximum of six years under article 27(4) of the *Consolidated Life Directive* (or a maximum of ten years during the transitional period referred to in paragraph 5) before

applying it to the estimated annual profit in order to determine the maximum value of the future profits *implicit item*.

#### Definition of period to run

40. The definition of the period to run and the basis of the allowance for early termination should clearly be considered together. For certain types of contracts (e.g. pension contracts with a range of retirement ages or other options), there is inherent uncertainty about the likely term to run. In such circumstances any estimate for determining the amount of the future profits *implicit item* for which a *waiver* is sought should be based on prudent assumptions tending, if anything, to underestimate the average period to run.

#### Zillmerising

41. The *FSA* does not normally expect to grant *waivers* permitting *implicit items* due to *zillmerisation* except in very exceptional circumstances. *Zillmerisation* is an allowance for acquisition costs that are expected, under prudent assumptions, to be recoverable from future *premiums*. *Firms* can make a direct adjustment to their reserves for *zillmerisation*, subject to the requirements on *mathematical reserves* set out in *PRU* 7.3.43R, and this is the usual approach. However, where no such adjustment has been made, or where the maximum adjustment has not been made in the *mathematical reserves*, the *FSA* will consider an application for an *implicit item*, if the amount is consistent with the amount that would have been allowed as an adjustment to *mathematical reserves* under *PRU* 7.3.43R.

#### Hidden reserves

42. The *FSA* will grant *waivers* permitting *implicit items* due to hidden reserves only in very exceptional circumstances. These items relate to hidden reserves resulting from the underestimation of assets. The *rules* for the valuation of assets and liabilities (see *PRU* 1.3) which apply to assets and liabilities other than *mathematical reserves* are based on the valuation used by the *firm* for the purposes of its external accounts, with adjustments for regulatory prudence such as concentration limits for large holdings, and would not normally be expected to contain hidden reserves.

#### Case studies on “unduly burdensome”

43. Some examples of situations where the existing *rules* might be considered to be unduly burdensome are given below:

*A firm* writes *with-profits business*. The *firm's* investment policy is affected by its published financial position. Application of the *rules* without an *implicit item* would result in the *firm* adopting a lower equity backing ratio. It may be possible to demonstrate that, in the circumstances, it would be unduly burdensome to require the *firm* to incur costs (which might prejudice *policyholders*) resulting from the lower equity backing ratio, rather than take allowance for an *implicit item*.

*A firm* has purchased a block of in-force business, on which the future profits may be reasonably estimated. However, this asset is given no value under the *rules*. It may be

possible to demonstrate that it is unduly burdensome for the *firm* to recognise the cost of acquiring the assets whilst giving no value to the asset acquired.

A *firm* has a block of in-force business, on which the future profits may be reasonably estimated. Application of the *rules* without an *implicit item* would result in a need to obtain additional capital. It may be possible to demonstrate that it is unduly burdensome, having regard to the particular circumstances of the *firm*, to require it to incur the costs involved in the injection of further capital rather than take allowance for an *implicit item*.

A *firm* has purchased matching assets for guaranteed annuity liabilities. The operation of the asset and liability valuation *rules* leads to statutory losses in certain circumstances in spite of good matching of assets and liabilities on a realistic basis of assessment. It may be possible to demonstrate that it is unduly burdensome to require the *firm* to incur the costs involved in the injection of further capital rather than take allowance for an *implicit item*.

Conditions which will typically be applied to implicit items waivers

Limits

44. Where *implicit items waivers* are granted, the value cannot exceed (and will normally be less than) the monetary limits described in paragraph 27, except that during the transitional period the pre-Solvency I limits will apply. In addition, time limits will apply and *waivers* will normally only last for 12 months.

Publicity

45. The *FSA* will publish the *waiver* (see *SUP* 8.6 and *SUP* 8.7). Public disclosure is standard practice unless the *FSA* is satisfied that publication is inappropriate or unnecessary (see section 148 of the *Act*). Any request that a direction not be published should be made to the *FSA* in writing with grounds in support, as set out in *SUP* 8.6.

Disclosure of a *waiver* will normally be required in the *firm's* annual *returns*.

	Annex 3G
A1	This annex provides an illustrative qualitative example of how a small <i>firm</i> could undertake its stress and scenario analysis without this being disproportionate to the size and complexity of its business so as to comply with <i>PRU</i> 1.2.35R. For these reasons, the example does not provide any quantitative guidance as we believe this would be impractical given the diverse nature of each <i>firm</i> 's individual circumstances.
A2	This example is based on <i>guidance</i> contained in <i>PRU</i> 2.3. The areas discussed are not exhaustive and it is likely that in practice a <i>firm</i> will need to consider a range of other issues.
A3	The scenarios that the <i>firm</i> generates as part of its analysis should aim to reflect the degree of risk in a variety of areas. How extreme these scenarios are will influence the ultimate level of capital required by the <i>firm</i> . The <i>firm</i> should not necessarily develop scenarios based on the current trading or economic conditions, but on possible trading or economic conditions that could occur during the next three to five years.
A4	In addition to examining its event scenarios, a <i>firm</i> should also be able to meet any individual risk (however unlikely) that it has accepted (or proposes to accept through its business plan) from <i>policyholders</i> . It therefore should analyse its exposures and ensure that it has sufficient capital or available <i>reinsurance</i> to cover its largest individual risks and accumulations.
	Worked example
	Background
A5	The <i>firm</i> used for this example is an <i>insurer</i> carrying on <i>general insurance business</i> within a large <i>group</i> , writing predominantly personal lines, household and motor policies of approximately £25m <i>gross written premium</i> . This business has a reasonable geographical spread, sourced significantly from within the <i>United Kingdom</i> . The <i>firm</i> has purchased appropriate <i>reinsurance</i> cover from a variety of <i>reinsurers</i> and has a demonstrated record of utilising this cover. Its settlement pattern for <i>claims</i> averages three years, however, there is a small element of the account with longer tail liability <i>claims</i> . The <i>firm</i> 's investments and IT support are outsourced.
	Insurance risk
A6	The risk of incorrect or inaccurate pricing of business over the scenario period can be addressed by examining typical uncertainties within the pricing basis and the volatility of <i>claims</i> experience.
A7	In examining the adequacy of its pricing, the <i>firm</i> establishes its underwriting and <i>claims</i> trend over a ten-year base period by reviewing profit and loss accounts (particularly underwriting profit). In particular it examines the following:
	(i) the volatility of losses in a particular line of business;
	(ii) whether the loss ratio exceeded 100% in any line of business; and
	(iii) whether the <i>deferred acquisition cost</i> (DAC) amount had been written down; e.g. whether an unexpired risk provision (URP) was necessary.
A8	The <i>firm</i> also examines whether its <i>premiums</i> over the last ten years have been:

	(i)	reasonably stable;
	(ii)	responsive enough to changes in <i>claim</i> exposures (so that profitability is maintained);
	(iii)	providing adequately for contingencies (such as major losses e.g. hail, earthquake etc);
	(iv)	encouraged loss control (through the use of deductibles, no claim bonuses etc);
A9	The <i>firm</i> also reviews its method of pricing. The <i>firm</i> considers and performs the following:	
	(i)	a review of acceptable rates, e.g. <i>premiums</i> being charged by competitors for similar products;
	(ii)	an examination of whether there have been any difficulties in the past with delegated authorities in relation to pricing including the ability and experience of staff members setting or recommending <i>premium</i> prices;
	(iii)	an examination of whether the <i>firm</i> has the appropriate mechanisms in place regarding <i>premium</i> rate changes (that is, who makes these decisions, frequency, and on what basis?); and
	(iv)	a benchmark price assessment (e.g. the ability to provide adequate competitive <i>premium</i> rates). For example, indicative rates being determined through the use of industry statistics, competitor statistics and the <i>firm's</i> own analysis for all classes.
A10	Other factors the <i>firm</i> considers are:	
	(i)	changes in environment (e.g. legislation, social, economic etc);
	(ii)	changes in <i>policy</i> conditions and deductibles; and
	(iii)	impact of market segments (e.g. the effects of different <i>claim</i> frequencies and costs impacting the price charged).
A11	Having completed its analysis, the <i>firm</i> makes the following assumptions to define its underwriting risk:	
	(i)	<i>claims</i> costs. The <i>firm</i> assumes these are X% higher than in the <i>premium</i> basis;
	(ii)	<i>claims</i> inflation. The <i>firm</i> assumes a X% <i>claims</i> inflation over the scenario period, compared to Y% in the pricing basis;
	(iii)	<i>policy</i> expenses (fixed and variable) are X% higher than anticipated in the pricing basis;
	(iv)	<i>reinsurance</i> charges are X% higher than anticipated in the pricing basis; and
	(v)	investment income is X% lower than anticipated in the pricing basis.
As a result of the above analysis on a per risk basis, the <i>firm</i> considers that capital of between £X and £Y would cover the possibility of material deviations to projected results.		
	Allowing for catastrophes	
A12	The allowance for catastrophic events within the insurance risk scenario should reflect both the severity and the frequency of these events.	
A13	After considering the catastrophe <i>reinsurance</i> programme it may be clear that the upper limit is set at a level unlikely to be breached e.g. a 1 in 200 year event. Thus, for the purposes of the capital assessment, it would not be necessary to assume losses in excess of this retention.	

A14	However, it may be determined that there is possible exhaustion of free reinstatements or of horizontal cover in total. For example, if there were a significant chance of three catastrophic losses in any one period but the <i>reinsurance</i> allowed only one free reinstatement, then the assessment may be to hold two retentions and the entire gross loss for the third event.
As a result of the above analysis, the <i>firm</i> considers it appropriate to hold capital sufficient to absorb three catastrophic losses: one European windstorm of £X, one UK flood of £Y, and one large man made explosion of £Z.	
The <i>reinsurance</i> structure in place allows for X number of reinstatements at full <i>premium</i> .	
Deterioration of reserves	
A15	The <i>firm</i> considers the adequacy of its <i>claims</i> reserves by focussing on the liability valuation.
A16	The liability valuation may contain a range of answers that might indicate possible reserve variability. Also, the valuation will contain areas where judgement has been applied and assumptions formulated which are subjective. These areas are considered and stressed as appropriate.
A17	The <i>firm</i> also reviews the historic level of <i>claims</i> reserves and subsequent level of settlements to help determine the size of any historic levels of under and over reserving.
A18	<i>Reinsurance</i> arrangements are considered and the extent to which these arrangements protect against reserve deterioration is assessed.
A19	For <i>unearned premium</i> , where losses have yet to occur, the <i>firm</i> considers that the level of uncertainty is greater and considers similar factors to those relating to underwriting risk in addition to those discussed above.
As a result of the above analysis, the <i>firm</i> considers it appropriate to apply a X% loading to the outstanding <i>claims</i> provision, a Y% loading to the <i>unearned premium</i> provision and Z% to all other liability values. The <i>firm</i> considers that capital of between £X and £Y would adequately cover reserve deterioration.	
Credit risk	
A20	Credit risk relates to the risk of default by <i>counterparties</i> . The <i>firm</i> believes its exposure to credit risk results from financial transactions with <i>counterparties</i> including issuers, debtors, borrowers, brokers, <i>policyholders</i> , <i>reinsurers</i> and guarantors.
A21	When assessing credit risk the <i>firm</i> makes an assessment of the creditworthiness of <i>counterparties</i> to the assets of the <i>firm</i> .
A22	The assessment includes an evaluation of the credit risk associated with loans and investment portfolios; the quality of on and off balance sheet assets; the ongoing management of the loans and investment portfolios; as well as loss provisions and reserves.
A23	The <i>firm</i> believes its exposure to credit risk also arises due to its exposure to its <i>reinsurers</i> . In this regard, the <i>firm</i> uses the credit ratings assigned to particular <i>counterparties</i> as a measure of credit risk, most notably Standard & Poor's, Moody's Investors Service and AM Best's (particularly for <i>reinsurers</i> ).
A24	When forming an opinion on credit risk the <i>firm</i> considers:
Reinsurance	
A25	The <i>firm</i> 's strategy is to lessen exposure to a single lead <i>reinsurer</i> to less than 30%, with other participants holding no more than 15%. In all cases,

	the panel of <i>reinsurers</i> all have a specified rating. The <i>firm</i> has no prior experience of disputes, and their working relationship with the panel may be excellent, and thus the <i>firm</i> does not envisage any future difficulties arising in this regard.
A26	Bond default rates could then be used to assess a likely credit risk figure for <i>reinsurance</i> recoveries (including <i>IBNR</i> recoveries).
	The <i>firm</i> considers that capital of between £X and £Y would cover <i>reinsurance</i> defaults, with no additional allowance for disputes.
	Overseas financial institutions and banks
A27	The <i>firm</i> investigates its business relationships with overseas financial institution <i>counterparties</i> including <i>banks</i> , and decides no additional allowance is required.
	Quality of counterparties and trends in counterparty risk
A28	The <i>firm</i> assesses the level and age of debtors, focussing particularly upon unpaid <i>premiums</i> , especially those greater than three months old, and reviews the level and trend of contingent liabilities. For example, the <i>firm</i> estimates that the credit risk scenario equates to taking a 10% reduction in the asset value of debtors, based on bond default rates and age of debt.
	The <i>firm</i> considers that capital of between £X and £Y would cover credit risk to counterparties.
	Off-balance sheet transactions
A29	The <i>firm</i> investigates any unfunded commitments, credit <i>derivatives</i> , commercial or standby letters of credit. Where these exist the possibility of a loss on these instruments is considered in relation to the requirement of the credit risk scenario.
	The <i>firm</i> considers that no additional capital is necessary.
	Market risk
A30	<i>Market risk</i> encompasses an adverse movement in the value of the assets as a consequence of market movements such as interest rates, foreign exchange rates, equity prices, etc. which is not matched by a corresponding movement in the value of the liabilities.
A31	In examining possible market risks, the <i>firm</i> considers its sensitivity to <i>market risk</i> by evaluating the degree to which changes in interest rates, foreign exchange rates, equity prices, or other areas can adversely affect the <i>firm's</i> earnings or capital.
A32	The <i>firm</i> believes its assets and liabilities are approximately matched e.g. there is no existence of large unmatched or unhedged currency positions; short tail business is backed by cash/fixed interest assets of suitable term and long tail business with real assets e.g. shares/property. If mismatching does exist this should be allowed for within the estimate.
A33	In developing the scenario the <i>firm</i> estimates the effect of a X% increase in interest rates on bond values.
A34	Similarly, the <i>firm</i> estimates the effect on equity values of a major recession to estimate the possible reduction in the value of equity capital. Also, it uses a suitable equity index to determine the size of historical falls in equity values and indicate possible future falls.
A35	<i>Counterparty</i> risk might be allowed for by assuming one or several major corporate bond holding defaults.
A36	For all investments, the stability of trading revenues should be examined to

	determine the volatility of investment.
From the above analysis, the <i>firm</i> considers that capital of between £X and £Y would be appropriate to protect it against adverse movement in <i>market risk</i> .	
Liquidity risk	
A37	<i>Liquidity risk</i> is the potential that the <i>firm</i> may be unable to meet its obligations as they fall due as a consequence of having a timing mismatch. The <i>firm</i> considers <i>liquidity risk</i> relates to the risk associated with the processes of managing timing relationship between asset and liability cash flow patterns.
A38	When assessing <i>liquidity risk</i> , the <i>firm</i> considers the extent of mismatch between assets and liabilities and the amount of assets held in a highly liquid, marketable form should unexpected cashflows lead to a liquidity crunch.
A39	The price concession of liquidating assets is a prime concern when assessing <i>liquidity risk</i> and is built into the scenario.
A40	In examining the <i>liquidity risk</i> , the <i>firm</i> examines the following:
Marketability, quality and liquidity of assets	
A41	The <i>firm</i> considers the assets held and makes an assessment regarding the quality and liquidity of these assets. Even though the assets matched the liabilities, residual risk remains given that timings are uncertain and there is a possibility that assets will be realised at unfavourable times. This is allowed for by assuming a 2.5% reduction in the market value of assets at realisation compared to the current market value.
The <i>firm</i> considers that capital of between £X and £Y would cover timing risk to <i>counterparties</i> .	
Reliance on new business income	
A42	The <i>firm</i> relies partially upon new business cash flows to meet current liabilities as they fall due. The <i>firm</i> analyses the sensitivity of future cash flow projections and new business assumptions and considers the effect of a reduced level of new business.
A43	The <i>firm</i> finds that it did not have immediate alternatives in place in case these expected new business cash flows were reduced. In this regard, it considers that these sources should be stressed by X%.
The <i>firm</i> considers that capital of between £X and £Y would cover possible effects of adjusting the asset portfolio to switch to more liquid assets.	
A44	The <i>firm</i> also examines the volatility and cost of on- and off-balance sheet funding sources. The <i>firm</i> is satisfied that no concerns need to be raised and that there should not be any impact on its liquidity position.
A45	The <i>firm</i> believes it is well placed to manage unplanned changes in funding sources as well as react to changes in market conditions that affect its ability to quickly liquidate assets with minimal loss. The <i>firm</i> assesses that it has reasonable access to money markets and other sources of funding such as lines of credit.
A46	The <i>firm</i> has no previous problems or delays in meeting obligations (or accessing external funding).
Overall, from the above analysis, the <i>firm</i> considers that capital of between £X and £Y would be necessary to withstand the effects of deterioration in liquidity.	
Governance Risk	
A47	Governance risk relates to the risk associated with the board and/or senior



	management of the <i>firm</i> not effectively performing their respective roles.
A48	The existence and level of directors and officers insurance in place is investigated compared to known incidence of <i>claims</i> of this type.
A49	The <i>firm</i> assesses whether the current level of governance is appropriate for the <i>firm</i> , and the likelihood that the <i>firm's</i> practices may result in the board and/or senior management not adequately undertaking their roles. The cost of altering and strengthening the current board structure is considered.
A50	In this regard, the <i>firm</i> makes an assessment that it may be reliant on only a few senior executives, and may be exposed if they experience any misadventure.
The <i>firm</i> considers that capital of between £X and £Y would cover governance risk.	
Strategic Risk	
A51	Strategic risk arises from an inability to implement appropriate business plans and strategies, make decisions, allocate resources or adapt to changes in the business environment.
A52	The <i>firm</i> therefore assesses the prudence and appropriateness of its business strategy in the context of the <i>firm's</i> competitive and economic environment. In particular the assumptions, forecasting and projections are assessed considering the possibility of a fundamental market change due, for example, to higher numbers of competitors, changes in sales channels, new forms of insurance or changes in legislation. This review includes whether the <i>reinsurance</i> programme is appropriate for the risks selected by the <i>firm</i> and whether it adequately takes account of the underwriting and business plans of the <i>firm</i> generally.
A53	The <i>firm</i> considers the likelihood of a fundamental strategic shift too remote to include within the scenario given the maturity of the market in which they operate.
Operational risks	
A54	In reviewing the operational risk exposures, the <i>firm</i> has examined its administration, compliance, event, fraud, governance, strategic and technological risks.
Administration	
A55	The <i>firm</i> considers the risk of error or failure associated with the administrative aspects of the operation of its business. In this regard, the <i>firm</i> considers likelihood of financial loss and reputation harm due to failure or errors occurring and the likely size of these losses.
A56	None of the <i>firm's</i> administration is out-sourced to service providers.
A57	In undertaking the assessment, the <i>firm</i> considers the history of failure or error from transaction processing or control within the <i>firm</i> . Exception reports are produced on a quarterly basis. Past reports highlighted past administrative deficiencies. The biggest event in the past 10 years related to a situation where <i>claim</i> -handling staff shared access codes to the <i>claims</i> administration system. This resulted in an overpayment to some clients.
A58	The <i>firm</i> also examines the nature and extent of centralised and decentralised functions within the <i>firm</i> . Three branches report regularly to the central office and an appropriate system is in place to record financial information, handle complaints etc.
A59	The <i>firm</i> also reviews the segregation of duties between staff. It is satisfied that an adequate segregation of duties between underwriting <i>claims</i> and

	payments divisions exist in terms of acceptance, authorisation and payments. It is also satisfied that sufficient interaction between the front, middle and back offices exist in terms of financial control and risk management. For example, it is confident that its guidelines for accepting risks are adequate and that any breach would be picked up by exception reporting.
A60	The <i>firm</i> also investigates the level of staff expertise and training to administer its product range/services.
	The <i>firm</i> considers that capital of between £X and £Y would cover the risk of future administration issues.
	Compliance Risk
A61	The <i>firm</i> believes its main compliance risk relates to the risk of non-adherence to legislative and internal <i>firm</i> requirements.
A62	An investigation into compliance over the last 10 years finds no history of non-compliance with <i>firm</i> policy and control systems nor have there been any reported areas of non-compliance with legislation or other requirements.
A63	Regulatory reforms including corporate and consumer law are considered and it is assumed that expenses costs will rise as a result of developments in the next 5 years. As a result an additional X% of <i>premium</i> income was assumed for the expense ratio.
	The <i>firm</i> considers that capital of between £X and £Y would cover the risk of future compliance issues.
	Event risk
A64	Event risk relates to risks associated with the potential impact of significant events (e.g., financial system crisis, major change in fiscal system, natural disaster) on the operations of the <i>firm</i> .
A65	The definition of event risk is not intended to cover events that are directly associated with products and services offered, for example, events which may directly impact on the <i>general insurance business</i> .
A66	The <i>firm</i> concludes that no additional specific allocation is required.
	Fraud Risk
A67	Fraud risk relates to the risk associated with intentional misappropriation of funds, undertaken with the objective of personal benefit at the expense of the <i>firm</i> .
A68	In assessing fraud risk, the <i>firm</i> considers the possibility of fraudulent acts occurring within the <i>firm</i> and the extent of controls which management has established to mitigate such acts.
A69	The <i>firm</i> examines fraud issues over a period of 10 years and finds one major incident where it was subject to a fraudulent activity. This involved fraudulent payments being made by a member of staff which resulted in a loss for the <i>firm</i> of £Xm. Based on this previous incident and allowing for improvements in controls, the company assessed a financial figure that it believes is consistent with the probability for this scenario.
	The <i>firm</i> considers that capital of between £X and £Y would cover the risk of future fraud.
	Technology Risk
A70	The <i>firm</i> considers the risk of error or failure associated with the technological aspects (IT systems) of its operations. Specifically, technology risk refers to both the hardware systems and the software utilised to run those systems.

A71	In relation to the <i>firm's</i> information systems, the <i>firm</i> assesses the past reliability and future functionality and believes them to be adequate. It does not have any future plans to either replace its systems or make major systems modifications.
A72	Concerning business continuity management and disaster recovery planning (and testing of plans), the <i>firm</i> reviews these plans regularly and tests them quarterly. A full back-up site exists with full recovery capabilities. Costs associated with utilising the site and associated business interruption insurance was estimated.
The <i>firm</i> considers that capital of between £X and £Y would cover technology risk.	
Group risk	
A73	The size of the group risk element within operational risk will depend on the ownership structure of the <i>firm</i> and how it is funded by the parent.
A74	The <i>firm</i> considers the likelihood and financial consequences of both insolvency and credit downgrading of its parent. Given the <i>firm</i> shares the parent's name there is a large risk of association.
A75	The <i>firm</i> considers it within the scope of the scenario to allow for a single downgrade of the parent's credit rating from AA to A. It does not believe the chance of insolvency great enough to allow for directly.
A76	The <i>firm</i> estimates the effect on its business plan and profit margins of the downgrade. It estimates the amount of business lost and the increase in marketing costs required to maintain the client base. It also allows for a change in the pricing basis to incorporate a reduced profit margin (with knock on impacts on the business volume and loss ratios).
From the above analysis, the <i>firm</i> considers that capital of between £X and £Y would be required to cover group risks.	
Overall assessment	
A77	After individually assessing each risk area, the <i>firm</i> considers the capital that it has estimated might be absorbed under each scenario. In aggregate the range of capital absorbed is between £X and £Y. It considers how many of these scenarios might reasonably occur within a period and the extent to which it could replace capital within that period. It takes into account scenarios which might reasonably be linked, the difficulty with which capital might be replaced if the scenarios occurred, and the changes in strategy which might need to be adopted if the scenarios occurred.
A78	The <i>firm</i> decides that the worst realistic combination of circumstances that might arise would absorb capital of between £A and £B.

## Annex E

### PRU 3

In this Annex, all the text is new and is not underlined.

#### 3.1 Credit risk management systems and controls

##### Application

3.1.1 G *PRU 3.1* applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

3.1.2 G *PRU 3.1* applies to:

- (1) an *EEA-deposit insurer*; and
- (2) a *Swiss general insurer*;  
only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

##### Purpose

3.1.3 G This section provides *guidance* on how to interpret *PRU 1.4* insofar as it relates to the management of credit risk.

3.1.4 G Credit risk is incurred whenever a *firm* is exposed to loss if another party fails to perform its financial obligations to the *firm*, including failing to perform them in a timely manner. It arises from both on and off balance sheet items. For contracts for traded *financial instruments*, for example the purchase and sale of *securities* or *over the counter derivatives*, risks may arise if the *firm's counterparty* does not honour its side of the contract. This constitutes counterparty risk, which can be considered a subset of credit risk. Another risk is issuer risk, which could potentially result in a *firm* losing the full price of a market instrument since default by the issuer could result in the value of its bonds or stocks falling to nil. In insurance *firms*, credit risk can arise from *premium* debtors, where cover under *contracts of insurance* may either commence before *premiums* become due or continue after their non-payment. Credit risk can also arise if a *reinsurer* fails to fulfil its financial obligation to repay a *firm* upon submission of a *claim*.

3.1.5 G Credit risk concerns the *FSA* in a *prudential context* because inadequate systems and controls for credit risk management can create a threat to the *regulatory objectives* of market confidence and consumer protection by:

- (1) the erosion of a *firm's* capital due to excessive credit losses thereby threatening its viability as a going concern;
- (2) an inability of a *firm* to meet its own obligations to depositors, *policvholders* or other market *counterparties* due to capital erosion.

- 3.1.6 G Appropriate systems and controls for the management of credit risk will vary with the scale, nature and complexity of the *firm's* activities. Therefore the material in this section is *guidance*. A *firm* should assess the appropriateness of any particular item of *guidance* in the light of the scale, nature and complexity of its activities as well as its obligations as set out in *Principle 3* to organise and control its affairs responsibly and effectively.

#### Requirements

- 3.1.7 G High level requirements for prudential systems and controls, including those for credit risk, are set out in *PRU 1.4*. In particular:
- (1) *PRU 1.4.19R(2)* requires a *firm* to document its policy for credit risk, including its risk appetite and how it identifies, measures, monitors and controls that risk;
  - (2) *PRU 1.4.19R(2)* requires a *firm* to document its provisioning policy. Documentation should describe the systems and controls that it intends to use to ensure that the policy is correctly implemented;
  - (3) *PRU 1.4.18R* requires it to establish and maintain risk management systems to identify, measure, monitor and control credit risk (in accordance with its credit risk policy), and to take reasonable steps to ensure that its systems are adequate for that purpose;
  - (4) In line with *PRU 1.4.11G*, the ultimate responsibility for the management of credit risk should rest with a *firm's governing body*. Where delegation of authority occurs the *governing body* and relevant *senior managers* should approve and periodically review systems and controls to ensure that delegated duties are being performed correctly.

#### Credit risk policy

- 3.1.8 G *PRU 1.4.18R* requires a *firm* to establish, maintain and document a business plan and risk policies. They should provide a clear indication of the amount and nature of credit risk that the *firm* wishes to incur. In particular, they should cover for credit risk:
- (1) how, with particular reference to its activities, the *firm* defines and measures credit risk;
  - (2) the *firm's* business aims in incurring credit risk including:
    - (a) identifying the types and sources of credit risk to which the *firm* wishes to be exposed (and the limits on that exposure) and those to which the *firm* wishes not to be exposed (and how that is to be achieved, for example how exposure is to be avoided or mitigated);

- (b) specifying the level of diversification required by the *firm* and the *firm's* tolerance for risk concentrations (and the limits on those exposures and concentrations); and
  - (c) drawing the distinction between activities where credit risk is taken in order to achieve a return (for example, lending) and activities where credit exposure arises as a consequence of pursuing some other objective (for example, the purchase of a *derivative* in order to mitigate *market risk*);
- (3) how credit risk is assessed both when credit is granted or incurred and subsequently, including how the adequacy of any security and other risk mitigation techniques is assessed;
- (4) the detailed limit structure for credit risk which should:
- (a) address all key risk factors, including *intra-group* exposures and indirect exposures (for example, exposures held by *related* and *subsidiary undertakings*);
  - (b) be commensurate with the volume and complexity of activity;
  - (c) be consistent with the *firm's* business aims, historical performance, and its risk appetite;
- (5) procedures for:
- (a) approving new or additional exposures to *counterparties*;
  - (b) approving new products and activities that give rise to credit risk;
  - (c) regular risk position and performance reporting;
  - (d) limit exception reporting and approval; and
  - (e) identifying and dealing with problem exposures caused by the failure or the downgrading of a *counterparty*;
- (6) the methods and assumptions used for the stress testing and scenario analysis required by *PRU 1.2* (Adequacy of financial resources), including how these methods and assumptions are selected and tested;
- (7) the allocation of responsibilities for implementing the credit risk policy and for monitoring adherence to, and the effectiveness of, the policy.

Counterparty assessment

- 3.1.9 G The *firm* should make a suitable assessment of the risk profile of the *counterparty*. The factors to be considered will vary according to both the type of credit and the *counterparty* being considered. This may include:
- (1) the purpose of the credit, the duration of the agreement and the source of repayment;
  - (2) an assessment and continuous monitoring of the credit quality of the *counterparty*;
  - (3) an assessment of the *claims* payment record where the *counterparty* is a *reinsurer*;
  - (4) an assessment of the nature and amount of risk attached to the *counterparty* in the context of the industrial sector or geographical region or country in which it operates, as well as the potential impact on the *counterparty* of political, economic and market changes; and
  - (5) the proposed terms and conditions attached to the granting of credit, including ongoing provision of information by the *counterparty*, covenants attached to the facility as well as the adequacy and enforceability of *collateral*, security and guarantees.
- 3.1.10 G It is important that sound and legally enforceable documentation is in place for each agreement that gives rise to credit risk as this may be called upon in the event of a default or dispute. A *firm* should therefore consider whether it is appropriate for an independent legal opinion to be sought on documentation used by the *firm*. Documentation should normally be in place before the *firm* enters into a contractual obligation or releases funds.
- 3.1.11 G Where *premium* payments are made via *brokers* or *intermediaries*, the *firm* should describe how it monitors and controls its exposure to those *brokers* and *intermediaries*. In particular, the policy should identify whether the risk of default by the *broker* or *intermediary* is borne by the *firm* or the *policyholder*.
- 3.1.12 G Any variation from the usual credit policy should be documented.
- 3.1.13 G A *firm* involved in loan syndications or consortia should not rely on other parties' assessment of the credit risks involved. It will remain responsible for forming its own judgement on the appropriateness of the credit risk thereby incurred with reference to its stated credit risk policy. Similarly a *firm* remains responsible for assessing the credit risk associated with any insurance or *reinsurance* placed on its behalf by other parties.
- 3.1.14 G Where a credit scoring approach or other *counterparty* assessment process is used, the *firm* should periodically assess the particular approach taken in the light of past and expected future *counterparty* performance and ensure that any statistical process is adjusted accordingly to ensure that the business written complies with the *firm's* risk appetite.

- 3.1.15 G In assessing its contingent exposure to a *counterparty*, the *firm* should identify the amount which would be due from the *counterparty* if the value, index or other factor upon which that amount depends were to change.

#### Credit risk measurement

- 3.1.16 G A *firm* should measure its credit risk using a robust and consistent methodology which should be described in its credit risk policy; the appropriate method of measurement will depend upon the nature of the credit product provided. The *firm* should consider whether the measurement methodologies should be backtested and the frequency of such backtesting.
- 3.1.17 G A *firm* should also be able to measure its credit exposure across its entire portfolio or within particular categories such as exposures to particular industries, economic sectors or geographical areas.
- 3.1.18 G Where a *firm* is a member of a *group* that is subject to consolidated reporting, the *group* should be able to monitor credit exposures on a consolidated basis. See *PRU 8* (Group risk).
- 3.1.19 G A *firm* should have the capability to measure its credit exposure to individual *counterparties* on at least a daily basis.

#### Risk monitoring

- 3.1.20 G A *firm* should implement an effective system for monitoring its credit risk which should be described in its credit risk policy.
- 3.1.21 G A *firm* should have a system of management reporting which provides clear, concise, timely and accurate credit risk reports to relevant functions within the *firm*. The reports could cover exceptions to the *firm's* credit risk policy, non-performing exposures and changes to the level of credit risk within the *firm's* credit portfolio. A *firm* should have procedures for taking appropriate action according to the information within the management reports, such as a review of *counterparty* limits, or of the overall credit policy.
- 3.1.22 G Individual credit facilities and overall limits should be periodically reviewed in order to check their appropriateness for both the current circumstances of the *counterparty* and the *firm's* current internal and external economic environment. The frequency of review should be appropriate to the nature of the facility.
- 3.1.23 G A *firm* should utilise appropriate stress testing and scenario analysis of credit exposures to examine the potential effects of economic or industry downturns, market events, changes in interest rates, changes in foreign exchange rates, changes in liquidity conditions and changes in levels of insurance losses where relevant.

#### Problem exposures



- 3.1.24 G A *firm* should have systematic processes for the timely identification, management and monitoring of problem exposures. These processes should be described in the credit risk policy.
- 3.1.25 G A *firm* should have adequate procedures for recovering exposures in arrears or that have had provisions made against them. A *firm* should allocate responsibility, either internally or externally, for its arrears management and recovery.

#### Provisioning

- 3.1.26 G *PRU* 1.4.19R(2) requires a *firm* to document its provisioning policy. A *firm*'s provisioning policy can be maintained either as a separate document or as part of its credit risk policy.
- 3.1.27 G At intervals that are appropriate to the nature, scale and complexity of its activities a *firm* should review and update its provisioning policy and associated systems.
- 3.1.28 G In line with *PRU* 3.1.6G, the *FSA* recognises that the frequency with which a *firm* reviews its provisioning policy once it has been established will vary from *firm* to *firm*. However, the *FSA* expects a *firm* to review at least annually whether its policy remains appropriate for the business it undertakes and the economic environment in which it operates.
- 3.1.29 G In line with *PRU* 1.4.12G, the provisioning policy referred to in *PRU* 3.1.26G must be approved by the *firm's governing body* or another appropriate body to which the *firm's governing body* has delegated this responsibility.
- 3.1.30 G In line with *PRU* 1.4.24G, the *FSA* may request a *firm* to provide it with a copy of its current provisioning policy.
- 3.1.31 G Provisions may be general (against the whole of a given portfolio), specific (against particular exposures identified as bad or doubtful) or both. The *FSA* expects contingent liabilities (for example guarantees) and anticipated losses to be recognised in accordance with accepted accounting standards at the relevant time, such as those embodied in the Financial Reporting Standards issued by the Accounting Standards Board.

#### Risk mitigation

- 3.1.32 G A *firm* may choose to use various credit risk mitigation techniques including the taking of *collateral*, the use of letters of credit or guarantees, or *counterparty netting* agreements to manage and control their *counterparty* exposures. The use of such techniques does not obviate the need for thorough credit analysis and procedures. The reliance placed by a *firm* on risk mitigation should be described in the credit risk policy.
- 3.1.33 G A *firm* should consider the legal and financial ability of a guarantor to fulfil the guarantee if called upon to do so.

- 3.1.34 G A *firm* should monitor the validity and enforceability of its *collateral* arrangements.
- 3.1.35 G The *firm* should analyse carefully the protection afforded by risk mitigants such as *netting* agreements or credit *derivatives*, to ensure that any residual risk is identified, measured, monitored and controlled.

#### Record keeping

- 3.1.36 G Prudential records made under *PRU* 1.4.53R should include appropriate records of:
- (1) credit exposures, including aggregations of credit exposures, as appropriate, by:
    - (a) groups of connected *counterparties*;
    - (b) types of *counterparty* as defined, for example, by the nature or geographical location of the *counterparty*;
  - (2) credit decisions, including details of the decision and the facts or circumstances upon which it was made; and
  - (3) information relevant to assessing current *counterparty* and risk quality.
- 3.1.37 G Credit records should be retained as long as they are needed for the purpose described in *PRU* 3.1.36G (subject to the minimum three year retention period). In particular, a *firm* should consider whether it is appropriate to retain information regarding *counterparty* history such as a record of credit events as well as a record indicating how credit decisions were taken.

## 3.2 Credit risk in insurance

### Application

- 3.2.1 R *PRU 3.2* applies to an *insurer* unless it is:
- (1) a *non-directive friendly society*; or
  - (2) an *incoming EEA firm*; or
  - (3) an *incoming Treaty firm*.
- 3.2.2 R All of *PRU 3.2*, except *PRU 3.2.20R* and *PRU 3.2.23R* to *PRU 3.2.32G*, applies to:
- (1) an *EEA-deposit insurer*; and
  - (2) a *Swiss general insurer*;
- but only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.
- 3.2.3 G The scope of application of *PRU 3.2* is not restricted to *firms* that are subject to relevant EC directives. It applies, for example, to *pure reinsurers*.
- 3.2.4 R (1) This section applies to a *firm* in relation to the whole of its business, except where a particular provision provides for a narrower scope.
- (2) Where a *firm* carries on both *long-term insurance business* and *general insurance business*, this section applies separately to each type of business.

### Purpose

- 3.2.5 G The purpose of this section is to protect *policyholders* and potential *policyholders* by setting out the requirements applicable to a *firm* in respect of credit risk. Credit risk is incurred whenever a *firm* is exposed to loss if a *counterparty* fails to perform its contractual obligations including failure to perform them in a timely manner. Credit risk may therefore have an impact upon a *firm*'s ability to meet its valid *claims* as they fall due. Credit risk can also arise from underlying causes that have an impact upon the creditworthiness of all *counterparties* of a particular description or geographical location. A detailed explanation of credit risk is given at *PRU 3.1.4G*.
- 3.2.6 G The requirements in this section address both current and contingent exposure to credit risk. *PRIN*, *SYSC* and *PRU 1.4* require a *firm* to establish adequate internal systems and controls for exposure to credit risk. This section requires a *firm* to restrict its exposure to different *counterparties* and assets to prudent levels and to ensure that those exposures are adequately diversified. It also requires a *firm* to make deductions from the value of assets in respect of exposures to one asset, *counterparty* or group of closely related *counterparties* in excess of prescribed limits.
- 3.2.7 G This section also sets limits on the *market risk* arising from holding assets including *securities* issued or guaranteed by *counterparties*. This *market risk* is incurred whenever a

*firm* is exposed to loss if an asset were to reduce in value or even become worthless. These *market risk* limits are set out in this section rather than the *market risk* sections in *PRU* because they are closely linked to the *counterparty* limits set out in this section.

#### Overall limitation of credit risk

- 3.2.8 R Taking into account relevant risks, a *firm* must restrict its *counterparty* exposures and asset exposures to prudent levels and ensure that those exposures are adequately diversified.
- 3.2.9 R
- (1) For the purposes of *PRU* 3.2, *counterparty* exposure is the amount a *firm* would lose if a *counterparty* were to fail to meet its obligations (either to the *firm* or to any other *person*) and if simultaneously *securities* issued or guaranteed by the *counterparty* were to become worthless.
  - (2) For the purposes of *PRU* 3.2, asset exposure is the amount a *firm* would lose if an asset or class of identical assets (whether or not held directly by the *firm*) were to become worthless.
  - (3) For the purposes of (1) and (2), the amount of loss is the amount, if any, by which the *firm's* capital resources (as calculated in accordance with *PRU* 2.2.14R but without making any deduction for assets in excess of *market risk* and *counterparty* limits) would decrease as a result of the *counterparty* failing to meet its obligations and the *securities* or assets becoming worthless.
  - (4) In determining the amount of loss in accordance with (3), the *firm* must take into account decreases in its capital resources that would result not only from its own direct exposures but also from:
    - (a) exposures held by any of its *subsidiary undertakings*; and
    - (b) synthetic exposures arising from *derivatives* or *quasi-derivatives* held or entered into by the *firm* or any of its *subsidiary undertakings*.
  - (5) If a *firm* elects under *PRU* 3.2.35R to make a deduction in respect of *collateral*, the *firm* must deduct from the amount of loss determined in accordance with (3) so much of the value of that *collateral* as:
    - (a) would be realised by the *firm* were it to exercise its rights in relation to the *collateral*; and
    - (b) does not exceed any of the relevant limits in *PRU* 3.2.22R(3).
- 3.2.10 G Exposure is defined in terms of loss (which is decrease in capital). It does not include exposures arising from assets that are not represented in capital or exposures which if crystallised in a loss would be offset by a consequent gain, reduction in liabilities or release of provisions, but only in so far as that gain, reduction or release would itself lead to an offsetting increase in *capital resources*. Examples include:
- (1) exposure from the holding of assets to which the *firm* has attributed no value;
  - (2) exposure from the holding of assets that the *firm* has deducted from *capital*

*resources*; and

- (3) exposure in respect of which (and to the extent that) the *firm* has established a provision.

3.2.11 G In assessing the adequacy of diversification required by *PRU 3.2.8R*, a *firm* should take into account concentrations of exposure including those arising from:

- (1) different types of exposure to the same *counterparty*, such as *deposits*, loans, *securities*, *reinsurance* and *derivatives*;
- (2) links between *counterparties* such that default by one might have an impact upon the creditworthiness of another; and
- (3) possible changes in circumstance that would have an impact upon the creditworthiness of all *counterparties* of particular description or geographical location.

3.2.12 G A *firm* should consider how the spreading of credit risk will impact on overall *counterparty* quality.

3.2.13 G In assessing its exposure to a *counterparty* for the purpose of *PRU 3.2.8R*, a *firm* should take into account:

- (1) the period for which the exposure to that *counterparty* might continue;
- (2) the likelihood of default during that period by the *counterparty*; and
- (3) the loss that might result in the event of default.

3.2.14 G In assessing the loss that might result from the default of a *counterparty* for the purposes of *PRU 3.2.8R*, a *firm* should take into account the circumstances that might lead to default and, in particular, how these might have an impact upon:

- (1) the amount of exposure to the *counterparty*; and
- (2) the effectiveness of any loss mitigation techniques employed by the *firm*.

3.2.15 G Often the same circumstances which lead to the crystallisation of contingent credit exposure, e.g. a significant *claims* event or a significant movement in interest, currency or asset values, also lead to an increase in the risk of default by the *counterparty*. In particular, if a *reinsurer* or *derivative counterparty* is being relied upon to provide protection against the consequences of an event or circumstance, a *firm* should take into account how that event or circumstance might have an impact upon the creditworthiness of the *reinsurer* or *derivative counterparty*.

3.2.16 R For the purposes of *PRU 3.2.8R* and of determining *counterparty* exposure and asset exposure in accordance with *PRU 3.2.9R* and *reinsurance* exposure in accordance with *PRU 3.2.25R*, a *firm* must only rely upon a loss mitigation technique where it has good reason to believe that, taking into account the possible circumstances of default, it is likely to be effective.

- 3.2.17 G Loss mitigation techniques include:
- (1) the right, upon default, to preferential access to some or all of the *counterparty's* assets, for example by exercising rights of set off, holding *collateral* or assets deposited back, or exercising rights under fixed or floating charges;
  - (2) rights against third parties upon default by the *counterparty*, such as guarantees, credit insurance and credit *derivatives*; and
  - (3) where the *counterparty* is a *reinsurer*, having back-up or flexible *reinsurance* which covers the gap in coverage left by the *reinsurer's* default, for example 'top and drop' *reinsurance*.
- 3.2.18 R For the purposes of *PRU* 3.2.8R and of determining *counterparty* exposure and asset exposure in accordance with *PRU* 3.2.9R and *reinsurance* exposure in accordance with *PRU* 3.2.25R, a *firm* must not rely upon preferential access to assets unless it has taken into account appropriate professional advice as to its effectiveness.
- 3.2.19 G In particular, a *firm* should consider whether any preferential access to a *counterparty's* assets would be effective even if the *counterparty* were wound up by a court or other legal process or it were to be subject to any other insolvency process. A *firm* should also consider, where it is relying upon a right against a third party, whether, in the circumstances of the *counterparty's* default, the creditworthiness of that third party might be impaired.

#### Large exposure limits

- 3.2.20 R (1) A *firm* must take reasonable steps to limit its *counterparty* exposure or asset exposure to:
- (a) a single *counterparty*;
  - (b) each of the *counterparties* within a group of closely related *counterparties*; and
  - (c) an asset or class of identical assets;
- to a level where, if a total default were to occur, the *firm* would not become unable to meet its liabilities as they fall due.
- (2) In (1), a total default occurs where:
- (a) the single *counterparty* or all of the *counterparties* within the group of closely related *counterparties* fail to meet its or their obligations and simultaneously any *securities* issued or guaranteed by it or any of them become worthless; or
  - (b) the asset becomes worthless or all of the assets within the identical class become worthless at the same time.
- (3) (1) does not apply to:
- (a) a *reinsurance* exposure; or

(b) a *counterparty* exposure or asset exposure to an *approved credit institution*.

3.2.21 G In assessing its exposure to a *counterparty* or group of closely related *counterparties*, a *firm* should consider exposures from different sources including *deposits*, loans, *securities* and *derivatives*.

#### Market risk and counterparty limits

3.2.22 R (1) A *firm* must calculate the amount of the deduction from total capital required by stage L in the Table in *PRU 2.2.14R* in respect of assets in excess of *market risk* and *counterparty* limits as the aggregate amount by which its *counterparty* exposures and asset exposures exceed the relevant limits set out in (3).

(2) Except where the contrary is expressly stated in *PRU*, whenever:

(a) a *rule* in *PRU* refers to assets of a *firm*, or of any part of a *firm*, or of any fund or part of a fund within a *firm*, which are assets of a kind referred to in any of the limits in (3); and

(b) the *firm's counterparty* exposure (or aggregate exposure arising from the *counterparty* exposures to each member of a group of closely related *persons*) or asset exposure in respect of those assets exceeds any of the limits in (3);

the *firm* must deduct from the measure of the value of those assets (as determined in accordance with *PRU 1.3*) the amount by which that exposure exceeds the relevant limit in (3), or that portion of the deduction that relates to the part of the *firm* or fund or part of a fund in question.

(3) The limits referred to in (1) and (2) are the following, expressed as a percentage of the *firm's* business amount:

(a) for a *counterparty* exposure to an individual, unincorporated body of individuals or the aggregate exposure arising from the *counterparty* exposures to each member of a group of closely related individuals or unincorporated bodies of individuals:

(i)  $\frac{1}{4}\%$  for that part of the exposure that arises from *unsecured debt*;

(ii) 1% for the whole exposure (after deduction of the excess arising from the limit in (a)(i));

(b) for a *counterparty* exposure to an *approved counterparty* or the aggregate exposure arising from the *counterparty* exposures to each member of a group of closely related *approved counterparties*:

(i) 5% for that part of the exposure not arising from short term *deposits* made with an *approved credit institution*; this limit is increased to 10% if the total of such exposures which exceed 5% is less than 40%;

(ii) 20% or £2 million if larger for the whole exposure (after deduction of the excess arising from the limit in (b)(i));

- (c) for a *counterparty* exposure to a *person*, or the aggregate exposure arising from the *counterparty* exposures to each member of a group of closely related *persons*, who do not fall into the categories of *counterparty* to whom (a) and (b) apply:
    - (i) 1% for that part of the exposure arising from *unsecured debt*; this limit is increased to 2.5% in the case of an exposure to a *regulated institution*;
    - (ii) 1% for that part of the exposure arising from *shares*, bonds, *debt securities* and other *money market instruments* and capital market instruments from the same *counterparty* that are not dealt in on a *regulated market*, or any beneficial interest in a *collective investment scheme* which is not a *UCITS scheme*, a *non-UCITS retail scheme* or a *recognised scheme*; the limit for that part of the exposure arising from *debt securities* (other than hybrid securities) issued by the same *regulated institution* is increased to 5%;
    - (iii) 5% for the whole exposure (after deduction of the excesses arising from the limits in (c)(i) and (ii));
  - (d) 5% for the aggregate of all *counterparty* exposures that fall within (c)(i) whether or not they arise from *persons* who are closely related, but excluding amounts that are in excess of the limit in (c)(i);
  - (e) 10% for the aggregate of all *counterparty* exposures that fall within (c)(ii) whether or not they arise from *persons* who are closely related, but excluding amounts that are in excess of the limit in (c)(ii);
  - (f) 5% for the aggregate of all *counterparty* exposures arising from unsecured loans, other than those falling within (3)(b);
  - (g) 3% for the asset exposure arising from all cash in hand;
  - (h) 10% for the asset exposure (including an exposure arising from a reversionary interest) arising from any one piece of land or building, or a number of pieces of land or buildings close enough to each other to be considered effectively as one investment.
- (4) In (3) a *firm's* business amount means the sum of:
- (a) the *firm's* total gross *technical provisions*;
  - (b) the amount of its other liabilities (except those included in the calculation of capital resources in accordance with *PRU 2.2.14R*); and
  - (c) such amount as the *firm* may select not exceeding the amount of the *firm's* total capital after deductions as calculated at stage M of the calculation in *PRU 2.2.14R* or, if higher:
    - (i) in the case of a *firm* carrying on *general insurance business*, the amount of its *general insurance capital requirement*; and



- (ii) in the case of a *firm* carrying on *long-term insurance business*, the amount of its *long-term insurance capital requirement* and the amount of its *resilience capital requirement*.
- (5) For the purpose of (4)(a), a *firm's* total gross *technical provisions* exclude *technical provisions* in respect of *index-linked liabilities* or *property-linked liabilities*, except that where the *linked long-term contract of insurance* in question includes a guarantee of investment performance or some other guaranteed benefit, the total gross *technical provisions* include the *technical provisions* in respect of that guaranteed element.
  - (6) In (3)(c)(ii) hybrid security means a *debt security*, other than an *approved security*, the terms of which provide, or have the effect that, the holder does not, or would not, have an unconditional entitlement to payment of interest and repayment of capital in full within 75 years of the date on which the *security* is being valued.

Large exposure calculation for reinsurance exposures

- 3.2.23 R A *firm* must notify the *FSA* in accordance with *SUP 15.7* as soon as it first becomes aware that:
  - (1) a *reinsurance* exposure to a *reinsurer* or group of closely related *reinsurers* is reasonably likely to exceed 100% of its *capital resources*, excluding *capital resources* held to cover *property-linked liabilities*; or
  - (2) if (1) does not apply, that it has exceeded this limit.
- 3.2.24 R Upon notification under *PRU 3.2.23R*, a *firm* must:
  - (1) demonstrate that prudent provision has been made for the *reinsurance* exposure in excess of the 100% limit, or explain why in the opinion of the *firm* no provision is required; and
  - (2) explain how the *reinsurance* exposure is being safely managed.
- 3.2.25 R (1) For the purposes of *PRU 3.2*, a *reinsurance* exposure is the amount of loss which a *firm* would suffer if a *reinsurer* or group of closely related *reinsurers* were to fail to meet its or their obligations under contracts of *reinsurance* reinsuring any of the *firm's contracts of insurance*.
  - (2) For the purposes of (1), the amount of loss is the amount, if any, by which the *firm's* capital resources (as calculated in accordance with *PRU 2.2.14R* but without making any deduction for assets in excess of *market risk* and *counterparty* limits) would decrease as a result of the *reinsurer* or group of closely related *reinsurers* failing to meet its or their obligations under the contracts of *reinsurance*.
  - (3) If a *firm* elects under *PRU 3.2.35R* to make a deduction in respect of *collateral*, the *firm* must deduct from the amount of loss determined in accordance with (2) so much of the value of that *collateral* as:
    - (a) would be realised by the *firm* were it to exercise its rights in relation to the

*collateral*; and

(b) does not exceed any of the relevant limits in *PRU 3.2.22R(3)*.

- 3.2.26 R A *firm* must, in determining its *reinsurance* exposures for the purposes of *PRU 3.2*, aggregate any *reinsurance* exposure where the identity of the *reinsurer* is not known by the *firm* with the highest *reinsurance* exposure where it does know the identity of the *reinsurer*.
- 3.2.27 G *PRU 3.2.8R* provides that, taking into account relevant risks, a *firm* must restrict to prudent levels, and adequately diversify, its exposure to *counterparties*.
- 3.2.28 E (1) In each *financial year*, a *firm* should restrict the *gross earned premiums* which it pays to a *reinsurer* or group of closely related *reinsurers* to the higher of:
- (a) 20% of the *firm's* projected *gross earned premiums* for that *financial year*; or
  - (b) £4 million.
- (2) Compliance with this provision may be relied upon as tending to establish compliance with *PRU 3.2.8R*.
- 3.2.29 R A *firm* must notify the *FSA* immediately in accordance with *SUP 15.7* if it has exceeded, or anticipates exceeding, the limit expressed in *PRU 3.2.28E*.
- 3.2.30 R Upon notification under *PRU 3.2.29R*, a *firm* must explain to the *FSA* how, despite the excess *reinsurance* concentration, the credit risk is being safely managed.
- 3.2.31 G For the purposes of *PRU 3.2.24R* and *PRU 3.2.30R*, a *firm's* explanation of how a *reinsurance* exposure is being safely managed should also describe the *reinsurance* market in which the exposure has occurred, and the nature of the *reinsurance* contract. If appropriate, the *firm* should also provide a detailed plan and timetable explaining how the excess exposure will be reduced to an acceptable level. The explanation should be approved by a person at the *firm* of appropriate seniority.
- 3.2.32 G Where a *firm* can demonstrate that the arrangement does not give rise to unacceptable levels of credit risk it is unlikely that further action will be required.

#### Exposures excluded from limits

- 3.2.33 R In *PRU 3.2.20R* and *PRU 3.2.22R*, references to a *counterparty* exposure or an asset exposure do not include such an exposure arising from:
- (1) a debt which is fully secured on assets whose value at least equals the amount of the debt;
  - (2) *premium* debts;
  - (3) advances secured on, and not exceeding the *surrender value* of, *long-term insurance contracts* of the *firm*;
  - (4) rights of salvage or subrogation;

- (5) *deferred acquisition costs*;
- (6) assets held to cover *index-linked liabilities* or *property-linked liabilities*, except that where the *linked long-term contract of insurance* in question includes a guarantee of investment performance or some other guaranteed benefit, *PRU 3.2.20R and PRU 3.2.22R* will nevertheless apply to assets held to cover that guaranteed element;
- (7) *moneys* due from, or guaranteed by, a *Zone A country*;
- (8) an *approved security*;
- (9) a holding in a *UCITS scheme*.

3.2.34 R In *PRU 3.2.22R* references to a *counterparty* exposure or an asset exposure do not include such an exposure arising from *reinsurance* debts and the *reinsurer's* share of *technical provisions*.

3.2.35 R If:

- (1) a *firm* has a *counterparty* exposure, an asset exposure or a *reinsurance* exposure in respect of which it has rights over *collateral*; and
- (2) the assets constituting that *collateral* would, if owned by the *firm*, be *admissible assets*;

the *firm* may, in determining the amount of that exposure, deduct the value of that *collateral* in accordance with *PRU 3.2.9R(5)* or, in the case of a *reinsurance* exposure, *PRU 3.2.25R(3)*.

3.2.36 R If a *firm* has a *counterparty* exposure, asset exposure or *reinsurance exposure* the whole or any part of which is:

- (1) guaranteed by a *credit institution* or an *investment firm* subject in either case to the *Capital Adequacy Directive* or supervision by a third country (non-EEA) supervisory authority with a *Capital Adequacy Directive*-equivalent regime; or
- (2) adequately mitigated by a *credit derivative*;

the *firm* may, for the purposes of *PRU 3.2.20R*, *PRU 3.2.22R* and *PRU 3.2.23R*, treat that exposure, or that part of the exposure which is so guaranteed or mitigated, as an exposure to the guarantor or *derivative counterparty*, rather than to the original *counterparty*, asset or *reinsurer*.

3.2.37 R For the purposes of *PRU 3.2.36R*, references to an exposure being guaranteed include an exposure secured by a letter of credit, but to fall within *PRU 3.2.36R* the guarantee or letter of credit must be direct, explicit, unconditional and irrevocable.

3.2.38 G The portion of exposure which is guaranteed or mitigated by a *credit derivative* is itself, as an exposure to the guarantor or *derivative counterparty*, subject to the limits in *PRU 3.2.20R* and *PRU 3.2.22R*.

- 3.2.39 R For the purposes of *PRU 3.2.20R* and *PRU 3.2.22R*, a *UCITS scheme*, a *non-UCITS retail scheme*, a *recognised scheme* or any other *collective investment scheme* that invests only in *admissible assets* (including any *derivatives* or *quasi-derivatives* held by the scheme) is to be treated as closely related to the *issuer* of the *units* in that scheme.

Meaning of closely related

- 3.2.40 R For the purposes of *PRU 3.2*, a group of *persons* is closely related if it consists solely of two or more natural or legal persons who, unless it is shown otherwise, constitute a single risk because as between any two of them one or other of the following relationships apply:
- (1) one of them, directly or indirectly, has control, as defined in *PRU 3.2.41R*, over the other or they are both controlled by the same third party; or
  - (2) there is no relationship of control as defined in *PRU 3.2.41R* but they are to be regarded as constituting a single risk because they are so interconnected that, if one of them were to experience financial problems, the other would be likely to encounter repayment difficulties.
- 3.2.41 R For the purposes of *PRU 3.2.40R*, control means the relationship between a *parent undertaking* and a *subsidiary undertaking*, as defined in Article 1 of the Consolidated Accounts Directive (83/349/EEC), or a similar relationship between any natural or legal person and an *undertaking*.

3.3 Asset-related Capital Requirement  
Application

- 3.3.1 R *PRU 3.3* applies to an *insurer* unless it is:
- (1) a *non-directive friendly society*; or
  - (2) a *Swiss general insurer*; or
  - (3) an *EEA-deposit insurer*; or
  - (4) an *incoming EEA firm*; or
  - (5) an *incoming Treaty firm*.

3.3.2 G The scope of application of *PRU 3.3* is not restricted to *firms* that are subject to the relevant EC directives. It applies, for example, to *pure reinsurers*.

3.3.3 R *PRU 3.3* applies to a *firm* only in relation to its *general insurance business*.

3.3.4 G The adequacy of a *firm's* financial resources needs to be assessed in relation to all the activities of the *firm* and the risks to which they give rise.

3.3.5 G The requirements in *PRU 3.3* apply to a *firm* on a solo basis.

Purpose

3.3.6 G *PRU 2.1.9R* requires that a *firm* must maintain at all times *capital resources* equal to or in excess of its *capital resources requirement*. *PRU 2.1.14R* provides that for a *firm* carrying on *general insurance business* the *firm's capital resources requirement* is the *Minimum Capital Requirement*.

3.3.7 G The *FSA* will use the *Enhanced Capital Requirement* as the benchmark for individual *capital guidance* for a *firm* carrying on *general insurance business*, other than a *non-directive insurer*. The *Enhanced Capital Requirement* is the sum of the *asset-related capital requirement* and the *insurance-related capital requirement* less the *firm's equalisation provisions*. This section sets out *rules and guidance* relating to the *asset-related capital requirement*. *Rules and guidance* relating to the *insurance-related capital requirement* are set out in *PRU 7.2*.

3.3.8 G The *asset-related capital requirement* is a measure of the capital that a *firm* should hold against the risk of loss if another party fails to perform its financial obligations to the *firm* or from adverse movements in the value of assets.

3.3.9 G The *asset-related capital requirement* is calculated by applying capital charge factors, expressed as a percentage, to different categories of a *firm's* assets. A *firm* should refer to *PRU 1.3* which sets out how a *firm* must recognise and value assets and liabilities.

Calculation of asset-related capital requirement

3.3.10 R A *firm* must calculate its *asset-related capital requirement* in accordance with *PRU 3.3.11R*.

- 3.3.11 R
- (1) The value of each of the *firm's* assets of a kind listed in the table in *PRU 3.3.16R* must be multiplied by the corresponding capital charge factor.
  - (2) If any amount which is to be multiplied by a capital charge factor is a negative amount, that amount shall be treated as zero.
  - (3) No account shall be taken of:
    - (a) the value of any asset which is not an *admissible asset*;
    - (b) the amount (if any) by which the value of any assets exceeds the limits on exposures to a type of asset or *counterparty* as set out in *PRU 3.2.22R*.
  - (4) Where a *firm* has entered into a *derivative*, then for the purposes of applying the appropriate capital charge factor as set out in *PRU 3.3.16R*, it must treat the value of the *derivative* and the value of the asset associated with the *derivative* as a single asset of a type and value which most closely reflects the economic risk to the *firm* of the combined rights and obligations associated with the *derivative* and the asset associated with the *derivative*.

- (5) The amounts resulting from multiplying each of the asset items referred to in (1) by the corresponding capital charge factor must be aggregated.
- (6) The *asset-related capital requirement* is the amount resulting from the aggregation in (5).
- 3.3.12 G *Options*: some *derivatives* may allow a *firm* an *option* whether to buy or sell a particular asset. If an *option* has a positive market value (that is, in-the-money) it is likely that the *firm* will exercise the *option* in the future and the current value of the *derivative* and associated asset will generally acquire new characteristics and volatility (a 'synthetic asset'). For instance, an *option* to acquire *shares* at a price below their current market value is likely to be exercised and the appropriate *asset-related capital requirement* calculation would be to combine the cash cost of acquiring the number of *shares* covered by the *option* with the value of the *derivative* and apply a factor of 16% to that combined value. If an *option* has no market value (that is, out-of-the-money) then it is unlikely that a *firm* would exercise the *option* in which case the appropriate *asset-related capital requirement* charge would be zero in respect of the *derivative*, and the corresponding capital charge contained in Table PRU 3.3.16R in relation to the asset associated with the *derivative*.
- 3.3.13 G *Futures and swaps*: *futures* or *swaps* may not allow the *firm* such an option in which case the appropriate asset-related capital charge factor to apply is the one corresponding to the asset that would be held on fulfilment of the contract and the value to which this should be applied would be the value of the asset held after the contract is fulfilled.
- 3.3.14 R (1) The asset-related capital charge factor for money market funds set out in the Table PRU 3.3.16R must be applied to exposures to funds that meet the definition in (2).
- (2) In PRU 3.3 an investment in a money market fund means a participation in a *collective investment scheme* which satisfies the following conditions:
- (a) the primary investment objective of the *collective investment scheme* is:
- (i) to maintain the net asset value of the *collective investment scheme* constant at par (net of earnings); or
- (ii) to maintain the net asset value of the *collective investment scheme* at the value of investors' initial capital plus earnings;
- (b) in order to pursue its primary investment objective the *collective investment scheme* invests exclusively in cash or in short term instruments with characteristics similar to cash or both; and
- (c) the *collective investment scheme* undertakes to abide by the following conditions:
- (i) not to allow the assets held in the *collective investment scheme* to exceed a weighted average maturity of 60 days;
- (ii) not to invest in equity or *securities* with characteristics similar to equity; and
- (iii) on a basis of marking-to-market at least weekly, not to permit the value of each *collective investment scheme* unit at any point in time to move by more than 50 basis points (0.5% of total *collective investment scheme* value).
- 3.3.15 R In PRU 3.3.16R an insurance dependant means a *regulated related undertaking* which is an *insurance undertaking* or an *insurance holding company*.

3.3.16R Table: Asset-related capital charge factors

Asset item			ECR asset-related capital charge factor	
Investments	Land and Buildings		7.5%	
	<i>Investments in group undertakings and participating interests</i>	<i>Shares in group undertakings</i> excluding participating interests	Insurance dependants	0%
			Other	7.5%
		<i>Debt securities</i> issued by, and loans to, <i>group undertakings</i>		3.5%
		Participating interests		7.5%
		<i>Debt securities</i> issued by, and loans to, <i>undertakings</i> in which the <i>insurer</i> has a participating interest		3.5%
		Other financial investments	<i>Shares</i> and other variable-yield <i>securities</i> and units in unit trusts	
	Money market funds		0%	
	<i>Debt securities</i> and other fixed income securities		<i>Approved securities</i>	3.5%
			Other	3.5%
	Participation in investment pools		16.0%	
	Loans secured by mortgages		2.5%	
	Other loans		2.5%	
	<i>Deposits with approved credit institutions and approved financial institutions</i>		0%	
	Other		7.5%	
		Deposits with ceding <i>undertakings</i>		3.5%
	<i>Reinsurers' share of technical provisions</i>	Provision for <i>unearned premium</i>		2.5%
		<i>Claims</i> outstanding		2.5%
		Other		2.5%
Debtors	Debtors arising out of direct insurance operations	<i>Policyholders</i>	4.5%	
		Intermediaries	3.5%	
	Debtors arising out of <i>reinsurance</i> operations		2.5%	
	Other debtors		1.5%	
	Called up <i>share</i> capital not paid		0%	
Other Assets	Tangible assets		7.5%	
	Cash at bank and in hand		0%	
	Other		0%	

Prepayments and accrued income	Accrued interest and rent	0%
	<i>Deferred acquisition costs</i>	0%
	Other prepayments and accrued income	0%



## Annex F

### PRU 4

In this Annex, all the text is new and is not underlined.

#### 4.1 Market risk management systems and controls

##### Application

4.1.1 G PRU 4.1 applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

4.1.2 G PRU 4.1 applies to:

- (1) an *EEA-deposit insurer*; and
- (2) a *Swiss general insurer*;

only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

4.1.3 G *Firms* should also see PRU 1.2 (PRU 1.2.40G to PRU 1.2.55G) and PRU 4.2.

##### Purpose

- 4.1.4 G
- (1) The purpose of this section is to amplify PRU 1.4 insofar as it relates to *market risk*.
  - (2) *Market risk* includes equity, interest rate, FX, commodity risk and interest rate risk on *long-term insurance contracts*. The price of *financial instruments* may also be influenced by other risks such as *spread risk, basis risk, correlation, specific risk* and *volatility risk*.
  - (3) This section does not deal with the risk management of *market risk* in a *group* context. A *firm* that is a member of a *group* should also read PRU 8.1 (Group risk systems and controls) which outlines the *FSA's* requirements for the risk management of *market risk* within a *group*.
  - (4) Appropriate systems and controls for the management of *market risk* will vary with the scale, nature and complexity of the *firm's* activities. Therefore the material in this section is *guidance*. A *firm* should assess the appropriateness of any particular item of *guidance* in the light of the scale, nature and complexity of its activities as well as its obligations as set out in *Principle 3* to organise and control its affairs responsibly and effectively.

##### Requirements

- 4.1.5 G High level requirements for prudential systems and controls, including those for *market risk*, are set out in PRU 1.4. In particular:
- (1) PRU 1.4.19R(2) requires a *firm* to document its policy for *market risk*, including its risk appetite and how it identifies, measures, monitors and controls that risk;

- (2) *PRU 1.4.19R(4)* requires a *firm* to document its asset and liability recognition policy. Documentation should describe the systems and controls that it intends to use to comply with the policy;
- (3) *PRU 1.4.19R* requires a *firm* to establish and maintain risk management systems to identify, measure, monitor and control *market risk* (in accordance with its *market risk* policy), and to take reasonable steps to establish systems adequate for that purpose;
- (4) In line with *PRU 1.4.11G*, the ultimate responsibility for the management of *market risk* should rest with a *firm's governing body*. Where delegation of authority occurs the *governing body* and relevant *senior managers* should approve and adequately review systems and controls to check that delegated duties are being performed correctly.

#### Market risk policy

- 4.1.6 G *PRU 1.4* requires a *firm* to establish, maintain and document a business plan and risk policies. They should provide a clear indication of the amount and nature of *market risk* that the *firm* wishes to incur. In particular, they should cover for *market risk*:
- (1) how, with particular reference to its activities, the *firm* defines and measures *market risk*;
  - (2) the *firm's* business aims in incurring *market risk* including:
    - (a) identifying the types and sources of *market risk* to which the *firm* wishes to be exposed (and the limits on that exposure) and those to which the *firm* wishes not to be exposed (and how that is to be achieved, for example how exposure is to be avoided or mitigated); and
    - (b) specifying the level of diversification required by the *firm* and the *firm's* tolerance for risk concentrations (and the limits on those exposures and concentrations).
- 4.1.7 G The *market risk* policy of a *firm* should be endorsed by the *firm's governing body* and implemented by its senior management, who should take adequate steps to disseminate the policy and train the relevant staff such that they can effectively implement the policy.
- 4.1.8 G The *market risk* policy of a *firm* should enforce the risk management and control principles and include detailed information on:
- (1) the *financial instruments*, commodities, assets and liabilities (and mismatches between assets and liabilities) that a *firm* is exposed to and the limits on those exposures;
  - (2) the *firm's* investment strategy as applicable between each insurance fund;
  - (3) activities that are intended to hedge or mitigate *market risk* including mismatches caused by for example differences in the assets and liabilities and maturity mismatches; and

- (4) the methods and assumptions used for measuring linear, non-linear and geared *market risk* including the rationale for selection, ongoing validation and testing. Methods might include stress testing and scenario analysis, option Greeks, asset/liability analysis, correlation analysis and Value-at-Risk (VaR). Exposure to non-linear or geared *market risk* is typically through the use of *derivatives*.

#### Risk identification

- 4.1.9 G A *firm* should have in place appropriate risk reporting systems that enable it to identify the types and amount of *market risk* to which it is, and potentially could be, exposed. The information that systems should capture may include but is not limited to:
- (1) position information which may include a description of individual *financial instruments* and their cash flows; and
  - (2) market data which may consist of raw time series of market rates, index levels and prices and derived time series of benchmark yield curves, spreads, implied volatilities, historical volatilities and correlations.

#### Risk measurement

- 4.1.10 G Having identified the *market risk* that the *firm* is exposed to on at least a daily basis, a *firm* should be able to measure and manage that *market risk* on a consistent basis. This may be achieved by:
- (1) regularly stress testing all or parts of the *firm's* portfolio to estimate potential economic losses in a range of market conditions including abnormal markets. Corporate level stress test results should be discussed regularly by risk monitors, senior management and risk takers, and should guide the *firm's market risk* appetite (for example, stress tests may lead to discussions on how best to unwind or hedge a position), and influence the internal capital allocation process;
  - (2) measuring the *firm's* exposure to particular categories of *market risk* (for example, equity, interest rate, foreign exchange and commodities) as well as across its entire portfolio of *market risks*;
  - (3) analysing the impact that new transactions or businesses may have on its *market risk* position on an on-going basis; and
  - (4) regularly backtesting realised results against internal model generated *market risk* measures in order to evaluate and assess its accuracy. For example, a *firm* should keep a database of daily risk measures such as VaR and option Greeks, and use these to back test predicted profit and loss against actual profit and loss for all trading desks and business units, and monitor the number of exceptions from agreed confidence bands.

#### Valuation

- 4.1.11 G A *firm* should take reasonable steps to establish systems and control procedures such that the *firm* complies with the requirements of *PRU 1.3* (Valuation).

- 4.1.12 G The systems and controls referred to in *PRU* 4.1.11G should include the following:
- (1) the department responsible for the validation of the value of assets and liabilities should be independent of the business trading area, and should be adequately resourced by suitably qualified staff. The department should report to a suitably qualified individual, independent from the business trading area, who has sufficient authority to enforce the systems and controls policies and any alterations to valuation treatments where necessary;
  - (2) all valuations should be checked and validated at appropriate intervals. Where a *firm* has chosen not to validate all valuations on a daily basis this should be agreed by senior management;
  - (3) a *firm* should establish a review procedure to check that the valuation procedures are followed and are producing valuations in compliance with the requirements in this section. The review should be undertaken by suitably qualified staff independent of the business trading area, on a regular and ad hoc basis. In particular, this review procedure should include:
    - (a) the quality and appropriateness of the price sources used;
    - (b) valuation reserves held; and
    - (c) the valuation methodology employed for each product and consistent adherence to that methodology;
  - (4) where a valuation is disputed and the dispute cannot be resolved in a timely manner it should be reported to senior management. It should continue to be reported to senior management until agreement is reached;
  - (5) where a *firm* is marking positions to market it should take reasonable steps to establish a price source that is reliable and appropriate to enable compliance with the provisions in this section on an ongoing basis;
  - (6) a *firm* should document its policies and procedures relating to the entire valuation process. In particular, the following should be documented:
    - (a) the valuation methodologies employed for all product categories;
    - (b) details of the price sources used for each product;
    - (c) the procedures to be followed where a valuation is disputed;
    - (d) the valuation adjustment and reserving policies;
    - (e) the level at which a difference between a valuation assigned to an asset or liability and the valuation used for validation purposes will be reported on an exceptions basis and investigated;
    - (f) where a *firm* is using its own internal estimate to produce a valuation, it should document in detail the process followed in order to produce the valuation; and

- (g) the review procedures established by a *firm* in relation to the requirements of this section should be adequately documented and include the rationale for the policy;
- (7) a *firm* should maintain records which demonstrate:
  - (a) senior management's approval of the policies and procedures established; and
  - (b) management sign-off of the reviews undertaken in accordance with *PRU* 4.1.11G.

#### Risk monitoring

- 4.1.13 G Risk monitoring is the operational process by which a *firm* monitors compliance with defined policies and procedures of the *market risk* policy. The *firm*'s risk monitoring system should be independent of the *employees* who are responsible for exposing the *firm* to *market risk*.
- 4.1.14 G The *market risk* policy of a *firm* may require the production of *market risk* reports at various levels within the *firm*. These reports should provide sufficiently accurate *market risk* data to relevant functions within the *firm*, and should be timely enough to allow any appropriate remedial action to be proposed and taken, for example:
  - (1) at *firm* wide level, a *market risk* report may include information:
    - (a) summarising and commenting on the total *market risk* that a *firm* is exposed to and *market risk* concentrations by business unit, asset class and country;
    - (b) on VaR reports against risk limits by business unit, asset class and country;
    - (c) commenting on significant risk concentrations and market developments; and
    - (d) on *market risk* in particular legal entities and geographical regions;
  - (2) at the business unit level, a *market risk* report may include information summarising *market risk* by currency, trading desk, maturity or duration band, or by instrument type;
  - (3) at the trading desk level, a *market risk* report may include detailed information summarising *market risk* by individual trader, instrument, position, currency, or maturity or duration band; and
  - (4) all risk data should be readily reconcilable back to the prime books of entry with a fully documented audit trail.
- 4.1.15 G Risk monitoring may also include information on:
  - (1) the procedures for taking appropriate action in response to the information within the *market risk* reports;
  - (2) ensuring that there are controls and procedures for identifying and reporting trades and positions booked at off-market rates;
  - (3) the process for new product approvals;

- (4) the process for dealing with situations (authorised and unauthorised) where particular *market risk* exposures exceed predetermined risk limits and criteria; and
  - (5) the periodic review of the risk monitoring process in order to check its suitability for both current market conditions and the *firm's* overall risk appetite.
- 4.1.16 G Risk monitoring should be subject to periodic independent review by suitably qualified staff.

#### Risk control

- 4.1.17 G Risk control is the independent monitoring, assessment and supervision of business units within the defined policies and procedures of the *market risk* policy. This may be achieved by:
- (1) setting an appropriate *market risk* limit structure to control the *firm's* exposure to *market risk*; for example, by setting out a detailed *market risk* limit structure at the corporate level, the business unit level and the trading desk level which addresses all the key *market risk* factors and is commensurate with the volume and complexity of activity that the *firm* undertakes;
  - (2) setting limits on risks such as price or rate risk, as well as those factors arising from *options* such as delta, gamma, vega, rho and theta;
  - (3) setting limits on net and gross positions, *market risk* concentrations, the maximum allowable loss (also called “stop-loss”), VaR, potential risks arising from stress testing and scenario analysis, gap analysis, correlation, liquidity and volatility; and
  - (4) considering whether it is appropriate to set intermediate (early warning) thresholds that alert management when limits are being approached, triggering review and action where appropriate.

#### Record keeping

- 4.1.18 G High level requirements for record keeping are set out in *PRU* 1.4.
- 4.1.19 G In relation to *market risk*, a *firm* should retain appropriate prudential records of:
- (1) off and on market trades in *financial instruments*;
  - (2) the nature and amounts of off and on balance sheet exposures, including aggregations of exposures;
  - (3) trades in *financial instruments* and other assets and liabilities; and
  - (4) methods and assumptions used in stress testing and scenario analysis and in VaR models.
- 4.1.20 G A *firm* should keep a data history to enable it to perform back testing of methods and assumptions used for stress testing and scenario analysis and for VaR models.

## 4.2 Market risk in insurance

### Application

- 4.2.1 R *PRU 4.2 applies to an insurer, unless it is:*
- (1) *a non-directive friendly society; or*
  - (2) *an incoming EEA firm; or*
  - (3) *an incoming Treaty firm.*
- 4.2.2 G The scope of application of *PRU 4.2* is not restricted to *firms* that are subject to the relevant EC directives. It applies, for example, to *pure reinsurers* (with the exception of *PRU 4.2.53R*).
- 4.2.3 R (1) *PRU 4.2 applies to a firm in relation to the whole of its business, except where a particular provision provides for a narrower scope.*
- (2) *Where a firm carries on both long-term insurance business and general insurance business, PRU 4.2 applies separately to each type of business.*

### Purpose

- 4.2.4 G This section sets out *rules and guidance* relating to *market risk*. Under *PRU 7.2.20R*, a *firm* is required to hold *admissible assets* of a value sufficient to cover *technical provisions*. In addition, *PRU 7.2.34R* sets the requirement that a *firm* must hold assets of appropriate amount, currency, term, safety and yield, to ensure that the cash inflows from those assets will be sufficient to meet expected cash outflows from its insurance liabilities as they are due.
- 4.2.5 G *Market risk* is the risk that as a result of market movements a *firm* may be exposed to fluctuations in the value of its assets, the amount of its liabilities, or the income from its assets. Sources of general *market risk* include movements in interest rates, equities, exchange rates and real estate prices. It is important to note that none of these sources of risk is independent of the others. For example, fluctuations in interest rates often have an impact upon equity and currency values and vice versa. Giving due consideration to these correlations is an important aspect of the prudent management of *market risk*.
- 4.2.6 G A *firm* may also be exposed to specific *market risk*, which is the risk that the *market value* of a specific asset, or income from that asset, may fluctuate for reasons that are not dependent on general market movements. The limits in *PRU 3.2.22R* cover *market risk* as well as *counterparty risk*.
- 4.2.7 G *PRU 4.2* addresses the impact of *market risk* on *insurance business* in the ways set out below:

- (1) Any *firm* that carries on *long-term insurance business* must comply with the *resilience capital requirement*. This requires the *firm* to hold capital to cover *market risk*. The *resilience capital requirement* is dealt with in *PRU 4.2.9G* to *PRU 4.2.26R*.
- (2) For a *firm* that carries on *long-term insurance business*, the assets that it must hold must be of a value sufficient to cover the *firm's mathematical reserve* requirements. *PRU 7.3* contains *rules* and *guidance* as to the methods and assumptions to be used in calculating these *mathematical reserves*. One of these assumptions is the assumed rate of interest to be used in calculating the present value of future payments by or to a *firm*. *PRU 4.2.28R* to *PRU 4.2.48G* set out the methodology to be used in relation to *long-term insurance liabilities*.
- (3) *Firms* carrying on either *long-term insurance business* or *general insurance business* are also subject to currency risk. That is, the risk that fluctuations in exchange rates may impact adversely on a *firm*. *PRU 4.2.49G* to *PRU 4.2.56G* set out the requirements a *firm* must meet so as to cover this risk.
- (4) For a *firm* carrying on *general insurance business*, the *Enhanced Capital Requirement* already captures some elements of *market risk*. In addition, the requirements as to the assumed rate of interest used in calculating the present value of *general insurance liabilities* are contained in the *insurance accounts rules*, and these requirements are outlined in *PRU 4.2.27G*.
- (5) *Firms* carrying on *long-term insurance business* that have *property-linked liabilities* or *index-linked liabilities* must cover these liabilities by holding appropriate assets. *PRU 4.2.57R* and *PRU 4.2.58R* set out these cover requirements.

## Definitions

- 4.2.8 R For the purposes of *PRU 4.2*:
- (1) real estate means an interest in land, buildings or other immovable property;
  - (2) a significant territory is any country or territory in which more than 2.5% of a *firm's long-term insurance assets* (by *market value*), excluding assets held to cover *index-linked liabilities* or *property-linked liabilities* (see *PRU 4.2.57R* and *PRU 4.2.58R*), are invested; and
  - (3) the long term gilt yield means the annualised equivalent of the fifteen year gilt yield for the *United Kingdom* Government fixed-interest *securities* index jointly compiled by the Financial Times, the Institute of Actuaries and the Faculty of Actuaries.

Resilience capital requirement (applicable to long-term insurance business only)



- 4.2.9 G The *resilience capital requirement* forms part of the calculation of the *capital resources requirement* for all firms carrying on *long-term insurance business*. *PRU 2.1.15R* to *PRU 2.1.20R* set out the different elements of this calculation. These include the *Minimum Capital Requirement* and the *Enhanced Capital Requirement*. The *resilience capital requirement* forms part of both of these requirements (see *PRU 2.1.22R(2)* and *PRU 2.1.34R(2)*).
- 4.2.10 R (1) A firm that carries on *long-term insurance business* must calculate a *resilience capital requirement* in accordance with (2) to (5).
- (2) From amongst its *long-term insurance assets*, the firm must identify assets which after applying the scenarios in (3) have a value that is equal to the firm's *long-term insurance liabilities* under those scenarios.
- (3) For the purpose of (2), the scenarios are:
- (a) for those assets invested in the *United Kingdom*, the *market risk* scenario set out in *PRU 4.2.16R*;
- (b) subject to (c) and to *PRU 4.2.26R*, for those assets invested outside of the *United Kingdom*, the *market risk* scenario set out in *PRU 4.2.23R*; and
- (c) where the assets in (b) are:
- (i) held to cover *index-linked liabilities* or *property-linked liabilities*; or
- (ii) not invested in a significant territory outside the *United Kingdom*;  
the *market risk* scenario set out in *PRU 4.2.16R*.
- (4) The *resilience capital requirement* is the result of deducting B from A, where:
- (a) A is the value of the assets which will produce the result described in (2); and
- (b) B is the firm's *long-term insurance liabilities*.
- (5) In calculating the value of the firm's *long-term insurance liabilities* under any scenario, a firm is not required to adjust the provision made under *PRU 1.3.5R* in respect of a *defined benefits pension scheme*.
- 4.2.11 G The purpose of the *resilience capital requirement* is to cover adverse deviation from:
- (1) the value of *long-term insurance liabilities*;
- (2) the value of assets held to cover *long-term insurance liabilities*; and
- (3) the value of assets held to cover the *resilience capital requirement*;

arising from the effects of *market risk* for equities, real estate and fixed interest *securities*. Other risks are not explicitly addressed by the *resilience capital requirement*.

- 4.2.12 G The amount of the *resilience capital requirement* calculated by the *firm* will depend on the *firm's* choice of assets held to cover the *resilience capital requirement*. The *resilience capital requirement* is held to cover not only the shortfall between the change in the value of *long-term insurance liabilities* and the change in the value of the assets identified to cover those liabilities, but also the change in the value of the assets identified to cover the *resilience capital requirement* itself.
- 4.2.13 G As part of the assessment of the financial resources a *firm* needs to hold to comply with *PRU 1.2.22R*, *PRU 1.2.35R* requires a *firm* to carry out stress tests and scenario analyses appropriate to the major sources of risk to its ability to meet its liabilities as they fall due identified in accordance with *PRU 1.2.31R*. In considering the stress tests and scenario analyses relevant to the major sources of risk in the category of *market risk*, a *firm* should consider the extent to which the *market risk* scenarios set out in *PRU 4.2.16R* to *PRU 4.2.26R* are appropriate to the nature of its asset portfolio. A *firm* may judge that given the nature of its portfolio, a more severe stress should be adopted. The *firm* may also wish to bring in other asset classes, such as index-linked bonds, which should be stressed on appropriate bases, and to consider the impact of currency mismatching and any *derivative* positions held.
- 4.2.14 G The *resilience capital requirement* requires *firms* to assume different adverse *market risk* scenarios for equities, real estate and fixed interest *securities* (see *PRU 4.2.16R* and *PRU 4.2.23R*) to those required by *PRU 7.4.68R* (UK and certain other assets) and *PRU 7.4.73R* (non-UK assets) in relation to the calculation of the *risk capital margin* for a *with-profits fund* by a *realistic basis life firm* calculating its *with-profits insurance capital component*.
- 4.2.15 G Where the *resilience capital requirement* is affected by the presence of *derivative* or *quasi-derivative* instruments, the *firm* will need to consider whether the protection afforded is of suitable length or security. The *firm* should include the exposure to *counterparties* in the credit considerations of *PRU 4.2.41R* both before and after calculating the *resilience capital requirement*. If the *derivative* protection is very short term the *firm* should consider whether issues arise under *PRU 7.3.26R* (Avoidance of future valuation strain); when a *derivative* expires the financial position of the *firm* may deteriorate as a result of, for example, falls in asset values. Unless the *firm* holds a further reserve, the *firm* is likely to need to have either undertaken a fresh protection strategy or carried through the alternative to the *derivative* protection (such as selling equities in place of a put *option*) if the existing protection expires before the financial year end. If the existing *derivative* protection continues beyond the time of financial year end the *firm* must have sufficient confidence that it can renew its *derivative* protection or an alternative to achieve the same effect.

Market risk scenario for assets invested in the United Kingdom

- 4.2.16 R In *PRU 4.2.10R(3)(a)*, the *market risk* scenario for assets invested in the *United Kingdom* and for assets (including assets invested outside the *United Kingdom*) held to cover *index-linked liabilities* or *property-linked liabilities* which a *firm* must assume is:
- (1) a fall in the *market value* of equities of at least 10% or, if greater, the lower of:
    - (a) a percentage fall in the *market value* of equities which would produce an earnings yield on the FTSE Actuaries All Share Index equal to  $\frac{4}{3}$  of the long-term gilt yield; and
    - (b) a fall in the *market value* of equities of 25% less the *equity market adjustment ratio* (see *PRU 4.2.19R*);
  - (2) a fall in real estate values of 20% less the *real estate market adjustment ratio* for an appropriate real estate index (see *PRU 4.2.21R*);
  - (3) (a) the more onerous of either a fall or rise in yields on all fixed interest *securities* by the percentage point amount determined in (b);
    - (b) for the purpose of (a), the percentage point amount is equal to 20% of the long-term gilt yield.
- 4.2.17 R For the purposes of *PRU 4.2.16R(1)* and (2), a *firm* must:
- (1) assume that earnings for equities and rack rents for real estate fall by 10%, but dividends for equities remain unaltered (see *PRU 4.2.36R* to *PRU 4.2.38R*); and
  - (2) model a fall in equity and real estate markets as if the fall occurred instantaneously.
- 4.2.18 G An example of *PRU 4.2.16R(3)* is that, where the long-term gilt yield is currently 6%, a *firm* would assume an increase of 20% in that yield, that is, a change of 1.2 percentage points. For the purpose of the scenario in *PRU 4.2.16R(3)(a)*, the *firm* would assume a fall or rise of 1.2 percentage points in yields on all fixed interest *securities*.

#### Equity market adjustment ratio

- 4.2.19 R The equity market adjustment ratio referred to in *PRU 4.2.16R(1)(b)* is:
- (1) if the ratio calculated in (a) and (b) lies between 75% and 100%, the result of 100% less the ratio (expressed as a percentage) of:
    - (a) the current value of the FTSE Actuaries All Share Index; to
    - (b) the average value of the FTSE Actuaries All Share Index over the preceding 90 calendar days;

- (2) 0%, if the ratio calculated in (1)(a) and (b) is more than 100%; and
- (3) 25%, if the ratio calculated in (1)(a) and (b) is less than 75%.

4.2.20 R In *PRU 4.2.19R*, the average value of the FTSE Actuaries All Share Index over any period of 90 calendar days means the arithmetic mean based on levels at the close of business on each of the days in that period on which the London Stock Exchange was open for trading.

#### Real estate market adjustment ratio

4.2.21 R The real estate market adjustment ratio for a real estate index referred to in *PRU 4.2.16R(2)* and *PRU 4.2.23R(2)* is:

- (1) if the ratio calculated in (a) and (b) lies between 90% and 100%, the result of 100% less the ratio (expressed as a percentage) of:

- (a) the current value of the real estate index; to
- (b) the average value of that real estate index over the three preceding *financial years*;

- (2) 0%, if the ratio calculated in (1)(a) and (b) is more than 100%; and
- (3) 10%, if the ratio calculated in (1)(a) and (b) is less than 90%.

4.2.22 G For the purpose of calculating the *real estate market adjustment ratio* in *PRU 4.2.21R*, a *firm* should select an appropriate index of real estate values such that:

- (1) the constituents of the index are reasonably representative of the nature and territory of the real estate included in the range of assets identified in accordance with *PRU 4.2.10R*; and
- (2) the frequency of, and historical data relating to, published values of the index are sufficient to enable an average value(s) of the index to be calculated over the three preceding *financial years*.

#### Market risk scenario for assets invested outside the United Kingdom

4.2.23 R In *PRU 4.2.10R(3)(b)*, subject to *PRU 4.2.26R*, the *market risk* scenario for assets invested outside the *United Kingdom* (other than assets held to cover *index-linked liabilities* or *property-linked liabilities*) which a *firm* must assume is, for each significant territory in which assets are invested outside the *United Kingdom*:

- (1) an appropriate fall in the *market value* of equities invested in that territory, which is at least equal to the percentage fall determined in *PRU 4.2.16R*;

- (2) a fall in real estate values in that territory of 20% less the *real estate market adjustment ratio* for an appropriate real estate index for that territory (see *PRU 4.2.21R*); and
  - (3) (a) the more onerous of either a fall or a rise in yields on all fixed interest *securities* by the percentage point amount determined in (b);
    - (b) for the purpose of (a), the percentage point amount is equal to 20% of the nearest equivalent (in respect of the method of calculation) to the long term gilt yield.
- 4.2.24 R For the purposes of *PRU 4.2.23R(1)*, an appropriate fall in the *market value* of equities invested in a significant territory must be determined having regard to:
- (1) an appropriate equity market index for that territory; and
  - (2) the historical volatility of the equity market index selected in (1).
- 4.2.25 G For the purpose of *PRU 4.2.24R(1)*, an appropriate equity market index for a territory is such that:
- (1) the constituents of the index are reasonably representative of the nature of the equities held in that territory which are included in the range of assets identified in accordance with *PRU 4.2.10R*; and
  - (2) the frequency of, and historical data relating to, published values of the index are sufficient to enable an average value(s) and historical volatility of the index to be calculated over at least the three preceding *financial years*.
- 4.2.26 R Where the assets of a *firm* invested in a significant territory of a kind referred to in *PRU 4.2.23R(1)*, (2) or (3)(a) represent less than 0.5% of the *firm's long-term insurance assets* (excluding assets held to cover *index-linked liabilities* or *property-linked liabilities*), measured by *market value*, the *firm* may assume for those assets the *market risk* scenario for assets of that kind invested in the *United Kingdom* set out in *PRU 4.2.16R* instead of the *market risk* scenario set out in *PRU 4.2.23R*.

#### Interest rate risk

#### Interest rates: general insurance liabilities

- 4.2.27 G The rates of interest to be used for the calculation of the present values of *general insurance liabilities* are specified in the *insurance accounts rules*. These state that the rate of interest to be used must not exceed the lowest of:
- (1) a rate prudently estimated by the *firm* to be earned by assets of the *firm* that are appropriate in magnitude and nature to cover the provisions for *claims* being discounted, during the period necessary for the payment of such *claims*;

- (2) a rate justified by the performance of such assets over the preceding five years; and
- (3) a rate justified by the performance of such assets during the year preceding the balance sheet date.

Interest rates: long-term insurance liabilities

- 4.2.28 R The rates of interest to be used for the calculation of the present value of a *long-term insurance liability* must not exceed 97.5% of the risk-adjusted yield (see *PRU 4.2.30R to PRU 4.2.48G*) that is expected to be achieved on:
- (1) the assets allocated to cover that liability;
  - (2) the reinvestment of sums expected to be received from those assets (see *PRU 4.2.45R to PRU 4.2.48G*); and
  - (3) the investment of future *premium* receipts (see *PRU 4.2.45R to PRU 4.2.48G*).
- 4.2.29 R For the purposes of *PRU 4.2.28R*, the rates of interest assumed must allow appropriately for the rates of tax that apply to the investment return on policyholder assets. The rates of tax assumed must be such that the *firm's* total implied liability for tax arising from the allocation of assets to liabilities is not less than the *firm's* actual expected liability for tax for the period in respect of which tax is to be assessed.

Risk-adjusted yield

- 4.2.30 R A risk-adjusted yield on an asset must be calculated by:
- (1) taking the asset together with any covering *derivatives*, forward transactions and *quasi-derivatives*;
  - (2) assuming that the factors which affect the yield will remain unchanged after the valuation date (see *PRU 4.2.33R*);
  - (3) valuing the asset (together with any offsetting transaction) in accordance with *PRU 1.3* (Valuation);
  - (4) making reasonable assumptions as to whether, and if so when, any options or other rights embedded in the asset (or in any offsetting transaction) will be exercised.
- 4.2.31 G Examples of calculating a combined yield for the purposes of *PRU 4.2.30R(1)*:
- (1) 1000 £1 *shares* (fully paid) of ABC plc covered by a sold *future* on the *shares*. Calculating the combined yield effectively results in a position that behaves like cash (with dividend income but no capital gain or loss on the value of the assets); and

- (2) where a covering *derivative* contains an *option* exercisable by the *firm* (e.g. a bought put *option* or receiver swaption), the calculation of the risk adjusted yield should take into account the fact that on the valuation assumptions any time value will reduce over time (known as the 'wasting' nature of the time value of the *option*), for example, an at-the money *option* will expire worthless and hence the covering *derivative* will effectively be a negative yielding asset. There are various ways of allowing for this, for example a *firm* could treat the covering *derivative* and the asset as a single asset and calculate an internal rate of return on this combined asset. Alternatively, an explicit reserve could be set up equal and opposite to the time value of the covering *derivative* which would be written off in the same way as the time value on the covering *derivative*.
- 4.2.32 G The requirements in relation to offsetting transactions are set out in *PRU 4.3*. The options and other rights referred to in *PRU 4.2.30R(4)* include those exercisable by the *firm* as well as those exercisable by other parties.
- 4.2.33 R For the purpose of *PRU 4.2.30R(2)*, the factors that affect yield should be ascertained as at the valuation date (that is, the date to which present values of cash flows are being calculated). All changes known to have occurred by that date must be taken into account including:
- (1) changes in the rental income from real estate;
  - (2) changes in dividends or audited profit on equities;
  - (3) known or forecast changes in dividends which have been publicly announced by the issuer by the valuation date;
  - (4) known or forecast changes in earnings which have been publicly announced by the issuer by the valuation date;
  - (5) alterations in capital structure; and
  - (6) the value (at the most recent date at or before the valuation date for which it is known) of any determinant of the amount of any future interest or capital payment.
- 4.2.34 R The risk-adjusted yield is either:
- (1) (for equities and real estate) a running yield (see *PRU 4.2.36R* to *PRU 4.2.38R*, *PRU 4.2.41R* and *PRU 4.2.44R*); or
  - (2) (for all other assets) the internal rate of return (see *PRU 4.2.39R*, *PRU 4.2.41R* and *PRU 4.2.44R*).
- 4.2.35 R The risk-adjusted yield on a basket of assets is the arithmetic mean of the risk-adjusted yield on each asset weighted by that asset's *market value*.

The running yield for real estate

- 4.2.36 R For real estate the running yield is the ratio of:
- (1) the rental income arising from the real estate over the previous 12 months; to
  - (2) the *market value* of the real estate.

The running yield for equities

- 4.2.37 R For equities the running yield is:
- (1) the dividend yield, if the dividend yield is more than the earnings yield;
  - (2) otherwise, the sum of the dividend yield and the earnings yield, divided by two.

- 4.2.38 R For the purposes of *PRU 4.2.37R*:
- (1) the dividend yield is the ratio (expressed as a percentage) of dividend income over the previous 12 months from the equities for which the running yield is being calculated (“the relevant equities”) to the *market value* of those equities;
  - (2) the earnings yield is the ratio (expressed as a percentage) of the audited profit (including exceptional items and extraordinary items) for the preceding *financial year* of the issuer of the relevant equities to the *market value* of those equities;
  - (3) the earnings yield must be calculated in accordance with whichever is most appropriate (to the issuer of the relevant equities) of *United Kingdom*, US or international generally accepted accounting practice.

The internal rate of return

- 4.2.39 R The internal rate of return on an asset is the annual rate of interest which, if used to calculate the present value of future income (before deduction of tax) and of repayments of capital (before deduction of tax) would result in the sum of those amounts being equal to the *market value* of the asset.
- 4.2.40 G The risk adjusted yield for a *collective investment scheme* may be determined as the weighted average of the yields on each of the investments held by the *collective investment scheme*.

Credit risk

- 4.2.41 R In both the running yield and internal rate of return the yield must be reduced to exclude that part of the yield that represents compensation for credit risk arising from the asset.
- 4.2.42 G An allowance for credit risk should be made for all *securities* except risk-free *securities*.



- 4.2.43 G Provision for credit risk for credit-rated *securities* may be made by reference to historic default rates of *securities* with a similar credit rating. However, allowance should be made both for any recent or expected changes in market conditions that may invalidate historic default rates and for the likelihood that the credit ratings on *securities* may deteriorate or (following such deterioration) that the issuer may default.
- 4.2.44 R Provision for credit risk for *securities* that are not credit-rated must be made on principles at least as prudent as those adopted for credit-rated *securities*.

#### Investment and reinvestment

- 4.2.45 R Except as provided in *PRU 4.2.46R*:
- (1) the risk-adjusted yield assumed for the investment or reinvestment of sterling sums (other than sums expected to be received within the next three years) must not exceed the lowest of:
    - (a) the long-term gilt yield;
    - (b) 3% per annum, increased by two thirds of the excess, if any, of the long-term gilt yield over 3% per annum; and
    - (c) 6.5% per annum; and
  - (2) the risk-adjusted yield assumed for the investment or reinvestment of those sterling sums expected to be received within the next three years must not exceed the risk-adjusted yield on the assets actually held adjusted linearly over the three-year period to the risk-adjusted yield determined under (1).
- 4.2.46 R For the *with-profits insurance contracts* of a *realistic basis life firm*, the risk-adjusted yield assumed for the investment or reinvestment of sums denominated in sterling must be no more than rates derived from the forward gilts yield.
- 4.2.47 R The risk-adjusted yield assumed for the investment or reinvestment of non-sterling sums must be at least as prudent as in *PRU 4.2.45R* and *PRU 4.2.46R*.
- 4.2.48 G The purpose of *PRU 4.2.45R* to *PRU 4.2.47R* is to help protect against ‘reinvestment risk’. Reinvestment risk is the risk that, when the sums are actually received, interest rates (and so yields available on assets) might have fallen below current expectations.

#### Currency risk

##### Sources of currency risk

- 4.2.49 G Fluctuations in foreign exchange rates may impact adversely upon a *firm*, including where it holds an open position in a foreign currency. This is where future cash outflows (that is liabilities) in one currency are matched by future cash inflows (that is assets) in a different currency. The circumstances in which this could arise include where the *firm*:
- (1) has entered into contracts for the purchase or sale of foreign currency; or
  - (2) has entered into *contracts of insurance* under which *claims* are payable in, or determined by reference to a value or price expressed in, a foreign currency; or
  - (3) holds assets denominated in a foreign currency.

#### Cover for spot and forward currency transactions

- 4.2.50 R A *firm* must cover a contract providing for the purchase or sale of foreign currency by:
- (1) holding the currency that must be paid by the *firm* under the contract; or
  - (2) being subject to an offsetting transaction.
- 4.2.51 G The requirements in relation to cover and offsetting transactions are set out in *PRU 4.3*.

#### Currency matching of assets and liabilities

- 4.2.52 G *PRU 7.2.34R* requires a *firm* to cover its liabilities with assets that enable it to match, in timing, amount and currency, the cash inflows and outflows from those assets and liabilities. This permits some currency mismatching of assets and liabilities, but only if sufficient excess assets are held to cover the exposure arising from such mismatching. The level of permitted currency mismatching is also limited by *PRU 4.2.53R*.
- 4.2.53 R Subject to *PRU 4.2.54R*, a *firm* must hold *admissible assets* in each currency of an amount equal to at least 80% of the amount of its liabilities (excluding, for a *firm* that carries on *general insurance business*, any *equalisation provision*) in that currency, except where the amount of those assets does not exceed 7% of the assets in other currencies.
- 4.2.54 R *PRU 4.2.53R* does not apply to:
- (1) a *pure reinsurer*; or
  - (2) assets held to cover *index-linked liabilities* or *property-linked liabilities*.
- 4.2.55 R For the purpose of *PRU 4.2.53R*, the currency of the liability under a *contract of insurance* is the currency in which the cover under the *contract of insurance* is expressed or, if the contract does not specify a currency:

- (1) the currency of the country or territory in which the risk is situated; or
- (2) if the *firm* on reasonable grounds so decides, the currency in which the *premium* payable under the contract is expressed; or
- (3) if, taking into account the nature of the risks insured, the *firm* considers it more appropriate:
  - (a) the currency (based on past experience) in which it expects the *claims* to be paid; or
  - (b) if there is no past experience, the currency of the country or territory in which the *firm* or relevant branch is established:
    - (i) for contracts covering risks falling within *general insurance business classes* 4, 5, 6, 7, 11, 12 and 13 (producer's liability only); and
    - (ii) for contracts covering risks falling within any other *general insurance business class* where, in accordance with the nature of the risks, the *firm's* liabilities are liabilities to be provided in a currency other than that which would result from the application of (1) or (2); or
- (4) (where a *claim* has been notified to the *firm* and the *firm's* liability in respect of that *claim* is payable in a currency other than that which would result from the application of (1), (2) or (3)) the currency in which the *claim* is to be paid; or
- (5) (where a *claim* is assessed in a currency known to the *firm* in advance and is a currency other than that which would result from the application of (1), (2), (3) or (4)) the currency in which the *claim* is to be assessed.

4.2.56 G The reasonable grounds in *PRU* 4.2.55R(2) include if, from the time the contract is entered into, it appears likely that a *claim* will be paid in the currency of the *premium* and not in the currency of the country in which the risk is situated.

#### Covering linked liabilities

4.2.57 R A *firm* must cover its *property-linked liabilities* with:

- (1) (as closely as possible) the assets to which those liabilities are linked; or
- (2) a property-linked *reinsurance* contract; or
- (3) a combination of (1) and (2).

4.2.58 R A *firm* must cover its *index-linked liabilities* with:

- (1) either:

- (a) the assets which represent that index; or
  - (b) assets of appropriate security and marketability which correspond, as closely as possible, to the assets which are comprised in, or which form, the index or other reference of value to which those liabilities are linked; or
- (2) a portfolio of assets whose value or yield is reasonably expected to correspond closely with the *index-linked liability*; or
  - (3) an index-linked *reinsurance* contract; or
  - (4) an index-linked *approved derivative*; or
  - (5) an index-linked *approved quasi-derivative*; or
  - (6) a combination of any of (1) to (5).
- 4.2.59 G For the purposes of *PRU 4.2.57R* and *PRU 4.2.58R*, a *firm* is not permitted to hold different assets and to cover the mismatch by holding excess assets.
- 4.2.60 G If a *firm* has incurred a *policy* liability which cannot be exactly matched by appropriate assets (for example the Limited Price Index (LPI) and Earnings Index), the *firm* should seek to match assets that at least cover the liabilities. For example, an LPI limited to 5% per annum may be matched by a 5% fixed interest bond or a RPI bond.
- 4.2.61 G In selecting the appropriate cover, the *firm* should ensure that both credit risk, and the risk that the value or yield in the assets will not, in all circumstances, match fluctuations in the relevant index, are within acceptable limits. *Rules* and *guidance* relating to credit risk are set out in *PRU 3.2*.

### 4.3 Derivatives in insurance

#### Application

- 4.3.1 R This section applies to an *insurer*, unless it is:
- (1) a *non-directive friendly society*; or
  - (2) an *incoming EEA firm*; or
  - (3) an *incoming Treaty firm*.
- 4.3.2 G The scope of application of *PRU 4.3* is not restricted to *firms* that are subject to the relevant EC directives. It applies, for example, to *pure reinsurers*.
- 4.3.3 (1) This section applies to a *firm* in relation to the whole of its business, except where a particular provision provides for a narrower scope.
- (2) Where a *firm* carries on both *long-term insurance business* and *general insurance business*, this section applies separately to each type of business.

#### Purpose

- 4.3.4 G *PRU 2.2.12R* requires a *firm* to calculate its *capital resources* for the purpose of *PRU* in accordance with Table *PRU 2.2.14R*, subject to the limits in *PRU 2.2.16R* to *PRU 2.2.26R*. Table *PRU 2.2.14R* and *PRU 2.2.86R* require a *firm* to deduct from total *capital resources* the value of any asset included in an insurance fund which is not an *admissible asset* as listed in *PRU 2 Ann 1R*. *PRU 2 Ann 1R* provides that a *derivative*, *quasi-derivative* or *stock lending transaction* will only be an *admissible asset* if it is approved. This section sets out the criteria for determining when a *derivative*, *quasi-derivative* or *stock lending transaction* is approved for this purpose. *PRU 4.3.5R* to *PRU 4.3.35R* set out the criteria for *derivatives* and *quasi-derivatives*. *PRU 4.3.36R* to *PRU 4.3.41R* set out the criteria for *stock lending transactions*.

#### Derivatives and quasi-derivatives

- 4.3.5 R For the purpose of *PRU 2 Ann 1R* (Admissible assets in insurance), a *derivative* or *quasi-derivative* is approved if:
- (1) it is held for the purpose of efficient portfolio management (*PRU 4.3.6R* to *PRU 4.3.7R*) or reduction of investment risk (*PRU 4.3.8R* to *PRU 4.3.13G*);
  - (2) it is covered (*PRU 4.3.14R* to *PRU 4.3.33G*); and
  - (3) it is effected or issued:
    - (a) on or under the rules of a *regulated market*; or
    - (b) off-market with an *approved counterparty* and, except for a forward transaction, on approved terms and is capable of valuation (*PRU 4.3.34R* to *4.3.35R*).

#### Efficient portfolio management

- 4.3.6 R A *derivative* or *quasi-derivative* is held for the purpose of efficient portfolio management if the *firm* reasonably believes the *derivative* or *quasi-derivative* (either alone or together with any other covered transactions) enables the *firm* to achieve its investment objectives by one of the following:
- (1) generating additional capital or income in one of the ways described in *PRU 4.3.7R*; or
  - (2) reducing tax or investment cost in relation to *admissible assets*; or
  - (3) acquiring or disposing of rights in relation to *admissible assets*, or their equivalent, more efficiently or effectively.

#### Generation of additional capital or income

- 4.3.7 R The generation of additional capital or income falls within *PRU 4.3.6R(1)* where it arises from:
- (1) taking advantage of pricing imperfections in relation to the acquisition and disposal (or disposal and acquisition) of rights in relation to assets the same as, or equivalent to, *admissible assets*; or
  - (2) receiving a premium for selling a covered call *option* or its equivalent, the underlying of which is an *admissible asset*, even if that additional capital or income is obtained at the expense of surrendering the chance of greater capital or income.
- Reduction of investment risk
- 4.3.8 R A *derivative* or *quasi-derivative* is held for the purpose of reducing investment risk if the *derivative* or *quasi-derivative* (either alone or together with other fully covered transactions) reduces any aspect of investment risk without significantly increasing any other aspect of that risk.
- Significant increase in risk
- 4.3.9 R For the purposes of *PRU 4.3.8R*, an increase in risk from a *derivative* or *quasi-derivative* is significant unless:
- (1) relative to any reduction in investment risk it is both small and reasonable; or
  - (2) the risk is remote.
- 4.3.10 G *PRU 4.3.8R* does not require that a *derivative* or *quasi-derivative* has no possible adverse consequences. Often a *derivative* or *quasi-derivative* is effected to protect against a severe adverse consequence that only arises in one circumstance. In all other circumstances it may itself lead to adverse consequences, even if only because it expires worthless resulting in the loss of the purchase price. Conversely a *derivative* or *quasi-derivative* may reduce risk in a wide range of circumstances but lead to adverse consequences when a particular circumstance arises, e.g. the default of the *counterparty*. Only rarely does a *derivative* or *quasi-derivative* give rise to no adverse consequences in any circumstances. The test is merely that the increase in risk should not be significant, that is it should be both small and reasonable, or the risk should be remote.
- 4.3.11 G *Firms* are reminded that *PRU 3.2* (Credit risk in insurance) sets out the different types of loss mitigation techniques.
- Investment risk
- 4.3.12 R For the purposes of *PRU 4.3.8R*, investment risk is the risk that the assets held by a *firm*:
- (1) (where they are *admissible assets* held by the *firm* to cover its *technical provisions*) might not be:
    - (a) of a value at least equal to the amount of those *technical provisions* as required by *PRU 7.2.20R*; or
    - (b) of appropriate safety, yield and marketability as required by *PRU 7.2.34R(1)(a)*; or
    - (c) of an appropriate currency match as required by *PRU 4.2.53R*;
  - (2) (where they are held to cover *index-linked liabilities*) might not be appropriate cover for those liabilities as required by *PRU 4.2.58R*; and

- (3) (where they are held to cover *property-linked liabilities*) might not be appropriately selected in accordance with contractual and constructive liabilities as required by *PRU 7.6.36R* and appropriate cover for those liabilities as required by *PRU 4.2.57R*.
- 4.3.13 G In assessing whether investment risk is reduced, the impact of a transaction on both the assets and liabilities should be considered. In particular, where the amount of liabilities depends upon the fluctuations in an index or other factor, investment risk is reduced where assets whose value fluctuates in the same way match those liabilities. In appropriate circumstances this may include:
- (1) a *derivative* or *quasi-derivative* that is linked to the same index as the liabilities from the index-linked contracts; and
  - (2) a *derivative* or *quasi-derivative* whose value depends upon the factors which give rise to general insurance claims, e.g. a weather *quasi-derivative*.
- Cover
- 4.3.14 R A *firm* must cover an obligation to transfer assets or pay monetary amounts that arises from:
- (1) a *derivative* or *quasi-derivative*; or
  - (2) a contract (other than a *contract of insurance*) for the purchase, sale or exchange of assets.
- 4.3.15 R An obligation to transfer assets or pay monetary amounts (see *PRU 4.3.14R*) must be covered:
- (1) by assets, a liability or a provision (see *PRU 4.3.16R* to *PRU 4.3.24R*); or
  - (2) by an offsetting transaction (see *PRU 4.3.25R* to *PRU 4.3.27R*).
- 4.3.16 R An obligation to transfer assets (other than *money*) or to pay monetary amounts based on the value of, or income from, assets is covered if the *firm* holds:
- (1) those assets; or
  - (2) in the case of an index or basket of assets, a reasonable approximation to those assets.
- 4.3.17 R An obligation to pay a monetary amount (whether or not falling in *PRU 4.3.16R*) is covered if:
- (1) the *firm* holds *admissible assets* that are sufficient in value so that the *firm* reasonably believes that following reasonably foreseeable adverse variations (relying solely on cashflows from, or from realising, those assets) it could pay the monetary amount in the right currency when it falls due; or
  - (2) the obligation to pay the monetary amount is offset by a liability. An obligation is offset by a liability where an increase in the amount of that obligation would be offset by a decrease in the amount of that liability; or
  - (3) a provision at least equal to the value of the assets in (1) is implicitly or explicitly set up. A provision is implicitly set up to the extent that the obligation to pay the monetary amount is recognised under *PRU 1.3* (Valuation) either by offset against an asset or as a separate liability. A provision is explicitly set up if it is in addition to an implicit provision.
- 4.3.18 R A *firm* must implicitly or explicitly set up a provision equal to the value of the assets or offsetting transactions held to cover a non-approved *derivative* or *quasi-derivative* transaction.

- 4.3.19 G Where a *firm* partially covers a *derivative* (or other contract falling within *PRU* 4.3.14R(1) and (2)), the *firm* may split the *derivative* into a covered portion and an uncovered portion. The portion of the *derivative* that is covered (after taking into account the requirement to cover reasonably foreseeable adverse variations in *PRU* 4.3.17R(1)) is an *approved derivative*, provided it also meets the requirements in *PRU* 4.3.5R(1) and (3); the uncovered portion is not an *approved derivative*.
- 4.3.20 G Exposure to a transaction includes exposure that arises from a right at the *firm's* (or its *subsidiary undertaking's*) option to dispose of assets.
- 4.3.21 G Cover serves three purposes. First, it protects against exposure to loss from the transaction which is being covered. The value of the cover increases (or if the cover is a liability the amount of that liability decreases) to match any increase in obligations under the transaction.
- 4.3.22 G The second purpose of cover is that it prevents excessive gearing in the investment portfolio by the use of *options* and their equivalent. A *firm* is required to cover all obligations under an admissible transaction including obligations that would arise only at the option of the *firm*, e.g. the liability to pay the exercise price under a bought *option*.
- 4.3.23 G The third purpose of cover is that it protects against the risk that the *firm* may not be able to deliver assets (including *money* in any currency) of the right type when the obligation falls due under the transaction. An obligation to deliver assets is covered only if the *firm* holds those assets or has entered into an offsetting transaction that would deliver those assets when needed. An obligation to pay *money* is offset only if the *firm* holds cash in the right currency, its equivalent or assets that could reliably be converted into cash in the right currency.
- 4.3.24 R Cover used for one transaction must not be used for cover in respect of another transaction or any other agreement to acquire, or dispose of, assets or to pay or repay *money*.
- Offsetting transactions
- 4.3.25 R An offsetting transaction means:
- (1) an *approved derivative*, *approved stock lending transaction* or an *approved quasi-derivative*; or
  - (2) a covered transaction with an *approved counterparty* for the purchase of assets.
- 4.3.26 R A transaction offsets an obligation to transfer assets away from the *firm* only if it provides for the transfer to the *firm* of those assets, or their value, at the time, or before, the obligation falls due.
- 4.3.27 R A transaction offsets an obligation to pay a monetary amount only if it provides for that monetary amount to be paid to the *firm* at or before the earliest date on which the obligation might fall due.
- Lending and borrowing assets
- 4.3.28 R Assets that have been lent by the *firm* are not available for cover, unless:
- (1) they are non-monetary assets that have been lent under a transaction that fulfils the conditions in *PRU* 4.3.36R; and
  - (2) the *firm* reasonably believes the assets to be obtainable (by return or re-acquisition) in time to meet the obligation for which cover is required.
- 4.3.29 R Assets that have been borrowed by the *firm* are not available for cover except as allowed by *PRU* 4.3.30R.
- 4.3.30 R Borrowed *money* may be used as cover only where:



- (1) the *money* has been advanced or an *approved credit institution* has committed itself to advance the *money*; and
- (2) the borrowing is or would be covered.
- 4.3.31 G *PRU 4.3.30R* in effect allows borrowings to be used to bridge the gap between an obligation under a transaction that might fall due at one date and cash or its equivalent that would only become due at a later date. Borrowings may not be used to gear the investment portfolio.

Examples of cover requirements

- 4.3.32 G Examples of cover by assets for the purposes of *PRU 4.3.16R* :
- (1) a bought put *option* (or a sold call *option*) on 1000 £1 *shares* (fully paid) of ABC plc is covered by an existing holding in the fund of 1000 £1 *shares* (fully paid) of ABC plc;
- (2) a bought call *option* (or sold put *option*) on 1000 ordinary £1 *shares* (fully paid) of ABC plc is covered by cash (or its equivalent) which is sufficient in amount to meet the purchase price of the *shares* on exercise of the *option*;
- (3) a bought or sold *contract for differences* on short-dated sterling is covered by cash (or its equivalent), the value of which together at least match the notional principal of the contract. For example, a LIFFE short sterling contract, or a successive series of such contracts, is covered by £500,000; and
- (4) a sold *future* on the FT-SE 100 index is covered by holdings of equities, which satisfy the reasonable approximation test for cover in *PRU 4.3.16R(2)* in relation to that *future*, and the values of which together at least match the current mark to market valuation of the *future*. For example, if the multiplier per full point is £10, and if the eventual obligation under the *future* is currently 2800, the valuation of the *futures* position is  $2800 \times £10 = £28,000$ .

- 4.3.33 G Examples of cover by offsetting transactions for the purpose of *PRU 4.3.25R* would include a bought *future* which is guaranteed to deliver to the *firm* at the relevant time sufficient assets to cover liabilities under a sold call *option*.

Over the counter transactions

- 4.3.34 R For the purpose of *PRU 4.3.5R(3)(b)*, a transaction is on approved terms only if the *counterparty* has agreed to enter into a further transaction to close out the first transaction at a price based on current market conditions.
- 4.3.35 R A transaction is capable of valuation only if the *firm*, throughout the life of the transaction, will be able to value it with reasonable accuracy on a reliable basis reflecting an up-to-date mark-to-market value.

Stock lending

- 4.3.36 R For the purposes of *PRU 2 Ann 1R* (Admissible assets in insurance), a *stock lending* transaction is approved if:
- (1) the assets lent are *admissible assets*;
- (2) the *counterparty* is an *authorised person* or an *approved counterparty*; and
- (3) adequate and sufficiently immediate *collateral* (*PRU 4.3.38R* to *PRU 4.3.41R*) is obtained to secure the obligation of the *counterparty*.
- 4.3.37 G *PRU 4.3.36R* refers only to *stock lending* transactions where the *firm* is the lender. There are no special *rules* for a transaction under which the *firm* borrows *securities*.

Collateral

- 4.3.38 R For the purposes of *PRU 4.3.36R(3)*, *collateral* is adequate only if it:
- (1) is transferred to the *firm* or its agent;
  - (2) is, at the time of the transfer, at least equal in value to the value of the *securities* transferred, or consideration provided, by the *firm*; and
  - (3) is of adequate quality.
- 4.3.39 G For the purposes of assessing adequate quality in *PRU 4.3.38R(3)*, reference should be made to the criteria for credit risk loss mitigation set out in *PRU 3.2.16R*. The valuation rules in *PRU 1.3* apply for the purpose of determining the value of both *collateral* received and the *securities* transferred. In addition, *collateral* that is not an *admissible asset* does not have a value (see *PRU 2 Ann 1R*).
- 4.3.40 R For the purposes of *PRU 4.3.36R(3)*, *collateral* is sufficiently immediate only if:
- (1) it is transferred before, or at the same time as, the transfer of the *securities* by the *firm*; or
  - (2) it will be transferred, at latest, by the close of business on the day of the transfer.
- 4.3.41 R *Collateral* continues to be adequate only if its value is at all times at least equal to the value of the *securities* transferred by the *firm*. This will be satisfied in respect of *collateral* the validity of which is about to expire or has expired where sufficient *collateral* will again be transferred at the latest by the close of business on the day of expiry.

## Annex G

### PRU 5

In this Annex, all the text is new and is not underlined.

- 5.1 Liquidity risk systems and controls
- Application
- 5.1.1 R *PRU 5.1* applies to an *insurer* unless *PRU 5.1.8R* applies.
- 5.1.2 R All of *PRU 5.1*, except *PRU 5.1.17G*, *PRU 5.1.27G*, *PRU 5.1.58G* to *PRU 5.1.60G*, *PRU 5.1.61E*, *PRU 5.1.62G*, *PRU 5.1.85G*, *PRU 5.1.86E*, and *PRU 5.1.87G* to *PRU 5.1.91G*, applies to:
- (1) an *EEA-deposit insurer*; and
  - (2) a *Swiss general insurer*;
- but only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.
- 5.1.3 R Subject to *PRU 5.1.5R*, *PRU 5.1.6R* and *PRU 5.1.8R*, the following provisions of *PRU 5.1* apply to a *firm* described in *PRU 5.1.4R*:
- (1) *PRU 5.1.18G*;
  - (2) *PRU 5.1.58G* to *PRU 5.1.60G*;
  - (3) *PRU 5.1.61E*;
  - (4) *PRU 5.1.62G*;
  - (5) *PRU 5.1.85G*;
  - (6) *PRU 5.1.86E*; and
  - (7) *PRU 5.1.87G* to *PRU 5.1.91G*.
- 5.1.4 R The *firms* referred to in *PRU 5.1.3R* are:
- (1) a *building society*;
  - (2) a *bank* or an *own account dealer* (other than a *venture capital firm*) that is a *UK firm*;
  - (3) an *incoming EEA firm* which:
    - (a) is a *full BCD credit institution*; and
    - (b) has a *branch* in the *United Kingdom*;
  - (4) an *overseas firm* which is a *bank* or an *own account dealer* (other than a *venture capital firm*) but which is not:
    - (a) an *incoming EEA firm*; or

- (b) a *lead-regulated firm*;
- (5) an *overseas firm* which:
  - (a) is a *bank*;
  - (b) is a *lead-regulated firm*;
  - (c) is not an *incoming EEA firm*; and
  - (d) has a *branch* in the *United Kingdom*.
- 5.1.5 R For a *firm* described in *PRU 5.1.4R(3)* or *PRU 5.1.4R(5)*, *PRU 5.1* applies only with respect to the *branch*.
- 5.1.6 R This section applies to an *incoming EEA firm* only to the extent that the relevant matter is not reserved by the relevant *Single Market Directive* to the *firm's Home State regulator*.
- 5.1.7 R If a *firm* carries on:
  - (1) *long-term insurance business*; and
  - (2) *general insurance business*;
 this section applies separately to each type of business.
- 5.1.8 R This section does not apply to:
  - (1) a *non-directive friendly society*; or
  - (2) a *UCITS qualifier*; or
  - (3) an *ICVC*; or
  - (4) an *incoming EEA firm* (unless *PRU 5.1.4R* applies); or
  - (5) an *incoming Treaty firm*.
- 5.1.9 R For the purposes of this section, the *guidance* in *PRU 1.4.14G* to *PRU 1.4.16G* applies to a *firm* described in *PRU 5.1.4R*.
- Purpose
- 5.1.10 G The purpose of this section is to amplify parts of *PRU* in their application to *liquidity risk* and, in so doing, to suggest minimum standards for systems and controls in respect of that risk. The main relevant part, *PRU 1.4*, itself amplifies *Principle 3* (Management and control) and *SYSC* (Senior management arrangements, Systems and Controls).
- 5.1.11 G Appropriate systems and controls for the management of *liquidity risk* will vary with the scale, nature and complexity of the *firm's* activities. Most of the material in this section is, therefore, *guidance*. The section lays out some of

the main issues that the *FSA* expects a *firm* to consider in relation to *liquidity risk*. A *firm* should assess the appropriateness of any particular item of *guidance* in the light of the scale, nature and complexity of its activities as well as its obligations as set out in *Principle 3* to organise and control its affairs responsibly and effectively.

- 5.1.12 G For *insurers*, references to *liquidity risk* in this section are intended to cover only those aspects of *liquidity risk* that do not fall under the heading of insurance risk. For such *firms*, the *FSA* sees the coverage of this section, broadly, as the management of risk arising from short-term cash-flows, rather than the risk arising from longer-term matching of assets and liabilities, which is part of insurance risk. *Guidance* on systems and controls for managing insurance risk is set out in *PRU 7.1*.
- 5.1.13 G The *FSA* recognises that a typical *firm* of a type described in *PRU 5.1.4R* generally faces *liquidity risk* from a wider range of sources and of greater significance than a typical *insurer*. This section therefore explicitly applies some items of *guidance to firms* in *PRU 5.1.4R*. Other parts of the *guidance* are also not relevant to many *insurers*. In particular, where the *guidance* refers to factors that a *firm* should consider in relation to a specific type of business, a *firm* that does not undertake such business does not need to carry out such consideration.
- 5.1.14 G This section addresses the need to have appropriate systems and controls to deal both with liquidity management issues under normal market conditions, and with stressed or extreme situations resulting from either general market turbulence or firm-specific difficulties.

#### Requirements

- 5.1.15 G High level requirements for prudential systems and controls including for *liquidity risk* are set out in *PRU 1.4*. In particular:
- (1) *PRU 1.4.18R* requires a *firm*, among other things, to take reasonable steps to ensure the establishment of a business plan and appropriate systems for the management of prudential risk; and
  - (2) *PRU 1.4.19R(2)* requires a *firm*, among other things, to document its policy for managing *liquidity risk*, including its appetite or tolerance for this risk and how it identifies, measures, monitors and controls this risk.
- 5.1.16 G This section sets out *guidance* on each of these areas, and notes a number of matters which the *FSA* would expect a *firm* to deal with in its *liquidity risk* policy statement as follows:
- (1) its *liquidity risk* strategy (see *PRU 5.1.23G* to *PRU 5.1.25G*), including:

- (a) the role of marketable, or otherwise realisable, assets (see *PRU 5.1.32G*); and
  - (b) its strategy for mitigating *liquidity risk* on the liability side (see *PRU 5.1.37G*);
  - (2) its method for measuring *liquidity risk* (see *PRU 5.1.55G*);
  - (3) its system for monitoring *liquidity risk* (see *PRU 5.1.63G*); and
  - (4) its system for controlling *liquidity risk* (see *PRU 5.1.71G*).
- 5.1.17 G High level requirements in relation to carrying out stress testing and scenario analysis are set out in *PRU 1.2*. In particular, *PRU 1.2.35R* requires a *firm* to carry out appropriate stress testing and scenario analysis. This section gives *guidance* in relation to these tests in the case of *liquidity risk*.

#### Firms with group liquidity management

- 5.1.18 G *Firms* with group liquidity management should refer to *PRU 1.4.14G* to *1.4.16G*.

#### Managing liquidity risk

- 5.1.19 G This section amplifies the general requirements in *PRU 1.4* by describing the key high level arrangements that the *FSA* would normally expect to be in place to ensure that a *firm's liquidity risk* management system is adequate.

#### Governing body and senior management oversight

- 5.1.20 G *PRU 1.4.11G* amplifies *SYSC 2.1.1R* and *SYSC 2.1.3R* which require the apportionment, and allocation, of significant responsibilities to be such that the business and affairs of the *firm* can be adequately monitored and controlled by the *directors*, relevant senior executives and *governing body* of the *firm*. Effective *liquidity risk* management entails an informed board, capable management and appropriate staffing. The *governing body* and senior management are responsible for understanding the nature and level of *liquidity risk* assumed by the *firm* and the tools used to manage that risk.
- 5.1.21 G In relation to *liquidity risk*, the *governing body's* responsibilities should normally include:
- (1) approving the *firm's liquidity risk* policy, which includes taking reasonable steps to ensure that it is consistent with the *firm's* expressed risk tolerance (see *PRU 5.1.23G* to *PRU 5.1.25G*);
  - (2) establishing a structure for the management of *liquidity risk* including the allocation of appropriate *senior managers* who have the authority and responsibility to manage *liquidity risk* effectively, including the establishment and maintenance of the *firm's liquidity risk* policy;

- (3) monitoring the *firm's* overall *liquidity risk* profile on a regular basis and being made aware of any material changes in the *firm's* current or prospective *liquidity risk* profile; and
- (4) taking reasonable steps to ensure that *liquidity risk* is adequately identified, measured, monitored and controlled.

5.1.22 G A *firm* should have an appropriate senior management structure in place to oversee the daily and long-term management of *liquidity risk* in line with the *governing body*-approved *liquidity risk* policy (see *PRU* 5.1.23G to *PRU* 5.1.25G). The *FSA* would normally expect the senior management to:

- (1) oversee the development, establishment and maintenance of procedures and practices that translate the goals, objectives and risk tolerances approved by the *governing body* into operating standards that are consistent with the *governing body's* intent and understood by the relevant members of a *firm's* personnel;
- (2) adhere to the lines of authority and responsibility that the *governing body* has established for managing *liquidity risk*;
- (3) oversee the establishment and maintenance of management information (see *PRU* 5.1.66G to *PRU* 5.1.70G) and other systems that identify, measure, monitor and control the *firm's* *liquidity risk*; and
- (4) oversee the establishment of effective *internal controls* over the *liquidity risk* management process (see *PRU* 5.1.71G to *PRU* 5.1.90G (Controlling liquidity risk)).

#### Liquidity risk policy

5.1.23 G *SYSC* 3.2.17G gives *guidance*, which amplifies *SYSC* 3.2.6R, on the need for a *firm* to plan its business appropriately so that it is able to identify, measure, monitor and control risks of regulatory concern. A *firm* should, therefore, have an agreed policy for the day-to-day and longer term management of *liquidity risk* which is appropriate to the nature, scale and complexity of the activities carried on.

5.1.24 G The *liquidity risk* policy should cover the general approach that the *firm* will take to *liquidity risk* management, including, as appropriate, various quantitative and qualitative targets. This general approach should be communicated to all relevant functions within the organisation and be included in the *firm's* *liquidity risk* policy statement.

5.1.25 G The policy for managing *liquidity risk* should cover specific aspects of *liquidity risk* management. So far as appropriate to the nature, scale and complexity of the activities carried on, such aspects might include:

- (1) the basis for managing liquidity (for example, regional or central);
- (2) the degree of concentrations, potentially affecting *liquidity risk*, that are acceptable to the *firm*;
- (3) a policy for managing the liability side of *liquidity risk* (see *PRU* 5.1.37G);
- (4) the role of marketable, or otherwise realisable, assets (see *PRU* 5.1.32G);
- (5) ways of managing both the *firm's* aggregate foreign currency liquidity needs and its needs in each individual currency;
- (6) ways of managing market access;
- (7) the use of *derivatives* to minimise *liquidity risk*; and
- (8) the management of intra-day liquidity, where this is appropriate, for instance where the *firm* is a member of or participates (directly or indirectly) in a system for the intra-day settlement of payments or transactions in investments.

#### Identifying liquidity risk

- 5.1.26 G In order to manage *liquidity risk* successfully, a *firm* should be aware of the ways in which its activities can affect its *liquidity risk* profile, and how outside influences may affect its liquidity position. A *firm* should consider not only its current *liquidity risk*, but how existing activities may affect its *liquidity risk* profile in the future; it should also consider the implications of new products or business lines. This section identifies the main sources of *liquidity risk* and the key factors that a *firm* might consider when analysing its *liquidity risk* profile.
- 5.1.27 G *PRU* 1.2.22R states that a *firm* must maintain overall financial resources adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due. The *firm* should, therefore, ensure that, overall, its financial resources are of appropriate maturity, and in a form which is sufficiently marketable or otherwise realisable, having regard to the expected timing of liabilities and the risk that liabilities may fall due earlier than expected (for which prudent allowance must be made when assessing whether assets are of appropriate maturity or sufficiently realisable).

#### Asset liquidity

- 5.1.28 G A *firm's* asset portfolio can provide liquidity in three major ways:
- (a) through the maturity of an asset;



(b) the sale of an asset for cash; or

(c) the use of an asset as *collateral* to back other transactions, such as for secured borrowing (including repos), or for deposits with insureds or cedants to back insurance or *reinsurance* transactions.

- 5.1.29 G A *firm* may incur *liquidity risk* where inflows from the realisation of assets (at either maturity or time of sale) are less than anticipated because of the crystallisation of credit risk or *market risk*. Inflows arising from the renewal of secured funding, including repos, are similarly affected, if the haircut (the difference between the value of an asset and the amount lent to the *firm* by the counterparty using that security as *collateral*) required by a *firm's* counterparty is larger than anticipated (see *PRU 5.1.39G*).
- 5.1.30 G Asset concentrations often increase these sources of *liquidity risk*. A *firm* should, therefore, identify significant concentrations within its asset portfolio, including in relation to:
- (1) individual counterparties or related groups of counterparties;
  - (2) credit ratings of the assets in its portfolio;
  - (3) the proportion of an issue held;
  - (4) instrument types;
  - (5) geographical regions; and
  - (6) economic sectors.

#### Marketable assets

- 5.1.31 G Criteria for the marketability of its assets should be decided by the *firm* and may reflect the *firm's* access to, and expertise in, individual markets. In determining the appropriateness of the marketability or realisability of assets, a *firm* may take into account:
- (1) the depth and liquidity of the market, including:
    - (a) the speed with which assets may be realised;
    - (b) the likelihood and extent of forced-sale loss; and
    - (c) the potential for using the asset as *collateral* in secured funding and the size of the haircut (see *PRU 5.1.29G*) likely to be required by the counterparty;
  - (2) the expected date of maturity, redemption, repayment or disposal;
  - (3) the proportion of an issue held;

- (4) the credit ratings of the assets;
  - (5) the impact of exchange rate risk on the realised value of the asset, where assets are denominated in different currencies from its liabilities; and
  - (6) where applicable, the impact on certain assets' liquidity of their use as eligible *collateral* either in open-market operations conducted by, or in real-time or other payment systems operated by, a central bank.
- 5.1.32 G The role of marketable, or otherwise realisable, assets in a *firm's liquidity risk* policy, in both normal and stressed conditions, should be set out in its *liquidity risk* policy statement.
- 5.1.33 G In considering the marketability of an asset, a *firm* should assess how its value and liquidity would be affected in a variety of scenarios (see *PRU 5.1.58G* to *PRU 5.1.60G*, *PRU 5.1.61E* and *PRU 5.1.62G*).

#### Adjusting for the behavioural characteristics of assets

- 5.1.34 G In order to manage its *liquidity risk* effectively, a *firm* should be able to adjust for the behavioural characteristics of the repayment profiles of assets, that is how their actual behaviour may vary from that suggested by their contractual terms. Such an adjustment may be necessary in order to reduce the risk of wrongly estimating the inflows in relation to, in particular:
- (1) standby facilities or other commitments that have already been drawn down;
  - (2) retail and wholesale overdrafts;
  - (3) mortgages; and
  - (4) credit cards.
- 5.1.35 G The repayment profiles should be considered under both normal market conditions and stressed conditions resulting from either general market turbulence or *firm-specific* difficulties (see *PRU 5.1.58G* to *PRU 5.1.60G*, *PRU 5.1.61E* and *PRU 5.1.62G*, and *PRU 5.1.85G*, *PRU 5.1.86E*, and *PRU 5.1.87G* to *PRU 5.1.90G*).

#### Inflows from off balance sheet items

- 5.1.36 G Where a *firm* has in place a committed facility for the provision of a portion of its funding, it should take care to monitor any covenants included in the agreement. It should also make efforts to retain a good relationship with the provider of the facility and, where possible without jeopardising that relationship, regularly test access to the funds. A *firm* should also assess the extent to which committed facilities can be relied upon under stressed conditions (see *PRU 5.1.62G(1)(c)* and *PRU 5.1.88G(4)*).

## Liability liquidity

- 5.1.37 G Holding marketable, or otherwise realisable, assets is not the only way for a *firm* to mitigate the *liquidity risk* it faces. There are a number of liability-side strategies that can be used to reduce a *firm's liquidity risk*, such as ensuring a spread of maturities and lengthening the term structure of its liabilities. In order to manage its *liquidity risk* effectively a *firm* should have a liability-side policy that is appropriate to the nature and scale of its activities; this policy should be described in its *liquidity risk* policy statement.
- 5.1.38 G When determining the appropriate mix of liabilities, a *firm's* management should consider potential concentrations. A concentration exists when a single decision or factor could cause a significant and sudden claim on liabilities. What constitutes a liability concentration depends on the nature and scale of a *firm's* activities. A *firm* should, however, normally consider:
- (1) the term structure of its liabilities;
  - (2) the credit-sensitivity of its liabilities;
  - (3) the mix of secured and unsecured funding;
  - (4) concentrations among its liability providers, or related groups of liability providers;
  - (5) reliance on particular instruments or products;
  - (6) the geographical location of liability providers; and
  - (7) reliance on intra-group funding.
- 5.1.39 G A *firm* with credit-sensitive liabilities should be aware that, in times of market turbulence, a proportion of that funding may be withdrawn, particularly funding which is unsecured. Secured funding may also be affected, with counterparties seeking better quality *collateral* or larger haircuts (see *PRU 5.1.29G*) on *collateral*. A *firm* should recognise these characteristics of its credit-sensitive liabilities and take account of them in its stress testing and scenario analysis and *contingency funding plan* (see *PRU 5.1.58G* to *PRU 5.1.60G*, *PRU 5.1.61E* and *PRU 5.1.62G*, and *PRU 5.1.85G*, *PRU 5.1.86E*, and *PRU 5.1.87G* to *PRU 5.1.90G*).
- 5.1.40 G A *firm* should consider the dynamics of its *liquidity risk* including, for example, the normal level of roll-overs, and growth, of liabilities.

## Adjusting for the behavioural characteristics of liabilities

- 5.1.41 G In order to meet the requirement to maintain sufficient liquid financial resources (see *PRU 5.1.27G*), a *firm* should consider the behavioural characteristics of its liabilities, that is how their actual behaviour may vary from that suggested by their contractual terms.

- 5.1.42 G In assessing how to adjust for the behavioural characteristics of its liabilities in the context of *liquidity risk*, an *insurer* may take into account:
- (1) the type of *insurance business*;
  - (2) the past history of volatility in the pattern of *claims* payment;
  - (3) options available to *policyholders* and the circumstances in which they are likely to be exercised;
  - (4) options available to the *insurer* and any incentive for the *insurer* to exercise them;
  - (5) any relevant requirements to deposit *collateral* either with the insured (or cedants) under the terms of the insurance Treaty or by requirements of overseas regulators as a condition for covering risks in a particular territory; and
  - (6) the other cash flow needs of the business.

Outflows from off balance sheet items

- 5.1.43 G The contingent or optional nature of many off balance sheet instruments adds to the complexity of managing off balance sheet cash flows. In particular, in stressed conditions off balance sheet commitments may be a significant drain on liquidity.
- 5.1.44 G A *firm* should consider how its wholesale off balance sheet activities affect its cash flows and *liquidity risk* profile under both normal and stressed conditions. In particular, as appropriate, it should consider the amount of funding required by:
- (1) commitments given;
  - (2) standby facilities given;
  - (3) wholesale overdraft facilities given;
  - (4) proprietary *derivatives* positions; and
  - (5) liquidity facilities given for securitisation transactions.
- 5.1.45 G Similarly, a *firm* with retail *customers* should be able to assess the likely draw-down on retail products under a variety of circumstances and taking into account seasonal factors. In particular, as appropriate, it should consider the amount of funding required in relation to:
- (1) mortgages that have been agreed but not yet drawn down;
  - (2) overdrafts; and

- (3) credit cards.

#### Asset securitisations

- 5.1.46 G If controlled properly, asset securitisation can be a useful tool in enhancing a *firm's* liquidity. However, features of certain securitisations, such as early amortisation triggers, as well as excessive reliance on a single funding vehicle, can increase *liquidity risk*.
- 5.1.47 G The implications of securitisations on a *firm's* liquidity position should be considered for both day-to-day liquidity management and its contingency planning for *liquidity risk*. A contemplated securitisation should be analysed for its impact on *liquidity risk*. A *firm* using securitisation should consider:
- (1) the volume of *securities* issued in connection with the securitisation that are scheduled to amortise during any particular period;
  - (2) the existence of early amortisation triggers (see also *PRU 5.1.62G(3)(c)*);
  - (3) its plans for meeting its funding requirements (including their timing);
  - (4) strategies for obtaining substantial amounts of liquidity at short notice (see also *PRU 5.1.86E* and *PRU 5.1.88G*); and
  - (5) operational issues associated with the rollover of short-dated *securities*, particularly commercial paper.
- 5.1.48 G If a *firm* is a provider of liquidity facilities for securitisation transactions it should be able to assess the probability and scale of draw-down and make provision for it.
- 5.1.49 G A *firm* using securitisation should also be aware that its ability to securitise assets may diminish in stressed market conditions and take account of this in its stress testing and *contingency funding plan*. In addition, the time taken to organise a securitisation transaction may mean that it cannot be relied upon to provide liquidity at short notice.

#### Foreign currency liquidity

- 5.1.50 G Foreign currency *liquidity risk* arises where a *firm* faces actual or potential future outflows in a particular currency which it may not be able to meet from likely available inflows in that currency. A *firm's* exposure to foreign currency *liquidity risk* depends on the nature, scale and complexity of its business. Where a *firm* has significant, unhedged liquidity mismatches in particular currencies, it should consider:
- (1) the volatilities of the exchange rates of the mismatched currencies;

- (2) likely access to the foreign exchange markets in normal and stressed conditions; and
- (3) the stickiness of deposits in those currencies with the *firm* in stressed conditions.

5.1.51 G A possible strategy for mitigating foreign currency *liquidity risk*, which is effective and simple, is for a *firm* to hold assets in a particular currency in an amount equal to, and realisable at maturities no later than, its liabilities in that currency. This strategy may be worth considering particularly where, as a result of the nature, scale and complexity of its business, a *firm's liquidity risk* is relatively small.

#### Intra-day liquidity

5.1.52 G SYSC 3.1.1R requires a *firm* to take reasonable care to establish and maintain systems and controls appropriate to its business. This includes appropriate systems and controls over activities that give rise to significant *market*, credit, *liquidity*, insurance, operational or group risk, including over the processes of settling and paying debts and other commitments that arise from those activities.

5.1.53 G Structural and operational changes in payment systems have increased the importance of intra-day liquidity for many *firms*. Within real time gross settlement systems, for example, a *firm* needs to take appropriate steps to ensure that it has sufficient *collateral* to cover cash positions and has systems capable of monitoring intra-day liquidity positions and cash needs.

5.1.54 G A *firm* should be aware that in stressed conditions it is likely to require more intra-day liquidity than in normal market conditions, for a variety of reasons including payments due to the *firm* being delayed and wholesale depositors withdrawing from the market. A *firm* should take account of this in its stress testing and scenario analysis.

#### Measuring liquidity risk

5.1.55 G A *firm* should establish and maintain a process for the measurement of *liquidity risk*, using a robust and consistent method which should be described in its *liquidity risk* policy statement.

5.1.56 G A number of techniques can be used for measuring *liquidity risk*, ranging from simple calculations to highly sophisticated modelling; a *firm* should use a measurement method which is appropriate to the nature, scale and complexity of its activities.

5.1.57 G The method that a *firm* uses for measuring *liquidity risk* should be capable of:

- (1) measuring the extent of the *liquidity risk* it is incurring;

- (2) dealing with the dynamic aspects of a *firm's* liquidity profile (for example, rollovers of funding and assets or new business);
- (3) assessing the behavioural characteristics of its on and off balance sheet instruments; and
- (4) where appropriate, measuring the *firm's* exposure to foreign currency *liquidity risk*.

#### Stress testing and scenario analysis

- 5.1.58 G *PRU 1.2.26R, PRU 1.2.27R, PRU 1.2.31R, PRU 1.2.33R and PRU 1.2.35R* entail that, for the purposes of determining the adequacy of its overall financial resources, a *firm* must carry out appropriate stress testing and scenario analysis, including taking reasonable steps to identify an appropriate range of realistic adverse circumstances and events in which *liquidity risk* might occur or crystallise.
- 5.1.59 G *PRU 1.2.36G and PRU 1.2.40G to PRU 1.2.55G* give guidance on stress testing and scenario analysis, including on how to choose appropriate scenarios, but the precise scenarios that a *firm* chooses to use will depend on the nature of its activities. For the purposes of testing *liquidity risk*, however, a *firm* should normally consider scenarios based on varying degrees of stress and both *firm-specific* and market-wide difficulties. In developing any scenario of extreme market-wide stress that may pose systemic risk, it may be appropriate for a *firm* to make assumptions about the likelihood and nature of central bank intervention.
- 5.1.60 G A *firm* should review frequently the assumptions used in stress testing scenarios to gain assurance that they continue to be appropriate.
- 5.1.61 E (1) A scenario analysis in relation to *liquidity risk* required under *PRU 1.2.35R* should include a cash-flow projection for each scenario tested, based on reasonable estimates of the impact (both on and off balance sheet) of that scenario on the *firm's* funding needs and sources.
- (2) Contravention of (1) may be relied on as tending to establish contravention of *PRU 1.2.35R*.
- 5.1.62 G In identifying the possible on and off balance sheet impact referred to in *PRU 5.1.61E(1)*, a *firm* may take into account:
- (1) possible changes in the market's perception of the *firm* and the effects that this might have on the *firm's* access to the markets, including:
    - (a) (where the *firm* funds its holdings of assets in one currency with liabilities in another) access to foreign exchange markets, particularly in less frequently traded currencies;

- (b) access to secured funding, including by way of repo transactions; and
  - (c) the extent to which the *firm* may rely on committed facilities made available to it;
- (2) (if applicable) the possible effect of each scenario analysed on currencies whose exchange rates are currently pegged or fixed; and
- (3) that:
- (a) general market turbulence may trigger a substantial increase in the extent to which *persons* exercise rights against the *firm* under off balance sheet instruments to which the *firm* is party;
  - (b) access to *OTC derivative* and foreign exchange markets are sensitive to credit-ratings;
  - (c) the scenario may involve the triggering of early amortisation in asset securitisation transactions with which the *firm* has a connection; and
  - (d) its ability to securitise assets may be reduced.

#### Monitoring liquidity risk

- 5.1.63 G A *firm* should establish and maintain an appropriate system for monitoring its *liquidity risk*, which should be described in its *liquidity risk* policy statement.
- 5.1.64 G A *firm* should establish and maintain a system of management reporting which provides clear, concise, timely and accurate *liquidity risk* reports to relevant functions within the *firm*. These reports should alert management when the *firm* approaches, or breaches, predefined thresholds or limits, including quantitative limits imposed by the *FSA* or another regulator.
- 5.1.65 G Where a *firm* is a member of a *group*, it should be able to assess the potential impact on it of *liquidity risk* arising in other parts of the *group*.

#### Management information systems

- 5.1.66 G A *firm* should have adequate information systems for controlling and reporting *liquidity risk*. The management information system should be used to check for compliance with the *firm's* established policies, procedures and limits.
- 5.1.67 G Reports on *liquidity risk* should be provided on a timely basis to the *firm's governing body*, senior management and other appropriate personnel. The appropriate content and format of reports depends on a *firm's* liquidity management practices and the nature, scale and complexity of the *firm's*



business. Reports to the *firm's governing body* may be less detailed and less frequent than reports to senior management with responsibility for managing *liquidity risk*.

- 5.1.68 G For a *firm* described in *PRU 5.1.4R*, management information would normally contain the following:
- (1) a cash-flow or funding gap report;
  - (2) a funding maturity schedule;
  - (3) a list of large providers of funding; and
  - (4) a limit monitoring and exception report.
- 5.1.69 G When considering what else might be included in *liquidity risk* management information, a *firm* should consider other types of information that may be important for understanding its *liquidity risk* profile.
- 5.1.70 G For a *firm* described in *PRU 5.1.4R*, the additional information referred to in *PRU 5.1.69G* may include:
- (1) asset quality and trends;
  - (2) any changes in the *firm's* funding strategy;
  - (3) earnings projections; and
  - (4) the *firm's* reputation in the market and the condition of the market itself.

#### Controlling liquidity risk

- 5.1.71 G A *firm* should establish and maintain an appropriate system for controlling its *liquidity risk*, which should be described in its *liquidity risk* policy statement. Such a system should allow the *firm's governing body* and senior management to review compliance with established limits and operating procedures.
- 5.1.72 G A *firm* should have in place appropriate approval processes, limits and other mechanisms designed to provide reasonable assurance that the *firm's liquidity risk* management processes are adhered to.
- 5.1.73 G When revisions or enhancements to *internal controls* are warranted, a *firm* should implement them in a timely manner.
- 5.1.74 G The effectiveness of a *firm's liquidity risk* management system should be regularly reviewed and evaluated by individuals unconnected with day-to-day *liquidity risk* management in order to check that personnel are following established policies and procedures, and that procedures accomplish the

intended objectives.

- 5.1.75 G In addition to the regular review and evaluation described in *PRU 5.1.74G*, a *firm's* internal audit function should periodically review the *liquidity risk* management process in order to identify any weaknesses or problems. Any weaknesses should be addressed by management in a timely and effective manner.

#### Limit setting

- 5.1.76 G A *firm's* senior management should decide what limits need to be set, in accordance with the nature, scale and complexity of its activities. The structure of limits should reflect the need for a *firm* to have systems and controls in place to guard against a spectrum of possible risks, from those arising in day-to-day *liquidity risk* management to those arising in stressed conditions.
- 5.1.77 G *PRU 1.4.18R* states that a *firm* must take reasonable steps to ensure the establishment and maintenance of a business plan and appropriate systems for the management of prudential risk.
- 5.1.78 E (1) If a *firm* has *liquidity risk* that arises because it has substantial exposures in foreign currencies, the risk management systems of the *firm* referred to in *PRU 1.4.18R* should include systems and procedures that are designed to ensure that the *firm* does not, except in accordance with those procedures, exceed limits that are designed to limit:
- (a) the aggregate amount of its *liquidity risk* for all exposures in foreign currencies; and
  - (b) the amount of its *liquidity risk* for each individual currency in which it has a significant exposure.
- (2) Contravention of (1) may be relied upon as tending to establish contravention of *PRU 1.4.18R*.
- 5.1.79 G The *FSA* would normally expect a *firm* described in *PRU 5.1.4R* to consider setting limits on:
- (1) liability concentrations in relation to:
    - (a) individual, or related groups of, liability providers;
    - (b) instrument types;
    - (c) maturities, including the amount of debt maturing in a particular period; and
    - (d) retail and wholesale liabilities; and
  - (2) where appropriate, *net leverage* and *gross leverage*.
- 5.1.80 G A *firm* should periodically review and, where appropriate, adjust its limits

when conditions or risk tolerances change.

- 5.1.81 G Policy or limit exceptions should receive the prompt attention of the appropriate management and should be resolved according to processes described in approved policies.

#### Managing market access

- 5.1.82 G A *firm* should periodically review its efforts to establish and maintain relationships with liability providers, to maintain adequate diversification of liabilities, and to ensure adequate capacity to sell assets, or use them as *collateral* in secured funding. Where possible the *firm* should aim regularly to test its access to the individual markets in assets that it holds for liquidity purposes.
- 5.1.83 G Market access should be assessed under a variety of normal and stressed conditions.
- 5.1.84 G In some circumstances, the disclosure of information about a *firm* may be useful in managing the public perception of its organisation and soundness. A *firm* should consider the role of disclosure in managing the *liquidity risk* to which it is exposed.

#### Contingency funding plans

- 5.1.85 G *PRU 1.2.22R* states that a *firm* must at all times maintain overall financial resources adequate to ensure that there is no significant risk that its liabilities cannot be met as they fall due. *PRU 1.2.35R(2)* states that for the purposes of determining the adequacy of its overall financial resources, a *firm* must estimate the financial resources it would need in each of the circumstances and events considered in carrying out its stress testing and scenario analysis in order to meet its liabilities as they fall due.
- 5.1.86 E (1) A *firm* should have a *contingency funding plan* for taking action to ensure, so far as it can, that, in each of the scenarios analysed under *PRU 1.2.35R(2)*, it would still have sufficient liquid financial resources to meet liabilities as they fall due.
- (2) The *contingency funding plan* should cover what events or circumstances will lead the *firm* to put into action any part of the plan.
- (3) Contravention of (1) or (2) may be relied upon as tending to establish contravention of *PRU 1.2.22R*.
- 5.1.87 G A *firm* should adequately document the *contingency funding plan* referred to in *PRU 5.1.86E*.

- 5.1.88 G The *contingency funding plan* of a *firm* described in *PRU 5.1.4R* should cover the extent to which the actions in *PRU 5.1.86E(1)* include:
- (1) selling, using as *collateral* in secured funding (including repo), or securitising, its assets;
  - (2) otherwise reducing its assets;
  - (3) modifying the structure of its liabilities or increasing its liabilities; and
  - (4) the use of committed facilities.
- 5.1.89 G A *firm's contingency funding plan* should, where relevant, take account of the impact of stressed market conditions on:
- (1) the behaviour of any credit-sensitive liabilities it has; and
  - (2) its ability to securitise assets.
- 5.1.90 G The *contingency funding plan* should contain administrative policies and procedures that will enable the *firm* to manage the plan's implementation effectively, including:
- (1) the responsibilities of senior management;
  - (2) names and contact details of members of the team responsible for implementing the *contingency funding plan*;
  - (3) where, geographically, team members will be assigned;
  - (4) who within the team is responsible for contact with head office (if appropriate), analysts, investors, external auditors, press, significant *customers*, regulators, lawyers and others; and
  - (5) mechanisms that enable senior management and the *governing body* to receive management information that is both relevant and timely.

#### Documentation

- 5.1.91 G *PRU 1.2.37R* states that a *firm* must document its assessment of the adequacy of its liquidity financial resources, how it intends to deal with those risks, and details of the stress tests and scenario analyses carried out and the resulting financial resources estimated to be required. Accordingly, a *firm* should document both its stress testing and scenario analysis (see *PRU 5.1.58G*) and its *contingency funding plan* (see *PRU 5.1.85G*).

## Annex H

### PRU 6

In this Annex, all the text is new and is not underlined.

#### 6.1 Operational Risk: Prudential Systems and Controls

##### Application

6.1.1 G *PRU 6.1* applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

6.1.2 G *PRU 6.1* applies to:

- (1) an *EEA-deposit insurer*; and
  - (2) a *Swiss general insurer*;
- only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

##### Purpose

6.1.3 G This section provides *guidance* on how to interpret *PRU 1.4.18R* and *PRU 1.4.19R(2)* (which relate to the design and documentation of risk management systems) in so far as they relate to the management of operational risk in a *prudential context*. Operational risk has been described by the Basel Committee on Banking Supervision as “the risk of loss, resulting from inadequate or failed internal processes, people and systems, or from external events”. Thus this section covers systems and controls relating to risks concerning any of the *firm*’s operations, whether caused by internal or external matters. However, it does not cover systems and controls as they relate to credit, market, liquidity and insurance risk. Examples of operational risk exposures that the systems and controls covered in this section are meant to address include internal and external fraud; failure to comply with employment law or meet workplace safety standards; damage to physical assets; business disruptions and system failures; and transaction processing failures.

6.1.4 G Operational risk concerns the *FSA* in a *prudential context* because inappropriate systems and controls for the management of operational risk can adversely affect the solvency or business continuity of a *firm*, threatening the *regulatory objectives* of market confidence and consumer protection.

6.1.5 G This section contains *guidance* on how a *firm* should determine, in a *prudential context*, its policy for operational risk management and its processes for the identification, assessment, monitoring and control of operational risk. In addition, *guidance* is provided on record keeping in relation to operational risk.

- 6.1.6 G The *guidance* contained within this section is not designed to be exhaustive. When establishing and maintaining its systems and controls for operational risk, a *firm* should have regard to other parts of the *Handbook* as well as the material that is issued by other industry or regulatory bodies. In particular, a *firm* should read this section in conjunction with SYSC 3A (Operational Risk Systems and Controls) which contains high level *guidance* on the management of people, processes and systems, and external events in relation to operational risk. SYSC 3A also outlines some *guidance* on the areas that are covered by operational risk systems and controls (including the FSA's interpretation of some frequently used risk management terms in relation to operational risk), business continuity management, outsourcing, and the role of insurance in financing operational risk. In addition, a *firm* should read PRU 1.4, which contains the FSA's general policy on prudential systems and controls. PRU 1.4 contains some *rules* and *guidance* on which this section offers additional *guidance*.
- 6.1.7 G *Guidance* on the application of this section to a *firm* that is a member of a *group* is provided in PRU 8.1 (Group Risk Systems and Controls).
- 6.1.8 G Appropriate systems and controls for the management of operational risk will vary with the scale, nature and complexity of a *firm's* activities. Therefore the material in this section is *guidance*. A *firm* should assess the appropriateness of any particular item of *guidance* in the light of the scale, nature and complexity of its activities as well as its obligations as set out in *Principle 3* to organise and control its affairs responsibly and effectively.

#### General Requirements

- 6.1.9 G High level *rules* and *guidance* for prudential systems and controls including those for operational risk are set out in PRU 1.4. In particular:
- (1) PRU 1.4.18R requires a *firm* to take reasonable steps to ensure that the risk management systems put in place to identify, assess, monitor and control operational risk are adequate for that purpose;
  - (2) PRU 1.4.19R(2) requires a *firm* to document its policy for operational risk, including its risk appetite and how it identifies, assesses, monitors and controls that risk; and
  - (3) PRU 1.4.27 R requires a *firm* to take reasonable steps to establish and maintain adequate *internal controls* to enable it to assess and monitor the effectiveness and implementation of its business plan and prudential risk management systems.

#### Operational risk policy

- 6.1.10 G Much of the management of operational risk is about identifying, assessing, monitoring and controlling failures or inadequacies in a *firm's* systems and controls. As such, a *firm* may often find that there is no clear boundary between its risk management systems for operational risk and all its other systems and controls. When drafting its operational risk policy, a *firm* should try to distinguish between its systems and controls for credit, market, liquidity and insurance risk, and its systems and controls for operational risk. Where such a distinction is not possible a *firm* should still try to identify those systems and controls that are used in the management of operational risk, even when they have other purposes as well.
- 6.1.11 G A *firm* should document its policy for managing operational risk. This policy should outline a *firm's* strategy and objectives for operational risk management and the processes that it intends to adopt to achieve these objectives. In complying with *PRU* 1.4.19R(2), the documented operational risk policy of a *firm* should include:
- (1) an analysis of the *firm's* operational risk profile (see the *FSA's* interpretation of this term in *SYSC* 3A.5.1G(3)), including where relevant some consideration of the effects that operational risk may have on the *firm*, including consideration of those operational risks within a *firm* that may have an adverse impact upon the quality of service afforded to its *clients*;
  - (2) the operational risks that the *firm* is prepared to accept and those that it is not prepared to accept, including where relevant some consideration of its appetite or tolerance (see *PRU* 6.1.13G) for specific operational risks;
  - (3) how the *firm* intends to identify, assess, monitor, and control its operational risks, including an overview of the people, processes and systems that are used; and
  - (4) where assessments of the *firm's* risk exposures are used for internal capital allocation purposes, a description of how operational risk is incorporated into this methodology.
- 6.1.12 G A *firm* may also wish to set threshold levels in its operational risk policy for particular types of operational risk (based on its risk appetite or tolerance for risk), which when exceeded trigger a response (such as the allocation of more resources to control the risk or a reappraisal of business plans).

- 6.1.13 G Given its association with a willingness to take risk, a *firm* may wish to replace the term appetite for tolerance when drafting its operational risk policy. Tolerance describes the types and degree of operational risk that a *firm* is prepared to incur (based on factors such as the adequacy of its resources and the nature of its operating environment). Tolerance may be described in terms of the maximum budgeted (that is, expected) costs of an operational risk that a *firm* is prepared to bear, or by reference to risk indicators such as the cost or number of system failures, available spare capacity and the number of failed trades.
- 6.1.14 G The term risk assessment can be used to represent both the qualitative and quantitative evaluation or measurement of operational exposures.

#### Risk identification

- 6.1.15 G In order to understand its operational risk profile, a *firm* should identify the types of operational risk that it is exposed to as far as reasonably possible. This might include, but is not limited to, consideration of:
- (1) the nature of a *firm's* customers, products and activities, including sources of business, distribution mechanisms, and the complexity and volumes of transactions;
  - (2) the design, implementation, and operation of the processes and systems used in the end-to-end operating cycle for a *firm's* products and activities;
  - (3) the risk culture and human resource management practices at a *firm*; and
  - (4) the business operating environment, including political, legal, socio-demographic, technological, and economic factors as well as the competitive environment and market structure.
- 6.1.16 G A *firm* should recognise that it may face significant operational exposures from a product or activity that may not be material to its business strategy. A *firm* should consider the appropriate level of detail at which risk identification is to take place, and may wish to manage the operational risks that it faces in risk categories that are appropriate to its organisational and legal structures.
- 6.1.17 G The *FSA's* interpretation of the term operational exposure is provided in SYSC 3A.5.1G(2).

#### Risk assessment

- 6.1.18 G The *FSA* recognises that risk management systems for operational risk are still developing, and that it may be neither feasible nor appropriate to measure certain types of operational risk in a quantitative way. A *firm* may wish to take a qualitative approach to the assessment of its operational risks using, for example, relative estimates (such as high, medium, low) to understand its exposure to them.



- 6.1.19 G In order to understand the effects of its operational exposures a *firm* should continually assess its operational risks. This might include, but is not limited to, consideration of:
- (1) actual operational losses that have occurred within a *firm*, or events that could have resulted in significant operational losses, but were avoided (for example, the waiving of financial penalties by a third party as a gesture of goodwill or where by chance the *firm* realised profits);
  - (2) internal assessment of risks inherent in its operations and the effectiveness of controls implemented to reduce these risks (through activities such as self-assessment or stress testing and scenario analysis);
  - (3) other risk indicators, such as *customer* complaints, processing volumes, *employee* turnover, large numbers of reconciling items, process or system failures, fragmented systems, systems subject to a high degree of manual intervention and transactions processed outside a *firm*'s mainstream systems;
  - (4) reported external (peer) operational losses and exposures; and
  - (5) changes in its business operating environment.
- 6.1.20 G When assessing its operational risks, a *firm* may be able to differentiate between expected and unexpected operational losses. A *firm* should consider whether it is appropriate to adopt a more quantitative approach to the assessment of its expected operational losses, for example by defining tolerance, setting thresholds, and measuring and monitoring operational losses and exposures. In contrast, a *firm* may wish to take a more qualitative approach to assessing its unexpected losses.
- 6.1.21 G Although a *firm* may currently be unable to assess certain operational risks with a high degree of accuracy or consistency, it should, according to the nature, scale and complexity of its business, consider the use of more sophisticated qualitative and quantitative techniques as they become available.

#### Risk monitoring

- 6.1.22 G In monitoring its operational risks, a *firm* should:
- (1) as appropriate, regularly report to the relevant level of management its operational exposures, loss experience (including if possible cumulative losses), and authorised deviations from the *firm*'s operational risk policy;
  - (2) engage in exception-based escalation to management of:

- (a) unauthorised deviations from the *firm's* operational risk policy;
- (b) likely or actual breaches in predefined thresholds for operational exposures and losses, where set; and
- (c) significant increases in the *firm's* exposure to operational risk or alterations to its operational risk profile.

#### Risk control

6.1.23 G A *firm* should control its operational risks, as appropriate, through activities for the avoidance, transfer, prevention or reduction of the likelihood of occurrence or potential impact of an operational exposure. This might include, but is not limited to, consideration of:

- (1) adjusting a *firm's* risk culture and creating appropriate incentives to facilitate the implementation of its risk control strategy (see SYSC 3A.6 People);
- (2) adapting internal processes and systems (see SYSC 3A.7 Processes and systems);
- (3) transferring or changing the operational exposure through mechanisms such as *outsourcing* (see SYSC 3A.9 Outsourcing) and insurance (see SYSC 3A.10 Insurance);
- (4) the active acceptance of a given operational risk within the *firm's* stated risk appetite or tolerance; and
- (5) providing for expected losses, and maintaining adequate financial resources against unexpected losses that may be encountered in the normal course of a *firm's* business activities.

#### Record keeping

6.1.24 G The FSA's high level *rules* and *guidance* for record keeping are outlined in SYSC 3.2.20R (Records). Additional *rules* and *guidance* in relation to the *prudential context* are set out in PRU 1.4.51G to PRU 1.4.64G (Record keeping). In complying with these *rules* and all associated *guidance*, a *firm* should retain an appropriate record of its operational risk management activities. This may, for example, include records of:

- (1) the results of risk identification, measurement, and monitoring activities;
- (2) actions taken to control identified risks;
- (3) where relevant, any exposure thresholds that have been set for identified operational risks;

- (4) an assessment of the effectiveness of the risk control tools that are used; and
- (5) actual exposures against stated risk appetite or tolerance.

## Annex I

### PRU 7

In this Annex, all the text is new and is not underlined.

#### 7.1 Insurance risk systems and controls

##### Application

7.1.1 G *PRU 7.1* applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

7.1.2 G *PRU 7.1* applies to:

- (1) an *EEA-deposit insurer*; and
- (2) a *Swiss general insurer*;  
only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

##### Purpose

7.1.3 G This section provides *guidance* on how to interpret *PRU 1.4* (Prudential risk management and associated systems and controls) in so far as it relates to the management of insurance risk. Insurance risk refers to fluctuations in the timing, frequency and severity of insured events, relative to the expectations of the *firm* at the time of underwriting. Insurance risk can also refer to fluctuations in the timing and amount of *claim* settlements. For *general insurance business* some specific examples of insurance risk include variations in the amount or frequency of *claims* or the unexpected occurrence of multiple *claims* arising from a single cause. For *long-term insurance business* examples include variations in the mortality and persistency rates of *policyholders*, or the possibility that guarantees could acquire a value that adversely affects the finances of a *firm* and its ability to treat its *policyholders* fairly consistent with the *firm's* obligations under *Principle 6*. More generally, insurance risk includes the potential for expense overruns relative to pricing or provisioning assumptions.

7.1.4 G Insurance risk concerns the *FSA* in a *prudential context* because inadequate systems and controls for its management can create a threat to the *regulatory objectives* of market confidence and consumer protection. Inadequately managed insurance risk may result in:

- (1) the inability of a *firm* to meet its contractual insurance liabilities as they fall due; and

- (2) the inability of a *firm* to treat its *policyholders* fairly consistent with the *firm's* obligations under *Principle 6* (for example, in relation to bonus payments).

- 7.1.5 G *Guidance* on the application of this section to a *firm* that is a member of a *group* is provided in *PRU 8.1* (Group risk systems and controls).
- 7.1.6 G The *guidance* contained within this section should be read in conjunction with *SYSC* and *PRU 1.4*.
- 7.1.7 G Appropriate systems and controls for the management of insurance risk will vary with the scale, nature and complexity of a *firm's* activities. Therefore, the material in this section is *guidance*. A *firm* should assess the appropriateness of any particular item of *guidance* in the light of the scale, nature and complexity of its activities as well as its obligations, as set out in *Principle 3*, to organise and control its affairs responsibly and effectively.

#### General requirements

- 7.1.8 G High level *rules* and *guidance* for prudential systems and controls for insurance risk are set out in *PRU 1.4*. In particular:
- (1) *PRU 1.4.18R* requires a *firm* to take reasonable steps to establish and maintain a business plan and appropriate risk management systems;
  - (2) *PRU 1.4.19R(2)* requires a *firm* to document its policy for insurance risk, including its risk appetite and how it identifies, measures, monitors and controls that risk; and
  - (3) *PRU 1.4.27R* requires a *firm* to take reasonable steps to establish and maintain adequate *internal controls* to enable it to assess and monitor the effectiveness and implementation of its business plan and prudential risk management systems.

#### Insurance risk policy

- 7.1.9 G A *firm's* insurance risk policy should outline its objectives in carrying out *insurance business*, its appetite for insurance risk and its policies for identifying, measuring, monitoring and controlling insurance risk. The insurance risk policy should cover any activities that are associated with the creation or management of insurance risk. For example, underwriting, *claims* management and settlement, assessing *technical provisions* in the balance sheet, risk mitigation and risk transfer, record keeping and management reporting. Specific matters that should normally be in a *firm's* insurance risk policy include:
- (1) a statement of the *firm's* willingness and capacity to accept insurance risk;
  - (2) the classes and characteristics of *insurance business* that the *firm* is prepared to accept;

- (3) the underwriting criteria that the *firm* intends to adopt, including how these can influence its rating and pricing decisions;
- (4) its approach to limiting significant aggregations of insurance risk, for example, by setting limits on the amount of business that can be underwritten in one region or with one *policyholder*;
- (5) where relevant, the *firm's* approach to pricing *long-term insurance contracts*, including the determination of the appropriate level of any reviewable *premiums*;
- (6) the *firm's* policy for identifying, monitoring and managing risk when it has delegated underwriting authority to another party (additional *guidance* on the management of *outsourcing* arrangements is provided in SYSC 3A.9);
- (7) the *firm's* approach to managing its expense levels, including acquisition costs, recurring costs, and one-off costs, taking account of the margins available in both the prices for products and in the *technical provisions* in the balance sheet;
- (8) the *firm's* approach to the exercise of any discretion (e.g. on charges or the level of benefits payable) that is available in its *long-term insurance contracts*, in the context also of the legal and regulatory constraints existing on the application of this discretion;
- (9) the *firm's* approach to the inclusion of options within new *long-term insurance contracts* and to the possible exercise by *policyholders* of options on existing contracts;
- (10) the *firm's* approach to managing persistency risk;
- (11) the *firm's* approach to managing risks arising from timing differences in taxation or from changes in tax laws;
- (12) the *firm's* approach to the use of *reinsurance* or the use of some other means of risk transfer;
- (13) how the *firm* intends to assess the effectiveness of its risk transfer arrangements and manage the residual or transformed risks (for example, how it intends to handle disputes over contract wordings, potential payout delays and *counterparty* performance risks);
- (14) a summary of the data and information to be collected and reported on underwriting, *claims* and risk control (including internal accounting records), management reporting requirements and external data for risk assessment purposes;
- (15) the risk measurement and analysis techniques to be used for setting underwriting *premiums*, *technical provisions* in the balance sheet, and assessing capital requirements; and

- (16) the *firm's* approach to stress testing and scenario analysis, as required by *PRU 1.2* (Adequacy of financial resources), including the methods adopted, any assumptions made and the use that is to be made of the results.

7.1.10 G Further, more detailed, *guidance* is given in *PRU 7.1.11G* to *PRU 7.1.37G* on the identification, measurement, monitoring and control (including the use of *reinsurance* and other forms of risk transfer) of insurance risk. A *firm* should consider what additional material to that set out above should be included in its insurance risk policy on each of these for its various activities.

#### Risk identification

7.1.11 G A *firm* should seek to identify the causes of fluctuations in the occurrence, amount and timing of its insurance liabilities. A *firm* should also seek to identify aggregations of risk that may give rise to large single or multiple *claims*.

7.1.12 G The identification of insurance risk should normally include:

- (1) in connection with the *firm's* business plan:
  - (a) processes for identifying the types of insurance risks that may be associated with a new product and for comparing the risk types that are present in different classes of business (in order to identify possible aggregations in particular insurance risks); and
  - (b) processes for identifying business environment changes (for example landmark legal rulings) and for collecting internal and external data to test and modify business plans;
- (2) at the point of sale, processes for identifying the underwriting risks associated with a particular *policyholder* or a group of *policyholders* (for example, processes for identifying potential claims for mis-selling and for collecting information on the *claims* histories of *policyholders*, including whether they have made any potentially false or inaccurate *claims*, to identify possible adverse selection or moral hazard problems);
- (3) after the point of sale, processes for identifying potential and emerging *claims* for the purposes of *claims* management and *claims* provisioning; this could include:
  - (a) identifying possible judicial rulings;
  - (b) keeping up to date with developments in market practice; and

- (c) collecting information on industry wide initiatives and settlements.
- 7.1.13 G A *firm* should also identify potential pricing risks, where the liabilities or costs arising from the sale of a product may not be as expected.
- Risk measurement
- 7.1.14 G A *firm* should have in place appropriate systems for collecting the data it needs to measure insurance risk. At a minimum this data should be capable of allowing a *firm* to evaluate the types of *claims* experienced, *claims* frequency and severity, expense levels, persistency levels and, where relevant, potential changes in the value of guarantees and options in *long-term insurance contracts*.
- 7.1.15 G A *firm* should ensure that the data it collects and the measurement methodologies that it uses are sufficient to enable it to evaluate, as appropriate:
- (1) its exposure to insurance risk at all relevant levels, for example, by contract, *policyholder*, product line or insurance class;
  - (2) its exposure to insurance risk across different geographical areas and time horizons;
  - (3) its total, firm-wide, exposure to insurance risk and any other risks that may arise out of the *contracts of insurance* that it issues;
  - (4) how changes in the volume of business (for example via changes in *premium* levels or the number of new contracts that are underwritten) may influence its exposure to insurance risk;
  - (5) how changes in *policy* terms may influence its exposure to insurance risk; and
  - (6) the effects of specific loss scenarios on the insurance liabilities of the *firm*.
- 7.1.16 G A *firm* should hold data in a manner that allows for it to be used in a flexible way. For example, data should be sufficiently detailed and disaggregated so that contract details may be aggregated in different combinations to assess different risks.
- 7.1.17 G A *firm* should be able to justify its choice of measurement methodologies. This justification should normally be documented.
- 7.1.18 G A *firm* should periodically review the appropriateness of the measurement methodologies that it uses. This could, for example, include back testing (that is, by comparing actual versus expected results) and updating for changes in market practice.



- 7.1.19 G A *firm* should ensure that it has access to the necessary skills and resources that it needs to measure insurance risk using its chosen methodology.
- 7.1.20 G When measuring its insurance risks, a *firm* should consider how emerging experience could be used to update its underwriting process, in particular in relation to contract terms and pricing and also its assessment of the *technical provisions* in the balance sheet.
- 7.1.21 G A *firm* should have the capability to measure its exposure to insurance risk on a regular basis. In deciding on the frequency of measurement, a *firm* should consider:
- (1) the time it takes to acquire and process all necessary data;
  - (2) the speed at which exposures could change; and
  - (3) that it may need to measure its exposure to certain types of insurance risk on a daily basis (for example, weather catastrophes).

#### Risk monitoring

- 7.1.22 G A *firm* should provide regular and timely information on its insurance risks to the appropriate level of management. This could include providing reports on the following:
- (1) a statement of the *firm's* profits or losses for each class of business that it underwrites (with an associated analysis of how these have arisen for any *long-term insurance contracts*), including a variance analysis detailing any deviations from budget or changes in the key performance indicators that are used to assess the success of its business plan for insurance;
  - (2) the *firm's* exposure to insurance risk at all relevant levels (see *PRU 7.1.15G(1)*), as well as across different geographical areas and time zones (see *PRU 7.1.15G(2)*), also senior management should be kept informed of the *firm's* total exposure to insurance risk (see *PRU 7.1.15G(3)*);
  - (3) an analysis of any internal or external trends that could influence the *firm's* exposure to insurance risk in the future (e.g. new weather patterns, socio-demographic changes, expense overruns etc);
  - (4) any new or emerging developments in *claims* experience (e.g. changes in the type of *claims*, average *claim* amounts or the number of similar *claims*);
  - (5) the results of any stress testing or scenario analyses;
  - (6) the amount and details of new business written and the amount of business that has lapsed or been cancelled;
  - (7) identified fraudulent *claims*;

- (8) a watch list, detailing, for example, material/catastrophic events that could give rise to significant numbers of new *claims* or very large *claims*, contested *claims*, client complaints, legal and other developments;
  - (9) the performance of any *reinsurance*/risk transfer arrangements; and
  - (10) progress reports on matters that have previously been referred under escalation procedures (see *PRU 7.1.23G*).
- 7.1.23 G A *firm* should establish and maintain procedures for the escalation of appropriate matters to the relevant level of management. Such matters may include:
- (1) any significant new exposures to insurance risk, including for example any landmark rulings in the courts;
  - (2) a significant increase in the size or number of *claims*;
  - (3) any breaches of the limits set out in *PRU 7.1.27G* and *PRU 7.1.28G*, in particular senior management should be informed where any maximum limits have been breached (see *PRU 7.1.29G*); and
  - (4) any unauthorised deviations from its insurance risk policy (including those by a *broker*, *appointed representative* or other delegated authority).
- 7.1.24 G A *firm* should regularly monitor the effectiveness of its analysis techniques for setting provisions for *claims* on *general insurance contracts*.
- 7.1.25 G A *firm* should have appropriate procedures in place to allow managers to monitor the application (and hence the effect) of its *reinsurance* programme. This would include, for a general *insurer*, procedures for monitoring how its *reinsurance* programme affects the gross provisions that it makes for outstanding *claims* (including *claims* that are incurred but not reported).
- Risk control
- 7.1.26 G A *firm* should take appropriate action to ensure that it is not exposed to insurance risk in excess of its risk appetite. In so doing, the *firm* should be both reactive, responding to actual increases in exposure, and proactive, responding to potential future increases. Being proactive should involve close co-ordination between the processes of risk control, risk identification and risk measurement, as potential future exposures need to be identified and understood before effective action can be taken to control them.
- 7.1.27 G A *firm* should consider setting limits for its exposure to insurance risk, which trigger action to be taken to control exposure. Periodically these limits should be amended in the light of new information (e.g. on the expected number or size of *claims*). For example, limits could be set for:

- (1) the *firm's* aggregate exposure to a single source of insurance risk or for events that may be the result of a number of different sources;
  - (2) the *firm's* exposure to specific geographic areas or any other groupings of risks whose outcomes may be positively correlated;
  - (3) the number of fraudulent *claims*;
  - (4) the number of very large *claims* that could arise;
  - (5) the number of unauthorised deviations from its insurance risk policy;
  - (6) the amount of insurance risk than can be transferred to a particular *reinsurer*;
  - (7) the level of expenses incurred in respect of each relevant business area; and
  - (8) the level of persistency by product line or distribution channel.
- 7.1.28 G A *firm* should also consider setting individual underwriting limits for all *employees* and agents that have the authority to underwrite insurance risk. This could include both monetary limits and limits on the types of risk that they can underwrite. Where individual underwriting limits are set, the *firm* should ensure that they are adhered to.
- 7.1.29 G In addition to setting some 'normal' limits for insurance risk, a *firm* should consider setting some maximum limits, beyond which immediate, emergency action should be taken. These maximum limits could be determined through stress testing and scenario analysis.
- 7.1.30 G A *firm* should pay close attention to the wording of its *policy* documentation to ensure that these wordings do not expose it to more, or higher, *claims* than it is expecting. In so doing, the *firm* should consider:
- (1) whether it has adequate in-house legal resources;
  - (2) the need for periodic independent legal review of *policy* documentation;
  - (3) the use of standardised documentation and referral procedures for variation of terms;
  - (4) reviewing the documentation used by other insurance companies;
  - (5) revising documentation for new *policies* in the light of past experience; and
  - (6) the operation of law in the jurisdiction of the *policyholder*.

- 7.1.31 G A *firm* should ensure that it has appropriate systems and controls for assessing the validity of *claims*. This could involve consideration of the evidence that will be required from *policyholders* and how this evidence is to be tested as well as procedures to determine when experts such as loss adjusters, lawyers or accountants should be used.
- 7.1.32 G Particular care should be taken to ensure that a *firm* has appropriate systems and controls to deal with large *claims* or large groups of *claims* that could significantly deplete its financial resources. This should include systems to ensure that senior management (that is, the *governing body* and relevant *senior managers*) is involved in the processing of such *claims* from the outset.
- 7.1.33 G A *firm* should consider how it intends to use *reinsurance* or some other form of insurance risk transfer agreement to help to control its exposure to insurance risk. Additional *guidance* on the use of *reinsurance*/risk transfer is provided below.

#### Reinsurance and other forms of risk transfer

- 7.1.34 G Before entering into or significantly changing a *reinsurance* agreement, or any other form of insurance risk transfer agreement, a *firm* should:
- (1) analyse how the proposed *reinsurance*/risk transfer agreement will affect its exposure to insurance risk, its underwriting strategy and its ability to meet its regulatory obligations;
  - (2) ensure there are adequate legal checking procedures in respect of the draft agreement;
  - (3) conduct an appropriate due diligence of the *reinsurer's* financial stability (that is, solvency) and expertise; and
  - (4) understand the nature and limits of the agreement (particular attention should be given to the wording of contracts to ensure that all of the required risks are covered, that the level of available cover is appropriate, and that all the terms, conditions and warranties are unambiguous and understood).
- 7.1.35 G In managing its *reinsurance* agreements, or any other form of insurance risk transfer agreement, a *firm* should have in place appropriate systems that allow it to maintain its desired level of cover. This could involve systems for:
- (1) monitoring the risks that are covered (that is, the scope of cover) by these agreements and the level of available cover;
  - (2) keeping underwriting staff informed of any changes in the scope or level of cover;
  - (3) properly co-ordinating all *reinsurance*/risk transfer activities so that, in aggregate, the desired level and scope of cover is maintained;

- (4) ensuring that the *firm* does not become overly reliant on any one *reinsurer* or other risk transfer provider;
  - (5) conducting regular stress testing and scenario analysis to assess the resilience of its *reinsurance* and risk transfer programmes to catastrophic events that may give rise to large and or numerous *claims*.
- 7.1.36 G In making a claim on a *reinsurance* contract (that is, its *reinsurance* recoveries) or some other risk transfer contract a *firm* should ensure:
- (1) that it is able to identify and recover any money that it is due in a timely manner; and
  - (2) that it makes adequate financial provision for the risk that it is unable to recover any money that it expected to be due, as a result of either a dispute with or a default by the *reinsurer*/risk transfer provider. Additional *guidance* on credit risk in *reinsurance*/risk transfer contracts is provided in *PRU* 3.2 (Credit risk in insurance).
- 7.1.37 G Where the planned level or scope of cover from a *reinsurance*/risk transfer contract is not obtained, a *firm* should consider revising its underwriting strategy.

#### Record keeping

- 7.1.38 G The *FSA*'s high level *rules* and *guidance* for record keeping are outlined in *SYSC* 3.2.20R (Records). Additional *rules* and *guidance* in relation to the *prudential context* are set out in *PRU* 1.4.51G to *PRU* 1.4.64G. In complying with these *rules* and *guidance*, a *firm* should retain an appropriate record of its insurance risk management activities. This may, for example, include records of:
- (1) each new risk that is underwritten (noting that these records may be held by agents or cedants, rather than directly by the *firm* provided that the *firm* has adequate access to those records);
  - (2) any material aggregation of exposure to risk from a single source, or of the same kind or to the same potential catastrophe or event;
  - (3) each notified *claim* including the amounts notified and paid, precautionary notices and any re-opened *claims*;
  - (4) *policy* and contractual documents and any relevant representations made to *policyholders*;
  - (5) other events or circumstances relevant to determining the risks and commitments that arise out of *contracts of insurance* (including discretionary benefits and charges under any *long-term insurance contracts*);

- (6) the formal wordings of *reinsurance* contracts; and
- (7) any other relevant information on the *firm's reinsurance* or other risk-transfer arrangements, including the extent to which they:
  - (a) have been exhausted by recoveries on paid *claims*; and
  - (b) will be exhausted by recoveries on reported *claims* and, to the extent known, on incurred but not reported *claims*.

7.1.39 G A *firm* should retain its underwriting and *claims* histories for as long as they may be needed to inform pricing or provisioning decisions.

## 7.2 Capital resources requirements and technical provisions for insurance business

### Application

- 7.2.1 R *PRU 7.2* applies to an *insurer* unless it is:
- (1) a *non-directive friendly society*; or
  - (2) an *incoming EEA firm*; or
  - (3) an *incoming Treaty firm*.
- 7.2.2 R (1) This section applies to a *firm* in relation to the whole of its business, except where a particular provision provides for a narrower scope.
- (2) Where a *firm* carries on both *long-term insurance business* and *general insurance business*, this section applies separately to each type of business.
- 7.2.3 R For a *non-EEA direct insurer* with a *branch* in the *United Kingdom*, the part of this section headed “Capital requirements for insurers” (*PRU 7.2.43G* to *PRU 7.2.91R*) applies to its world-wide activities, whilst the parts of this section headed “Establishing technical provisions” (*PRU 7.2.12R* to *PRU 7.2.19G*), “Assets of a value sufficient to cover technical provisions” (*PRU 7.2.20R* to *PRU 7.2.29G*), “Matching of assets and liabilities” (*PRU 7.2.34R* to *PRU 7.2.40G*) and “Premiums for new business” (*PRU 7.2.41R* to *PRU 7.2.42G*) apply in respect of its activities carried on from a *branch* in the *United Kingdom*. The part of this section headed “Localisation” (*PRU 7.2.30R* to *PRU 7.2.33R*) does not apply (see *PRU 7.6* (Internal contagion risk)).
- 7.2.4 R For an *EEA-deposit insurer* or a *Swiss general insurer*, the parts of this section headed “Establishing technical provisions” (*PRU 7.2.12R* to *PRU 7.2.19G*), “Assets of a value sufficient to cover technical provisions” (*PRU 7.2.20R* to *PRU 7.2.29G*), “Matching of assets and liabilities” (*PRU 7.2.34R* to *PRU 7.2.40G*) and “Premiums for new business” (*PRU 7.2.41R* to *PRU 7.2.42G*) apply in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*. The parts of this section headed “Capital requirements for insurers” (*PRU 7.2.43G* to *PRU 7.2.91R*) and “Localisation” (*PRU 7.2.30R* to *PRU 7.2.33R*) do not apply.
- 7.2.5 R For an *UK-deposit insurer*, the part of this section headed “Capital requirements for insurers” (*PRU 7.2.43G* to *PRU 7.2.91R*) applies to its world-wide activities, whilst the parts of this section headed “Establishing technical provisions” (*PRU 7.2.12R* to *PRU 7.2.19G*), “Assets of a value sufficient to cover technical provisions” (*PRU 7.2.20R* to *PRU 7.2.29G*), “Matching of assets and liabilities” (*PRU 7.2.34R* to *PRU 7.2.40G*) and “Premiums for new business” (*PRU 7.2.41R* to *PRU 7.2.42G*) apply in respect of the activities of the *firm* carried on from *branches* in *EEA States*. The part of this section headed “Localisation” (*PRU 7.2.30R* to *PRU 7.2.33R*) does not apply (see *PRU 7.6* (Internal contagion risk)).

- 7.2.6 G This section may apply in cases where a *firm* has its head office in another *EEA State* but is neither an *incoming EEA firm* nor an *incoming Treaty firm*; this could arise in the case of a *non-directive mutual* or a *pure reinsurer*.

#### Purpose

- 7.2.7 G *PRU 7.2* has the aim of reducing the risk that a *firm* may fail to meet its liabilities to its *policyholders* as a result of insurance risk, that is, the risk that arises from the inherent uncertainties as to the occurrence, amount and timing of insurance liabilities.
- 7.2.8 G This section requires that the *technical provisions* that *firms* establish are adequate to meet their liabilities to *policyholders* under *contracts of insurance*. It also requires that *firms* hold assets of a value sufficient to cover their liabilities, including *technical provisions*, and that there is suitable matching of assets and liabilities. *Technical provisions* are the on-balance sheet provisions made by a *firm* in respect of liabilities arising under or in connection with *contracts of insurance*. There are different *rules* and *guidance* applicable to the calculation of *technical provisions* for *general insurance business* and for *long-term insurance business*.
- 7.2.9 G This section implements requirements of the *Insurance Directives* for both *general insurance business* and *long-term insurance business* with regard to the *technical provisions*. The relevant articles of the Directives include:
- (1) article 15 of the *First Non-Life Directive*, as substituted by article 17 of the *Third Non-Life Directive*; and
  - (2) article 20 of the *Consolidated Life Directive* (this Directive consolidates the provisions of the previous *First, Second* and *Third Life Directives*).
- 7.2.10 G This section also sets out detailed *rules* and *guidance* on the calculation of the following elements of a *firm's capital resources requirement (CRR)* (see *PRU 2.1*):
- (1) the *general insurance capital requirement*; and
  - (2) the *long-term insurance capital requirement*.
- 7.2.11 G These requirements are dealt with in the part of this section headed “Capital requirements for insurers” (see *PRU 7.2.43G* to *PRU 7.2.91R*). That part of this section also contains *rules* about the calculation of the *insurance-related capital requirement*, which forms part of the *enhanced capital requirement* for *firms* carrying on *general insurance business*. The *asset-related capital requirement* for *firms* carrying on *general insurance business* is set out in *PRU 3.3*.

#### Establishing technical provisions

- 7.2.12 R For *general insurance business*, a *firm* must establish adequate technical provisions:
- (1) in accordance with the *rules* in *PRU 7.5* for *equalisation provisions*; and



- (2) otherwise, in accordance with *PRU 1.3.5R*.
- 7.2.13 G For *general insurance business*, the *technical provisions* include outstanding *claims provisions*, *unearned premiums provisions*, unexpired risk provisions and *equalisation provisions*. These provisions take into account the expected ultimate cost of *claims*, including those not yet incurred, related expenses and include an allowance for smoothing *claims* (the *equalisation provision*).
- 7.2.14 G *Discounting* (that is discounting for the time value of money) *general insurance business technical provisions* may be carried out only in limited circumstances and on a prudent basis (see *PRU 2.2.80R* and *PRU 2.2.81R* and paragraph 48 of the *insurance accounts rules*). The fact that the expected liabilities are generally not *discounted* helps to protect against risk from inherent uncertainty in the timing, but not necessarily the amount, of *claims*.
- 7.2.15 G For some categories of *general insurance business*, *equalisation provisions* are required. These ensure that a *firm* retains additional assets to provide some extra protection against uncertainty as to the amount of *claims*. *Equalisation provisions* are particularly suitable for volatile business, where *claims* in any future year may be subject to significant adverse deviation from recent or average expected *claims* experience, or where trends in *claims* experience may be subject to change. Such volatile *claims* experience arises in a number of types of business, for example, property, marine and aviation, nuclear, certain *non-proportional reinsurance treaty* business, and credit insurance. The *equalisation provisions* help to equalise fluctuations in loss ratios in future years (see *PRU 7.5 (Equalisation provisions)*).
- 7.2.16 R For *long-term insurance business*, a *firm* must establish adequate technical provisions:
- (1) for its *long-term insurance contracts*, in accordance with the *rules* and *guidance* in *PRU 7.3* relating to *mathematical reserves*, and with due regard to generally accepted actuarial practice; and
  - (2) for *long-term insurance liabilities* which have fallen due, in accordance with *PRU 1.3.5R*.
- 7.2.17 G *Rules* and *guidance* for calculating *mathematical reserves* are set out in *PRU 7.3*. *Firms* are advised by the *actuarial function* (see *SUP 4*) on the methods and assumptions to be used in calculating the *mathematical reserves*. The standards and guidance issued by the Faculty and Institute of Actuaries to assist actuaries appointed to the *actuarial function* are important sources of evidence as to generally accepted actuarial practice, as referred to in *PRU 7.2.16R(1)*.
- 7.2.18 G For *long-term insurance business*, the *technical provisions* include the *mathematical reserves*. These are actuarial estimates of a *firm's* liabilities in respect of future benefits due to *policyholders*, including bonuses already declared. The *mathematical reserves* may be reduced by the actuarial value of that component of future *premiums* attributable to meeting future liabilities (see *PRU 7.3 (Mathematical reserves)*).

- 7.2.19 G For *long-term insurance business*, the *mathematical reserves* are typically valued on a discounted basis but include valuation margins intended to provide protection against adverse deviations in experience (see *PRU 7.3*).

Assets of a value sufficient to cover technical provisions

- 7.2.20 R A *firm* must hold *admissible assets* of a value at least equal to the amount of the *technical provisions* that it is required to establish under *PRU 7.2.12R* and *PRU 7.2.16R* (excluding *technical provisions* for *property-linked* and *index-linked benefits* and the assets held to cover them under *PRU 4.2.57R* and *PRU 4.2.58R*).
- 7.2.21 R A *composite firm* must ensure that:
- (1) its separately identified *long-term insurance assets* have a value at least equal to the amount of:
    - (a) its *technical provisions* for *long-term insurance liabilities*; and
    - (b) any other liabilities connected with *long-term insurance business*; and
  - (2) that it has other *admissible assets* of a value at least equal to the amount of its *technical provisions* for *general insurance liabilities*.
- 7.2.22 G *PRU 7.6* (Internal-contagion risk) sets out the *rules* and *guidance* on identifying and holding in a separate fund *long-term insurance assets*.
- 7.2.23 G When valuing assets for the purposes of *PRU 7.2.20R* and *PRU 7.2.21R*, a *firm* should bear in mind:
- (1) that the *technical provisions* should be covered by *admissible assets* (see *PRU 2 Ann 1R*); and
  - (2) the market and *counterparty* limits set out in *PRU 3.2* (Credit risk in *insurance*). *PRU 3.2* requires that a *firm* restrict to prudent levels its exposure to *reinsurer* and other *counterparties*, and, in particular, that for the purpose of its balance sheet, a *firm* must not take into account any exposure which exceeds the large exposure limits.
- 7.2.24 G *Rules* and *guidance* on the valuation of assets are set out in *PRU 1.3* (Valuation), including the treatment of *shares* in, and debts due from, *related undertakings* in *PRU 1.3.31R* to *PRU 1.3.42G*. *PRU 4.2* (Market risk in insurance) addresses *market risk* and sets out the matching requirements for linked assets and liabilities. *PRU 4.2* also sets out *rules* and *guidance* on the matching by currency of assets and liabilities, to reduce a *firm's* exposure to currency *market risk*.
- 7.2.25 R For the purpose of determining the value of assets available to meet *long-term insurance liabilities* in accordance with *PRU 7.2.20R*, *PRU 7.2.21R*, *PRU 7.2.27R* and *PRU 7.2.28R*, no value is to be attributed to debts and *claims* other than in respect of:
- (1) amounts that have already fallen due;

- (2) tax recoveries and claims against *compensation funds* to the extent not already offset in *mathematical reserves*.
- 7.2.26 G Certain debts and *claims* are excluded from *PRU 7.2.20R*, *PRU 7.2.21R*, *PRU 7.2.27R* and *PRU 7.2.28R* to avoid double-counting. The *rules and guidance* in *PRU 7.3 (Mathematical reserves)* set out how a *firm* may offset debts and *claims* against liabilities in calculating the *mathematical reserves* required for *long-term insurance business*. Tax recoveries and claims against *compensation funds* in *PRU 7.2.25R(2)* are set out in the list of *admissible assets* (see *PRU 2 Ann 1R*).
- 7.2.27 R A *firm* carrying on *long-term insurance business* must ensure that it has *admissible assets* in each of its *with-profits funds* of a value sufficient to cover the *technical provisions* in respect of all the business written in that *with-profits fund*.
- 7.2.28 R In addition to complying with *PRU 7.2.27R*, a *realistic basis life firm* must also ensure that the *realistic value of assets* for each of its *with-profits funds* is at least equal to the *realistic value of liabilities* of that fund.
- 7.2.29 G *PRU 7.2.27R* and *PRU 7.2.28R* support the funding of *policyholder* benefits by requiring *firms* to maintain *admissible assets* in *with-profits funds* to cover the *technical provisions* relating to all the business in that fund and, in the case of a *realistic basis life firm*, realistic assets to cover the realistic liabilities of the *with-profits insurance contracts* written in the fund.

Localisation (UK firms only)

- 7.2.30 R (1) Subject to (2), a *UK firm* must hold *admissible assets* held pursuant to *PRU 4.2.53R*:
- (a) (where the *admissible assets* cover *technical provisions* in pounds sterling), in any *EEA State*; and
- (b) (where the *admissible assets* cover *technical provisions* in any currency other than pounds sterling), in any *EEA State* or in the country of that currency.
- (2) In the case of a *community co-insurance operation* and a *relevant insurer*, the *admissible assets* covering *technical provisions* must be held in any *EEA State*.
- 7.2.31 G *PRU 7.6 (Internal contagion risk)* sets out the *rules and guidance* on localisation for *firms* other than *UK firms*.
- 7.2.32 R *PRU 7.2.30R* does not apply to:
- (1) a *pure reinsurer*; or
- (2) debts owed by *reinsurers*; or
- (3) *insurance business* carried on by a *UK firm* outside the *EEA States*; or

- (4) *general insurance business class* groups 3 and 4 in IPRU(Ins), Annex 11.2, Part II.

7.2.33 R For the purposes of *PRU 7.2.30R*:

- (1) a tangible asset is to be treated as held in the country or territory where it is situated;
- (2) an *admissible asset* consisting of a claim against a debtor is to be treated as held in any country or territory where it can be enforced by legal action;
- (3) a *listed security* is to be treated as held in any country or territory where there is a *regulated market* on which the *security* is dealt; and
- (4) a *security* which is not a *listed security* is to be treated as held in the country or territory in which the *issuer* has its head office.

#### Matching of assets and liabilities

7.2.34 R (1) Subject to (4), the assets held by a *firm* to cover its *technical provisions* (see *PRU 7.2.20R* and *PRU 7.2.21R*) must:

- (a) have characteristics of safety, yield and marketability which are appropriate to the type of business carried on by the *firm*;
- (b) be diversified and adequately spread; and
- (c) comply with (2).
- (2) The assets referred to in (1) must, in addition to meeting the criteria set out in (1)(a) and (b), be of a sufficient amount, and of an appropriate currency and term, to ensure that the cash inflows from those assets will meet the expected cash outflows from the *firm's* insurance liabilities as they become due.
- (3) For the purpose of (2), a *firm* must take into consideration in determining expected cash outflows any options which exist in the *firm's contracts of insurance*.
- (4) (1) does not apply to assets held to cover *index-linked liabilities* or *property-linked liabilities*, except that where the *linked long-term contract of insurance* in question includes a guarantee of investment performance or some other guaranteed benefit, (1) will nevertheless apply to assets held to cover that guaranteed element.

7.2.35 G A *firm* should take account of the amount, currency and timing of its expected cash outflows in determining whether the assets it holds to cover its *technical provisions* meet the requirements of *PRU 7.2.34R(2)*.

7.2.36 G For the purpose of *PRU 7.2.34R(2)*, the relevant cash inflows are those which the *firm* reasonably expects to receive from the *admissible assets* which it holds to cover its *technical provisions*. A *firm* may receive cash inflows as a result of:

- (1) selling assets or closing out transactions;
  - (2) holding assets that generate dividends, interest or other income; and
  - (3) receiving future *premiums* for existing business.
- 7.2.37 G Anticipated cash inflows from future new business should not be included, for example where the *customer* has not yet contracted to pay the *premium*, and where the associated liabilities and potential cash outflows should also not be included.
- 7.2.38 G A *firm* should compare cash inflows and outflows based on current expectations of amounts and timings. Current market expectations of future asset values, interest rates and currency exchange rates should be used. Where inflows are received in a currency different from that in which outflows are to be paid, account should be taken of the cost of converting the currency received.
- 7.2.39 G In considering the value and suitability of assets required to ensure that the *firm*'s liabilities are met as they become due, a *firm* should take account of the risk of default on inflows from those assets, and other risks that may mean that future inflows are reduced relative to outflows.
- 7.2.40 G *PRU 7.2.20R* lays down a general requirement for a *firm* that carries on *long-term insurance business* to hold *admissible assets* that are of a value sufficient to cover its *mathematical reserves* (calculated in accordance with the *rules* in *PRU 7.3*). The *PRU 7.2.34R(2)* requirement to match liabilities with assets that allow cash outflows to be met with suitable inflows as the outflows become due may mean that a *firm* has to hold assets of a value greater than would otherwise be required by the general *rule* in *PRU 7.2.20R*.

#### Premiums for new business

- 7.2.41 R A *firm* must not enter into a *long-term insurance contract* unless it is satisfied on reasonable actuarial assumptions that:
- (1) the *premiums* receivable and the investment income expected to be earned from those *premiums*; and
  - (2) the *reinsurance* arrangements made in respect of the risk or risks covered by that new contract;
- are sufficient to enable it, when taken together with the *firm's* other resources, to:
- (a) establish adequate *technical provisions* as required by *PRU 7.2.16R*;
  - (b) hold *admissible assets* of a value at least equal to the amount of the *technical provisions* as required by *PRU 7.2.20R* to *PRU 7.2.28R*; and
  - (c) maintain adequate overall financial resources as required by *PRU 1.2.22R*.

- 7.2.42 G For the purposes of *PRU 7.2.41R*, the adequacy of *premiums* may be assessed in the context of a *firm's* total portfolio of business and its other resources. It thus does not prevent a *firm* writing loss leaders nor writing contracts which might incur large losses, but only if the *firm* can meet the losses that might reasonably arise, including those that would arise from an event specifically insured against.

#### Capital requirements for insurers

- 7.2.43 G (1) *PRU 2.1.9R* requires a *firm* to maintain *capital resources* equal to or in excess of its *capital resources requirement (CRR)*. *PRU 2.1* sets out the overall framework of the *CRR*; in particular, *PRU 2.1.14R* requires that for a *firm* carrying on *general insurance business* the *CRR* is equal to the *minimum capital requirement (MCR)*. *PRU 2.1.15R* requires that for *realistic basis life firms* the *CRR* is the higher of the *MCR* and the *ECR*. *PRU 2.1.20R* requires that for *regulatory basis only life firms* the *CRR* is equal to the *MCR*.
- (2) For non-life *firms* the *MCR* represents the *minimum capital requirement* (or margin of solvency) prescribed by the *Insurance Directives*. *PRU 2.1.21R* provides that, for a *firm* carrying on *general insurance business*, the *MCR* in respect of that business is the higher of the *base capital resources requirement for general insurance business* applicable to that *firm* and the *general insurance capital requirement*. *PRU 2.1.22R* provides that, for a *firm* carrying on *long-term insurance business*, the *MCR* in respect of that business is the higher of the *base capital resources requirement for long-term insurance business* applicable to that *firm* and the sum of the *long-term insurance capital requirement* and the *resilience capital requirement*. As specified in *PRU 2.1.10R*, a *firm* carrying on both *general insurance business* and *long-term insurance business* must apply *PRU 2.1.9R* (referred to in paragraph (1) above) separately to its *general insurance business* and its *long-term insurance business*.
- (3) The calculation of the *general insurance capital requirement* is set out in *PRU 7.2.44G* to *PRU 7.2.72R* below. *PRU 7.2.73G* to *PRU 7.2.79R* set out the calculation of the *insurance-related capital requirement* for non-life *firms*. The calculation of the *long-term insurance capital requirement* is set out in *PRU 7.2.80G* to *PRU 7.2.91R* below.

#### General insurance capital requirement

- 7.2.44 G In relation to the *MCR* (see *PRU 7.2.43G*), *PRU 2.1.30R* requires a *firm* to calculate its *general insurance capital requirement (GICR)* as the highest of the *premiums amount*, the *claims amount*, and the *brought forward amount*. The elements for this computation are set out in *PRU 7.2* as follows:
- (1) the *premiums amount* in *PRU 7.2.45R*;
  - (2) the *claims amount* in *PRU 7.2.47R*; and
  - (3) the *brought forward amount* in *PRU 7.2.51R*.

#### The premiums amount

- 7.2.45 R The *premiums amount* is:
- (1) 18% of the *gross adjusted premiums amount*; less 2% of the amount, if any, by which the *gross adjusted premiums amount* exceeds €50 million; multiplied by
  - (2) the reinsurance ratio set out in *PRU 7.2.54R*.

7.2.46 G *Rules and guidance* as to how the *gross adjusted premiums amount* is to be calculated are set out in *PRU 7.2.56R* to *PRU 7.2.59G*.

The claims amount

- 7.2.47 R The *claims amount* is:
- (1) 26% of the *gross adjusted claims amount*; less 3% of the amount, if any, by which the *gross adjusted claims amount* exceeds € 35 million; multiplied by
  - (2) the reinsurance ratio set out in *PRU 7.2.54R*.

7.2.48 G *Rules and guidance* as to how the *gross adjusted claims amount* is to be calculated are set out in *PRU 7.2.60R* to *PRU 7.2.65G*.

- 7.2.49 R
- (1) Subject to (2) and (3), the Euro amounts specified in *PRU 7.2.45R(1)* and *7.2.47R(1)* will increase each year, starting on the first review date of 20 September 2005 (and annually after that), by the percentage change in the European index of consumer prices (comprising all European Union member states, as published by Eurostat) from 20 March 2002 to the relevant review date, rounded up to a multiple of €100,000.
  - (2) In any year, if the percentage change since the last increase is less than 5%, then there will be no increase.
  - (3) The increase will take effect 30 days after the EU Commission has informed the European Parliament and Council of its review and the relevant percentage change.

7.2.50 R For the purposes of *PRU 7.2.45R(1)* and *PRU 7.2.47R(1)*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union.

The brought forward amount

7.2.51 R The *brought forward amount* is the *general insurance capital requirement (GICR)* for the prior *financial year*, multiplied, if the ratio is less than one, by the ratio (expressed as a percentage) of:

- (1) the *technical provisions* (calculated net of *reinsurance*) for *claims* outstanding at the end of the prior *financial year*, determined in accordance with *PRU 7.2.12R*; to
- (2) the *technical provisions* (calculated net of *reinsurance*) for *claims* outstanding at the beginning of the prior *financial year*, determined in accordance with *PRU 7.2.12R*.

7.2.52 G The *brought forward amount* is the same as the *GICR* for the prior *financial year*, except where *claims* outstanding have fallen during that *financial year*. If they have fallen, the *brought forward amount* is itself reduced by the same percentage fall.

7.2.53 G If the *GICR* for the prior *financial year* is less than the *premiums amount* or the *claims amount*, then a *brought forward amount* is not required to be calculated.

Reinsurance ratio used in calculating the premiums amount and the claims amount

7.2.54 R The reinsurance ratio referred to in *PRU 7.2.45R(2)* and *PRU 7.2.47R(2)* is:

- (1) if the ratio lies between 50% and 100%, the ratio (expressed as a percentage) of:
  - (a) the *claims* incurred (net of *reinsurance*) in the *financial year in question* and the two previous *financial years*; to
  - (b) the gross *claims* incurred in that three-year period;
- (2) 50%, if the ratio calculated in (a) and (b) of (1) is 50% or less; and
- (3) 100%, if the ratio calculated in (a) and (b) of (1) is 100% or more.

7.2.55 G *Rules* and *guidance* as to how the net and gross *claims* are to be calculated are set out in *PRU 7.2.66R* to *PRU 7.2.71R*.

Gross adjusted premiums amount used in calculating the premiums amount

7.2.56 R For the purpose of *PRU 7.2.45R*, the *gross adjusted premiums amount* is the higher of the *written* and *earned gross premiums* (as determined in accordance with *PRU 7.2.66R*) for the *financial year in question*, adjusted by:

- (1) except for a *pure reinsurer* that does not have *permission* under the *Act* to *effect contracts of insurance*, increasing by 50% the amount included in respect of the *premiums* for *general insurance business classes* 11, 12 and 13;
- (2) deducting 66.7% of the *premiums* for *actuarial health insurance* that meets the conditions set out in *PRU 7.2.72R*; and



- (3) multiplying the resulting figure by 12 and dividing by the number of months in the *financial year*. For the purposes of this calculation, the number of months in the *financial year* is the number of complete calendar months in the *financial year* plus any fractions of a month at the beginning and the end of the *financial year*.

- 7.2.57 G A *firm* may use statistical methods in order to allocate *premiums* in respect of the *classes* 11, 12 and 13 for the purposes of *PRU 7.2.56R*.
- 7.2.58 G *General insurance business classes* 11, 12 and 13 are, respectively, the marine liability, aviation liability and general liability insurance classes.
- 7.2.59 G Where the *firm* did not carry on *insurance business* in the *financial year in question*, the *gross adjusted premiums amount*, and therefore the *premiums amount*, is nil.

Gross adjusted claims amount used in calculating the claims amount

- 7.2.60 R For the purpose of *PRU 7.2.47R* and subject to *PRU 7.2.62R*, the *gross adjusted claims amount* is the amount of *gross claims* incurred (as determined in accordance with *PRU 7.2.66R*) over the reference period (as specified in *PRU 7.2.63R*) and adjusted by:
- (1) except for a *pure reinsurer* that does not have *permission* under the *Act* to effect contracts of insurance, increasing by 50% the amount included in respect of the *claims* incurred for *general insurance business classes* 11, 12 and 13;
  - (2) deducting 66.7% of the *claims* for *actuarial health insurance* that meets the conditions set out in *PRU 7.2.72R*; and
  - (3) multiplying the resulting figure by 12 and dividing by the number of months in the reference period. For the purposes of this calculation, the number of months in the reference period is the number of complete calendar months in the reference period plus any fractions of a month at the beginning and the end of the reference period.
- 7.2.61 G A *firm* may use statistical methods in order to allocate *claims* in respect of *classes* 11, 12 and 13 for the purposes of *PRU 7.2.60R*.
- 7.2.62 R For the purposes of *PRU 7.2.47R*, in relation to *general insurance business class* 18, the amount of *claims* incurred used to calculate the *gross adjusted claims amount* must be the amount of costs recorded in the *firm's* books in the reference period as borne by the *firm* (whether or not borne in the reference period) in respect of the assistance given.
- 7.2.63 R (1) Except in those cases where paragraph (2) applies, the reference period to be used in *PRU 7.2.60R* and *PRU 7.2.62R* must be:
- (a) the *financial year in question* and the two previous *financial years*; or

- (b) the period the *firm* had been in existence at the end of the *financial year in question*, if shorter.
- (2) In the case of a *firm* which underwrites only one or more of the *general insurance business* risks of credit, storm, hail or frost (including other business written in connection with such risks), the reference period to be used must be:
- (a) the *financial year in question* and the six previous *financial years*; or
  - (b) the period the *firm* had been in existence at the end of the *financial year in question*, if shorter.
- 7.2.64 G The classification of the risks referred to in *PRU 7.2.63R(2)* is as follows: credit - as included in *general insurance business class 14*; storm – as included in *general insurance business class 8*; hail – as included in *general insurance business class 9*; and frost – as included in *general insurance business class 9*.
- 7.2.65 G Where the *firm* did not carry on *insurance business* in the reference period, the *gross adjusted claims amount*, and therefore the *claims amount*, is nil.

Accounting for premiums and claims

- 7.2.66 R For the purposes of *PRU 7.2.54R*, *PRU 7.2.56R*, *PRU 7.2.60R* and *PRU 7.2.62R*, amounts of *premiums* and *claims* must be:
- (1) determined in accordance with *PRU 1.3 (Valuation)*; and
  - (2) adjusted for transfers that were approved by the relevant authority (or became effective where approval by an authority was not required) before the end of the *financial year in question*:
    - (a) to exclude any amount included in, or adjustment made to, *premiums* and *claims* to reflect the consideration for a transfer of *contracts of insurance* to or from the *firm*;
    - (b) to exclude *premiums* and *claims* which arose from *contracts of insurance* that have been transferred by the *firm* to another body; and
    - (c) to account for *premiums* and *claims* which arose from *contracts of insurance* that have been transferred to the *firm* from another body as if they were receivable by or payable to the *firm*.

- 7.2.67 G To ensure that all rights and obligations under a *contract of insurance* are transferred, a number of alternative mechanisms could be used. These are: an *insurance business transfer* under Part VII of the *Act*; under earlier *United Kingdom* insurance legislation; under equivalent foreign legislation; or by novation of contracts. The term “relevant authority” in paragraph (2) of *PRU 7.2.66R* may refer to whatever body has responsibility in a country, whether within or outside the *EEA*, for the approval of transfers of portfolios of *contracts of insurance*; the body may be a supervisory authority for financial services as such or it may be a judicial authority which has the necessary responsibility.
- 7.2.68 G *PRU 7.2.66R(2)(b)* requires a *firm*, for the purpose of calculating its *GICR*, to account for *contracts of insurance* transferred by it to another body as if it had never written those contracts. All amounts of *premiums* and *claims* arising in respect of those contracts are excluded, including amounts that arose in the *financial year in question* or previous *financial years*.
- 7.2.69 G Conversely, *PRU 7.2.66R(2)(c)* requires a *firm*, for the purpose of calculating its *GICR*, to account for *contracts of insurance* transferred to it by another body as if it had been responsible for those contracts from inception and not merely from the date of transfer. All amounts of *premiums* and *claims* that arose from those contracts are included even where they arose prior to the date of transfer and were, in fact, receivable by or payable to the other body.
- 7.2.70 G For both transfers to and from the *firm*, the consideration receivable or payable in respect of the transfer is excluded from *premiums* and *claims* in order to avoid double counting.
- 7.2.71 R Where there has been a significant change in the business portfolio of the *firm* since the end of the *financial year in question*, for example, a line of business has been transferred to another *firm*, or the *firm* no longer carries on a particular *class of insurance business*, the *gross adjusted premiums amount* and the *gross adjusted claims amount* must both be recalculated to take into account the impact of this change. The recalculation must take into account the requirements of *PRU 1.3* (Valuation).

#### Actuarial health insurance

- 7.2.72 R The conditions referred to in *PRU 7.2.56R(2)* and *PRU 7.2.60R(2)* are that:
- (1) the health insurance is underwritten on a similar technical basis to that of life insurance;
  - (2) the *premiums* paid are calculated on the basis of sickness tables according to the mathematical method applied in insurance;
  - (3) a provision is set up for increasing age;
  - (4) an additional *premium* is collected in order to set up a safety margin of an appropriate amount;
  - (5) it is not possible for the *firm* to cancel the contract after the end of the third year of insurance; and

- (6) the contract provides for the possibility of increasing *premiums* or reducing payments even for current contracts.

#### Insurance-related capital requirement (general insurance business only)

- 7.2.73 G *PRU 2.3.11R* requires *firms* carrying on *general insurance business*, other than a *non-directive insurer*, to calculate their *ECR* as the sum of the *asset-related capital requirement* and the *insurance-related capital requirement* less the *firm's equalisation provisions*. The *ECR* for *firms* carrying on *general insurance business* is an indicative measure of the *capital resources* that a *firm* may need to hold based on risk sensitive calculations applied to its business profile. For *firms* carrying on *general insurance business*, the *FSA* will use the *ECR* as a benchmark for individual capital guidance for a *firm* carrying on *general insurance business*. Details of the calculation of the *asset-related capital requirement* are set out in *PRU 3.3*. Details of the calculation of the *insurance-related capital requirement* are set out in *PRU 7.2.76R* to *PRU 7.2.79R*.
- 7.2.74 G The *insurance-related capital requirement* is a measure of the capital that a *firm* should hold against the risk of:
- (1) an adverse movement in the value of a *firm's* liabilities, to recognise that there may be substantial volatility in *claims* and other *technical provisions* made by the *firm*. Such variations may be due to inflationary increases, interest rate changes, movements in the underlying provisions themselves, changes in expense costs, inadequate rate pricing or *premium* collections (or both) from intermediaries differing from projected assumptions; and
  - (2) the *premiums* a *firm* charges in respect of particular business not being adequate to fund future liabilities arising from that business.
- 7.2.75 G The *insurance-related capital requirement* is calculated by applying capital charge factors, expressed as a percentage, to the value of the *net written premiums* and the *technical provisions* in respect of different classes of business. *Firms* should refer to *PRU 1.3.5R* which sets out how a *firm* must recognise and value assets and liabilities.

#### Calculation of the insurance-related capital requirement

- 7.2.76 R A *firm* must calculate its *insurance-related capital requirement* in accordance with *PRU 7.2.77R*.
- 7.2.77 R (1) The value of:
- (a) the *net written premiums*; and
  - (b) the *technical provisions*;
- in respect of each class of business listed in the table in *PRU 7.2.79R* must be multiplied by the corresponding capital charge factor.

- (2) If any amount which is to be multiplied by a capital charge factor is a negative amount, that amount shall be treated as zero.
- (3) The amounts resulting from multiplying the *net written premiums* in respect of each such class of business by the corresponding capital charge factor must be aggregated.
- (4) The amounts resulting from multiplying the *technical provisions* in respect of each such class of business by the corresponding capital charge factor must be aggregated.
- (5) The *insurance-related capital requirement* is the sum of the amounts calculated in accordance with (3) and (4).

7.2.78 R In PRU 7.2.77R references to *technical provisions* comprise:

- (1) outstanding *claims*;
- (2) provisions for incurred but not reported (*IBNR claims*);
- (3) provisions for incurred but not enough reported (*IBNER claims*);
- (4) *unearned premium* reserves less *deferred acquisition costs*; and
- (5) unexpired risk reserves;

in each case net of *reinsurance* receivables.

7.2.79 R Table: Insurance-related Capital Charge Factors

Class of Business	Net Written Premium capital charge factor	Technical provision capital charge factor
Reporting Group: Direct Personal Motor		
Private motor – comprehensive	10.0%	9.0%
Private motor – non-comprehensive	10.0%	9.0%
Motor cycle	10.0%	9.0%
Reporting Group: Direct Commercial Motor		
Fleets	10.0%	9.0%
Commercial vehicles (non-fleet)	10.0%	9.0%
Reporting Group: Direct Accident & Health		

Private medical insurance	5.0%	7.5%
HealthCare cash plans	5.0%	7.5%
Personal accident or sickness	5.0%	7.5%
Travel	5.0%	7.5%
Reporting Group: Direct Personal Lines Property		
Household and domestic all risks	10.0%	10.0%
Reporting Group: Direct Personal Lines Pecuniary Loss		
Assistance	25.0%	14.0%
Creditor	25.0%	14.0%
Extended warranty	25.0%	14.0%
Legal expenses	25.0%	14.0%
Reporting Group: Direct Commercial Lines Property		
Commercial property damage and theft	10.0%	10.0%
Engineering all risks	10.0%	10.0%
Contractors all risks	10.0%	10.0%
Energy	10.0%	10.0%
Mixed commercial package	10.0%	10.0%
Reporting Group: Direct Commercial Lines Liability		
Employers liability	14.0%	14.0%
Product liability	14.0%	14.0%
Public liability	14.0%	14.0%
Professional indemnity	14.0%	14.0%
Reporting Group: Direct Commercial Lines Pecuniary Loss		
Fidelity and contract guarantee	25.0%	14.0%
Mortgage indemnity	25.0%	14.0%
Credit	25.0%	14.0%

Consequential loss	25.0%	14.0%
Suretyship	25.0%	14.0%
Reporting Group: Direct Aviation		
Aviation liability	32.0%	14.0%
Aviation hull	32.0%	14.0%
Space and satellite	32.0%	14.0%
Reporting Group: Direct Marine		
Marine liability	22.0%	17.0%
Marine hull	22.0%	17.0%
Yacht	22.0%	17.0%
War risks	22.0%	17.0%
Protection and Indemnity	22.0%	17.0%
Freight demurrage and defence	22.0%	17.0%
Reporting Group: Direct Transport		
Goods in transit	12.0%	14.0%
Reporting Group: Direct Miscellaneous		
Miscellaneous direct business	25.0%	14.0%
Reporting Group: Non-Proportional Treaty		
Non-proportional accident & health	35.0%	16.0%
Non-proportional motor	10.0%	14.0%
Non-proportional transport	16.0%	15.0%
Non-proportional aviation	61.0%	16.0%
Non-proportional marine	38.0%	17.0%
Non-proportional property non-catastrophe	53.0%	12.0%
Non-proportional property catastrophe	53.0%	12.0%
Non-proportional liability (non-motor)	14.0%	14.0%

Non-proportional pecuniary loss	39.0%	14.0%
Non-proportional aggregate cover	53.0%	12.0%
Reporting Group: Proportional Treaty		
Proportional assumed accident & health	12.0%	16.0%
Proportional assumed motor	10.0%	12.0%
Proportional transport	12.0%	15.0%
Proportional aviation	33.0%	16.0%
Proportional marine	22.0%	17.0%
Proportional property	23.0%	12.0%
Proportional liability (non-motor)	14.0%	14.0%
Proportional pecuniary loss	25.0%	14.0%
Proportional aggregate cover	23.0%	12.0%
Reporting Group: Facultative Reinsurance Categories		
Facultative accident & health	5.0%	7.5%
Facultative motor	10.0%	9.0%
Facultative personal property	10.0%	10.0%
Facultative personal financial loss	25.0%	14.0%
Facultative commercial property	10.0%	10.0%
Facultative commercial liability	14.0%	14.0%
Facultative commercial financial loss	25.0%	14.0%
Facultative marine	22.0%	17.0%
Facultative aviation	32.0%	14.0%
Facultative transport	12.0%	14.0%
Reporting Group: Miscellaneous Reinsurance		
Miscellaneous reinsurance accepted business	39.0%	14.0%



## Long-term insurance capital requirement

- 7.2.80 G *PRU 2.1.9R* requires a *firm* to which *PRU 2* applies to maintain *capital resources* equal to or in excess of its *capital resources requirement*. *PRU 2.1.15R* defines the *capital resources requirement* for a *firm* to which that rule applies (a *realistic basis life firm*) as the higher of the *MCR* and the *ECR*. For other *firms* carrying on *long-term insurance business (regulatory basis only life firms)*, the *capital resources requirement* is equal to the *MCR*. The *MCR* is defined as the higher of the *base capital resources requirement* and the sum of the *long-term insurance capital requirement (LTICR)* and the *resilience capital requirement* (see *PRU 2.1.22R*). *PRU 2.1.32R* defines the *LTICR* as the sum of the *insurance death, health, expense, and market risk capital components* (see *PRU 7.2.81R* to *PRU 7.2.91R*). *Rules and guidance* about the *resilience capital requirement* are set out in *PRU 4.2.9G* to *PRU 4.2.26R*.

## Insurance death risk capital component

- 7.2.81 R The *insurance death risk capital component* is the aggregate of the amounts which represent the fractions specified by *PRU 7.2.82R* of the capital at risk, defined in *PRU 7.2.83R*, for those contracts where the capital at risk is not a negative figure, multiplied by the higher of:
- (1) 50%; and
  - (2) the ratio as at the end of the preceding *financial year* of:
    - (a) the aggregate capital at risk net of *reinsurance* cessions; to
    - (b) the aggregate capital at risk gross of *reinsurance* cessions.
- 7.2.82 R For the purpose of *PRU 7.2.81R*, the fraction is:
- (1) for *long-term insurance business classes I, II and IX*, except for a *pure reinsurer*:
    - (a) 0.1% for temporary insurance on death where the original term of the contract is three years or less;
    - (b) 0.15% for temporary insurance on death where the original term of the contract is five years or less but more than three years; and
    - (c) 0.3% in any other case;
  - (2) 0.3% for *long-term insurance business classes III, VII and VIII*, except for a *pure reinsurer*; and
  - (3) 0.1% for a *pure reinsurer*.
- 7.2.83 R For the purpose of *PRU 7.2.81R*, the capital at risk is:

- (1) where the benefit under a *contract of insurance* payable as a result of death includes periodic or deferred payments, the present value of the benefits payable; and
- (2) in any other case, the amount payable as a result of death;

less, in either case, the *mathematical reserves* for the contract.

- 7.2.84 G The *insurance death risk capital component* only relates to the risk of death. There is a separate risk component for insured health risks (*class IV*). *Tontines* (*class V*) and *capital redemption* operations (*class VI*) also have separate risk components. There is no specified risk margin for other insured risks.

#### Insurance health risk capital component

- 7.2.85 R The *insurance health risk capital component* is the highest of:
- (1) the *premiums amount* (determined in accordance with *PRU 7.2.45R*);
  - (2) the *claims amount* (determined in accordance with *PRU 7.2.47R*); and
  - (3) the *brought forward amount* (determined in accordance with *PRU 7.2.51R*);
- in respect of:
- (a) *contracts of insurance* falling in *long-term insurance business class IV* (see *PRU 7.2.86R*); and
  - (b) risks falling in *general insurance business classes 1 or 2* that are written as part of a *long-term insurance contract*.

- 7.2.86 R For the purposes of *PRU 7.2.85R*, in the case of *contracts of insurance* falling in *long-term insurance business class IV*, condition (3) as set out in *PRU 7.2.72R* (*Actuarial health insurance*) is modified to: "either the reserves include a provision for increasing age, or the business is conducted on a group basis."

- 7.2.87 G The *insurance health risk capital component* only arises for *permanent health insurance* (*long-term insurance business class IV*) and *accident and sickness insurance* (*general insurance business classes 1 and 2*).

#### Insurance expense risk capital component

- 7.2.88 R The *insurance expense risk capital component* is:
- (1) in respect of *long-term insurance business classes III, VII and VIII*, an amount equivalent to 25% of the net *administrative expenses* in the preceding *financial year* relevant to the business of each of those *classes*, in so far as the *firm* bears no investment risk and the allocation to cover *management expenses* in the *contract of insurance* does not have a fixed upper limit which is effective as a limit for a period exceeding 5 years from the commencement of the contract;

- (2) in respect of any *tontine* (*long-term insurance business class V*), 1% of the assets of the *tontine*;
- (3) in the case of any other *long-term insurance business*, 1% of the “adjusted *mathematical reserves*” (as defined in *PRU 7.2.90R* and *PRU 7.2.91R*).

Insurance market risk capital component

- 7.2.89 R The *insurance market risk capital component* is 3% of the “adjusted *mathematical reserves*” (as defined in *PRU 7.2.90R* and *PRU 7.2.91R*) for all *contracts of insurance* except those which:
- (1) fall in *long-term insurance business classes III, VII or VIII* and in respect of which the *firm* does not bear any investment risk; or
  - (2) fall in *long-term insurance business class V*.

Adjusted mathematical reserves

- 7.2.90 R For the purpose of *PRU 7.2.88R* and *PRU 7.2.89R*, the “adjusted *mathematical reserves*” is the amount of *mathematical reserves* (gross of *reinsurance cessions*), multiplied by the higher of:
- (1) 85% or, in the case of a *pure reinsurer*, 50%; and
  - (2) the ratio as at the end of the preceding *financial year* of:
    - (a) the *mathematical reserves* net of *reinsurance cessions*; to
    - (b) the *mathematical reserves* gross of *reinsurance cessions*.
- 7.2.91 R The “adjusted *mathematical reserves*” do not include:
- (1) for the purposes of *PRU 7.2.88R(3)* and *PRU 7.2.89R*, amounts arising from *tontines* (*long-term insurance business class V*);
  - (2) for the purposes of *PRU 7.2.88R(3)*, amounts arising from *insurance business* in *classes III, VII or VIII*, to the extent that such business meets the conditions in *PRU 7.2.88R(1)*;
  - (3) for the purposes of *PRU 7.2.89R*, amounts arising from *insurance business* in *classes III, VII or VIII*, to the extent that such business meets the conditions in *PRU 7.2.89R(1)*.

## 7.3 Mathematical reserves

### Application

7.3.1 R *PRU 7.3 applies to a long-term insurer unless it is:*

- (1) *a non-directive friendly society; or*
- (2) *an incoming EEA firm; or*
- (3) *an incoming Treaty firm.*

### Purpose

7.3.2 G This section follows on from the overall requirement on *firms* to establish adequate *technical provisions* (see *PRU 7.2.16R*). The *mathematical reserves* form the main component of *technical provisions* for *long-term insurance business*. *PRU 7.3* sets out *rules and guidance* as to the methods and assumptions to be used in calculating the *mathematical reserves*. The *rules and guidance* set out the minimum basis for *mathematical reserves*. Methods and assumptions that produce reserves that are demonstrably equal to or greater than the minimum basis may also be used, though they must meet the basic requirements for methods and assumptions set out in *PRU 7.3.7R* to *PRU 7.3.27G*.

7.3.3 G This section applies to all *firms* carrying on *long-term insurance business* and implements some of the requirements contained in article 20 of the *Consolidated Life Directive*. The implementation is designed to ensure that a *firm's mathematical reserves* in respect of *long-term insurance contracts* meet the minimum requirements set by the *Consolidated Life Directive*. A *firm* may use a prospective or a retrospective method to value its *mathematical reserves* (see *PRU 7.3.7R*).

7.3.4 G The required procedures are summarised in the flowchart in *PRU 7 Ann 1G*.

7.3.5 G *Firms* to which *PRU 2.1.15R* applies are required to calculate a *with-profits insurance capital component* (see *PRU 2.1.34R*). In order to calculate its *with-profits insurance capital component*, such a *firm* is required to carry out additional calculations of its liabilities on a realistic basis (see *PRU 7.4*), which it is required to report to the *FSA* (see Forms 18,19). A *firm* that reports its liabilities on a realistic basis is referred to in *PRU* as a *realistic basis life firm*. Such *firms* are subject to different *rules* relating to the calculation of *mathematical reserves* (see *PRU 7.3.46R* and *PRU 7.3.76R*) compared with those that apply to *firms* that report on a regulatory basis only (*regulatory basis only life firms*).

7.3.6 G A number of the *rules* in this section require a *firm* to take into account its regulatory duty to treat *customers* fairly. In this section, references to such a duty are to a *firm's* duty to pay due regard to the interests of its *customers* and to treat them fairly (see *Principle 6* in *PRIN*). This duty is owed to both *policyholders* and potential *policyholders*.

### Basic valuation method

7.3.7 R (1) Subject to (2), a *firm* must establish its *mathematical reserves* using a prospective actuarial valuation on prudent assumptions of all future cash flows expected to arise under, or in respect of, each of its *long-term insurance contracts*.

(2) But a *firm* may use a retrospective actuarial valuation where:

- (a) a prospective method cannot be applied to a particular type of contract;

- or
- (b) the *firm* can demonstrate that the resulting amount of the *mathematical reserves* would be no lower than would be required by a prudent prospective actuarial valuation.
- 7.3.8 G A prospective valuation sets the *mathematical reserves* at the present value of future net cash flows. A retrospective method typically sets the *mathematical reserves* at the level of *premiums* received (and accumulated with investment return), less *claims* and expenses paid. A prospective valuation is preferred because it takes account of circumstances that might have arisen since the *premium* rate was set and of changes in the perception of future experience. Circumstances in which a retrospective valuation might be appropriate include:
- (1) where the assumptions initially made in determining the *premium* rate were sufficiently prudent at inception and have not been overtaken by subsequent events; and
  - (2) where the liability depends on the emerging experience.
- 7.3.9 R Except in *PRU 7.3.71R(1)*, *PRU 7.3* does not apply to *final bonuses*. In addition, for *realistic basis life firms* only, *PRU 7.3* does not apply to future *annual bonuses*.
- Methods and assumptions
- 7.3.10 R In the actuarial valuation under *PRU 7.3.7R*, a *firm* must use methods and prudent assumptions which:
- (1) are appropriate to the business of the *firm*;
  - (2) are consistent from year to year without arbitrary changes (see *PRU 7.3.11G*);
  - (3) are consistent with the method of valuing assets (see *PRU 1.3*);
  - (4) include appropriate margins for adverse deviation of relevant factors (see *PRU 7.3.12G*);
  - (5) recognise the distribution of profits (that is, emerging surplus) in an appropriate way over the duration of each *contract of insurance*;
  - (6) take into account its regulatory duty to treat its *customers* fairly (see *Principle 6*); and
  - (7) are in accordance with generally accepted actuarial practice.
- 7.3.11 G *PRU 7.3.10R(2)* prohibits only arbitrary changes in methods and assumptions, that is, changes made without adequate reasons. Any such changes would hinder comparisons over time as to the amount of the *mathematical reserves* and so obscure trends in solvency and the emergence of surplus.
- 7.3.12 G The relevant factors referred to in *PRU 7.3.10R(4)* may include, but are not limited to, factors such as future investment returns, expenses, mortality, morbidity, options, persistency and *reinsurance* (see also *PRU 7.3.13R* to *PRU 7.3.19G*).
- Margins for adverse deviation
- 7.3.13 R The appropriate margins for adverse deviation required by *PRU 7.3.10R(4)* must be sufficiently prudent to ensure that there is no significant foreseeable risk that liabilities to *policyholders* in respect of *long-term insurance contracts* will not be met as they fall due.
- 7.3.14 G The margins for adverse deviation are a prudential margin in respect of the risks that arise under a *long-term insurance contract*.
- 7.3.15 G *PRU 7.3.13R* sets the normal standard of prudence required for margins. *PRU*

- 7.3.16G suggests benchmarks against which a *firm* should compare the margins it has set in accordance with *PRU 7.3.10R(4)* and *PRU 7.3.13R*. *PRU 7.3.17G* gives *guidance* where a market risk premium is not readily obtainable.
- 7.3.16 G When setting the margins for adverse deviation required by *PRU 7.3.10R(4)* in relation to a particular contract, a *firm* should consider, where appropriate:
- (1) the margin for adverse deviation included in the *premium* for similar *long-term insurance contracts*, if any, newly issued by the *firm*; and
  - (2) where a sufficiently developed and diversified market for transferring a risk exists, the risk premium that would be required by an unconnected party to assume the risk in respect of the contract.
- The margin for adverse deviation of a risk should generally be greater than or equal to the relevant market price for that risk.
- 7.3.17 G Where a risk premium is not readily available, or cannot be determined, an external proxy for the risk should be used, such as adjusted industry mortality tables. Where there is a considerable range of possible outcomes, the *FSA* expects *firms* to use stochastic techniques to evaluate these risks. In time, for example, longevity risk, where this constitutes a significant risk for the *firm*, may fall into this category.
- 7.3.18 G The margins for adverse deviation should be recognised as profit only as the *firm* itself is released from risk over the duration of the contract.
- 7.3.19 G Further detailed *rules* and *guidance* on margins for adverse deviation are included in *PRU 7.3.32G* to *PRU 7.3.91G*. In particular, the cross-references for the different assumptions used in calculating the *mathematical reserves* are as follows:
- (1) expenses (*PRU 7.3.50R* to *PRU 7.3.58G*);
  - (2) mortality and morbidity (*PRU 7.3.59R* to *PRU 7.3.61G*);
  - (3) options (*PRU 7.3.62R* to *PRU 7.3.72G*);
  - (4) persistency (*PRU 7.3.73G* to *PRU 7.3.77G*); and
  - (5) *reinsurance* (*PRU 7.3.78G* to *PRU 7.3.91G*).
- The *rules* and *guidance* on margins for adverse deviation in respect of future investment returns, which are also required in the calculation of *mathematical reserves*, are set out in *PRU 4.2.28R* to *PRU 4.2.48G*.
- Record keeping
- 7.3.20 R A *firm* must make, and retain for an appropriate period, a record of:
- (1) the methods and assumptions used in establishing its *mathematical reserves*, including the margins for adverse deviation, and the reasons for their use; and
  - (2) the nature of, reasons for, and effect of, any change in approach, including the amount by which the change in approach increases or decreases its *mathematical reserves*.
- 7.3.21 G *PRU 1.4.53R* requires *firms* to maintain accounting and other records for a minimum of three years, or longer as appropriate. For the purposes of *PRU 7.3.20R*, a period of longer than three years will be appropriate for a *firm's long-term insurance business*. In determining an appropriate period, a *firm* should have regard to:
- (1) the detailed *rules* and *guidance* on record keeping in *PRU 1.4.51G* to *PRU 1.4.64G*;
  - (2) the nature and term of the *firm's long-term insurance business*; and

- (3) any additional provisions or statutory requirements applicable to the *firm* or its records.

Valuation of individual contracts

- 7.3.22 R (1) Subject to (2) and (3), a *firm* must determine the amount of the *mathematical reserves* separately for each *long-term insurance contract*.  
(2) Approximations or generalisations may be made where they are likely to provide the same, or a higher, result.  
(3) A *firm* must set up additional *mathematical reserves* on an aggregated basis for general risks that are not specific to individual contracts.
- 7.3.23 G *PRU 7.3.22R* to *PRU 7.3.91G* set out *rules* and *guidance* for the separate prospective valuation of each contract. These may be applied instead to groups of contracts where the conditions set out in *PRU 7.3.22R(2)* are satisfied.

Contracts not to be treated as assets

- 7.3.24 R A *firm* must not treat a *long-term insurance contract* as an asset.
- 7.3.25 G A separate prospective valuation for each contract may identify contracts for which the value of future cash inflows exceeds that of outflows, that is, the contracts have an asset value, rather than liability value. However, the *surrender value* of a contract is always greater than or equal to zero and the *Consolidated Life Directive* requires that no contract should be valued at less than its guaranteed *surrender value*. As a result, no contract should be treated as an asset.

Avoidance of future valuation strain

- 7.3.26 R (1) A *firm* must establish *mathematical reserves* for a *contract of insurance* which are sufficient to ensure that, at any subsequent date, the *mathematical reserves* then required are covered solely by:  
(a) the assets covering the current *mathematical reserves*; and  
(b) the resources arising from those assets and from the contract itself.  
(2) For the purposes of (1), the *firm* must assume that:  
(a) the assumptions adopted for the current valuation of liabilities remain unaltered and are met; and  
(b) discretionary benefits and charges will be set so as to fulfil its regulatory duty to treat its *customers* fairly.  
(3) (1) may be applied to a group of similar contracts instead of to the individual contracts within that group.
- 7.3.27 G The valuation of each contract, or group of similar contracts, should allow for the possibility, where it exists, that contracts may be surrendered (wholly or in part), lapsed or made paid-up at any time. The valuation assumptions include margins for adverse deviation (see *PRU 7.3.13R*). *PRU 7.3.26R* requires *mathematical reserves* to be established such that, if future experience is in line with the valuation assumptions, there would be no future valuation strain.

Cash flows to be valued

- 7.3.28 R In a prospective valuation, a *firm* must include the following in the cash flows to be valued:  
(1) future *premiums* (see *PRU 7.3.35G* to *PRU 7.3.47G*);  
(2) expenses, including *commissions* (see *PRU 7.3.50R* to *PRU 7.3.58G*);  
(3) benefits payable (see *PRU 7.3.29R*); and  
(4) amounts to be received or paid in respect of the *long-term insurance*

- contracts* under contracts of *reinsurance* or analogous non-*reinsurance* financing agreements (*PRU 7.3.78G* to *PRU 7.3.91G*).
- 7.3.29 R For the purpose of *PRU 7.3.28R(3)*, benefits payable include:
- (1) all guaranteed benefits including guaranteed *surrender values* and paid-up values;
  - (2) vested, declared and allotted bonuses to which the *policyholder* is entitled;
  - (3) all options available to the *policyholder* under the terms of the contract; and
  - (4) discretionary benefits payable in accordance with the *firm's regulatory duty* to treat its *customers* fairly.
- 7.3.30 G All cash flows are to be valued using prudent assumptions in accordance with generally accepted actuarial practice. Cash flows may be omitted from the valuation calculations provided the reserves obtained as a result of leaving those cash flows out of the calculation are not less than would have resulted had all cash flows been included (see *PRU 7.3.22R(2)*). Provision for future expenses in respect of *with-profits insurance contracts* (excluding *accumulating with-profits policies*) may be made implicitly, using the *net premium* method of valuation (see *PRU 7.3.43R* below). For the purposes of *PRU 7.3.28R(2)*, any charges included in expenses should be determined in accordance with the *firm's regulatory duty* to treat its *customers* fairly.
- 7.3.31 G *PRU 7.3.29R(4)* requires *regulatory basis only life firms* to make allowance for any future *annual bonus* that a *firm* would expect to grant, assuming future experience is in line with the assumptions used in the calculation of the *mathematical reserves*. *Final bonuses* do not have to be taken into consideration in these calculations (see *PRU 7.3.9R*). For *realistic basis life firms*, except for *accumulating with-profits policies*, the *mathematical reserves* may be calculated as the amount required to cover guaranteed benefits as for such *firms* full allowance for discretionary benefits is made in the calculation of the *realistic value of liabilities* (see *PRU 7.4.105R(5)*). The calculations required for *accumulating with-profits policies* are set out in *PRU 7.3.71R(1)*.
- Valuation assumptions: detailed rules and guidance
- 7.3.32 G More detailed *rules* and *guidance* about the valuation of cash flows are set out in *PRU 7.3.33R* to *PRU 7.3.91G*.
- Valuation rates of interest
- 7.3.33 R In calculating the present value of future net cash flows, a *firm* must determine the rates of interest to be used in accordance with *PRU 4.2.28R* to *PRU 4.2.47R*.
- 7.3.34 G The *rules* in *PRU 4.2.28R* to *PRU 4.2.47R* set out the approach *firms* must take in setting margins for adverse deviation in the interest rates assumed in calculating the *mathematical reserves*. This includes a margin to allow for adverse deviation in *market risk* and, where relevant, credit risk. The requirements set out in *PRU 4.2.28R* to *PRU 4.2.47R* protect against the *market risk* that the return actually achieved on assets may fall below the market yields on assets at the *actuarial valuation date*.
- Future premiums
- 7.3.35 G *PRU 7.3.46R* and *PRU 7.3.47G* apply to the valuation of *with-profits insurance liabilities* for a *realistic basis life firm*. *PRU 7.3.38R* to *PRU 7.3.45G* apply to a *regulatory basis only life firm*.
- 7.3.36 G For *non-profit insurance contracts* no specific method of valuation for future



*premiums* is required by *PRU*. However, the method of valuation used should be sufficiently prudent taking into account, in particular, the risk of voluntary discontinuance by the *policyholder*.

Future premiums: firms reporting only on a regulatory basis

- 7.3.37 R *PRU 7.3.38R to PRU 7.3.43R apply to a regulatory basis only life firm.*
- 7.3.38 R (1) This rule applies to *with-profits insurance contracts* except *accumulating with-profits policies* written on a recurring single *premium* basis.
- (2) The value attributed to a *premium* due in any future *financial year* (a future *premium*) must not exceed the lower of the value of:
- (a) the actual *premium* payable under the contract; and
- (b) the *net premium*.
- (3) The *net premium* may be increased for *deferred acquisition costs* in accordance with *PRU 7.3.43R*.
- 7.3.39 G The valuation method for future *premiums* in *PRU 7.3.38R* retains the difference, if any, between the gross *premium* and the *net premium* as an implicit margin available to finance future bonuses, expenses and other costs. It thus helps to protect against the risk that adequate resources may not be available in the future to meet those costs.
- 7.3.40 R Where the terms of a *contract of insurance* have changed since it was first entered into, a *firm* must apply one of the methods in *PRU 7.3.41R* in determining the *net premium* for the purpose of *PRU 7.3.38R(2)(b)*.
- 7.3.41 R A *firm* must treat the change referred to in *PRU 7.3.40R* as if either:
- (1) it had been included in the original contract but came into effect from the time the change became effective; or
- (2) the original contract were cancelled and replaced by a new contract (with an initial *premium* paid on the new contract equal to the liability under the original contract immediately prior to the change); or
- (3) it gave rise to two separate contracts where:
- (a) all *premiums* are payable under the first contract and that contract provides only for such benefits as those *premiums* could have purchased from the *firm* at the date the change became effective; and
- (b) no *premiums* are payable under the second contract and that contract provides for all the other benefits.
- 7.3.42 G *PRU 7.3.41R* permits three alternative methods. However, the third method is only possible where a meaningful comparison can be made between the terms of the contract (as changed) and the terms upon which the *firm* was *effecting* its new *contracts of insurance* at the time the contract was changed.

Future net premiums: adjustment for deferred acquisition costs

- 7.3.43 R (1) The amount of any increase to the *net premium* for *deferred acquisition costs* must not exceed the equivalent of the recoverable acquisition expenses spread over the period of *premium* payments and calculated in accordance with the rates of interest, mortality and morbidity assumed in calculating the *mathematical reserves*.
- (2) For the purpose of (1), recoverable acquisition expenses means the amount of expenses, after allowing for the effects of taxation, which it is reasonable to expect will be recovered from future *premiums* payable under the contract.
- (3) The recoverable acquisition expenses in (1) must not exceed the lower of:
- (a) the value of the excess of actual *premiums* over *net premiums*; and

- (b) 3.5% of the *relevant capital sum*.
- (4) Recoverable acquisition expenses may be calculated as the average for a group of similar contracts weighted by the *relevant capital sum* for each contract.
- 7.3.44 G *PRU 7.3.43R* allows a *firm* to spread acquisition costs over the lifetime of a *contract of insurance*, but only if it is reasonable to expect those costs to be recoverable from future *premium* income from that contract. Further prudence is provided by the limitation of recoverable acquisition expenses to 3.5% of the *relevant capital sum*. This adjustment for acquisition costs is sometimes termed a Zillmer adjustment.
- 7.3.45 G In determining the extent, if any, to which it is reasonable to expect acquisition costs to be recoverable from future *premium* income, the *firm* should make prudent assumptions as to levels of voluntary discontinuance by *policyholders*.  
Future premiums: firms also reporting with-profits insurance liabilities on a realistic basis
- 7.3.46 R (1) Subject to (2), for a *realistic basis life firm*, the future *premiums* to be valued in the calculation of the *mathematical reserves* for its *with-profits insurance contracts* must not be greater than the gross *premiums* payable by the *policyholder*.  
(2) This *rule* does not apply to *accumulating with-profits policies* written on a recurring single *premium* basis (see *PRU 7.3.48R*).
- 7.3.47 G The gross *premium* is the full amount of *premium* payable by the *policyholder* to the *firm*. The gross *premium* method contrasts with the *net premium* method which is required from *regulatory basis only life firms* (see *PRU 7.3.37R* to *PRU 7.3.45G*).  
Future premiums: accumulating with-profits policies
- 7.3.48 R (1) This *rule* applies to *accumulating with-profits policies* written on a recurring single *premium* basis.  
(2) A *firm* must not attribute any value to a future *premium* under the contract.  
(3) Any liability arising only upon the payment of that *premium* may be ignored except to the extent that the value of that liability upon payment would exceed the amount of that *premium*.
- 7.3.49 G *PRU 7.3.48R* prohibits a *firm* from taking credit for recurring single *premiums* under *accumulating with-profits policies*. As there is no contractual commitment to pay any future *premiums* the amount and timing of which are uncertain, the recognition of any potential margins would not be prudent. Where the payment of a future *premium* would give rise to a liability in excess of the *premium* a provision should be established.  
Expenses
- 7.3.50 R (1) A *firm* must make provision for expenses, either implicitly or explicitly, in its *mathematical reserves* of an amount which is not less than the amount expected, on prudent assumptions, to be incurred in fulfilling its *long-term insurance contracts*.  
(2) For the purpose of (1), expenses must be valued:  
(a) after taking account of the effect of taxation;  
(b) having regard to the *firm's* actual expenses in the last 12 months before the *actuarial valuation date* and any increases in expenses

- expected to occur in the future;
- (c) after making prudent assumptions as to the effects of inflation on future increases in prices and earnings; and
  - (d) at no less than the level that would be incurred if the *firm* were to cease to transact new business 12 months after the *actuarial valuation date*.
- (3) A *firm* must not rely upon an implicit provision arising from the method of valuing future *premiums* except to the extent that:
- (a) it is reasonable to assume that expenses will be recoverable from future *premiums*; and
  - (b) the expenses would only arise if the future *premiums* were received.
- 7.3.51 G For *with-profits insurance contracts* where the *net premium* valuation method applies, an implicit provision arises because the future *premiums* valued are limited to the *net premium* adjusted as permitted by *PRU 7.3.43R*. This excludes the allowance within the gross *premium* for expenses (other than recoverable acquisition expenses). It also excludes other margins within the actual *premium* that are a prudential margin in respect of the risks that arise under the contract or that are needed to provide for future discretionary benefits. To the extent that these other margins are not needed for the purpose for which they were originally established, they may also constitute an implicit provision for expenses.
- 7.3.52 G An implicit provision may also arise for other types of *long-term insurance contract* where, for example, no value is attributed to future *premiums*, but the *firm* is entitled to make deductions from future regular *premiums* before allocating them to secure *policyholder* benefits.
- 7.3.53 G A *firm* should only reduce the provision for future expenses to take account of expected taxation recoveries related to those expenses where recovery is reasonably certain, and after taking into account the assumption that the *firm* ceases to transact new business 12 months after the *actuarial valuation date*. An appropriate adjustment for discounting should be made where receipt of the taxation recoveries is not expected until significantly after the expenses are incurred.
- 7.3.54 G The *firm's* actual expenses in the 12 months prior to the *actuarial valuation date* may serve as a guide to the assumptions for future expenses, taking into consideration the mix of acquisition and renewal expenses. The expense assumptions should not be reduced to account for expected future improvements in efficiency until such efficiency improvements result in a reduced level of actual expenditure. However, the assumptions should take account of all factors which might increase costs including earnings and price inflation.
- 7.3.55 R The provisions for expenses (whether implicit or explicit) required by *PRU 7.3.50R* must be sufficient to cover all the expenses of running off the *firm's* existing *long-term insurance business* including:
- (1) all discontinuance costs (for example, redundancy costs and closure costs) that would arise if the *firm* were to cease transacting new business 12 months after the *actuarial valuation date* in circumstances where (and to the extent that) the discontinuance costs exceed the projected surplus available to meet such costs;
  - (2) all costs of continuing to service the existing business taking into account the loss of economies of scale from, and any other likely consequences of, ceasing to transact new business at that time; and
  - (3) the lower of:

- (a) any projected valuation strain from writing new business for the 12 months following the *actuarial valuation date* to the extent the actual amount of that strain exceeds the projected surplus on prudent assumptions from existing business in the 12 months following the *actuarial valuation date*; and
  - (b) any projected new business expense overrun from writing new business for the 12 months following the *actuarial valuation date* to the extent the projected expenses exceed the expenses that the new business can support on a prudent basis.
- 7.3.56 G The provision for future expenses, whether implicit or explicit, should include a prudent margin for adverse deviation in the level and timing of expenses (see *PRU 7.3.13R* to *PRU 7.3.19G*). The margin should cover the risk of underestimating expenses whether due to, for example, initial under-calculation or subsequent increases in the amount of expenses. In setting the amount of the margin, the *firm* should take into account the extent to which:
- (1) an appropriately validated method based on reliable data is used to allocate expenses by product type, by distribution channel and as between acquisition and non-acquisition expenses;
  - (2) the volume of existing and new business and its distribution by product type or distribution channel is stable or predictable;
  - (3) costs vary in the short, medium or long term dependent upon the volume of existing or new business and its distribution by product type or distribution channel; and
  - (4) cost control is well-managed.
- 7.3.57 G In setting the margin, the *firm* should also take into account:
- (1) the length of the period over which it is necessary to project costs;
  - (2) the extent to which it is reasonable to expect inflation to be stable or predictable over that period; and
  - (3) whether, if inflation is higher than expected, it is reasonable to expect that the excess would be offset by increases in investment returns.
- 7.3.58 G Where a *firm* has entered into an agreement with any other person for the sharing or reimbursement of costs, in setting the margin it should take into account the potential impact of that agreement and of its discontinuance.
- Mortality and Morbidity
- 7.3.59 R A *firm* must set the assumptions for mortality and morbidity using prudent rates of mortality and morbidity that are appropriate to the country or territory of residence of the person whose life or health is insured.
- 7.3.60 G The rates of mortality or morbidity should contain prudent margins for adverse deviation (see *PRU 7.3.13R* to *PRU 7.3.19G*). In setting those rates, a *firm* should take account of:
- (1) the systems and controls applied in underwriting *long-term insurance contracts* and whether they provide adequate protection against anti-selection (that is, selection against the *firm*) including:
    - (a) adequately defining and identifying non-standard risks; and
    - (b) where such risks are underwritten, allocating to them an appropriate weighting;
  - (2) the nature of the contractual exposure to mortality or morbidity risk including:
    - (a) whether lower mortality increases or decreases the *firm*'s liability;

- (b) the period of cover and whether risk charges can be varied during that period and, if so, how quickly; and
- (c) whether the options in the contract give rise to a significant risk of anti-selection (for example, opportunities for voluntary discontinuance, guaranteed renewal at the option of the *policyholder* and rights for conversion of benefits);
- (3) the credibility of the *firm's* actual experience as a basis for projecting future experience including:
  - (a) whether there is sufficient data (especially for medical or financial risks and for new types of benefit or new methods of distribution); and
  - (b) whether the data is reliable and has been appropriately validated;
- (4) the availability and reliability of:
  - (a) any published tables of mortality or morbidity for the country or territory of residence of the person whose life or health is insured; and
  - (b) any other information as to the industry-wide insurance experience for that country or territory;
- (5) anticipated or possible future trends in experience including, but only where they increase the liability:
  - (a) anticipated improvements in mortality;
  - (b) changes arising from improved detection of morbidity (including critical illnesses);
  - (c) diseases the impact of which may not yet be reflected fully in current experience; and
  - (d) changes in market segmentation (such as impaired life annuities) which, in the light of developing experience, may require different assumptions for different parts of the policy class.

7.3.61 G An additional provision for diseases covered by *PRU 7.3.60G(5)(c)* may be needed, in particular for unit-linked policies. In determining whether such a provision is needed a *firm* may take into consideration any ability to increase product charges commensurately (provided that such increase does not infringe on its regulatory duty to treat its *customers* fairly), but a provision would still be required for the period until such an increase could be brought into effect.

Options

7.3.62 R When a *firm* establishes its *mathematical reserves* in respect of a *long-term insurance contract*, the *firm* must include an amount to cover any increase in liabilities which might be the direct result of its *policyholder* exercising an option under, or by virtue of, that *contract of insurance*. Where the *surrender value* of a contract is guaranteed, the amount of the *mathematical reserves* for that contract at any time must be at least as great as the value guaranteed at that time.

7.3.63 G An option exists where a *policyholder* is given a choice between alternative forms of benefit, for example, a choice between receiving a cash benefit upon maturity or an annuity at a guaranteed rate. In some cases, the contract may designate one or other of these alternatives as the principal benefit and any other as an option. This designation, in itself, is not one of substance in the context of reserving since it does not affect the *policyholder's* choices. Other forms of option include:

- (1) the right to convert to a different contract on guaranteed terms;
- (2) the right to increase cover on guaranteed terms;
- (3) the right to a specified amount on surrender; and
- (4) the right to a paid up value.

- 7.3.64 G The *firm* should provide for the benefit which the *firm* anticipates the *policyholder* is most likely to choose. Except for the “option” of voluntary discontinuance in the case of *regulatory basis only life firms* (see *PRU 7.3.74R*), past experience may be used as a guide, but only if this is likely to give a reasonable estimate of future experience. For example, past experience of the take-up of a cash payment option instead of an annuity would not be a reliable guide, if, in the past, market rates exceeded those guaranteed in the annuity but no longer do so. Similarly, past experience on the take-up of options may not be relevant in the light of the assumptions made in respect of future interest rates and mortality rates in the valuation of the benefits.
- 7.3.65 G Many options are long-term and need careful consideration. Improving longevity, for example, can increase the value of guaranteed annuity options vesting further in the future. *Firms* also need to have regard to the fact that *policyholder* behaviour can change in the future as *policyholders* become more aware of the value of their options. The impact on *policyholder* behaviour of possible changes in taxation should also be considered.
- 7.3.66 G In accordance with *PRU 7.3.7R* and *PRU 7.3.13R*, take-up rates for guaranteed annuity options should be assessed on a prudent basis with assumptions that include margins for adverse deviation (see *PRU 7.3.13R* to *PRU 7.3.19G*) that take account of current experience and the potential for future change. The *firm* should reserve for option take-up at least at a prudent margin over current experience for options shortly to vest. For longer term options where the option becomes increasingly valuable in the future due to projected mortality improvements, increased take-up rates should be assumed. In view of the growing uncertainty over take-up rates for projections further in the future, for guaranteed annuity option dates 20 years or more ahead at least a 95% take-up rate assumption should be made.
- 7.3.67 G Where there is considerable variation in the cost of the option depending on conditions at the time the option is exercised, and where that variation constitutes a material risk for the *firm*, it will generally be appropriate to use stochastic modelling. In this case prices from the asset model used in the stochastic approach should be benchmarked to relevant market asset prices before determining the value of the option. Where stochastic modelling is not undertaken, market option prices should be used to determine suitable assumptions for the valuation of the option. If no market exists for a particular option, a *firm* should take the value of the nearest equivalent benefit or right for which a market exists and document the way in which it has adjusted that valuation to reflect the original option.
- 7.3.68 G Where the option offers a choice between two non-discretionary financial benefits (such as between a guaranteed cash sum or a guaranteed annuity value, or between a unit value and a maturity guarantee) and where there is a wide range of possible outcomes, the *firm* should normally model such liabilities stochastically. In carrying out such modelling *firms* should take into account the likely choices to be made by *policyholders* in each scenario. *Firms* should make and retain a record of the development and application of the model.
- 7.3.69 G The value of a contract with an option is greater than the value of a similar contract without the option, that is, the option has value whether it is expected to be exercised or not. Although in theory a *firm* can rebalance its investments to match the expected cost of the option to the *firm* (including the time value of the option), this takes time to achieve and the market may move more quickly than the *firm* is able to respond. Also, there are likely to be transaction costs. *Firms* should

- take these aspects into consideration in setting up *mathematical reserves*.
- 7.3.70 R (1) Where a *policyholder* may opt to be paid a cash amount, or a series of cash payments, the *mathematical reserves* for the *contract of insurance* established under *PRU 7.3.7R* must be sufficient to ensure that the payment or payments could be made solely from:
- (a) the assets covering those *mathematical reserves*; and
  - (b) the resources arising from those assets and from the contract itself.
- (2) In (1) references to a cash amount or a series of cash payments include the amount or amounts likely to be paid on a voluntary discontinuance.
- (3) For the purposes of (1), the *firm* must assume that:
- (a) the assumptions adopted for the current valuation remain unaltered and are met; and
  - (b) discretionary benefits and charges will be set so as to fulfil the *firm's* regulatory duty to treat its *customers* fairly.
- (4) (1) may be applied to a group of similar contracts instead of to the individual contracts within that group.
- 7.3.71 R For the purposes of *PRU 7.3.70R*, a *firm* must assume that the amount of a cash payment secured by the exercise of an option is:
- (1) in the case of an *accumulating with-profits policy*, the lower of:
    - (a) the amount which the *policyholder* would reasonably expect to be paid if the option were exercised, having regard to the representations made by the *firm* and including any expectations of a *final bonus*; and
    - (b) that amount, disregarding all discretionary adjustments;
  - (2) in the case of any other *policy*, the amount which the *policyholder* would reasonably expect to be paid if the option were exercised, having regard to the representations made by the *firm*, without taking into account any expectations regarding future distributions of profits or the granting of discretionary additions in respect of an *established surplus*.
- 7.3.72 G In *PRU 7.3.71R(1)(a)* *firms* must take into consideration, for example, a market value adjustment where such an adjustment has been described in representations made to *policyholders* by the *firm*. However, any discretionary adjustment, such as a market value adjustment, cannot be included in the amount calculated in *PRU 7.3.71R(1)(b)*.
- Persistence assumptions
- 7.3.73 G *PRU 7.3.76R* and *PRU 7.3.77G* apply to the valuation of the *with-profits insurance liabilities* of *realistic basis life firms*. *PRU 7.3.74R* and *PRU 7.3.75G* apply to the valuation of all other liabilities.
- 7.3.74 R Except as permitted by *PRU 7.3.76R*, a *firm* must not make any allowance in the calculation of the *mathematical reserves* for the voluntary discontinuance of any *contract of insurance* if the amount of the *mathematical reserves* so determined would, as a result, be reduced.
- 7.3.75 G The rate of voluntary discontinuance (that is, lapse, surrender or paying up) is often difficult to predict and may be volatile especially in the short term during stressful economic conditions. Depending upon the circumstances and contract terms, voluntary discontinuance may increase or decrease the *firm's* liability. In effect, *PRU 7.3.74R* requires a *firm* to assume that there will be no voluntary discontinuance if assuming voluntary discontinuance would reduce the liability. This protects against the risk that arises from volatility in the rate of voluntary discontinuance. In addition, there is the risk of assets not being realisable when

- needed due to the rates of discontinuance exceeding expected levels.
- 7.3.76 R *A realistic basis life firm* may make assumptions about voluntary discontinuance rates in the calculation of the *mathematical reserves* for its *with-profits insurance business* provided that those assumptions meet the general requirements for prudent assumptions as set out in *PRU 7.3.10R* and *PRU 7.3.13R*.
- 7.3.77 G The prudential margin in respect of assumptions of voluntary discontinuance should be validated both in relation to recent experience and to variations in future experience that might arise as a result of reasonably foreseeable changes in conditions. In particular, where estimates of experience are being made well into the future, the assumptions should contain margins that take into account the increased risk of adverse experience arising from changed circumstances. *Firms* should also consider the possibility of anti-selection by *policyholders* and of variations in persistency experience for different classes and cohorts of business.

#### Reinsurance

- 7.3.78 G The prospective valuation of future cash flows to determine the amount of the *mathematical reserves* includes amounts to be received or paid under contracts of *reinsurance* in respect of *long-term insurance business* (see *PRU 7.3.28R(4)*). This applies even where those cash flows cannot be identified as related to particular *long-term insurance contracts* (see *PRU 7.3.22R(3)*).
- 7.3.79 R *A firm* must value *reinsurance* cash flows using methods and assumptions which are at least as prudent as the methods and assumptions used to value the underlying *contracts of insurance* which have been reinsured. In particular:
- (1) *reinsurance* recoveries must not be recognised unless the underlying liabilities to which they relate have also been recognised;
  - (2) *reinsurance* cash outflows that are unambiguously linked to the emergence as surplus of margins included in the valuation of existing *contracts of insurance* or to the exercise by a *reinsurer* of its rights under a termination clause need not be valued (see *PRU 7.3.85R*); and
  - (3) *reinsurance* cash inflows that are contingent on factors or conditions other than the insurance risks that are reinsured must not be valued.
- 7.3.80 G In valuing *reinsurance* cash flows, a *firm* should establish prudent margins for adverse deviation (see *PRU 7.3.13R* to *PRU 7.3.19G*) including margins in respect of:
- (1) any uncertainty as to the amount or timing of amounts to be paid or received; and
  - (2) the risk of credit default by the *reinsurer*.
- 7.3.81 G In assessing the risk of credit default, the *firm* should take into account the *rules and guidance* in *PRU 3.2* (Credit risk in insurance).
- 7.3.82 G It will not necessarily be appropriate to use the same assumptions in *PRU 7.3.79R* as for the underlying contracts. For example, if only a subgroup of the original contracts is reinsured, it may be appropriate to use different mortality rates.
- 7.3.83 G Only *reinsurance* cash inflows that are triggered unambiguously by the insurance risks of the *firm* that are reinsured may be valued. *Reinsurance* cash inflows that depend on other contingencies where the outcome does not form part of the valuation basis should not be given credit.
- 7.3.84 G *Firms* should assess the extent of margins in the valuation of the existing *contracts of insurance* where these provide implicit provision for the *reinsurance* cash outflows in *PRU 7.3.79R*. Where the *reinsurance* asset exceeds the estimated value of the future surplus under reinsured contracts *firms* should assess their



- credit risk exposure to the *reinsurer* .
- 7.3.85 R For the purposes of *PRU 7.3.79R(2)*, the “link” must be such that a contingent liability to pay or repay the amount to the *reinsurer* could not arise except when, and to the extent that, the margins in the valuation of the existing *contracts of insurance* emerge as surplus, or the *reinsurer* exercises its rights under a termination clause as a result of fraud, misrepresentation, the non-payment of *reinsurance premiums* by the *firm* or a failure by the *firm* to obtain the agreement of the *reinsurer* to a transfer of business by the *firm*.
- 7.3.86 R For the purposes of *PRU 7.3.79R(2)* and *PRU 7.3.85R*, future surplus may only be offset against future *reinsurance* cash outflow in respect of surplus on *non-profit insurance contracts* and the charges or shareholder transfers arising as surplus from *with-profits insurance contracts*. Such charges and transfers may only be allowed for to the extent consistent with the regulatory duty of the *firm* to treat its *customers* fairly.
- 7.3.87 G For the purposes of *PRU 7.3.85R*, a contingent liability means a liability that would only arise upon the happening of a particular contingency, even where that contingency is not expected to occur. For example, if the *firm* has a *reinsurance* arrangement in force that in the event the *firm* were wound up would give rise to repayments other than out of surplus emerging, the *reinsurance* cash outflows should be valued as a liability.
- 7.3.88 G *PRU 7.3.85R* allows a *firm* not to value *reinsurance* cash outflows provided the contingencies in which the *reinsurance* would require repayment other than out of future surpluses are limited to termination clauses concerning fraud, misrepresentation, non-payment of *reinsurance premiums* by the *firm* or a failure by the *firm* to obtain the agreement of the *reinsurer* to a transfer of business by the *firm*.
- 7.3.89 G Where the *reinsurance* cash outflow is payable by a fund or sub-fund that generates such profits, charges or transfers, the *firm* need make no provision for such payments provided that repayment to the *reinsurer* is linked unambiguously (as defined in *PRU 7.3.85R*) to the emergence of future surplus. Where the profits, charges or transfers arising under a block of business are payable by a fund or sub-fund to another part of the *firm* then only where the *firm* has committed to remit such profits, charges or transfers directly to the *reinsurer* would it be acceptable for no provision for payments to the *reinsurer* to be made.
- 7.3.90 R In *PRU 7.3.78G* to *PRU 7.3.89G* references to *reinsurance* and contracts of *reinsurance* include analogous non-*reinsurance* financing agreements.
- 7.3.91 G In *PRU 7.3.78G* to *PRU 7.3.89G* references to *reinsurance* cash outflow include any provision for the reduction in *policy* liabilities recognised as covered under a contract of *reinsurance* or for the reduction of any debt to the *firm* previously created under a contract of *reinsurance*. In *PRU 7.3.90R* analogous non-*reinsurance* financing agreements include contingent loans, securitisations and any other arrangements giving rise to charges on future surplus arising.

## 7.4 With-profits insurance capital component

### Application

- 7.4.1 R *PRU 7.4 applies to a realistic basis life firm.*
- 7.4.2 G *A realistic basis life firm means a firm to which PRU 2.1.15R applies. The application of PRU 2.1.15R is set out in PRU 2.1.16R and PRU 2.1.17R. PRU 2.1.9R requires that a firm must maintain at all times capital resources equal to or in excess of its capital resources requirement. The enhanced capital requirement forms part of the capital resources requirement for a realistic basis life firm. The with-profits insurance capital component forms part of the enhanced capital requirement which a realistic basis life firm is required to calculate in accordance with PRU 2.1.34R.*

### Purpose

- 7.4.3 G *This section sets out rules and guidance as to the methods and assumptions to be used in calculating the with-profits insurance capital component.*
- 7.4.4 G *The purpose of the with-profits insurance capital component is to supplement the mathematical reserves so as to ensure that a firm holds adequate financial resources for the conduct of its with-profits insurance business. In particular, capital in excess of the mathematical reserves may be needed to ensure that adequate final bonuses can be awarded to policyholders. That is, adequate in the sense that in setting bonuses payable to policyholders the firm pays due regard to the interests of its policyholders and treats them fairly. The mathematical reserves for a realistic basis life firm are not required to include provision for future annual bonuses or final bonuses (PRU 7.3.9R).*
- 7.4.5 G *The required procedures are summarised in the flowchart in PRU 7 Ann 1G.*

### Main requirements

- 7.4.6 R *A firm must calculate the with-profits insurance capital component in accordance with PRU 7.4.7R.*
- 7.4.7 R (1) *The with-profits insurance capital component for a firm is the aggregate of any amounts that:*
- (a) *result from the calculations specified in (2) and (3); and*
  - (b) *are greater than zero.*
- (2) *Subject to (3), in relation to each with-profits fund within the firm, the firm must deduct B from A, where:*

- (a) A is the amount of the *regulatory excess capital* for that fund (see *PRU 7.4.23R*); and
  - (b) B is the amount of the *realistic excess capital* for that fund (see *PRU 7.4.32R*).
- (3) Where a capital instrument that can be included in the *firm's capital resources* in accordance with *PRU 2.2* has been attributed wholly or partly to a *with-profits fund* and that instrument meets the requirements of *PRU 2.2.93R*, the *firm* must add to the amount calculated under (2) for that fund the result, subject to a minimum of zero, of deducting D from C where:
- (a) C is the outstanding face amount of the instrument to the extent attributed to the fund; and
  - (b) D is the realistic value of the instrument to the extent attributed to the fund in the single event that determines the *risk capital margin* under *PRU 7.4.43R*.
- 7.4.8 G Subordinated debt which is subordinated to *policyholder* interests (see *PRU 2.2.93R*) is an example of the sort of capital instrument that may give rise to a component of the *WPICC* under *PRU 7.4.7R(3)*. Such instruments are treated as capital under *PRU 2.2*, subject to the requirements of *PRU 2.2.93R*. Under realistic reserving the capital instrument is valued as a realistic liability (see *PRU 7.4.40R*) and in calculating the *risk capital margin* such an instrument would be valued at its realistic value in the single event outlined in *PRU 7.4.43R* (see also *PRU 7.4.162R*). Overall, the effect of *PRU 2.2*, *PRU 7.4.7R(3)* and *PRU 7.4.43R* is to enable a *firm* that obtains subordinated debt to benefit from additional *capital resources* equal to the face amount of that debt.
- 7.4.9 G *SUP 4* (Actuaries) sets out the role and responsibilities of the *actuarial function* and of the *with-profits actuary*.
- (1) As part of his duties under *SUP 4.3.13R*, the *actuary* appointed by the *firm* to perform the *actuarial function* must calculate the *firm's mathematical reserves* and, in the context of the calculation of the *with-profits insurance capital component*, must also:
- (a) advise the *firm's governing body* on the methods and assumptions to be used in the calculation of the *firm's with-profits insurance capital component*;
  - (b) perform that calculation in accordance with the methods and assumptions determined by the *firm's governing body*; and
  - (c) report to the *firm's governing body* on the results of that calculation.

- (2) As part of his duties under SUP 4.3.16R, the *with-profits actuary* must advise the *firm's governing body* on the discretion exercised by the *firm*. In the context of the calculation of the *with-profits insurance capital component*, the *with-profits actuary* must also advise the *firm's governing body* as to whether the methods and assumptions (including the allowance for management actions) used for that calculation are consistent with the *firm's Principles and Practices of Financial Management (PPFM - see COB 6.10)* and with its regulatory duty to treat its *customers* fairly.

## General

### Definitions

- 7.4.10 R In this section, real estate means an interest in land, buildings or other immovable property.
- 7.4.11 R In this section, the long-term gilt yield is the annualised equivalent of the yield on the 15-year index for United Kingdom Government fixed-interest securities jointly compiled by the Financial Times, the Institute of Actuaries and the Faculty of Actuaries.
- 7.4.12 R For the purposes of this section, a *firm* has an exposure to an asset or liability where the *firm's* valuation of its assets or liabilities changes when the value of the asset or liability changes.
- 7.4.13 R Unless the context otherwise requires, all references (however expressed) in this section to realistic liabilities, or to liabilities which are included in the calculation of realistic liabilities, include discretionary benefits payable by the *firm* in accordance with the *firm's* regulatory duty to treat its *customers* fairly.
- 7.4.14 G In this section, any reference to a *firm's* regulatory duty to treat its *customers* fairly is a reference to the *firm's* duty under *Principle 6* (Customers' interests). This states that a *firm* must pay due regard to the interests of its *customers* and treat them fairly.
- 7.4.15 G In this section, any reference to the *Principles and Practices of Financial Management (PPFM)* is a reference to the requirements in COB 6.10 (Principles and Practices of Financial Management) for *firms* to establish, maintain and record the principles and practices of financial management according to which the business of its *with-profits funds* is conducted.
- 7.4.16 G The extent to which a *firm* requires a separate *PPFM* for each of its *with-profits funds* will depend on the *firm's* circumstances and any relevant representations made by the *firm* to its *with-profits policyholders*. In this section, any reference to a *firm's PPFM* refers to the *PPFM* which relate to the *with-profits fund* or the *with-profits insurance contracts* in question.

### Record keeping

- 7.4.17 R A *firm* must make, and retain for an appropriate period of time, a record of:
- (1) the methods and assumptions used in making any calculation required for the purposes of this section (and any subsequent changes) and the reasons for their use; and
  - (2) any change in practice and the nature of, reasons for, and effect of, any change in approach with respect to those methods and assumptions.
- 7.4.18 G *PRU 1.4.53R* requires *firms* to maintain accounting and other records for a minimum of three years, or longer as appropriate. For the purposes of *PRU 7.4.17R*, a period of longer than three years will be appropriate for a *firm's long-term insurance business*. In determining an appropriate time period, a *firm* should have regard to:
- (1) the detailed *guidance* on record keeping in *PRU 1.4.51G* to *PRU 1.4.64G*;
  - (2) the nature and term of the *firm's long-term insurance contracts*; and
  - (3) any additional provisions or statutory requirements applicable to the *firm* or its records.
- 7.4.19 R A *firm* must also identify in the record required to be kept by *PRU 7.4.17R* changes in practice, in particular changes in those items which will or may be significant in relation to the eventual *claim* values.
- 7.4.20 G Some of the changes identified in accordance with *PRU 7.4.19R* may have to be notified to the *firm's policyholders* in accordance with the *firm's PPFM*.

General principles for allocating aggregate amounts

- 7.4.21 R Where any calculation is required under this section which:
- (1) is to be made in respect of any *with-profits fund* of a *firm*; and
  - (2) covers an amount that is otherwise calculated in relation to the *firm* as a whole;
- the *firm* must make an allocation of that amount as between all of its funds (including funds which are not *with-profits funds*).
- 7.4.22 R In any case where:
- (1) *non-profit insurance contracts* are written in any *with-profits fund* of a *firm*; and
  - (2) any calculation is required under this section which:

- (a) is to be made in respect of the *regulatory excess capital* or *realistic excess capital* for the fund; and
- (b) covers an amount that is otherwise calculated or allocated in relation to the fund as a whole;

the *firm* must make an allocation of the amount in (2)(b) as between the *with-profits insurance contracts* and *non-profit insurance contracts* written in the fund.

#### Calculation of regulatory excess capital

- 7.4.23 R A *firm* must calculate the *regulatory excess capital* for each of its *with-profits funds* by deducting B from A, where:
- (1) A is the *regulatory value of assets* of the fund (see *PRU 7.4.24R*); and
  - (2) B is the sum of:
    - (a) the *regulatory value of liabilities* of the fund (see *PRU 7.4.29R*);
    - (b) the *long-term insurance capital requirement* in respect of the fund's *with-profits insurance contracts*; and
    - (c) the *resilience capital requirement* in respect of the fund's *with-profits insurance contracts*.

#### Regulatory value of assets

- 7.4.24 R (1) For the purposes of *PRU 7.4.23R(1)*, the *regulatory value of assets* of a *with-profits fund* is equal to the sum of:
- (a) the amount of the fund's *long-term admissible assets*; and
  - (b) the amount of any *implicit items* allocated to that fund;
- less an amount, representing any *non-profit insurance contracts* written in that fund, determined in accordance with (2).
- (2) Where *non-profit insurance contracts* are written in a *with-profits fund*, the amount representing those contracts is the sum of:
- (a) the *mathematical reserves* in respect of the *non-profit insurance contracts* written in the fund; and
  - (b) the following amounts, to the extent that each of them is covered by the fund's *long-term admissible assets*:

- (i) an amount in respect of the *non-profit insurance contracts* written in the fund which represents an appropriate allocation of the *firm's long-term insurance capital requirement*; and
  - (ii) an amount in respect of the *non-profit insurance contracts* written in the fund which represents an appropriate allocation of the *firm's resilience capital requirement*.
- 7.4.25 R For the purpose of determining the value of a fund's *long-term admissible assets* in accordance with *PRU 7.4.24R(1)(a)*, no value is to be attributed to debts and claims other than in respect of:
- (1) amounts that have already fallen due; and
  - (2) tax recoveries and claims against *compensation funds* to the extent not already offset in the *mathematical reserves*.
- 7.4.26 R In making a determination in accordance with *PRU 7.4.24R(2)*, a *firm* must allocate *long-term admissible assets* of an appropriate nature and term to any *non-profit insurance contracts* written in the *with-profits fund*.
- 7.4.27 G In calculating the amount of a *firm's resilience capital requirement* allocated to the *non-profit insurance contracts* in the *with-profits fund*, the *firm* should calculate the amount of resilience capital that would be required if that business were in a standalone company owning the assets allocated. The *resilience capital requirement* for the *with-profits insurance business* should also be calculated as if it were a stand-alone company. An allocation of the *firm's total resilience capital requirement* should then be made in a manner that would produce a result materially consistent with an allocation in proportion to the amounts calculated for each part of the business as stand-alone entities.
- 7.4.28 G A *firm* needs to obtain an *implicit item waiver* from the *FSA* in order to bring in an amount under *PRU 7.4.24R(1)(b)*. For *guidance* on applying for an *implicit item waiver* in respect of future surpluses relating to *with-profits funds* see *PRU 2 Ann 2G*. The amount of any *implicit item* allocated to a *with-profits fund* may be defined in the terms of any *waiver* granted.

#### Regulatory value of liabilities

- 7.4.29 R For the purposes of *PRU 7.4.23R(2)(a)*, the *regulatory value of liabilities* of a *with-profits fund* is equal to the sum of:
- (1) the *mathematical reserves*, in respect of the fund's *with-profits insurance contracts*, including the value of any provisions reflecting bonuses allocated at the *actuarial valuation date*; and
  - (2) the *regulatory current liabilities* of the fund (see *PRU 7.4.30R*).

- 7.4.30 R For the purposes of *PRU 7.4.29R(2)*, the *regulatory current liabilities* of a *with-profits fund* are equal to the sum of the following amounts to the extent that they relate to that fund:
- (1) accounting liabilities (including *long-term insurance liabilities* which have fallen due before the end of the *financial year*);
  - (2) liabilities from *deposit back arrangements*; and
  - (3) any provision for adverse variations (determined in accordance with *PRU 4.3.17R*).

- 7.4.31 G The amount of *regulatory current liabilities* for a *with-profits fund* refers to the sum of the amounts in (1) and (2) in respect of the fund:
- (1) the amount of ‘Total other insurance and non-insurance liabilities’; and
  - (2) the amount of ‘Cash bonuses which had not been paid to *policyholders* prior to the end of the financial year’;

as disclosed at lines 49 and 12 respectively of the appropriate Form 14 (‘Long-term business liabilities and margins’) for that fund as part of the Annual Returns required to be deposited with the *FSA* under *IPRU(INS)* rule 9.6(1).

#### Calculation of realistic excess capital

- 7.4.32 R A *firm* must calculate the *realistic excess capital* for each of its *with-profits funds* by deducting B from A, where:
- (1) A is the *realistic value of assets* of the fund (see *PRU 7.4.33R*); and
  - (2) B is the sum of:
    - (a) the *realistic value of liabilities* of the fund (see *PRU 7.4.40R*); and
    - (b) the *risk capital margin* for the fund (see *PRU 7.4.43R*).

#### Realistic value of assets

- 7.4.33 R (1) For the purposes of *PRU 7.4.32R(1)*, the *realistic value of assets* of a *with-profits fund* is the sum of:
- (a) the amount of the fund’s *regulatory value of assets* determined in accordance with *PRU 7.4.24R*, but with no value given to any *implicit item* and excluding the regulatory value of any *shares* in a *related undertaking* which carries on *long-term insurance business*;
  - (b) the amount of the fund’s excess *admissible assets* (see *PRU 7.4.36R*);



- (c) the present value of future profits (or losses) on any *non-profit insurance contracts* written in the *with-profits fund* (see *PRU 7.4.37R*);
  - (d) the value of any *derivative* or *quasi-derivative* held in the fund (see *PRU 1.3.11R* to *PRU 1.3.30R*) to the extent its value is not reflected in (a), (b) or (c);
  - (e) any amount determined under (2); and
  - (f) the amount of any prepayments made from the fund.
- (2) Where any equity *shares* held (directly or indirectly) by a *firm* (A):
- (a) are *shares* in a *related undertaking* (B) which carries on *long-term insurance business*; and
  - (b) have been identified by A under *PRU 7.4.21R* as *long-term insurance assets* which are held in the *with-profits fund* for which the realistic value is to be determined under (1);

the amount required under (1)(e) is the relevant proportion of the value of all B's equity *shares* as determined in (3).

- (3) For the purposes of (2):
- (a) the relevant proportion is the proportion of the total number of equity *shares* issued by B which are held (directly or indirectly) by A;
  - (b) the value of all B's equity *shares* must be taken as D deducted from C, where C is equal to the sum of:
    - (i) the shareholder net assets of B;
    - (ii) any surplus assets in the *non-profit funds* of B;
    - (iii) any additional amount arising from the excess of the present value of future profits (or losses) on any *non-profit insurance contracts* written by B (calculated on a basis consistent with *PRU 7.4.37R*), excluding any amount arising from business that is written in a *with-profits fund*, over any present value of future profits (or losses) used in calculating B's regulatory capital requirements and arising from business outside its *with-profits funds*; and
    - (iv) where B has any *with-profits funds*, the present value of projected future transfers out of those funds to shareholder funds of B;

and D is equal to the sum of:

- (v) the *long-term insurance capital requirement* in respect of any *non-profit insurance contracts* written in a *non-profit fund* of B;
  - (vi) the amount of the *resilience capital requirement* in respect of any *non-profit insurance contracts* written in a *non-profit fund* of B;
  - (vii) any part of the *with-profits insurance capital component* of B, to the extent that this is not covered from the assets of the *with-profits fund* from which it arises after deducting from those assets the amount calculated under (iv); and
  - (viii) any assets of B that back its regulatory capital requirements and that are valued in (iii) in the calculation of the present value of future profits of *non-profit insurance business* written by B.
- (4) The methods and assumptions used in the calculations under (3)(b)(iii) and (iv) must follow a consistent approach to that set out in *PRU 7.4.37R*.
- 7.4.34 G In *PRU 7.4.33R(1)(d)*, where a *derivative* or *quasi-derivative* has a positive asset value, credit should be given within the *realistic value of assets*. If the *derivative* or *quasi-derivative* has a negative asset value it should be valued within realistic liabilities as an element of *realistic current liabilities* (see *PRU 7.4.40R(3)*).
- 7.4.35 G Where a *firm* identifies *shares* in a *related undertaking* which carries on *long-term insurance business* as *shares* held in one of its *with-profits funds*, *PRU 7.4.33R(1)(e)*, (2) and (3) brings in a realistic valuation of the *related undertaking* equal to its net assets plus the present value of future profits, less its regulatory capital requirements (see *PRU 7.4.33R(3)(v)*, (vi) and (vii)). Where the *related undertaking* has taken the present value of future profits arising from its contracts into consideration in covering its regulatory capital requirements (for example, its *risk capital margin*, under *PRU 7.4.45R(2)(c)*), *PRU 7.4.33R(3)(b)(iii)* requires a *firm* to exclude those future profits in valuing the *related undertaking*. The subtraction of the capital requirements in the calculation provides a straightforward method of allowing for the change in the *related undertaking's* value in stress conditions, as the value of the *related undertaking* is not subject to the realistic stress tests of the *risk capital margin*. In calculating the present value of future profits on *non-profit insurance business* written in the *related undertaking* under *PRU 7.4.33R(3)(b)(iii)*, a *firm* may value the release of capital requirements as the business runs off (see *PRU 7.4.38G*). *PRU 7.4.33R(3)(b)(viii)* ensures that any such capital is not double-counted.
- 7.4.36 R Excess *admissible assets* of a *with-profits fund* means *admissible assets* which exceed any of the percentage limits referred to in *PRU 3.2.22R*.
- 7.4.37 R A *firm* must calculate the present value of future profits (or losses) on *non-profit insurance contracts* written in the *with-profits fund* using methodology and assumptions which:
- (1) are based on current estimates of future experience;

- (2) involve reasonable (but not excessively prudent) adjustments to reflect risk and uncertainty;
- (3) allow for a market-consistent valuation of any guarantees or options within the contracts valued;
- (4) are derived from current market yields;
- (5) have regard to generally accepted actuarial practice and generally accepted industry standards appropriate for *firms* carrying on *long-term insurance business*;
- (6) are consistent with the allocation, made in accordance with *PRU 7.4.22R*, of any aggregate amounts as between the *with-profits insurance contracts* and the *non-profit insurance contracts* written in the fund;
- (7) allow for any tax that would be payable out of the *with-profits fund* in respect of the contracts valued; and
- (8) are consistent with the allocation, made in accordance with *PRU 7.4.26R*, of *long-term admissible assets* as between the *with-profits insurance contracts* and any *non-profit insurance contracts* written in the fund.

7.4.38 G In calculating the present value of future profits (or losses) for *non-profit insurance business* required by *PRU 7.4.33R(1)(c)*, to the extent that the *long-term insurance capital requirement* and the *resilience capital requirement* are covered by the *with-profits fund's long-term admissible assets*, a *firm* may take into consideration any release of these items as the relevant *policies* go off the books.

7.4.39 G Annuities do not typically fall to be valued on a market-consistent basis under *PRU 7.4.37R(3)* as they are not "options and guarantees" as defined for accounting purposes. This is because they do not have "time value" in the option-pricing meaning of that term. However where, atypically, annuities do fall to be valued on a market-consistent basis under *PRU 7.4.37R(3)*, the discount rate used should be appropriate to the characteristics of the liability, including its illiquidity. The appropriate interest rate, therefore, would not typically be the risk-free rate. Where illiquid assets are used to closely match similar illiquid liabilities, as could be the case in annuities business, it would be appropriate to look at the liquidity premium that is implicit in the market value of the assets as a proxy for the liquidity premium that should be included in a market consistent valuation of the liabilities. However, care should be exercised in doing this. Assets and liabilities are rarely perfectly matched and an appropriate margin needs to be included in the valuation to cover the risk of unexpected mismatch.

#### Realistic value of liabilities: general

7.4.40 R For the purposes of *PRU 7.4.32R(2)(a)*, the *realistic value of liabilities* of a *with-profits fund* is the sum of:

- (1) the *with-profits benefits reserve* of the fund;
- (2) the *future policy related liabilities* of the fund; and
- (3) the *realistic current liabilities* of the fund.

7.4.41 G All liabilities arising under, or in connection with, *with-profits insurance contracts* written in the fund should be included in the *realistic value of liabilities* referred to in *PRU 7.4.40R*, including those in respect of guarantees and the value of options.

7.4.42 G Detailed *rules and guidance* for the calculation of the three elements referred to in *PRU 7.4.40R* are contained below in this section:

- (1) *PRU 7.4.116R* to *PRU 7.4.135G* refer to the *with-profits benefits reserve*;
- (2) *PRU 7.4.136G* to *PRU 7.4.189G* refer to the *future policy related liabilities*; and
- (3) *PRU 7.4.190R* and *PRU 7.4.191R* refer to the *realistic current liabilities*.

#### Risk capital margin

- 7.4.43 R
- (1) A *firm* must calculate a *risk capital margin* for each of its *with-profits funds* in accordance with (2) to (6).
  - (2) The *firm* must identify relevant assets (see *PRU 7.4.45R*) which, in the most adverse scenario, will have a value (see *PRU 7.4.46R*) which is equal to the *realistic value of liabilities* of the fund under that scenario.
  - (3) The most adverse scenario means the single event comprising that combination of the scenarios in *PRU 7.4.44R* which gives rise to the largest positive value that results from deducting B from A, where:
    - (a) A is the value of relevant assets which will produce the result described in (2); and
    - (b) B is the *realistic value of liabilities* of the fund.
  - (4) The *risk capital margin* for the fund is the result of deducting C from A, where C is the sum of:
    - (a) B; and
    - (b) any amount included within relevant assets under *PRU 7.4.45R(2)(c)*.

- (5) In calculating the value of relevant assets for the purpose of determining the most adverse scenario in (3), a *firm* must not adjust the valuation of any asset taken into consideration under *PRU 7.4.33R(1)(e) (related undertakings carrying on long-term insurance business)* or *PRU 7.4.45R(2)(c) (present value of future profits arising from insurance contracts written outside the with-profits fund)*.
- (6) In calculating the *realistic value of liabilities* of a fund under any scenario, a *firm* is not required to adjust the best estimate provision made under *PRU 7.4.190R(1)* in respect of a *defined benefits pension scheme* in accordance with *PRU 7.4.191R*.

7.4.44 R For the purposes of *PRU 7.4.43R(3)*, the scenarios are one scenario selected from each of the following:

- (1) in respect of *UK* and other assets within *PRU 7.4.62R(1)(a)*:
  - (a) the range of *market risk* scenarios identified in accordance with *PRU 7.4.68R(1)* (equities);
  - (b) the range of *market risk* scenarios identified in accordance with *PRU 7.4.68R(2)* (real estate); and
  - (c) the range of *market risk* scenarios identified in accordance with *PRU 7.4.68R(3)* (fixed interest securities);
- (2) in respect of non-*UK* assets within *PRU 7.4.62R(1)(b)*:
  - (a) the range of *market risk* scenarios identified in accordance with *PRU 7.4.73R(1)* (equities);
  - (b) the range of *market risk* scenarios identified in accordance with *PRU 7.4.73R(2)* (real estate); and
  - (c) the range of *market risk* scenarios identified in accordance with *PRU 7.4.73R(3)* (fixed interest securities);
- (3) the range of credit risk scenarios identified in accordance with *PRU 7.4.78R(1)* (bond or debt items);
- (4) the range of credit risk scenarios identified in accordance with *PRU 7.4.78R(2)* (*reinsurance* items or analogous non-*reinsurance* financing agreements);
- (5) the range of credit risk scenarios identified in accordance with *PRU 7.4.78R(3)* (other items including *derivatives* and *quasi-derivatives*); and
- (6) the persistency risk scenario identified in accordance with *PRU 7.4.100R*.

- 7.4.45 R (1) In *PRU 7.4.43R*, in relation to a *with-profits fund*, the relevant assets means a range of assets which meets the following conditions:
- (a) the range is selected on a basis which is consistent with the *firm's* regulatory duty to treat its *customers* fairly;
  - (b) the range must include assets from within the *with-profits fund* the value of which is greater than or equal to the *realistic value of liabilities* of the fund;
  - (c) the range is selected in accordance with (2); and
  - (d) no asset of the *firm* may be allocated to the range of assets identified in respect of more than one *with-profits fund*.
- (2) The range of assets must be selected from the assets specified in (a) to (c), in the order specified:
- (a) assets that have a realistic value under *PRU 7.4.33R*;
  - (b) where a *firm* has selected all the assets within (a), any *admissible assets* that are not identified as held within the *with-profits fund*; and
  - (c) where a *firm* has selected all the assets within (a) and (b), any additional assets.
- (3) But a *firm* must not bring any amounts into account under (2)(b) or (2)(c) in respect of any *with-profits fund* if that would result in the *firm* exceeding its overall maximum limit (determined according to whether the *firm* has only one *with-profits fund* or more than one such fund).
- (4) A *firm* exceeds its overall maximum limit for amounts brought into account under (2)(b) where:
- (a) in the case of a *firm* with a single *with-profits fund*, the amount the *firm* brings into account in respect of that fund;
  - (b) in the case of a *firm* with two or more *with-profits funds*, the aggregate of the amounts the *firm* brings into account in respect of each of those funds;
- exceeds the sum of the *firm's* shareholder net assets and the surplus assets in the *firm's non-profits funds*, less any regulatory capital requirements in respect of business written outside its *with-profits funds*.
- (5) A *firm* exceeds its overall maximum limit for amounts brought into account under (2)(c) where:

- (a) in the case of a *firm* with a single *with-profits fund*, the amount the *firm* brings into account in respect of that fund;
- (b) in the case of a *firm* with two or more *with-profits funds*, the aggregate of the amounts the *firm* brings into account in respect of each of those funds;

exceeds 50% of the present value of future profits arising from *insurance contracts* written by the *firm* outside its *with-profits funds*.

- 7.4.46 R In valuing the relevant assets identified under *PRU 7.4.43R(2)*, a *firm* must use the same methods of valuation as in *PRU 7.4.33R*, except that:
- (1) the value of any *admissible assets* not identified as held within the *with-profits fund* (see *PRU 7.4.45R(2)(b)*) must be as determined under *PRU 1.3*; and
  - (2) the value of any asset which forms part of the range of assets as a result of *PRU 7.4.45R(2)(c)* must be determined on a basis consistent with that described in *PRU 7.4.37R*.
- 7.4.47 G The purpose of the *risk capital margin* for a *with-profits fund* is to cover adverse deviation from:
- (1) the fund's *realistic value of liabilities*;
  - (2) the value of assets identified, in accordance with *PRU 7.4.43R(2)*, to cover the amount in (1) and the fund's *risk capital margin*;
- arising from the effects of *market risk*, credit risk and persistency risk. Other risks are not explicitly addressed by the *risk capital margin*.
- 7.4.48 G The amount of the *risk capital margin* calculated by the *firm* for a *with-profits fund* will depend on the *firm*'s choice of assets held to cover the fund's *realistic value of liabilities* and the margin. *PRU 7.4.43R* requires the relevant assets to be sufficient, in the most adverse scenario, to cover the *realistic value of liabilities* in the event that scenario was to arise.

- 7.4.49 G *PRU 7.4.45R(2)(c)* allows *firms* to bring the economic value of *non-profit insurance business* written outside a *with-profits fund* into the assets available to cover the *risk capital margin*. To place a prudent limit on the amount of future profits taken into consideration a maximum of 50% of the present value of *non-profit insurance business* can be taken into the calculation (*PRU 7.4.45R(5)*). Where a contract is written in a *non-profit fund* but the assets arising from that contract are invested in a *with-profits fund* which is subject to charges for investment management or other services which benefit the *non-profit fund*, such charges can be taken into consideration in calculating the present value of future profits of the *non-profit insurance business*. Where a proportion of the present value of future profits on *non-profit insurance business* written outside a *with-profits fund* is brought in as an asset, no stress tests apply to this asset (see *PRU 7.4.43R(5)*) as the amount taken into consideration is limited to 50% of the total present value.
- 7.4.50 G A *firm* using a stochastic approach in *PRU 7.4.169R(1)* should keep recalibration in the post-stress scenarios to the minimum required to reflect any change in the underlying risk-free yields. A *firm* using the market costs of hedging approach, as in *PRU 7.4.169R(2)*, may assume in estimating the market cost of hedging in the post-stress scenarios that market volatilities are unchanged.
- 7.4.51 G In the scenario tests set out in *PRU 7.4.62R* to *PRU 7.4.103G*, *firms* are required to test for worst case scenarios across a range of assumptions. The tests are, with the exception of the credit risk test, two-sided, requiring both increases and decreases in the assumptions. The *FSA* does not expect a *firm* to investigate every possible stress, but a *firm* should be able to demonstrate that it is reasonable to assume that it has successfully identified the single event that determines the *risk capital margin* for the *firm's* business, as required by *PRU 7.4.43R(3)*.

#### Management actions

- 7.4.52 R In calculating the *risk capital margin* for a *with-profits fund*, a *firm* may reflect, in its projections of the value of assets and liabilities under the scenarios in *PRU 7.4.44R*, the *firm's* prospective management actions (see *PRU 7.4.53R*).
- 7.4.53 R Prospective management actions refer to the foreseeable actions that would be taken by the *firm's* management, taking into account:
- (1) an appropriately realistic period of time for the management actions to take effect; and
  - (2) the *firm's* *PPFM* and its regulatory duty to treat its *customers* fairly.
- 7.4.54 G The management actions in *PRU 7.4.53R* may include, but are not limited to, changes in future bonus rates, reductions in *surrender values*, changes in asset dispositions (taking into account the associated selling costs) and changes in the amount of charges deducted from asset shares for *with-profits insurance contracts*.



- 7.4.55 G A *firm* should use reasonable assumptions in incorporating management actions into its projections of *claims* such that the mitigating effects of the management actions are not overstated. In modelling management actions, a *firm* should ensure consistency with its *PPFM* and take into account its regulatory duty to treat its *customers* fairly.
- 7.4.56 G In accordance with *PRU 7.4.17R*, a *firm* should make and retain a record of the approach used, in particular the nature and effect of anticipated management actions (including, where practicable, the amount by which the actions would serve to reduce the projected values of assets and liabilities).
- 7.4.57 G A *firm* which deducts charges in respect of any adverse experience or cost of capital to *with-profits insurance contracts* should keep a record under *PRU 7.4.17R* of the amount of any such charges to its *customers* and of how it has ensured their fair treatment.

#### Policyholder actions

- 7.4.58 R In calculating the *risk capital margin* for a *with-profits fund*, a *firm* must reflect, in its projections of the value of assets and liabilities under the scenarios in *PRU 7.4.44R*, a realistic assessment of the actions of its *policyholders* (see *PRU 7.4.59R*).
- 7.4.59 R *Policyholder* actions refer to the foreseeable actions that would be taken by the *firm's policyholders*, taking into account:
- (1) the experience of the *firm* in the past; and
  - (2) the changes that may occur in the future if options and guarantees become more valuable to *policyholders* than in the past.
- 7.4.60 G A *firm* should use realistic assumptions in incorporating *policyholder* actions into its projections of *claims* such that any mitigating effects of *policyholder* actions are not overstated and any exacerbating effects of *policyholder* actions are not understated. In modelling *policyholder* actions, a *firm* should ensure consistency with its *PPFM* and take into account its regulatory duty to treat its *customers* fairly in determining the options and information that would be available to *policyholders*.
- 7.4.61 G In calculating the persistency scenario in *PRU 7.4.100R*, a *firm* needs to make assumptions regarding the future termination rates exhibited by *policies*, at points described in particular in *PRU 7.4.101R*. Such assumptions should be realistic. However, the *firm* must have regard to the economic scenarios being projected. For example, if the value of an option became significantly greater in a future scenario than in the recent past, then the behaviour of *policyholders* in taking up the option is likely to differ in this future scenario compared with the recent past.

#### Market risk scenario

- 7.4.62 R (1) For the purposes of *PRU 7.4.44R*, the ranges of *market risk* scenarios that a *firm* must assume are:
- (a) for exposures to *UK* assets and for exposures to non-*UK* assets within (2), the ranges of scenarios set out in *PRU 7.4.68R*; and
  - (b) for exposures to other non-*UK* assets, the ranges of scenarios set out in *PRU 7.4.73R*.
- (2) The exposures to non-*UK* assets within this paragraph are:
- (a) exposures which do not arise from a significant territory outside the *United Kingdom* (see *PRU 7.4.63R*); or
  - (b) exposures which do arise from a significant territory outside the *United Kingdom* but which represent less than 0.5% of the *realistic value of assets* of the *with-profits fund*, measured by *market value*.
- 7.4.63 R For the purposes of this section in relation to a *with-profits fund*, a significant territory is any country or territory in which more than 2.5% of the fund's *realistic value of assets* (by *market value*) are invested.
- 7.4.64 G In determining its most adverse scenario, a *firm* applying *PRU 7.4.68R* and *PRU 7.4.73R* should consider separately possible movements in *UK* and non-*UK* markets. It should not assume that market prices in different markets move in a similar way at the same time. A *firm* should also allow for the effect of the other components of the single event comprising the combination of scenarios applicable under *PRU 7.4.43R*.
- 7.4.65 G In relation to the *market risk* scenarios in *PRU 7.4.68R* and *PRU 7.4.73R*, the effect of *PRU 7.4.52R* and *PRU 7.4.58R* is that a *firm* may reflect management actions and must make a realistic assessment of *policyholder* actions in projecting the assets and liabilities in its calculation of the *risk capital margin* for a *with-profits fund* within the *firm*. This contrasts with the position for calculating the *resilience capital requirement* for the *firm* (see *PRU 4.2.9G* to *PRU 4.2.26R*).
- 7.4.66 G In *PRU 7.4.62R* to *PRU 7.4.76G*, where there is reference to exposure to assets invested in a territory this should be interpreted as follows:
- (1) for equities, a stock that is listed on a stock market in that territory or, if unlisted, the stock of a *company* that is incorporated in that territory;
  - (2) for bonds, one that is denominated in the currency of that territory, or issued by an institution incorporated in that territory;
  - (3) for real estate, a property that is located in that territory; and

- (4) for *derivatives, quasi-derivatives* and other instruments, one where the assets to which the instrument is exposed are assets invested in that territory.

In *PRU 7.4.62R* to *PRU 7.4.76G*, a *preference share* should be subjected to the same stress tests as an equity share.

- 7.4.67 G The relevant assets identified under *PRU 7.4.43R(2)* to calculate the *risk capital margin* may, in certain circumstances, include up to 50% of the present value of future profits arising from *insurance contracts* written by the *firm* outside its *with-profits funds*. *PRU 7.4.43R(5)* exempts such an asset from the *market risk* stress tests.

Market risk scenario for exposures to UK assets and certain non-UK assets

- 7.4.68 R The range of *market risk* scenarios referred to in *PRU 7.4.62R(1)(a)* is:
- (1) a rise or fall in the *market value* of equities of up to the greater of:
    - (a) 10%; and
    - (b) 20%, less the *equity market adjustment ratio* (see *PRU 7.4.71R*);
  - (2) a rise or fall in real estate values of up to 12.5%; and
  - (3) a rise or fall in yields on all fixed interest securities of up to 17.5% of the long-term gilt yield.

- 7.4.69 R For the purposes of *PRU 7.4.68R*, a *firm* must:
- (1) assume that yields on equities and real estate remain unchanged from those applicable at market levels before applying each scenario; and
  - (2) model a rise or fall in equity, real estate and fixed interest markets as if the movement occurred instantaneously.

- 7.4.70 G For example, where the long-term gilt yield is 6%, a change of 17.5% in that yield would amount to a change of 1.05 percentage points. For the purpose of the scenarios in *PRU 7.4.68R(3)*, the *firm* would assume a fall or rise of up to 1.05 percentage points in yields on all fixed interest securities.

Equity market adjustment ratio

- 7.4.71 R The equity market adjustment ratio referred to in *PRU 7.4.68R(1)(b)* is:
- (1) if the ratio calculated in (a) and (b) lies between 80% and 100%, the result of 100% less the ratio (expressed as a percentage) of:
    - (a) the current value of the FTSE Actuaries All Share Index; to

- (b) the average value of the FTSE Actuaries All Share Index over the preceding 90 calendar days;
  - (2) 0%, if the ratio calculated in (1)(a) and (b) is more than 100%; and
  - (3) 20%, if the ratio calculated in (1)(a) and (b) is less than 80%.
- 7.4.72 R In *PRU 7.4.71R(1)(b)*, the average value of the FTSE Actuaries All Share Index over any period of 90 calendar days means the arithmetic mean based on levels at the close of business on each of the days in that period on which the London Stock Exchange was open for trading.
- Market risk scenario for exposures to other non-UK assets
- 7.4.73 R The range of *market risk* scenarios referred to in *PRU 7.4.62R(1)(b)* is:
- (1) an appropriate rise or fall in the *market value* of equities listed in that territory (see *PRU 7.4.75R*), which must be at least equal to the percentage determined in *PRU 7.4.68R(1)*;
  - (2) a rise or fall in real estate values in that territory of up to 12.5%; and
  - (3) a rise or fall in yields on all fixed interest securities of up to 17.5% of the nearest equivalent (in respect of the method of calculation) of the long-term gilt yield.
- 7.4.74 R For the purposes of *PRU 7.4.73R*, a *firm* must:
- (1) assume that yields on equities and real estate remain unchanged from those applicable at market levels before applying each scenario; and
  - (2) model a rise or fall in equity, real estate and fixed interest markets as if the movement occurred instantaneously.
- 7.4.75 R For the purposes of *PRU 7.4.73R(1)*, an appropriate rise or fall in the *market value* of equities to which a *firm* has exposure in a significant territory must be determined having regard to:
- (1) an appropriate equity market index (or indices) for that territory; and
  - (2) the historical volatility of the equity market index (or indices) selected in (1).
- 7.4.76 G For the purpose of *PRU 7.4.75R(1)*, an appropriate equity market index (or indices) for a territory should be such that:

- (1) the constituents of the index (or indices) are reasonably representative of the nature of the equities to which the *firm* is exposed in that territory which are included in the relevant assets identified in accordance with *PRU* 7.4.43R(2); and
- (2) the frequency of, and historical data relating to, published values of the index (or indices) are sufficient to enable an average value(s) and historical volatility of the index (or indices) to be calculated over at least the three preceding *financial years*.

#### Credit risk scenarios

##### General

- 7.4.77 G (1) The purpose of the credit risk scenarios in *PRU* 7.4.78R to *PRU* 7.4.99G is to show the financial effect of specified changes in the general credit risk environment on a *firm*'s direct (*counterparty*) and indirect credit risk exposures. The scenarios apply in relation to corporate bonds, debt, *reinsurance* and other exposures, including *derivatives* and *quasi-derivatives*. This is thus quite separate from any reference to allowance for credit risk in *PRU* 4.2.
- (2) In the case of bonds and debts, the scenarios are described in terms of an assumed credit rating dependent on the widening of credit spreads - changes in bond and debt credit spreads will have a direct impact on the value of bond and debt assets. Credit ratings are intended to give an indication of the security of the income and capital payments for a bond – the higher the credit rating, the more secure the payments. The reaction of credit spreads to developments in markets for credit risk varies by credit rating and so the scenarios to be assumed for bonds and debts depend on their ratings. The credit spreads on bonds and debt represent compensation to the investor for the risk of default and downgrade, but also for illiquidity, price volatility and the uncertainty of recovery rates relative to government bonds. Credit spreads on bonds tend to widen during an economic recession to reflect the increased expectations that corporate borrowers may default on their obligations or be subject to rating downgrades.
  - (3) Changes in bond and debt credit spreads will also be indicative of a change in direct *counterparty* exposure in relation to *reinsurance* and other exposures including *derivatives* and *quasi-derivatives*.
  - (4) In addition, changes in bond and debt credit spreads may indirectly impact on credit exposures, for example by affecting the payments anticipated under credit *derivative* instruments.

- (5) A *firm* will also need to allow for the effect of other components of the single event comprising the combination of scenarios applicable under *PRU 7.4.43R* in assessing exposure to credit risk. For example, in the case of an equity put *option* and a fall in equity market values, the resulting increase in the level of exposure to the *firm's counterparty* for the *option* combined with a change in the quality of the *counterparty* should be allowed for.
- 7.4.78 R For the purposes of *PRU 7.4.44R*, the range of credit risk scenarios that a *firm* must assume is:
- (1) changes in value resulting from an increase in credit spreads by an amount of up to the spread stress determined according to *PRU 7.4.84R* in respect of any bond or debt item;
  - (2) changes in value determined according to *PRU 7.4.94R* in respect of any *reinsurance* item or any analogous non-*reinsurance* financing agreement item; and
  - (3) changes in value determined according to *PRU 7.4.98R* for any other item (including any *derivative* or *quasi-derivative*).
- 7.4.79 R For the purposes of *PRU 7.4.78R*, a *firm* must make appropriate allowance for any loss mitigation techniques to the extent that they are loss mitigation techniques relied on for the purpose of *PRU 3.2.8R* in accordance with *PRU 3.2.16R* and *PRU 3.2.18R*.
- 7.4.80 G The change in asset or liability values to be determined in relation to a credit risk scenario for the purposes of *PRU 7.4.43R* and *PRU 7.4.44R* is the change in value which would arise on the occurrence of the relevant credit risk scenario as a result of bond, debt, *reinsurance* or other exposures whether or not there is a direct *counterparty* exposure.
- 7.4.81 R Where a bond or a debt item or *reinsurance* asset is currently in default, it may be ignored by a *firm* for the purpose of applying *PRU 7.4.78R*.
- 7.4.82 G Where a bond or a debt item or a *reinsurance* asset is currently in default and has been specifically provisioned, in accordance with relevant accounting standards, a *firm* is not required to increase the existing default provisions to reflect a worsening of recovery rates.
- 7.4.83 R Where the credit risk scenarios in *PRU 7.4.78R* to *PRU 7.4.99G* require a *firm* to assume a change in current credit spread, or a direct change in market value, the *firm* must not change the risk-free yields used to discount future cash flows in calculating the revised *realistic value of liabilities* and *realistic value of assets* (see *PRU 7.4.43R(2)*) resulting from those credit risk scenarios.

Spread stresses to be assumed for bonds and debt

- 7.4.84 R (1) In *PRU 7.4.78R*(1) the spread stress which a *firm* must assume for any bond or debt item is:
- (a) for any bond or debt item issued or guaranteed by an organisation which is in accordance with *PRU 7.4.87R* a credit risk scenario exempt organisation in respect of that item, zero basis points; and
  - (b) for any other bond or debt item:
    - (i) Y if the credit rating description of that other bond or debt item determined by reference to *PRU 7.4.89R* is not "Highly speculative or very vulnerable"; and
    - (ii) otherwise the larger of Y and Z.
- (2) For the purpose of (1)(b):
- (a) Y is the product of the spread factor for that bond or debt item and the square root of S, where:
    - (i) the spread factor for a bond or debt item is the spread factor shown in the final column of Table *PRU 7.4.90R*, in the row of that Table corresponding to the credit rating description of the bond or debt item determined for the purpose of this *rule* by reference to *PRU 7.4.89R*; and
    - (ii) subject to (3), S is the current credit spread for a bond or debt item, expressed as a number of basis points, which the *firm* must determine as the current yield on that bond or debt item in excess of the current gross redemption yield on the government bond most similar to that bond or debt item in terms of currency of denomination and equivalent term; and
  - (b) Z is the change in credit spread expressed as a number of basis points that would result in the current market value of the bond or debt falling by 5%.
- (3) Where, for the purposes of (2)(a)(ii), there is no suitable government bond, the *firm* must use its best estimate of the gross redemption yield that would apply for a notional government bond similar to the bond or debt item in terms of currency of denomination and equivalent term.
- 7.4.85 R For the purpose of *PRU 7.4.84R*(1)(a), a guarantee must be direct, explicit, unconditional and irrevocable.

- 7.4.86 G (1) As an example, a bond item has the credit rating description "exceptional or extremely strong" and currently yields 49 basis points in excess of the most similar government bond. The spread factor for that bond item is 3.00 by reference to Table *PRU 7.4.90R*. Since S is 49, the square root of S is 7 and the spread stress for that item is 3 times 7, that is, 21 basis points. The *firm* must consider the impact of an increase in spreads by up to 21 basis points for that item.
- (2) As a further example, a bond item has the credit rating description "highly speculative or very vulnerable". For this bond, S is 400, being the current spread for that bond expressed as a number of basis points. The spread factor for the bond is 24.00. So the *firm* must consider the impact of an increase in spreads by up to 24.00 times 20 i.e. 480 basis points for that item. The bond is however of short duration and the reduction in market value resulting from an additional spread of 480 basis points is less than 5 per cent of its current market value. A 5 per cent reduction in its market value would result from a spread widening of 525 basis points. The *firm* must consider the impact of an increase in spreads by up to 525 basis points for that item by virtue of its credit rating description.
- (3) The calculation of the credit spread on commercial floating rate notes warrants particular consideration. Suppose, for example, that a notional floating rate note guaranteed by the *UK* government would have a market consistent price of X. This price can be estimated based on an assumed distribution of future payments under the floating rate note, and the current forward gilt curve. Suppose further that the market price of the commercial floating rate note is Y, where Y is less than X. A *firm* could calculate what parallel upward shift in the forward gilt curve would result in the notional government-backed floating rate note having a market price of Y for an unchanged assumed distribution of future payments. The size of the resulting shift could then be taken as the credit spread on the commercial floating rate note.
- (4) In arriving at the estimated gross redemption yield in *PRU 7.4.84R(3)*, the *firm* may have regard to any appropriate swap rates for the currency of denomination of the bond or debt item, adjusted to take appropriate account of observed differences between swap rates and the yields on government bonds.

7.4.87 R For the purposes of this section:

- (1) an organisation is a credit risk scenario exempt organisation in respect of an item if the organisation is:
- (a) the European Central Bank; or
  - (b) any central government or central bank which, in relation to that item, satisfies the conditions in (2); or



- (c) a multilateral development bank which is listed in (3); or
  - (d) an international organisation which is listed in (4);
- (2) the conditions in (1)(b) are that, for any claim against the central government or central bank denominated in the currency in which the item is denominated:
- (a) a credit rating is available from at least one listed rating agency nominated in accordance with *PRU 7.4.92R*; and
  - (b) the credit rating description in the first column of Table *PRU 7.4.90R* corresponding to the lowest such credit rating is either "exceptionally or extremely strong" or "very strong";
- (3) for the purposes of (1)(c) the listed multilateral development banks are:
- (a) the International Bank for Reconstruction and Development;
  - (b) the International Finance Corporation;
  - (c) the Inter-American Development Bank;
  - (d) the Asian Development Bank;
  - (e) the African Development Bank;
  - (f) the Council of Europe Development Bank;
  - (g) the Nordic Investment Bank;
  - (h) the Caribbean Development Bank;
  - (i) the European Bank for Reconstruction and Development;
  - (j) the European Investment Bank; and
  - (k) the European Investment Fund;
  - (l) the Multilateral Investment Guarantee Agency;
- (4) for the purposes of (1)(d) the listed international organisations are:
- (a) the European Community;
  - (b) the International Monetary Fund; and
  - (c) the Bank for International Settlements.

7.4.88 G Under *PRU 7.4.87R(2)*, a *firm* needs to take account of the currency in which the claim is denominated when it is considering claims on or guaranteed by a central government or central bank. It is possible, for example, that a given central bank would be a credit risk scenario exempt organisation in respect of claims on it denominated in its domestic currency, while not being a credit risk scenario exempt organisation in respect of claims on it denominated in a currency other than its domestic currency – the central government or central bank may have been assigned different credit assessments depending on the currency in which the claim on it is denominated.

- 7.4.89 R (1) For the purposes of this section, the credit rating description of a bond or debt item is to be determined in accordance with (2) and (3).
- (2) If the item has at least one credit rating nominated in accordance with *PRU 7.4.92R* ("a rated item"), its credit rating description is:
- (a) where it has only one nominated credit rating, the general description given in the first column of Table *PRU 7.4.90R* corresponding to that rating; or
  - (b) where it has two or more nominated credit ratings and the two highest nominated ratings fall within the same general description given in the first column of that Table, that description; or
  - (c) where it has two or more nominated credit ratings and the two highest nominated ratings do not fall within the same general description given in the first column of that Table, the second highest of those two descriptions.
- (3) If the item is not a rated item, its credit rating description is the general description given in the first column of Table *PRU 7.4.90R* that most closely corresponds to the *firm's* own assessment of the item's credit quality.
- (4) An assessment under (3) must be made by the *firm* for the purposes of the credit risk scenario having due regard to the seniority of the bond or debt and the credit quality of the bond or debt issuer.

7.4.90 R Table : Listed rating agencies, credit rating descriptions, spread factors

Credit Rating Description	Listed rating agencies				Spread Factor
	A.M. Best Company	Fitch Ratings	Moody's Investors Service	Standard & Poor's Corporation	
Exceptional or extremely strong	aaa	AAA	Aaa	AAA	3.00
Very strong	aa	AA	Aa	AA	5.25
Strong	a	A	A	A	6.75
Adequate	bbb	BBB	Baa	BBB	9.25

Speculative or less vulnerable	bb	BB	Ba	BB	15.00
Very speculative or more vulnerable	b	B	B	B	24.00
Highly speculative or very vulnerable	Below b	Below B	Below B	Below B	24.00

- 7.4.91 G Where listed rating agencies provide ratings by sub-category then all ratings should be allocated to the main ratings category (e.g. ratings sub-category A+ or A- would be allocated to the assigned ratings category "Strong").
- 7.4.92 R For the purposes of *PRU 7.4.87R* and *PRU 7.4.89R*, a *firm* may, subject to (1) to (5), nominate for use credit ratings produced by one or more of the rating agencies listed in *PRU 7.4.93R*:
- (1) if the *firm* decides to nominate for use for an item the credit rating produced by one or more rating agencies, it must do so consistently for all similar items;
  - (2) the *firm* must use credit ratings in a continuous and consistent way over time;
  - (3) the *firm* must nominate for use only credit ratings that take into account both principal and interest;
  - (4) if the *firm* nominates for use credit ratings produced by one of the listed rating agencies then the *firm* must use solicited credit ratings produced by that listed rating agency; and
  - (5) the *firm* may nominate for use unsolicited credit ratings produced by one or more of the listed rating agencies except where there are reasonable grounds for believing that any unsolicited credit ratings produced by the agency are used so as to obtain inappropriate advantages in the relationship with rated parties.
- 7.4.93 R In this section, a listed rating agency is:
- (1) A.M. Best Company; or
  - (2) Fitch Ratings; or
  - (3) Moody's Investors Service; or
  - (4) Standard & Poor's Corporation.

Credit risk scenario for reinsurance

- 7.4.94 R (1) The contracts of *reinsurance* or analogous non-*reinsurance* financing agreements to which *PRU 7.4.78R(2)* applies are those:
- (a) into which the *firm* has entered;
  - (b) which represent an economic asset under the single event applicable under *PRU 7.4.43R(3)*; and
  - (c) which are material (individually or in aggregate).
- (2) For the purposes of (1), no account is to be taken of *reinsurance* or analogous non-*reinsurance* financing arrangements between *undertakings* in the same *group* where:
- (a) the ceding and accepting *undertakings* are regulated by the *FSA* or a regulatory body in a *designated State or territory* for insurance (including *reinsurance*);
  - (b) no subsequent cessions of the ceded risk which are material (individually or in aggregate) are made to subsequent accepting *undertakings* by accepting *undertakings* (including subsequent accepting *undertakings*) other than to subsequent accepting *undertakings* which are in the same *group*; and
  - (c) for any subsequent cession or cessions of the ceded risk which are material (individually or in aggregate) each of the ceding and accepting *undertakings* (including subsequent accepting *undertakings*) is regulated by the *FSA* or a regulatory body in a *designated State or territory* for insurance (including *reinsurance*).
- (3) The change in value which a *firm* must determine for a contract of *reinsurance* or an analogous non-*reinsurance* financing agreement is the *firm's* best estimate of the change in realistic value which would result from changes in credit risk market conditions consistent, subject to (4), with the changes in credit spreads determined in accordance with *PRU 7.4.78R(1)*.
- (4) For the purpose of (3), 5% should be replaced by 10% in *PRU 7.4.84R(2)(b)*.

- 7.4.95 G (1) *Reinsurance* and analogous non-*reinsurance* financing agreements entered into by the *firm*, either with or acting as a *reinsurer*, must be included within the scope of the scenario. The combined rights and obligations under a contract of *reinsurance* or an analogous non-*reinsurance* financing agreement may represent an economic asset or liability. The value placed by the *firm* on the *reinsurance* item or non-*reinsurance* financing item should allow for a realistic assessment of the risks transferred and the risks of *counterparty* default associated with the item. In the case of analogous non-*reinsurance* financing agreements, references to terms such as "*reinsurer*", "*ceding undertakings*" and "*accepting undertakings*" include *undertakings* which by analogy are *reinsurers*, *ceding* or *accepting undertakings*. Analogous non-*reinsurance* financing agreements include contingent loans, securitisations and any other arrangements giving rise to charges on future surplus arising.
- (2) In assessing values in accordance with *PRU 7.4.94R*, a *firm* may consider it appropriate to determine values by drawing an analogy with the approach in respect of bond and debt items set out in *PRU 7.4.84R*. (This might be the case if, in economic terms, the item being valued sufficiently resembles a bond or debt item - an alternative approach might otherwise be preferred). If the *firm* does consider it appropriate to draw an analogy, the "credit spread" assumed should be consistent with the assumed default probabilities and the values placed on the *reinsurance* asset for the purposes of determining the *realistic values of assets and liabilities*. A *firm* may regard it as appropriate to have regard to any financial strength ratings applicable to the *reinsurer*, but if so should apply the same principles set out in *PRU 7.4.92R* for the nomination of financial strength ratings. Table *PRU 7.4.97G* provides *guidance* as to the allocation of spread factors which a *firm* may, by analogy, deem appropriate to apply. Appropriate allowance should be made for any change in the extent of the *counterparty* exposure under the assumed scenario.
- (3) The changes in credit risk spreads determined for bond and debt items in accordance with *PRU 7.4.78R(1)* are required to result in a reduction in market value for some items of 5% of their current value through the operation of *PRU 7.4.84R(2)(b)*. For *reinsurance* contracts and analogous non-*reinsurance* financing agreements, determining the change in value by reference to *PRU 7.4.94R(3)* requires a *firm* to consider the possibility of *counterparty* default in changed credit risk market conditions. Where in the changed credit risk market conditions assumed to apply the *firm's* assessment of the *counterparty* risk would result in the asset being considered equivalent to "Highly speculative or very vulnerable", the reduction in value required is at least 10% of its current value. *PRU 7.4.94R(4)* relates to this requirement.
- 7.4.96 G A financial strength rating of a *reinsurer* refers to a current assessment of the financial security characteristics of the *reinsurer* with respect to its ability to pay *claims* under its *reinsurance* contracts and treaties in accordance with their terms.
- 7.4.97 G Table: Listed rating agencies, financial strength descriptions and spread factors

Financial Strength Description	A.M. Best Company	Fitch Ratings	Moody's Investors Service	Standard & Poor's Corporation	Spread Factor
Superior, extremely strong	A++	AAA	Aaa	AAA	3.00
Superior, very strong	A+	AA	Aa	AA	5.25
Excellent or strong	A, A-	A	A	A	6.75
Good	B++,B+	BBB	Baa	BBB	9.25
Fair, marginal	B, B-	BB	Ba	BB	15.00
Marginal, weak	C++,C+	B	B	B	24.00
Unrated or very weak	Unrated or below C++,C+	Unrated or below B	Unrated or below B	Unrated or below B	24.00

Credit risk scenario for other exposures (including any derivative or quasi-derivative)

- 7.4.98 R For the purposes of *PRU 7.4.78R(3)*, the change in value which must be determined for any other item (including any *derivative* or *quasi-derivative*) which represents an economic asset under the single event applicable under *PRU 7.4.43R(3)* is the *firm's* best estimate of the change in the realistic value of that item which would result from changes in credit risk market conditions consistent with the changes in credit spreads determined in accordance with *PRU 7.4.78R(1)* and the changes in value determined in accordance with *PRU 7.4.78R(2)*.
- 7.4.99 G In applying *PRU 7.4.98R*, a *firm* should assess the total impact on the value of the item resulting from the assumed changed credit risk market conditions. The total change in value may result from the interaction of a number of separate influences. For example, a widening of credit spreads may imply an impact on the amount exposed to *counterparty* default as well as on the likelihood of that default. Each factor influencing the change in value needs separate consideration. It should be assumed, both for determining amounts exposed to *counterparty* default and the likelihood of such default that there will be no change in the likelihood of default in relation to an item issued by or guaranteed by an organisation which is in respect of that item a credit risk scenario exempt organisation (see *PRU 7.4.87R*). *PRU 7.4.77G(5)* is also relevant in this context.

Persistency risk scenario

- 7.4.100 R For the purposes of the persistency risk scenario in *PRU 7.4.44R(6)*, a *firm* must allow for the effects of an increase or a decrease in persistency experience of its *with-profits insurance contracts* by adjusting the termination rates in each year of projection by 32.5% of the termination rates assumed in the calculation of the *realistic value of liabilities* in *PRU 7.4.40R*.

- 7.4.101 R The termination rates referred to in *PRU 7.4.100R* are the rates of termination (including the paying-up of *policies*, but excluding deaths, maturities and retirements) other than on dates specified by the *firm* where:
- (1) a guaranteed amount applies as the minimum amount which will be paid on *claim*; or
  - (2) any payments to the *policyholder* cannot be reduced at the discretion of the *firm* by its applying a market value adjustment.
- 7.4.102 R For the purposes of *PRU 7.4.100R*, the increase or decrease in termination rates must be applied to the projection of terminations up to *policy* guarantee dates and between *policy* guarantee dates, but not to the assumptions as to the proportion of *policyholders* taking up the guarantees at *policy* guarantee dates.
- 7.4.103 G *PRU 7.4.100R* to *PRU 7.4.102R* require *firms* to apply a persistency stress test to the *realistic value of liabilities*. Where a *firm* brings the present value of *non-profit insurance business* in a *with-profits fund* into the calculation of the *realistic value of assets* (see *PRU 7.4.33R*) there is no requirement to stress this asset for changes in persistency assumptions.

Realistic value of liabilities: detailed provisions

- 7.4.104 G *PRU 7.4.40R* sets out the three elements comprising the *realistic value of liabilities* for a *with-profits fund*. The remainder of this section contains general *rules* and *guidance* on determining the *realistic value of liabilities* plus further detail relating to each of those elements separately, as follows:
- (1) general *rules* and *guidance* in *PRU 7.4.105R* to *PRU 7.4.115G*;
  - (2) *with-profits benefits reserve* in *PRU 7.4.116R* to *PRU 7.4.135G*;
  - (3) *future policy related liabilities* in *PRU 7.4.136G* to *PRU 7.4.189G*; and
  - (4) *realistic current liabilities* in *PRU 7.4.190R* and *PRU 7.4.191R*.

Methods and assumptions: general

- 7.4.105 R In calculating the *realistic value of liabilities* for a *with-profits fund*, a *firm* must use methods and assumptions which:
- (1) are appropriate to the business of the *firm*;
  - (2) are consistent from year to year without arbitrary changes (that is, changes without adequate reasons);
  - (3) are consistent with the method of valuing assets (see *PRU 1.3*);

- (4) make full provision for tax payable out of the *with-profits fund*, based on current legislation and practice, together with any known future changes, and on a consistent basis with the other methods and assumptions used;
- (5) take into account discretionary benefits which are at least equal to, and charges which are no more than, the levels required for the *firm* to fulfil its regulatory duty to treat its *customers* fairly;
- (6) take into account prospective management actions (see *PRU 7.4.53R*) and *policyholder* actions (see *PRU 7.4.59R*);
- (7) provide for shareholder transfers out of the *with-profits fund* as a liability of the fund;
- (8) have regard to generally accepted actuarial practice; and
- (9) are consistent with the *firm's PPFM*.

- 7.4.106 G More specific *rules* and *guidance* are set out below on some aspects of the methods and assumptions to be used in calculating the *realistic value of liabilities* for a *with-profits fund*. In contrast to the *mathematical reserves* requirements in *PRU 7.3.10R(4)* and *PRU 7.3.13R*, there is no requirement to include margins for adverse deviation of relevant factors in calculating the *realistic value of liabilities*. Assumptions need be no more prudent than is necessary to achieve a best estimate, taking into account the *firm's PPFM* and its regulatory duty to treat its *customers* fairly. Where there is no requirement for a *PPFM*, for example non-UK business, a *firm* should use assumptions that are consistent with the *firm's* documented approach to treating its *customers* fairly. A *firm* may judge that a margin should be included in its calculations to avoid an understatement of the *realistic value of liabilities* as a result of uncertainty, for example, either in its method or in its data.
- 7.4.107 G The amount and timing of tax charges affect the amount of assets available to meet *policyholder* liabilities. *PRU 7.4.105R(4)* requires *firms* to provide fully for all tax payable out of the *with-profits fund* on a basis consistent with the other assumptions and methods used in deriving the realistic balance sheet. So, for example, all projections which underlie the realistic valuation of assets or liabilities must allow for taxation. The approach adopted should not give any credit for any reduction in tax deriving from future expenses or deficits which is attributable to future new business. For assets backing capital requirements it is not necessary to take into consideration future tax charges on investment income generated by those assets. However, *firms* should consider this aspect in their capital planning.
- 7.4.108 G *PRU 7.4.105R(7)* requires *firms* to provide fully for shareholder transfers. Such transfers do not therefore count as capital in the *with-profits fund*. However, a *firm* may apply under section 148 of the *Act* for a *waiver* from this requirement. In exercising its discretion under section 148 of the *Act*, the *FSA* will have regard (among other factors) to whether a *firm* has put in place undertakings satisfactory to the *FSA*, including that future transfers will not be paid out of the *firm* by way of dividend.



## Valuation of contracts: General

- 7.4.109 R (1) A *firm* must determine the amount of the *with-profits benefits reserve* or the *future policy related liabilities* for a *with-profits fund* by carrying out a separate calculation in relation to each *with-profits insurance contract* or for each group of similar contracts.
- (2) Appropriate approximations or generalisations may be made where they are likely to provide the same, or a higher, result than a separate calculation for each contract.
- (3) A *firm* must set up additional reserves on an aggregated basis for general risks which are not specific to individual contracts or a group of similar contacts where the *firm* considers the *realistic value of liabilities* may otherwise be understated.
- 7.4.110 R For the purpose of *PRU 7.4.109R(1)*, a group of similar contracts is such that the conditions in *PRU 7.4.109(2)* are satisfied.
- 7.4.111 G Where a *firm* has grouped individual contracts for the purpose of calculating the *mathematical reserves* for a *with-profits fund* (in accordance with *PRU 7.3.22R*), the *firm* is not required to use the same grouping of contracts in calculating the *with-profits benefits reserve* or *future policy related liabilities* for that fund.
- 7.4.112 G In contrast to *PRU 7.3.24R* for the *mathematical reserves*, treating individual contracts as an asset is not prohibited if, and to the extent that, this treatment does not conflict with a *firm's* regulatory duty to treat its *customers* fairly.
- 7.4.113 G In calculating the *with-profits benefits reserve*, an overall (grouped or pooled) approach may be appropriate under either of the two methods set out in *PRU 7.4.116R*. In particular, the calculation of aggregate retrospective reserves (see *PRU 7.4.118R*) and the projection of future cash flows (see *PRU 7.4.128R*) based on suitable specimen *policies* is permitted.
- 7.4.114 G In calculating the *future policy related liabilities*, the grouping of *policies* for valuing the costs of guarantees, options or smoothing, and their representation by representative *policies*, is acceptable provided the *firm* can demonstrate that the grouping of *policies* does not materially misrepresent the underlying exposure and does not significantly misstate the costs. A *firm* should exercise care in grouping *policies* in order to ensure that the risk exposure is not inappropriately distorted by, for example, forming groups containing *policies* with guarantees that are “in the money” and *policies* with guarantees well “out of the money”. A *firm* should also have regard to the effects of *policyholder* behaviour over time on the spread of the outstanding guarantees or options.
- 7.4.115 G Where a *firm* groups similar *policies* for the purpose of calculating the *with-profits benefits reserve* or the *future policy related liabilities*, the *firm* should carry out sufficient validation to be reasonably sure that the grouping of *policies* has not resulted in the loss of any significant attributes of the portfolio being valued.

With-profits benefits reserve

- 7.4.116 R A *firm* must calculate a *with-profits benefits reserve* for a *with-profits fund* using either:
- (1) a retrospective calculation under *PRU 7.4.118R* (the retrospective method); or
  - (2) a prospective calculation under *PRU 7.4.128R* of all future cash flows expected to arise under, or in respect of, each of the *with-profits insurance contracts* written in that fund (the prospective method).
- 7.4.117 R Subject to *PRU 7.4.105R(2)*, a *firm* may use different methods under *PRU 7.4.116R* for different types or generations of *with-profits insurance contracts*.

Retrospective method

- 7.4.118 R In the retrospective method of calculating a *with-profits benefits reserve*, a *firm* must calculate either the aggregate of the retrospective reserves in respect of each *with-profits insurance contract* or, to the extent permitted by *PRU 7.4.109R* and *PRU 7.4.110R*, the total retrospective reserve in respect of each group of *with-profits insurance contracts*.
- 7.4.119 R In calculating the retrospective reserve for a *with-profits insurance contract*, or the total retrospective reserve in respect of a group of *with-profits insurance contracts*, a *firm* must take account of at least the following:
- (1) *premiums* received from the *policyholder*;
  - (2) any expenses incurred or charges made (including *commissions*);
  - (3) any partial benefits paid or due;
  - (4) any investment income on, and any increases (or decreases) in, asset values;
  - (5) any tax paid or payable;
  - (6) any amounts received (or paid) under contracts of *reinsurance* or analogous non-*reinsurance* financing agreements, where relevant to retrospective reserves;
  - (7) any shareholder transfers and any associated tax paid or payable; and
  - (8) any permanent enhancements to (or deductions from) the retrospective reserves made by the *firm*.

- 7.4.120 G In taking account of amounts in *PRU 7.4.119R(6)*, due regard should be had to the specific details of each relevant contract of *reinsurance* or analogous non-*reinsurance* financing agreement and the relationship between the amounts received (or paid) and the value of the benefit granted (or received) under the arrangement. This should take into consideration, for example, the risk of default and differences in the *firm's* realistic assessment of the risks transferred and the contractual terms for such transfer of risk. Analogous non-*reinsurance* financing agreements include contingent loans, securitisations and any other arrangements giving rise to charges on future surplus arising.
- 7.4.121 G Where allowance is made for shareholder transfers, this should be in respect of the accrued bonus entitlement reflected in the retrospective reserve. This would include both *annual bonuses* already declared and accrued *final bonus*. However, shareholder transfers in respect of surplus yet to be credited to retrospective reserves should not be charged to those reserves until the corresponding surplus is credited.
- 7.4.122 R In calculating retrospective reserves, a *firm* must have regard to its regulatory duty to treat its *customers* fairly and must ensure that its approach is consistent with its *Principles and Practices of Financial Management*.
- 7.4.123 R In calculating retrospective reserves, a *firm* must ensure its treatment of past cash flows, and of any future cash flows, is consistent with those cash flows valued in its prospective calculation of the *future policy related liabilities* for that fund in accordance with the *rules* in *PRU 7.4.136G* to *PRU 7.4.189G*.
- 7.4.124 G An example of *PRU 7.4.123R* concerns future shareholder transfers. A *firm* must make adequate provision for future shareholder transfers within the *future policy related liabilities* (see *PRU 7.4.165R*). The basis of provisioning needs to be consistent with the amounts accrued within retrospective reserves and the amounts already transferred out of the *with-profits fund*.
- 7.4.125 G Another example of the application of *PRU 7.4.123R* relates to the reference in *PRU 7.4.119R(8)* to past permanent enhancements to (or deductions from) retrospective reserves made by *firms*. This item may include past miscellaneous surplus (or losses) which have been credited to (or debited from) retrospective reserves. Any other enhancements (or deductions) made on a temporary basis and any future surplus (or losses) that *firms* intend to credit to (or debit from) retrospective reserves should be included under the *future policy related liabilities* (see *PRU 7.4.137R*).

- 7.4.126 G *Firms* characteristically use a range of calculation methods to determine retrospective reserves. A *firm's* definition and calculation of retrospective reserves will depend on a number of factors. These include: the *firm's* practice; its administration and accounting systems; the extent of its historical records; and the composition of its with-profits portfolio. The *rules* and *guidance* for the retrospective method are drawn up to be sufficiently flexible to accommodate the diversity of calculation methods used by *firms*, rather than to enforce any particular method of calculation of retrospective reserves. *PRU 7.4.119R* simply sets minimum standards that all retrospective methods must meet.
- 7.4.127 G For the purposes of *PRU 7.4.119R(2)* and *PRU 7.4.128R(2)*, the phrases 'charges made' or 'charges to be made' refer to circumstances where types of risk (such as mortality risk, longevity risk and investment risk) are met by the *firm* or *with-profits fund* in return for a charge deducted by the *firm* from the *with-profits benefits reserve*.

#### Prospective method

- 7.4.128 R In the prospective method of calculating a *with-profits benefits reserve*, a *firm* must take account of at least the following cash flows:
- (1) future *premiums*;
  - (2) expenses to be incurred or charges to be made, including *commissions*;
  - (3) benefits payable (see *PRU 7.4.129R*);
  - (4) tax payable;
  - (5) any amounts to be received (or paid) under contracts of *reinsurance* or analogous non-*reinsurance* financing agreements, where relevant to *with-profits insurance contracts* being valued; and
  - (6) shareholder transfers.
- 7.4.129 R For the purposes of *PRU 7.4.128R(3)*, benefits payable include:
- (1) all guaranteed benefits, including guaranteed amounts payable on death and maturity, guaranteed *surrender values* and paid-up values;
  - (2) vested, declared and allotted bonuses to which *policyholders* are entitled; and
  - (3) future *annual* and *final bonuses* at least equal to the levels required for the *firm* to fulfil its regulatory duty to treat its *customers* fairly.
- 7.4.130 R A *firm* must value the cash flows listed in *PRU 7.4.128R* using best estimate assumptions of future experience, having regard to generally accepted actuarial practice and taking into account the *firm's PPFM* and its regulatory duty to treat its *customers* fairly.

- 7.4.131 G The prospective method sets the *with-profits benefits reserve* at the net present value of future cash flows listed in *PRU 7.4.128R*.
- 7.4.132 G In contrast to *PRU 7.3.10R(4)* and *PRU 7.3.13R* relating to the methods and assumptions used to value the *mathematical reserves*, there is no requirement to value future cash flows using assumptions that include margins for adverse deviation. Also there are no detailed *rules* as to the future yields on assets, discount rates, *premium* levels, expenses, tax, mortality, morbidity, persistency and *reinsurance*. A *firm* should make its own assessment as to the amount of these future cash flows including bonuses and discretionary surrender or transfer values. A *firm* should make a realistic assessment of longevity risk and asset default risk (including default risk arising under contracts of *reinsurance* or analogous non-*reinsurance* financing agreements) within the best estimate assumptions of future experience required by *PRU 7.4.130R*.
- 7.4.133 G In valuing the future cash flows listed in *PRU 7.4.128R*, the *firm* should use a projection term which is long enough to capture all material cash flows arising from the contract or groups of contracts being valued. If the projection term does not extend to the term of the last *policy*, the *firm* should check that the shorter projection term does not significantly affect the results.
- 7.4.134 R Where a *firm* expects to pay additional benefits that are not included in the cash flows listed in *PRU 7.4.128R*, it must make adequate provision for these benefits in calculating the *future policy related liabilities* in accordance with the *rules* in *PRU 7.4.136G* to *PRU 7.4.189G*.
- 7.4.135 G The prospective assessment of the *with-profits benefits reserve* will usually be on a deterministic basis. A *firm* will have to make further provision in the *future policy-related liabilities* for, for example, the costs of potential asset fluctuations or *policy* options.

#### Future policy related liabilities

#### Overview of liabilities

- 7.4.136 G *PRU 7.4.137R* lists the *future policy related liabilities* for a *with-profits fund* that form part of a *firm's realistic value of liabilities* in *PRU 7.4.40R*. Detailed *rules* and *guidance* relating to particular types of liability and asset are set out in *PRU 7.4.139R* to *PRU 7.4.168G*. These are followed by *rules* and *guidance* that deal with certain aspects of several liabilities (that is, liabilities relating to guarantees, options and smoothing):
- (1) *PRU 7.4.169R* to *PRU 7.4.186G* refer to valuing the costs of guarantees, options and smoothing; and
  - (2) *PRU 7.4.187R* to *PRU 7.4.189G* refer to the treatment of surplus on guarantees, options and smoothing.

- 7.4.137 R The *future policy related liabilities* for a *with-profits fund* are equal to the sum of amounts, as they relate to that fund, in respect of (1) to (11) to the extent each is valued as a liability less the sum of amounts, as they relate to that fund, in respect of (1) to (11) to the extent each is valued as an asset:
- (1) past miscellaneous surplus (or deficit) planned to be attributed to the *with-profits benefits reserve* (see *PRU 7.4.139R*);
  - (2) planned enhancements to the *with-profits benefits reserve* (see *PRU 7.4.141R*);
  - (3) planned deductions for the costs of guarantees, options and smoothing from the *with-profits benefits reserve* (see *PRU 7.4.144R*);
  - (4) planned deductions for other costs deemed chargeable to the *with-profits benefits reserve* (see *PRU 7.4.146R*);
  - (5) future costs of contractual guarantees (other than financial options) (see *PRU 7.4.148R*);
  - (6) future costs of non-contractual commitments (see *PRU 7.4.154R*);
  - (7) future costs of financial options (see *PRU 7.4.156G*);
  - (8) future costs of smoothing (see *PRU 7.4.158R*);
  - (9) financing costs (see *PRU 7.4.162R*);
  - (10) any other further liabilities required for the *firm* to fulfil its regulatory duty to treat its *customers* fairly; and
  - (11) other *long-term insurance liabilities* (see *PRU 7.4.165R*).
- 7.4.138 G Some of the elements of the calculation set out in *PRU 7.4.137R* may have already been taken into consideration in the calculation of the *with-profits benefits reserve*, either under the retrospective method (see *PRU 7.4.118R* onwards) or the prospective method (see *PRU 7.4.128R* onwards). Where this is the case, the adjustments made under *PRU 7.4.137R* should be such that no double-counting arises.

Past miscellaneous surplus (or deficit) planned to be attributed to the with-profits benefits reserve

- 7.4.139 R In calculating the *future policy related liabilities* for a *with-profits fund*, a *firm* must allow for past miscellaneous surplus (or deficit) which it intends to attribute to the *with-profits benefits reserve* for that fund but which has not yet been permanently credited to (or debited from) the *with-profits benefits reserve* for that fund.

- 7.4.140 G Past miscellaneous surplus (or deficit) already permanently credited to (or debited from) the *with-profits benefits reserve* will have been included in the calculation of the *with-profits benefits reserve* in accordance with *PRU 7.4.119R(8)*.

Planned enhancements to the with-profits benefits reserve

- 7.4.141 R In calculating the *future policy related liabilities* for a *with-profits fund*, a *firm* must make provision for any future planned enhancements to the *with-profits benefits reserve* for that fund that cannot be financed out of the resources of the *with-profits benefits reserve* and future *premiums*.
- 7.4.142 G For the purposes of *PRU 7.4.141R*, planned enhancements to the *with-profits benefits reserve* will arise when a *firm* has a contractual obligation, or a non-contractual commitment (arising from its regulatory duty to treat *customers* fairly), to enhance *claims* on some classes of *policy* (perhaps in the form of specially enhanced future bonus rates). In such circumstances, the present value of the costs of paying out a target asset share that is more than the projected *with-profits benefit reserve* for those classes of *policy* for which this practice is applicable should be included in the amount of the *future policy related liabilities*. For example, a *firm* may have a non-contractual commitment (arising from its regulatory duty to treat *customers* fairly) to pay enhanced benefits but have discretion not to make such payments in adverse circumstances. Such planned enhancements should be provided for in the realistic balance sheet, but allowance should be made for management action in the calculation of the *risk capital margin*.
- 7.4.143 G The valuation of *claims* in excess of targeted asset shares in respect of guarantees, options and smoothing, including those arising under guaranteed annuity rates, should be carried out in accordance with *PRU 7.4.169R* to *PRU 7.4.186G*.

Planned deductions for the costs of guarantees, options and smoothing from the with-profits benefits reserve

- 7.4.144 R Where a *firm* expects to deduct future charges from the *with-profits benefits reserve* for a *with-profits fund* to cover the costs of guarantees, options or smoothing for that fund, the *firm* must take credit for these future charges in calculating the *future policy related liabilities* for that fund.
- 7.4.145 G In calculating *future policy related liabilities* for a *with-profits fund*, a *firm* should take credit under *PRU 7.4.137R(3)* for the present value of the future “margins” available in respect of charges deducted to cover the costs of guarantees, options and smoothing. *PRU 7.4.188R* requires *firms* that accumulate the charges made less costs incurred to provide for any surplus on the experience account as a realistic liability. Any such provision should be made under *PRU 7.4.137R(5)*, (7) or (8), depending on the nature of the charges made, and has no effect on the amount calculated under *PRU 7.4.144R*.

Planned deductions for other costs deemed chargeable to the with-profits benefits reserve

- 7.4.146 R Where a *firm* expects to deduct future charges (other than those valued in *PRU 7.4.144R*) from the *with-profits benefits reserve* for a *with-profits fund*, the *firm* must take credit for these future charges in calculating the *future policy related liabilities* for that fund.
- 7.4.147 G A *firm* should take credit for the present value of the other future “margins” available. The circumstances where such margins may arise include:
- (1) where a *firm* is targeting *claims* at less than 100% of the *with-profits benefits reserve*, the amount of such shortfall; and
  - (2) where a *firm* expects to deduct any future charges (other than those for guarantees, options and smoothing) from the *with-profits benefits reserve*.

Future costs of contractual guarantees (other than financial options)

- 7.4.148 R A *firm* must make provision for the costs of paying excess *claim* amounts for a *with-profits fund* where the *firm* expects that the amount in (1) may be greater than the amount in (2), calculated as at the date of *claim*:
- (1) the value of guarantees arising under a *policy* or group of *policies* in the fund; and
  - (2) the fund’s *with-profits benefits reserve* allocated in respect of that *policy* or group of *policies*.
- 7.4.149 R For the purposes of *PRU 7.4.148R*, the future costs of guarantees cannot be negative.
- 7.4.150 G In carrying out projections to calculate the cost of guarantees under *PRU 7.4.137R* the opening liability should be set equal to the *with-profits benefit reserve* (see *PRU 7.4.118R*), adjusted for miscellaneous surplus or deficits (see *PRU 7.4.137R(1)*) and planned enhancements (see *PRU 7.4.141R*).
- 7.4.151 G In projecting forward the *with-profits benefits reserve*, adjusted as in *PRU 7.4.150G*, to the date of *claim* for the purposes of *PRU 7.4.148R*, the *firm* should use market consistent assumptions for the expected future *premium* and investment income (including realised and unrealised gains or losses), expenses and *claims*, any charges to be deducted, tax and any other item of income or outgo. This projection should be carried out on the same basis as is described in *PRU 7.4.130R*.
- 7.4.152 G *PRU 7.4.169R* to *PRU 7.4.186G* contain further *rules* and *guidance* on the valuation of guarantees, options and smoothing.
- 7.4.153 G Some examples of contractual guarantees are:
- (1) for conventional *with-profits insurance contracts*, guaranteed sums assured and bonuses on death, maturity or retirement; and



- (2) for *accumulating with-profits policies*, guarantees at a point in time or guaranteed minimum bonus rates.

#### Future costs of non-contractual commitments

- 7.4.154 R A *firm* must make provision for future costs in addition to those in *PRU 7.4.148R* where the *firm* expects to pay further amounts to meet non-contractual commitments to *customers* or pay other benefits that need to be provided to fulfil a *firm's* regulatory duty to treat its *customers* fairly.
- 7.4.155 G Some examples of these non-contractual commitments are:
- (1) statements by the *firm* regarding the ability of *policies* to cover defined amounts, such as the repayment of a mortgage;
  - (2) statements by the *firm* regarding regular withdrawals from a *policy* being without penalty;
  - (3) guaranteed annuity and cash option rates being provided beyond the strict interpretation of the *policy*; and
  - (4) the costs of any promises to *customers* or other benefits that need to be provided to fulfil a *firm's* regulatory duty to treat its *customers* fairly.

#### Future costs of financial options

- 7.4.156 G Financial options include guaranteed annuity and cash option rates.
- 7.4.157 G *PRU 7.4.169R* to *PRU 7.4.186G* contain further *rules* and *guidance* on the valuation of options.

#### Future costs of smoothing

- 7.4.158 R A *firm* must make provision for future smoothing costs of a *with-profits fund* where the *firm* expects that the *claims* paid on a *policy* or group of *policies* in the fund will vary from the greater of:
- (1) the value of guarantees determined in *PRU 7.4.148R* in respect of that *policy* or group of *policies*; and
  - (2) the fund's *with-profits benefits reserve* allocated in respect of that *policy* or group of *policies*, which must be enhanced as described in *PRU 7.4.141R*;
- calculated as at the date of *claim*.
- 7.4.159 R For the purposes of *PRU 7.4.158R*, smoothing costs are defined as the present value of the difference between projected *claims* and the projected *with-profits benefit reserve* after enhancements (see *PRU 7.4.141R*), other than payouts on guarantees (see *PRU 7.4.148R*).

- 7.4.160 R Subject to *PRU 7.4.188R*, the future costs of smoothing can be negative.
- 7.4.161 G *PRU 7.4.169R* to *PRU 7.4.186G* contain further *rules* and *guidance* on the valuation of the future costs of smoothing.
- Financing costs
- 7.4.162 R A *firm* must provide for future liabilities to repay financing costs of a *with-profits fund* where the *firm* expects to have to meet such liabilities and to the extent that these liabilities are not already provided for by amounts included in the fund's *realistic current liabilities* (see *PRU 7.4.190R* and *PRU 7.4.191R*). The amount of the liabilities to repay financing costs must be assessed on a market-consistent basis.
- 7.4.163 G In *PRU 7.4.162R*, financing costs refer to the future costs incurred by way of capital, interest and fees payable to the provider. A *firm* should make a realistic assessment of the requirement to repay such financing in its expected future circumstances (which may be worse than currently). Having taken account of its particular circumstances:
- (1) where a *firm* has no liability to repay such financing, it should not include such repayment as a liability;
  - (2) where a *firm* has a reduced liability to repay such financing, it should include a reduced repayment as a liability.
- 7.4.164 G In *PRU 7.4.162R*, financing includes *reinsurance* financing arrangements and analogous non-*reinsurance* financing arrangements, such as contingent loans, securitisations and any other arrangements giving rise to charges on future surplus arising.
- Other long-term insurance liabilities
- 7.4.165 R A *firm* must provide for any other *long-term insurance liabilities* arising from or in connection with *with-profits insurance contracts* in a *with-profits fund*, to the extent that adequate provision has not been made in the *with-profits benefits reserve* or in any other part of the *future policy related liabilities* for that fund.
- 7.4.166 G Some examples of these other *long-term insurance liabilities* are:
- (1) pension and other mis-selling reserves;
  - (2) provisions for tax; and
  - (3) provisions for future shareholder transfers.
- 7.4.167 G In determining the realistic liability for taxation *firms* should apply the general principles set out in *PRU 7.4.105R* and the *guidance* given in *PRU 7.4.107G*.

- 7.4.168 G *PRU 7.4.105R* requires *firms* to provide for shareholder transfers out of the *with-profits fund* as a liability of the fund. The provision should be consistent with the methods and assumptions used in valuing the other realistic liabilities. So, for example, where the *with-profits benefits reserve* includes amounts that would be paid to *policyholders* through future bonuses, provision should also be made for future shareholder transfers associated with those bonuses.

Valuing the costs of guarantees, options and smoothing

- 7.4.169 R For the purposes of *PRU 7.4.137R(5)*, (7) and (8), a *firm* must calculate the costs of any guarantees, options and smoothing using one or more of the following three methods:
- (1) a stochastic approach using a market-consistent asset model (see *PRU 7.4.170R*);
  - (2) using the market costs of hedging the guarantee or option;
  - (3) a series of deterministic projections with attributed probabilities.
- 7.4.170 R The market-consistent asset model in *PRU 7.4.169R(1)*:
- (1) means a model that delivers prices for assets and liabilities that can be directly verified from the market; and
  - (2) must be calibrated to deliver market-consistent prices for those assets that reflect the nature and term of the *with-profits insurance liabilities* of the *with-profits fund*.
- 7.4.171 G Deterministic approaches will not usually capture the time value of the option generated by a guarantee. In order to calculate this value properly, *firms* are expected either to use market option values where these are readily available or to undertake a stochastic approach using a market-consistent asset model.
- 7.4.172 G The *FSA* considers stochastic modelling to be preferable for material groups or classes of *with-profits insurance contracts* unless it can be shown that more simplistic or alternative methods are both appropriate and sufficiently robust.

- 7.4.173 G Where the guarantee or option is relatively simple in nature, is capable of being hedged, and has a value unlikely to be affected by management actions (see *PRU 7.4.185R*) (for example, a guaranteed annuity rate option) then the cost of the guarantee or option would be the market cost of hedging the guarantee. Where that is generally the case but, in respect of a minor part of a portfolio, no market exists for hedging the option generated by the guarantee, a *firm* should take the value of the nearest equivalent benefit or right for which a market exists and record how it has adjusted the valuation to reflect the original option. Where the market value of the hedge is used *firms* should also make provisions for the credit risk arising from the hedge, both that arising from exposure to a *counterparty* and that arising from credit risk in the underlying instrument. The extent to which the guarantee or option is capable of being hedged depends on a *firm's* assumptions regarding future investment mix, persistency, annuitant mortality and take-up rates. While the *FSA* recognises that the hedge may not be perfectly matched to the underlying guarantee or option, a *firm* should ensure that hedge is reasonably well matched having regard to the sensitivity of the guarantee or option to the *firm's* choice of key assumptions.
- 7.4.174 G Where a *firm* has large cohorts of guarantees and uses stochastic or deterministic approaches, a *firm* should have regard to whether the cost of the guarantees determined under those approaches bears a reasonable relationship to the market cost of hedging those guarantees (where it exists).
- 7.4.175 G In determining the costs of smoothing, a *firm* should consider:
- (1) the consistency of its assumptions (including the exercise of management discretion over bonus rates); and
  - (2) where targeted payouts currently exceed retrospective reserves in respect of those *claims*, the assumptions used in reducing the excess, if applicable,
- having regard to the *firm's PPFM* and its regulatory duty to treat its *customers* fairly.

#### Stochastic approach

- 7.4.176 G For the purposes of *PRU 7.4.169R(1)*, a stochastic approach would consist of an appropriate market-consistent asset model for projections of asset prices and yields (such as equity prices, fixed interest yields and property yields), together with a dynamic model incorporating the corresponding value of liabilities and the impact of any foreseeable actions to be taken by management. Under the stochastic approach, the cost of the guarantee, option or smoothing would be equal to the average of these stochastic projections.
- 7.4.177 G In performing the projections of assets and liabilities under the stochastic approach in *PRU 7.4.169R(1)*, a *firm* should have regard to the aspects in (1) and (2).

- (1) The projection term should be long enough to capture all material cash flows arising from the contract or groups of contracts being valued. If the projection term does not extend to the term of the last *policy*, the *firm* should check that the shorter projection term does not significantly affect the results.
  - (2) The number of projections should be sufficient to ensure a reasonable degree of convergence in the results, including the determination of the result of the *risk capital margin*. The *firm* should test the sensitivity of the results to the number of projections.
- 7.4.178 G The *FSA* considers a holistic approach to stochastic modelling to be preferable so as to value all items of costs together rather than using separate methods for different items of the *realistic value of liabilities*. This approach requires the projection of all material cash flows arising under the contract or group of contracts for each stochastic projection, rather than only those arising from the guarantee or option within the contract. The advantages of this approach are that it ensures greater consistency in the valuation of different components of the contract and explicitly takes into account the underlying hedges or risk mitigation between components of the contract or group of contracts being valued. Where a *firm* can use a stochastic approach to value simultaneously all components of the contract or group of contracts, the *firm* should adopt this approach where practical and feasible.
- 7.4.179 G Where a stochastic approach is used, a *firm* should make and retain a record under *PRU 7.4.17R* of the nature of the asset model and of the assumptions used (including the volatility of asset values and any assumed correlations between asset classes or between asset classes and economic indicators, such as inflation).
- 7.4.180 G In calibrating asset models for the purposes of *PRU 7.4.170R*, a *firm* should have regard to the aspects in (1), (2) and (3).
- (1) Few (if any) asset models can replicate all the observable *market values* for a wide range of asset classes. A *firm* should calibrate its asset models to reflect the nature and term of the fund's liabilities giving rise to significant guarantee and option costs.
  - (2) A *firm* will need to apply judgement to determine suitable estimates of those parameters which cannot be implied from observable market prices (for example, long-term volatility). A *firm* should make and retain a record under *PRU 7.4.17R* of the choice of parameters and the reasons for their use.
  - (3) A *firm* should calibrate the model to the current risk-free yield curve. Risk-free yields should be determined after allowing for credit and all other risks arising. *Firms* may have regard to any guidance from the actuarial profession on the calculation of the risk-free yield but should not assume a higher yield than suggested by any such guidance.

#### Deterministic approach

- 7.4.181 R For the purposes of the deterministic approach in *PRU 7.4.169R(3)*, a *firm* must calculate a series of deterministic projections of the values of assets and corresponding liabilities, where each deterministic projection corresponds to a possible economic scenario or outcome.
- 7.4.182 G A *firm* should determine a range of scenarios or outcomes appropriate to both valuing the costs of the guarantee, option or smoothing and the underlying asset mix, together with the associated probability of occurrence. These probabilities of occurrence should be weighted towards adverse scenarios to reflect market pricing for risk. The costs of the guarantee, option or smoothing should be equal to the expected cost based on a series of deterministic projections of the values of assets and corresponding liabilities. In using a series of deterministic projections, a *firm* should consider whether its approach provides a suitably robust estimate of the costs of the guarantee, option or smoothing.
- 7.4.183 G In performing the projections of assets and liabilities under the deterministic approach in *PRU 7.4.169R(3)*, a *firm* should have regard to the aspects in (1) and (2).
- (1) The projection term should be long enough to capture all material cash flows arising from the contract or group of contracts being valued. If the projection term does not extend to the term of the last contract, the *firm* should check that the shorter projection term does not significantly affect the results.
- (2) The series of deterministic projections should be numerous enough to capture a wide range of possible outcomes and take into account the probability of each outcome's likelihood. The costs will be understated if only relatively benign or limited economic scenarios are considered.
- 7.4.184 G Where a series of deterministic projections is used, a *firm* should make and retain a record under *PRU 7.4.17R* of the range of projections and how the probabilities attributed to each projection or outcome were determined (including the period of reference for any relevant data on past experience).

#### Management and policyholder actions

- 7.4.185 R In calculating the costs of any guarantees, options or smoothing, a *firm*:
- (1) may reflect its prospective management actions (within the meaning of *PRU 7.4.53R*); and
- (2) must reflect a realistic assessment of the *policyholder* actions (within the meaning of *PRU 7.4.59R*);
- in its projections of the value of assets and liabilities.
- 7.4.186 G For the purposes of *PRU 7.4.185R*, the related *guidance* in *PRU 7.4.54G* to *PRU 7.4.57G* (management actions) and in *PRU 7.4.60G* (policyholder actions) applies.

#### Treatment of surplus on guarantees, options and smoothing

- 7.4.187 R *PRU 7.4.188R* applies to *firms* calculating the costs of guarantees, options and smoothing to be included in the *future policy-related liabilities* in accordance with *PRU 7.4.137R(5), (7) and (8)*.
- 7.4.188 R Where a *firm* accumulates past experience and deducts or is otherwise able to take credit for charges for guarantees or options or smoothing, the future costs of guarantees or options or smoothing (as appropriate) must not be less than the greater of:
- (1) the prospective calculation of the future cost of guarantees (see *PRU 7.4.148R*) or options (see *PRU 7.4.156G*) or smoothing (see *PRU 7.4.158R*) (as appropriate); and
  - (2) the sum of:
    - (a) the accumulated charges (after deduction of past costs) for guarantees or options or smoothing (as appropriate); and
    - (b) the prospective calculation of the future charges deducted for guarantees or options or smoothing (see *PRU 7.4.144R*) (as appropriate).
- 7.4.189 G The extent to which the amount in *PRU 7.4.188R(2)* exceeds the amount in *PRU 7.4.188R(1)* will determine the surplus available to support actions that would be taken by the *firm's* management. The purpose of *PRU 7.4.188R* is to ensure that any resulting surplus at the valuation date arising from the accumulation of charges less costs remains available to support foreseeable actions that would be taken by the *firm's* management. Any additional liability arising from *PRU 7.4.188R* is added to the liabilities under *PRU 7.4.137R(5), (7) and (8)* but has no impact on the adjustment for planned deductions for the costs of guarantees, options and smoothing (see *PRU 7.4.137R(3)* and *PRU 7.4.144R*).

#### Realistic current liabilities

- 7.4.190 R For the purposes of *PRU 7.4.40R(3)*, the *realistic current liabilities* of a *with-profits fund* are equal to the sum of the following amounts:
- (1) the *firm's* best estimate provision for those liabilities for which prudent provision is made in *regulatory current liabilities* (see *PRU 7.4.30R*); and
  - (2) to the extent that amounts have not been provided in (1), any tax and any other costs arising either in respect of excess *admissible assets* (within the meaning of *PRU 7.4.36R*) or on the recognition of future shareholder transfers.
- 7.4.191 R In assessing the best estimate provision to be made under *PRU 7.4.190R(1)* in respect of a *defined benefits pension scheme*, the *firm* must use the same amount as results from the application of *PRU 1.3.5R*.

## 7.5 Equalisation provisions

### Application

7.5.1 R *PRU 7.5* applies to an *insurer* carrying on *general insurance business* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

7.5.2 G The scope of *PRU 7.5.11R* to *PRU 7.5.37G* (non-credit equalisation provisions) is not restricted to *firms* subject to the relevant EC directives. It applies, for example, to *pure reinsurers*.

7.5.3 G The requirements of this section apply to a *firm* on a solo basis.

### Purpose

7.5.4 G This section sets out *rules* and *guidance* on the calculation of the amount of the *equalisation provisions* that are required to be maintained by *firms* that carry on non-credit *insurance business* or credit *insurance business*.

7.5.5 G *Credit* or *non-credit equalisation provisions* form part of the *technical provisions* that a *firm* is required to establish under *PRU 7.2.12R(1)*. They help to smooth fluctuations in loss ratios in future years for business where *claims* in any future year may be subject to significant deviation from recent or average *claims* experience, or where trends in experience may be subject to change. Such volatile *claims* experience might arise in the case, for example, of insurance against losses caused by major catastrophes such as hurricanes or earthquakes.

7.5.6 G In general terms, *PRU 7.5* sets out *rules* and *guidance* as to:

- (a) the circumstances in which a *firm* is required to maintain *equalisation provisions*;
- (b) the methods to be used in calculating the amount of each provision;
- (c) the geographical location of the business relevant to certain calculations for different types of *firm* – this is summarised in the Table in *PRU 7.5.7G*.



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Table : Scope of <i>insurance business</i> to be included in calculations				
Type Of Firm		Credit Equalisation Provision		Non Credit Equalisation Provision
		Threshold in <i>PRU 7.5.44R</i>	Provision in <i>PRU 7.5.43R</i>	Threshold in <i>PRU 7.5.18R(2)</i> and provision in <i>PRU 7.5.17R</i>
<i>UK insurer</i>		World-wide	World-wide	World-wide
<i>Pure reinsurer with head office outside United Kingdom</i>		<i>PRU 7.5.39R to PRU 7.5.47G do not apply</i>		<i>UK</i>
<i>Pure reinsurer with head office in United Kingdom</i>		<i>PRU 7.5.39R to PRU 7.5.47G do not apply</i>		World-wide
<i>Non-EEA direct insurers</i>	<i>EEA-deposit insurer</i>	<i>UK</i>	<i>UK</i>	<i>UK</i>
	<i>Swiss general insurer</i>	<i>UK</i>	<i>UK</i>	<i>UK</i>
	<i>UK-deposit insurer</i>	All <i>EEA</i>	World-wide	<i>UK</i>
	All other <i>non-EEA direct insurers</i>	<i>UK</i>	World-wide	<i>UK</i>

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The *First Non-Life Directive* (as amended) requires the calculation of *credit equalisation provisions*. *Non-credit equalisation provisions* are a domestic *United Kingdom* requirement. For insurance regulatory purposes under EC Directives, *credit equalisation provisions* are classified as liabilities.

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However, *firms* are permitted to include *equalisation provisions* within their financial resources when demonstrating compliance with non-Directive capital requirements. Hence *equalisation provisions* are deducted from the available

*capital resources* of a *firm* for the purpose of meeting its *minimum capital requirement* for *general insurance business*; but, in the calculation of a *firm's enhanced capital requirement* for *general insurance business* under PRU 2.3.11R, its *equalisation provisions* (if any) are added back to its *capital resources*.

- 7.5.10 G Under International Accounting Standards (IAS), which will apply to the financial statements of some *insurers* from 2005, there will be no requirement to treat *equalisation provisions* as liabilities in *insurers'* published financial statements. However, they will continue to be treated as liabilities for the purposes of demonstrating compliance with Directive capital requirements.

Non-credit equalisation provision

Firms carrying on non-credit insurance business

- 7.5.11 R (1) PRU 7.5.11R to PRU 7.5.37G apply to any *firm*, other than an *assessable mutual*, which carries on the business of *effecting* or *carrying out general insurance contracts* falling within any description in column 2 in Table PRU 7.5.12R ("non-credit *insurance business*").
- (2) A *firm* falling within (1) must classify all of its non-credit *insurance business* into separate *insurance business groupings*, as specified in Table PRU 7.5.12R.

- 7.5.12 R Table : Groupings of non-credit *insurance business*

<i>Insurance Business Grouping</i>	General Insurance Contracts
A	<i>Contracts of insurance</i> which fall within <i>general insurance business classes</i> 4, 8 or 9, other than:
(a)	<i>contracts of insurance</i> under <i>non-proportional reinsurance treaties</i> ; and
(b)	<i>contracts of insurance</i> against <i>nuclear risks</i> .
B	<i>Contracts of insurance</i> which fall within <i>general insurance business class</i> 16(a) , other than:
(a)	<i>contracts of insurance</i> under <i>non-proportional reinsurance treaties</i> ; and
(b)	<i>contracts of insurance</i> against <i>nuclear risks</i> .

C		<i>Contracts of insurance</i> which fall within <i>general insurance business classes</i> 5, 6, 11 or 12, other than:
	(a)	<i>contracts of insurance</i> against nuclear risks; and
	(b)	<i>reinsurance</i> contracts corresponding to contracts in (a).
D		<i>Contracts of insurance</i> against nuclear risks.
E		<i>Contracts of insurance</i> under <i>non-proportional reinsurance treaties</i> and which fall within <i>general insurance business classes</i> 4, 8, 9 or 16(a) other than <i>contracts of insurance</i> against nuclear risks.

- 7.5.13 R For the purposes of *PRU 7.5.11R* to *PRU 7.5.37G*, a *firm* with its head office in the *United Kingdom* must take account of non-credit *insurance business* carried on by it world-wide.
- 7.5.14 R For the purposes of *PRU 7.5.11R* to *PRU 7.5.37G*, a *firm* with its head office outside the *United Kingdom* need only take account of non-credit *insurance business* carried on by it from a *branch* in the *United Kingdom*.
- 7.5.15 G The *insurers* affected by *PRU 7.5.11R* include *pure reinsurers*, *UK–deposit insurers*, *EEA–deposit insurers*, and *Swiss general insurers*.
- 7.5.16 G For *insurers* (including *pure reinsurers*) with a head office in the *United Kingdom*, the calculations must be made in respect of world-wide business.

Requirement to maintain non-credit equalisation provision

- 7.5.17 R In respect of each *financial year*, a *firm* must, unless *PRU 7.5.18R* applies:
- (1) calculate the amount of its *non-credit equalisation provision* as at the end of that year in accordance with *PRU 7.5.20R*; and
  - (2) maintain a *non-credit equalisation provision* calculated in accordance with *PRU 7.5.20R* for the following *financial year*.
- 7.5.18 R
- (1) *PRU 7.5.17R* does not apply to any *firm* in respect of any *financial year* if, as at the end of that year:
    - (a) no *non-credit equalisation provision* has been brought forward from the preceding *financial year*; and
    - (b) the amount of the *annualised net written premiums* for all the non-credit *insurance business* carried on by it in the *financial year* is less than the threshold amount.
  - (2) The threshold amount in respect of any *financial year* is the higher of:

- (a) 1,500,000 Euro; and
- (b) 4% of *net written premiums* in that *financial year* in respect of all its *general insurance business*, if this amount is less than 2,500,000 Euro.

7.5.19 G For *non-EEA insurers*, the calculation of the threshold amount in *PRU 7.5.18R (2)* is limited by *PRU 7.5.14R* to the business of the *firm* carried on in the *United Kingdom*. Such a *firm* may do little *UK non-credit insurance business*, and so would not be required to set up a *non-credit equalisation provision* under *PRU 7.5*, but may do significant business outside the *United Kingdom* characterised by high-impact, low-frequency *claims*. Such a *firm* is required by *PRU 7.6.41R* to hold adequate world-wide financial resources to avoid internal-contagion strain on the *branch* in the *United Kingdom*. In determining the adequacy of its financial resources, the *firm* should undertake stress and scenario testing of its underwriting and other risks as set out in *PRU 1.2*.

#### Calculating the amount of the provision

- 7.5.20 R (1) Unless *PRU 7.5.22R* applies, the amount of a *firm's non-credit equalisation provision* as at the end of a *financial year* is the higher of:
- (a) zero; and
  - (b) whichever is the lower of:
    - (i) the aggregate of the amounts of the maximum provision for each *insurance business grouping* as at the end of that *financial year*; and
    - (ii) the sum of A and B.
- (2) For the purposes of (1)(b)(ii):
- (a) A is the amount of the *non-credit equalisation provision*, if any, brought forward from the *financial year* immediately preceding that in respect of which the calculation is being performed; and
  - (b) B is:
    - (i) the aggregate of the amounts of the provisional transfers-in for each *insurance business grouping*; minus
    - (ii) the aggregate of the amounts of the provisional transfers-out for each *insurance business grouping*.
- (3) For any *insurance business grouping*:
- (a) the amount of the maximum provision in (1)(b)(i) is to be determined in accordance with *PRU 7.5.24R*;

- (b) the amount of the provisional transfers-in in (2)(b)(i) is to be determined in accordance with *PRU 7.5.26R*; and
  - (c) the amount of the provisional transfers-out in (2)(b)(ii) is to be determined in accordance with *PRU 7.5.29R*.
- 7.5.21 G If provisional transfers-out are in excess of provisional transfers-in, the *non-credit equalisation provision* as calculated in accordance with *PRU 7.5.20R* in respect of a particular *financial year* may be less than that calculated for the preceding *financial year* although, by virtue of *PRU 7.5.20R(1)(a)*, it cannot be negative.
- 7.5.22 R (1) The amount of a *firm's non-credit equalisation provision* as at the end of a *financial year* is zero if:
- (a) as at the end of that year, the *firm* meets either of the conditions specified in (2) and (3); and
  - (b) the *annualised net written premiums* for all the *non-credit insurance business* carried on by the *firm* in that year are less than the threshold amount.
- (2) The first condition is that the *firm* carried on *non-credit insurance business* in the first *financial year* of the relevant period and, for each of any two or more *financial years* of that period, the *annualised net written premiums* for business of that description were less than the threshold amount.
- (3) The second condition is that the *firm* did not carry on *non-credit insurance business* in the first *financial year* of the relevant period and the average of the *annualised net written premiums* for business of that description carried on by the *firm* in each *financial year* of the relevant period was less than the threshold amount.
- (4) For the purposes of this *rule*:
- (a) the threshold amount is the amount determined in accordance with *PRU 7.5.18R(2)*; and
  - (b) the relevant period is the period of four *financial years* ending immediately before the beginning of the *financial year* in (1).
- 7.5.23 G If *PRU 7.5.22R* applies, a *firm* may need to make sufficient transfers from its *non-credit equalisation provision* to bring the *non-credit equalisation provision* for that *financial year* to zero.

The calculation: the maximum provision

- 7.5.24 R (1) For the purposes of the calculation required by *PRU 7.5.20R*, the amount of the maximum provision for any *insurance business grouping* is to be determined in accordance with (2) to (5).

- (2) Unless (4) applies, the amount of the maximum provision for the grouping, as at the end of a *financial year*, is the amount determined by multiplying X and Y.
- (3) For the purposes of (2):
  - (a) X is the percentage specified in Table *PRU 7.5.25R* in relation to the grouping; and
  - (b) Y is the average of the amount of the *annualised net written premiums* for non-credit *insurance business* in the grouping carried on by the *firm* in each *financial year* of the relevant period.
- (4) Where Y is a negative amount, the maximum provision for that *insurance business grouping* is zero.
- (5) For the purposes of (3)(b), the relevant period is the five-year period comprising:
  - (a) the *financial year* in (2); and
  - (b) the previous four *financial years*.

7.5.25 R Table : Calculation of maximum provision for any *insurance business grouping*

Insurance Business Grouping	Percentage of average annualised net written premiums
A	20
B	20
C	40
D	600
E	75

The calculation: provisional transfers-in

- 7.5.26 R
- (1) For the purposes of the calculation required by *PRU 7.5.20R*, the amount of the provisional transfers-in for any *insurance business grouping* is to be determined in accordance with (2).
  - (2) The amount of the provisional transfers-in for the grouping, as at the end of a *financial year*, is the amount determined by multiplying X and Y.
  - (3) For the purposes of (2):

- (a) X is the percentage specified in Table *PRU 7.5.27R* in relation to the grouping; and
- (b) Y is the amount of the *net written premiums* for non-credit *insurance business* in the grouping that was carried on by the *firm* in the *financial year* in (2), including adjustments in respect of previous *financial years*.

7.5.27 R Table : Provisional transfers-in for any *insurance business grouping*

Insurance Business Grouping	Percentage of net written premiums
A	3
B	3
C	6
D	75
E	11

7.5.28 G Since each *insurance business grouping* should be assessed individually, negative *net written premiums* in relation to any *insurance business grouping* should be transferred in to the *non-credit equalisation provision*.

The calculation: provisional transfers-out

- 7.5.29 R (1) For the purposes of the calculation required by *PRU 7.5.20R*, the amount of the provisional transfers-out for any *insurance business grouping* is to be determined in accordance with (2).
- (2) The amount of the provisional transfers-out for the grouping, as at the end of a *financial year*, is the lower of:
- (a) the amount of the maximum provision for the grouping under *PRU 7.5.24R* for that *financial year*; and
  - (b) the abnormal loss for the grouping under *PRU 7.5.30R* for that *financial year*.

7.5.30 R For each *insurance business grouping*, the abnormal loss as at the end of a *financial year* in relation to which an *equalisation provision* is calculated is:

- (1) (for business within the *insurance business grouping* accounted for on an accident year basis) the amount, if any, by which the amount of net *claims* incurred exceeds the greater of:
  - (a) zero; and
  - (b) the percentage of *net earned premiums* in that *financial year*

specified in the Table in *PRU 7.5.31R*; or

- (2) (for business within the *insurance business grouping* accounted for on an underwriting year basis) the amount, if any, by which the amount of net *claims* paid (plus adjustment for change in net *technical provisions*, other than any change in provisions for *claims* handling expenses or equalisation) exceeds the greater of:
- (a) zero; and
  - (b) the percentage of *net written premiums* in that *financial year* specified in the Table in *PRU 7.5.31R*.

7.5.31 R Table : Abnormal loss for any insurance business grouping

Insurance business grouping	Percentage of net written premiums
A	72.5
B	72.5
C	95
D	25
E	100

Adjustments to calculations

Transfers of business from the firm

- 7.5.32 R (1) This *rule* applies to modify the application of *PRU 7.5.24R* and *PRU 7.5.26R* in any case where a *firm* has transferred to another *undertaking* any rights and obligations under *general insurance contracts* falling within any *insurance business grouping*.
- (2) As at the end of the *financial year* in which the transfer takes place, *net written premiums* in respect of the transferred contracts in any grouping must be deducted from total *net written premiums* for that grouping before calculating the maximum provision under *PRU 7.5.24R* or provisional transfers-in under *PRU 7.5.26R*.

7.5.33 R If all the rights and obligations of a *firm* in relation to non-credit *insurance business* in any *insurance business grouping* have been transferred, the maximum provision for the grouping under *PRU 7.5.24R* is zero.

Transfers of business to the firm



- 7.5.34 R (1) This *rule* applies to modify the application of *PRU 7.5.24R*, *PRU 7.5.26R* and *PRU 7.5.29R* in any case where another *undertaking* has transferred to a *firm* any rights and obligations under *general insurance contracts* falling within any *insurance business grouping*.
- (2) As at the end of the *financial year* in which the transfer takes place a sum equal to that part of the consideration for the transfer that relates to business in an *insurance business grouping* must be:
- (a) excluded from net *premiums* (written or earned) before performing the calculations required by *PRU 7.5.24R* (maximum provision) and *PRU 7.5.26R* (provisional transfers in);
- (b) included in net *premiums* (written or earned) before performing the calculation required by *PRU 7.5.30R* (abnormal loss); and
- (c) excluded from net *claims* (paid or incurred) before performing the calculation required by *PRU 7.5.30R* (abnormal loss).
- 7.5.35 G For the purposes of *PRU 7.5.34R*, the consideration payable should be apportioned between *insurance business groupings* according to the groupings within which the *general insurance contracts* which are the subject of the acquisition fall. In appropriate cases, apportionment may reflect the split of liabilities acquired, including *unearned premium*.
- 7.5.36 G Where business is accounted for on an accounting year basis, in any year following the transfer, *net earned premiums* must include an appropriate amount in respect of the transfer.
- 7.5.37 G *PRU 7.5.32R* to *PRU 7.5.34R* apply to transfers by way of transfer under Part VII of the *Act* and by novation.

#### Credit Equalisation Provisions

##### Firms carrying on credit insurance business

- 7.5.38 R *PRU 7.5.39R* to *PRU 7.5.47G* apply to:
- (1) any *UK insurer*; and
- (2) any *non-EEA direct insurer*;
- which carries on the business of *effecting* or *carrying out general insurance contracts* falling within *general insurance business class 14* (which business, excluding contracts of *reinsurance*, is referred to in *PRU 7.5* as "*credit insurance business*").
- 7.5.39 R For the purposes of *PRU 7.5.43R*, a *UK insurer* must take account of the *credit insurance business* carried on by it world-wide.
- 7.5.40 R (1) For the purposes of *PRU 7.5.43R*:

- (a) a *Swiss general insurer* or an *EEA-deposit insurer* must take account of the *credit insurance business* carried on by it in the *United Kingdom*; and
  - (b) a *UK-deposit insurer* must take account of the *credit insurance business* carried on by it world-wide.
- (2) For the purposes of *PRU 7.5.44R*:
- (a) a *UK-deposit insurer* need only take account of the *credit insurance business* carried on by it in all *EEA States*, taken together; and
  - (b) any other description of *non-EEA direct insurer* (including an *EEA-deposit insurer* and a *Swiss general insurer*) need only take account of the *credit insurance business* carried on by it in the *United Kingdom*.

7.5.41 G For *UK insurers* the calculations must be made in respect of world-wide business

7.5.42 G The requirements of *PRU 7.5.39R* and *PRU 7.5.40R* are summarised in the table in *PRU 7.5.7G*.

#### Requirement to maintain credit equalisation provision

7.5.43 R In respect of each *financial year*, a *UK insurer* or a *non-EEA direct insurer* must, unless *PRU 7.5.44R* applies:

- (1) calculate the amount of its *credit equalisation provision* as at the end of that year in accordance with *PRU 7.5.45R*; and
- (2) maintain a *credit equalisation provision* calculated in accordance with *PRU 7.5.45R* for the following *financial year*.

7.5.44 R *PRU 7.5.43R* does not apply to any *UK insurer* or a *non-EEA direct insurer* in respect of any *financial year* if, as at the end of that year, the *annualised net written premiums* for its *credit insurance business* are less than 4% of *annualised net written premiums* in that *financial year* in respect of all its *general insurance business*, if this amount is less than 2,500,000 Euro.

#### Calculating the amount of the provision

7.5.45 R (1) The amount of a *UK insurer's*, or a *non-EEA direct insurer's*, *credit equalisation provision* as at the end of a *financial year* ("*financial year A*") is the higher of:

- (a) zero; and
- (b) whichever is the lower of:

- (i) 150% of the highest amount of *net written premiums* for credit *insurance business* carried on by the *firm* in *financial year A* or in any of the previous four *financial years*; and
- (ii) the amount of the *credit equalisation provision* brought forward from the preceding *financial year*, after making either of the adjustments in (2).

(2) The adjustments are:

- (a) the deduction of the amount of any technical deficit arising in *financial year A*; or
- (b) the addition of the lower of:
  - (i) 75% of the amount of any technical surplus arising in *financial year A*; and
  - (ii) 12% of the amount of the *net written premiums* for credit *insurance business* carried on by the *firm* in *financial year A*.

(3) For the purposes of (2) the amount of technical deficit or technical surplus is to be determined in accordance with *PRU 7.5.46R*.

7.5.46 R For the purposes of the adjustments in *PRU 7.5.45R(2)*, technical surplus (or technical deficit) in respect of credit *insurance business* is the amount by which the aggregate of *net earned premiums* and other technical income exceeds (or falls short of) the sum of net *claims* incurred, *claims* management costs and any technical charges.

7.5.47 G The calculation of technical surplus or technical deficit should be made before tax and before any transfer to or from the *credit equalisation provision*. Investment income should not be included in these calculations.

#### Euro conversion

7.5.48 R For the purposes of *PRU 7.5*, the exchange rate from the Euro to the pound sterling for each year beginning on 31 December is the rate applicable on the last day of the preceding October for which the exchange rates for the currencies of all the European Union member states were published in the Official Journal of the European Union.

- 7.6 Internal-contagion risk
- Application
- 7.6.1 R *PRU 7.6* applies to an *insurer*.
- 7.6.2 R *PRU 7.6* does not apply, to the extent stated, to any *insurer* in (1) to (4):
- (1) none of the provisions apply to *non-directive friendly societies*;
  - (2) none of the provisions, apart from *PRU 7.6.33R* (payment of financial penalties) apply to *firms* which qualify for authorisation under Schedule 3 or 4 of the *Act*;
  - (3) *PRU 7.6.33R* (payment of financial penalties) does not apply to *mutuals*;
  - (4) *PRU 7.6.41R* to *PRU 7.6.57R* (*UK branches* of certain *non-EEA insurers*) do not apply to:
    - (a) *UK insurers*; or
    - (b) *non-EEA insurers* which are *pure reinsurers*; or
    - (c) *EEA-deposit insurers*; or
    - (d) *Swiss general insurers*.
- 7.6.3 G The scope of application of *PRU 7.6* is not restricted to *firms* that are subject to the relevant EC directives. It applies, for example, to *pure reinsurers*.
- 7.6.4 R In its application to a *firm* with its head office in the *United Kingdom*, this section applies to the whole of the *firm's* business carried on world-wide.
- 7.6.5 R In the application of this section to activities carried on by a *non-EEA insurer*:
- (1) *PRU 7.6.13R* to *PRU 7.6.15G* and *PRU 7.6.41R* apply in relation to the whole of its business carried on world-wide;
  - (2) all other provisions of this section apply only in relation to:
    - (a) in the case of any *UK-deposit insurer*, activities carried on from *branches* in any *EEA State*; and
    - (b) in any other case, activities carried on from a *branch* in the *United Kingdom*.
- 7.6.6 G The adequacy of a *firm's* financial resources needs to be assessed in relation to all the activities of the *firm* and the risks to which they give rise.

7.6.7 G The requirements of this section apply to a *firm* on a solo basis.

Purpose

7.6.8 G This section sets out requirements for a *firm* relating to ‘internal-contagion risk’. This is the risk that losses or liabilities from one activity might deplete or divert financial resources held to meet liabilities from another activity. It arises where the two activities are carried on within the same *firm*. It may also arise from the combination of activities within the same *group*, but this aspect of internal-contagion risk falls outside the scope of this section. Requirements relevant to *group* contagion risk are set out in *PRU* 8.

7.6.9 G Internal-contagion risk includes in particular the risk that arises where a *firm* carries on:

- (1) both insurance and non-insurance activities; or
- (2) two or more different types of insurance activity; or
- (3) insurance activities from offices or *branches* located in both the *United Kingdom* and overseas.

7.6.10 G This section requires *firms* to limit non-insurance activities to those that directly arise from their *insurance business*, e.g. investing assets, employing insurance staff etc. It also requires that an adequate provision be established for non-insurance liabilities.

7.6.11 G This section also sets out requirements for the separation of different types of insurance activity. However, in most circumstances the combination of different types of insurance activity within the same *firm* is a source of strength. Adequate pooling and diversification of insurance risk is fundamental to sound business practice. The requirements, therefore, only apply in two specific cases where without adequate protection the combination might operate to the detriment of *policyholders*. They apply where a *firm* carries on both:

- (1) *general insurance business* and *long-term insurance business*;
- (2) *linked and non-linked insurance business*.

7.6.12 G Finally, the section sets out requirements to protect *policyholders* of *branches* of non-*EEA firms* where these are supervised by the *FSA*. These apply only to a non-*EEA firm* that has established a *branch* in the *United Kingdom*.

Requirements: non-insurance activities

Restriction of business to insurance

7.6.13 R (1) A *firm* must not carry on any commercial business other than *insurance business* and activities directly arising from that business.

- (2) (1) does not prevent a *friendly society* which was on 15 March 1979 carrying on *long-term insurance business* from continuing to carry on savings business.

Financial limitation of non-insurance activities

- 7.6.14 R A *firm* must limit, manage and control its non-insurance activities so that there is no significant risk arising from those activities that it may be unable to meet its liabilities as they fall due.
- 7.6.15 G For the purpose of *PRU 7.6.14R* a *firm* should consider how the financial impact of non-insurance activities might diverge from expectations. However, it need only take into account unexpected variations in amount and timing in so far as they are reasonably possible and may take into account effective mitigating factors.

Requirements: long-term insurance business

- 7.6.16 G *PRU 7.6.18R*, *PRU 7.6.21R*, *PRU 7.6.30R* and *PRU 7.6.31R* require a *firm* to identify the assets attributable to the receipts of the *long-term insurance business*, called *long-term insurance assets*, and only to apply those assets for the purpose of that business. This has the effect of prohibiting a *composite firm* from using *long-term insurance assets* to meet *general insurance liabilities*. It also keeps *long-term insurance assets* separate from shareholder funds.

Permissions not to include both types of insurance

- 7.6.17 G Under section 31 of the *Act*, a *firm* may not carry on a *regulated activity* unless it has *permission* to do so (or is exempt in relation to the particular activity). Both *general insurance business* and *long-term insurance business* are *regulated activities* and *permission* will extend to the *effecting* or *carrying out* of one or more particular *classes of contracts of insurance*. A *firm's permission* can be varied so as to add other *classes*. It is *FSA* policy, in compliance with EC directives on insurance, not to grant or vary *permission* if that would allow a *firm* to engage in both *general insurance business* and *long-term insurance business*. This does not apply where a *firm's permission* is restricted to *reinsurance*. It also does not apply where a *firm's permission* extends to *effecting* or *carrying out life and annuity contracts of insurance*. This will automatically include *permission* to *effect* or *carry out accident contracts of insurance* or *sickness contracts of insurance* on an ancillary or supplementary basis (see article 2(1) of the *Consolidated Life Directive*).

Separately identify and maintain long term insurance assets

- 7.6.18 R A *firm* carrying on *long-term insurance business* must identify the assets relating to its *long-term insurance business* which it is required to hold by virtue of *PRU 7.2.20R* and *PRU 7.2.21R*.
- 7.6.19 G *PRU 7.2.16R* requires a *firm* to establish adequate *technical provisions* for its *long-term insurance contracts*. *PRU 7.2.20R* requires a *firm* to hold *admissible assets* of a value at least equal to the amount of the *technical provisions*. *PRU*

7.2.21R ensures that a *composite firm* identifies separate *long-term insurance assets* with a value at least equal to the *technical provisions* for *long-term insurance business* as well as holding other assets of a value at least equal to the amount of its *technical provisions* for *general insurance business*. The overall impact of these provisions in *PRU 7.2*, and of *PRU 7.6.18R*, is that any *firm* writing *long-term insurance business* must identify separately its *long-term insurance assets* and ensure that their value is at least equal to the amount of its *long-term insurance business technical provisions*.

- 7.6.20 G *PRU 7.6.18R* does not prohibit a *firm* from identifying other assets as being available to meet the liabilities of its *long-term insurance business*. It may transfer such other assets to a *long-term insurance fund* (see *PRU 7.6.21R* and *PRU 7.6.22R*) and the transfer will take effect when it is recorded in the *firm's* accounting records (see *PRU 7.6.23R*). After the transfer takes effect, a *firm* may not transfer the assets out of a *long-term insurance fund* except where they represent an *established surplus* (see *PRU 7.6.27R*).
- 7.6.21 R (1) A *firm's* long-term insurance assets are the items in (2), adjusted to take account of:
- (a) outgo in respect of the *firm's* *long-term insurance business*; and
  - (b) any transfers made in accordance with *PRU 7.6.27R*.
- (2) The items are:
- (a) the assets identified under *PRU 7.6.18R* (including assets into which those assets have been converted);
  - (b) any other assets identified by the *firm* as being available to cover its *long-term insurance liabilities*;
  - (c) *premiums* and other receivables in respect of *long-term insurance contracts*;
  - (d) other receipts of the *long-term insurance business*; and
  - (e) all income and capital receipts in respect of the items in (2).
- 7.6.22 R (1) Unless (2) applies, all the *long-term insurance assets* of the *firm* constitute its long-term insurance fund.
- (2) Where a *firm* identifies particular *long-term insurance assets* in connection with different parts of its *long-term insurance business*, the assets identified in relation to each such part constitute separate long-term insurance funds of the *firm*.
- 7.6.23 R A *firm* must maintain a separate accounting record in respect of each of its *long-term insurance funds* (including any *with-profits fund*).

- 7.6.24 G *Firms* must ensure that *long-term insurance assets* are separately identified and allocated to a *long-term insurance fund* at all times. Assets in external accounts, for example at banks, custodians, or brokers should be segregated in the *firm's* books and records into separate accounts for *long-term insurance business* and *general insurance business*. Where a *firm* has more than one *long-term insurance fund*, a separate accounting record must be maintained for each fund. Accounting records should clearly document the allocation.
- 7.6.25 G Where the surplus arising from business is shared between *policyholders* and shareholders in different ways for different blocks of business, it may be necessary to maintain a separate fund to ensure that *policyholders* are, and will be, treated fairly. For example, if a proprietary company writes some business on a with-profits basis, this should be written in a *with-profits fund* separate from any business where the surplus arising from that business is wholly owned by shareholders.
- 7.6.26 G Where a *firm* merges separate funds for different types of business, it will need to ensure that the merger will not result in *policyholders* being treated unfairly. When considering merging the funds, the *firm* should consider the impact on its *PPFM* (see *COB* 6.10) and on its obligations to notify the *FSA* (see *SUP* 15.3). In particular, a *firm* would need to consider how any *inherited estate* would be managed and how the fund would be run in future, such that *policyholders* are treated fairly.
- 7.6.27 R A *firm* may not transfer assets out of a *long-term insurance fund* unless:
- (1) the assets represent an *established surplus*; and
  - (2) no more than three months have passed since the determination of that surplus.
- 7.6.28 G As a result of *PRU* 7.6.27R(2), an *actuarial investigation* undertaken to determine an *established surplus* remains in-date for three months from the date as at which the determination of the surplus was made. However, even where the investigation is still in-date, the *firm* should not make the transfer unless there is sufficient surplus at the time of the transfer to allow it to be made without breach of *PRU* 7.2.20R or *PRU* 7.2.21R.
- 7.6.29 G *PRU* 7.2.27R and *PRU* 7.2.28R provide further constraints on the transfer of assets out of a *with-profits fund*. *PRU* 7.2.27R requires a *firm* to have *admissible assets* in each of its *with-profits funds* to cover the *technical provisions* relating to all the business in that fund. *PRU* 7.2.28R requires a *realistic basis life firm* to ensure that the *realistic value of assets* for each of its *with-profits funds* is at least equal to the *realistic value of liabilities* of that fund.

#### Exclusive use of long-term insurance assets

- 7.6.30 R (1) A *firm* must apply a *long-term insurance asset* only for the purposes of its *long-term insurance business*.



- (2) For the purpose of (1), applying an asset includes coming under any obligation (even if only contingently) to apply that asset.

- 7.6.31 R A *firm* must not agree to, or allow, any mortgage or charge on its *long-term insurance assets* other than in respect of a *long-term insurance liability*.
- 7.6.32 G The purposes of the *long-term insurance business* include the payment of *claims*, expenses and liabilities arising from that business, the acquisition of lawful access to fixed assets to be used in that business and the investment of assets. The payment of liabilities may include repaying a loan but only where that loan was incurred for the purpose of the *long-term insurance business*. The purchase or investment of assets may include an exchange at fair *market value* of assets (including *money*) between the *long-term insurance fund* and other assets of the *firm*.

#### Payment of financial penalties

- 7.6.33 R If the *FSA* imposes a financial penalty on a *long-term insurer*, the *firm* must not pay that financial penalty from a *long-term insurance fund*.
- 7.6.34 G *PRU 7.6.2R* states that this provision applies to all *firms*, except *mutuals*, and includes *firms* qualifying for authorisation under Schedule 3 or 4 to the *Act*.

#### Requirements: property-linked funds

- 7.6.35 G *PRU 4.2.57R* requires a *firm* to cover, as closely as possible, its *property-linked liabilities* by the property to which those liabilities are linked. In order to comply with this *rule*, a *firm* should identify the assets it holds to cover *property-linked liabilities* and should not apply those assets (as long as they are needed to cover the *property-linked liabilities*) for any purpose other than to meet those liabilities.
- 7.6.36 R A *firm* must select, allocate and manage the assets to which its *property-linked liabilities* are linked taking into account:
- (1) the *firm's* contractual obligations to holders of *property-linked policies*; and
  - (2) its regulatory duty to treat *customers* fairly, including in the way it makes discretionary decisions as to how it selects, allocates and manages assets.
- 7.6.37 G *Property-linked liabilities* may be linked either to specified assets (with no contractual discretion given to the *firm* as to the choice of assets) or to assets of a specified kind where the selection of the actual assets is left to the *firm*.

#### Requirements: UK branches of certain non-EEA firms

- 7.6.38 G The purpose of the *rules* and *guidance* set out in *PRU 7.6.38G* to *PRU 7.6.57R* is to protect against the risk that the financial resources required in respect of the activities of the *United Kingdom* (or *EEA*) *branch(es)* might be depleted by the other activities of the *non-EEA direct insurer*.

- 7.6.39 G By virtue of *PRU 7.6.2R(4)*, the *rules* in *PRU 7.6.41R* to *PRU 7.6.57R* apply to *non-EEA direct insurers* except for *Swiss general insurers* and *EEA-deposit insurers*. Responsibility for determining the adequacy of the world-wide financial resources of *Swiss general insurers* or *EEA-deposit insurers* rests exclusively with the Swiss authorities or the authorities in the *EEA state* (other than the *United Kingdom*) in which the deposit was made.
- 7.6.40 G (1) *PRU 7.6.41R* requires a *non-EEA direct insurer* to hold adequate world-wide resources to meet the needs of the world-wide business without the need to rely on *UK* or *EEA branch* assets other than to meet *branch liabilities*.
- (2) *PRU 7.6.42R* to *PRU 7.6.47R* require *non-EEA direct insurers* to calculate a local *MCR* and to hold assets representing that requirement in the *EEA* or the *United Kingdom*.
- (3) *PRU 7.6.48R* to *PRU 7.6.52R* require *non-EEA direct insurers* to hold a minimum level of assets in the *United Kingdom* or *EEA*.
- (4) *PRU 7.6.54R* requires the deposit of a minimum level of assets in the *United Kingdom*.
- (5) *PRU 7.6.56R* and *PRU 7.6.57R* require *non-EEA direct insurers* to keep adequate accounting records in the *United Kingdom*.

#### Worldwide financial resources

- 7.6.41 R (1) A *non-EEA direct insurer* must maintain adequate worldwide financial resources, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.
- (2) For the purpose of (1):
- (a) a *UK-deposit insurer* must not rely upon the assets held under *PRU 7.2.20R* as available to meet liabilities other than those arising from the activities of its *branches* in *EEA States*;
- (b) other *non-EEA direct insurers* to whom (1) applies must not rely upon the assets held under *PRU 7.2.20R* as available to meet liabilities other than those arising from the activities of any *UK branch*.

#### UK or EEA MCR to be covered by admissible assets

- 7.6.42 R A *non-EEA direct insurer* must:
- (1) calculate a *UK* or *EEA MCR* in accordance with *PRU 7.6.44R* to *PRU 7.6.47R*; and
- (2) hold *admissible assets* (in addition to those required under *PRU 7.2.20R*)

to represent its *UK* or *EEA MCR* calculated under (1).

- 7.6.43 R The assets held under *PRU 7.6.42R(2)* must be identified and valued as if the *non-EEA direct insurer* was a *firm* with its head office in the *United Kingdom*.
- 7.6.44 R For the purposes of *PRU 7.6.42R*, a *non-EEA direct insurer* (except a *UK-deposit insurer*) must calculate a *UK MCR*:
- (1) for *long-term insurance business*, in accordance with *PRU 7.2.81R* to *PRU 7.2.91R* but only in relation to business carried on by the *firm* in the *United Kingdom*;
  - (2) for *general insurance business*, in accordance with *PRU 7.2.45R* to *PRU 7.2.72R* but only in relation to business carried on by the *firm* in the *United Kingdom*.
- 7.6.45 R For a *composite firm*, the *UK MCR* is the sum of the amounts arrived at under *PRU 7.6.44R(1)* and (2).
- 7.6.46 R For the purposes of *PRU 7.6.42R*, a *UK-deposit insurer* must calculate an *EEA MCR*:
- (1) for *long-term insurance business*, in accordance with *PRU 7.2.81R* to *PRU 7.2.91R* but only in relation to business carried on by the *firm* in all *EEA States*, taken together;
  - (2) for *general insurance business*, in accordance with *PRU 7.2.45R* to *PRU 7.2.72R* but only in relation to business carried on by the *firm* in all *EEA States*, taken together.
- 7.6.47 R For a *composite firm*, the *EEA MCR* is the sum of the amounts arrived at under *PRU 7.6.46R(1)* and (2).

#### Localisation of assets

- 7.6.48 R A *non-EEA direct insurer* (except a *UK-deposit insurer*) must hold *admissible assets*, which are required to cover its *technical provisions* in accordance with *PRU 7.2.20R* and to represent its *UK MCR* in accordance with *PRU 7.6.44R*:
- (1) (where the assets cover the *technical provisions* and the *guarantee fund*) in the *United Kingdom*;
  - (2) (where the assets represent the amount of the *UK MCR* in excess of the *guarantee fund*) in any *EEA State*.
- 7.6.49 R A *UK-deposit insurer* must hold *admissible assets*, which are required to cover its *technical provisions* in accordance with *PRU 7.2.20R* and to represent its *EEA MCR* in accordance with *PRU 7.6.46R*:

- (1) (where the assets cover the *technical provisions* and the *guarantee fund*) within the *EEA* states where the *firm* carries on *insurance business*;
  - (2) (where the assets represent the amount of the *EEA MCR* in excess of the *guarantee fund*) in any *EEA State*.
- 7.6.50 R *PRU 7.6.48R* and *PRU 7.6.49R* do not apply to assets covering *technical provisions* which are debts owed by *reinsurers*.
- 7.6.51 G The *admissible assets* in excess of the *technical provisions* and *UK* or *EEA MCR* may be held outside the *EEA*.
- 7.6.52 R For the purpose of *PRU 7.6.48R* and *PRU 7.6.49R*:
- (1) a tangible asset is to be treated as held in the country or territory where it is situated;
  - (2) an *admissible asset* consisting of a *claim* against a debtor is to be regarded as held in any country or territory where it can be enforced by legal action;
  - (3) a *listed security* is to be treated as held in any country or territory where there is a *regulated market* in which the security is dealt; and
  - (4) a *security* which is not a *listed security* is to be treated as held in the country or territory in which the *issuer* has its head office.
- 7.6.53 G *PRU 4.2.53R* to *PRU 4.2.55R* (currency matching of assets and liabilities) apply to the assets held to match insurance liabilities calculated under *PRU 7.2.12R* or *PRU 7.2.16R*.

#### Deposit of assets as security

- 7.6.54 R A *non-EEA direct insurer* must keep assets of a value at least equal to one half of the *base capital resources requirement* on deposit in the *United Kingdom* with a *BCD credit institution*.
- 7.6.55 G The assets deposited as security may count towards the assets required under *PRU 7.6.48R* and *PRU 7.6.49R*. If, after the deposit is made, the value of the deposited assets falls below one half of the *base capital resources requirement*, the *firm* should deposit further *admissible assets* in order to comply with *PRU 7.6.48R* and *PRU 7.6.49R*. Deposited assets may be exchanged for other *admissible assets* and excess assets may be withdrawn, provided that the exchange or deposit does not cause a breach of *PRU 7.6.48R* or *PRU 7.6.49R*.

#### Branch accounting records in the United Kingdom

- 7.6.56 R A *non-EEA direct insurer* must maintain at a place of business in the *United Kingdom* adequate records relating to:
- (1) the activities carried on from its *United Kingdom branch*; and

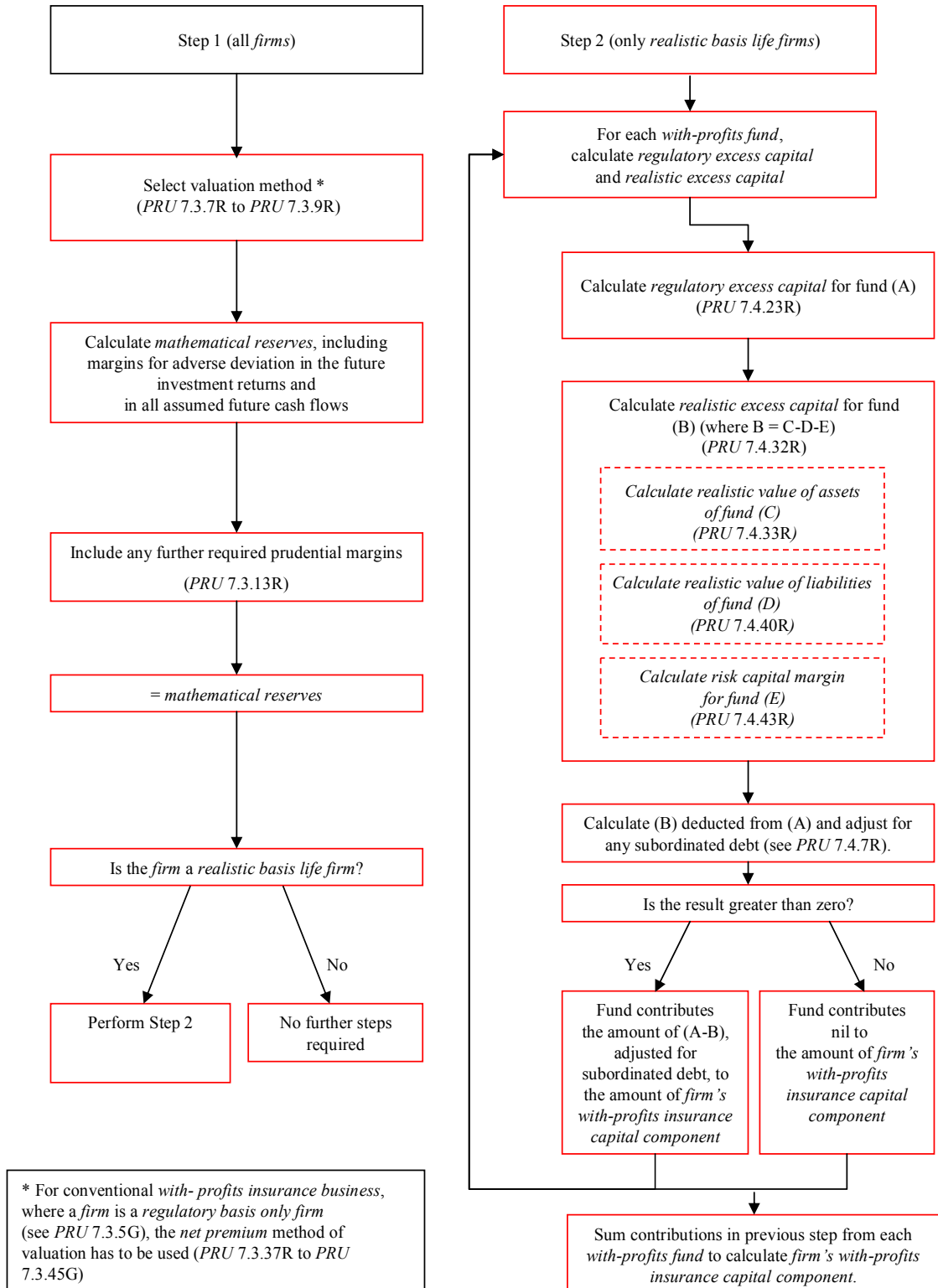
- (2) if it is an *EEA-deposit insurer*, the activities carried on from the *branches* in other *EEA States*.

7.6.57 R The records maintained as required by *PRU 7.6.56R* must include a record of:

- (1) the income, expenditure and liabilities arising from activities of the *branch* or *branches*; and
- (2) the assets identified under *PRU 7.2.20R* as available to meet those liabilities.

**Annex 1G**

**PRU 7.3 (Mathematical reserves) and PRU 7.4 (With-profits insurance capital component)**



## Annex J

### PRU 8.3

In this Annex, all the text is new and is not underlined.

#### 8.3 Group Risk: Insurance Groups

##### Application

8.3.1 R *PRU 8.3* applies to an *insurer* that is:

- (1) a *participating insurance undertaking*; or
- (2) a member of an *insurance group* (which is not a *participating insurance undertaking*).

8.3.2 R *PRU 8.3* does not apply to:

- (1) a *non-directive friendly society*; or
- (2) a *Swiss general insurer*; or
- (3) an *EEA-deposit insurer*; or
- (4) an *incoming EEA firm*; or
- (5) an *incoming Treaty firm*.

8.3.3 G *PRU 8.3* applies to a *firm*:

- (1) on a solo basis, as an adjusted solo calculation, where that *firm* is a *participating insurance undertaking*; and
- (2) on a group basis where that *firm* is a member of an *insurance group*.

8.3.4 G For the purposes of *PRU 8.3*, an *insurer* includes a *pure reinsurer*, a *friendly society* (other than a *non-directive friendly society*) and a *non-EEA insurer*.

##### Purpose

8.3.5 G The purpose of this section is to implement the *Insurance Groups Directive* on supplementary supervision of *firms* in an *insurance group*, as amended by the *Financial Groups Directive*. The *Financial Groups Directive* (by amending the *Insurance Directives* and the *Insurance Groups Directive*) introduces specific requirements for the treatment of *related undertakings* of an *insurance parent undertaking* or a *participating insurance undertaking* that are *credit institutions*, *investment firms* or *financial institutions*.

8.3.6 G *PRU 8.3* sets out the *sectoral rules* for *insurers* for:

- (1) *firms* that are *participating insurance undertakings* carrying out an adjusted solo calculation as contemplated by *PRU 2.1.9R(2)*;
- (2) *insurance groups*; and
- (3) *insurance conglomerates*.

8.3.7 G For a *firm* that is a *participating insurance undertaking*, the *rules* in *PRU 8.3* set out the minimum capital adequacy requirements for the *firm* itself. A *firm* that satisfies the test in *PRU 8.3.9R* in relation to its *group capital resources* is deemed by *PRU 2.1.9R(2)* to be in compliance with the capital adequacy requirement set out in *PRU 2.1.9R(1)*.

Requirement to calculate GCR and GCRR

8.3.8 R A *firm* must on a regular basis calculate the *group capital resources (GCR)* and *group capital resources requirement (GCRR)* of each *undertaking* referred to in *PRU 8.3.17R*.

Requirement to maintain group capital

8.3.9 R Where a *firm* is the *undertaking* referred to in *PRU 8.3.17R(1)(c)* or *PRU 8.3.17R(2)*, it must maintain at all times *tier one capital resources* and *tier two capital resources* of such an amount that its *group capital resources* are equal to or exceed its *group capital resources requirement*.

8.3.10 R A *firm* that is both:

- (1) a *composite firm*; and
- (2) an *undertaking* referred to in *PRU 8.3.17R(1)(c)* or *PRU 8.3.17R(2)*;

must comply with *PRU 8.3.9R* separately in respect of its *long-term insurance business* and its *general insurance business*.

8.3.11 R For the purposes of *PRU 8.3.10R*, a *firm* must include in the calculation of the *group capital resources* and *group capital resources requirement* of its *long-term insurance business* the *regulated related undertakings* and *ancillary services undertakings* that are *long-term insurance assets*.

8.3.12 G *PRU 7.6* sets out the detailed requirements for the separation of *long-term* and *general insurance business*.

8.3.13 G In order to comply with *PRU 8.3.10R*, a *composite firm* will need to:

- (1) establish the *group capital resources requirement* of its *general insurance business* and its *long-term insurance business* separately; and
- (2) allocate its *group capital resources* between its *general insurance business* and its *long-term insurance business* so that:



- (a) the *group capital resources* allocated to its *general insurance business* are equal to or in excess of the *group capital resources requirement* of its *general insurance business*; and
  - (b) the *group capital resources* allocated to its *long-term insurance business* are equal to or in excess of the *group capital resources requirement* of its *long-term insurance business*.
  
- 8.3.14 G Surplus *group capital resources* in the *long-term insurance business* cannot be used towards meeting the requirements of the *general insurance business* (see *PRU 8.3.41R*) but surplus *group capital resources* in the *general insurance business* may be used towards meeting the amount of the *group capital resources requirement* that relates to the *long-term insurance business*.
  
- 8.3.15 R Subject to *PRU 8.3.27R*, a *firm* must ensure that at all times its *capital resources* are of such an amount that the *group capital resources* of each *undertaking* referred to in *PRU 8.3.17R* (excluding those referred to in *PRU 8.3.9R*) are equal to or exceed that *undertaking's group capital resources requirement*.
  
- 8.3.16 G *Principle 4* requires a *firm* to maintain adequate financial resources, taking into account any activity of other members of the *group* of which the *firm* is a member. *PRU 8.3* sets out provisions that deal specifically with the way the activities of other members of the *group* should be taken into account. This results in the *firm* being required to hold sufficient capital resources so that the *group capital resources* are at least equal to the *group capital resources requirement*. However, the adequacy of the *group capital resources* needs to be assessed both by the *firm* and the *FSA*. *Firms* are required to carry out an assessment of the adequacy of their financial resources (*PRU 1.2.26R*) and the *FSA* will review this and may provide individual guidance on the amount and quality of *capital resources* the *FSA* considers adequate. As part of such reviews, the *FSA* may also form a view on the appropriateness of the *group capital resources requirement* and *group capital resources*. Where necessary, the *FSA* may also give individual guidance on the *capital resources* a *firm* should hold in order to comply with *Principle 4* expressed by reference to *PRU 8.3.9R* and *PRU 8.3.15R*.

Scope – undertakings whose group capital is to be calculated and maintained

- 8.3.17 R The *undertakings* referred to in *PRU 8.3.8R*, *PRU 8.3.9R*, *PRU 8.3.10R* and *PRU 8.3.15R* are:
  - (1) for any *firm* that is not within (2), each of the following:
    - (a) its *ultimate insurance parent undertaking*;
    - (b) its *ultimate EEA insurance parent undertaking* (if different);

- and
- (c) the *firm* itself, if it is a *participating insurance undertaking*; and
- (2) the *firm* itself, where the *firm* is a *participating insurance undertaking* and is:
- (a) a *pure reinsurer*; or
- (b) a *non-EEA insurer*; or
- (c) a *friendly society*.
- 8.3.18 G Article 3(3) of the *Insurance Groups Directive* allows an *undertaking* to be excluded from supplementary supervision if:
- (1) its head office is in a non-*EEA State* where there are legal impediments to the transfer of the necessary information; or
- (2) in the opinion of the *competent authority* responsible for exercising supplementary supervision, having regard to the objectives of supplementary supervision:
- (a) its inclusion would be inappropriate or misleading; or
- (b) it is of negligible interest.
- 8.3.19 G If an application is made for a *waiver*, it is the policy of the *FSA* to consider the effect, in the circumstances described in *PRU 8.3.18G*, of granting a *waiver* allowing the exclusion of a *related undertaking* from the calculation of *group capital resources* and the *group capital resources requirement* required by *PRU 8.3.8R*.
- 8.3.20 G Examples of *related undertakings* which may be excluded from supplementary supervision by Article 3(3) of the *Insurance Groups Directive* include *insurance holding companies* in the *insurance group* that are not the *ultimate insurance parent undertaking* or, if different, the *ultimate EEA insurance parent undertaking* of a *firm*.
- 8.3.21 G If more than one member of the *insurance group* is to be excluded in the circumstances described in *PRU 8.3.18G(2)(b)*, they may only be excluded if, considered together, they are of negligible interest in the context of the *insurance group*.
- 8.3.22 G When giving a *waiver* in the circumstances described in *PRU 8.3.18G*, the *FSA* may impose a condition requiring the *firm* to provide information about any member of the *insurance group* excluded pursuant to a *waiver* granted in the circumstances described in *PRU 8.3.18G*.

Optional alternative method of calculation for firms subject to supplementary

supervision by another EEA competent authority

- 8.3.23 R If the *competent authority* in an *EEA State* other than the *United Kingdom* has agreed to be the *competent authority* responsible for exercising supplementary supervision of an *insurance group* of which a *firm* is a member under Article 4(2) of the *Insurance Groups Directive*, the *firm* may prepare the calculations required under *PRU 8.3.8R* in relation to the *ultimate EEA insurance parent undertaking* in accordance with the requirements of supplementary supervision in that *EEA State*.
- 8.3.24 G The *FSA* will notify the *firm* if it has reached agreement with the *competent authority* in an *EEA State* other than the *United Kingdom* in accordance with Article 4(2) of the *Insurance Groups Directive*.

Non-EEA ultimate insurance parent undertakings

- 8.3.25 R Where the *ultimate insurance parent undertaking* of a *firm* has its head office in a non-*EEA State*, the *firm* may:
- (1) calculate the *group capital resources* and the *group capital resources requirement* of its *ultimate insurance parent undertaking* in accordance with accounting practice applicable for the purposes of the regulation of *insurance undertakings* in the state or territory of the head office of the *ultimate insurance parent undertaking* adapted as necessary to apply the general principles set out in Annex I (1) paragraphs B, C and D of the *Insurance Groups Directive*; and
  - (2) elect (see *PRU 8.3.26R*) to carry out the calculation referred to in (1) in accordance with the accounting consolidation method set out in Annex I (3) of the *Insurance Groups Directive*.
- 8.3.26 R A *firm* may elect to use the calculation method referred to in *PRU 8.3.25R* (2) if it has made the election by written notice to the *FSA* in a way that complies with the requirements for written notice in *SUP 15.7*.
- 8.3.27 R *PRU 8.3.15R* does not apply in respect of the *group capital resources* of a *firm's ultimate insurance parent undertaking* if that *ultimate insurance parent undertaking* has its head office in a non-*EEA State*.

Proportional holdings

- 8.3.28 R Subject to *PRU 8.3.30R* and *PRU 8.3.31R*, when calculating *group capital resources* and the *group capital resources requirement* of an *undertaking* in *PRU 8.3.17R*, a *firm* must take only the relevant proportion of the following items ("calculation items") into account:
- (1) the *solo capital resources* of a *regulated related undertaking*;
  - (2) the assets of a *regulated related undertaking* which are required to be deducted as part of the calculation of *group capital resources*; and
  - (3) the *individual capital resources requirement* of a *regulated related*

*undertaking.*

- 8.3.29 R In *PRU 8.3.28R*, the relevant proportion is either:
- (1) the proportion of the total number of issued *shares* in the *regulated related undertaking* held, directly or indirectly, by the *undertaking* in *PRU 8.3.17R*; or
  - (2) where a *consolidation Article 12(1) relationship* exists between *related undertakings* within the *insurance group*, such proportion as the *FSA* determines in accordance with Article 28(5) of the *Financial Groups Directive* and Regulation 15 of the *Financial Groups Directive Regulations*.
- 8.3.30 R Where the *undertaking* in *PRU 8.3.17R* is a *firm*, if the *individual capital resources requirement* of a *regulated related undertaking* that is a *subsidiary undertaking* and not an *insurer* exceeds the *solo capital resources* of that *undertaking* less the amount calculated in *PRU 8.3.74R(3)* (if any), the full amount of the calculation items of that *regulated related undertaking* less the amount in *PRU 8.3.74R(3)* must be taken into account in the calculation of *group capital resources* and the *group capital resources requirement*.
- 8.3.31 R Except where *PRU 8.3.30R* applies, if the *individual capital resources requirement* of a *regulated related undertaking* that is a *subsidiary undertaking* of the *undertaking* in *PRU 8.3.17R* exceeds its *solo capital resources*, the full amount of the calculation items of that *regulated related undertaking* must be taken into account in the calculation of *group capital resources* and the *group capital resources requirement*.
- 8.3.32 R For the purposes of *PRU 8.3.10R*, where a *composite firm* that is an *undertaking* in *PRU 8.3.17R(1)(c)* or (2):
- (1) holds directly or indirectly *shares* in a *regulated related undertaking*; and
  - (2) the *shares* in (1) are held partly by its *long-term insurance business* and partly by its *general insurance business*;
- the relevant proportion of the calculation items calculated in accordance with *PRU 8.3.29R*, subject to *PRU 8.3.30R* and *PRU 8.3.31R*, must be allocated between the *long-term* and *general insurance business* in proportion to their respective holdings, directly or indirectly, in the *shares* in that *regulated related undertaking*.

#### Calculation of the GCRR

- 8.3.33 R Subject to *PRU 8.3.23R* and *PRU 8.3.25R*, a *firm* must calculate the *group capital resources requirement* of an *undertaking* in *PRU 8.3.17R* as the sum of the *individual capital resources requirement* of that *undertaking* and the *individual capital resources requirement* of each of its *regulated related*

*undertakings.*

8.3.34 R For the purposes of *PRU 8.3*, an *individual capital resources requirement* is:

- (1) in respect of an *insurer* that is not within (2):
  - (a) its *capital resources requirement* calculated in accordance with *PRU 2.1*; less
  - (b) where the *capital resources requirements* of both the *insurer* and its *insurance parent undertaking* that is an *insurer* include *with-profits insurance capital components*, any element of double-counting that may arise from the aggregation of the *individual capital resources requirements* for the purposes of *PRU 8.3.33R*;
- (2) in respect of an *insurer* that is either a *pure reinsurer* or whose main business otherwise consists of *reinsurance*, and whose head office is in the *United Kingdom*, the *capital resources requirement* that would apply to the *firm* in accordance with *PRU 2.1* if its *insurance business* was not restricted to *reinsurance*;
- (3) in respect of an *insurance undertaking* that is not within (1) or (2) and whose main business is *reinsurance* and whose head office is in a *designated State or territory*, either:
  - (a) the *proxy capital resources requirement* that would apply to it if, in connection with its *reinsurance* activities, the *permissions* on the basis of which that *proxy capital resources requirement* is calculated were *permissions* to carry on *insurance business* that is not restricted to *reinsurance*; or
  - (b) the *solo capital resources requirement* that would apply to it if, in connection with its *reinsurance* activities, the *insurance undertaking* were a *regulated insurance entity* whose *insurance business* is not restricted to *reinsurance* for the purposes of calculating the *solo capital resources requirement* in accordance with the relevant *sectoral rules* of the *designated State or territory*;
- (4) in respect of an *insurance undertaking* that is not within (1) to (3) and whose main business is *reinsurance*, the *proxy capital resources requirement* that would apply to it if, in connection with its *reinsurance* activities, the *permissions* on the basis of which that *proxy capital resources requirement* is calculated were *permissions* to carry on *insurance business* that is not restricted to *reinsurance*;
- (5) in respect of an *EEA insurer*, the equivalent of the *capital resources requirement* as calculated in accordance with the applicable requirements in its *Home State*;

- (6) in respect of an *insurance undertaking* that is not within (1) to (5) and whose head office is in a *designated State or territory*, either:
  - (a) the *solo capital resources requirement* applicable to it in that *designated State or territory*; or
  - (b) its *proxy capital resources requirement*;
- (7) in respect of an *insurance undertaking* that is not within (1) to (6), its *proxy capital resources requirement*;
- (8) in respect of a *regulated entity* with its head office in the *EEA* (excluding an *insurance undertaking*), its *solo capital resources requirement* calculated in accordance with the *sectoral rules* for the *financial sector* applicable to it in the *EEA State* in which it has its head office;
- (9) in respect of a *regulated entity* not within (8) (excluding an *insurance undertaking*), its *solo capital resources requirement*;
- (10) in respect of an *asset management company*, the *solo capital resources requirement* that would apply to it if, in connection with its activities, it were treated as an *investment firm* for the purposes of calculating the *solo capital resources requirement*;
- (11) in respect of a *financial institution* that is not a *regulated entity* (including a *financial holding company*), the *solo capital resources requirement* that would apply to it if, in connection with its activities, it were treated as being within the *banking sector*; and
- (12) in respect of an *insurance holding company*, zero.

8.3.35 G The *Insurance Groups Directive* defines reinsurers in terms of the 'main business' they carry on. Under the directive, the individual capital resources requirements for reinsurers (including those whose head office is in the *United Kingdom*) are to be calculated on the basis of requirements analogous to those applicable to direct insurers (that is, *insurers* carrying on insurance business that is not restricted to *reinsurance*). Although *insurers* that are *pure reinsurers* are already subject to *PRU*, there are a number of respects in which the capital regime that applies to them differs from that applicable to *insurers* who are direct insurers. The effect of *PRU* 8.3.34R(2) to (4) is to calculate the *individual capital resources requirement* for all reinsurers as if they were carrying on direct insurance. This applies to:

- (1) *pure reinsurers* whose head office is in the *United Kingdom*;
- (2) *insurers* whose head office is in the *United Kingdom* and whose main business is *reinsurance* (because an *insurer* that is not a *pure reinsurer* with their business restricted to *reinsurance* may nevertheless in principle still have *reinsurance* as its main business);

- (3) reinsurers whose head office is in another *EEA State*;
- (4) reinsurers whose head office is in a *designated State or territory* (other than an *EEA State*); and
- (5) reinsurers whose head office is outside the *EEA*.

#### Calculation of GCR

- 8.3.36 R For the purposes of *PRU 8.3.8R* and subject to *PRU 8.3.23R* and *PRU 8.3.25R*, a *firm* must calculate the group capital resources of an *undertaking* in *PRU 8.3.17R* in accordance with the table in *PRU 8.3.43R*, subject to the limits in *PRU 8.3.45R*.
- 8.3.37 R For the purposes of *PRU 8.3*, the following expressions when used in relation to either an *undertaking* in *PRU 8.3.17R* or a *regulated related undertaking* which is not subject to *PRU 2.2.14R*, are to be construed as if that *undertaking* were required to calculate its capital resources in accordance with *PRU 2.2.14R*, but with such adjustments being made to secure that the *undertaking's* calculation of its *solo capital resources* complies with the relevant *sectoral rules* applicable to it:
- (1) *tier one capital resources*;
  - (2) *tier two capital resources*;
  - (3) *upper tier two capital resources*;
  - (4) *lower tier two capital resources*;
  - (5) *innovative tier one capital resources*; and
  - (6) *core tier one capital*.
- 8.3.38 R For the purposes of *PRU 8.3.37R*, the *sectoral rules* applicable to:
- (1) an *insurance holding company* are the *sectoral rules* that would apply to it if, in connection with its activities, it were treated as an *insurer*;
  - (2) an *asset management company* are the *sectoral rules* that would apply to it if, in connection with its activities, it were treated as an *investment firm*; and
  - (3) subject to *PRU 8.3.39R*, a *financial institution*, that is not a *regulated entity*, are the *sectoral rules* that would apply to it if, in connection with its activities, it were treated as being within the *banking sector*.
- 8.3.39 R Where a *financial institution*, that is not a *regulated entity*, has invested in *tier one capital* or *tier two capital* issued by a *parent undertaking* that is:

- (1) an *insurance holding company*; or
- (2) an *insurer*;

the *sectoral rules* that apply to that *financial institution* are the *sectoral rules* for the *insurance sector*.

8.3.40 R For the purposes of *PRU 8.3.36R*, the *capital resources* of a *financial institution* within *PRU 8.3.39R* that can be included in the calculations in *PRU 8.3.48R(2)*, *PRU 8.3.50R(2)*, *PRU 8.3.53R(2)*, *PRU 8.3.55R(2)* and *PRU 8.3.57R(2)* are:

- (1) the issued *tier one capital* or *tier two capital* of that *financial institution* held, directly or indirectly, by its *parent undertaking* referred to in *PRU 8.3.39R*; and
- (2) the lower of:
  - (a) the *tier one capital* or *tier two capital* issued by the *parent undertaking* referred to in *PRU 8.3.39R* pursuant to the investment by the *financial institution*; and
  - (b) the *tier one capital* or *tier two capital* issued by the *financial institution* to raise funds for its investment in the *capital resources* of the *parent undertaking* referred to in (a).

8.3.41 R (1) In calculating *group capital resources*, a *firm* must exclude the restricted assets of a *regulated related undertaking* except insofar as those assets are available to meet the *individual capital resources requirement* of that *regulated related undertaking*.

(2) In (1), "restricted assets" means assets of a *regulated related undertaking* which are subject to a legal restriction or other requirement having the effect that those assets cannot be transferred or otherwise made available to another *regulated related undertaking* for the purposes of meeting its *individual capital resources requirement* without causing a breach of that legal restriction or requirement.

8.3.42 G For the purposes of *PRU 8.3.41R*, in respect of an *insurance undertaking* that is a member of an *insurance group*, the assets of a *long-term insurance fund* are restricted assets within the meaning of *PRU 8.3.41R*. Any excess of assets over liabilities in the *long-term insurance business* may only be included in the calculation of the *group capital resources* up to the amount of the *capital resources requirement* related to that *long-term insurance business*.

8.3.43 R Table: Group capital resources

	Stage	Related text
Total group tier one capital		



	A	PRU 8.3.48R
Total group tier two capital	B	PRU 8.3.50R
Group capital resources before deductions	C=(A+B)	
Total deductions of inadmissible assets	D	PRU 8.3.59R
Total deductions under the requirement deduction method from group capital resources	E	PRU 8.3.62R
Total deductions of ineligible surplus capital*	F	PRU 8.3.65R
Deduction of assets in excess of market risk and counterparty exposure limits*	G	PRU 8.3.70R
Group capital resources	H=(C-(D+E+F*+G*))	
* = section (F) of the table (the deductions for ineligible surplus capital) and section (G) of the table (assets in excess of market risk and counterparty exposure limits) only apply and are required to be calculated for the purposes of the adjusted solo calculation of an <i>undertaking</i> in PRU 8.3.17R that is a <i>participating insurance undertaking</i> .		

#### Calculation of GCR – Limits on the use of different forms of capital

- 8.3.44 G As the various components of capital differ in the degree of protection that they offer the *insurance group*, restrictions are placed on the extent to which certain types of capital are eligible for inclusion in the *group capital resources* of the *undertaking* in PRU 8.3.17R. These restrictions are set out in PRU 8.3.45R.
- 8.3.45 R (1) For the purposes of PRU 8.3.9R, PRU 8.3.10R and PRU 8.3.15R, a *firm* must ensure that at all times its *tier one capital resources* and *tier two capital resources* are of such an amount that the *group capital resources* of the *undertaking* in PRU 8.3.17R comply with the following limits:
- (a)  $(P - Q) \geq \frac{1}{2} (R - S)$ ;

- (b)  $(P - Q + T - W) \geq \frac{3}{4} (R - S)$ ;
  - (c)  $V \geq \frac{1}{2} P$ ;
  - (d)  $Q \leq 15\%$  of P;
  - (e)  $T \leq P$ ; and
  - (f)  $W \leq \frac{1}{2} P$
- (2) For the purposes of *PRU 8.3.9R* and *PRU 8.3.10R*, a *firm* must ensure that at all times its *tier one capital resources* and *tier two capital resources* are of such an amount that its *group capital resources* comply with the following limit:

$$(P - Q + T) \geq \frac{1}{3}X + (R - S - U - X).$$

- (3) For the purposes of (1) and (2):
- (a) P is the *total group tier one capital* of the *undertaking* in *PRU 8.3.17R*;
  - (b) Q is the sum of the *innovative tier one capital resources* calculated in accordance with *PRU 8.3.53R*;
  - (c) R is the *group capital resources requirement* of the *undertaking* in *PRU 8.3.17R*;
  - (d) S is the sum of all the *with-profits insurance capital components* of an *undertaking* in *PRU 8.3.17R* that is an *insurer* and each of its *regulated related undertakings* that is an *insurer*;
  - (e) T is the *total group tier two capital* of the *undertaking* in *PRU 8.3.17R*;
  - (f) U is the sum of all the *resilience capital requirements* of an *undertaking* in *PRU 8.3.17R* that is an *insurer* and each of its *regulated related undertakings* that is an *insurer*;
  - (g) V is the sum of all the *core tier one capital* calculated in accordance with *PRU 8.3.55R*;
  - (h) W is the sum of the *lower tier two capital resources* calculated in accordance with *PRU 8.3.57R*; and
  - (i) X is the *MCR* of the *firm* less its *resilience capital requirement*, if any.

8.3.46 G The amount of any capital item excluded from *group capital resources* under *PRU 8.3.45R(1)(d)* may form part of *total group tier two capital* calculated in accordance with *PRU 8.3.50R* subject to the limits in *PRU*

8.3.45R(1)(e) and (f).

- 8.3.47 R For the purposes of *PRU 8.3.10R*, a *firm* must ensure that the *tier one capital resources* and *tier two capital resources* of each of its *long-term insurance business* and its *general insurance business* are of such an amount that the *group capital resources* of each its *long-term insurance business* and its *general insurance business* comply with the limits in *PRU 8.3.45R* separately for each type of business.

Calculation of GCR – Total group tier one capital

- 8.3.48 R For the purposes of *PRU 8.3.43R*, the *total group tier one capital* of an *undertaking* in *PRU 8.3.17R* is the sum of:
- (1) the *tier one capital resources* of the *undertaking* in *PRU 8.3.17R*; and
  - (2) subject to *PRU 8.3.40R*, the *tier one capital resources* of each of the *related undertakings* of that *undertaking* that is a *regulated related undertaking* after the deduction in *PRU 8.3.49R*.

- 8.3.49 R The deduction referred to in *PRU 8.3.48R* is the sum of:
- (1) the book value of the investment by the *undertaking* in *PRU 8.3.17R* in the *tier one capital resources* of each of its *related undertakings* that is a *regulated related undertaking*; and
  - (2) the book value of the investments by *related undertakings* of the *undertaking* in *PRU 8.3.17R* in the *tier one capital resources* of the *undertaking* in *PRU 8.3.17R* and each of its *related undertakings* that is a *regulated related undertaking*.

Calculation of GCR – Total group tier two capital

- 8.3.50 R For the purposes of *PRU 8.3.43R*, the *total group tier two capital* of an *undertaking* in *PRU 8.3.17R* is the sum of:
- (1) the *upper tier two capital resources* and the *lower tier two capital resources* of that *undertaking*; and
  - (2) subject to *PRU 8.3.40R*, the *upper tier two capital resources* and the *lower tier two capital resources* of each of the *related undertakings* of that *undertaking* that is a *regulated related undertaking* after the deduction in *PRU 8.3.51R*.
- 8.3.51 R The deduction referred to in *PRU 8.3.50R* is the sum of:
- (1) the book value of the investments by the *undertaking* in *PRU 8.3.17R* in the *upper tier two capital resources* and the *lower tier two capital resources* of each of its *related undertakings* that is a *regulated related undertaking*; and

- (2) the book value of the investments by *related undertakings* of the *undertaking* in PRU 8.3.17R in the *upper tier two capital resources* and the *lower tier two capital resources* of the *undertaking* in PRU 8.3.17R and each of its *related undertakings* that is a *regulated related undertaking*.

8.3.52 G For the purposes of PRU 8.3.50R(2), the limits in PRU 2.2.23R apply to the *upper tier two capital resources* and the *lower tier two capital resources* of any *regulated related undertaking* that is an *insurer*. Similar limits may apply to other *regulated related undertakings* under the relevant *sectoral rules*.

Calculation of GCR – Innovative tier one capital resources, lower tier two capital resources and core tier one capital

8.3.53 R For the purposes of PRU 8.3.45R(3)(b), the *innovative tier one capital resources* is the sum of:

- (1) the *innovative tier one capital resources* of the *undertaking* in PRU 8.3.17R; and
- (2) subject to PRU 8.3.40R, the *innovative tier one capital resources* of each of the *related undertakings* of that *undertaking* that is a *regulated related undertaking* after the deduction in PRU 8.3.54R.

8.3.54 R The deduction referred to in PRU 8.3.53R is the sum of:

- (1) the book value of the investments by the *undertaking* in PRU 8.3.17R in the *innovative tier one capital resources* of each of its *related undertakings* that is a *regulated related undertaking*; and
- (2) the book value of the investments by *related undertakings* of the *undertaking* in PRU 8.3.17R in the *innovative tier one capital resources* of the *undertaking* in PRU 8.3.17R and each of its *related undertakings* that is a *regulated related undertaking*.

8.3.55 R For the purposes of PRU 8.3.45R(3)(g), the *core tier one capital* is the sum of:

- (1) the *core tier one capital* of the *undertaking* of PRU 8.3.17R; and
- (2) subject to PRU 8.3.40R, the *core tier one capital* of each of the *related undertakings* of that *undertaking* that is a *regulated related undertaking* after the deduction in PRU 8.3.56R.

8.3.56 R The deduction referred to in PRU 8.3.55R is the sum of:

- (1) the book value of the investments by the *undertaking* in PRU 8.3.17R in the *core tier one capital* of each of its *related undertakings* that is a *regulated related undertaking*; and
- (2) the book value of the investments by *related undertakings* of the

*undertaking in PRU 8.3.17R in the core tier one capital of the undertaking in PRU 8.3.17R and each of its related undertakings that is a regulated related undertaking.*

- 8.3.57 R For the purposes of *PRU 8.3.45R(3)(h)*, the *lower tier two capital resources* is the sum of:
- (1) the *lower tier two capital resources* of the *undertaking in PRU 8.3.17R*; and
  - (2) subject to *PRU 8.3.40R*, the *lower tier two capital resources* of each of the *related undertakings* of that *undertaking* that is a *regulated related undertaking* after the deduction in *PRU 8.3.58R*.
- 8.3.58 R The deduction referred to in *PRU 8.3.57R* is the sum of:
- (1) the book value of the investments by the *undertaking in PRU 8.3.17R* in the *lower tier two capital resources* of each of its *related undertakings* that is a *regulated related undertaking*; and
  - (2) the book value of the investments by *related undertakings* of the *undertaking in PRU 8.3.17R* in the *lower tier two capital resources* of the *undertaking in PRU 8.3.17R* and each of its *related undertakings* that is a *regulated related undertaking*.

#### Calculation of GCR – Inadmissible assets

- 8.3.59 R For the purpose of *PRU 8.3.43R*, a *firm* must deduct from the group capital resources before deduction (calculated at stage C in the table in *PRU 8.3.43R*) of the *undertaking in PRU 8.3.17R*, the value of all assets of the *undertaking in PRU 8.3.17R* and each of its *regulated related undertakings* that are not admissible assets as set out in *PRU 8.3.60R*.
- 8.3.60 R For the purposes of *PRU 8.3.59R*, an asset is not an admissible asset if:
- (1) in respect of a *regulated related undertaking* or *undertaking in PRU 8.3.17R* that is an *insurer*, it is not an *admissible asset* as listed in *PRU 2 Ann 1R*;
  - (2) in respect of a *regulated related undertaking* or *undertaking in PRU 8.3.17R* that is not an *insurer*, it is an asset of the *undertaking* that is not admissible for the purpose of calculating that *undertaking's solo capital resources* in accordance with the *sectoral rules* applicable to it.
- 8.3.61 R For the purposes of *PRU 8.3.60R(2)*, the *sectoral rules* applicable to:
- (1) an *asset management company* are the *sectoral rules* that would apply to it if, in connection with its activities, it were treated as an *investment firm*; and
  - (2) a *financial institution* that is not a *regulated entity* are the *sectoral*

*rules* that would apply to it if, in connection with its activities, it were treated as being within the *banking sector*.

#### Calculation of GCR – Deductions under requirement deduction method from group capital resources

- 8.3.62 R For the purposes of *PRU 8.3.43R*, a *firm* must deduct from the group capital resources before deduction (calculated at stage C in the table in *PRU 8.3.43R*) of an *undertaking* in *PRU 8.3.17R*, the sum of the value of the direct or indirect investments by the *undertaking* in *PRU 8.3.17R* in each of its *related undertakings* which is an *ancillary services undertaking*, calculated in accordance with *PRU 8.3.63R*.
- 8.3.63 R The value of an investment in an *undertaking* referred to in *PRU 8.3.62R* is the higher of the book value of the direct or indirect investment by the *undertaking* in *PRU 8.3.17R* and the notional capital resources requirement of that *undertaking*.
- 8.3.64 R For the purposes of *PRU 8.3.63R*, the notional capital resources requirement is:
- (1) for an *ancillary insurance services undertaking*, zero;
  - (2) for any other *ancillary services undertaking*, the *capital resources requirement* that would apply to that *undertaking*, if it were a *regulated related undertaking*, in accordance with the *sectoral rules* applicable to a *regulated related undertaking* whose activities are closest in nature and scope to the activities of that *undertaking*.

#### Calculation of GCR – Deductions of ineligible surplus capital

- 8.3.65 R Where the *undertaking* in *PRU 8.3.17R* is a *participating insurance undertaking*, the *firm* must, for the purposes of *PRU 8.3.43R*, deduct from its group capital resources before deduction (calculated at stage C in the table in *PRU 8.3.43R*) the sum of the ineligible surplus capital of each of its *regulated related undertakings* that is an *insurance undertaking*, calculated in accordance with *PRU 8.3.67R*.
- 8.3.66 G The purpose of *PRU 8.3.65R* is to ensure that, where the *undertaking* in *PRU 8.3.17R* is a *firm*, *group capital resources* are not overstated by the inclusion of capital that, although surplus to the requirements of the relevant *regulated related undertaking* that is an *insurance undertaking*, cannot practically be transferred to support requirements arising elsewhere in the group. Therefore, ineligible surplus capital in a *regulated related undertaking* that is an *insurance undertaking* is deducted in arriving at *group capital resources*. Surplus capital in such a *regulated related undertaking* is regarded as transferable only to the extent that:
- (1) it can be transferred without the *regulated related undertaking* breaching its own limits on the use of different forms of capital;
  - (2) it does not contain assets that are restricted within the meaning of

*PRU 8.3.41R*; and

- (3) in the case of a *regulated related undertaking* that has a *long-term insurance business*, it does not contain any assets allocated to the *capital resources* of that *undertaking* for the purposes of the *capital resources* of its *long-term insurance business* meeting the *capital resources requirement* of its *long-term insurance business*.

8.3.67 R (1) For the purposes of *PRU 8.3.65R*, the ineligible surplus capital of a *regulated related undertaking* that is an *insurance undertaking* is calculated by deducting B from A where:

- (a) A is the *regulatory surplus value* of that *insurance undertaking* less any restricted assets of the *insurance undertaking* that have been excluded under *PRU 8.3.41R*; and
- (b) B is the transferable capital of that *undertaking*.

- (2) If A minus B is negative, the ineligible surplus capital is zero.

8.3.68 R For the purposes of *PRU 8.3.67R(1)(b)*, the transferable capital is calculated by deducting the sum of the following from the *tier one capital resources* of the *regulated related undertaking* that is an *insurance undertaking*:

- (1) any restricted assets of that *insurance undertaking* that have been excluded under *PRU 8.3.41R*;
- (2) any *tier one capital resources* of that *insurance undertaking* that have been allocated towards meeting the *individual capital resources requirement* of its *long-term insurance business*; and
- (3) the higher of:
- (a) 50% of the *individual capital resources requirement* of the *general insurance business* of that *insurance undertaking*; and
- (b) the *individual capital resources requirement* of the *general insurance business* of that *insurance undertaking* less the difference between E and F where:
- (i) E is its *tier two capital resources*; and
- (ii) F is the amount of its *tier two capital resources* that have been allocated towards meeting the *individual capital resources requirement* of its *long-term insurance business*.

8.3.69 G Examples of transferable and ineligible surplus capital:

Example 1

Share capital	Audited reserves	FFA	Tier two	Requirement
30	20	0	40	50

- (i) Under *PRU* 8.3.68R, transferable capital = *tier one capital resources* of 50, less the sum of:
- (1) restricted assets excluded under *PRU* 8.3.41R = (none);
  - (2) *tier one capital resources* allocated to the *long-term insurance business* = (none); and
  - (3) higher of (50% of 50 = 25 and 50 – 40 = 10) = (25)  
= (50 – 25) = 25
- (ii) Under *PRU* 8.3.67R, ineligible surplus capital = *regulatory surplus value* (40) less restricted assets excluded under *PRU* 8.3.41R (0) less transferable capital (25) = 15.

Example 2

Share capital	Audited reserves	FFA (of which 5 is restricted)	Tier two	Requirement (of which 5 relates to the <i>long-term insurance business</i> )
30	20	10	40	50

- (i) Under *PRU* 8.3.68R, transferable capital = *tier one capital resources* of 60, less the sum of:
- (1) restricted assets excluded under *PRU* 8.3.41R = (5);
  - (2) *tier one capital resources* allocated to the *long-term insurance business* = (5); and
  - (3) the higher of (50% of 45 = 22.5; and 45 – 40 = 5) = (22.5)  
= 60 – 32.5 = 27.5



- (ii) Under *PRU 8.3.67R*, ineligible surplus capital = *regulatory surplus value* (50) – restricted assets excluded under *PRU 8.3.41R* of (5) – transferable capital (27.5) = 17.5.

Example 3

Share capital	Audited reserves	FFA (of which 0 is restricted)	Tier two (40, of which 5 is excluded at the solo level – see below)	Requirement (of which 25 relates to the <i>long-term insurance business</i> )
20	10	20	35	50

The requirement relating to the *long-term insurance business* is met by the FFA of 20 and *tier two capital resources* of 5. Of the remaining *tier two capital resources* of 35, 5 is excluded at the solo level because the *tier one capital resources* allocated to the *general insurance business* are 30.

- (i) Under *PRU 8.3.68R*, transferable capital = *tier one capital resources* of 50, less the sum of:
- (1) restricted assets excluded under *PRU 8.3.41R* = (none);
  - (2) *tier one capital resources* allocated to the *long-term insurance business* = (20); and
  - (3) the higher of (50% of 25 = 12.5; and 25 – (35 - 5) = -5) = (12.5)
- = 50 – 32.5 = 17.5.
- (ii) Under *PRU 8.3.67R*, ineligible surplus capital = *regulatory surplus value* (35) – restricted assets excluded under *PRU 8.3.41R* of (0) – transferable capital (17.5) = 17.5.

Calculation of GCR – Assets in excess of market risk and counterparty exposure limits

- 8.3.70 R Where the *undertaking* in *PRU 8.3.17R* is a *participating insurance undertaking*, the *firm* must deduct from its group capital resources before deduction (calculated at stage C in the table in *PRU 8.3.43R*) the assets in excess of *market risk* and *counterparty* exposure limits calculated in accordance with *PRU 8.3.74R*.
- 8.3.71 G For the purposes of *PRU 8.3.43R*, where the *undertaking* in *PRU 8.3.17R* is a *participating insurance undertaking*, the investments referred to in *PRU*

8.3.48R and *PRU* 8.3.50R are not subject to the *market risk* and *counterparty* exposure limits.

- 8.3.72 R The *firm* (A) must, subject to *PRU* 8.3.73R, include in the calculation in *PRU* 8.3.74R each *related undertaking* (B) that is:
- (1) a *regulated related undertaking* that is a *subsidiary undertaking*; or
  - (2) a *related undertaking* where the *firm* has elected to value the *shares* held in that *undertaking* by the *firm* in accordance with *PRU* 1.3.35R for the purposes of calculating the *tier one capital resources* of the *firm*.
- 8.3.73 R The *related undertakings* in *PRU* 8.3.72R need only be included in the calculation in *PRU* 8.3.74R if:
- (1) where B is a *regulated related undertaking*, the *solo capital resources* of that *undertaking* exceed its *individual capital resources requirement*; or
  - (2) where B is an *undertaking* in *PRU* 8.3.72R(2), its assets that fall within one or more of the categories in *PRU* 2 Ann 1R exceed its accounting liabilities.
- 8.3.74 R A's assets in excess of the *market risk* and *counterparty* exposure limits are calculated as follows:
- (1) Subject to (2), a *firm* must apply the *market risk* and *counterparty* exposure limits in *PRU* 3.2.22R(3) to:
    - (a) where B is an *insurer*, the *admissible assets* of B;
    - (b) where B is a *regulated related undertaking* that is not an *insurer*, the assets of that *undertaking* less those assets identified in *PRU* 8.3.60R(2) as not being *admissible assets*.
  - (2) The *market risk* and *counterparty* exposure limits do not need to be applied to an *undertaking* in *PRU* 8.3.72R(2).
  - (3) Where the assets of B in *PRU* 8.3.74R(1) exceed the limits in *PRU* 3.2.22R(3), the assets of B in excess of the limits must be deducted by the *firm* from B's *solo capital resources* for the purposes of *PRU* 8.3.30R.
  - (4) After the application of (1) and (2), the surplus assets of B are aggregated with the *admissible assets* of A, where the surplus assets of B are:
    - (a) where B is a *firm*, the *admissible assets* of B that represent the amount by which the *capital resources* of B exceed its *capital resources requirement*, subject to *PRU* 8.3.77R, and limited to the amount of transferable capital calculated in

accordance with *PRU 8.3.68R*;

- (b) where B is a *regulated related undertaking* that is not a *firm*, the assets of the *undertaking* in *PRU 8.3.74R(1)(b)* that represent the amount by which the *solo capital resources* of B exceed its *individual capital resources requirement* and, where B is an *insurance undertaking* that is not a *firm*, limited to the amount of transferable capital calculated in accordance with *PRU 8.3.68R*; and
- (c) where B is an *undertaking* in *PRU 8.3.72R(2)*, the assets of the *undertaking* which represent those assets that fall within one or more of the categories in *PRU 2 Ann 1R* which exceed its accounting liabilities.

(5) The *market risk* and *counterparty* exposure limits are then applied to the aggregate of A's *admissible assets* and the surplus assets in *PRU 8.3.74R(4)*.

- 8.3.75 R The *firm* (A) must then deduct the amount by which the *admissible assets* aggregated in accordance with *PRU 8.3.74R(5)* exceed the *market risk* and *counterparty* exposure limits from A's group capital resources before deduction (calculated at stage C in the table in *PRU 8.3.43R*) in accordance with *PRU 8.3.70R*.
- 8.3.76 R In relation to any of its *regulated related undertakings* that is not an *insurer*, A may modify the calculation in *PRU 8.3.74R* by:
- (1) omitting the calculation in *PRU 8.3.74R(1)* and (3); and
  - (2) aggregating all of the assets of B identified in *PRU 8.3.74R(1)(b)* as *admissible assets* with the *admissible assets* of A in *PRU 8.3.74R(4)*.
- 8.3.77 R The *admissible assets* of either A or B that are part of a *long-term insurance fund* of A or B are excluded for the purposes of the calculation in *PRU 8.3.74R* except insofar as those assets are available to meet the liabilities and *capital resources requirement* of that *long-term insurance fund*.
- 8.3.78 R If B is itself either a *participating insurance undertaking* or an *insurance parent undertaking*, the *admissible assets* of B for the purposes of *PRU 8.3.74R(1)* must be calculated as in *PRU 8.3.75R* but as if B were A.

## Annex K

### Other amendments to the Integrated Prudential sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where existing text will be replaced by new text, this is indicated and the new text is not underlined. Where new text is being inserted at the end of existing text, this is indicated and the additional text is not underlined. Where an entire section of text is being deleted, the place where the change will be made is indicated and the text is not struck through or reproduced.

Transitional provisions

...

Transitional provisions 3 and 4 are deleted.

3 [deleted]

4 [deleted]

Insert new transitional provisions as follows:

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
5	<i>Rules</i> in <i>PRU</i> listed in the Table at <i>PRU</i> TR Table 10R	R	<p>(1) A <i>rule</i> listed in column (2) is disappplied, or is modified in its application, to a <i>firm</i>:</p> <p>(a) in order to produce the same effect, including any conditions, as a <i>waiver</i> had on the corresponding <i>rule</i> in <i>IPRU(INS)</i>;</p> <p>(b) for the same period as the <i>waiver</i> would have lasted, if shorter than the period in column (5);</p> <p>provided the conditions set out in (2) are satisfied.</p> <p>(2) The conditions referred to in (1) are:</p>	From 31 December 2004 until the relevant <i>rule</i> is revoked	31 December 2004

			<p>(a) the <i>rule</i> is shown in the Table at <i>PRU</i> TR Table 10R as corresponding with the <i>rule</i> in <i>IPRU(INS)</i> in relation to which the <i>waiver</i> was granted to the <i>firm</i>;</p> <p>(b) the <i>waiver</i> was current as respects the <i>firm</i> immediately before the date specified in column (6); and</p> <p>(c) there is no specific transitional <i>rule</i> relating to the <i>waiver</i>.</p> <p>(3) (1) does not have effect if, and to the extent that, it would be inconsistent with any community obligation of the <i>United Kingdom</i>.</p>		
6	Rules in <i>PRU</i> not listed in the Table at <i>PRU</i> TR Table 10R	R	<p>(1) A <i>rule</i> listed in column (2) is disapplied, or is modified in its application, to a <i>firm</i>:</p> <p>(a) in order to produce the same effect, including any conditions, as a <i>waiver</i> had on a <i>rule</i> in <i>IPRU(INS)</i> or <i>IPRU(FSOC)</i>, or a written concession had on a pre-commencement provision listed in <i>PRU</i> TR 7 R;</p> <p>(b) for the same period as the <i>waiver</i> or written concession would have lasted, if shorter than the period in column (5); provided the conditions set out in (2) are satisfied.</p> <p>(2) The conditions referred to in (1) are:</p> <p>(a) the <i>rule</i> in <i>PRU</i> is substantially similar to the <i>rule</i> in <i>IPRU(INS)</i>, <i>IPRU(FSOC)</i>, or the pre-commencement provision, as the case may be,</p>	From 31 December 2004 until 30 June 2005	31 December 2004

			<p>with which the <i>waiver</i> or written concession was concerned;</p> <p>(b) the <i>waiver</i> or written concession was current as respects the <i>firm</i> immediately before the date specified in column (6);</p> <p>(c) there is no specific transitional <i>rule</i> relating to the <i>waiver</i> or written concession; and</p> <p>(d) in the case of a written concession, it has not been superseded by a <i>waiver</i> from the <i>FSA</i>.</p> <p>(3) (1) does not have effect if, and to the extent that, it would be inconsistent with any community obligation of the <i>United Kingdom</i>.</p>		
7	As <i>PRU TR 6R</i>	R	<p>The pre-commencement provisions referred to in these transitional provisions are those contained in:</p> <p>(1) the Insurance Companies Act 1982 and relevant secondary legislation;</p> <p>(2) the Friendly Societies Act 1992 and relevant secondary legislation.</p>	As <i>PRU TR 6R</i>	As <i>PRU TR 6R</i>
8	As <i>PRU TR 5R</i> to <i>PRU TR 7R</i>	R	<p>A <i>firm</i> which has the benefit of a <i>waiver</i> to which <i>PRU TR 5R</i> applies, or a <i>waiver</i> or written concession to which <i>PRU TR 6R</i> applies, must:</p> <p>(1) notify the <i>FSA</i> immediately if it becomes aware of any matter which is material to the relevance or appropriateness of the <i>waiver</i> or written</p>	As <i>PRU TR 5R</i> or <i>PRU TR 6R</i>	As <i>PRU TR 6R</i>

			<p>concession;</p> <p>(2) maintain a written record of the <i>rule</i> in <i>PRU</i> to which it considers the <i>waiver</i> or written concession applies; and</p> <p>(3) make the record available to the <i>FSA</i> on request.</p>		
9	<i>PRU</i> TR 5R to <i>PRU</i> TR 25R	R	<p>In these transitional provisions:</p> <p>(1) "substantially similar" means substantially similar in purpose and effect;</p> <p>(2) "written concession" means a waiver, exemption, concession, modification, consent, approval, determination or similar exercise of discretion which:</p> <p>(a) disappplied, or tended to reduce the burden of complying with, a <i>pre-commencement</i> provision (with or without conditions); and</p> <p>(b) was evidenced in writing.</p>	As <i>PRU</i> TR 5R or <i>PRU</i> TR 6R	31 December 2004

**PRU TR Table 10 R**

This Table belongs to *PRU* TR 5R to *PRU* TR 9R

<b>Rules in PRU</b>	<b>Corresponding rules in IPRU(INS)</b>
1.3.35R	4.2 (3)
2.1.9R	2.9 (3)
2.1.21R	2.9
2.1.22R	2.9
2.1.30R	2.4 (6)
2.2.80R	2.10 (7)
2.2.81R	2.10 (7)
2.2.86R	4.14

	4.5 (7)
3.2.22R	4.14 (1)
4.2.34R	5.11
4.2.39R	5.11
	5.11 (4)
	5.11 (5)
	5.11 (9)
	5.11 (11)
4.2.58R	2.3 (2)
7.2.51R	2.4 (6)
7.2.56R	2.4 (1)
7.2.66R	Appendix 2.1 2.4(1)(b)
	Appendix 2.2 2.4(1)(b)
	5.9 (1)
7.3.40R	5.9 (2)
7.3.41R	5.9 (2)
7.3.43R	5.10
7.3.74R	5.16
8.3.17R(1)(a)-(b)	10.1
	10.2
	10.2 (1)
	10.2 (2)
	10.2 (3)
8.3.23R	10.2
	10.2 (1)
	10.2 (2)
	10.2 (3)



(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
11	PRU 1.2 PRU 5.1	R	If a <i>firm</i> , as at 31 December 2004, has the benefit of a <i>waiver</i> of: (1) SUP 16.7.10R; or (2) SUP 16.7.12R; under which the <i>firm</i> does not have to supply adequate information on mismatch liquidity, the provisions referred to in column (2) do not apply.	From 31 December 2004 until the date the <i>waiver</i> referred to in column (4) ceases to have effect.	31 December 2004
12	PRU 1.3.5R PRU 7.4.191R	R	(1) This <i>rule</i> applies to a <i>firm</i> which for the period specified in column (5) is required by PRU 1.3.5R to measure the surplus or deficit in a <i>defined benefits pension scheme</i> , for the purposes of PRU, in accordance with FRS 17 (Retirement Benefits).  (2) A <i>firm</i> must derecognise any measure of actuarial gains in respect of a <i>defined benefits pension scheme</i> .  (3) A <i>firm</i> may deduct from its liabilities the difference between the measure of actuarial losses in respect of a <i>defined benefits pension scheme</i> which would result from the application of PRU 1.3.5R and the <i>firm's</i> best estimate of the level of additional funding that it will provide for that <i>defined benefits pension scheme</i> over the next five years, as determined in conjunction with the scheme's <i>actuaries</i> or trustees (or both) as appropriate.	From 31 December 2004 to 30 December 2005	31 December 2004
13	PRU 1.3.14R	R	A <i>firm</i> will be treated as complying with the <i>rule</i> listed in column (2) if it marks to	From 31 December 2004 to 30 December	31 December 2004

			market by reference to market value as determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate to <i>insurers</i> .	2006	
14	PRU 1.3.31R PRU 2.2.90R	R	<p>(1) A <i>firm</i> may elect to apply PRU 1.3.11R to <i>shares</i> in a <i>regulated related undertaking</i> that is not an <i>insurance undertaking</i> or an <i>insurance holding company</i>.</p> <p>(2) A <i>firm</i> may apply PRU 1.3.11R if it has made the election referred to in subparagraph (1) by written notice to the <i>FSA</i> in a way which complies with the requirements for written notice in SUP 15.7.</p> <p>(3) Where a <i>firm</i> has made the election referred to in (1):</p> <p>(a) PRU 2.2.90R is disapplied in respect of the <i>shares</i> in that <i>regulated related undertaking</i>; and</p> <p>(b) the <i>shares</i> in that <i>regulated related undertaking</i> must be valued in accordance with (4).</p> <p>(4) Subject to (5), the <i>shares</i> in the <i>regulated related undertaking</i> within (3) must be valued in accordance with PRU 1.3.11R.</p> <p>(5) For the purposes of valuing the <i>shares</i> in a <i>regulated related undertaking</i> within (4), the value of those <i>shares</i> determined in accordance with PRU 1.3.11R must be reduced:</p> <p>(a) by an approximate amount, to the extent that the value of those <i>shares</i> in the <i>regulated</i></p>	From 31 December 2004 until the first day of the <i>firm's financial year</i> beginning in 2005	31 December 2004

			<p><i>related undertaking</i> cannot effectively be realised to meet the <i>capital resources requirement</i> of the <i>firm</i>; and</p> <p>(b) by an approximate amount, to exclude value attributable to goodwill generated from the business of the <i>regulated related undertaking</i> with other members of the <i>insurance group</i>.</p>		
15	As PRU TR 14R	G	<p>(1) The application of PRU 1.3.31R to a <i>regulated related undertaking</i> which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> implements the amendments to the <i>First Non-Life Directive</i>, the <i>First Life Directive</i> and the <i>Insurance Groups Directive</i> in Articles 22(2), 23(2) and 28(6) of the <i>Financial Groups Directive</i>.</p> <p>(2) PRU TR 14R allows the requirement to treat a <i>regulated related undertaking</i> which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> in accordance with PRU 1.3.31R to be postponed until the effective date of the <i>Financial Groups Directive</i>.</p> <p>(3) In the interim, a <i>firm</i> may elect either to apply PRU 1.3.11R or to value <i>shares</i> in a <i>regulated related undertaking</i> which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> in accordance with PRU 1.3.31R. The intention is to allow <i>firms</i> to continue to account for the value of <i>shares</i> held in these <i>regulated related undertakings</i> as they would formerly have done under <i>IPRU(INS)</i> for the purposes of calculating the</p>	As PRU TR 14R	As PRU TR 14R

			<i>capital resources of a firm.</i>		
16	<p>PRU 2.2.93R (3) PRU 2.2.101R (3) PRU 2.2.101R (4) PRU 2.2.102R PRU 2.2.103R PRU 2.2.105R</p>	R	<p>(1) This paragraph applies to a <i>firm</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS)</i> rule 2.10 or 5.2, or a written concession in relation to a pre-<i>commencement</i> provision listed in <i>PRU TR 7R</i>, in either case allowing the <i>firm</i> to exclude from the calculation of its liabilities obligations under a particular capital instrument issued by the <i>firm</i>.</p> <p>(2) Subject to (3) and to compliance with the conditions set out in (4), a <i>firm</i> will be treated as complying with a <i>rule</i> listed in column (2) in relation to the capital instrument to which the <i>waiver</i> or written concession referred to in (1) related so long as the <i>firm</i> is not obliged to pay any interest under the terms of the capital instrument in circumstances where the <i>firm</i> does not have <i>capital resources</i> equal to or in excess of its required margin of solvency under the <i>Insurance Directives</i>.</p> <p>(3) (2) ceases to apply to a <i>firm</i>:</p> <p>(a) once the <i>firm</i> has redeemed the capital instrument; or</p> <p>(b) on or after any date upon which the <i>firm</i> has the option to redeem the capital instrument and may prudently do so.</p> <p>(4) The conditions referred to in (2) are:</p> <p>(a) the <i>firm</i> must notify the <i>FSA</i> immediately if it becomes aware of any matter which is material</p>	<p>From 31 December 2004 until the relevant <i>rule</i> is revoked</p>	<p>31 December 2004</p>

			<p>to the relevance or appropriateness of the <i>waiver</i> or written concession;</p> <p>(b) the <i>firm</i> must maintain a written record of the <i>rule</i> in <i>PRU</i> to which it considers the <i>waiver</i> or written concession applies; and</p> <p>(c) the <i>firm</i> must make the record available to the <i>FSA</i> on request.</p>		
17	<i>PRU</i> 2.2.93R (2)	R	<p>(1) This paragraph applies to a <i>firm</i> carrying on <i>with-profits insurance business</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS)</i> rule 2.10 or 5.2 or a written concession in relation to a <i>pre-commencement</i> provision listed in <i>PRU</i> TR 7R in either case allowing the <i>firm</i> to exclude from the calculation of its liabilities obligations under a particular capital instrument issued by the <i>firm</i>.</p> <p>(2) Subject to compliance with the conditions set out in (3), <i>PRU</i> 2.2.93R (2) does not apply in relation to the capital instrument to which the <i>waiver</i> or written concession referred to in (1) related provided that capital instrument was issued by the <i>firm</i> on or before 30 December 2004.</p> <p>(3) The conditions referred to in (2) are:</p> <p>(a) the <i>firm</i> must notify the <i>FSA</i> immediately if it becomes aware of any matter which is material to the relevance or appropriateness of the <i>waiver</i> or written concession;</p>	From 31 December 2004 until 30 December 2005	31 December 2004

			<p>(b) the <i>firm</i> must maintain a written record of the <i>rule</i> in <i>PRU</i> to which it considers the <i>waiver</i> or written concession applies; and</p> <p>(c) the <i>firm</i> must make the record available to the <i>FSA</i> on request.</p>		
18	<p><i>PRU</i> 2.2.108R (5)</p> <p><i>PRU</i> 2.2.108R (7)</p>	R	<p>(1) This <i>rule</i> applies to a <i>firm</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS)</i> rule 2.10 or 5.2, or a written concession in relation to a pre-<i>commencement</i> provision listed in <i>PRU</i> TR 7R, in either case allowing the <i>firm</i> to exclude from the calculation of its liabilities obligations under a particular capital instrument issued by the <i>firm</i>.</p> <p>(2) Subject to compliance with the conditions set out in (3), a <i>firm</i> will be treated as complying with a <i>rule</i> listed in column (2) in relation to the capital instrument to which the <i>waiver</i> or written concession referred to in (1) related.</p> <p>(3) The conditions referred to in (2) are:</p> <p>(a) the <i>firm</i> must notify the <i>FSA</i> immediately if it becomes aware of any matter which is material to the relevance or appropriateness of the <i>waiver</i> or written concession;</p> <p>(b) the <i>firm</i> must maintain a written record of the <i>rule</i> in <i>PRU</i> to which it considers the <i>waiver</i> or written concession applies; and</p> <p>(c) the <i>firm</i> must make the</p>	From 31 December 2004 until 30 June 2005	31 December 2004

			record available to the <i>FSA</i> on request.		
19	<p><i>PRU 2.2.108R</i> (6)</p> <p><i>PRU 2.2.108R</i> (10)</p> <p><i>PRU 2.2.108R</i> (11)</p> <p><i>PRU 2.2.111R</i></p>	R	<p>(1) This paragraph applies to a <i>firm</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS)</i> rule 2.10 or 5.2, or a written concession in relation to a pre-<i>commencement</i> provision listed in <i>PRU TR 7R</i>, in either case allowing the <i>firm</i> to exclude from the calculation of its liabilities obligations under a particular capital instrument issued by the <i>firm</i>.</p> <p>(2) Subject to compliance with the conditions set out in (3), a <i>firm</i> will be treated as complying with a <i>rule</i> listed in column (2) in relation to the capital instrument to which the <i>waiver</i> or written concession referred to in (1) related.</p> <p>(3) The conditions referred to in (2) are:</p> <p>(a) the <i>firm</i> must notify the <i>FSA</i> immediately if it becomes aware of any matter which is material to the relevance or appropriateness of the <i>waiver</i> or written concession;</p> <p>(b) the <i>firm</i> must maintain a written record of the <i>rule</i> in <i>PRU</i> to which it considers the <i>waiver</i> or written concession applies; and</p> <p>(c) the <i>firm</i> must make the record available to the <i>FSA</i> on request.</p>	From 31 December 2004 until the relevant <i>rule</i> is revoked	31 December 2004
20	<p><i>PRU 2.2.12R</i></p> <p><i>PRU 2.2.14R</i> (Table)</p>	R	<p>(1) This <i>rule</i> applies to a <i>firm</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS)</i> rule 2.10</p>	From 31 December 2004 until the relevant <i>rule</i> is revoked	31 December 2004

			<p>(4).</p> <p>(2) For the period specified in column (5) or the same period as the <i>waiver</i> would have lasted if shorter, subject to (3) and to compliance with the conditions set out in (4), for the purposes of calculating its <i>capital resources</i> a <i>firm</i> may include the value of claims against its members by way of calls for supplementary contributions as <i>core tier one capital</i> to the same extent as it was permitted by the <i>waiver</i> to include the value of those claims in the calculation of its margin of solvency.</p> <p>(3) (2) does not apply for the purposes of <i>PRU 2.2.18R</i> or <i>SUP Appendix 2.4</i>.</p> <p>(4) The conditions referred to in (2) are:</p> <p>(a) the limits specified in the <i>waiver</i> on the extent to which the <i>firm's</i> claim against its members by way of call for supplementary contributions may be brought into account apply as if the reference (if any) in the <i>waiver</i> to the <i>firm's</i> required margin of solvency referred to its <i>general insurance capital requirement</i> and the reference (if any) in the <i>waiver</i> to the <i>firm's</i> margin of solvency referred to its <i>capital resources</i>; and</p> <p>(b) the <i>firm</i> must comply with any further conditions imposed by the <i>waiver</i>.</p>		
21	<i>PRU 2.2.12R</i> <i>PRU 2.2.14R</i> (Table)	R	(1) This <i>rule</i> applies to a <i>firm</i> which immediately before the date specified in column (6) had the benefit of a <i>waiver</i> in relation to <i>IPRU(INS) rule 2.10</i>	From 31 December 2004 until the relevant <i>rule</i> is revoked	31 December 2004



			<p>(5) or <i>IPRU(FSOC)</i> rule 4.7 (3).</p> <p>(2) For the period specified in column (5) or the same period as the <i>waiver</i> would have lasted if shorter, subject to (3) and to compliance with the conditions set out in (4), for the purpose of calculating its <i>capital resources</i> a <i>firm</i> may include the value of <i>implicit items</i> at Stage B of the calculation in <i>PRU 2.2.14R</i> Table to the same extent to which it was permitted by the <i>waiver</i> to include the value of those <i>implicit items</i> in the calculation of its margin of solvency.</p> <p>(3) (2) does not apply for the purposes of <i>PRU 2.2.17R</i>.</p> <p>(4) The conditions referred to in (2) are:</p> <p>(a) the limits specified in the <i>waiver</i> on the extent to which the value of <i>implicit items</i> may be brought into account apply as if the reference (if any) in the <i>waiver</i> to the <i>firm's</i> required margin of solvency referred to its <i>minimum capital requirement</i> and the reference (if any) in the <i>waiver</i> to the <i>firm's</i> margin of solvency referred to its <i>capital resources</i>; and</p> <p>(b) the <i>firm</i> must comply with any further conditions imposed by the <i>waiver</i>.</p>		
22	<p><i>PRU 2.1.21R</i>  <i>PRU 2.1.30R</i>  <i>PRU 2.2.18R</i>  <i>PRU 3.2.22R</i>  <i>PRU 7.2.51R</i>  <i>PRU 7.2.85R</i></p>	R	<p>In relation to any <i>financial year</i> starting on or before 30 December 2004, a <i>firm's</i> <i>general insurance capital requirement</i> or a <i>firm's</i> <i>insurance health risk capital component</i> is its margin of solvency calculated in</p>	<p>From 31 December 2004 until the relevant <i>rule</i> is revoked</p>	<p>31 December 2004</p>

			<p>accordance with:</p> <p>(1) <i>IPRU(INS)</i> rule 2.4 (excluding 2.4(1)(a)) and Appendices 2.1 and 2.2, or <i>IPRU(INS)</i> rule 2.4 (excluding 2.4(1)(a)) and Appendices 2.1 and 2.2 (as applied by rule 2.7 to <i>long-term insurance business</i> of <i>class IV</i>); or</p> <p>(2) <i>IPRU(FSOC)</i> rule 4.2 (excluding 4.2(1)(a)) and Appendix 2 Parts I and II, or <i>IPRU(FSOC)</i> rules 4.2 (excluding 4.2(1)(a)) and Appendix 2 Parts I and II, (as applied by paragraph 3 of Appendix I to <i>long-term insurance business</i> of <i>class IV</i>);</p> <p>as the case may be, as those <i>rules</i> had effect immediately prior to the date in column (6).</p>		
23	<p><i>PRU</i> 4.3.5R (3) (b) <i>PRU</i> 4.3.34R <i>PRU</i> 4.3.35R</p>	R	<p>(1) <i>PRU</i> 4.3.5R(3)(b) has effect as if the words "and is capable of valuation" and "to 4.3.35R" were omitted.</p> <p>(2) <i>PRU</i> 4.3.34R has effect as if it read "For the purpose of <i>PRU</i> 4.3.5R(3)(b), a transaction is on approved terms only if the <i>firm</i> reasonably believes that it may be readily closed out".</p> <p>(3) <i>PRU</i> 4.3.35R does not apply.</p>	<p>From 31 December 2004 until 30 December 2005</p>	<p>31 December 2004</p>
24	<p><i>PRU</i> 7.5.20R <i>PRU</i> 7.5.45R</p>	R	<p>In relation to any <i>financial year</i> starting on or before 30 December 2004:</p> <p>(1) a <i>firm's non-credit equalisation provision</i> is its equalisation reserve in respect of Part II business carried on by the <i>firm</i> calculated in accordance with <i>IPRU(INS)</i> rules 6.4 to 6.10 and Appendix 6.1 as those rules had effect</p>	<p>From 31 December 2004 until the relevant <i>rule</i> is revoked.</p>	<p>31 December 2004</p>

			<p>immediately prior to the date in column (6); and</p> <p>(2) a <i>firm's credit equalisation provision</i> is its equalisation reserve in respect of credit insurance business carried on by the <i>firm</i> calculated in accordance with <i>IPRU(INS)</i> rules 6.11 to 6.12 and Appendix 6.2 as those rules had effect immediately prior to the date in column (6).</p>		
25	<p><i>PRU 8.3.8R</i>  <i>PRU 8.3.9R</i>  <i>PRU 8.3.10R</i>  <i>PRU 8.3.15R</i></p>	R	<p>(1) For the purpose of the calculation of the <i>group capital resources</i> and <i>group capital resources requirement</i> of an <i>undertaking</i> referred to in <i>PRU 8.3.17R</i>, a <i>firm</i> may elect not to take a <i>regulated related undertaking</i>, which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i>, into account in accordance with <i>PRU 8.3.33R</i> and <i>PRU 8.3.36R</i>.</p> <p>(2) A <i>firm</i> may elect not to take a <i>regulated related undertaking</i>, which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> into account as referred to in (1), if it has made the election by written notice to the <i>FSA</i> in a way that complies with the requirements for written notice in <i>SUP 15.7</i></p> <p>(3) A <i>firm</i> that has made an election referred to in (2) must value that <i>regulated related undertaking</i> in accordance with (4) for the purpose of the calculation of the <i>group capital resources</i> and <i>group capital resources requirement</i> of an <i>undertaking</i> referred to in <i>PRU 8.3.17R</i>.</p> <p>(4) Subject to (5), a <i>regulated related undertaking</i> within (3)</p>	<p>From 31 December 2004 until the first day of the <i>firm's</i> financial year beginning in 2005</p>	<p>31 December 2004</p>

			<p>must, for the purposes of the calculations referred to in (1), be valued in accordance with <i>PRU 1.3.11R</i>.</p> <p>(5) For the purposes of valuing a <i>regulated related undertaking</i> within (3), the value of that <i>regulated related undertaking</i> determined in accordance with <i>PRU 1.3.11R</i>, must be reduced:</p> <p>(a) by an approximate amount, to the extent that the value of the <i>regulated related undertaking</i> cannot effectively be realised to meet the group <i>capital resources requirement</i> of an <i>undertaking</i> in <i>PRU 8.3.17R</i>; and</p> <p>(b) by an approximate amount, to the extent needed to exclude value attributable to goodwill generated from the business of the <i>regulated related undertaking</i> with other members of the <i>insurance group</i>.</p>		
26	As <i>PRU TR 25R</i>	G	<p>(1) The inclusion of a <i>regulated related undertaking</i> which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> in the scope of application of <i>PRU 8.3.33R</i> and <i>PRU 8.3.36R</i> implements the amendments to the <i>First Non-Life Directive</i>, the <i>First Life Directive</i> and the <i>Insurance Groups Directive</i> in Articles 22(2), 23(2) and 28(6) of the <i>Financial Groups Directive</i>.</p> <p>(2) <i>PRU TR 25R</i> allows the requirement to include a <i>regulated related undertaking</i> which is not an <i>insurance undertaking</i> or an <i>insurance holding company</i> in the calculations required by <i>PRU</i></p>	As <i>PRU TR 25R</i>	As <i>PRU TR 25R</i>

		<p>8.3 to be postponed until the effective date of the <i>Financial Groups Directive</i>.</p> <p>(3) In the interim, a <i>firm</i> may apply <i>PRU</i> 8.3, or elect to use the general valuation rules for <i>related undertakings</i> which do not fall within the scope of <i>PRU</i> 8.3, as set out in <i>PRU</i> 1.3.11R, subject to the adjustments required by <i>PRU</i> TR 25R(5). The intention is to allow <i>firms</i> to continue to take the <i>regulated related undertakings</i> referred to in <i>PRU</i> TR 25R(1) and any other <i>related undertaking</i> not referred to in <i>PRU</i> 8.3 into account as they would formerly have done for the purposes of calculating the <i>group capital resources</i> of an <i>undertaking</i> in <i>PRU</i> 8.3.17R.</p>		
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...

PRU 8 Ann 1R

5 Table: Paragraph 4.2: Application of sectoral consolidation rules

....	
<i>Insurance Conglomerate</i>	<del>Whichever of <i>IPRU(INS)</i> or <i>IPRU(FSOC)</i> would apply if those rules were <u><i>PRU</i> 8.3</u> amended in accordance with Part 5.</del>
....	

...

8 Table

A mixed financial holding company	4.6	<p>...</p> <p>(1) ...</p> <p>(2) an <i>insurance holding company</i> (if the rules in <del><i>IPRU(INS)</i></del> <u><i>PRU</i> 8.3</u> are applied).</p>
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...

10 Table: PART 6: Definitions used in this Annex

	6.6	<p>...</p> <p>(1) ...</p> <p>(2) ...</p> <p>(3) (for the <i>insurance sector</i>) the <i>sectoral rules</i> of the <del>states or territories in the definition of designated states or territories in chapter 11 of IPRU(INS) (Definitions)</del>, <u>designated States or territories</u> <del>but</del> excluding <i>EEA States</i>.</p>
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...

**The Integrated Prudential Sourcebook**  
**Schedule 1**  
**Record keeping requirements**

The existing text in Schedule 1 is deleted in its entirety and replaced by the following:

G

- 1 The aim of the *guidance* in the following table is to give the reader a quick overall view of the relevant record keeping requirements.
- 2 It is not a complete statement of those requirements and should not be relied on as if it were.
- 3 Table

Handbook reference	Subject of Record	Contents of record	When record must be made	Retention period
<i>PRU 1.2.37R</i> <i>PRU 1.2.38R</i>	<i>Firm's</i> assessment of the adequacy of its financial resources	(1) The major sources of risk identified in accordance with <i>PRU 1.2.31R</i> (2) How the <i>firm</i> intends to deal with those risks (3) Details of the stress tests and scenario analyses carried out and the resulting financial resources estimated to be required in accordance with <i>PRU 1.2.35R</i>	Not specified	At least 3 years
<i>PRU 1.4.53R</i>	Prudential risk management and systems and controls	Accounting and other records that are sufficient to enable the <i>firm</i> to demonstrate to the <i>FSA</i> : (1) that the <i>firm</i> is financially sound and has appropriate systems and	Not specified	3 years, or longer as appropriate

		controls; (2) the <i>firm's</i> financial position and exposure to risk (to a reasonable degree of accuracy); (3) the <i>firm's</i> compliance with the <i>rules</i> in <i>PRU</i>		
<i>PRU 7.3.20R</i>	<i>Mathematical reserves</i>	(1) The methods and assumptions used in establishing the <i>firm's mathematical reserves</i> , including the margins for adverse deviation, and the reasons for their use (2) The nature of, reasons for, and effect of, any change in approach, including the amount by which the change in approach increases or decreases its <i>mathematical reserves</i>	Not specified	An appropriate period
<i>PRU 7.4.17R</i> <i>PRU 7.4.19R</i>	Calculation of <i>with-profits insurance capital component</i>	(1) The methods and assumptions used in making any calculation required for the purposes of <i>PRU 7.4</i> (and any subsequent changes) and the reasons for their use (2) Any change	Not specified	An appropriate period



		in practice (in particular changes in those items which will or may be significant in relation to the eventual <i>claim</i> values) and the nature of, reasons for, and effect of, any change in approach with respect to those methods and assumptions		
<i>PRU 7.6.23R</i>	<i>Long-term insurance funds</i>	A separate accounting record in respect of each of a <i>firm's long-term insurance funds</i>	Not specified	Not specified
<i>PRU 7.6.56R</i> <i>PRU 7.6.57R</i>	<i>Branch accounting records in the United Kingdom</i>	A record of the activities carried on from a <i>non-EEA direct insurer's United Kingdom branch</i> and, if it is an <i>EEA-deposit insurer</i> , from its <i>branches</i> in other <i>EEA States</i> including a record of: (1) the income, expenditure and liabilities arising from activities of the <i>branch</i> or <i>branches</i> (2) the assets identified under <i>PRU 7.2.20R</i> as available to meet those liabilities	Not specified	Not specified

**The Integrated Prudential Sourcebook**  
**Schedule 2**  
**Notification requirements**

The existing text in Schedule 2 is deleted in its entirety and replaced by the following:

G

- 1 The aim of the *guidance* in the following table is to give the reader a quick overall view of the relevant notification requirements.
- 2 It is not a complete statement of those requirements and should not be relied on as if it were.
- 3 Table

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
<i>PRU 2.1.38R</i>	Breach or expected breach of <i>PRU 2.1.9R</i>	Fact of breach or expectation of breach	Breach or expectation of breach	Immediately
<i>PRU 2.2.71R</i>	Intention to include any perpetual non-cumulative <i>preference shares</i> or <i>innovative tier one instruments</i> in the <i>firm's tier one capital resources</i> for the purposes of <i>PRU 2.2</i>	Fact of intention	Intention to include	At least one month before the <i>firm</i> first includes the relevant items in its <i>tier one capital resources</i>
<i>PRU 2.2.72R</i>	Intention to redeem a <i>tier one instrument</i> that a <i>firm</i> has included in its <i>tier one capital resources</i> for the purpose of <i>PRU 2.2</i>	Fact of intention	Intention to redeem	At least one month before the intended redemption
<i>PRU 2.2.116R</i>	Proposed amendment to the terms of the debt and the documents referred to in <i>PRU</i>	Details of the proposed amendment and confirmation that the legal opinions referred to in	Proposal to amend	At least one month before the amendment is due to take effect

	2.2.108R(8)	<i>PRU</i> 2.2.108R(11) and, if applicable, <i>PRU</i> 2.2.105R and <i>PRU</i> 2.2.111R, continue in full force and effect in relation to the terms of the debt and the documents notwithstanding any proposed amendment		
<i>PRU</i> 2.2.117R	Intention to repay a <i>tier two instrument</i> (unless the <i>firm</i> intends to repay an instrument on its contractual repayment date)	Fact of intention and details of how the <i>firm</i> will meet its <i>capital resources requirement</i> after such repayment	Intention to repay	At least six months before the date of the proposed repayment
<i>PRU</i> 3.2.23R	That a <i>reinsurance exposure</i> to a <i>reinsurer</i> or group of closely related <i>reinsurers</i> is reasonably likely to exceed, or has exceeded, 100% of the <i>firm's capital resources</i> excluding <i>capital resources</i> held to cover <i>property-linked liabilities</i>	Fact that the limit is reasonably likely to be, or has been, exceeded  Note: upon notification under <i>PRU</i> 3.2.23R the <i>firm</i> must: (1) demonstrate that prudent provision has been made for the <i>reinsurance exposure</i> in excess of the 100% limit, or explain why in the opinion of the <i>firm</i> no provision is required, and (2) explain how	(1) A reasonable likelihood that the limit will be exceeded, or (2) if (1) does not apply, the limit being exceeded	As soon as the <i>firm</i> first becomes aware of the matter required to be notified

		the <i>reinsurance</i> exposure is being safely managed (see <i>PRU 3.2.24R</i> )		
<i>PRU 3.2.29R</i>	That the <i>firm</i> has exceeded, or anticipates exceeding, the limit expressed in <i>PRU 3.2.28E</i> (in each <i>financial year</i> a <i>firm</i> should restrict the <i>gross earned premiums</i> which it pays to a <i>reinsurer</i> or group of closely related <i>reinsurers</i> to the higher of (a) 20% of the <i>firm's</i> projected <i>gross earned premiums</i> for that <i>financial year</i> and (b) £4 million)	Fact that the limit has been exceeded, or that the <i>firm</i> anticipates exceeding the limit  Note: upon notification under <i>PRU 3.2.29R</i> the <i>firm</i> must explain to the <i>FSA</i> how, despite the excess <i>reinsurance</i> concentration, the credit risk is being safely managed (see <i>PRU 3.2.30R</i> )	The limit being exceeded, or an anticipation that the limit will be exceeded	Immediately

**The Integrated Prudential Sourcebook**  
**Schedule 3**  
**Fees and other required payments**

The existing text in Schedule 3 is deleted in its entirety and replaced by the following:

G

- 1 There are no requirements for fees or other payments in *PRU*.

**The Integrated Prudential Sourcebook**  
**Schedule 4**  
**Powers exercised**

The existing text in Schedule 4 is deleted in its entirety and replaced by the following:

G

1 The following powers and related provisions in the *Act* have been exercised by the *FSA* to make the *rules* in *PRU*:

- (1) section 138 (General rule-making power);
- (2) section 141 (Insurance business rules);
- (3) section 149 (Evidential provisions);
- (4) section 150(2) (Actions for damages); and
- (5) section 156 (General supplementary powers).

2 The following power in the *Act* has been exercised by the *FSA* to give the *guidance* in *PRU*:

Section 157(1) (Guidance).

...

**The Integrated Prudential Sourcebook**  
**Schedule 6**  
**Rules that can be waived**

The existing text in Schedule 6 is deleted in its entirety and replaced by the following:

G

- 1 The *rules* in *PRU* can be waived by the *FSA* under section 148 of the *Act* (Modification or waiver of rules), except for *PRU* 1.8.1R (actions for damages).

**CHILD TRUST FUNDS INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 139 (Miscellaneous ancillary matters);
  - (3) section 145 (Financial promotion rules);
  - (4) section 149 (Evidential provisions);
  - (5) section 156 (General supplementary powers); and
  - (6) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 December 2004.

**Amendments to the Handbook**

- D. The modules of the FSA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Interim Prudential sourcebook for Investment Businesses (IPRU(INV))	Annex A
Integrated Prudential sourcebook (PRU)	Annex B
Conduct of Business sourcebook (COB)	Annex C
Training and Competence sourcebook (TC)	Annex D
Supervision manual (SUP)	Annex E
Authorisation manual (AUTH)	Annex F
Credit Unions sourcebook (CRED)	Annex G
Glossary of definitions	Annex H

**Citation**

- E. This instrument may be cited as the Child Trust Funds Instrument 2004.

By order of the Board  
18 November 2004



## Annex A

### Amendments to Interim Prudential sourcebook for Investment Businesses

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

#### Contents

Chapter

...

8. Requirements on credit unions which are CTF providers

...

1.2.2 R (1) ...

(g) the Society of Lloyd's (in relation to underwriting agents); ~~and~~

(h) a *UCITS management company*; and

(i) a *credit union which is a CTF provider*.

1.2.5 R Table

This table belongs to IPRU (INV) 1.2.3R

...	
<i>Credit union which is a CTF provider</i>	Chapters 1 and 8

Insert after Chapter 7, a new Chapter 8, the text of this new chapter is not underlined.

8 Requirements on credit unions which are CTF providers

8.1 Application, general and professional indemnity insurance requirements

Application

8.1.1R (1) This chapter applies to a *credit union* to the extent that it is a *CTF provider* whose *permissions* relate to *accepting deposits* and *making arrangements with a view to transactions in investments*.

(2) The definitions in the Glossary at Appendix 13(1) apply to this chapter.

## General requirements

- 8.1.2R A *credit union* to which this chapter applies must:
- (1) have and maintain at all times financial resources of the kinds and amounts specified in, and calculated in accordance with, the *rules* of this chapter, in *CRED* and, where applicable, in *PRU* 9.3 (capital resources for *insurance mediation activity, mortgage mediation activity, mortgage lending and mortgage administration*); and
  - (2) be able to meet its liabilities as they fall due.
- 8.1.3G The *rules* in this chapter should be read with the *rules* relating to capital in *CRED* and, where applicable, *PRU*.

## Requirement to hold professional indemnity insurance

- 8.1.4G
- (1) Under *Principles* 3 and 4, a *credit union* is required to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems and to maintain adequate financial resources.
  - (2) Although financial resources and appropriate systems and controls can generally mitigate operational risk, professional indemnity insurance has a role in mitigating the risks a *credit union* faces in its day to day operations. The purpose of *IPRU(INV)* 8.1.6R to *IPRU(INV)* 8.1.14E is to ensure that a *credit union* has in place the type, and level, of professional indemnity insurance necessary to mitigate these risks.
- 8.1.5R The term "relevant income" in *IPRU(INV)* 8.1 refers to all income received or receivable which is commission, brokerage, fees or other related income, whether arising from the *credit union's* activities related to *making arrangements with a view to transactions in investments* or not, for the last accounting year prior to inception or renewal of the professional indemnity insurance policy ("the policy").
- 8.1.6R A *credit union* must take out and maintain at all times professional indemnity insurance that is at least equal to the requirements of *IPRU(INV)* 8.1.7R to *IPRU(INV)* 8.1.14E.

## Professional indemnity insurance policy terms

- 8.1.7R The professional indemnity insurance policy must incorporate terms which are appropriate and must make provision for:
- (1) cover in respect of any claim for loss or damage, for which the *credit union* may be liable as a result of an act or omission by:
    - (a) the *credit union*; or

- (b) any *person* acting on behalf of the *credit union* including *employees, appointed representatives* or its other agents;
- (2) the minimum *limits of indemnity* in each year if the *credit union* is an *IMD insurance intermediary* are as set out in *PRU 9.2.13R*;
- (3) the following *limits of indemnity* if the *credit union* is an investment intermediary other than an *IMD insurance intermediary*:
  - (a) if the *credit union* has relevant income of up to £3,000,000, no lower than £500,000 for a single claim against the *credit union* and £500,000 in the aggregate; or
  - (b) if the *credit union* has relevant income of more than £3,000,000, no lower than £650,000 for a single claim against the *credit union* and £1,000,000 in the aggregate.
- (4) If (2) applies, and the policy is denominated in any currency other than euros, a *credit union* must take reasonable steps to ensure that the *limits of indemnity* are, when the policy is effected (i.e. agreed) and at renewal, at least equivalent to those required in *IPRU(INV) 8.1.7R*.

Readily realisable own funds

8.1.8G For the purposes of the following provisions relating to professional indemnity insurance, the *FSA* expects items included in *own funds* to be regarded as “readily realisable” only if they can be realised, at any given time, within 90 days.

Additional requirements

- 8.1.9E (1) In addition to the specific requirements in *IPRU(INV) 8.1.7R*, to incorporate appropriate terms, the policy should make provision for the following:
- (a) for a *credit union* with relevant income of more than £6,000,000, the aggregate limit identified in the table below:

Relevant income is (£)		Minimum aggregate <i>limit of Indemnity</i> (£)
more than	up to	
6,000,000	7,000,000	1,150,000
7,000,000	8,000,000	1,300,000
8,000,000	9,000,000	1,450,000
9,000,000	10,000,000	1,600,000
10,000,000	12,500,000	2,000,000

12,500,000	15,000,000	2,400,000
15,000,000	17,500,000	2,800,000
17,500,000	20,000,000	3,150,000
20,000,000	25,000,000	3,800,000
25,000,000	30,000,000	4,250,000
30,000,000	35,000,000	4,500,000
35,000,000	40,000,000	4,750,000
40,000,000	50,000,000	5,500,000
50,000,000	60,000,000	6,000,000
60,000,000	70,000,000	6,750,000
70,000,000	80,000,000	7,250,000
80,000,000	90,000,000	7,750,000
90,000,000	100,000,000	8,500,000
100,000,000	150,000,000	11,250,000
150,000,000	200,000,000	14,000,000
200,000,000	250,000,000	17,000,000
250,000,000	300,000,000	19,750,000
300,000,000	n/a	22,500,000

(b) full retroactive cover in respect of the kinds of liabilities described in *IPRU(INV)* 8.1.7R for claims arising from work carried out by the *credit union*, or on its behalf, in the past; and

(c) cover in respect of *Ombudsman* awards made against the *credit union*.

(2) Compliance with (1)(a) may be relied on as tending to establish compliance with the requirement in *IPRU(INV)* 8.1.7R for the professional indemnity insurance terms to be appropriate.

(3) Contravention of (1)(a) may be relied on as tending to establish contravention of the requirement in *IPRU(INV)* 8.1.7R for the professional indemnity insurance terms to be appropriate.

8.1.10G A *credit union* should consider whether the overall cover is adequate taking account of *IPRU(INV)* 8.1.13G(2) and whether the *credit union* should seek additional cover or legal expenses insurance. (Legal defence costs are costs of defence against claims that fall under the terms of the policy.)

8.1.11G The cover provided by the policy should be wide enough to include the liability of the *credit union*, its *appointed representatives*, *employees* and its agents for breaches of the *credit union's* duty of skill and care, fiduciary duty,

duty to look after documents or assets, fraud, and breaches of obligations imposed by or under the *Act*.

#### Exclusions

- 8.1.12R The policy must not be subject to conditions or exclusions which unreasonably limit the cover provided for in *IPRU(INV)* 8.1.7R (whether by exclusion of cover, by policy excesses or otherwise).
- 8.1.13 G (1) The *FSA* considers it reasonable for a *credit union*'s policy to exclude cover for:
- (a) specific business lines if that type of business has not been carried out by the *credit union* in the past and will not be carried out by the *credit union* during the life of the policy; or
  - (b) specific claims that have been previously notified to the *credit union's insurer* and claimed for under another policy.
- (2) The *FSA* does not consider it reasonable for a *credit union's* policy to treat legal defence costs cover as part of the *limits of indemnity* if this reduces the cover available for any individual substantive claim.
- 8.1.14E (1) The policy should not:
- (a) make provision for payment by the *credit union* of an excess on any claim of more than £5,000. (This does not apply to the extent that the *credit union* holds additional *own funds* in a readily realisable form, in accordance with *IPRU(INV)* 8.1.16E); or
  - (b) exclude any type of business or activity that has been carried out by the *credit union* in the past or will be carried out by the *credit union* during the time for which the policy is in force. (This does not apply to the extent that the *credit union* holds, by way of additional *own funds* in a readily realisable form, an amount equivalent to a reasonable provision against its potential liabilities for that business or activity. *Guidance* on this is given in *IPRU(INV)* 8.1.17G and *IPRU(INV)* 8.1.18G); or
  - (c) exclude liability which is identified or crystallised as a result of regulatory action against the *credit union* (either individually or as a member of a class of *authorised person*).
- (2) Contravention of (1)(a) may be relied on as tending to establish contravention of *IPRU(INV)* 8.1.12R.

## Excess level

8.1.15E The reference to “excess” in *IPRU(INV)* 8.1.14E(1)(a) is to the highest excess level required to be paid under the policy unless that excess relates to a type of business that has not been carried out by the *credit union* in the past. In those circumstances, the reference is to the next highest excess level required by the policy.

## Additional own funds

8.1.16E The amount of additional *own funds* in *IPRU(INV)* 8.1.14E (1)(a) should be calculated by referring to the *credit union*'s relevant income and excess obtained in the following table:

All amounts are shown in £000s													
Relevant income is		Excess obtained, up to and including											
more than	up to	5	10	15	20	25	30	40	50	75	100	150	200+
0	100	0	4	7	9	12	14	18	21	28	34	45	54
100	200	0	7	11	14	17	20	25	29	38	46	59	70
200	300	0	9	14	18	21	24	30	35	45	54	69	82
300	400	0	11	16	21	24	28	34	39	50	60	77	91
400	500	0	13	18	23	27	30	37	43	55	66	83	98
500	600	0	14	20	25	29	33	40	46	59	70	89	105
600	700	0	16	22	27	31	35	42	49	63	74	94	111
700	800	0	17	23	28	33	37	45	52	66	78	99	117
800	900	0	18	24	30	35	39	47	54	69	82	103	122
900	1,000	0	19	26	31	36	41	49	56	72	85	107	126
1,000	1,500	0	23	31	37	43	48	57	66	83	99	124	146
1,500	2,000	0	26	35	42	48	54	64	73	93	109	138	161
2,000	2,500	0	29	38	46	53	59	71	81	102	121	152	179
2,500	3,000	0	32	42	51	58	65	78	89	112	132	166	195
3,000	3,500	0	35	46	55	63	71	84	96	121	142	179	210
3,500	4,000	0	38	50	59	68	76	90	102	129	152	191	223
4,000	4,500	0	41	53	63	72	80	95	108	137	161	202	236
4,500	5,000	0	43	56	67	76	85	100	114	144	169	212	248
5,000	6,000	0	48	62	73	84	93	110	125	157	185	231	271
6,000	7,000	0	52	67	79	90	101	119	135	169	199	249	291
7,000	8,000	0	56	72	85	97	107	127	144	181	212	265	310
8,000	9,000	0	59	76	90	103	114	134	152	191	224	280	328
9,000	10,000	0	63	80	95	108	120	141	160	201	236	294	344
10,000	100,000	0	63y	80y	95y	108y	120y	141y	160y	201y	236y	294y	344y
100,000	n/a	0	630	800	950	1080	1200	1410	1600	2010	2360	2940	3440
For <i>firms</i> with relevant income more than £10m but up to £100m value y is calculated by relevant income/ £10m													

## Exclusions

- 8.1.17G A *credit union* should take into account the following when assessing the amount of additional *own funds* to be held as provision as described in *IPRU(INV)* 8.1.14E(1)(b):
- (1) the type of business line or activity excluded and the types of claim which might arise from it;
  - (2) the number of contracts written or volume of activity;
  - (3) the number of complaints received by the *credit union* relating to the excluded business or activity;
  - (4) generally accepted accounting principles applicable to provisions; and
  - (5) any other relevant information.

- 8.1.18G If the *credit union* holds additional *own funds* in accordance with *IPRU(INV)* 8.1.17G then the amount should be reviewed regularly. The reviews should take account of changes in the status of the policy exclusion(s) and any relevant changes to the *credit union*'s circumstances.

## Policies providing cover for more than one credit union

- 8.1.19R If the policy provides cover to more than one *credit union* then in relation to *IPRU(INV)* 8.1.7R:
- (1) the relevant income for calculating the *limits of indemnity* is that of all the *credit unions* named in the policy combined;
  - (2) each *credit union* named in the policy must have the benefit of the minimum *limits of indemnity* as required in *IPRU(INV)* 8.1.7R;
  - (3) each *credit union* named in the policy must notify the *FSA* if the aggregate cover in the policy falls below the minimum in *IPRU(INV)* 8.1.7R.

## Exemption from holding professional indemnity insurance

- 8.1.20R
- (1) A *credit union* is not required to effect or maintain professional indemnity insurance in relation to *insurance mediation activity*, if another *authorised person* which has net tangible assets of more than £10 million provides a comparable guarantee.
  - (2) A 'comparable guarantee' means a written agreement on terms at least equal to those in *PRU* 9.2.10R to finance the claims that might arise as a result of a breach by the *credit union* of its duties under the *regulatory system* or civil law.

- 8.1.21R A *credit union* must take out professional indemnity insurance from:
- (1) any *insurance undertaking* which is authorised to transact professional indemnity insurance in the *EEA*; or
  - (2) a *person* of equivalent status in:
    - (a) a *Zone A country*;
    - (b) the Channel Islands, Gibraltar, Bermuda or the Isle of Man.

Notification requirements

- 8.1.22G Rule *IPRU(INV)* 8.1.24R is a *notification rule* and is in addition to any notification requirements in the Supervision manual (*SUP* 15).
- 8.1.23G *Credit unions* are reminded to comply with *SUP* 15.7 (Form and method of notification) when notifying the *FSA* in accordance with *IPRU(INV)* 8.1.24R.
- 8.1.24R A *credit union* must notify the *FSA* immediately it becomes aware, or has information which reasonably suggests, that any of the matters in Table 8.1(1) has occurred, may have occurred or may occur in the foreseeable future.

Table 8.1(1)

This table forms part of *IPRU(INV)* 8.1.24R

NOTIFIABLE EVENTS
<p>In relation to professional indemnity insurance, required in accordance with <i>IPRU(INV)</i> 8.1.6R to <i>IPRU(INV)</i> 8.1.21R, if:</p> <ol style="list-style-type: none"> <li>(1) it cannot be obtained within 28 days of the inception or renewal date;</li> <li>(2) it is cancelled;</li> <li>(3) the amount of aggregate cover is exhausted;</li> <li>(4) the <i>credit union</i> commences business lines for which it had not obtained cover;</li> <li>(5) the <i>credit union</i> is relying on <i>IPRU(INV)</i> 8.1.19R; or</li> <li>(6) the <i>credit union</i> is relying on <i>IPRU(INV)</i> 8.1.20R.</li> </ol>

8.2 Capital requirements

- 8.2.1R ‘Capital’ in this chapter has the meaning described in *CRED* 8.2.1R.
- 8.2.2R A *version 1 credit union* with total assets of more than £5 million or a total number of members of more than 5,000, or both, or a *version 2 credit union*, which acts as a *CTF provider* and whose *permissions* include *regulated activities* relating to *accepting deposits* and *making arrangements with a view*



*to transactions in investments other than contracts of insurance or rights to or interests in a life policy* must maintain at all times capital which is equal to the higher of:

- (1) £10,000; and
- (2) the capital requirements for the *credit union* under *CRED*.

8.2.3R

A *version 1 credit union* with total assets of more than £5 million or a total number of members of more than 5,000, or both, or a *version 2 credit union*, which acts as a *CTF provider* which *makes arrangements with a view to transactions in investments including contracts of insurance or rights to or interests in a life policy* must maintain at all times capital which is equal to the highest of:

- (1) £10,000;
- (2) the capital requirements for the *credit union* under *CRED*; and
- (3) the capital requirements for the *credit union* under *PRU 9.3*.

## Annex B

### Amendments to the Integrated Prudential sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

Application: credit unions

- 9.3.9 G
- (1) For *credit unions* to which this section applies and which are not CTF providers, the capital requirements will be the higher of the requirements in this section and in *CRED* (see *PRU* 9.3.25R).
  - (2) For *credit unions* to which this section applies and which are CTF providers with permission to carry on designated investment business, the capital requirements will be the highest of the requirements in this section, those in *CRED* and of *IPRU(INV)* Chapter 8 (see *PRU* 9.3.25R).

...

Capital resources requirement: firms carrying on regulated activities including designated investment business

9.3.24 R The capital resources requirement for a *firm* (other than a credit union) carrying on *regulated activities*, including *designated investment business*, is the higher of:

- (1) ...

Capital resources requirement: credit unions

9.3.25 R The capital resources requirement for a *credit union* to which this section applies (see *PRU* 9.3.8R) is the highest~~r~~ of:

- (1) the requirement which is applied by *PRU* 9.3.30R (Capital resources requirement: mediation activity only) treating that *rule* as applying to the *credit union* by disregarding activities which are not *insurance mediation activity* or *mortgage mediation activity*; ~~and~~
- (2) the amount which is applied by *CRED* 8 (Capital requirements)-; and
- (3) if the credit union is a CTF provider that has a permission to carry on designated investment business, the amount which is applied by IPRU(INV) Chapter 8.

## Annex C

### Amendments to the Conduct of Business Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.11.1 G Table: Application of rules in COB in relation to deposits

COB	Subject matter	Application for cash deposit ISAs <u>and cash deposit CTFs</u>	Application for other deposits
2.5.5 R	Exclusion of liability	Y <i>(distance contract only)</i>	Y <i>(distance contract only)</i>
2.6	General provisions related to distance marketing	Y <i>(distance marketing only)</i>	Y <i>(distance marketing only)</i>
3.5.5R to 3.5.7R 3.8.4R to 3.8.5E	Financial promotions	Y	Y
3.8.8R, 3.8.11R, 3.8.15R	Specific non-real time financial promotions	Y <i>(if the financial promotion relates to a structured deposit)</i>	Y <i>(if the financial promotion relates to a structured deposit)</i>
3.9.6R(1), 3.9.7AR and 3.9.8R	Direct offer financial promotions	Y	X
<u>3.9.21R</u>	<u>Direct offer financial promotions</u>	<u>Y</u>	<u>X</u>
<u>3.9.30R</u>	<u>Direct offer financial promotions</u>	<u>Y</u> <i>(cash deposit CTFs only)</i>	<u>X</u>
6.1.4R, 6.1.5R, 6.2.2R, 6.4.13R, 6.5.2R(2), 6.5.3R, <del>6.5.42R</del>	Product disclosure	Y	X
<u>6.5.42R</u>	<u>Product disclosure</u>	<u>Y</u> <i>(cash deposit ISAs only)</i>	<u>X</u>
<u>6.5.42AR</u>	<u>Product disclosure</u>	<u>Y</u> <i>(cash deposit CTFs only)</i>	<u>X</u>
6.4.25R	Pre-contract information when entering into a <i>distance contract</i> for <i>accepting deposits</i>	X	Y <i>(distance contract only)</i>
6.4.27R to 6.4.31R	Exemptions for telephone sales; certain other <i>means of distance communication</i> ; and successive operations	Y <i>(distance contract and other telephone sales only)</i>	Y <i>(distance contract only)</i>

<u>6.5.40R(7)</u>	<u>Product disclosure</u>	<u>Y</u> <i>(cash deposit CTFs only)</i>	<u>X</u>
6.7.7R(1), 6.7.17R, 6.7.18R, 6.7.21R	Cancellable contracts	X	Y <i>(distance contract only)</i>
6.7.7R(3)	Cancellable contracts	Y	X
6.7.10R(2), 6.7.10AR, 6.7.11R	Cancellation period	Y	Y <i>(distance contract only)</i>
6.7.42R to 6.7.48R	Exercising the right to cancel	Y	Y <i>(distance contract only)</i>
6.7.51R to 6.7.53R	Effects of, and obligations on, cancellation	Y	Y <i>(distance contract only)</i>
<u>6.7.52AR</u>	<u>Effects of, and obligations on, cancellation</u>	<u>Y</u> <i>(cash deposit CTFs only)</i>	<u>X</u>
Note:			
<p>1. Those <i>rules</i> marked with "X" do not apply; those marked with "Y" do apply.</p> <p>2. This Table lists <i>rules</i> imposing obligations. It does not list all application <i>rules</i>, exemptions, transitional <i>rules</i> or guidance.</p>			

...

3.2.3R (1) To the extent that a *financial promotion* relates to one or more of the following:

(a) ...

(b) ...

only *COB 3.1* to *COB 3.5* and *COB 3.8.4R* to *COB 3.8.6G* and *COB 3.14* apply, unless the *financial promotion* relates to a *cash deposit ISA* or *cash deposit CTF* in which case *COB 3.9.6R(1)*, *COB 3.9.7AR*, and *COB 3.9.8R* and *COB 3.9.21R* also apply and, if the *financial promotion* relates to a *cash deposit CTF*, *COB 3.9.30R* also applies; and

...

...

3.9.3G Table: Location of the provisions applicable to direct offer financial promotions

This table belongs to COB 3.9.2G

		...	
	(k)	<u>CTFs</u>	<u>COB 3.9.8R</u> <u>COB 3.9.30R</u>

3.9.4G *Firms* are reminded that under COB 3.2.3R:

(1) ...

(a) a deposit (except a cash deposit ISA or cash deposit CTF); or

...

Cash deposit ISAs and cash deposit CTFs

3.9.8R A *direct offer financial promotion* relating to a cash deposit ISA or cash deposit CTF must contain the information required by whichever of COB 6.5.42R (1) to (8) or COB 6.5.42AR applies to it and COB App 1.

...

EIS or non-packaged product ISA, ~~or~~ PEP or CTF with no right of withdrawal

3.9.21R A *direct offer financial promotion* which relates to an EIS or non-packaged product ISA, ~~or~~ PEP or CTF for which no right to withdraw is given under case 8 of row 2, COB 6.7.17R, must include the statement required by that provision.

...

Child trust funds

3.9.30R ~~To follow.~~ A direct offer financial promotion relating to a CTF must contain the information referred to in COB 6.5.40R (7).

...

2 Table: Contents

....	
Section II: Guidance relevant to direct offer financial promotions for <del>PEP</del> <u>ISA</u> or <u>CTF</u> transfers and personal pensions and stakeholder pension schemes	
E	<del>PEP</del> <u>ISA</u> or <u>CTF</u> transfers
...	

...

7 Table: E

<del>PEP</del> <u>ISA</u> or <u>CTF</u> transfers
<p><i>A direct offer financial promotion</i> for a <del>PEP</del> <u>ISA</u> or <u>CTF</u> transfer should include details of the likely advantages and disadvantages of transferring an existing <del>PEP</del> <u>ISA</u> or <u>CTF</u> holding, including:</p> <p>...</p> <p>(5) potential for loss of income or growth, following a rise in the markets, whilst the <del>PEP</del> <u>ISA</u> or <u>CTF</u> transfer remains pending.</p>

...

COB 4 Ann 2E

1 Table: Content of terms of business provided to a customer: general requirements

This table belongs to *COB 4.2.11E*.

<i>A firm's terms of business</i> (including a <i>client agreement</i> ) provided to a <i>customer</i> should, where relevant, include some provision about:	
....	
(9)	<p>Cancellation and withdrawal</p> <p>(a) In the case of a <i>non-packaged product</i> <del>ISA</del> <u>PEP</u> or <u>CTF</u>, an explanation of any right to withdraw (see <i>COB 6.7</i> (Cancellation and withdrawal)) or, if it is the case, a statement that such rights will not apply.</p>
...	

...

5.1.4 R (1) If a decision is made by a *provider firm* to provide *advice on investments* in accordance with this section, to a *private customer* on a *stakeholder pension scheme* or a CTF produced by a *person* ("the

producer") other than the *firm* (or, where applicable, outside the *marketing group* of the *firm*), then that *stakeholder pension scheme* or CTF becomes an *adopted packaged product* of the *firm* (and, where relevant, of all the members of its *marketing group*).

...

...

- 5.1.12 R (1) A *provider firm* must, subject to (2), take reasonable steps to ensure that its *representatives* are able to sell with advice each type of *packaged product* that it issues itself, or is issued by its *marketing group*, or is an *adopted packaged product* other than an adopted packaged product to be held within a *CTF*.

...

5.3.13G

...

- (4) *COB 5.3.29G* contains *guidance* which is relevant for assessing the suitability of:

...

- (f) *ISA*, ~~or~~ PEP or CTF transfers; and

...

5.3.29G Guidance on matters which should be taken into account when assessing the suitability of various personal recommendations. This table belongs to *COB 5.3.13G (4)*.

Suitability guidance	
...	
F	<u>ISA</u> , <del>or</del> <u>PEP or CTF transfers</u>
	When a firm is advising a <i>customer</i> on whether to transfer existing <i>ISA</i> , <del>or</del> <u>PEP or CTF</u> holdings, <i>COB 5.2</i> (Know your <i>customer</i> ) and <i>COB 5.3</i> (Suitability) apply. All the advantages and disadvantages of transferring should be considered. In particular the following information (which is not exhaustive) should be considered and provided to the <i>customer</i> , usually as part of the <i>suitability letter</i> , before the transfer takes place:
	(a) ...
	...
	(e) potential for loss of income or growth, following a rise in markets, while the <i>ISA transfer</i> , <del>or</del> <u>PEP transfer or CTF transfer</u> remains pending.

...

6.1.1R COB 6.1 to COB 6.5 apply to a *firm*:

...

- (2) which manages, sells or *personally recommends* a *cash deposit ISA* or *cash deposit CTF* for or to a *private customer*; or

...

6.1.3G COB 6.1 to COB 6.5 amplify *Principle 7* (Communications with clients), which requires a *firm* to pay due regard to the information needs of its *customers*. In the case of *packaged products* there is a special need to ensure that *private customers* are supplied with information which will highlight particular *packaged product* features. This also needs to be achieved in a way which will optimise the *private customer's* ability to make a comparative analysis of different *packaged products*. These *rules* also address a similar information need in relation to *cash deposit ISAs*, *cash deposit CTFs* and when a *firm* enters into a *distance contract* to *accept deposits* with a *retail customer*.

6.1.4R ...

- (2) A *firm* to which COB 6.4.13R(1) applies must, for each *cash deposit ISA* or *cash deposit CTF* it offers, produce the information document required by COB 6.5.42R or COB 6.5.42AR instead of *key features*. That information document must comply with COB 6.1, COB 6.2 and COB 6.5 as to design and content.

Quality and production of key features

6.1.5R A *firm* must ensure that any *key features* or information document it produces in relation to a *packaged product*, ~~or~~ *cash deposit ISA* or *cash deposit CTF* is in writing, whether in printed hard copy or in electronic format, and:

- (1) is produced and presented to at least the same quality and standard as the associated sales or marketing material being used by the *firm* to promote the *packaged product*, ~~or~~ *cash deposit ISA* or *cash deposit CTF* to *customers*; and

...

6.2.2R The *key features* or information which the rules COB 6.1, COB 6.2 and COB 6.4 require a *firm* to provide to a *private customer* in relation to a *packaged product*, ~~or~~ *cash deposit ISA* or *cash deposit CTF* must be provided by the *firm* in a *durable medium*.

...



Exceptions for life policies: variations of policies held within a CTF

6.2.21AR COB 6.2.7R does not apply to a CTF provider in relation to a variation to an existing policy held within a CTF, if:

- (1) the terms and conditions, including all charges, are the same as applied at the time of the purchase, or the most recent purchase or payment, of the existing policy; and
- (2) key features outlining those terms and conditions were issued to the customer in respect of that previous purchase.

...

6.2.24R A firm need not provide *key features* to a *private customer* in respect of a *scheme* if:

...

- (6) a *private customer* is making a purchase of a *scheme holding* (whether or not held within a CTF) in a fund in which he already has a *scheme holding* and has already been provided with appropriate *key features* covering the purchase;

...

6.4.1R COB 6.4 applies to a *firm* in accordance with COB 6.1.1R, in respect of *occupational pension schemes, self invested personal pensions schemes, income withdrawals, cash deposit ISAs, cash deposit CTFs, Revenue allocated CTFs, traded life policies, stakeholder pension schemes, packaged products, other deposits and long-term care insurance contracts.*

...

Cash deposit ISAs and cash deposit CTFs

6.4.13R When a *firm* manages, *personally recommends* or sells a *cash deposit ISA* or *cash deposit CTF* to a *private customer*, that *customer* must be provided with the information specified in whichever of COB 6.5.42R or COB 6.5.42AR applies to it in good time before the *customer* is bound by the transaction, unless COB 6.4.27R to COB 6.4.31R (telephone sales and other exemptions) applies.

...

- 6.4.27R
- (1) Where this chapter requires *key features* or other information to be provided, in the case of voice telephony communications, a *firm*:
    - (a) must provide the *customer* at the beginning of the telephone conversation with the name of the *firm* and (if the call is initiated by the *firm*) the commercial purpose of the call; ~~and~~
    - (b) ...

- (vi) that other information is available on request, and the nature of that information, and
- (vii) in addition to (a) and (b) above, where the product is a CTF, provided the customer gives his explicit consent to receiving only limited information, may proceed on the basis of the information referred to in COB 6.5.40R (7) given orally.

...

Exemption: Revenue allocated accounts

6.4.34R When a firm opens a Revenue allocated CTF, the firm must send the private customer on the first available opportunity after the account has been opened, whichever of key features or other information is required in a durable medium.

6.4.35G In considering what the first available opportunity mentioned in COB 6.4.34R is, firms may take into account that there may generally be a delay between a Revenue allocated CTF being opened and the customer being informed that it had been opened.

6.5 Content of key features and important information: life policies, schemes, ISA and CTF cash deposit components and stakeholder pension schemes

...

6.5.2R A firm must ensure, unless COB 6.5.3R applies, that:

...

- (2) the information it produces under COB 6.4.13R (1) for a cash deposit ISA or cash deposit CTF ~~under COB 6.4.13R (1)~~ complies with whichever of 6.5.42R or COB 6.5.42AR applies to it;

...

6.5.21G The information required by COB 6.5.20R should include:

...

- (8) for a life policy or a scheme which is to be held within a CTF the information referred to in COB 6.5.40R (7).

...

6.5.28R The information relating to 'Total actual deductions to date' and 'Effect of deductions to date' in *COB 6.5.23R*, ...

- (1) ...
- (2) a *life policy* for a term not exceeding five years; and
- (3) a *life policy* held within a *CTF*.

...

6.5.30R For a *schemes*, a *firm* must include the contents of *COB 6.5.31R* unless the *scheme* is to be held within a *stakeholder CTF*.

...

Further information for life policies, schemes, insurance or equity ISAs, PEPs, CTFs and stakeholder pension schemes

6.5.40R A *firm* must include the following information in the *key features*, separately or as part of the information required by *COB 6.5.2R*:

...

- (7) For *investments* held within a *CTF*:
  - (a) a prominent statement that after *money* is paid into a *CTF* it is locked in, and that this means that it can only be accessed by the child when he is 18, except as permitted by the *CTF Regulations*, and any contributions made to the *CTF* cannot be returned to the donor;
  - (b) if the *CTF* is a *stakeholder CTF*, an explanation of the minimum standards (as described in paragraph 2 of the Schedule to the *CTF Regulations*) and *CTF* lifestyling approach (as defined in subparagraph 2 of the Schedule to the *CTF Regulations*), together with a statement that satisfying these minimum standards does not mean that the *investment* is suitable for the *customer* or that there is any guarantee of performance;
  - (c) if the *CTF* is a *non-stakeholder CTF*, a prominent statement that it is not a *stakeholder CTF* and that a *stakeholder CTF* is available from a named alternative *CTF provider*, together with a detailed description of that *stakeholder CTF*;
  - (d) a statement that the *CTF* will not be opened until any cancellation period has expired; and
  - (e) a balanced comparison between *stakeholder CTFs* and *non-stakeholder CTFs*.

Information requirements for cash deposit ISAs, cash deposit CTFs, friendly society tax-exempt policies, traded life policies and broker funds

...

6.5.42AR If COB 6.4.13R applies, for a cash deposit CTF, the private customer must be given in place of key features:

- (1) the information contained in COB 6.5.42R (4) to (6) and (8) to (11) and in COB 6.5.40R (7);
- (2) details of the arrangements for exercising any right to cancel;
- (3) a statement explaining where a private customer can obtain further information about CTFs; and
- (4) in relation to a distance contract with a retail customer, all the contractual terms and conditions and the information in COB App 1.

...

6.6.50R

Rate of return assumptions for all schemes, ordinary branch non-pensions, industrial branch, friendly society, immediate annuity and Holloway sickness policies (all monetary rates of return)			
	Lower rate	Intermediate rate	Higher rate
....			
(c) Tax-exempt business held within an ISA, or PEP or CTF or by a friendly society, relating to schemes, ordinary branch non-pensions and industrial branch business	5%	7%	9%
...			

...

6.7.1R COB 6.7 applies to:

- (1) a product provider;
- (1A) a CTF provider;
- (2) ...

(3) an independent intermediary, when acting as an *EIS manager*, *ISA manager*, *CTF provider* or *plan manager*, or when selling on to a customer units which the firm has bought or redeemed as *principal* for that purpose;

(4) a deposit-taking firm, when acting as *ISA manager*, *CTF provider* or as the firm responsible for holding deposits in respect of another firm's cash deposit *ISA* or *cash deposit CTF*; or

...

6.7.5G Table: Cancellable investment agreements  
This table belongs to COB 6.7.4G

Cancellable investment agreements			
	Post-sale right to cancel?	Pre-sale right to withdraw?	Maximum period of reflection (but see COB 6.7.11R)
A. Contracts where the right arises regardless of means of sale.			
...			
<i>Life policy (including pension policy, pension annuity or within ISA or CTF)</i>	Yes <sup>1,5, 6, 12</sup>	No <sup>1</sup>	30 days
...			
Certain variations of existing <i>life policies, pension contracts</i> and <i>SHPs</i>	Yes <sup>1,5, 6, 8</sup>	No <sup>1</sup>	30 days
B. Contracts where the right arises only if advice is given or if sold by <i>distance contract</i>			
...			
<u>Units in an AUT, recognised scheme or ICVC (within a CTF):</u>			
(1) if sold by <i>distance contract</i>	Yes <sup>10, 12</sup>	No	
(2) <i>non-stakeholder CTFs</i> not sold by <i>distance</i>	Yes <sup>11, 12</sup>	No	

<u>contract sold with advice</u>			
<u>(3) non-stakeholder CTFs not sold by distance contract sold without advice</u>	<u>No</u>	<u>No</u>	
<u>(4) stakeholder CTFs not sold by distance contract</u>	<u>No</u>	<u>No</u>	
<u>ISA, PEP or CTF not mentioned in any other row</u>			
(1) if sold by <i>distance contract</i>	Yes <sup>5, 6, 12</sup>	No	14 days
(2) if sold otherwise with advice	No	Yes <sup>3, 2</sup>	7 days
<u>Units in an AUT, recognised scheme or ICVC (outside an ISA, PEP or CTF)</u>	...	...	...
...			
Notes:			
...			
6. There is no post-sale right to cancel for a <i>distance contract</i> :			
(a) ...; or			
(b) where <del>the</del> a <i>firm</i> has an initial service agreement with the <i>customer</i> and the contract is in relation to a successive operation or separate operation of the same nature under that agreement (see COB 1.10.2G).			
<u>In the case of <i>life policies</i> held within a <i>CTF</i> sold by <i>distance contract</i>, the right to cancel applies only to any initial service agreement.</u>			
...			
<u>8. There is no right to cancel for variations of <i>life policies</i> held within a <i>CTF</i>.</u>			
<u>9. For contracts relating to a <i>CTF</i>, there is no right to withdraw.</u>			
<u>10. The initial service agreement is cancellable.</u>			
<u>11. The <i>cancellation rules</i> that apply are the same as those that apply to the <i>underlying investments</i>.</u>			

12. Where a right to cancel applies to an agreement relating to a <i>CTF</i> that has been opened, the <i>money</i> may be reinvested but will not be returned to the <i>private customer</i> .
---

...

6.7.7R A *retail customer* has a right to cancel:

...

- (3) a contract for a *cash deposit ISA*, unless the right to cancel is disapplied for a *distance contract* by case 15 of row 2 to *COB* 6.7.17R, or a *cash deposit CTF* if the *cash deposit CTF* is sold by *distance contract*;

...

6.7.10A R The cancellation period begins on:

- (1) (other than for *distance contracts*, ~~and~~ *cash deposit ISAs* and *CTFs*) the date the *customer* receives the reminder notice of his right to cancel in accordance with *COB* 6.7.30R;
- (2) for *distance contracts*, ~~and~~ *cash deposit ISAs* and *CTFs* the later of:
  - (a) ...

...

6.7.15R Cancellable contracts and exceptions – life

This table belongs to *COB* 6.7.7R (1).

Cancellable contracts and exceptions – life	
Row 1	... A. <i>Life policy</i> (whether or not held within an <i>ISA</i> or <i>CTF</i> – see notes 1, 2, <del>and</del> 3, 6 and 7 in <i>COB</i> 6.7.16R) (see <i>COB</i> 6.7.23R regarding variation of an existing <i>life policy</i> ).
Row 2	... 11. the contract is a <i>distance contract</i> where: ... (b) <del>the</del> a <i>firm</i> has an initial service agreement with the <i>retail customer</i> and the contract is in relation to a successive operation or successive operations of the same nature under the agreement (see <i>COB</i> 1.10.2G).

6.7.16R

...
-----

6. In the case of *life policies* held within *CTFs* that are *distance contracts*, the initial service agreement is cancellable.

7. If the *CTF* has been opened the life insurer must not cancel the *life policy* until it has new instructions to deal with the proceeds in accordance with the *CTF Regulations*.

8. In relation to *Revenue allocated accounts*, the life insurer must not accept any additional contributions until the cancellation period has expired without the right to cancel being exercised.

6.7.17R Cancellable contracts and exceptions – non-life

This table belongs to *COB 6.7.7R (1)* and *COB 6.7.14R (1)*

Cancellable contracts and exceptions – non-life	
Contracts which a <i>retail customer</i> has a right to cancel under <i>COB 6.7.7R(1)</i> (subject to row 2):	
Row 1	<p>...</p> <p>C. subscriptions (but see notes 1, 2 and 5 in <i>COB 6.7.18R</i>) which can be invested only in <i>units</i> (whether or not held within an <i>ISA</i>, <i>PEP</i> or <i>pension contract</i>, <u>but not if held within a <i>CTF</i></u>) in an <i>AUT</i>, <i>recognised scheme</i> or <i>ICVC</i> purchased from:</p> <p>(a) the <i>operator</i>; or</p> <p>(b) its <i>marketing group associate</i> acting as an <i>ISA manager</i>, or <i>plan manager</i>;</p> <p>D. <i>distance contracts</i> (but see notes 6 and 8 in <i>COB 6.7.18R</i>) (whether or not held within a <i>CTF</i>) (other than for a <i>life policy</i>, <i>stakeholder pension scheme</i>, <i>cash deposit ISA</i>, <i>cash deposit CTF</i> or a contract in A, B or C) the making or performance of which by the <i>firm</i> constitutes or is part of:</p> <p>(a) <i>dealing as agent</i>, <i>advising</i> or <i>arranging</i> in relation to <i>designated investments</i>, unless the <i>distance contract</i> is concluded merely as a stage in the provision of another service by the <i>firm</i> or another <i>person</i> (see <i>COB 1.10.6G</i>); or</p> <p>(b) any other <i>designated investment business</i>; or</p> <p>(c) <i>accepting deposits</i>.</p> <p><u>E. subscriptions (but see note 7 in <i>COB 6.7.18R</i>) which can be invested only in <i>units</i> held within a <i>non-stakeholder CTF</i></u></p>



	<u>(other than a contract contained in D) in an <i>AUT</i>, <i>recognised scheme</i> or <i>ICVC</i> purchased from a <i>CTF provider</i>, where advice is given.</u>
	...
Row 2	There is no right to cancel where any one or more of the following cases applies:
	...
	6. The contract is entered into under a <i>customer agreement</i> or during negotiations (which are not <i>ISA</i> , <del><i>or PEP</i></del> or <i>CTF</i> related) intended to lead to a <i>client agreement</i> (unless note 4 or note 5 in <i>COB 6.7.18R</i> applies);
	...
	8. The contract relates to an <i>EIS</i> or non-packaged product <i>ISA</i> , <del><i>or PEP</i></del> or <i>CTF</i> and is entered into, following <i>advice on investments</i> , and following an explanation that neither of the rights specified in case 7 will apply, given to the <i>customer</i> in accordance with <i>COB 3.9.21R</i> or <i>COB 4 Ann 2E(9)(a)</i> in a <i>direct offer financial promotion</i> , <i>terms of business</i> , or given in <i>EIS particulars</i> (but see note 5 in <i>COB 6.7.18R</i> );
	...

6.7.18R

...
<u>6. In the case of contracts held within <i>CTFs</i>, the initial service agreement is cancellable in all cases.</u>
<u>7. Cancellation rights exist only where the <i>registered contact</i> has received advice. In cases in which cancellation rights apply, they are the same as the cancellation rights that would apply to the underlying <i>units</i> if they were not held within a <i>CTF</i>.</u>
<u>8. In relation to <i>Revenue allocated accounts</i>, the <i>firm</i> must not accept any additional contributions until the cancellation period has expired without the right to cancel being exercised.</u>

...

6.7.23R

- ...
- (2) Paragraph (1) does not apply if:
- ...
- (b) ...; or
- (c) the variation is in respect of a *life policy* held within a *CTF*.
- ...

...

6.7.30R Other than for *distance contracts* and *cash deposit ISAs* and *CTFs* that are not *distance contracts*, where there is a right to cancel, the *firm* which enters into the contract with the *customer* must send the *customer*, in writing, a clear and prominent reminder notice of this right:

(1) ...

...

6.7.52R Unless the agreement relates to a CTF, when a retail customer exercises a right to cancel under COB 6.7.7R (1), (2), (3) or (4):

...

6.7.52AR (1) When a person exercises a right to cancel a contract in connection with a CTF that has been opened, the CTF provider must ensure that:

(a) where the CTF provider and the firm that provides the underlying investment are different persons, any money that was held by the firm that provides the underlying investment in connection with the CTF is returned to the CTF provider as soon as reasonably practicable;

(b) any sums which any person has paid to or for the benefit of any firm in connection with the CTF continue to be held in a CTF bank account until the CTF provider receives further instructions regarding the investment of those sums in accordance with the CTF Regulations;

(c) where a CTF provider holds sums in accordance with COB 6.7.52AR, the CTF provider notifies the private customer in writing as soon as reasonably practicable, stating that the money is held awaiting re-investment instructions; and

(d) if the CTF bank account is non-interest bearing, the registered contact is informed of that fact as soon as possible after the money has been deposited in the account.

(2) When a person exercises a right to cancel a contract in connection with a CTF that has not been opened and the CTF provider holds money awaiting instructions, the CTF provider must comply with the requirements of COB 6.7.52AR(1)(b), (c) and (d).

6.7.52BG Where cancellation rights are exercisable by a customer in relation to a CTF, the CTF provider will need permission to hold client money to be able to deal with the money from the cancelled contract unless they can take advantage of any exemption from the client money rules.

...

8.1.6R A *firm* need not despatch a confirmation when:

...

- (1A) the *designated investment* is held within a *CTF* and the annual statement provided under the *CTF Regulations* includes the information that would have been contained in a confirmation despatched in accordance with *COB* 8.1.3R relating to the transactions executed during the relevant period (but information which has since become irrelevant may be excluded); or

...

...

8.2.6R A *firm* need not:

...

- (2) ...; or
- (3) provide a *periodic statement* in respect of a *CTF* if the annual statement provided under the *CTF Regulations* contains the information that would be required to comply with *COB* 8.2.4R

8.2.6AG If *COB* 8.2.6R (3) applies, *COB* 8.2.10E provides an indication of how the requirement in *COB* 8.2.4R may be satisfied. Further *guidance* that is relevant if the *CTF* includes a discretionary managed portfolio or a *structured capital-at-risk product* is contained in *COB* 8.2.12R and *COB* 8.2.17E.

...

## Annex D

### Amendments to the Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.1.4R Table            Activities to which TC 2 applies

	Activity	Extent of Application
...		
2. <i>Employees</i> overseeing on a day-to-day basis:	...	Whole of <i>TC 2</i> applies except <i>TC 2.7</i> (Supervising).
	(c) the following <i>administrative functions</i> in relation to <i>managing investments</i> :	
	...	
	(iv) <i>ISA</i> , <del>or</del> <i>PEP</i> or <i>CTF</i> administration;	

## Annex E

### Amendments to the Supervision manual

In this Annex, underlining indicates new text.

#### CTF providers

- 15.8.8R
- (1) If a firm begins or ceases to hold itself out as acting as a CTF provider, it must notify the FSA as soon as reasonably practicable that it has done so.
- (2) A firm that acts as a CTF provider must provide the FSA, as soon as reasonably practicable, with details of:
- (a) any third party administrator that it engages;
- (b) details of whether it intends to offer Revenue allocated CTFs; and
- (c) whether it intends to provide its own stakeholder CTF account.

In SUP Schedule 2: Notification Requirements, insert the following:

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...	...	...	...	...
<u>SUP 15.8.8R</u>	<u>CTF provider status</u>	<u>The fact of the firm beginning or ceasing to hold itself out as a CTF provider</u>	<u>Firm beginning or ceasing to hold itself out as a CTF provider</u>	<u>As soon as reasonably practicable</u>
	<u>CTF third party administrator</u>	<u>Engagement of third party administrator</u>	<u>Thirds party administrator engaged</u>	<u>As soon as reasonably practicable</u>
	<u>Intention to offer Revenue allocated CTFs</u>	<u>Whether it intends to offer Revenue allocated CTFs</u>	<u>Becoming a CTF provider</u>	<u>As soon as reasonably practicable</u>
	<u>Intention to provide stakeholder CTF</u>	<u>Whether it intends to provide its own stakeholder CTFs</u>	<u>Becoming a CTF provider</u>	<u>As soon as reasonably practicable</u>
...				

## Annex F

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 3.7.3G (1) ...
- (2) As a result, applicants will be asked to specify as part of their application whether or not they wish to carry on business activities that include:
- ...
- (b) ~~ISA, or PEP or CTF~~ management (including, in the case of CTF management, details of any third party administrator that it engages and with details of whether it intends to offer Revenue allocated CTFs and whether it intends to provide its own stakeholder CTF); or
- ...

## Annex G

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Transitional provisions

##### 1. Table Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1	...				
5	<i>CRED</i> 7A.3.1R and 7A.3.1AG	R	<i>CRED</i> 7A.3.1R and 7A.3.1AG shall have no effect unless and until any amendment to the <i>CTF Regulations</i> is made to allow a <i>credit union</i> to provide <i>cash deposit CTFs</i> .	1 December 2004	1 December 2004

...

1.1.2G *CRED* does not encompass the requirements associated with any regulatory *permission* other than a *Part IV permission to accept deposits*. There are also additional requirements in the Handbook for credit unions that are CTF providers in relation to cash-deposit CTFs. Other *permissions* are covered elsewhere in the *Handbook*. Thus, for example, a *credit union* seeking a *permission* to undertake a *regulated mortgage activity* would need to comply with the requirements in *MCOB* and a *credit union* seeking a *permission* to undertake *insurance mediation activity* in relation to *non-investment insurance contracts* would need to comply with the requirements in *ICOB*.

...

#### 7A.3 Deposits

- 7A.3.1R (1) ...
- (2) A *credit union* must not accept *deposits* exceeding the greater of £5,000 and 1.5 per cent of the total shareholdings in the *credit union* from a person who is under the age at which, under section 20 of the Industrial and Provident Societies Act 1965, he may become a member

of the *credit union* unless the *deposits* are held in a *CTF*, in which case the *credit union* may accept a larger *deposit*.

7A3.1A G *Credit unions* that provide *CTFs* should ensure that under their rules depositors under the age of 18 whose *deposits* are held within a *CTF* continue to be treated as juvenile depositors until the age of 18. This will provide for the fact that *CTF* account holders may not withdraw any money from the *CTF* until they reach the age of 18 in contrast to the position in relation to other *deposits* which become shares and may be withdrawn earlier.

...

CTF providers

11.1.7G A *credit union* which acts as a *CTF provider* needs to be aware of the requirements relating to *CTFs* in *COB*, in particular *COB* Chapters 3,4,5,6 and 8, *SUP* 15 and, where relevant, *IPRU(INV)* Chapter 8 and *PRU* 9.

...

11.4.9G The effects of cancellation are set out in *COB* 6.7.51R to *COB* 6.7.52AR. Unless the contract relates to a *CTF*, the *credit union* has to return, ...



## Annex H

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

Insert or amend the following definitions in the appropriate alphabetical position:

<i>administrative functions</i>	(a) (in relation to <i>managing investments</i> ): ... (iv) <del>ISA</del> , <del>or PEP</del> <u>or CTF</u> administration; ...
<i>adopted packaged product</i>	(in relation to a <i>firm</i> ) a <i>stakeholder pension scheme</i> <u>or a CTF</u> which is a <i>packaged product</i> :  (a) not produced by the <i>firm</i> or in the <i>firm's marketing group</i> , but by another producer (whether a <i>firm</i> or not); and  (b) on which the <i>firm</i> is able to advise as a result of a decision taken under <i>COB 5.1.4R(1)</i> .
<u><i>cash deposit CTF</i></u>	<u>a <i>deposit</i> account held within a <i>CTF</i>.</u>
<u><i>CTF</i></u>	<u>(as defined in section 1(2) of the Child Trust Funds Act 2004) a child trust fund, that is, an account which:</u>  (1) <u>is held by a child who is or has been an eligible child (as defined in section 2 of that Act);</u>  (2) <u>satisfies the requirements imposed by or under the Child Trust Funds Act 2004; and</u>  (3) <u>has been opened in accordance with the Child Trust Funds Act 2004.</u>
<u><i>CTF bank account</i></u>	<u>a bank account which fulfils the requirements of Regulation 11(5) of the <i>CTF Regulations</i>.</u>
<u><i>CTF provider</i></u>	<u>(in accordance with section 3(1) of the Child Trust Funds Act 2004) a <i>person</i> approved by the Inland Revenue in accordance with the <i>CTF Regulations</i>.</u>
<u><i>CTF Regulations</i></u>	<u>the Child Trust Funds Regulations 2004 (SI 2004/1450), as amended.</u>

<u>CTF transfer</u>	a transaction resulting from a decision by a <i>customer</i> , made with or without advice from a <i>firm</i> , to transfer the <i>investments</i> (or their value) held in an existing <i>CTF</i> into another <i>CTF</i> whether or not provided by the same <i>CTF provider</i> .
<u>non-stakeholder CTF</u>	a <i>CTF</i> that is not a <i>stakeholder CTF</i> .
<u>own funds</u>	...  (3) <u>(in IPRU(INV) Chapter 8) capital, as defined in CRED 8.2.1R.</u>
<u>packaged product</u>	(a) a <i>life policy</i> ;  (b) a <i>unit</i> in a <i>regulated collective investment scheme</i> ;  (c) an interest in an <i>investment trust savings scheme</i> ;  (d) a <i>stakeholder pension scheme</i> ;  whether or not (in the case of (a),(b) or (c)) held within a <i>PEP</i> , or an <i>ISA</i> or a <i>CTF</i> .
<u>parental responsibility</u>	<u>(as defined in section 3(9) of the Child Trust Fund Act 2004):</u>  (a) <u>parental responsibility within the meaning of the Children Act 1989 or the Children (Northern Ireland) Order 1995 (SI 1995/755 (N.I. 2)); or</u>  (b) <u>parental responsibilities within the meaning of the Children (Scotland) Act 1995.</u>
<u>private customer</u>	(1) (except in COB 3, 4.2 and 6.4) <u>subject to (h), a client who is not a market counterparty or an intermediate customer, including:</u>  ...  (e) <u>where the regulated activity (except for a personal recommendation relating to a contribution to a CTF) relates to a CTF and there is a registered contact, the registered contact;</u>  (f) <u>(in COB 6.1 to 6.5) where the regulated activity (except for a personal recommendation relating to a contribution to a CTF) relates to a CTF and there is no registered contact, the person to whom the annual statement must be sent in accordance with Regulation 10 of the CTF Regulations;</u>

- (g) (in COB 6.7) where the regulated activity (except for a personal recommendation relating to a contribution to a CTF) relates to a CTF and there is no registered contact, the child, via the person to whom the annual statement must be sent in accordance with Regulation 10 of the CTF Regulations;
- (h) a client who would otherwise be excluded as a market counterparty or intermediate customer if the client is within (e), (f) or (g);

but excluding a *client*, who would otherwise be a *private customer*;

- (i) when he is classified as an intermediate customer in accordance with COB 4.1.9R (Expert private customer classified as an intermediate customer); or
  - (ii) when the regulated activity relates to a CTF, any person other than (e), (f), (g) or (h).
- (2) (in COB 3) a person in (1) or a person excluded under (1)(h)(ii) or a person who would be such a person if he were a client.

...

registered contact

(as defined in regulation 8(1)(d) of the CTF Regulations) the person who is capable of giving instructions to the CTF provider with respect to the management of the CTF.

responsible person

(as defined in section 3(8) of the Child Trust Funds Act 2004) a person with parental responsibility in relation to a child under 16 who is not:

- (a) a local authority or, in Northern Ireland, an authority within the meaning of the Children (Northern Ireland) Order 1995 (SI 1995/755 (NI 2)); or
- (b) a person under 16.

Revenue allocated CTF

a CTF opened in accordance with Regulation 6 of the CTF Regulations.

stakeholder CTF

a CTF that has the characteristics, and complies with the conditions, set out in paragraph 2 of the Schedule to the CTF Regulations.

**DEPOLARISATION INSTRUMENT 2004****Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 145 (Financial promotion rules);
  - (3) section 149 (Evidential provisions);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) Annexes A to F, H and J to L come into force on 1 December 2004, other than the provisions specified in (2);
  - (2) the following provisions in Annex B come into force on 14 January 2005: COB 4.3.19R to 4.3.26R; COB 5.2.12R to 5.2.17G; and COB 5.3.18AR to 5.3.18DG;
  - (3) Annexes G and I come into force on 14 January 2005.
- D. The transitional rules operate so that a firm:
- (1) must, if applicable, comply with the provisions in this instrument that implement the Insurance Mediation Directive from 14 January 2005;
  - (2) must comply with the Handbook as otherwise amended by this instrument, from 1 June 2005; and
  - (3) may elect to comply with the Handbook as amended by this instrument, other than the provisions which implement the Insurance Mediation Directive, at any time during the period 1 December 2004 to 31 May 2005.

**Amendments to the Handbook**

- E. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with Annexes to this instrument listed in column (2) below:

(1)	(2)
General provisions (GEN)	Annex A
Conduct of Business sourcebook (COB)	Annex B
Insurance: Conduct of Business sourcebook (ICOB)	Annex C
Mortgages: Conduct of Business sourcebook (MCOB)	Annex D
Client Assets (CASS)	Annex E
Training and Competence sourcebook (TC)	Annex F
Authorisation manual (AUTH)	Annex G
Supervision manual (SUP)	Annex H
Dispute Resolution: Complaints (DISP)	Annex I
Credit Unions sourcebook (CRED)	Annex J
Professional Firms sourcebook (PROF)	Annex K
Glossary of definitions	Annex L

## Citation

F. This instrument may be cited as the Depolarisation Instrument 2004.

By order of the Board

18 November 2004

Amended by Addendum

9 December 2004

Amended by Second Addendum

18 August 2005

## Annex A

### Amendments to General Provisions

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Chapter 5 The FSA logo and the keyfacts logo

##### Application

- 5.1.1 G This chapter contains:
- (a) *guidance for firms and appointed representatives on the circumstances in which the FSA permits firms and their appointed representatives to reproduce the FSA logo;*
  - (b) rules on the use by firms of the keyfacts logo.

...

- 5.1.4 G ...

##### The keyfacts logo

- 5.1.5 R A firm must not use the keyfacts logo other than as and when it is required to be used by the rules.
- 5.1.6 R A firm must take all reasonable steps to ensure that its representatives do not use the keyfacts logo other than as and when the logo is required to be used by the rules.
- 5.1.7 R A firm must take all reasonable steps to ensure that the keyfacts logo is not reproduced on any document that the firm, or any person acting on its behalf, provides to a customer unless the reproduction is required by the rules.

## Annex B

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire section is deleted or inserted, the place where the change is made is indicated and the text is not struck through or underlined.

COB TR1, Transitional Rules for pre-N2 and ex Section 43 firms

...

Table: COB TR 1

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1.0	Extra time provisions				
1.1	<i>ETP1</i>	R	Transitional relief		
			(1) A <i>pre-N2 firm</i> will not contravene any of the provisions labelled <i>ETP1</i> in Table <i>COB TR2</i> ...	(1) <i>commencement</i> to 30 June 2002...  (3) for <i>COB</i> 3.9.10R, <del><i>COB</i> 4.2.15E(7)</del> ; <del><i>COB</i> 5.3</del> , <del><i>COB</i> 5.7</del> , <i>COB</i> 6.1 to 6.8 until a date yet to be specified	<i>commencement</i>

Insert new *COB TR7* as follows:

*COB TR7*: Transitional Rules for depolarisation

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
1.	<i>COB</i>	R	From 1 December 2004 to 31 May 2005, a <i>firm</i> may, subject to TR 7.6, comply with <i>COB</i> as if it were not amended by the	From 1 December 2004 to 31 May 2005.	1 December 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			Depolarisation Instrument 2004, unless the <i>firm</i> is a <i>product provider</i> in which case it must comply with <i>COB 2.2.7G (7A)</i> , as it applies to a <i>product provider</i> , from 1 December 2004.		
2.	<i>COB rules</i> amended by the Depolarisation Instrument 2004	R	<p>(1) Subject to <i>COB TR7.1</i> and <i>TR7.6</i>, the Depolarisation Instrument 2004 may apply to a <i>firm</i> as follows.</p> <p>(2) A <i>firm</i> may elect at any time from 1 December 2004 to 31 May 2005, to comply with <i>COB</i> as amended by the Depolarisation Instrument 2004.</p> <p>(3) A <i>firm</i> must notify the <i>FSA</i> in writing of an election in (2) and of the date prior to 31 May 2005 from which it will commence compliance with <i>COB</i> as amended by the Depolarisation Instrument 2004.</p> <p>(4) A <i>firm</i> may make different elections in (2) for each <i>appointed representative</i> that acts on its behalf but can only make a single election in respect of each single <i>appointed representative</i>.</p>	From 1 December 2004 to 31 May 2005.	1 December 2004



(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
3	<i>COB rules</i> amended by the Depolarisation Instrument 2004	R	A <i>firm</i> must, in relation to any <i>private customer</i> to whom it has begun to provide services in respect of a <i>packaged product</i> before 14 January 2005 or, if applicable, the date of an election in TR7 2(2), complete the provision of that service in accordance with <i>COB</i> as it applied before amendment by the Depolarisation Instrument 2004.	From 1 December 2004	1 December 2004
4	<i>COB 4 Annex 2E</i> and <i>COB 5.5.5E</i>	R	A <i>firm</i> may continue to rely upon compliance with <i>COB 4 Annex 2E</i> and <i>COB 5.5.5E</i> (including to the extent that a <i>firm</i> issues a <i>financial promotion</i> that complies with <i>COB 4 Annex 2E</i> ) provided:  (1) the information given to a <i>private customer</i> is not contradicted by any information given to the <i>customer</i> by way of an <i>initial disclosure document</i> or a <i>fees and commission statement</i> and;  (2) any <i>financial promotion</i> complies with <i>COB 3.8.19R</i> .	From 1 December 2004 until 30 November 2005	1 December 2004
5	<i>COB 2.2.6</i>	G	The <i>FSA</i> will not regard a <i>firm</i> as being in contravention of <i>COB 2.2.3R</i> if it gives or receives assistance in conducting the review of past business in <i>pension transfers</i> and <i>opt outs</i> provided the provision or receipt of such a benefit does not conflict with any duty the recipient owes to its <i>customers</i> .	From 1 December 2004 to 31 May 2006	1 December 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
6	COB as amended by the Depolarisation Instrument 2004	R	<p>Notwithstanding COB TR7.1 and TR 7.2, a <i>firm</i> which does not elect under TR 7.2(2) to comply with COB as amended by the Depolarisation Instrument 2004 must, from 14 January 2005, comply with:</p> <p>(1) COB 1.2.1R, COB 1.4.12R and COB 4.3.19R to 4.3.26R, as amended by the Depolarisation Instrument 2004;</p> <p>(2) COB 4.3.19R to COB 4.3.25R as amended by the Depolarisation Instrument 2004 but as if they applied to a <i>firm</i> carrying out the activities in COB 4.3.19R (1)(a)-(c) with or on behalf of <i>private customers</i>;</p> <p>(3) COB 5.2.12R to 5.2.14R as amended by the Depolarisation Instrument 2004; and</p> <p>(4) COB 5.3.14R (1) and COB 5.3.18AR to COB 5.3.18CR, as amended by the Depolarisation Instrument 2004;</p> <p>unless the <i>firm</i> is an <i>insurer</i>, in which case it does not need to comply with the provisions specified in (2), (3) and (4).</p>	14 January 2005 until 31 May 2005	14 January 2005
7		G	<p>The effect of COB TR 7.6 is that from 14 January 2005, if a <i>firm</i> has not elected to comply with the new COB provisions, the <i>firm</i> is in any event required to comply with the requirements of the IMD as set out in the provisions referred to in COB TR 7.6.</p>		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			As regards the information requirements of the <i>IMD</i> , <i>firms</i> have the choice (by virtue of <i>COB</i> 4.3.23G) of providing the minimum information set out in <i>COB</i> 4.3.19R or using an <i>initial disclosure document</i> .		

...

1.2.1 R ...

- (3) ...; ~~and~~
- (4) *COB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities*, except for:
  - (a) ...
  - (b) ...
  - (c) ...; and
  - (d) the *IMD* minimum implementation provisions and *COB* 4.3.19R to 4.3.25R as if they also applied to a *firm* carrying out the activities in *COB* 4.3.19R (1)(a)-(c) with or on behalf of *private customers*, unless:
    - (i) the *designated professional body* of the *firm* has made rules which implement some or all of the provisions of articles 12 and 13 of the *IMD*;
    - (ii) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and
    - (iii) the *firm* is subject to the rules in the form in which they were approved;

in which case they are disappplied to the extent that articles 12 and 13 of the *IMD* are implemented by the rules of the *designated professional body*.

...

1.2.1B G The effect of *COB* 1.2.1R(4)(d) is that if the relevant *designated professional body* of an *authorised professional firm* does not make rules implementing articles 12 and 13 of the *IMD* applicable to *authorised professional firms*, those *firms* will need to comply with:

- (a) the IMD minimum implementation provisions; and
- (b) COB 4.3.19R to COB 4.3.25R as if they also applied to a firm carrying out the activities in COB 4.3.19R (1)(a)-(c) with or on behalf of private customers.

1.3.3 G (1) The application of many provisions in COB depends on the classification of the client with whom a firm is conducting business. A client must fall within one of three classifications: private customer, intermediate customer or market counterparty. In COB, the term "customer" refers to private customers and intermediate customers, but not market counterparties. The term "client" covers customers and market counterparties. Where relevant, each of the provisions of COB makes clear whether it applies to activities carried on with or for private customers, intermediate customers or both.

...

...

1.3.5\*\* G Firms are reminded that the definition of *inter-professional business* does not include:

- (1) ...
- (3) ...; ~~or~~
- (4) ...; or
- (5) regulated activities relating to life policies.

...

IMD passported activities

1.4.12R R (1) Notwithstanding COB 1.4.2R, the IMD minimum implementation provisions apply, on the basis outlined in (4), to the passported activities carried on by a UK firm under the IMD from a branch elsewhere in the EEA unless the Host State regulator imposes measures which implement articles 12 and 13 of the IMD for those activities.

(2) Notwithstanding COB 1.4.2R, the provisions in COB which implement articles 12 and 13 of the IMD (including COB 4.3.3R (1)(i) and (ii) (provision of initial disclosure document and fees and commission statement)) do not apply to a UK firm providing cross-border services in another EEA State under the IMD or the Consolidated Life Directive, except that the IMD minimum implementation provisions apply, on the basis outlined in (4), to a UK firm providing cross-border services in another EEA State under the IMD if the Host State regulator does not impose measures which implement the articles for those activities.

(3) In addition to the situation in COB 1.4.3R, the IMD minimum implementation provisions apply to an incoming EEA firm providing cross-border services in the United Kingdom under the IMD unless the firm's Home State regulator imposes measures which implement the articles for these activities.

(4) The IMD minimum implementation provisions apply to an activity pursuant to this rule as follows:

- (a) as outlined in the IMD minimum implementation provisions; and

\*\*See Second Addendum 18 August 2005 p.171

(b) as if COB 4.3.19R to 4.3.25R also applied to a firm carrying out the activities in COB 4.3.19R (1)(a)-(c) with or on behalf of private customers.

- 1.4.13 G (1) The IMD minimum implementation provisions are the minimum provisions required for the implementation of articles 12 and 13 of the IMD.
- (2) The effect of COB 1.4.12R is to apply these minimum provisions to firms in respect of their insurance mediation activities passported under the IMD if other EEA States have not implemented articles 12 and 13 of the IMD for those activities.
- (3) Firms are reminded that insurers have passporting rights under the Consolidated Life Directive but not under the IMD.

Restriction in connection with the sale of packaged products

- 2.2.5 E (1) A firm should not enter, and should take reasonable steps to ensure that no person acting on its behalf enters, into any of the following arrangements with ~~an independent intermediary~~ another firm in relation to the sale of a packaged product if any commission is required to be disclosed to a customer.
- ...
- (d) an arrangement to pay *commission* other than to the *firm* responsible for the sale, unless:
- (i) the *firm* responsible for the sale has passed on its right to receive the *commission* to the recipient; or
- (ii) another *firm* has given *advice on investments* to the same *customer* after the sale; or
- (iii) ~~the firm is a provider firm, the recipient is an independent intermediary and~~ the *commission* is paid following the sale of a *packaged product* by the ~~provider~~ *firm* in response to a *direct offer financial promotion* communicated by that *firm* to a *customer* of the ~~independent intermediary~~ *recipient firm*.
- (1A) COB 2.2.5 E (1) does not apply to arrangements between *firms* that are in the same *immediate group*. In this situation COB 5.7.5R will apply.

...

Financial assistance and product providers

- 2.2.5A\*\* E (1) This evidential provision applies in relation to a holding in, or the provision of credit to, a firm which holds itself out as giving advice on investments to private customers on packaged products except where the relevant transaction is between persons who are in the same immediate group.
- (2) A product provider should not take any step which would result in it:
- (a) having a direct or indirect holding in a firm in (1) of its capital or voting power; or
- (b) providing credit to a firm in (1) (other than commission due from the firm to the product provider in accordance with an indemnity commission clawback arrangement).
- (3) A firm in (1) should not take any step which would result in a product provider having a holding as in (2)(a) or providing credit as in (2)(b), unless

all the conditions in (4) are satisfied.

- (4) The conditions referred to in (3) are that:
- (a) the holding is acquired, or credit is provided, on commercial terms; that is terms objectively comparable to those on which an independent person unconnected to a product provider would, taking into account all relevant circumstances, be willing to acquire the holding or provide credit;
  - (b) the firm (or, if applicable, each of the firms) taking the step has reliable written evidence that (a) is satisfied;
  - (c) there are no arrangements, in connection with the holding or credit, relating to the channelling of business from the firm in (1) to the product provider; and
  - (d) the product provider is not able, and none of its associates is able, because of the holding or credit, to exercise any influence over the advice on investments in relation to packaged products given by the firm.
- (5) In this evidential provision, in applying (2) and (3) any holding of, or credit provided by, a product provider's associate is to be regarded as held by, or provided by, that product provider.
- (6) In this evidential provision, in applying (3) references to a "product provider" are to be taken as including an unauthorised equivalent of a product provider; that is, an unauthorised insurance undertaking or an unauthorised operator of a regulated collective investment scheme or of an investment trust savings scheme.
- (7) Contravention of (2) or (3) may be relied upon as tending to establish contravention of COB 2.2.3R.

Packaged products: guidance on indirect benefits

- 2.2.6 G (-2) To comply with COB 2.2.3R, neither a product provider nor any of its associates should give, and a firm should not receive from such persons, any indirect benefit, if the benefit is likely to conflict to a material extent with any duty owed by the receiving firm when giving advice on investments to private customers on packaged products. Such conflicts may arise, for example, where the gift might induce material bias as regards:
- (a) the choice of product provider whose products are recommended; or
  - (b) the type of product which is recommended.
- (-1) The guidance in COB 2.2.7 G is not relevant to indirect benefits which may be given by a product provider or its associate to its own representatives.
- (1) The FSA will not regard a firm as being in contravention of COB 2.2.3R if it gives or receives gifts, hospitality and promotional competition prizes of a reasonable value any of the following indirect benefits, providing they do not conflict with the duties that the recipient owes to his its customers.
- (a) gifts, hospitality and promotional competition prizes of a reasonable value;
  - (b) business leads channelled toward a particular independent intermediary provided that the independent intermediary is an

~~associate and complies with the requirements of COB 5.3.95R (Requirement for suitability: independent intermediary);~~

(e) ~~assistance in conducting the Review of past business in pension transfers and opt outs.~~

(2) A ~~product provider~~ may assist ~~an independent intermediary~~ another firm to promote its packaged products so that the quality of ~~their~~its service to customers is enhanced. Such assistance should not be of a kind or value that is likely to impair ~~an independent intermediary's~~ the other firm's ability to ~~act independently~~ pay due regard to the interests of its customers, and to give advice on, and recommend, packaged products available from the ~~market as a whole~~ recipient firm's whole range or ranges of packaged products. The ~~independent intermediary~~ recipient firm should be mindful of the requirements of COB 5.3.95R (Requirement for suitability: independent intermediaries generally).

...

(4) COB 2.2.6G does not apply to indirect benefits provided by a firm to another firm that is in the same immediate group. In this situation COB 5.7.5R will apply.

2.2.7 G Table Reasonable indirect benefits

This Table belongs to COB 2.2.6G

Reasonable indirect benefits	
	Joint marketing exercises
1	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may provide generic product literature (that is, letterheading, leaflets, forms and envelopes) that is suitable for use and distribution by or on behalf of <del>an independent intermediary</del> <u>another firm</u> if:
	(a) the literature does not feature the <del>independent intermediary's</del> <u>recipient firm's</u> name or features it less prominently than that of the <u>product provider firm</u> and is not used to promote the <del>independent intermediary's</del> <u>recipient firm's broker fund</u> service; and
	(b) the total costs (for example, packaging, posting, mailing lists) of distributing such literature to its <u>customers</u> <del>is</del> are borne by the <del>independent intermediary</del> <u>recipient firm</u> .
2	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may supply <del>an independent intermediary</del> <u>another firm</u> with 'freepost' envelopes, for forwarding such items as completed applications, medical reports or copy <u>client agreements</u> , when these are made generally available to all <del>independent intermediaries</del> <u>firms</u> from <del>which</del> <u>whom</u> the <u>provider</u> obtains business.
3	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may supply product specific literature (for example, <u>key features</u> , minimum information, <u>direct offer financial promotions</u> ) to <del>an independent intermediary</del> <u>another firm</u> if:
	(a) the literature is not designed to promote the <del>independent intermediary's</del> <u>recipient firm's broker fund</u> service; or
	(b) the literature does not contain the name of any <del>independent</del>

		<i>intermediary</i> <u>other firm</u> ; or-
	(e)	the name of the <i>independent intermediary</i> <u>other firm</u> is only overprinted on the literature and the <i>provider firm's</i> name appears on the literature more prominently than that of the <i>independent intermediary</i> <u>other firm</u> .
	(c)	the name of the recipient <i>firm</i> (if it is included) appears only incidentally in the literature and the supplying <i>firm's</i> name appears with greater prominence.
4	A <del>provider firm</del> <u>product provider</u> or its <i>associate</i> may supply draft articles, news items and <i>financial promotions</i> for publication in an <i>independent intermediary's</i> <u>another firm's</u> magazine, only if in each case any costs paid by the <i>product provider</i> or its <i>associate</i> for placing the articles and <i>financial promotions</i> are not more than market rate, and exclude distribution costs.	
	Seminars and conferences	
5	A <del>provider firm</del> <u>product provider</u> or its <i>associate</i> may take part in a seminar organised by an <i>independent intermediary</i> <u>another firm</u> or a third party and may pay toward the cost of the seminar, if:	
	(a)	its participation is for a genuine business purpose;
	(b)	the contribution is reasonable and proportionate to its participation and by reference to the time and sessions at the seminar when its staff play an active role; and
	(c)	in the case of a seminar organised by a third party, the seminar is open to participation by <i>independent intermediaries</i> <u>other firms</u> generally.
	Technical services and information	
6	A <del>provider firm</del> <u>product provider</u> or its <i>associate</i> may supply a 'freephone' link to which it is connected only if it is available to <i>independent intermediaries</i> <u>other firms</u> generally.	
7	A <del>provider firm</del> <u>product provider</u> or its <i>associate</i> may supply an <i>independent intermediary</i> <u>another firm</u> with any of the following:	
	(a)	quotations and <i>projections</i> relating to its <i>packaged products</i> and, in relation to specific <i>investment</i> transactions (or for the purpose of any scheme for review of past business), advice on the completion of forms or other <i>documents</i> ;
	(b)	access to data processing facilities, or access to data, that is related to the <i>product provider's firm's</i> business;
	(c)	access to third party electronic dealing or quotation systems that are related to the <i>provider firm's product provider's</i> business; and
	(d)	software that gives information about the <i>product provider's firm's packaged products</i> or which is appropriate to its business (for example, for use in a scheme for review of past business or for producing <i>projections</i> or technical product information).
7A	A <u>product provider</u> may pay cash amounts or give other assistance to a <i>firm</i> not in the same <i>immediate group</i> for the development of software or other computer facilities necessary to operate software supplied by the <i>product</i>	



	<u>provider</u> , but only to the extent that by doing so it will generate equivalent cost savings to itself or consumers.
8	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may supply a <u>broker fund adviser</u> (and its <u>customer</u> ) with a <u>periodic statement</u> relating to the relevant <u>broker fund</u> if the <u>broker fund adviser</u> is unable to supply the <u>periodic statement</u> .
9	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may supply <del>an</del> <u>independent intermediary</u> <u>another firm</u> with information about sources of mortgage finance.
10	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may supply <del>an</del> <u>independent intermediary</u> <u>another firm</u> with generic technical information in writing, not necessarily related to the <u>product provider's firm's</u> business, when this information:
	(a) is made available generally to <del>independent intermediaries</del> <u>other firms which give or might give advice on the product provider's packaged products</u> ; or
	(b) (i) is of a specialist nature and is made available to a particular class of <del>independent intermediary</del> <u>firm</u> (that is, one that promotes itself as an expert in the same specialist area); and
	(i) states clearly and prominently that it is produced by the <u>product provider</u> or (if different) <u>supplying firm</u> .
	Training
11	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may provide <del>an</del> <u>independent intermediary</u> <u>another firm</u> with training facilities of any kind (for example, lectures, venue, written material and software) only if these are made available generally to all <del>independent intermediaries</del> <u>other firms which give or might give advice on the product provider's packaged products</u> .
	Travel and accommodation expenses
12	A <del>provider firm</del> <u>product provider</u> or its <u>associate</u> may reimburse an <del>independent intermediary's</del> <u>other firm's</u> reasonable travel and accommodation expenses when the <del>independent intermediary</del> <u>other firm</u> :
	(a) participates in market research conducted by or for the <u>product provider firm</u> ;
	(b) attends an annual national event of a <u>UK trade association</u> , hosted or co-hosted by the <u>product provider firm</u> ;
	(c) participates in the <u>product provider's firm's</u> training facilities (see 11);
	(d) visits the <u>product provider's firm's</u> <u>UK office</u> in order to:
	(i) receive information about the <u>product provider's firm's</u> administrative systems; or
	(ii) attend a meeting with the <u>product provider firm</u> and an existing or prospective <u>customer</u> of the <del>independent intermediary</del> <u>receiving firm</u> .

...

2.2.20 R ...  
(3) A firm must make a record of each benefit given to ~~an independent intermediary~~ another firm in accordance with COB 2.2.6G, and must keep that record for at least six years from the date on which it was given.

...

3.2.2 G ...  
(2) *Financial promotions* may be communicated, for example, by means of:  
...  
(e) written correspondence, telephone calls and face to face discussions including by ~~advisers~~ representatives;

...

...

3.2.8 G ...  
(2) Firms are reminded that if in the course of making a *financial promotion* of any kind ~~an adviser (independent or tied)~~ a representative gives specific *advice on investments* to a *private customer* about the suitability of a product for that individual, the ~~adviser~~ representative in giving the ~~advice~~ *advice on investments* is subject to the rules, as appropriate, on advising and selling in *COB 5*.

...

3.7.3 G ...  
(2) Records which should be retained include:  
(a) any written *financial promotion* used by a ~~financial adviser or representative~~;

...

...

Specific non-real time financial promotions: ~~provider firms~~ packaged products

Delete the existing *COB 3.8.19R rule* and replace with the following text which is not underlined:

3.8.19 R (1) A firm must not *communicate* or *approve* a *specific non-real time financial promotion* containing or offering *advice on investments* on *packaged products* unless the *promotion* discloses information to show whether the scope of the *advice on investments* which is given or offered is or will be based upon a selection of products from:  
(a) the whole market (or from the whole of a named sector of the market); or  
(b) a limited number of *product providers*; or  
(c) a single *product provider*.  
(2) A firm must not *communicate* or *approve* a *specific non-real time financial promotion* offering *packaged products* produced by a person, A:  
(a) that holds out any *person* other than A as the *packaged product's* producer; or

- (b) that does or says anything which might reasonably lead a *private customer* to be mistaken as to the identity of the product's producer; or
- (c) in which the prominence of A's brand is less than that of other brands included in the promotion.

...  
3.8.22 R ...

- (7) ~~If applicable, acts in conformity with the rules in COB 4.3 (Disclosing information about services, fees and commission - packaged products) and COB 5.1 (Advising on packaged products), concerning polarisation and status disclosure.~~

...  
3.8.24 G

- The requirements of COB 3.8.22R:
- (1) apply in respect of all individuals who initiate the communication, including ~~advisers~~ representatives, call centre operators and *introducers*.

...  
3.9.6 R

- (1) ...
- (2) In particular a *direct offer financial promotion* must contain:
  - (a) ...
  - (b) where it is the case that no advice on investments has been given, a prominent statement that: ~~if a person has any doubt about the suitability of the agreement which is the subject of the financial promotion, he should contact the firm which has communicated or approved the financial promotion for advice (or independent financial adviser, if the firm does not offer advice).~~
    - (i) no advice on investments has been given; and
    - (ii) if a person has any doubt about the suitability of the agreement which is the subject of the financial promotion he should contact the firm for advice on investments (or another appropriate firm if the firm does not offer advice on investments)

...  
3.9.18A G Firms are reminded of the provisions in COB 4.3, 5.2 and 5.3 requiring particular disclosures to clients in relation to life policies.

...  
Specific guidance

- 3.14.5 G
- (1) Key features, initial disclosure document and written contractual terms
    - (a) To meet the requirements of COB 3.9.10R, a *firm* should make it clear that the information is available to a recipient of the *direct offer financial promotion*, and easily obtainable, before any application is made.
    - (b) It is important that recipients should have the opportunity to view the

full text of the relevant *key features*, initial disclosure document, terms and conditions, customer agreement and any other applicable risk information required by the *rules*.

...

...

- 4.1.11 E (1) In the written warning required by *COB* 4.1.9R(1)(b)(i), a *firm* should, where relevant:
- (a) advise the *client* that he will lose the protection afforded by the following *rules* in *COB* applicable to *private customers*:
    - (i) *COB* 3 (Financial promotion);
    - (ii) *COB* 4.3 (Disclosing information about services, fees and commissions - packaged products);
    - (iii) *COB* 5.1 (Advising on packaged products);
    - (~~iv~~v) *COB* 5.4 (Customers' understanding of risk);
    - (~~iii~~v) *COB* 5.7 (Disclosure of charges, remuneration and commission);
    - (~~iv~~v) *COB* 6.1: (Packaged product and ISA disclosure);
    - (vii) *COB* 7.9 (Lending to private customers);
    - (viii) *COB* 7.10 (Margin requirements);
    - (~~viii~~x) *COB* 7.11 (Non-exchange traded securities);
  - (b) explain any consequences to the *client* in respect of the following *rules* in *COB* which are limited or modified in their application to *intermediate customers*:
    - (i) ~~{deleted}~~
    - (ii) ~~*COB* 5.1 (Polarisation and status disclosure)~~;
    - (iii) *COB* 8.1 (Confirmation of transactions);
    - (~~ii~~v) *COB* 8.2 (Periodic statements);

...

After *COB* 4.2 insert the following new section which is not underlined:

4.3 Disclosing information about services, fees and commission - packaged products

Application

4.3.1 R *COB* 4.3 applies:

- (1) to a *firm* when carrying on with or for *private customers* any of the following in relation to *packaged products*:
  - (a) *advising on investments*; or
  - (b) *dealing as agent*; or
  - (c) *arranging*;
- (2) to a *firm*, other than an *insurer*, that carries on in relation to a *life policy* any of the activities in (1) with or for an *intermediate customer* or a *market counter-party*.

## Purpose

- 4.3.2 G The *rules* in this section give further support to *Principle 7* (Communication with clients). There is, in relation to *packaged products*, a particular need for *private customers* to have information at an early stage about the nature and scope of the services which a *firm* may offer and the basis on which it may be remunerated. The *rules* also implement the *Insurance Mediation Directive*.

## Disclosure to private customers on first making contact

- 4.3.3 R (1) (a) A *firm* must take reasonable steps to ensure that its *representatives* on first making contact with a *private customer* with a view to:
- (i) *advising on investments on packaged products*; or
  - (ii) *dealing as agent in packaged products*; or
  - (iii) *arranging*;
- provide the *customer*, in a *durable medium*, with information concerning:
- (b) (i) the *firm* and the scope of and nature of its services (an *initial disclosure document*); and
  - (ii) where (a) applies, the *firm's* arrangements for charging and receiving *fees* and *commission* (a *fees and commission statement*);
- in both cases being information which the *firm* reasonably considers will be, or is likely to be, appropriate for the *customer* having regard to the type of service which the *firm* may provide or business which the *firm* may conduct.
- (2) A *firm* must also provide a *private customer* with an *initial disclosure document* if, in relation to the amendment of a *life policy* for that *private customer*, it:
- (a) *advises on investments on packaged products*; or
  - (b) *deals as agent in packaged products*; or
  - (c) *arranges*.
- (3) (a) The requirements in (1) and (2) do not apply:
- (i) to the extent that the appropriate information has already been given to the *customer* on a previous occasion and that information is still likely to be accurate and appropriate for the *customer*; or
  - (ii) if *COB 4.3.16R* (initial contact by telephone) applies; or
  - (iii) to a *firm* when it carries out an execution only *transaction* in non-life *packaged products*; or
  - (iv) to an *insurer* for those *customers* in respect of which it is not *advising on investments*.

- (b) A *firm* that reasonably expects it will not be *advising on investments* in respect of products falling within any of the product groups set out in Note 14 to COB 4 Annex 6R does not have to comply with the requirements in (1)(b)(ii) but if it does *advise on investments* on these products the *rules* will apply to the *firm* in respect of the *fees and commission statement* as if it was required by (1)(b)(ii) to provide the statement.
- (4) The requirements in (1) and (2) will apply to :
- (a) a *firm* that is acting as a discretionary *investment manager* for *private customers*; or
- (b) a *firm* which is effecting *execution-only transactions* in *packaged products* for *private customers*;
- only if the *firm* is carrying on an *insurance mediation activity* in relation to *life policies* for those *private customers*, in which case the requirements in (1) and (2) will only apply to the extent of requiring the *firm* to provide those *private customers* with an *initial disclosure document*.
- (5) A *firm* which acts for a *private customer* under a *non-discretionary management agreement* need not comply with the requirements in (1) above to provide an *initial disclosure document* or a *fees and commission statement* if the following are satisfied:
- (a) the *firm* is remunerated by the *customer* by the payment of a *fee*; and
- (b) the *agreement* provides that the *firm* may recommend *securities* as well as *packaged products* for inclusion in the *customer's* portfolio and that in respect of *packaged products* the *firm* will make selections from the whole market;
- but such a *firm* must, if it is carrying on an *insurance mediation activity* for a *private customer* in relation to *life policies*, comply with the requirements in (1) as to the provision of an *initial disclosure document* to the *private customer*.
- (6) A *firm* which is required in accordance with this *rule* to provide an *initial disclosure document* to a *private customer* may instead provide the *customer* with a *combined initial disclosure document* if it has reasonable grounds to be satisfied that the *services* which it is likely to provide to the *customer* will, in addition to *packaged products*, relate to one or more of the following:
- (a) *regulated mortgage contracts*;
- (b) *regulated lifetime mortgage contracts*;
- (c) *non-investment insurance contracts*.
- (7) The information contained in the *initial disclosure document* may be provided orally if a *firm* has not made a *personal recommendation* to a *private customer*, and:
- (a) the *customer* requests it; or
- (b) immediate cover is necessary;
- but in both cases the *firm* must provide the *initial disclosure document* immediately after the conclusion of the contract, in a *durable medium*.

- 4.3.4 G For certain types of *life policies*, such as annuities, it is customary for a *customer* to contact various *firms* for quotations which he can then compare. In these circumstances, it is not necessary for the *firm* to give an *initial disclosure document* (COB 4.3.3R(1)(i)) at the time that the quotation is provided, if the quotation cannot be accepted (and a contract cannot be formed) without the *firm* obtaining further information from the *customer*.

Provision of fees and commission statement on request

- 4.3.5 R A *firm* must take reasonable steps to ensure that it provides a *private customer* with an appropriate *fees and commission statement* whenever requested to do so.

Firms which charge fees

- 4.3.6 R (1) A *firm* must before starting to act for a *private customer* on the basis of a *fee* charging arrangement:
- (a) secure the *customer's* agreement to the particular rate or amount which the *firm* will charge for its services; and
  - (b) provide the *customer* with a record in a *durable medium* of the particular *fee* charging arrangement which will apply unless the *firm* starts to act for the *private customer* during a telephone call, in which case this record must be forwarded to the *customer* on conclusion of the call.
- (2) A *firm* which charges a *private customer* a *fee* must do so on the basis that it will, in respect of any *commission* which it receives in respect of transactions in *packaged products* for that *customer* (and to which the particular *fee* charging arrangement relates), ensure the value of that *commission* is transferred to the *customer* by one or more of the following:
- (a) reducing the amount of its *fee*;
  - (b) arranging for the amount invested by the *customer* to be increased; or
  - (c) refunding the amount of the *commission* to the *customer*;
- except that this does not prohibit such a *firm* from agreeing with the *customer* (in writing) that it will retain an amount or rate of trail or renewal *commission* up to an amount each year specified in the agreement and so small, relative to the overall amount of fees paid by the *customer*, that it would be manifestly disproportionate for the *firm* to be required to account to the *customer* in one of the ways outlined in (a) to (c).

Ongoing disclosure

- 4.3.7 R (1) A *firm* which has started to provide a *private customer* with services in relation to *packaged products* following the provision of a *fees and commission statement* must not (at least until the completion of those services):
- (a) increase the rate or amount of the *fees* it is charging the *customer*; or
  - (b) subject to (4), arrange to retain any *commission* which exceeds the maximum amount or rate disclosed in the *statement*;
- without first providing a further appropriate *statement* and obtaining the *customer's* prior consent to the proposed alteration in a *durable medium*.

- (2) A *firm* which in accordance with (1) secures a *private customer's* agreement to retain an increased rate or amount of *commission* must ensure that, if it subsequently provides the *customer* with a *suitability letter*, it includes an explanation of why it was necessary for the *firm* to recommend a *packaged product* in respect of which the *firm* will retain such higher *commission* or *fees*.
- (3) If a *firm* decides to provide a *private customer* with *advice on investments* on a type of *packaged product* (which falls within a product group specified in Note 14 to COB 4, Annex 6R) in relation to which the *fees and commission statement* previously given to the *customer* does not contain the information required in Note 14 to COB 4, Annex 6R, it must issue a new and appropriate *statement* to that *customer*.
- (4) (a) Notwithstanding (1)(b) a *firm* is not required to provide a further *fees and commission statement* for the purposes of (1) if:
  - (i) the maximum amounts or rates disclosed in the *statement* already provided to the *customer* only apply to policies of the example term or age of *policyholder* given in the *fees and commission statement* or to policies with shorter terms; and
  - (ii) the *firm* arranges a policy for a term longer than the example term in the *statement* (or longer than the term deemed for the example age given) and the increase in the *commission* which the *firm* arranges to retain over the maximum disclosed in the *statement* is not more than an amount that is directly proportional to the increase in the duration of the term of the policy (or to the term deemed from the age of *policyholder*).
- (b) If requested by a *customer*, a *firm* must explain the basis of the higher maximum *commission* or *fees* charged in accordance with (4)(a)(ii).

- 4.3.8 G (1) COB 4.3.7R (4) is intended to allow *firms* to arrange policies for a longer term than that given as the example in the *fees and commission statement* without requiring any further disclosure but only if the *commissions* the *firm* arranges to retain are directly proportional to the maximum *commissions* disclosed in the *statement* having regard to the duration of the policy. For example, if the *statement* disclosed a maximum *commission* of 10% on a 10 year policy, then on a 20 year policy the maximum *commission* the *firm* could arrange to retain is 20% without further disclosure
- (2) The maximum *commissions* that apply to *policies* of a particular term also apply as the relevant maxima for *policies* with a shorter duration. The *rule* is of no application in circumstances where a *firm* arranges to retain *commission* exceeding the maximum disclosed in the *fees and commission statement* if the policy arranged has a term shorter than the example given in the *statement*.
  - (3) Long-term care and whole of life *policies*, for which the example given in the *fees and commission statement* refers to the age of the *policyholder*, are deemed to have a term equal to the difference between the age of the *policyholder* (at the time that the policy is taken out) and the age of 85.



#### Initial disclosure document

- 4.3.9 R (1) An *initial disclosure document* must contain the keyfacts logo, headings and text in the order shown in *COB 4*, Annex 4R and in accordance with the Notes.
- (2) A *combined initial disclosure document* must contain the keyfacts logo, headings and text in the order shown in *COB 4*, Annex 5R and in accordance with the Notes.
- (3) If a *private customer* so requests, a *firm* should be able to provide an explanation of the basis on which it has chosen to market the particular *packaged products* within the *range* from which *advice on investments* will be given to that *customer* including an explanation of why the *firm* has selected particular *product providers*.
- (4) Information given in the initial disclosure information about compensation arrangements made by an *investment firm* must:
- (a) (if it relates to the activities of an *establishment* in the *United Kingdom*) be in English; or
- (b) (if it relates to the activities of a *branch* in another *EEA State*) be in an official language of that *EEA State*.
- (5) Information given in the initial disclosure information about the *insurance mediation activities* of a *firm* must be in English, unless the *customer* requests it to be, and the *firm* agrees to it being, in another language.
- 4.3.10 G *Firms* can obtain from the *FSA* website <http://www.fsa.gov.uk> a specimen of the *initial disclosure document*. Subject to *COB 4.3.9R*, a *firm* may produce its *initial disclosure document* by using its own house style and brand.

#### Fees and commission statement

- 4.3.11 R (1) A *fees and commission statement* must contain the keyfacts logo, heading and text in the order shown in *COB 4*, Annex 6R and in accordance with the Notes.
- (2) A *firm* must maintain as many versions of the *fees and commission statement* set out at *COB 4* Annex 6R as are appropriate to the different bases on which it may conduct business with *private customers*:
- (a) *fee* only (version 1);
- (b) *commission* (or *equivalent*) only (version 2);
- (c) *fee* or *commission* (or *equivalent*) (version 3);
- (d) *fee* or *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* (version 4);
- (e) *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* (version 5);
- (f) *fee*; or combination of *commission* (or *equivalent*) and *fee* (version 6).
- (3) A *firm* must keep its *fees and commission statements* up to date and keep a record of each *statement* for a period of six years from the date on which it was updated or replaced.

- (4) A *firm* must maintain a record of each particular *fees and commission statement* which it provides to a *private customer* (other than when given merely in response to a request).

4.3.12 G Where, as envisaged in COB 4.3.5R, a *firm* is asked to provide a *fees and commission statement* by a *person* with whom the *firm* has had no prior contact it may provide the *fees and commission statement* which is appropriate for its typical or most prevalent *customer* type and the business it conducts with them.

- 4.3.13 G (1) COB 4.3.11 requires a *firm* to maintain statements showing the amount it may charge its *customers* by way of *fees*, or which it may receive from others by way of *commission*, in either case in respect of services it provides in relation to the sale of *packaged products*. Consistent with COB 5.1 and COB 5.5 the basis on which a *firm* may provide such services may differ from *customer* to *customer* (for example as to whether the *firm* will select from the whole market, or a limited number of *product providers*).
- (2) A *firm* may maintain more than one version of the *fees and commission statement* but if it does, it must take reasonable steps to ensure that the statement provided to each *customer* in their initial contact is consistent with the description of the services given to the *customer* in the *firm's initial disclosure document* (as required by COB 4.3.3R) and with the record of the *range of packaged products* which the *firm* has supplied to the *customer* or which it would supply on request to the *customer* in accordance with COB 4.3.15R.
- (3) If a *firm* alters the nature of the services it provides for any *customer* then it may also change the basis or amount by which it will be remunerated whether by *fees* or *commission*. A *firm* proposing to make such a change should first provide the *customer* with a new *fees and commission statement* and explain its proposed altered basis for charging and receiving *commission* and seek the *customer's* consent to proceeding on that basis. A *firm* may when conducting further and separate services with a *customer* seek to do so on the basis of different arrangements for its remuneration.

#### Record for distribution of range of packaged products

4.3.14 R A *firm* which operates with a *range (or ranges) of packaged products* must produce in a *durable medium*, and in a form which is appropriate for distribution to *private customers*, the record of its *range (or ranges) of packaged products* which it maintains for the purposes of COB 5.1.6AR (1).

4.3.15 R A *firm* must take reasonable steps to ensure that its *representatives* provide a copy of the appropriate *range of packaged products* on the request of a *private customer* having regard to the services it is providing or may provide to the *customer*.

#### keyfacts information, terms of business and telephone sales

4.3.16 G (1) COB 4.3.17R and 4.3.18R enable provision by a *firm* of an *initial disclosure document* to a *private customer* to be taken as compliance also with analogous information provision requirements contained in COB 4.2 (Terms of business and client agreements with customers).

- (2) In cases where *firms* make initial contact with a *customer* on the telephone a *firm* may, in addition, have to take into account and comply with the additional requirements applicable to the conclusion of *distance contracts*. *COB 4.3.18R* expands on the items of information which a firm is required to give in accordance with *COB 4, Annex 1R* so that where the firm expects to conduct business relating to *packaged products* adequate information is given during the telephone call about the nature and scope of the services which the *firm* will or may provide.
- 4.3.17 R (1) A *firm* which complies with *COB 4.3.3R* will, in respect of any requirement imposed by *COB 4.2* as to the delivery or content of information to be included in its *terms of business*, be regarded as complying with any such analogous requirement.
- (2) Any information required by *COB 4.2* which is not covered by (1) may be satisfied by it being included at the end of an *initial disclosure document* which is given to a *private customer* in accordance with *COB 4.3.3R* or, if provided at the same time, by way of separate items of information.
- 4.3.18 R (1) Where a *firm's* initial contact with a *private customer* (for a purpose set out in *COB 4.3.3R*) is by telephone then the following information must be provided and requirements satisfied before proceeding further:
- (a) the name of the *firm* and, if the call is initiated by or on behalf of a *firm*, the commercial purpose of the call;
  - (b) whether the *firm* offers *packaged products* from the whole market or from a limited number of companies or from a single company or single group of companies;
  - (c) whether the *firm* will provide the *customer* with *advice on investments on packaged products*;
  - (d) if the *firm* does not offer products from the whole market, that the *customer* can request a copy of the appropriate *range of packaged products*;
  - (e) whether the *firm* offers a *fee based service*, a *commission based service*, a service based on a combination of fee and commission, or a combination of these three types of services, and the consequences for the *customer* of proceeding with each type of service;
  - (f) that the information given under (a) to (e) will subsequently be confirmed in writing.
- (2) A *firm* which complies with (1) will, subject to (3), satisfy the condition set out in item (1) of *COB 4, Annex 1R*.
- (3) If during the course of a telephone call a *firm* is to conclude a contract (whether for the provision of a mediation services and/or for the purchase or sale of a *packaged product*), it must as well as complying with (1) and (2) above satisfy the requirement in *COB 4.2.5R* and *COB 4, Annex 1R*.
- (4) If a *firm's* initial contact with a *private customer* by telephone is such that *COB 4.3.3R* (other than *COB 4.3.3R(2)(a)(ii)*) applies then, subject to any relevant exclusions, it must send the *customer* an *initial disclosure document* and a *fees and commission statement* as soon as is reasonably practicable following the conclusion of the call.

Intermediate customers and market counterparties (and private customers who are introduced): disclosure before conclusion of the contract or immediately after conclusion of the contract

- 4.3.19 R (1) *COB* 4.3.20R to 4.3.25R apply to a *firm*, other than an *insurer*, when it conducts any of the following in relation to *life policies* with or for an *intermediate customer* or a *market counterparty*:
- (a) *advising on investments*; or
  - (b) *dealing*; or
  - (c) *arranging*
- (2) *COB* 4.3.26R (disclosure by introducers) applies to a *firm*:
- (a) when it *introduces* a *private customer* to another *firm*;
  - (b) other than an *insurer* when it *introduces* an *intermediate customer* or *market counterparty* to another *firm*.
- 4.3.20 R (1) The information in *COB* 4.3.21R must be provided to the *client* in a *durable medium* at any time before conclusion of the contract, and if necessary upon amendment or renewal thereof, unless (2) or (4) applies.
- (2) The information in *COB* 4.3.21R:
- (a) may be provided orally if:
    - (i) the *client* requests this; or
    - (ii) the *client* requires immediate cover;
  - (b) need not be provided before conclusion of the contract if the contract is concluded by telephone, but if the *client* is a *retail customer* the requirements in *COB* 4.2.5R and *COB* 4, Annex 1R must be satisfied.
- (3) If (2) applies, the *client* must be provided with the information in *COB* 4.3.21R in a *durable medium* immediately after the conclusion of the contract.
- (4) The requirements in (1) do not apply to the extent that the information has already been given to the *client* on a previous occasion and that information is still likely to be accurate and up to date.
- 4.3.21 R Table Information to be provided before conclusion of the contract or immediately after conclusion of the contract.

This table belongs to *COB* 4.3.20R

1.	The name and address of the <i>firm</i> and, where relevant, the name and address of the <i>appointed representative</i> .
2.	The <i>firm's</i> statutory status (in accordance with <i>GEN</i> Ann 1R (Statutory status disclosure)).
3.	That items 1 and 2 can be checked on the <i>FSA Register</i> by visiting the <i>FSA's</i> website <a href="http://www.fsa.gov.uk/register">www.fsa.gov.uk/register</a> or by contacting the <i>FSA</i> on 0845 606 1234.
4.	Whether the <i>firm</i> or any <i>appointed representative</i> of the <i>firm</i> has any holding, direct or indirect, representing more than 10 per cent of the voting rights or of the capital in an <i>insurance undertaking</i> .
5.	Whether an <i>insurance undertaking</i> or parent of an <i>insurance undertaking</i>

	has a holding, direct or indirect, representing more than 10 per cent of the voting rights or of the capital in the <i>firm</i> or in any <i>appointed representative</i> of the <i>firm</i> .
6.	In relation to the <i>life policy</i> provided, whether the <i>firm</i> offers the product: <ul style="list-style-type: none"> <li>(a) on the basis of a fair analysis of the market; or</li> <li>(b) from a limited number of <i>insurance undertakings</i>; or</li> <li>(c) from a single <i>insurance undertaking</i>.</li> </ul> If (b) or (c) apply, the <i>firm</i> must also disclose whether it is contractually obliged to conduct <i>insurance mediation activity</i> in this way.
7.	If the contract has not been offered on the basis of a fair analysis of the market, that the <i>client</i> can request a copy of the list of the <i>insurance undertakings</i> from which the <i>firm</i> has offered the product.
8.	How to complain to the <i>firm</i> and, where relevant, that complaints may subsequently be referred to a named complaints scheme.
9.	Where relevant, that compensation may be available from a named compensation scheme should the <i>firm</i> be unable to meet its liabilities; the <i>firm</i> must describe the extent and level of cover and how further information can be obtained.

- 4.3.22 R (1) A *firm* must provide the information specified in COB 4.3.21R (9):
- (a) (if it relates to the activities of an *establishment* in the *United Kingdom*) in English; or
  - (b) (if it relates to the activities of a *branch* in another *EEA State*) in an official language of that *EEA State*.
- (2) The information provided by a *firm* pursuant to COB 4.3.20R and which relates to the *firm's insurance mediation activities*, must be in English, unless the *customer* requests it to be, and the *firm* agrees to it being, in another language.
- 4.3.23 G A *firm* can, subject to COB 4.3.24G, comply with COB 4.3.20R by providing the information specified in COB 4.3.21R in an *initial disclosure document* or, if appropriate, a *combined initial disclosure document*.
- 4.3.24 G A *firm* that provides the information required by COB 4.3.20R in an *initial disclosure document* or *combined initial disclosure document* may amend or delete sections of the document subject to the following:
- (a) the *firm* must not include the keyfacts logo and the heading and text in Section 1 unless it uses the document in full and without altering the text other than that in sections 5, 7 and 8, which may be amended or deleted; and
  - (b) the *firm* must still provide the information covered by the amended or deleted sections if required to do so by COB 4.3.20R.
- Information to be provided to clients on request
- 4.3.25 R (1) A *firm* that provides a service of a type described in COB 4.3.21R (6)(b) or (c) must maintain, and keep up to date, for each type of *life policy* it deals with, a list of *insurance undertakings* it deals with.
- (2) The information in (1) must be maintained in a form which allows a copy to

be provided to a *client* on request, in accordance with COB 4.3.21R (7), in a *durable medium*.

#### Disclosure by introducers

- 4.3.26 R (1) A *firm* that only *introduces* a *client* to another *firm* with a view to a transaction in a *life policy*, must provide the information in COB 4.3.21R (1) and (2) at the time it makes initial contact with the *client*. The information may be provided orally.
- (2) If the information required in (1) is provided orally, the information in COB 4.3.21R (1) and (2) must be provided in a *durable medium* immediately after the initial contact between the *firm* and the *client*.

#### Group Personal Pensions

- 4.3.27 R A *firm* must take reasonable steps to ensure that its *representatives* on first making contact with an employee with a view to advising on his employer's *group personal pension scheme* or *stakeholder pension scheme*, inform the employee:
- (1) that the *firm* will be providing *advice on investments* on *group personal pension schemes* and/or *stakeholder pension schemes* provided by the employer;
- (2) whether the employee will be provided with *advice on investments*:
- (a) that is restricted to the *group personal pension scheme* or *stakeholder pension scheme* provided the employer; or
- (b) the matters in (a) and other products;
- (3) the amount and nature (ie *fees* and/or *commission* (or *equivalent*)) and/or a combination of *fees* and *commission* (or *equivalent*)) of any payments that the employee will have to pay for the *advice on investments*.

Insert after COB 4 Annex 3 the following new annexes: Annex 4R, Annex 5R, Annex 6R, Annex 7R, Annex 8G and Annex 9G:

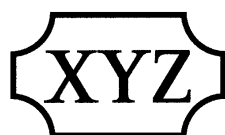
COB 4 Annex 4 R: Initial disclosure document required by COB 4.3.9 R (1) ("IDD")

1. Firms should omit the notes and square brackets which appear in the following specimen.

The IDD must contain the keyfacts logo, headings and text in the order shown and in accordance with the notes. [Note 1]



about our services [Note 2]



Financial Services

[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

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## 1. The Financial Services Authority (FSA)

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The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

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## 2. Whose products do we offer? [Note 6] [Note 7]

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- We offer products from the whole market. [Note 6A]
- We [can] [Note 8] only offer products from a limited number of companies.  
 Ask us for a list of the companies and products we offer. [Note 11]
- We [can] [Note 8] only offer [a] product[s] from [a single group of companies] [name of single company]. [Note 9(1)] [Note 12]  
 [or] [Note 9(2)]  
 We only offer our own products.  
Ask us for a list of the companies and products we offer. [Note 11]

---

**3. Which service will we provide you with? [Note 6]**

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- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.
- We will ask questions about your income, savings and other circumstances in order to provide basic advice on stakeholder products but we will not:
- conduct a full assessment of your needs;
  - consider whether any other product outside the range we offer may be more suitable. **[Note 6A]**

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**4. What will you have to pay us for our services?**

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- Before we provide you with advice, we will give you our keyfacts guide 'about the cost of our services'.**[Note 13]**
- We will tell you how we get paid, and the amount, before we carry out any business for you.

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**5. Who regulates us? [Note 14]**

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[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] **[Note 15]** **[Note 16]** is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. **[Note 17]**

Our permitted business is [ ]. **[Note 18]**

[or] **[Note 19]**

[Name of *appointed representative*] **[Notes 3 and 4]****[Note 3]** **[Note 4]** is an appointed representative of [name of *firm*] [address of *firm*] **[Note 15]** **[Note 16]** which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] **[Note 18]**

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.



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**6. Loans and ownership [Note 20]**

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[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.]  
[Note 20][Note 21]Note 22][Note 23]

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**7. What to do if you have a complaint [Note 14]**

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If you wish to register a complaint, please contact us:

**...in writing**      Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone**      Telephone [0121 100 1234]. [Note 24]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 25]

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**8. Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 14]**  
[Note 26] [Note 26A]

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.

Further information about compensation scheme arrangements is available from the FSCS.

The following notes do not form part of the IDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common keyfacts logo to be used on significant pieces of information directed to *customers*. The keyfacts logo and the text 'about our services' must be used and positioned as shown in the IDD. The logo may be re-sized, but it must be reasonably prominent and its proportions must not be distorted. When reproducing the logo, *firms* may use colour providing this does not diminish the prominence of the logo. A specimen of the keyfacts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the IDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – The *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 6A** – if a *firm* indicates that it will be providing *basic advice on stakeholder products* then the first box in section 2 must not be ticked as the *firm* will not be doing so on the basis of *advice on investments* from the whole market.

**Note 7** - if the IDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with *COB 5*.

**Note 8** – insert “can” if the *firm's* range of products is determined by any contractual obligation. This does not apply where a *product provider, insurer, lender* or company is selling its own products.

**Note 9** – if the *firm* selects this box, it will be offering the products of one provider to the *customer*. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. If the *firm* does not select this box, then the text must follow that set out in Note 12 below.

- (1) Insert the name of the provider. For example: "We can only offer products from [name of *product provider*]". If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a pension from [name of lender]".

- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part's trading name, it should use this alternative text.

**Note 11** – this sentence is required only where a *firm* selects this service option. The list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOB 4.2.14R*.

**Note 12** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies". For example: "We only offer the products from a single group of companies" should replace the text in the specimen *IDD*.

#### **Section 4: What will you have to pay us for our services?**

**Note 13** – *firms* are only required to provide a *private customer* with an appropriate keyfacts guide 'about the costs of our services' (i.e. a menu) if they propose to give that *customer advice on investments on packaged products*. Where a *firm* is not required to provide that *customer* with a menu because the *firm* does not intend to give him *advice on investments on packaged products*, then it should tick the second box in section 4.

#### **Section 5: Who regulates us?**

**Note 14** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information including the *firm's permitted business*. If this section is omitted, the other sections of the *IDD* must be renumbered accordingly.

**Note 15** – if the *firm's* address on the *FSA Register* differs from that given on the *IDD* under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 16** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 17** - an *incoming EEA firm* will need to modify this section if it chooses to use this *IDD* (see *GEN 4 Ann 1R(2)*).

**Note 18** – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 19** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

#### **Section 6: Loans and ownership**

**Note 20** – omit this section where there are no relevant loan or ownership arrangements under the following notes. If this section is omitted the other sections of the IDD must be renumbered accordingly. Where the information is provided by an *appointed representative*, it must cover loans made to or by that *appointed representative*, or holdings in or held by that *appointed representative*, as appropriate.

**Note 21** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 22** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 23** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

### **Section 7: What to do if you have a complaint**

**Note 24** - if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 25** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

### **Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 26** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 26A** - when a *firm* which is not a *participant firm* provides the CIDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained.

COB 4 Annex 5 R: Combined initial disclosure document required by COB 4.3.9 R (2) (“CIDD”)

1. Firms should omit the notes, asterisks and square brackets which appear in the following specimen.

This specimen covers services in relation to *packaged products, non-investment insurance contracts and regulated mortgage contracts* (including *regulated lifetime mortgage contracts* and home reversion schemes). If the *firm* is only providing services in relation to two types of these products, the parts of the CIDD that are not relevant must be omitted. *Firms* must omit the notes and square brackets that appear in the following CIDD. The CIDD must contain the keyfacts logo, headings and text in the order shown and in accordance with the notes.

[Note 1]



about our services [Note 2]



Financial Services

[Note 5]  
[123 Any  
Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

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## 1 The Financial Services Authority (FSA)

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The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

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## 2 Whose products do we offer? [Note 6] [Note 7]

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### Investment

- We offer products from the whole market. [Note 6A]
- We [can] [Note 8] only offer products from a limited number of companies.  
Ask us for a list of the companies and products we offer. [Note 12]
- We [can] [Note 8] only offer [a] product[s] from [a single group of companies] [name of single company]. [Note 10(1)] [Note 13]

[or] [Note 10(2)]

We only offer our own products.

Ask us for a list of the companies and products we offer. [Note 12]

## Insurance

- We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].
- We [can] [**Note 8**] only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. [**Note 12**]

- We [can] [**Note 8**] only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. [**Note 9**] [**Note 10(1)**] [**Note 13**]

[or] [**Note 10(2)**]

We only offer our own products for [list the types of *non-investment insurance contracts*].

## [Lifetime] Mortgages [and home reversion schemes] [**Note 14**]

- We offer mortgages from the whole market.
- We [can] [**Note 8**] only offer mortgages from a limited number of lenders.

Ask us for a list of the lenders we offer mortgages from. [**Note 11**]

- We [can] [**Note 8**] only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender]. [**Note 10(1)**][**Note 13**]

[or] [**Note 10(2)**]

We only offer our own mortgages.

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### 3 Which service will we provide you with? [**Note 6**]

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## Investment

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.
- We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances but we will not:

- Conduct a full assessment of your needs;
- Offer advice on whether a non-stakeholder product may be more suitable

[Note 6A]

### Insurance

- We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].
- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

### [Lifetime] Mortgages [and home reversion schemes] [Note 14]

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

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## 4 What will you have to pay us for our services?

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### Investment

- Before we provide you with advice, we will give you our keyfacts guide 'about the cost of our services'. [Note 15]
- We will tell you how we get paid, and the amount, before we carry out any business for you.

### Insurance [Note 16]

- A fee [of £ [ ] ] [for] [list the types of services provided for *non-investment insurance contracts*].
- No fee [for] [list the types of services provided for *non-investment insurance contracts*].

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

### [Lifetime] Mortgages [and home reversion schemes] [Note 14]

- No fee. [We will be paid by commission from the [lender/company].] [Note 17]

- A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] mortgage [or home reversion scheme]. [We will also be paid commission from the [lender/company.]] [Note 17] [Note 18]

You will receive a key facts illustration when considering a particular [lifetime] mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. [Note 14]

### Refund of fees [Note 19] [Note 14]

If we charge you a fee, and your [lifetime] mortgage [or home reversion scheme] does not go ahead, you will receive:

[Note 20]

- A full refund [if the [lender/company] rejects your application]. [Note 21]
- A refund of £ [ ] [if your application falls through]. [Note 21] [Note 22]
- No refund [if you decide not to proceed]. [Note 21]

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## 5 Who regulates us? [Note 23]

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[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 24] [Note 25] is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. [Note 26]

Our permitted business is [ ]. [Note 27]

[or] [Note 28]

[Name of *appointed representative*] [Note 3] [Note 4] is an appointed representative of [name of *firm*] [address of *firm*] [Note 24] [Note 25] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] [Note 27]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

[Home reversion schemes are not regulated by the FSA.] [Note 14]

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## 6 Loans and ownership [Note 29]

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[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.] [Note 29][Note 30][Note 31][Note 32][Note 33][Note 34]



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**7 What to do if you have a complaint [Note 23]**

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234]. [Note 35]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 36] [Note 36A] [Note 37] [The Financial Ombudsman Service does not consider complaints about home reversion schemes.] [Note 14]

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**8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 23] [Note 38] [Note 38A]**

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

**Investment**

Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.

**Insurance**

Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.

[or] [Note 39] [Note 39A]

For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.

**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

Mortgage advising and arranging is covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000. [Home reversion schemes are not covered by the Financial Services Compensation Scheme.] [Note 14]

Further information about compensation scheme arrangements is available from the FSCS.

**[Note 40] Message from the Financial Services Authority**

**Think carefully about this information before deciding whether you want to go ahead. If you are at all unsure about which lifetime mortgage or home reversion scheme is right for you, you should ask your adviser to make a recommendation.**

**Please remember that home reversion schemes are not regulated by the FSA.**

The following notes do not form part of the CIDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common key facts logo to be used on significant pieces of information directed to *customers*. The key facts logo and the text 'about our services' must be used and positioned as shown in the CIDD. The logo may be re-sized, but it must be reasonably prominent and its proportions must not be distorted. When reproducing the logo, *firms* may use colour providing this does not diminish the prominence of the logo. A specimen of the key facts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the CIDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – for services in relation to *packaged products* and *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes the *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. For services in relation to *non-investment insurance contracts*, the *firm* must select more than one box if the scope of the service or the type of service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance or if it provides *advice* on some types of contract but not others. In the case where more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the CIDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 6A** – if a *firm* indicates that it will be providing *basic advice on stakeholder products* then the first box in section 2 must not be ticked as the *firm* will not be doing so on the basis of *advice on investments* from the whole market.

**Note 7** - if the CIDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with *COB 5*, *ICOB 4.2.8R* note 1(e) and *MCOB 4.3.10R*.

**Note 8** – insert “can” if the *firm's* range of products is determined by any contractual obligation. This does not apply where a *product provider*, *insurer*, lender or company is selling its own products.

**Note 9** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the CIDD. This only needs to be done in

relation to the service it is offering a particular *customer*. For example, “we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance”.

**Note 10** – if the *firm* selects this box, it will be offering the products of one provider to the *customer* for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*. If the *firm* does not select this box, then the text must follow that set out in note 13 below.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the lender for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the company for home reversion schemes. For example: "We can only offer products from [name of *product provider*]". For *non-investment insurance contracts* the type of insurance offered should also be included. For example: "We only offer XYZ's household insurance and ABC's motor insurance." If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a mortgage from [name of lender]". If the *firm* does not offer all of the mortgages or home reversion schemes generally available from that provider, it must insert the words "a limited range of" as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part's trading name, it should use this alternative text.

**Note 11** – for services provided in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes, this sentence is required only where a *firm* selects this service option. It may also be omitted if a *firm* chooses to list all of the lenders it offers mortgages from instead of the text "a limited number of lenders", in the previous line, so long as the *firm* offers all of the products generally available from each lender.

**Note 12** – this sentence is required only where a *firm* selects this service option. For services provided in relation to *packaged products*, the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOB* 4.2.14R.

**Note 13** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies" for *packaged products*, "a single insurer" for *non-investment insurance contracts*, "a single lender" for *regulated mortgage contracts* or *regulated lifetime mortgage contracts* and "a single company" for home reversion schemes. For example: "We only offer the products from a single group of companies" should replace the text in the specimen CIDD.

**Note 14** – change “mortgage” to “lifetime mortgage” where the *firm* sells only *regulated lifetime mortgage contracts*. *Firms* must insert the text relating to home reversion schemes and change “mortgage” to “product” and “lender” to “company” if they advise or give personalised information on home reversion schemes in addition to *advising on investments* or giving personalised information on *regulated lifetime mortgage contracts*.

#### **Section 4: What will you have to pay us for our services?**

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate keyfacts guide "about the cost of our services" (i.e. a menu) if they propose to give that *customer advice on investments on packaged products*. Where a *firm* is not required to provide that *customer* with a menu because the *firm* does not intend to give him *advice on investments on packaged products*, then it should tick the second box in section 4.

**Note 16** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* or *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'. If the *firm* is offering more than one type of service in connection with *non-investment insurance contracts*, the *firm* may aggregate the *fees* over all the services provided, and (if that is the case) identify the services for which there is no *fee*.

**Note 17** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer* for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes, it must insert a plain language explanation of this (see specimen for a plain language example). If the *firm* will pay over to the *customer* any commission the *firm* receives, it may refer to that fact here.

**Note 18** – insert a plain language description of when any *fees* are payable for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If a *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

**Note 19** – omit this part of the CIDD on 'Refund of fees' if the *firm* has indicated that there will be "No fee" for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes or that any *fee* will be payable only if the product completes.

**Note 20** – *firms* may select as many boxes as appropriate.

**Note 21** – insert a short, plain language description of the circumstances in which the *fee* for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes is refundable or not refundable as described.

**Note 22** – a *firm* may delete this line if it does not offer a partial refund for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes in any circumstances.

### **Section 5: Who regulates us?**

**Note 23** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information including the *firm's permitted business*. This section may be omitted for services relating to *non-investment insurance contracts* if the *firm* provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. This section may be omitted for services relating to *regulated mortgage contracts* (including *regulated lifetime mortgage contracts*) and home reversion schemes in accordance with *MCOB 4.4.1R(3)*. If this section is omitted, the other sections of the CIDD must be renumbered accordingly.

**Note 24** – if the *firm's* address on the *FSA Register* differs from that given on the CIDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 25** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 26** - an *incoming EEA firm* will need to modify this section if it chooses to use this CIDD (see *GEN 4 Ann 1R(2)*).

**Note 27** – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 28** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

## **Section 6: Loans and ownership**

**Note 29** – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the CIDD must be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section must be changed to 'Ownership'. Where the information is provided by an appointed representative, it must cover loans made to or by that appointed representative or holdings in, or held by, that appointed representative as appropriate.

**Notes 30, 31 and 32** apply only to a *firm advising on, dealing in, or arranging* in relation to *packaged products* ~~for private customers~~.

**Note 30** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 31** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 32** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

**Notes 33 and 34** apply to an *insurance intermediary* that is not an *insurer* providing services in relation to *non-investment insurance contracts*.

**Note 33** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

**Note 34** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

**Section 7: What to do if you have a complaint**

**Note 35** – if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 36** – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

**Note 36A** – if the CIDD is provided by an authorised professional firm which is exclusively carrying on non-mainstream regulated activities, the authorised professional firm should delete this sentence and refer to the alternative complaints handling arrangements. It should also omit the information required under note 14.

**Note 37** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

**Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 38** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 38A** - when a *firm* which is not a *participant firm* provides the CIDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained. It should also omit the information required under note 14.

**Note 39** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it must use this alternative text.

**Note 39A** – where the *insurance intermediary* provides a service in relation to a contract which covers both a compulsory class of insurance and a class of insurance which is not compulsory, it should indicate the level of compensation that applies to each class.

**Lifetime mortgage warning**

**Note 40** - This warning box should be added when the *firm* sells *regulated lifetime mortgage contracts* or home reversion schemes or both

COB 4 Annex 6R (Fees and Commission Statement required by COB 4.3.11R (1) and (2))

1. (1) Versions of the templates for the *fees and commission statement* prescribed for the purposes of COB 4.3.11R:
  - (a) *fee* only (version 1);
  - (b) *commission* (or *equivalent*) only (version 2);
  - (c) *fee* or *commission* (or *equivalent*) (version 3);
  - (d) *fee* or *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* (version 4);
  - (e) *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* (version 5); and
  - (f) *fee*; or combination of *commission* (or *equivalent*) and *fee* (version 6).
- (2) *Firms* must omit the notes and square brackets that appear in the following templates. Except to the extent indicated in the Notes set out at the end of this annex, *firms* must use the text, format and type size shown in the templates. In particular, the templates must contain the 'keyfacts' logo, headings and prescribed text in the position and order shown and in accordance with the Notes. Subject to this, a *firm* may use its own house style and brand.

2. Version 1 - fee only template in accordance with COB 4.3.11R.

[Note 1]



about the cost of our services



[Note 2]

Financial Services

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

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## 1. The Financial Services Authority (FSA)

The FSA is the independent regulator of financial services. It requires us to give you this document when advising on some savings and investments. You may use this information to compare value for money, to shop around and to decide which firm to use.

---

## 2. Our services [Note 5]

We offer an initial discussion (without charge) when we will describe our services more fully and explain the payment options. If you decide to go ahead, we will:

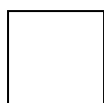
- gather and analyse personal information about you, your finances, your needs and objectives;
  - recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.
- 

## 3. What are your payment options? [Note 6(a)]

Not all firms charge for advice in the same way. We will discuss your payment options with you and answer any questions you have. We will not charge you anything until you have agreed how we are to be paid. **We have ticked the payment options we offer.**



**Paying by fee.** Whether you buy a product or not, you will pay us a fee for our advice and services. If we also receive commission from the product provider when you buy a product, we will pass on the full value of that commission to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the commission to you. [Note 6(b),(c),(d)]



**Paying by commission (or product charges).** If you buy a financial product, we will normally receive commission on the sale from the product provider. Although you pay nothing up-front, that does not mean our service is free. You still pay us indirectly through product charges. Product charges pay for the product provider's own costs and any commission. These charges reduce the amount left for investment. If you buy direct, the product charges could be the same as when buying through an adviser, or they could be higher or lower. We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier. [Note 6(e)]

---



#### 4. How much might our services cost? [Note 7] [Note 8]

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT. [Note 9]

Our typical charges are: [Note 10]

Principal/Director/Partner	<b>£150-200 per hour</b>
Financial adviser	<b>£100-150 per hour</b>
Administration	<b>£25 per hour</b>

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. [Note 9]

---

#### 5. Further information [Note 22]

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]

3. Version 2 - *commission* (or *equivalent*) only template in accordance with COB 4.3.11R.

[Note 1]



about the cost of our services



[Note 2]

Financial Services

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

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- gather and analyse personal information about you, your finances, your needs and objectives;
- recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.

---

## 3. What are your payment options? [Note 6a]

Not all firms charge for advice in the same way. We will discuss your payment options with you and answer any questions you have. We will not charge you anything until you have agreed how we are to be paid. **We have ticked the payment options we offer.**

**Paying by fee.** Whether you buy a product or not, you will pay us a fee for our advice and services. If we also receive commission from the product provider when you buy a product, we will pass on the full value of that commission to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the commission to you. [Note 6(b),(c),(d)]

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## 4. How much might our services cost? [Note 7] [Note 8]

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly [Notes 12-17]**

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Endowments</b>	10 year term	[Note 18]	[Note 19]	[Note 20]
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	[Note 18]	[Note 19]	[Note 20]
	10 year term	[Note 18]	[Note 19]	[Note 20]

**Table 2 - Commission if you invest a lump sum [Notes 12-17]**

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		Our maximum	Market average	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Investment bond</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>At retirement</b>				
<b>Annuities</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Income drawdown</b>	Any	[Note 18]	[Note 19]	[Note 20]

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines. [Note 21]

**5. Further information [Note 22]**

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]

4. Version 3 - *fee or commission (or equivalent)* template in accordance with COB 4.3.11R.

[Note 1]

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about the cost of our services



Financial Services

[Note 2]

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

---

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---

## 2. Our services [Note 5]

We offer an initial discussion (without charge) when we will describe our services more fully and explain the payment options. If you decide to go ahead, we will:

- gather and analyse personal information about you, your finances, your needs and objectives;
- recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.

---

## 3. What are your payment options? [Note 6a]

Not all firms charge for advice in the same way. We will discuss your payment options with you and answer any questions you have. We will not charge you anything until you have agreed how we are to be paid. **We have ticked the payment options we offer.**



**Paying by fee.** Whether you buy a product or not, you will pay us a fee for our advice and services. If we also receive commission from the product provider when you buy a product, we will pass on the full value of that commission to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the commission to you. [Note 6(b),(c),(d)]



**Paying by commission (or product charges).** If you buy a financial product, we will normally receive commission on the sale from the product provider. Although you pay nothing up front, that does not mean our service is free. You still pay us indirectly through product charges. Product charges pay for the product provider's own costs and any commission. These charges reduce the amount left for investment. If you buy direct, the product charges could be the same as when buying through an adviser, or they could be higher or lower. We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier. [Note 6(e)]

## 4. How much might our services cost? [Note 7] [Note 8]

### If you choose the fee option

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT. [Note 9]

Our typical charges are: [Note 10]

Principal/Director/Partner      **£150-200 per hour**

Financial adviser                      **£100-150 per hour**

Administration                        **£25 per hour**

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. [Note 9]

### If you choose the commission option

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly** [Notes 12-17]

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Endowments</b>	10 year term	[Note 18]	[Note 19]	[Note 20]
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	[Note 18]	[Note 19]	[Note 20]
	10 year term	[Note 18]	[Note 19]	[Note 20]

**Table 2 - Commission if you invest a lump sum [Notes 12-17]**

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		Our maximum	Market average	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Investment bond</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>At retirement</b>				
<b>Annuities</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Income drawdown</b>	Any	[Note 18]	[Note 19]	[Note 20]

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines. **[Note 21]**

**5. Further information [Note 22]**

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]

5. Version 4 - *fee* or *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* template in accordance with COB 4.3.11R.

[Note 1]



about the cost of our services



[Note 2]

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

---

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- recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.

---

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**Paying by a combination of commission and fee.** In some circumstances, we also charge a fee on top of any commission we might receive. [Note 6(f)(g)]



## 4. How much might our services cost? [Note 7] [Note 8]

### If you choose the fee option

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT. [Note 9]

Our typical charges are: [Note 10]

Principal/Director/Partner	<b>£150-200 per hour</b>
Financial adviser	<b>£100-150 per hour</b>
Administration	<b>£25 per hour</b>

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. [Note 9]

### If you choose the combination of commission and fee option [Note 11]

We will charge you a combination of fees and commission. The actual amounts will depend on the service provided to you, but will not exceed the total of the maximum fees set out above and the maximum commission set out in the tables below.

### If you choose the commission option

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly [Notes 12-17]**

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Endowments</b>	10 year term	[Note 18]	[Note 19]	[Note 20]
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	[Note 18]	[Note 19]	[Note 20]
	10 year term	[Note 18]	[Note 19]	[Note 20]

**Table 2 - Commission if you invest a lump sum** [Notes 12-17]

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		Our maximum	Market average	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Investment bond</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>At retirement</b>				
<b>Annuities</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Income drawdown</b>	Any	[Note 18]	[Note 19]	[Note 20]

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines. [Note 21]

**5. Further information** [Note 22]

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- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]

6. Version 5 - *commission* (or *equivalent*); or combination of *commission* (or *equivalent*) and *fee* template in accordance with COB 4.3.11R.

[Note 1]



keyfacts

## about the cost of our services

[Note 2]

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

---

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- recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.

---

### 3. What are your payment options? [Note 6a]

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**Paying by a combination of commission and fee.** In some circumstances, we also charge a fee on top of any commission we might receive. [Note 6(f)(g)]

---

## 4. How much might our services cost? [Note 7] [Note 8]

### If you choose the fee option

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT. [Note 9]

Our typical charges are: [Note 10]

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Administration	<b>£25 per hour</b>

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. [Note 9]

### If you choose the combination of commission and fee option [Note 11]

We will charge you a combination of fees and commission. The actual amounts will depend on the service provided to you, but will not exceed the total of the maximum fees set out above and the maximum commission set out in the tables below.

### If you choose the commission option

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly [Notes 12- 17]**

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Endowments</b>	10 year term	[Note 18]	[Note 19]	[Note 20]
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	[Note 18]	[Note 19]	[Note 20]
	10 year term	[Note 18]	[Note 19]	[Note 20]

**Table 2 - Commission if you invest a lump sum [Notes 12-17]**

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		Our maximum	Market average	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Investment bond</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>At retirement</b>				
<b>Annuities</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Income drawdown</b>	Any	[Note 18]	[Note 19]	[Note 20]

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines. [Note 21]

**5. Further information [Note 22]**

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]

7. Version 6 *fee*; or combination of *commission* (or *equivalent*) and *fee* template in accordance with COB 4.3.11R.

[Note 1]



about the cost of our services



Financial Services

[Note 2]

[Note 3] Last updated [22 October 2004]

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[ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB] [Note 4]

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## 1. The Financial Services Authority (FSA)

The FSA is the independent regulator of financial services. It requires us to give you this document when advising on some savings and investments. You may use this information to compare value for money, to shop around and to decide which firm to use.

---

## 2. Our services [Note 5]

We offer an initial discussion (without charge) when we will describe our services more fully and explain the payment options. If you decide to go ahead, we will:

- gather and analyse personal information about you, your finances, your needs and objectives;
- recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.

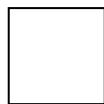
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## 3. What are your payment options? [Note 6a]

Not all firms charge for advice in the same way. We will discuss your payment options with you and answer any questions you have. We will not charge you anything until you have agreed how we are to be paid. **We have ticked the payment options we offer.**



**Paying by fee.** Whether you buy a product or not, you will pay us a fee for our advice and services. If we also receive commission from the product provider when you buy a product, we will pass on the full value of that commission to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the commission to you. [Note 6(b),(c),(d)]



**Paying by commission (or product charges).** If you buy a financial product, we will normally receive commission on the sale from the product provider. Although you pay nothing up front, that does not mean our service is free. You still pay us indirectly through product charges. Product charges pay for the product provider's own costs and any commission. These charges reduce the amount left for investment. If you buy direct, the product charges could be the same as when buying through an adviser, or they could be higher or lower. We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier. [Note 6(e)]



**Paying by a combination of commission and fee.** In some circumstances, we also charge a fee on top of any commission we might receive. [Note 6(f)(g)]

## 4. How much might our services cost? [Note 7] [Note 8]

### If you choose the fee option

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT. [Note 9]

Our typical charges are: [Note 10]

Principal/Director/Partner	<b>£150-200 per hour</b>
Financial adviser	<b>£100-150 per hour</b>
Administration	<b>£25 per hour</b>

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. [Note 9]

### If you choose the combination of commission and fee option [Note 11]

We will charge you a combination of fees and commission. The actual amounts will depend on the service provided to you, but will not exceed the total of the maximum fees set out above and the maximum commission set out in the tables below.

### If you choose the commission option

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly [Notes 12- 17]**

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Endowments</b>	10 year term	[Note 18]	[Note 19]	[Note 20]
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	[Note 18]	[Note 19]	[Note 20]
	10 year term	[Note 18]	[Note 19]	[Note 20]

**Table 2 - Commission if you invest a lump sum** [Notes 12-17]

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		Our maximum	Market average	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Investment bond</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>At retirement</b>				
<b>Annuities</b>	Any	[Note 18]	[Note 19]	[Note 20]
<b>Income drawdown</b>	Any	[Note 18]	[Note 19]	[Note 20]

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines. [Note 21]

**5. Further information** [Note 22]

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

[Note 23]

[Note 3] Last updated [22 October 2004]



The following Notes do not form part of the template.

- Note 1 The 'keyfacts' logo and the text "about the cost of our services" must be positioned as illustrated in the templates. The logo may be resized and re-coloured, but the size and colour must be prominent and its proportions must not be distorted.
- Note 2 Insert the name of the *firm* or its *appointed representative* (which in either case may be its *authorised* name or its trading name). A corporate logo or logos may also be included, where illustrated, but must be of equal prominence to 'keyfacts' logo. Where an *appointed representative* is providing the *fees and commission statement*, then the *appointed representative's* name must be inserted. An appointed representative may include its logo, but this must be in place of, and not in addition to, its principal's logo.
- Note 3 Insert the date on which the *fees and commission statement* was prepared or last amended, in accordance with COB 4.3.11R(3). This date may be shown either at the top of the front page of the *fees and commission statement* or at the end of the *fees and commission statement* after Section 5.
- Note 4 Insert the name and address of the head office or, if more appropriate, the principal place of business from where the *firm* or *appointed representative* expects to provide *advice on investments* to *private customers* on *packaged products*. The name and address of the *authorised firm* must not be included if the *fees and commission statement* is to be given by an *appointed representative*, which must insert its own address.

## Section 2

- Note 5 The text in Section 2 is not prescribed, but *firms* may adopt a form of the wording shown. *Firms* must describe the services they offer relating to *packaged products* in their own words, concisely, in plain language and within the space indicated in the template. This description must make clear that the initial discussion (not necessarily the initial meeting) about whether the *customer* wishes to use any of the *firm's* services will be without charge. A *firm* may choose to start charging (if appropriate) for the remainder of any or meeting, but only after any discussion on the content of the *fees and commission statement* has been concluded.

## Section 3

- Note 6
- (a) A *firm* must select, by inserting a tick, the appropriate boxes which show the service that the *firm* expects to provide to the *customer*. If the *fees and commission statement* is provided by an *appointed representative*, the service selected must be that offered by the *appointed representative*. The text in this Section 3 of the *fees and commission statement* is prescribed, except as indicated in Note 6(d) and (g) below.
  - (b) The "Paying by fee" option must be included in each *fees and commission statement* even if the *firm* is not offering a purely *fee* based option - in which case, the box and prescribed text must be included, but without a tick.

- (c) A *firm* which holds itself out as acting independently in the provision of *advice on investments on packaged products* must, in accordance with COB 5.1.11AR (1), offer a *private customer* the "Paying by fee" option.
- (d) A *firm* which offers a "contingent" *fee* based option (see COB 5.1.11BG(3)) must modify the wording by the "Paying by fee" option to explain (clearly and in plain language) how the contingent *fee* arrangement will operate. A *firm* could use the following example description: "If you buy a financial product, you will pay us a fee for our advice and services. But if no sale is made, you will not have to pay us anything."
- (e) The "Paying by commission (or product charges)" option must be included in each *fees and commission statement* even if the *firm* is not offering this option - in which case, the box and the prescribed text must be included, but without a tick. In this option, reference to "commission" means *commission* and *commission equivalent*.
- (f) A *firm* may only include the "Paying by a combination of commission and fee" option in the *fees and commission statement* where this option is actually offered to the *customer* to whom the *fees and commission statement* is given.
- (g) The text that accompanies the "Paying by a combination of commission and fee" option is not prescribed. However, a *firm* must insert a clear plain language description of how its maximum remuneration is calculated using both the *fee* and the *commission* information provided in Section 4 of the *fees and commission statement*.

## Section 4

- Note 7 In this section 4, if a *firm* offers both payment options to the *customer* to whom the *fees and commission statement* is given, then it must include the prescribed headings ("If you choose the fee option" and "If you choose the commission option") and accompanying text relating to both options. If either *fees* or *commission* are not offered, then the prescribed headings and text for whichever option is not offered should not be included in this section.
- Note 8 A *firm* which provides the "Paying by a combination of commission and fee" option must: (i) set out its maximum *fee* amount in the fee section of Section 4, and set out its maximum *commission* (or *equivalent*) amount in the commission section of Section 4; (ii) and ensure that the maximum amount of *fee* and *commission* (or *equivalent*) does not exceed the total of both options.

## Section 4 - Fees

Note 9 If a *fees and commission statement* contains information relating to *fees*, then a *firm* must ensure that the following statements are included:

1. "We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT."
2. "You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first."

Note 10 The text for describing a *firm's fee* charging arrangements is not prescribed, but must be clear and in plain language. A *firm* must provide numerical statements of the amount or rate of its *fees* and these must be expressed in pounds sterling or another appropriate currency, where relevant. Examples of statements which *firms* may use are:

### Hourly Rate

We will agree the rate we will charge before beginning work. Our typical charges are:

Principal/Director/Partner	£00-000 per hour
Financial adviser	£00-000 per hour
Administration	£00 per hour

Your adviser will tell you if you have to pay VAT.

### Lump Sum

We will agree what we will charge you before beginning work. Our typical charges are:

Individual financial review £00

Your adviser will tell you if you have to pay VAT.

### Percentage of funds under management

We will agree what we will charge you before beginning work. Our typical charges are:

Investment management agreement  
0% per year of the value of the investments you ask us to manage  
Your adviser will tell you if you have to pay VAT.

## Section 4 – Combination of commission (or equivalent) and fee

Note 11 If a *fees and commission statement* contains information relating to the combination of *commission* (or *equivalent*) and *fees*, then a *firm* must ensure that the maximum amount of *fee* and *commission* (or *equivalent*) does not exceed the total of both the fee and commission options. The maximum fee amount that a *firm* might charge must be set out in the fee section, and the maximum commission (or equivalent) amount must be set out in the commission section.

The text for describing a *firm's* charging arrangements where a *firm* offers the combination of *commission* (or *equivalent*) and *fees* option is not prescribed, but a *firm* must describe correctly (clearly and in plain language) its usual way of charging a combination of *fee* and *commission*. *Firms* may use a form of the wording set out in the following examples:

1. Where we charge a combination of fees and commission, our maximum rates are set out in the fee information section above and the commission section below.
2. We charge a consultation fee of up to £x, and, if you buy a financial product, we will also retain commission within the amounts set out in the commission tables below.
3. We will charge you a combination of fees and commission. The actual amounts will depend on the service provided to you, but will not exceed the total of the maximum fees set out above and the maximum commission set out in the tables below.
4. We charge an annual fee as described in the fee information set out above. If we arrange for you to purchase a financial product, then we will also retain commission which will be within the maximum commission amounts set out in the tables below.

## Section 4 – Commission (or equivalent)

Note 12 If a *fees and commission statement* contains information relating to *commission*, then a *firm* must set out information concerning *commission* (or *equivalent*) in the tabular format prescribed. The headings for Tables 1 and Table 2; the headings and sub-headings for each column; the product headings in each row of the first column; and the example term and age set out in the second column of each table are all prescribed and must not be amended.

Note 13 Each *fees and commission statement* must refer to the range of packaged products which the *firm* expects to be relevant for the particular *customer* or group of *customers* to whom the *fees and commission statement* is likely to be given. Where this stated range does not contain a product that is included in the templates, then a *firm* may delete the appropriate product row from the tables in its *fees and commission statement*.

Note 14 The text and information contained in the commission section of Section 4 must be included if a *firm* reasonably expects to provide those services to a *private customer* receiving the *fees and commission statement* in respect of any of the following product groups.

### Regular contribution business

The following product groups relate to regular contribution investments (including annual and quarterly premium contracts) and includes any non-contractual top-ups or increments (to existing regular contribution investments) which generate *commission (or equivalent)*.

(a) Collective investments

*Any regulated collective investment scheme or investment trust savings scheme.*

(b) Endowments

*A life policy that pays a sum of money on the survival of the life assured to a specific date or, if earlier, on death.*

(c) Whole of life assurance

*A life policy which, disregarding any benefit payable on surrender, secures a capital sum only on death or either on death or on disability, but does not include term assurance.*

(d) Personal and stakeholder pensions

*Any personal pension scheme, FSAVC scheme or stakeholder pension scheme (other than a group personal pension scheme or stakeholder pension scheme arranged on a group basis for the employees of a particular employer).*

### Lump sum business

*The following product groups relate to single contribution business, including commission (or equivalent) generating, non-contractual, top-ups or increments to existing lump sum investments.*

(a) Collective investments

*Any regulated collective investment scheme.*

(b) Investment bond

*A single premium whole of life assurance policy or endowment policy.*

(c) Personal and stakeholder pensions

*Any personal pension scheme, FSAVC scheme or stakeholder pension scheme (other than a group personal pension scheme or stakeholder pension scheme arranged on a group basis for the employees of a particular employer).*

(d) Annuities

*A pension annuity or purchased life annuity.*

(e) Income drawdown

*A pension contract effected for the purpose of income withdrawal from a pension fund.*

- Note 15 A *firm* which conducts business with *private customers* in relation to any *packaged products* not falling within any of the product groups may provide a *customer* with information about *commission* (or *equivalent*) relating to that business by way of a separate annex. For the purpose of the *rules*, any such information does not form part of a *firm's fees and commission statement*.
- Note 16 Having regard to the nature of the business which a *firm* reasonably expects to conduct with the *customers* to whom the *fees and commission statement* will be provided, a *firm* must (i) present information about *commission* receivable on regular monthly payments in accordance with Table 1; and (ii) present information about *commission* receivable on lump sums in accordance with Table 2. The information must be presented in the two separate but sequential Tables 1 and 2.
- Note 17 Where a *firm* reasonably expects not to conduct either regular contribution or lump sum business with the *customers* to whom the *fees and commission statement* will be provided, it may exclude the relevant table so that its *fees and commission statement* contains only the table relevant to the type of business it expects to conduct.
- Note 18 For each product group shown a *firm* must disclose the maximum amount or rate of *commission* (or *equivalent*) where applicable under COB 5.7.5R which it reasonably expects it would retain in respect of the sale of a *packaged product* falling within the product group. The maximum rate or amount must be ascertained in accordance with the procedure set out in COB 4 Annex 7R.
- Note 19 For each product group shown a *firm* must disclose the corresponding market average calculated and published by the FSA and in accordance with the procedure set out in COB 4 Annex 7R.
- Note 20 For each product group illustrated a *firm* must include an example in accordance with COB 4 Annex 7R.
- Note 21 The two notes shown at the end of Section 4 of the *fees and commission statement* are prescribed.

## **Section 5**

- Note 22 The text in section 5 is prescribed.
- Note 23 An example of a completed *fees and commission statement* is shown at COB 4 Annex 9 G.

## COB 4 Annex 7 R

### Identifying and describing the maximum rate of commission (or equivalent), the market average and the Example

1. A *firm* must state in each *fees and commission statement* it issues:
  - (a) its maximum rate of *commission (or equivalent)* for each product group in the statement;
  - (b) the market average rate for each product group;
  - (c) an illustration in the example column of an amount of *commission (or equivalent)* calculated by reference to its maximum rate for each product group in the statement and the example contribution levels stated in the tables (ie eg £100 per month or £10,000 lump sum).

### Maximum rate of commission (or equivalent)

2. The maximum rate of *commission (or equivalent)* specified by a *firm* must be the maximum amount that the firm decides to retain.
3. If the maximum *commission (or equivalent)* is not apparent from the rates supplied by a *product provider* then a *firm* must adopt the net present value comparison method set out below.
4. For any product group, the maximum rate of *commission (or equivalent)* must not be more than a *firm* could reasonably expect to receive from any *product provider*.

### Identifying a maximum rate of commission – comparison of net present value

5. A *firm* must use the assumptions set out in paragraphs 8-12 below when calculating the maximum commission figures to be inserted into its *fees and commission statement*. Where a *firm* uses a tool provided by the FSA for this express purpose (for example a calculator provided by the FSA on a cd-rom for the purpose of calculating the maximum commission figures), the calculations can be presumed to have used these assumptions.
6. The net present value for each *commission (or equivalent)* rate must be calculated as the sum of the discounted values of each *commission (or equivalent)* payment that the *firm* may retain for that *commission (or equivalent)* rate, using the assumptions set out in paragraphs 8-12 below.
7. For any product group, the *firm's* maximum rate of *commission (or equivalent)* is the *commission (or equivalent)* rate in that product group with the highest net present value.
8. A *firm* must use the assumptions outlined in Table 1 when calculating net present values.

COB 4 Annex 7 R Table 1 Table of assumptions to be used in calculating net present values.

<b>Product</b>	<b>a) Discount Rate</b>	<b>b) Net growth rate</b>	<b>c) Lapse rate (per annum)</b>	<b>d) Assumed Term</b>	<b>e) Withdrawal rate (per annum)</b>
<b>Regular premiums/contributions</b>					
<b>Collective investment scheme</b>	Net growth rate + 3%	6%	6%	10 years	
<b>Endowment</b>	Net growth rate + 3%	6%	6%	Maturity	
<b>Personal Pensions / SHP</b>	Net growth rate + 3%	6%	12% for 5 years then 5%	Maturity	
<b>Whole of Life</b>	Net growth rate + 3%	6%	6%	37 years	
<b>Single premiums/contributions</b>					
<b>Annuities</b>	Net growth rate + 3%	6%	0%	16 years	
<b>Bonds</b>	Net growth rate + 3%	6%	2.5%	7 years	5%
<b>Collective investment scheme</b>	Net growth rate + 3%	6%	6%	7 years	
<b>Personal Pensions / SHP</b>	Net growth rate + 3%	6%	2.5%	10 years	
<b>Income withdrawals</b>	Net growth rate + 3%	6%	0%	10 years	6%

9. *Commission (or equivalent)* payments must be assumed to be payable as outlined in COB 4 Annex 7 R Table 2

COB 4 Annex 7 R Table 2 – The timing of *commission (or equivalent)* payments

<b>Type of commission (or equivalent payment)</b>	<b>When payable</b>
Initial / indemnified commission	immediately at outset of the contract
Commission as a % of premiums	at the time of payment of the relevant monthly premium
Commission as a % of fund value	at the end of each policy month, immediately after any withdrawals and lapses, at a monthly rate of 1/12 <sup>th</sup> of the annual % of the fund value



10. Withdrawals must be assumed to occur monthly at a rate that is 1/12th of the assumed annual withdrawal rate.
11. Lapses must be assumed to occur monthly, at a rate that is 1/12<sup>th</sup> of the assumed annual lapse rate. In calculating the net present value, no commission should be assumed to be payable on the proportion of policies that are assumed to have lapsed.
12. Mortality rates must be ignored.

**Describing the maximum rate of commission (or equivalent)**

13. Subject to paragraph 14, a *firm* must use each appropriate description in COB 4 Annex 7 R Table 3 (ie one or more) to describe the maximum rates of *commission (or equivalent)* in its *fees and commission statement*.

COB 4 Annex 7 R Table 3

Type of commission (or equivalent)	Descriptions
Regular premium or contributions	i. "X% of the first 12 month's payments" ii. "X % of each of the first n month's payments" iii. "Y% of all payments" iv. "Y% of all payments from month p" v. "Z% of your fund value each year from year q".
Lump sums	i. "X% of the amount you invest" ii. "Z% of your fund value each year from year q"

14. A *firm* must adapt any of the descriptions prescribed by Tables 3 so that its *fees and commission statements* adequately describe the particular characteristics of a *firm's commission (or equivalent)* arrangements. For example, a *firm* can and should re-express the percentage figure, in the description taken from Table 3, in a "shape" (that is a description of the pattern of payments) that it considers to be typical of the way in which it retains *commission (or equivalent)*. This may differ from the shape in which the particular maximum rate of *commission (or equivalent)* is actually payable. Another example of the way in which a *firm* should adapt the descriptions in Table 3 is if the *commission* received by a *firm* is payable as a fixed cash amount per policy then alternative wording should be used by the *firm* to adequately describe the fixed nature of the payment in its description of the rate of commission.
15. A *firm* that uses more than one of the descriptions in COB 4 Annex 7 R Table 3 must make it clear that it has used more than one description (eg by inserting the word "plus" in between each description).
16. The maximum rate of *commission (or equivalent)* must be rounded to the nearest 0.1% unless the *commission (or equivalent)* is a multiple of 0.25% of a fund value in which case it should be shown rounded to the nearest 0.25%.

## Identifying and describing the market average

17. The *FSA* will publish the net present value of market average rates on its website from time to time.
18. A *firm* must express the market average rate in the shape or pattern of payments which most closely corresponds to the number, frequency and nature of payments in the shape or pattern of payments used to describe the firm's maximum *commission* (or *equivalent*).
19. A *firm* can use any suitable tool or method to re-express the market average in its *fees and commission statements*, as long as that method uses the assumptions set out in 8 - 12 above (for example a calculator contained on a cd-rom of the type referred to in paragraph 5).
20. The market average rate shown in the *fees and commission statement* must be a re-expression of the published net present value of the market average using the assumptions set out in 8 – 12 above. Subject to any rounding in the final description, this re-expression should have the same net present value as the published market average.
21. A *firm* must describe the market average rate using the most appropriate description in the Descriptions column in Table 3.

The market average may be equivalently expressed by adopting the method set out in the worked example in *COB 4 Annex 9 G* below, used in conjunction with tables of net present value factors that will be made available by the *FSA*. These factors will be calculated using the assumptions set out above. Alternatively, the market average expression may be expressed using such other tools, systems or methods as the *FSA* may make available from time to time.

## Changes in the market average

22. A *firm* must ensure that its *fees and commission statements* are revised to take account of changes in the market average rates published by the *FSA* by not later than:
  - (a) 2 months from the date on which the *FSA* prescribes amended market average rates if the effect of the amendment is to reduce any of the averages for a relevant product group by 4% or more of the previous average; and
  - (b) in all other cases at such time as the *firm* has occasion to revise its *statements*.

## The example

23. Subject to paragraph 26, a *firm* must use, in the example in its *fees and commission statement*, the description in Table 4 that corresponds to description(s) of the maximum rate of the *commission* (or *equivalent*) that appears in its *fees and commission statement*.

COB 4 Annex 7 R Table 4

Type of <i>commission</i> (or <i>equivalent</i> )	Description of the maximum rate of <i>commission</i> (or <i>equivalent</i> )	Corresponding description to be used in the example
Regular premium or contributions	i. "X% of the first 12 month's payments"	i. "£X initially"
	ii. "X % of each of the first n month's payments"	ii. "£X spread evenly over the first n months"
	iii. "Y% of all payments"	iii. "£Y each year"
	iv. "Y% of all payments from month p"	iv. "£Y each year from month p"
	v. "Z% of your fund value each year from year q".	v. "£Z in year p, £Z + A in year p + 1, and so on (the actual amounts will vary in line with your fund value)"
Lump sums	i. "X% of the amount you invest"	"£X initially"
	ii. "Z% of your fund value each year from year q"	"£Z each year from year p (The actual amounts will vary in line with your fund value)"

24. A *firm* that uses more than one of the descriptions in Table 4 must make it clear that it has used more than one description (eg by inserting the word "plus" in between each description).
25. A *firm* must adapt any of the descriptions prescribed by Tables 3 and 4 as are necessary to ensure that a *fees and commission statement* adequately describes the particular characteristics of a *firm's commission (or equivalent)* arrangement. Examples of the way in which the descriptions could be adapted are provided in paragraph 14 above.

## COB 4 Annex 8 G

### Calculation of a maximum rate of commission

1. The net present value of each *commission* (or *equivalent*) rate may be calculated by adopting the method set out in the worked example below, used in conjunction with tables of sample net present value factors issued by the *FSA*. These factors will be calculated using the assumptions set out in paragraphs 8 to 12 of *COB 4 Annex 7 R*.

### Worked Example of Commission Disclosure in a *fees and commission statement*

2. For the purposes of the following worked example four variations of *commission* (or *equivalent*) are shown for an investment bond. The market averages and NPV factors are purely illustrative.

A *firm* has commission arrangements for the sale of investment bonds with five *product providers* involving all four variations. The *firm* retains all commissions from each provider. The arrangements are:

Provider	Provider Commission		
	Initial	% of fund value	Fund based start month
1	5.25%	-	-
2	4.5%	-	-
3	-	0.75%	13
4	3.0%	0.5%	1
5	3.5%	0.25%	1

### Stage 1 - Comparison of net present value

The *firm* has to decide which provider pays "our maximum". The test is to calculate the net present value of the different commissions using the assumptions prescribed by the *FSA*. To do this, the method in form 1b below is used. The *firm* needs to look up the table of NPV factors which shall be made available by the *FSA*. Looking these up, and completing the form as follows gives:

Product group	Investment Bonds						
	Initial Commission			Fund Based Renewal / Trail Commission			Total NPV
	Commission Rate	NPV Factor	Value = Rate x Factor	Commission Rate (& Start Month)	NPV Factor	Value= Rate x Factor	
	A	B	$C = A \times B$	J	K	$L = J \times K$	
1	5.25%	1.00	5.25%	-	-	-	5.25%
2	4.5%	1.00	4.5%	-	-	-	4.5%
3	-	1.00	-	0.75% from month 13	3.997	2.98%	2.98%
4	3.0%	1.00	3.0%	0.5% from month 1	4.943	2.47%	5.47%
5	3.5%	1.00	3.5%	0.25% from month 1	4.943	1.24%	4.74%

So commission shape 4 has the highest net present value and is thus "our maximum".

### Stage 2 – Worked example

An example is calculated by applying "our maximum" rates to the prescribed lump sum or monthly amounts. £10000 in this case gives "£300 immediately plus £50 each year from year 1".

### Stage 3 – Market Average

"The market average" is the market average rate published by the *FSA* expressed in the shape that most corresponds to the shape of "our maximum". To do this, the method used in form 2 below is used. The *firm* needs to look up the table of NPV factors and the table of market average NPVs prescribed by the *FSA*. Looking these up, and completing the form as follows gives:

Form 1 (Worked Example)

Product group		Investment Bond						
Market Average NPV		5.0%						
		Fund Based Renewal / Trail Commission		Premium Based Renewal Commission		Spread initial / Non-Indemnified Commission		Initial / Indemnified Commission
		Commission rate	Start month	Commission rate	Start month	Commission rate	Spread period	Commission rate
Commission Shape of your maximum	A	0.5%	Month 1	-	-	-	-	3.0%
NPV Factor	B	4.943		-		-		1.000
Value of Commission Shape	C = A x B	2.47%		-		-		3.0%
Value of market average - Fund Based Commission	D1 – see notes	2.47%						
Value of market average – Premium Based Commission	D2 – see notes			-				
Value of market average - Spread Initial Commission	D3 – see notes					-		
Value of market average - Initial Commission	D4 – see notes							5.0% - 2.47% = 2.53%
Market Average Commission Shape	E = D ÷ B	2.47% / 4.943 = 0.5% from month 1		-		-		2.53% / 1.000 = 2.5%

Therefore the market average, expressed in the shape that most closely resembles "our maximum" is 2.5% of the lump sum plus 0.5% of the fund from month 1

#### Stage 4

Enter the appropriate figures in the fees and commission statement as shown below.

Lump sum products	Example term or age	Comparison of costs		Example based on £10,000 lump sum
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10,000 ignoring any changes to fund value</i>
<b>Savings and investments</b>				
<b>Investment bond</b>	Any	<b>3.0%</b> of the amount you invest plus <b>0.5%</b> of your fund value each year from year 1	<b>2.5%</b> of the amount you invest plus <b>0.5%</b> of your fund value each year from year 1	<b>£300</b> in year 1 plus <b>£50</b> each year from year 1 (The actual amount will vary in line with your fund)

**Form 1a – Calculation of Maximum Commission Amounts (Monthly Premium Products)**

This form should be used to help decide which of the commission options received for a product group in the "monthly products" table should appear as "our maximum" on the *fees and commission statement*.

<b>Product group</b>													
	<b>Initial / Indemnified Commission</b>			<b>Spread Initial Commission</b>			<b>Premium Based Renewal Commission</b>			<b>Fund Based Renewal / Trail Commission</b>			<b>Total NPV</b>
	<b>Commission Rate</b>	<b>NPV Factor</b>	<b>Value = Rate x Factor</b>	<b>Commission Rate (&amp; Spread Period)</b>	<b>NPV Factor</b>	<b>Value= Rate x Factor</b>	<b>Commission Rate (&amp; Start Month)</b>	<b>NPV Factor</b>	<b>Value= Rate x Factor</b>	<b>Commission Rate (&amp; Start Month)</b>	<b>NPV Factor</b>	<b>Value= Rate x Factor</b>	
A	B	C = A x B	D	E	F = D x E	G	H	I = G x H	J	K	L = J x K	M = C + F + I + L	
1		1.00											
2		1.00											
3		1.00											
4		1.00											
5		1.00											
6		1.00											
7		1.00											
8		1.00											

***The maximum rate of commission for this product group is the shape with the highest Total NPV (column M).  
This maximum rate of commission should be included in the fees and commission statement for this product group***



## Notes for completion of form 1a

1. A separate form should be completed for all monthly product groupings appearing on the *fees and commission statement*.
2. Complete a separate row for each potential maximum commission shape that you receive in the chosen product group.
3. Commission shapes that are clearly lower in value than others of the same shape should be omitted – for example, 15% initial + 0.5% fund based paid from month 12 is clearly lower than 20% initial + 0.5% fund based paid from month 12, and so only the latter needs to be included in the calculations.
4. Commission rates used should be the highest rates of the total commission payable that you may retain;
5. Commission rates should be entered for each commission type as follows:
  - Column A (Initial/Indemnified) - a percentage of the first 12 months' premiums;
  - Column D (Spread Initial/Non-Indemnified Initial) – a percentage of each premium paid in the initial commission period;
  - Column I (Premium based renewal) – a percentage of each premium paid in the renewal period;
  - Column L (Fund Based renewal/trail) – a percentage of the fund value each year.
6. Level commissions, payable as a percentage of all monthly premiums, should be treated as premium-based renewal commissions.
7. The relevant NPV Factors in columns B, E, H & K should be inserted for the relevant Product Group, Commission Type, Spread Period and Start Month. They can be obtained from the document "Published NPV Factors".
8. Columns C, F, I, L & M should be calculated based on the figures inserted in the previous columns.
9. The commission shape which has the highest total NPV in column M should be used in the "Our Maximum" section of the *fees and commission statement*.

**Form 1b – Calculation of Maximum Commission Amounts (Lump Sum Products)**

This form should be used to help decide which of the commission options received for a product group in the "lump sum products" table should appear as "our maximum" on the *fees and commission statement*.

Product group							
	Initial Commission			Fund Based Renewal / Trail Commission			Total NPV
	Commission Rate	NPV Factor	Value = Rate x Factor	Commission Rate (& Start Month)	NPV Factor	Value= Rate x Factor	
	A	B	C = A x B	J	K	L = J x K	
		1.00					
2		1.00					
3		1.00					
4		1.00					
5		1.00					
6		1.00					
7		1.00					
8		1.00					

***The maximum rate of commission for this product group is the shape with the highest Total NPV (column M). This maximum rate of commission should be included in the fees and commission statement for this product group***

### Notes for completion of form 1b

1. A separate form should be completed for all lump sum products appearing on the *fees and commission statement*.
2. Complete a separate row for each potential maximum commission shape that you receive in the chosen product group.
3. Commission shapes that are clearly lower in value than others of the same shape should be omitted – for example, 15% initial + 0.5% fund based paid from month 12 is clearly lower than 20% initial + 0.5% fund based paid from month 12, and so only the latter needs to be included in the calculations.
4. Commission rates used should be the highest rates of the total commission payable that you may retain.
5. Commission rates should be entered for each commission type as follows:
  - Column A (Initial) - a percentage of the lump sum payment;
  - Column J (Fund Based renewal/trail) – a percentage of the fund value each year.
6. The relevant NPV Factors in columns B & K should be inserted for the relevant Product Group, Commission Type and Start Month. They can be viewed in the document "Published NPV Factors".
7. Columns C, L & M should be calculated based on the figures inserted in the previous columns.
8. The commission shape which has the highest total NPV in column M should be used in the "Our Maximum" section of the *fees and commission statement*.

**Form 2 – Re-expression of market average commission**

This form should be used to re-express the market average NPV into the relevant shape, for use in the *fees and commission statement*.

Product group								
Market Average NPV								
		Fund Based Renewal / Trail Commission		Premium Based Renewal Commission		Spread initial / Non-Indemnified Commission		Initial / Indemnified Commission
		Commission rate	Start month	Commission rate	Start month	Commission rate	Spread period	Commission rate
Commission Shape of your maximum	A							
NPV Factor	B							
Value of Commission Shape	C = A x B							
Value of market average - Fund Based Commission	D1 – see notes							
Value of market average – Premium Based Commission	D2 – see notes							
Value of market average - Spread Initial Commission	D3 – see notes							
Value of market average - Initial Commission	D4 – see notes							
Market Average Commission Shape	E = D ÷ B							

## Notes for completion of form 2

1. A separate form should be completed for each product group appearing on your fees and commission statement;
2. The Market Average NPV should be obtained from the FSA's most recent published list of market averages, choosing the appropriate rate for the relevant product group.
3. In row A, enter the details of the commission shape that the market average is to be expressed in. This should be the commission shape shown as "your maximum" for the relevant product group in your fees and commission statement.
4. Commission rates should be entered for each commission type as follows:
  - Fund Based renewal/trail – a percentage of the fund value each year;
  - Premium based renewal – a percentage of each premium paid in the renewal period;
  - Spread Initial/Non-Indemnified Initial – a percentage of each premium paid in the initial commission period;
  - Initial/Indemnified - a percentage of the first 12 months' premiums, or a percentage of the lump sum, as appropriate.
5. Level commissions, payable as a percentage of all monthly premiums, should be treated as premium-based renewal commissions.
6. Where "your maximum" commission does not contain a commission type (e.g. your maximum has no spread initial commission), the column relating to that commission type should be left blank.
7. The relevant NPV Factors in row B should be inserted for the relevant Product Group, Commission Type, Spread Period and Start Month. They can be obtained from the document "Published NPV Factors".
8. Row C should be calculated as the product of the relevant commission rate in row A and the NPV factor in row B.
9. Row D1 should be calculated as the lower of:
  - the Market Average NPV, and
  - Row C - The Value of Commission Shape for the **fund based commission** type (but see the note below)

**Note:** If the commission shape in row A contains no premium-based, spread initial or initial/indemnified commission (i.e. if fund based commission is the final commission type being considered) then the calculation in row C should be ignored when calculating D1. In this instance, the value in D1 should be equal to:

- the Market Average NPV

10. Row D2 should be calculated as the lower of:

- The Market Average NPV minus the value calculated for row D1; and
- Row C – The Value of Commission Shape for the **premium based commission** type (but see note below).

If this calculation gives a negative value, D2 should be set to zero.

**Note:** If the commission shape in row A contains no spread initial or initial/indemnified commission (i.e. if premium-based commission is the final commission type being considered) then the calculation in row C should be ignored when calculating D2. In this instance, the value in D2 should be equal to:

- The Market Average NPV minus the value calculated for row D1.

11. Row D3 should be calculated as the lower of:

- The Market Average NPV minus the value calculated for row D1,  
minus the value calculated for row D2, and
- Row C – The Value of Commission Shape for the **spread initial / non-indemnified commission** type (but see note below).

If this calculation gives a negative value, D2 should be set to zero.

**Note:** If the commission shape in row A contains no initial/indemnified commission (i.e. if premium-based commission is the final commission type being considered) then the calculation in row C should be ignored when calculating D3. In this instance, the value in D3 should be equal to:

- The Market Average NPV minus the value calculated for row D1, minus the value calculated for row D2.

12. Row D4 should be calculated as:

- The Market Average NPV minus the value calculated for row D1, minus the value calculated for row D2, minus the value calculated for row D3.

If this calculation gives a negative value, D4 should be set to zero.

13. Row E should be calculated as the value in the relevant row D (for that commission type, e.g. row D2 for premium based renewal commission) divided by the relevant NPV factor in row B. For presentation in the *fees and commission statement*, this result should be rounded to the nearest 0.1% (or the nearest 0.25%, if fund-based commission is paid as an exact multiple of this).

**keyfacts** about the cost of our services **ABC plc**  
Financial Services

Last updated 22 October 2004

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ABC Financial Services plc, 123 Any Street, Some Town, ST21 7QB

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## 1. The Financial Services Authority (FSA)

The FSA is the independent regulator of financial services. It requires us to give you this document when advising on some savings and investments. You may use this information to compare value for money, to shop around and to decide which firm to use.

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## 2. Our services

We offer an initial discussion (without charge) when we will describe our services more fully and explain the payment options. If you decide to go ahead, we will:

- gather and analyse personal information about you, your finances, your needs and objectives;
  - recommend and discuss any action we think you should take and, with your agreement, arrange relevant investments for you.
- 

## 3. What are your payment options

Not all firms charge for advice in the same way. We will discuss your payment options with you and answer any questions you have. We will not charge you anything until you have agreed how we are to be paid. **We have ticked the payment options we offer.**



**Paying by fee.** Whether you buy a product or not, you will pay us a fee for our advice and services. If we also receive commission from the product provider when you buy a product, we will pass on the full value of that commission to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the commission to you.



**Paying by commission (or product charges).** If you buy a financial product, we will normally receive commission on the sale from the product provider. Although you pay nothing up front, that does not mean our service is free. You still pay us indirectly through product charges. Product charges pay for the product provider's own costs and any commission. These charges reduce the amount left for investment. If you buy direct, the product charges could be the same as when buying through an adviser, or they could be higher or lower. We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier.



## 4. How much might our services cost?

### If you choose the fee option

We will agree the rate we will charge before beginning work. We will tell you if you have to pay VAT.

Our typical charges are:

Principal/Director/Partner	<b>£150-200 per hour</b>
Financial adviser	<b>£100-150 per hour</b>
Administration	<b>£25 per hour</b>

You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first.

### If you choose the commission option

Tables 1 and 2 show examples of the amounts of commission we could receive (or the equivalent we earn through product charges) and compare those amounts with the market average (see notes 1 & 2 at the end of this section 4).

The amounts vary according to: the type of product, the amount you invest, and (sometimes) how long you invest for, or your age when you start the product. We will confirm the actual amount to you before you buy a product.

**Table 1 - Commission if you invest monthly**

Products	Example term or age	Comparison of costs		Example based on £100 per month
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a monthly investment or premium of £100, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	5% of all payments	5.5% of all payments	£60.00 each year
<b>Endowments</b>	10 year term	30% of each of the first 16 month's payments plus 2.5% of all payments from month 17	25.9% of each of the first 16 month's payments plus 2.5% of all payments from month 17	£360.00 spread evenly over the first 16 months plus £30.00 each year from month 17
<b>Protection</b>				
<b>Whole of life assurance</b>	Age 40	90% of each of the first 12 month's payments plus 2.5% of all payments from month 49	104.2% of each of the first 12 month's payments plus 2.5% of all payments from month 49	£1080.00 spread evenly over the first 12 months plus £30.00 each year from month 49
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	25 year term	20% of each of the first 12 month's payments plus 0.25% of your fund value each year from year 1	20.9% of each of the first 12 month's payments plus 0.25% of your fund value each year from year 1	£240.00 spread evenly over the first 12 months plus £3.00 in year 1, £6.00 in year 2, and so on (The actual amount in later years will vary in line with your fund value)
	10 year term	15% of each of the first 12 month's payments plus 0.25% of your fund value each year from year 1	19.2% of each of the first 12 month's payments plus 0.25% of your fund value each year from year 1	£180.00 spread evenly over the first 12 months plus £3.00 in year 1, £6.00 in year 2, and so on (The actual amount in later years will vary in line with your fund value)

**Table 2 - Commission if you invest a lump sum**

Products	Example term or age	Comparison of costs		Example based on £10 000 lump sum
		<i>Our maximum</i>	<i>Market average</i>	<i>This shows the maximum costs of our sales and advice for a lump sum investment of £10 000, ignoring any changes in fund value</i>
<b>Savings and investments</b>				
<b>Collective investments (eg unit trusts)</b>	Any	<b>3%</b> of the amount you invest plus <b>0.25%</b> of your fund value each year from year 1	<b>2.5%</b> of the amount you invest plus <b>0.25%</b> of your fund value each year from year 1	<b>£300.00</b> initially plus <b>£25.00</b> each year from year 1 (The actual amount in later years will vary in line with your fund value)
<b>Investment bond</b>	Any	<b>7%</b> of the amount you invest	<b>5%</b> of the amount you invest	<b>£700.00</b> initially
<b>Saving for retirement</b>				
<b>Personal and Stakeholder pensions</b>	Any	<b>0.5%</b> of your fund value each year from year 1	<b>0.6%</b> of your fund value each year from year 1	<b>£50.00</b> each year from year 1 (The actual amount in later years will vary in line with your fund value)
<b>At retirement</b>				
<b>Annuities</b>	Any	<b>1.5%</b> of the amount you invest	<b>1.4%</b> of the amount you invest	<b>£150.00</b> initially
<b>Income drawdown</b>	Any	<b>3%</b> of the amount you invest plus <b>0.5%</b> of your fund value each year from year 1	<b>1.8%</b> of the amount you invest plus <b>0.5%</b> of your fund value each year from year 1	<b>£300.00</b> initially plus <b>£50.00</b> each year from year 1 (The actual amount in later years will vary in line with your fund value)

**Notes:**

1. The market average figures are calculated by the FSA using actual data from a representative sample of regulated firms and are shown in a way that you may compare with our own maximum rates. The market average figures will be updated by the FSA from time to time based on new data.
2. Where a firm sells its own products it must calculate its figures according to FSA guidelines.

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**5. Further information**

If you need any more help or information

- ask your adviser; or
- visit [www.fsa.gov.uk/consumer](http://www.fsa.gov.uk/consumer).

Last updated 22 October 2004

5.1 ~~Polarisation and Status Disclosure~~ Advising on packaged products

Application

- 5.1.1 R This section applies to a *firm* which gives *advice on investments* to a *private customer* on *packaged products* ~~(including *adopted packaged products*), and to a *firm* which is a member of a *marketing group*.~~

Purpose

- 5.1.2 G This section gives support to *Principle 6* (Customers' interests) and *Principle 7* (Communications with clients) which require *firms* to have due regard to the information needs of their *customers* and treat them fairly. The purpose of this section is to ensure that *private customers* are adequately informed about the nature of the *advice on investments* which they may receive from a *firm* in relation to *packaged products*. In particular *firms* need to be clear to *private customers* about the scope and range of the products and *product providers* on which their *advice on investments* is based. ~~When *advice on investments* which are *packaged products* is given, it is important that a *private customer* is always clear whether a *firm*, its *advisers* or *representatives*, will act solely in his interests or whether the range of advice offered by the *firm* will be determined by the nature and number of the *firm's* commercial relationships. Accordingly, the *rules and guidance* in *COB 5.1* give effect to the regulatory policy of polarisation which, in relation only to *advice on packaged products* requires a *firm* to act either independently for the *private customer*, or to act on a tied basis where advice is restricted to its own products, those of its *marketing group* and *adopted packaged products*. Polarisation does not extend to an *execution-only transaction* or to a *financial promotion* of a *packaged product* which does not contain any *advice on investments*.~~

Delete the existing COB 5.1.3G to COB 5.1.6G inclusive, which are not shown struck through, and replace with the following new rules: COB 5.1.6AR to 5.1.6GR, which are not underlined:

- 5.1.3 G [deleted]
- 5.1.4 G [deleted]
- 5.1.5 G [deleted]

5.1.6 G [deleted]

Scope and range of advice on packaged products: general

- 5.1.6A R (1) A *firm* which gives *advice on investments* to *private customers* about *packaged products* must, subject to (2), take reasonable steps to ensure that the scope of the *advice on investments* given to a *private customer* is based upon a selection from one of the following:
- (a) the whole market (or the whole of a named sector of the market);  
or
  - (b) a limited number of *product providers*; or
  - (c) a single *company* or single group of *companies*.
- (2) A *firm* may change the scope of the *advice on investments* it gives to a particular *private customer* by widening the scope from that in (1)(c) through to that in (b) or (a) or from (b) to (a), but it must take reasonable steps to ensure that before doing so the *customer* is made aware of the proposed change by a communication in a durable *medium*.
- (3) If a *firm*:
- (a) extends the scope of the *advice on investments* it will give a *private customer*; or
  - (b) extends the *range of packaged products* on which its *advice on investments* will be based;

and as a consequence the *firm's* arrangements for its remuneration are materially altered, the *firm* must provide the *customer* with a new and appropriate *fees and commission statement*.

- 5.1.6B G (1) *COB 5.1.6AR* requires a *firm* when giving *advice on investments* to a *private customer* to do so on the basis that the scope of its *advice on investments* will involve a selection from the whole market (or from the whole of a sector of the market), or from a limited number of *product providers* or from a single provider and to adhere to such a scope during the advisory process unless the *firm* decides, and if necessary secures the *customer's* agreement, to widen the scope for the *customer* and, if necessary, any changes in the arrangements by which the *firm* will be remunerated (see *COB 4.3.6R*). A *firm* can choose to offer both whole of market and more limited *advice on investments*. The scope of the advice which the *customer* subsequently receives should always however be made clear and explained in a way which is likely to be understood.

- (2) The scope of *advice on investments* prescribed in each of COB 5.1.6AR (1) (a) to (c) will require different competencies on the part of a *firm's representatives* to enable the *firm* to discharge its advisory functions.
- (3) A *firm* selecting *packaged products* from a limited number of *product providers* or from a single provider may do so on the basis of a *range of packaged products* which comprises a selection of products available from those providers and accordingly a *firm* may have one or more such *ranges*. COB 4.3.3R requires a *firm* to give each *customer* some initial disclosure information – an *initial disclosure document* - which must indicate the scope of the *advice on investments* which the *customer* can expect to receive. This initial information must also invite the *customer* to ask for a copy of the *range of packaged products* from which the *firm* will make a selection. A *firm* which has several *ranges of packaged products* will need to ensure that each *customer* who asks for it is given information about the *range* which is appropriate for that *customer*.
- (4) If a *firm* holds itself out as giving *advice on investments* to *private customers* on *packaged products* from the whole market (or the whole of any sector of that market; see (5)), the *firm's* selection for this purpose will need to be sufficiently large to enable the *firm* to satisfy the suitability requirement in COB 5.3.9R (Requirement for suitability: whole-of-market advisers). One way in which such *firms* may wish to satisfy this requirement is by using “panels” of *product providers* which are sufficient for the purpose of giving advice from the whole market and which are reviewed on a regular basis. A *firm* which provides *advice on investments* from the whole market (or from the whole of a sector of the market) should ensure that its analysis of the market and the available *packaged products* is kept adequately up to date.
- (5) References to a *firm* advising on *packaged products* from the whole of a sector of the market are to a *firm* which, though holding itself out as giving *advice on investments* from the whole market, *advises on investments* in practice only on a relatively limited selection of *packaged products* which are available to meet the needs of a specialist sector or niche market (for example pension annuities). In such circumstances the quality of the *firm's* analysis of the sector or niche market should be commensurate with that which a *firm* would apply for the purposes of selecting products from the market as a whole.
- (6) IPRU(INS) 1.3 (Restriction of business to insurance) in practice restricts the *range of packaged products* that a *long-term insurer* may have and CIS 16.5.1R (Managers of UCITS schemes) restricts the *range of packaged products* that a *manager* of a *UCITS scheme* may have.

- (7) If a *firm* gives *advice on investments* to a *private customer* on a *packaged product* produced by another *person*, the *key features* must be “appropriate” (see *COB 6.2.7R* (Provision of key features: life policies) *COB 6.2.22R* (1) (Provision of key features: schemes) and *COB 6.4.15R* (Stakeholder pension schemes)). Therefore, if the terms of the *packaged product* are different from the terms of the product for which the *key features* was originally prepared by the *product provider*, for example there are additional charges, then the *key features* will need to be amended.
- (8) There are restrictions on *communicating* and *approving a financial promotion* relating to a *life policy* produced by an *unauthorised person* (see *COB 3.13.1R* (Additional requirements for financial promotions for an overseas long-term insurer)).
- (9) When a *firm* gives *advice on investments* relating to a *packaged product* which is not produced by the *firm*, it is responsible for the *advice on investments* given. The *product provider* is responsible for the relevant terms and conditions of the *packaged product*.
- (10) The *rules* in *COB 5.1* are mainly concerned to ensure that *firms* can offer a wide range of advisory services in relation to *packaged products*. In the course of giving such advice a *firm's representatives* may also need to consider the merits of whether a *customer* should give up, surrender or cease contributing to an existing *packaged product* and the *rules* in this section do not place a restriction on this (subject always to such *advice on investments* being suitable having regard to the *customer's* circumstances).

Range of packaged products: appointed representatives

- 5.1.6C R (1) A *firm* must maintain in writing and keep up to date a statement of:
- (a) the scope of *advice on investments* (within the meaning of *COB 5.1.6AR(1)*) which each of its *appointed representatives* is, through its contract with the *firm*, permitted to give; and including
  - (b) the *range* (or *ranges*) of *packaged products* on which each *appointed representative* advises.
- (2) In applying the *rules* in *COB* to a *firm* in respect of its *appointed representatives*, references to a *firm's* scope or *range of packaged products* are to be taken as references to the scope (or scopes) and to the *range* (or *ranges*) of its *appointed representatives*.

- 5.1.6D G An *appointed representative's range of packaged products* may be defined by a particular category of *packaged product* or by individual product, as long as it is clear (for example, "all pension products of ABC Co Limited"). It may be set out in a document separate from the *appointed representative's* contract of appointment and should, in any event, be separate from the main body of the contract for clarity.

Range of packaged products: records

- 5.1.6E R (1) A *firm* must make, and keep up to date, a record of the scope (or scopes) of the *advice* (within the meaning of COB 5.1.6AR(1)) which it provides, its *range* (or *ranges*) of *packaged products* and the *range* or *ranges* of each of its *appointed representatives* (if different from the *firm's*).
- (2) The record in (1) must be retained for six years from the date on which it was superseded by a more up-to-date record.
- (3) The record for distribution to a *customer* must be the particular *range of packaged products* which is appropriate for the services provided to that *customer* and include details of:
- (a) the identity of the *product providers* within the *range* whose *packaged products* the *firm* may sell; and
  - (b) a list of the categories of their products the *firm* may sell.
- (4) In the case of a *firm* whose scope of *advice on investments* is the selection of *packaged products* from the whole of the market (or from the whole of a sector of the market) and which provides no other scope of *advice on investments*, it will be sufficient if the *firm's* record is restricted to confirming that the *advice on investments* it provides is given on this basis (and in the case of a *firm* which provides *advice on investments* on the whole of a sector of the market, confirms the nature and parameters of that sector).
- (5) For the purposes of the record in (1), (3) and (6), in relation to the *packaged products* within a particular category available from a *product provider*:
- (a) where a *firm* provides services to a particular *customer* in relation to all of the products within that category the record may refer simply to that category and the *product provider* and not each particular product within the category; and
  - (b) notwithstanding (3)(b), where a *firm* does not provide services to a particular *customer* in relation to all of the products within that category the record must give details of each of the products in the category on which it does provide services.

- (6) A *firm* must maintain a record of the particular *range* of *packaged products* on which its *advice on investments* to each *private customer* is based and such a record must be kept for six years from the date on which the *advice on investments* is given.

#### Branding packaged products

- 5.1.6F R If a *firm* gives *advice on investments* to a *private customer* on a *packaged product* produced by another *person*, it must not:
- (1) hold itself out as the *packaged product's* producer; or
  - (2) do or say anything which might reasonably lead a *private customer* to be mistaken as to the identity of the product's producer.
- 5.1.6G R A *firm* must display the brand of the *product provider* at least as prominently as any other brand in the documentation that it makes available to its *customers* in relation to a *packaged product*.

#### ~~Tied advice by provider firms~~ Staying within the range of advice of packaged products

- 5.1.7 R (1) A ~~*provider firm*~~ must, subject to (2), take reasonable steps to ensure that neither it nor any of its *representatives* gives *advice on investments* to a *private customer* about the purchase of a *packaged product* unless the product is:
- ~~(a) issued by the *firm* itself or by another member of its *marketing group*; or~~
  - ~~(b) an *adopted packaged product*~~
  - (a) within the *firm's range* (or *ranges*) of *packaged products*; and
  - (b) is within the particular *range of packaged products* on which *advice on investments* is given to that *customer*.
- (2) The restriction in (1) does not apply where COB 5.3.7R (Suitability of packaged products: out-of-range recommendations) applies.
- 5.1.8 R [deleted]
- 5.1.9 G COB 5.1.7R (1) does not inhibit the sale by a ~~*provider firm*~~;



- (1) where the sale does not involve the provision of *advice on investments* to a *private customer*; a ~~A provider~~ firm may act as an intermediary for a transaction in a *packaged product* where that transaction is an *execution-only transaction* (*long-term insurers* are reminded of IPRU(INS)1.3 (Restriction of business to insurance) and *managers of UCITS schemes* are reminded of CIS 16.5.1R (Managers of UCITS schemes)); or
- (2) when the firm acts a discretionary investment manager.

5.1.11 R [deleted]

Restriction on holding out

- 5.1.11A R (1) A firm that, in relation to packaged products, provides advice on investments to a private customer, must not hold itself out as acting independently unless it intends to:
- (a) provide advice on investments to that customer that is on packaged products from the whole market (or the whole of a sector of the market); and
  - (b) offers the customer the opportunity of paying fees for the provision of such advice.
- (2) A firm which in accordance with (1) holds itself out as independent must ensure that the advice on investments subsequently given to the private customer concerned is on packaged products from the whole market (or the whole of a sector of the market).
- (3) A firm will not contravene (2) and does not need to offer the option of fee based advice on investments in accordance with (1), if it acts in accordance with COB 4.3.27R.
- 5.1.11B G (1) COB 5.1.11AR stipulates what a firm must do if it is to hold itself out to any particular client that it will act independently. Firms which wish to hold themselves out generally as acting independently should ensure that doing so (for example through a trading name or advertising) is consistent with the kind of service which private customers receive in relation to packaged products.
- (2) A firm that carries on business both in relation to packaged products and regulated mortgage contracts can do so in relation to the whole market and therefore be "independent" for one but offer only a limited service for the other. If this is the case the firm should explain the different nature of the services in a way which meets the requirement for clear, fair and not misleading communications in COB 2.1.3R (Clear, fair and not misleading communications).

- (3) COB 5.1.11AR (1)(b) means that a *firm* wishing to hold itself out as independent will need to give *customers* a purely *fee* based option for paying for its services. Such a *fee* may be offered on a contingent basis so that it does not become payable if the *customer* does not acquire a product. A *firm* offering a fee-based service may, in addition, provide the *customer* with other payment options, such as by *commission*.

Representatives to have access to whole range

- 5.1.12 R (1) A ~~provider~~ *firm* must, subject to (2), take reasonable steps to ensure that those of its representatives who give advice on investments on packaged products are able to sell with advice on investments each ~~type of packaged product~~ within the particular range of packaged products from which products are selected for a *customer* ~~that it issues itself or is issued by a member of its marketing group, or is an adopted packaged product~~.
- (2) A ~~provider~~ *firm* may restrict the ~~type of packaged products~~ it authorises a particular *representative* to sell, if:
- (a) that *representative* is not sufficiently competent to sell certain types of product; and
  - (b) it requires that *representative* to identify instances when another ~~packaged product of its own, or of the marketing group, or an adopted packaged product~~ outside his own restricted range within the relevant range of packaged products ought to be recommended; ~~The representative must then be required to refer the private customer to another representative within the marketing group of the firm~~ who is authorised and competent to sell that product.

Remuneration structure and referrals

- 5.1.13- R A ~~provider~~ *firm* must take reasonable steps to ensure that none of its representatives:
- (1) ~~is are not~~ likely to be influenced by the structure of ~~their~~ his or her remuneration to give unsuitable *advice on investments* to a *private customer*; and
  - (2) ~~do not~~ refers private customers to an independent intermediary another firm in circumstances which would amount to the provision of an inducement under COB 2.2.3R (Prohibition of inducements).

Excess charges on price-capped products

5.1.14 R A ~~firm which is a provider firm~~ must, if it gives advice on investments to a private customer about ~~on an adopted packaged product~~ stakeholder pensions scheme or other price capped product for which the firm is not the product provider, ensure that it does so only in accordance with arrangements under which the firm discloses any charges imposed by the firm in excess of those charged by the producer of the ~~adopted packaged product.~~

5.1.14A G Products subject to price caps within COB 5.1.14R would include ISAs marketed as “CAT standard”.

Delete the remaining provisions in this section COB 5.1.15R to 5.1.23G inclusive, these are not shown struck through.

5.1.15 R [deleted]  
to  
5.1.23G

...

5.2.1 R ...  
  
(3) ... ~~customer~~; or  
  
(4) is not an insurer and makes a personal recommendation to take out a life policy to an intermediate customer or a market counterparty; or  
  
(5) is not an insurer and is arranging (but not merely by introducing) a life policy;  
  
(6) is an insurer and is arranging a life policy for a private customer.

5.2.2 G ... However, the Insurance Mediation Directive requires that a statement of the demands and needs of a client is provided to the client, whether advice is given or not. This is required whatever the status of the client. Accordingly the demands and needs provisions in COB 5.2.12R to COB 5.2.17G apply to all circumstances relating to life policies.

#### Statement of demands and needs

5.2.12 R (1) Unless either COB 5.2.13R or COB 5.2.14R applies, a firm must provide the client with a statement of his demands and needs if:  
  
(a) it makes a personal recommendation of a life policy to a client; or

- (b) it arranges (whether through issuing a *direct offer financial promotion* or otherwise) for the *client* to enter into a *life policy*.
  - (2) Unless (3) applies, the statement in (1) must be provided:
    - (a) as soon as practicable, and in any event before the conclusion of the contract for the *life policy*; and
    - (b) in a durable *medium*.
  - (3) A *firm* may provide the statement in (1) orally if:
    - (a) the *client* requests it; or
    - (b) immediate cover is necessary;

but in both cases the *firm* must provide the information in (1) immediately after the conclusion of the contract, in a durable *medium*.
- 5.2.13 R If the only contact between the *firm* and the *client* before conclusion of the contract is by telephone, the statement of demands and needs must be provided immediately after the conclusion of the contract, in a durable *medium*.
- 5.2.14 R A *firm* need not provide a statement of demands and needs if the required information is contained in a *suitability letter*, or explanation of a *personal recommendation*, provided under COB 5.3.
- 5.2.15 G (1) A *firm* may provide the demands and needs statement as part of an application form so that the demands and needs statement is made dependent upon the *customer* providing personal information on the application form (including an application forming part of a *direct offer financial promotion*).
- (2) For quotations (see COB 4.3.3AG), there is no requirement for the *firm* to provide a demands and needs statement, but one must be provided before the conclusion of the contract, unless the only contact between the *firm* and the *client* is by telephone, in which case COB 5.2.13R applies.
- (3) A *key features* document that complies with COB 6.1.4R (Requirement to produce key features) may be used as the statement of demands and needs required by COB 5.1.12R (1)(b).
- 5.2.16 G COB 5.2.17G contains guidance on the contents of the statement required by COB 5.2.12R(1).
- 5.2.17 G Table
- Guidance on the contents of the statement required by COB 5.2.12R(1).

This table belongs to COB 5.2.16G.

	<u>Introduction</u>
(1)	<u>Where relevant, the statement should explain simply and clearly why the <i>personal recommendation</i> is viewed as suitable, having regard to the <i>client's</i> demands and needs.</u>
	<u>Style and Presentation</u>
(2)	<u>The style and presentation of the statement is left for the <i>firm</i> to decide, so that a statement can be designed which works best for the market in which the <i>firm</i> transacts business. A statement is more likely to be effective if it demonstrates these features:</u>
(a)	<u>simplicity and plain language: when technical terms need to be incorporated, they should be explained if the <i>client</i> is unlikely to understand their meaning; and</u>
(b)	<u>concise and clear messages: lengthy explanations and extensive statements are likely to reduce the effectiveness of the statement, and make the <i>client</i> less likely to read the statement properly.</u>

5.2.18 G Firms are reminded of the record keeping obligations under SYSC 3.2.20R.

...

5.3.1 R ...

(4) ... employees; ; or

(5) if the *firm* is not an *insurer*, makes a *personal recommendation* to an *intermediate customer* or a *market counterparty* to take out a *life policy*.

...

5.3.3 G Firms are reminded of the requirements of COB 3.9.6R (Direct offer financial promotions: general requirements). A *direct offer financial promotion* must make it clear that, if a *private customer* is in any doubt about the suitability of the agreement which is the subject of the promotion, he should contact the *firm*, or ~~an *independent intermediary*~~ another appropriate *firm* if the *firm* does not offer advice.

...

Requirement for suitability generally

5.3.5 R (1) A *firm* must take reasonable steps to ensure that, ~~it does not if~~ in the course of *designated investment business*:

(a) it makes any personal recommendation to a private customer to:

(i) buy, ~~or sell~~, subscribe for or underwrite a *designated investment* (or to exercise any right conferred by such an *investment* to do so); or

(ii) elect to make *income withdrawals*; or

... (iii) enter into a *pension transfer* or *pension opt-out* from an *occupational pension scheme*; or

(b) it effects a discretionary transaction for a *private customer* (except as in (3 5)); or

(c) it makes a *personal recommendation* to an *intermediate customer* or a *market counterparty* to take out a *life policy*;

~~unless the recommendation~~ *advice on investments* or transaction is suitable for the *private customer-client*. having regard to the facts disclosed by him and other relevant facts about the *private customer* of which the *firm* is, or reasonably should be, aware.

(2) If the recommendation or transaction in (1) relates to a *packaged product*:

(a) it must, subject to COB 5.3.7R - COB 5.3.10R, be the most suitable from the *range of packaged products*, on which *advice on investments* is given to the *client* as determined by COB 5.1.7R; and

(b) if there is no *packaged product* in the *firm's* relevant *range of packaged products* which is suitable for the *client*, no recommendation must be made.

(3) In making the recommendation or effecting the transaction in (1), the *firm* must have regard to:

(a) the facts disclosed by the *client*; and

(b) other relevant facts about the *client* of which the *firm* is, or reasonably should be, aware.

~~(2)~~ A *firm* which acts as an *investment manager* for a *private customer* must  
(4) take reasonable steps to ensure that the *private customer's* portfolio or account remains suitable, having regard to the facts disclosed by the *private customer* and any other relevant facts about the *private customer* of which the *firm* is or reasonably should be aware.

~~(3)~~ Where, with the agreement of the *private customer*, a *firm* has pooled his  
(5) funds with those of others with a view to taking common discretionary management decisions, the *firm* must take reasonable steps to ensure that a discretionary transaction is suitable for the *fund*, having regard to the stated *investment objectives* of the fund.

5.3.5A G (1) If circumstances arise in which a *firm* reasonably concludes that there are several *packaged products* in the relevant *range* which would satisfy the test in COB 5.3.5(2)R, it will act in conformity with that *rule* if it recommends only one of those *products*.

(2) If a *client* does not wish to proceed in accordance with a recommendation, a *firm* may nonetheless make further recommendations providing any such recommendation is suitable for the *client* in accordance with the obligation in COB 5.3.5R.

Delete the provisions, COB 5.3.6R to 5.3.8G inclusive, these are not shown struck through.

5.3.6 R ~~[deleted]~~

5.3.7 R ~~[deleted]~~

5.3.8 G ~~[deleted]~~

Suitability of packaged products: out-of-range recommendations

5.3.8A R (1) A *firm* when not selecting *packaged products* from the whole market (and notwithstanding COB 5.3.5R (2)) may recommend a *packaged product* outside the *range of packaged products* on which it provides advice to a particular *client* if the recommended *packaged product* is suitable for the *client* and had it been included would have been at least as suitable as the most suitable *packaged product* in that *range*.

(2) A *firm* must take reasonable steps to ensure that an *appointed representative* of a *firm* only acts as in (1) with its explicit written permission, either generally or in relation to the specific recommendation.

5.3.8B     G    COB 5.3.8AR enables a firm to advise on packaged products from outside a particular range of packaged products. This will enable such advice on investments to be given on a one-off basis by firms which have only one range of packaged products and by other firms which may have more than one but without the firm needing to change the scope or range of the advice on investments which the client is expecting to receive.

Delete the rules, COB 5.3.9R and COB 5.3.10R, these are not shown struck through.

5.3.9        R    [deleted]

5.3.10      R    [deleted]

Requirement for suitability: whole-of-market advisers

5.3.10A    R    (1) A firm which holds itself out as giving personal recommendations to private customers on packaged products from the whole market (or the whole of a sector of that market) must not give any such personal recommendation unless it:

(a) has carried out a reasonable analysis of a sufficiently large number of packaged products which are generally available from the market (or sector of the market); and

(b) conducts the analysis in (a) on the basis of criteria which reflect adequate knowledge of the packaged products generally available from the market as a whole (or from a relevant sector).

(2) A firm in (1) must satisfy the obligation in COB 5.3.5R (2) by taking reasonable steps to ensure that a personal recommendation given to a private customer is:

(a) in accordance with its analysis carried out under (1); and

(b) is the packaged product which on the basis of that analysis is the most suitable to meet the customer's needs.

5.3.10B    R    (1) A firm which holds itself out as giving personal recommendations to intermediate customers or market counterparties on life policies from the whole market (or from a relevant sector) must not give any such personal recommendation unless it:

(a) has carried out an analysis of a sufficiently large number of life policies which are generally available from the market (or sector of the market); and

(b) conducts the analysis in (a) on the basis of criteria which reflect adequate knowledge of the life policies generally available from the market as a whole (or from a relevant sector).



- (2) A firm in (1) must satisfy the obligation in COB 5.3.5R (2) by taking reasonable steps to ensure that a personal recommendation given to a client is :
- (a) in accordance with its analysis carried out under (1); and
  - (b) for a life policy which on the basis of that analysis is suitable to meet the client's needs.

Delete COB 5.3.11G in its entirety, the text of this provision is not shown struck through.

5.3.11 G [deleted]

...

Requirements for suitability letter: other specific requirements

5.3.14 R (1) A firm that gives a personal recommendation, in relation to a life policy, to a person who is a policyholder or a prospective policyholder of a life policy, must provide the person with a suitability letter prior to the conclusion of the contract, unless one of the exceptions in COB 5.3.19R applies.

(2) If, following a personal recommendation by the firm that does not fall within (1), a private customer:

(a)(4) buys, sells, surrenders, converts, cancels, or suspends premiums for or contributions to, a ~~life policy~~, pension contract or a stakeholder pension scheme; or

(b)(2) elects to make income withdrawals;

(c)(3) acquires a holding in, or sells all or part of a holding in, a scheme; or

(d)(4) enters into a pension transfer or pension opt-out from an OPS;

the firm must provide the customer with a suitability letter, within the time period stipulated by COB 5.3.18R, unless one of the exceptions in COB 5.3.19R applies.

...

5.3.16 R The suitability letter in COB 5.3.14R must:

...

(3) ...; ~~and~~

- (4) ...;
- (5) if the recommended product is from a *product provider* (or if relevant, an undertaking in the *immediate group* of that *provider*) which is identified in section 6 of the *firm's initial disclosure document* given in accordance with *COB 4.3.3R(1)*, include the information given in section 6 or in section 6 of the *firm's combined initial disclosure document*; and
- (6) in the case of a recommendation by a *firm* under *COB 5.3.7R* (Suitability of packaged products: out-of-range recommendations) explain why it has recommended a *packaged product* outside the *firm's range of packaged products*, including why it is suitable for the *customer*.

...

- 5.3.18 R The firm must provide the letter required by *COB 5.3.14R (2)* to the *customer*:
- (1) in the case of a *life policy*, *pension contract* or *stakeholder pension scheme*, where...

...

- 5.3.18A R A *firm* may provide a statement of demands and needs to the *client* orally, instead of the *suitability letter* in *COB 5.3.14R*, if:
- (1) the *client* requests it; or
  - (2) immediate cover is necessary;
- but in both cases the *firm* must provide the *suitability letter* immediately after the conclusion of the contract, on a *durable medium*.
- 5.3.18B R If the only contact between the *firm* and the *client* before conclusion of the contract is by telephone, the *suitability letter* must be provided immediately after the conclusion of the contract, on a *durable medium*.

Suitability: intermediate customers and market counterparties

- 5.3.18C R (1) If a *firm* makes a *personal recommendation* to an *intermediate customer* or a *market counterparty* to take out a *life policy*, it must explain to the *client* the reasons for *personally recommending* that *life policy*.
- (2) The explanation required under (1) must:
    - (a) take account of the complexity of the *life policy* proposed; and
    - (b) be provided to the *client* before the contract is concluded.

5.3.18D G A firm should take the following into account when explaining the reasons for a personal recommendation to an intermediate customer or a market counterparty in accordance with COB 5.3.18AR:

- (1) the firm should explain why the client's demands and needs combine to make the recommended contract suitable for the client;
- (2) the firm should not merely state what contract is being recommended with no link to the client's demands and needs;
- (3) a firm that offers contracts from more than one insurance undertaking should include a statement of why a particular insurance undertaking has been recommended; reasons may include contract features not available anywhere else, price, or service levels.

...

5.3.19 R COB 5.3.14R does not apply:

...

- (4) to any personal recommendation by a friendly society for a life policy sold by it ~~a friendly society~~ with a premium not exceeding £50 a year or, if payable weekly, £1 a week;

...

...

5.3.29 G Table Guidance on matters which should be taken into account when assessing the suitability of various personal recommendations. This Table belongs to COB 5.3.13G (4).

Suitability guidance

A Pension transfers and pension opt-outs.

...

Pension Transfers only

- 4. (a) ...
  - (v) enabling the ~~adviser~~ representative to look at other pension options, if available;

...

...

B. Personal pension schemes and FSAVCs compared to Stakeholder Pension Schemes

...

2. ~~Both independent intermediaries and r~~ Representatives will need to undertake the comparison between *personal pension schemes* and *stakeholder pension schemes* and, as required by COB 5.3.16R(3), explain in the *suitability letter* why, if they have recommended a *personal pension scheme*, it is considered to be at least as suitable.

...

4. ~~Both independent intermediaries and r~~ Representatives will need to undertake a comparison between the three options and explain in the *suitability letter* why, if they have recommended an *FSAVC*, it is considered to be at least as suitable as a *stakeholder pension scheme* or the in-house *AVC*.

...

C. Hybrid products

...

2. The requirements for suitability in giving *investment advice* apply to all elements of a hybrid product:
  - (a) ~~independent intermediaries~~ if appropriate, representatives need to scrutinise ready-made packages from a single *product provider* to make sure that each element is competitive and that a better solution is not available by combining elements from different providers;

...

...

G. Contracting out of SERPS

When a *firm* is advising a *customer* on whether to contract out of SERPS in favour of an *appropriate personal pension* or contracted-out *money-purchase scheme* ('COMP'):

- (a) ~~advisers~~ representatives should give careful consideration to:

...

5.3.30 G Table Guidance on the contents of suitability letters

This table belongs to *COB 5.3.17G*

Guidance on the contents of suitability letters

Introduction

...

5. Ideally each *suitability letter* will be different, reflecting the approach of the ~~*adviser representative*~~, the *customer's* profile, subjects discussed and the considerations on which the *advice* was based. ...

Content

6. A *firm* should take the following into account when constructing a *suitability letter*:

...

- (e) ~~*independent intermediaries*~~ where the range of *packaged products* from which *advice on investments* has been given contains the products of more than one *product provider* in respect of the same type of *packaged product*, the letter should include (the list is not exhaustive) why a particular *product provider* has been recommended; reasons may include product features not available elsewhere, price, service levels, performance track record, *investment* prospects, medical evidence terms, reputation and financial strength.

Signing

7. Each *suitability letter* should be signed by a *person* authorised by the *firm* to advise on the type of product which is being recommended. Ideally this will be the ~~*adviser representative*~~ who gave the particular *advice* but, if not, both the signatory and the ~~*adviser representative*~~ should accept responsibility for the letter and the recommendation.

5.5.5 E Table Table of information to be disclosed in written communications

This Table belongs to *COB 5.5.4E*.

Written communications

- (1) Any written communication, including stationery, business cards or other business documentation published by the *firm*, or used by its agents, ~~*representatives, financial advisers*~~ or *introducers*, should include:

...

(b) ~~[deleted]~~ the name of the *firm's marketing group* (if any);

...

(e) ~~[deleted]~~ In the case of a *provider firm*:

(i) a statement that the individual using the communication is the *representative* of, or represents only, the *firm* or its *marketing group*; and

(ii) a brief description, except in the case of business cards, of the *packaged products* and services provided by the *firm* or by members of its *marketing group* including any *adopted packaged products* which the *firm* or an member of the *marketing group* has adopted;

...

(2) ~~[deleted]~~ In the case of a *provider firm*, when the *firm's representative* first meets a *private customer*, the *customer* should be given the following particulars in writing, which may be in the form of a business card, either before progressing beyond the social preliminaries or as soon as reasonably practicable after a telephone conversation has ended:

(a) the name, address and telephone number of the *representative*;

(b) the name, business address and telephone number of the *firm's* branch or office to which the *representative* reports;

(c) the name of the *firm's marketing group* (if any);

(d) a statement that the *firm* is regulated by or authorised by the Financial Services Authority; and

(e) where relevant a statement that the *appointed representative* or *marketing group associate* represents only the specified *firm* or *marketing group* together (except in the case of a business card) with a brief description of the *packaged products* and services provided by that *firm* or *marketing group*, indicating which of those he is appointed to sell.

...

5.5.6 G ~~A firm which gives advice on investments to a private customer about packaged products is reminded of the additional disclosure requirements in COB 5.1 (Polarisation and status disclosure).~~~~[deleted]~~

...

5.6.2 G Principle 6 (Customer's interests) requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly. The purpose of this section is to ensure that the *charges* a *firm* makes to its *private customers* are not excessive. The obligation to disclose to a *private customer* the *charges* that a *firm* intends to make are set out in COB 4.3 (Disclosing information about services, fees and commission – packaged products) and COB 5.7 (Disclosure of charges, remuneration and commission).

...

5.7.4 G (1) A *firm* may make the disclosures required by COB 5.7.3 R in its *terms of business* in a *client agreement*, or in a separate written statement. Disclosure should include any product-related *charges* that are deducted from the *private customer's investment*. If the product is a *packaged product*, product-related *charges* and expenses will be disclosed in the *key features document* or in the minimum information that the *firm* is required to provide to the *private customer* in accordance with COB 6.2 (Provision of key features) and COB 6.4 (Product disclosure: special situations). When a *firm* is a *broker fund adviser*, disclosure should include any *fees* payable to the *firm* or its *associate* in connection with that activity by a *provider firm*. In the case of advice provided in connection with *packaged products* a *firm* should, in accordance with COB 4.3.3 R, have provided its customer with a *fees and commission statement* setting out the maximum rates of any *fees* which the *customer* will pay and/or with an indication of the maximum rates of *commission* (or *equivalent*) which it, or its *representatives*, may retain in connection with the sale of *packaged products*. COB 5.7.3 R does not require any further disclosure of a *firm's fees* if, in accordance with COB 4.3.5 R it has confirmed the exact amount or rate that it will charge.

(2) In addition it is necessary that a *private customer* should, as soon as is practicable, be informed of the exact rate or the exact amount in cash terms of any *commission* (or *equivalent*) which the *firm* or its *representatives* will receive in respect of a specific transaction.

(3) In the case of a *packaged product*, product related charges and expenses will be disclosed in the *key features* document or in the minimum information that the *firm* is required to provide to *private customers* in accordance with COB 6.2 (Provision of key features) and COB 6.4 ( Product disclosure: special situations). When a *firm* is a *broker fund adviser*, disclosure should include any *fees* payable to the *firm* or its *associate* in connection with that activity by a *product provider*.

Delete the text within the existing COB 5.7.5 R and replace with the following text, which is not underlined:

Disclosure of commission (or equivalent) for packaged products

- 5.7.5 R (1) When a *firm* sells, *personally recommends* or arranges the sale of a *packaged product* to a *private customer*, and subsequently on the request of a *private customer*, the *firm* must disclose to the *private customer*, in cash terms:
- (a) any *commission equivalent* payable by it to a *representative* or *appointed representative*; and.
  - (b) any *commission* or *commission equivalent* receivable by it, or by any of its *associates* in connection with the transaction
- unless *COB 5.7.9 R* or *COB 5.7.10 R* applies.
- (2) In (1)(b) a *firm* is, in respect of any transaction, to be regarded as receiving *commission equivalent* if:
- (a) it is received from a *product provider* (“P”), or an *associate* of P; and
  - (b) either P or its *associate* is in the same *immediate group* as the *firm*; and
  - (c) the value of the *commission equivalent* (as assessed in accordance with these *rules*) is greater than the amount of *commission* in cash terms.
- (3) In (1) and (2) “cash terms” in relation to *commission* does not include the value of any indirect benefits which the *firm* may receive in accordance with *COB 2.2*.
- 5.7.6 R In determining the amount to be disclosed as ~~remuneration~~ commission equivalent in accordance with *COB 5.7.5R* a *firm* must put a proper value on the cash payments, benefits and services provided to its ~~employees and agents~~ representatives in connection with the transaction.
- 5.7.7 G ~~[deleted] For an adopted packaged product COB 5.7.6 R includes all cash payments, benefits and services provided by the provider of the adopted packaged product.~~
- 5.7.8 E (1) When determining the value of cash payments, benefits and services under *COB 5.7.6R*, a ~~provider~~-*firm* should follow the provisions of *COB 5.7.16E*.

...



5.7.10 R The requirement in *COB 5.7.5R* to disclose to a *private customer* the amount or value, in cash terms, of ~~remuneration or commission~~ or equivalent does not apply if the *firm* provides the *private customer* with example *key features*, in accordance with *COB 6.2.7R* (Life policies) and *COB 6.2.22R* (Schemes), provided that the *firm* *discloses* to the *private customer* the actual amount of value of ~~remuneration or commission~~ or equivalent within five *business days* of effecting the transaction.

...

5.7.12 G If the precise rate of ~~remuneration~~ or value of *commission* or equivalent is not known in advance, the *firm* should estimate the rate likely to apply to the ~~employee or agent in question~~ representative in respect of the transaction.

5.7.13 G The disclosures required by *COB 5.7.5R* should normally be made in writing. For example, if a specific *key features* document or *projection* is provided to a *private customer*, the required disclosures should either be contained in the *projection* or the *key features* document, or be given to the *private customer*. When a *private customer* does not make a written application to enter into a transaction contemplated by *COB 5.7.5 R*, for example, when the transaction is a telephone *deal* for *units* in a *regulated collective investment scheme*, the *firm* may disclose the amount or value of ~~remuneration or commission~~ or equivalent orally. In these circumstances, the *firm* should give written confirmation as soon as possible after the date of the transaction, and in any event within five *business days*. In preparing its written disclosure statement, a *firm* may wish to follow the *guidance* on content and wording set out in *COB 5.7.17G*.

...

5.7.15 R If the terms of a *packaged product* are varied in circumstances that require the issue of a cancellation notice, a *firm* must disclose to a *private customer* in writing any consequent increase in ~~remuneration or commission~~ or equivalent.

5.7.16 E Table Calculating ~~remuneration~~ commission equivalent

This table forms part of *COB 5.7.8 E*

Calculating ~~remuneration~~ commission equivalent

~~COB 5.7.8E applies only to a firm which is a product provider firm.~~ This table sets out the basis on which the *firm* should determine the value of cash payments, benefits and services to be disclosed as ~~remuneration~~ commission equivalent under COB 5.7.5R. Benefits and services, as set out in parts B and C below, need be included only where their value is such that they could not be provided to ~~an independent intermediary~~ a firm as an indirect benefit under COB 2.2.6G (Packaged products – guidance on indirect benefits) and COB 2.2.7G (Reasonable indirect benefits ~~—joint marketing exercises~~).

The result of the calculation should be that the amounts disclosed as commission equivalent are, as far as possible, the same as the amounts and value of commission which would be paid in a corresponding sale.

#### Part A: Cash payments

1. These cover all payments by a *firm* to a representative, appointed representative or a firm in the same immediate group in relation to a transaction in a *packaged product*, including:
  - (a) payments to any ~~employee or~~ *representative* of the *firm* in respect of the transaction (for example, a manager's override), including any payments from the *firm* to *introducers*;
  - (b) ...
  - (c) that element of any payment made in relation to other business which may be considered to result directly or indirectly from the transaction; for example, any extra element of ~~remuneration~~ commission equivalent payable on the sale of a mortgage which is to be repaid through an *investment* in a *packaged product*;
  - (d) payments resulting directly from business written in previous years (for example, renewal ~~remuneration~~ commission equivalent), which are conditional on the completion of minimum amounts of new business;
  - (e) ...
  - (f) salaries and other payments which do not relate directly to any one transaction, provided they are treated similarly to 'benefits' and 'services' (see paragraph ~~11~~ 14).
2. In determining the amounts to be included in the calculation, a *firm* should have regard to the following:
  - (a) When the precise rate of ~~remuneration~~ commission equivalent is not known in advance ...
  - ...

- (c) When a payment is made before the *firm* receives the *premium* or the investment monies to which it relates (for example, indemnity ~~remuneration~~ commission equivalent), it should be included as being received at the time of payment. If the ~~adviser-representative~~ or the *product provider* wishes to explain this arrangement to the *customer*, he is free to do so, provided this does not detract from the required disclosure.

...

#### Part C Services

5. These include benefits which could not be provided to ~~an independent intermediary a firm, A,~~ as an indirect benefit (under COB 2.2.3R (Prohibition of inducements) and COB 2.2.6G (*Packaged products – guidance on indirect benefits*)), and which ~~the intermediary A~~ would therefore have to fund out of its disclosable *commission*. For those services which can be provided as an indirect benefit, it is not necessary for the *firm* providing the benefit, B, actually to provide services to ~~an independent intermediary another firm, A,~~ for ~~it B~~ to be able to apply this criterion in relation to its *employees, representatives* or agents.
6. The following services should be included:
- (a) ...
- (b) loans where a commercial rate of interest is not charged, including ~~remuneration~~ commission equivalent advances overdue for repayment;
- ...
7. To put a value on these services, the following costs should be included:
- ...
- (h) in respect of ~~marketing group associates a firm in the same immediate group~~ and connected *appointed representatives*, where the name of the company is included in the *direct offer financial promotion*, the costs of any promotion in a newspaper or elsewhere and the provision of ~~representative specific~~ literature specific to the *representative* in connection with a *direct offer financial promotion*.
8. The following costs should be excluded:
- ...
- (g) the costs of head office and branch level management and support, other than payments to *managers* falling under Part 1, for *representatives*, where these services could also be provided to ~~an~~

~~independent intermediary a firm not in the same immediate group,~~  
for example, broker branches consultants and ‘inspectors’;

...

Part D: Calculation methodology ~~actuarial advice~~

9. ~~A long-term insurer or friendly society should take the advice of its appointed actuary (or if does not have one, an actuary) in determining the costs of benefits and services to be included and their apportionment over individual packaged product transactions. Where the firm does not follow its actuary’s advice, it should notify the FSA, giving the reasons for that decision and the alternative assumptions it plans to use.~~

Estimating commission equivalent

The cost of benefits and services should normally be based on the most recent relevant experience of the firm, except where one of the following applies:

- (a) the firm has reasonable grounds to believe that the commission equivalent for the period concerned will be higher than that implied by the experience; or
- (b) the firm has strong grounds to believe that the commission equivalent for the period concerned will be lower than that implied by the experience; or
- (c) no such experience is available.

If any of (a) to (c) applies, the estimate should be based on and evidenced by business plans which the firm is satisfied on reasonable grounds are achievable.

Delete the text COB 5.7.16E (10) to (12) and replace with the following new text for COB 5.7.16E(10) to (19), which is not shown underlined.

10. *Firms* that receive or expect to receive:
- (a) *commission* in respect of *packaged products* which are not its own products or the products of a *product provider* who is in the same *immediate group*; and
  - (b) *commission equivalent* in respect of its own products

must ensure that the costs and benefits attributed to these products do not exceed the amounts that can be financed from that *commission*.

Construction of ~~Remuneration~~ commission equivalent scales

11. The total costs of cash payments, benefits and services should be assessed and the normal approach is to split them into new business costs and after sale servicing costs. The costs of each of these functions should be assessed directly in relation to the work carried out by the *representatives*.
12.
  - (a) The *commission equivalent* costs identified in 11 should be spread across the business using a new business *commission equivalent* scale and a servicing *commission equivalent* scale respectively. The new business *commission equivalent* scales when applied to the total value/volumes of business should reproduce the total new business *commission equivalent* costs, and similarly for the servicing scales.
  - (b) The *commission equivalent* scales should distinguish between products for which the *commission equivalent to representatives* is likely to be different.
13. Where the *representative's commission equivalent* includes a cash payment related to volume and/or value of the transactions sold, the following method would be appropriate:
  - (a) The basic payment scale should comprise a new business payment scale and a servicing payment scale. The cost of benefits and services should be expressed in the form of a new business uplift factor and a servicing uplift factor. So the "new business uplift factor" would be the cost of new benefits and services divided by the new business payments. The "servicing uplift factor" would be the cost of servicing benefits and services divided by servicing payments.
  - (b) The payment scales should be grossed up by new business uplift factors or servicing uplift factors as appropriate to reflect the cost of benefits and services. The grossed up scales represent the new business and servicing *commission equivalent* scales, and are applied to each contract to derive the *commission equivalent* to be disclosed.
  - (c) Where the level of payment in the first year of a policy equals the level of payment in subsequent years then "new business payments" refers to payments in the first year of a contract and "servicing payment" refers to the level of payment in subsequent years.
  - (d) If servicing costs are expected to be incurred in any year in which no servicing payments are to be made on a contract, disclosure should still be made, for example by using a technique similar to that described in 14.

14. (a) When a *representative* receives a salary, or other payment unrelated to volume or sales:
  - (i) this should be amalgamated with the cost of benefits and services; and
  - (ii) the total costs should be apportioned over individual transactions in a way that reflects the value of a contract to a *firm* or the *firm's immediate group*.
- (b) Where a *firm* is a distributor for a *product provider* within the same *immediate group*, the *firm* must apportion total costs over individual transactions in a way that reflects the value of the contract to the *firm's immediate group*.
15. Where other methods of *commission equivalent* are employed, for example, part salary and part related to the volume/value of the sale, the salary element should be added to the cost of benefits and services and the method in 13 should be used.
16. Where a *representative* agrees to forgo part of his or her normal payment to improve the terms of the contract, the same uplift factor (in line with 13(a)) may be applied to the reduced payment, or the same monetary cost of benefits and services may be used, subject to the following constraints:
  - (a) the same uplift factor approach should only be adopted if the *customer* will also receive the full benefit of the lower of:
    - (i) the reduction in the amount of disclosed *commission equivalent* for non-financial benefits and services; and
    - (ii) an equivalent proportion of the policy loadings intended to cover non-financial benefits and services.
  - (b) Where the 'same uplift factor' approach is adopted, the proportion of payments foregone must be allowed for in calculating the uplift factor.
  - (c) Where an average scale of *commission equivalent* is used, the percentage reduction in payment in respect of the individual *representative* may be applied to the average payment in order to calculate the reduced payment.
17. The *firm* should review the *commission equivalent* scales if at any time it becomes aware that the *commission equivalent* figures have become misleading. A review should take place at least annually.

18. When an identical *commission equivalent* scale applies to all *representatives* (although they might earn differing percentages of it), the same average amount of *commission equivalent* (and the value of other benefits and services) in respect of identical transactions may be disclosed, regardless of the percentage of the scale paid to each individual *representative*. Averaging may be used for *representatives* on the same scale and *employees of firms* in the same *immediate group*, but not *appointed representatives*.

Payments to associates

19. Where a *firm* pays *commission equivalent* to a another *firm* in the same *immediate group*, or an *appointed representative* which is an *associate* of the *firm*, it should ensure that the calculation of the sum to be disclosed is the higher of:
- (a) all payments, benefits and services provided to the *firm* or *appointed representative*, from whatever source, plus an additional allowance for profit of 15% - unless the *firm* can demonstrate that another figure (higher or lower) is more appropriate; and
  - (b) the cash payments actually paid by the *firm*, plus the value of services provided.

...

- 6.2.9\*\* R (1) *COB 6.2.7R* does not apply to a *product provider* when its *life policy* is sold on the *personal recommendation* of, or arranged to be sold by, ~~an independent intermediary or marketing group associate~~ another firm.

...

...

- 6.2.11\*\* G An adequate oral explanation of the information required by *COB 6.2.9R (2)* should include the following:

...

- (4) where it is the case, the fact that *commission* or *commission equivalent* will be paid to the ~~adviser~~ *or representative*; and

...

...

6.2.19\*\* R (1) *COB 6.2.16R and COB 6.2.18R do not apply to a product provider when the variation to its life policy is effected on the personal recommendation of or arranged to be sold by an independent intermediary or marketing group associate another firm.*

...

...

Provision of key features: Schemes

6.2.22 R When a firm sells, personally recommends or arranges for the sale of a scheme to a private customer:

*the firm must, unless COB 6.2.24R (exceptions) or COB 6.4.27R to COB 6.4.31R (telephone sales and other exemptions) applies, provide the private customer with appropriate key features for the scheme before he completes an application for the scheme holding; or*

6.2.23\*\* G ...

(3) An adequate oral explanation of the information required by *COB 6.2.22R* should include the following:

...

(e) where it is the case, that *commission* or remuneration will be paid to the ~~adviser or representative~~; and

...

...

6.2.25\*\* R *COB 6.2.22R does not apply to a product provider when the scheme holding is sold on the personal recommendation of, or arranged to be sold by, an independent intermediary or marketing group associate another firm.*

...

*Commission and remuneration commission equivalent* for life policies, schemes and stakeholder pension schemes

6.5.38 R ....

(2) (a) the amount or value in cash terms of the *commission or remuneration equivalent*, and an indication of the timing of these payments; and



- (b) a statement that *commission* or ~~remuneration~~ *equivalent* is paid for out of ‘the deductions or charges, if more appropriate’ and, if applicable, that the amount will depend on the size of the premium or contribution and the length of the *life policy, scheme* or *stakeholder pension scheme* term.

6.5.39 G ~~The information given under~~ *COB 6.5.38 R (2)* may include the name of the *adviser representative* to whom the *commission* or ~~remuneration~~ *equivalent* is to be paid ~~may be given.~~

...

6.5.46 R The post-sale confirmation to be given to *private customers* in accordance with *COB 6.3.3 R* must include:

- (1) the information required by *COB 6.5.15 R - COB 6.5.19 R* (an Example), *COB 6.5.23 R* to *COB 6.5.28 R* (Tables and Deductions Summary) and *COB 6.5.38 R* (Commission and ~~Remuneration~~ *commission equivalent*);
- (2) ~~where the investment has been recommended to a private customer by a representative, a statement under the heading ‘adviser’s status’ that: ‘the person who advised you about this policy represents only [Name of firm, or, if appropriate, marketing group associate.]’~~

...

6.6.7 R ~~An independent intermediary~~ A firm must, in addition to complying with other rules in this section, ensure that a *projection* given to a particular *customer* is relevant to that *customer’s* circumstances.

...

6.7.1 R *COB 6.7* applies to:

- (1) a *product provider*;
- (2) an *insurer* which provides *pure protection contracts*;
- (3) ~~An independent intermediary~~ a firm when acting as an *EIS manager, ISA manager* or *plan manager*, or when selling on to a *customer units* which the *firm* has bought or redeemed as *principal* for that purpose;

...

6.7.16 R Table Notes to cancellable investment agreements - life  
  
This table belongs to *COB 6.7.15 R*

...

2. Multiple agreements: Where a *customer* enters into a set of *investment agreements* at the same time (for example, the different components held within a *maxi-ISA* and with the same *firm*) (~~or another person in the same marketing group as that firm~~), and that set ...

...

6.7.17 R Table Cancellable investment agreements - non-life

This table belongs to *COB 6.7.7 R (1)* and *COB 6.7.14 R (1)*

...

Column 1

Column 2

...

...

C. Subscriptions (see notes 1 and 2 in *COB 6.7.18R*) which can be invested only in units (whether or not held within an *ISA*, *PEP* or *pension contract*) to an *AUT* or *ICVC* purchased from the:

2. The agreement is entered into with the *firm* (~~and where relevant with any independent intermediary firm which arranged the transaction~~) as an *execution-only transaction* (unless note 4 in *COB 6.7.18R* applies).

(a) the operator; or

(b) its ~~marketing group~~ associate acting as an *ISA manager* or *plan manager*.

...

...

6.7.18 R Table Notes to cancellable investment agreements - non-life

This Table belongs to *COB 6.7.17 R*

...

2. Multiple agreements: Where a *customer* enters into a set of *investment agreements* at the same time (for example, the different components held within a *maxi-ISA* and with the same *firm*) (~~or another person in the same marketing group as that firm~~), and that set ...

...

11.3 ~~Polarisation~~ Packaged products  
(Title)

...

Sch 1 Record keeping requirements

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...	...	...	...	...
<i>COB 5.1.4R(3)</i>	Adoption of a packaged product	Decision to adopt	On making the decision to adopt	Throughout the period the adoption remains in effect and for 6 years thereafter
<u>COB 4.3.9 R</u>	<u>Fees and commission statement</u>	<u>Fees and commission statement</u>	<u>At the time a firm sets its fees and commission statements</u>	<u>6 years from the date on which the record is superseded by a more up-to-date record</u>
<u>COB 5.1.6CR</u>	<u>The scope and range (or ranges) of advice each of the firm's appointed representatives is permitted to give</u>	<u>The scope of advice and range (or ranges) of packaged products in respect of which an appointed representative is permitted to advise.</u>	<u>At the time the appointed representative is appointed and on each change to the permitted scope and range (or ranges) of advice</u>	<u>6 years from the date on which the record is superseded by a more up-to-date record</u>

<u>COB 5.1.6FR</u>	<u>Range of packaged products</u>	<u>Range of packaged products</u>	<u>When the range changes</u>	<u>6 years from the date on which the record is superseded by a more up-to-date record</u>
...	...	...	...	...

## Annex C

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex underlining indicates new text and strikethrough indicates text to be deleted

#### ICOB Transitional Rules

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
8	<i>ICOB</i> 4.2.4G(1)	G	Until 31 May 2005, the reference in <i>ICOB</i> 4.2.4G <del>(1)</del> to the <i>initial disclosure document</i> set out in <i>ICOB</i> 4 Ann 1G <u>and the combined initial disclosure document set out in <i>ICOB</i> 4 Ann 2R</u> includes an <i>initial disclosure document</i> which complies with <i>ICOB</i> 4 Ann 1G and a <i>combined initial disclosure document</i> which complies with <i>ICOB</i> 4 Ann <u>2R</u> in the Insurance: Conduct of Business Sourcebook Instrument 2004 (FSA 2004/06).	14 January 2005 – 31 May 2005	Already in force

ICOB 4 Annex 1 G: Initial disclosure document (“IDD”)

...

The following notes do not form part of the IDD

...

#### Section 6: Ownership

Note 22 – the *insurance intermediary* should omit this section where there is no relevant ownership arrangements under the following notes or the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections should be renumbered accordingly. Where the information is provided by an appointed representative, it must cover holdings in or held by that appointed representative, as appropriate.

...

ICOB 4 Annex 2 R: Combined initial disclosure document (“CIDD”)\*\*

This Annex belongs to *ICOB 4.2.7R(1)*.

This specimen covers services in relation to *packaged products, non-investment insurance contracts* and *regulated mortgage contracts* (including *regulated lifetime mortgage contracts* and home reversion schemes). If the *firm* is only providing services in relation to two types of these products, the parts of the CIDD that are not relevant must be omitted. *Firms* must omit the notes and square brackets that appear in the following CIDD. The CIDD must contain the keyfacts logo, headings and text in the order shown and in accordance with the notes. **[Note 1]**

---

**keyfacts** | about our services [Note 2]

**XYZ** Financial Services

**[Note 5]**  
[123 Any Street  
Some Town  
ST21 7QB]

**[Note 3] [Note 4]**

---

---

1 The Financial Services Authority (FSA)

---

The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

---

2 Whose products do we offer? [Note 6] [Note 7]

---

**Investment**

- We offer products from the whole market. **[Note 6A]**
- We [can] **[Note 8]** only offer products from a limited number of companies.

Ask us for a list of the companies and products we offer. **[Note 12]**

- We [can] **[Note 8]** only offer [a] ~~[a limited range of the]~~ product[s] from [a single group of companies] [name of single company]. **[Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own products.

Ask us for a list of the companies and products we offer. **[Note 12]**

- ~~[We will advise you about group personal pensions.]~~

**Insurance**

- We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].
- We [can] **[Note 8]** only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. **[Note 12]**

- We [can] **[Note 8]** only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. **[Note 9] [Note 10(1)] [Note 13]**

[or] **[Note 10(2)]**

We only offer our own products for [list the types of *non-investment insurance contracts*].

**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We offer mortgages from the whole market.
- We [can] **[Note 8]** only offer mortgages from a limited number of lenders.

Ask us for a list of the lenders we offer mortgages from. **[Note 11]**

- We [can] **[Note 8]** only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender]. **[Note 10(1)]****[Note 13]**

[or] **[Note 10(2)]**

We only offer our own mortgages.

---

### **3 Which service will we provide you with? [Note 6]**

---

#### **Investment**

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.
- We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances but we will not:
- Conduct a full assessment of your needs;
  - Offer advice on whether a non-stakeholder product may be more suitable

**[Note 6A]**

#### **Insurance**

- We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].
- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.



**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

---

**4 What will you have to pay us for our services?**

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**Investment**

- Before we provide you with advice, we will give you our keyfacts guide 'about the cost of our services'. **[Note 15]**
- We will tell you how we get paid, and the amount, before we carry out any business for you.

**Insurance [Note 16]**

- A fee [of £ [ ] ] [for] [list the types of services provided for *non-investment insurance contracts*].
- No fee [for] [list the types of services provided for *non-investment insurance contracts*].

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- No fee. [We will be paid by commission from the [lender/company].] **[Note 17]**
- A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] mortgage [or home reversion scheme]. [We will also be paid commission from the [lender/company].] **[Note 17] [Note 18]**

You will receive a keyfacts illustration when considering a particular [lifetime] mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. **[Note 14]**

**Refund of fees [Note 19] [Note 14]**

If we charge you a fee, and your [lifetime] mortgage [or home reversion scheme] does not go ahead, you will receive:

**[Note 20]**

- A full refund [if the [lender/company] rejects your application]. **[Note 21]**
- A refund of £ [ ] [if your application falls through]. **[Note 21]** **[Note 22]**
- No refund [if you decide not to proceed]. **[Note 21]**

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**5 Who regulates us? [Note 23]**

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[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] **[Note 24]** **[Note 25]** is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. **[Note 26]**

Our permitted business is [ ]. **[Note 27]**

[or] **[Note 28]**

[Name of *appointed representative*] **[Note 3]** **[Note 4]** is an appointed representative of [name of *firm*] [address of *firm*] **[Note 24]** **[Note 25]** which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] **[Note 27]**

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

[Home reversion schemes are not regulated by the FSA.] **[Note 14]**

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**6 Loans and ownership [Note 29]**

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[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.] **[Note 29]****[Note 30]****[Note 31]****[Note 32]****[Note 33]****[Note 34]**

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**7 What to do if you have a complaint [Note 23]**

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234]. [Note 35]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 36] [Note 36A] [Note 37] [The Financial Ombudsman Service does not consider complaints about home reversion schemes.] [Note 14]

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**8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 23] [Note 38] [Note 38A]**

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

**Investment**

Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.

**Insurance**

Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.

[or] [Note 39] [Note 39A]

For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.

**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

Mortgage advising and arranging is covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000. [Home reversion schemes are not covered by the Financial Services Compensation Scheme.] [Note 14]

Further information about compensation scheme arrangements is available from the FSCS.

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*9 — Group personal pensions [Notes 40, 41 and 42]*

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*This meeting has been arranged so that we can provide you with [information about] [advice upon whether or not you should join] the Group Personal Pension scheme which your employer has established. You should be aware that we cannot advise upon or recommend any other specific investment products during this meeting.*

**[Note 403] Message from the Financial Services Authority**

**Think carefully about this information before deciding whether you want to go ahead.**

**If you are at all unsure about which lifetime mortgage or home reversion scheme is right for you, you should ask your adviser to make a recommendation.**

**Please remember that home reversion schemes are not regulated by the FSA.**

The following notes do not form part of the CIDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common keyfacts logo to be used on significant pieces of information directed to *customers*. ~~ICOB 4.2.6R sets out the requirements on the use of the key facts logo.~~ The keyfacts logo and the text 'about our services' must be used and positioned as shown in the CIDD. The logo may be re-sized, but it must be reasonably prominent and its proportions must not be distorted. When reproducing the logo, firms may use colour providing this does not diminish the prominence of the logo. A specimen of the keyfacts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the CIDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – for services in relation to *packaged products* and *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes the *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. For services in relation to *non-investment insurance contracts*, the *firm* must select more than one box if the scope of the service or the type of service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance or if it provides *advice* on some types of contract but not others. In the case where more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to

the CIDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 6A** – if a *firm* indicates that it will be providing *basic advice on stakeholder products* then the first box in section 2 must not be ticked as the *firm* will not be doing so on the basis of *advice on investments* from the whole market.

**Note 7** - if the CIDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with COB 5, ICOB 4.2.8R note 1(e) and MCOB 4.3.10R.

**Note 8** – insert “can” if the *firm*'s range of products is determined by any contractual obligation. This does not apply where a *product provider, insurer, lender* or company is selling its own products.

**Note 9** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the CIDD. This only needs to be done in relation to the service it is offering a particular *customer*. For example, “we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance”.

**Note 10** – if the *firm* selects this box, it will be offering the products of one provider to the *customer* for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*. If the *firm* does not select this box, then the text must follow that set out in note 13 below.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the lender for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the company for home reversion schemes. For example: "We can only offer products from [name of *product provider*]". For *non-investment insurance contracts* the type of insurance offered should also be included. For example: "We only offer XYZ's household insurance and ABC's motor insurance." If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a mortgage from [name of lender]". If the *firm* does not offer all of the ~~*packaged products*~~ or mortgages or home reversion schemes generally available from that provider, it must insert the words "a limited range of" as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part's trading name, it should use this alternative text.

**Note 11** – for services provided in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes, this sentence is required only where a firm selects this service option. It may also be omitted if a the firm chooses to list all of the ~~companies~~ lenders it offers mortgages from instead of the text "a limited number of lenders", in the previous line, so long as the *firm* offers all of the products generally available from each ~~provider~~ lender.

**Note 12** – this sentence is required only where a firm selects this service option. For services provided in relation to *packaged products*, the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOB 4.2.14R*.

**Note 13** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies" for *packaged products*, "a single insurer" for *non-investment insurance contracts*, "a single lender" for *regulated mortgage contracts* or *regulated lifetime mortgage contracts* and "a single company" for home reversion schemes. For example: "We only offer the products from a single group of companies" should replace the text in the specimen CIDD.

**Note 14** – change “mortgage” to “lifetime mortgage” where the *firm* sells only *regulated lifetime mortgage contracts*. *Firms* must insert the text relating to home reversion schemes and change “mortgage” to “product” and “lender” to “company” if they advise or give personalised information on home reversion schemes in addition to *advising* or giving personalised information on *regulated lifetime mortgage contracts*.

#### **Section 4: What will you have to pay us for our services?**

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate "keyfacts guide to the costs of services" (i.e. a menu) if they propose to give that *customer advice* on *packaged products*. Where a *firm* is not required to provide that *customer* with a menu because the *firm* does not intend to give him advice on *packaged products*, ~~the firm may omit the part of section 4 of the CIDD that relates to packaged products~~ then it should tick the second box in section 4.

**Note 16** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* or *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'. If the firm is offering more than one type of service in connection with non-investment insurance contracts, the firm may aggregate the fees over all the services provided, and (if that is the case) identify the services for which there is no fee.

**Note 17** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer* for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes, it must insert a plain language

explanation of this (see specimen for a plain language example). If the firm will pay over to the customer any commission the firm receives, it may refer to that fact here.

**Note 18** – insert a plain language description of when any *fees* are payable for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If a *firm* offers more than one pricing option, it may illustrate each with a separate box. If a firm does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

**Note 19** – omit this part of the CIDD on 'Refund of fees' if the *firm* has indicated that there will be "No fee" for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes or that any fee will be payable only if the product completes.

**Note 20** – *firms* may select as many boxes as appropriate.

**Note 21** – insert a short, plain language description of the circumstances in which the *fee* for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes is refundable or not refundable as described.

**Note 22** – a *firm* may delete this line if it does not offer a partial refund for services in relation to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes in any circumstances.

### **Section 5: Who regulates us?**

**Note 23** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information including the *firm's permitted business*. This section may be omitted for services relating to *non-investment insurance contracts* if the *firm* provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. This section may be omitted for services relating to *regulated mortgage contracts* (including *regulated lifetime mortgage contracts*) and home reversion schemes in accordance with *MCOB 4.4.1R(3)*. If this section is omitted, the other sections of the CIDD must be renumbered accordingly.

**Note 24** – if the *firm's* address on the *FSA Register* differs from that given on the CIDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 25** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 26** - an *incoming EEA firm* will need to modify this section if it chooses to use this CIDD (see *GEN 4 Ann 1R(2)*).

**Note 27** – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 28** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

## **Section 6: Loans and ownership**

**Note 29** – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the CIDD must be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section must be changed to 'Ownership'. Where the information is provided by an *appointed representative*, it must cover loans made to or by that *appointed representative* or holdings in, or held by, that *appointed representative* as appropriate.

**Notes 30, 31 and 32** apply only to a *firm* *advising on, dealing in, or arranging* in relation to *packaged products* ~~for private customers~~.

**Note 30** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 31** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 32** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

**Notes 33 and 34** apply to an *insurance intermediary* that is not an *insurer* providing services in relation to *non-investment insurance contracts*.

**Note 33** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.



**Note 34** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

**Section 7: What to do if you have a complaint**

**Note 35** – if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 36** – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

**Note 36A** – if the CIDD is provided by an *authorised professional firm* which is exclusively carrying on *non-mainstream regulated activities*, the *authorised professional firm* should delete this sentence and refer to the alternative complaints handling arrangements. It should also omit the information required under note 14.

**Note 37** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

**Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 38** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 38A** - when a *firm* which is not a *participant firm* provides the CIDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained. It should also omit the information required under note 14.

**Note 39** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it must use this alternative text.

**Note 39A** – where the *insurance intermediary* provides a service in relation to a contract which covers both a compulsory class of insurance and a class of insurance which is not compulsory, it should indicate the level of compensation that applies to each class.

**Section 9: Group personal pensions**

~~**Note 40** – *firms* should only include section 9 if they intend to give information about, or advise on, the opportunity for *employees* to join a *group personal pension scheme* established by their employer. In all other cases it should be omitted entirely.~~

~~**Note 41** – the words in square brackets should be omitted or included, as appropriate, depending upon whether the *firm* is *advising employees* whether or not to join a *group*~~

*personal pension scheme*, or merely providing them with factual information about the scheme.

**Note 42**—although *firms* must not use the occasion of a meeting to discuss a *group personal pension scheme* as an opportunity to give advice on other *designated investments*, this does not preclude the provision of *advice on non investment insurance contracts, regulated mortgage contracts or regulated lifetime mortgage contracts*. A *firm* may also, when giving *advice on a group personal pension scheme*, suggest that a further meeting be arranged to discuss *designated investments* and if so must provide a further appropriate IDD or CIDD.

### **Lifetime mortgage warning**

**Note 403** - This warning box should be added when the *firm* sells *regulated lifetime mortgage contracts* or home reversion schemes or both.

## Annex D

### Amendments to the Mortgages: Conduct of Business sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

#### MCOB 4 Annex 2 R: Combined initial disclosure document (“CIDD”)\*\*

This Annex belongs to MCOB 4.4.1R(1).

This specimen covers services in relation to *packaged products, non-investment insurance contracts* and *regulated mortgage contracts* (including *regulated lifetime mortgage contracts* and home reversion schemes). If the *firm* is only providing services in relation to two types of these products, the parts of the CIDD that are not relevant must be omitted. *Firms* must omit the notes and square brackets that appear in the following CIDD. The CIDD must contain the keyfacts logo, headings and text in the order shown and in accordance with the notes. [Note 1]

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about our services [Note 2]



[Note 5]  
[123 Any Street  
Some Town  
ST21 7QB]

[Note 3] [Note 4]

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#### 1 The Financial Services Authority (FSA)

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The FSA is the independent watchdog that regulates financial services. It requires us to give you this document. Use this information to decide if our services are right for you.

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#### 2 Whose products do we offer? [Note 6] [Note 7]

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##### Investment

- We offer products from the whole market. [Note 6A]
- We [can] [Note 8] only offer products from a limited number of companies.

Ask us for a list of the companies and products we offer. [Note 12]

We [can] [**Note 8**] only offer [a] [~~a limited range of the~~] product[s] from [a single group of companies] [name of single company]. [**Note 10(1)**] [**Note 13**]

[or] [**Note 10(2)**]

We only offer our own products.

Ask us for a list of the companies and products we offer. [**Note 12**]

[~~We will advise you about group personal pensions.~~]

### Insurance

We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].

We [can] [**Note 8**] only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. [**Note 12**]

We [can] [**Note 8**] only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. [**Note 9**] [**Note 10(1)**] [**Note 13**]

[or] [**Note 10(2)**]

We only offer our own products for [list the types of *non-investment insurance contracts*].

### [Lifetime] Mortgages [and home reversion schemes] [**Note 14**]

We offer mortgages from the whole market.

We [can] [**Note 8**] only offer mortgages from a limited number of lenders.

Ask us for a list of the lenders we offer mortgages from. [**Note 11**]

We [can] [**Note 8**] only offer [a limited range of the] [a] mortgage[s] from [a single lender] [name of single lender]. [**Note 10(1)**][**Note 13**]

[or] [**Note 10(2)**]

We only offer our own mortgages.

## 3 Which service will we provide you with? [**Note 6**]

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## Investment

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.
- We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances but we will not:
- Conduct a full assessment of your needs;
  - Offer advice on whether a non-stakeholder product may be more suitable

### [Note 6A]

## Insurance

- We will advise and make a recommendation for you after we have assessed your needs [for] [list the types of *non-investment insurance contracts*].
- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

## **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

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## **4 What will you have to pay us for our services?**

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## Investment

- Before we provide you with advice, we will give you our keyfacts guide 'about the cost of our services'. **[Note 15]**

- We will tell you how we get paid, and the amount, before we carry out any business for you.

### **Insurance [Note 16]**

- A fee [of £ [ ] ] [for] [list the types of services provided for non-investment insurance contracts].
- No fee [for] [list the types of services provided for non-investment insurance contracts].

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

### **[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

- No fee. [We will be paid by commission from the [lender/company].] [Note 17]
- A fee of £[ ] payable at the outset and £[ ] payable when you apply for a [lifetime] mortgage [or home reversion scheme]. [We will also be paid commission from the [lender/company].] [Note 17] [Note 18]

You will receive a keyfacts illustration when considering a particular [lifetime] mortgage, [or further information about a particular home reversion scheme] which will tell you about any fees relating to it. [Note 14]

### **Refund of fees [Note 19] [Note 14]**

If we charge you a fee, and your [lifetime] mortgage [or home reversion scheme] does not go ahead, you will receive:

#### **[Note 20]**

- A full refund [if the [lender/company] rejects your application]. [Note 21]
- A refund of £ [ ] [if your application falls through]. [Note 21] [Note 22]
- No refund [if you decide not to proceed]. [Note 21]

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## **5 Who regulates us? [Note 23]**

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[XYZ Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 24] [Note 25] is authorised and regulated by the Financial Services Authority. Our FSA Register number is [ ]. [Note 26]

Our permitted business is [ ]. [Note 27]

[or] [Note 28]

[Name of *appointed representative*] [Note 3] [Note 4] is an appointed representative of [name of *firm*] [address of *firm*] [Note 24] [Note 25] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [ ].

[Name of *firm's*] permitted business is [ ] [Note 27]

You can check this on the FSA's Register by visiting the FSA's website [www.fsa.gov.uk/register](http://www.fsa.gov.uk/register) or by contacting the FSA on 0845 606 1234.

[Home reversion schemes are not regulated by the FSA.] [Note 14]

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## 6 Loans and ownership [Note 29]

---

[B&C Investments plc owns 20% of our share capital.]

[London Union plc provides us with loan finance of £250,000 per year.]

[XYZ Financial Services (or we) have 20% of the voting rights in Royal Edinburgh.]  
[Note 29][Note 30][Note 31][Note 32][Note 33][Note 34]

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## 7 What to do if you have a complaint [Note 23]

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If you wish to register a complaint, please contact us:

**...in writing** Write to [XYZ Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

**... by phone** Telephone [0121 100 1234]. [Note 35]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 36] [Note 36A] [Note 37] [The Financial Ombudsman Service does not consider complaints about home reversion schemes.] [Note 14]

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## 8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 23] [Note 38] [Note 38A]

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We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

### Investment

*Most types of investment business are covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000.*

### Insurance

***Insurance advising and arranging is covered for 100% of the first £2,000 and 90% of the remainder of the claim, without any upper limit.***

*[or] [Note 39] [Note 39A]*

***For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.***

**[Lifetime] Mortgages [and home reversion schemes] [Note 14]**

***Mortgage advising and arranging is covered for 100% of the first £30,000 and 90% of the next £20,000 so the maximum compensation is £48,000. [Home reversion schemes are not covered by the Financial Services Compensation Scheme.] [Note 14]***

***Further information about compensation scheme arrangements is available from the FSCS.***

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*9 — Group personal pensions [Notes 40, 41 and 42]*

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***~~This meeting has been arranged so that we can provide you with [information about] [advice upon whether or not you should join] the Group Personal Pension scheme which your employer has established. You should be aware that we cannot advise upon or recommend any other specific investment products during this meeting.~~***

***[Note 40~~3~~] Message from the Financial Services Authority***

***Think carefully about this information before deciding whether you want to go ahead.***

***If you are at all unsure about which lifetime mortgage or home reversion scheme is right for you, you should ask your adviser to make a recommendation.***

***Please remember that home reversion schemes are not regulated by the FSA.***



The following notes do not form part of the CIDD.

**Note 1** – subject to this, a *firm* may use its own house style and brand.

**Note 2** – the *Financial Services Authority* has developed a common keyfacts logo to be used on significant pieces of information directed to *customers*. ~~ICOB 4.2.6R sets out the requirements on the use of the key facts logo.~~ The keyfacts logo and the text 'about our services' must be used and positioned as shown in the CIDD. The logo may be re-sized, but it must be reasonably prominent and its proportions must not be distorted. When reproducing the logo, firms may use colour providing this does not diminish the prominence of the logo. A specimen of the keyfacts logo can be obtained from the *FSA* website [http://www.fsa.gov.uk/pubs/other/keyfacts\\_logo](http://www.fsa.gov.uk/pubs/other/keyfacts_logo).

**Note 3** – insert the *firm's* or *appointed representative's* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included.

**Note 4** – if an individual who is employed or engaged by an *appointed representative* provides the information, the individual should not put his or her own name on the CIDD.

**Note 5** – insert the head office or if more appropriate the principal place of business from which the *firm* or *appointed representative* expects to conduct business (this can include a *branch*) with *customers*. (An *appointed representative* must not include the name and address of the *authorised firm* instead of its own.)

## **Section 2: Whose products do we offer?**

**Note 6** – for services in relation to *packaged products* and *regulated mortgage contracts*, *regulated lifetime mortgage contracts* and home reversion schemes the *firm* must select, for example by ticking, one box which is appropriate for the service which it expects to provide to the *customer*. For services in relation to *non-investment insurance contracts*, the *firm* must select more than one box if the scope of the service or the type of service it provides to a particular *customer* varies by type of contract. For example, if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance or if it provides *advice* on some types of contract but not others. In the case where more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the CIDD. This needs to be done only in relation to the service it is offering to a particular *customer*.

**Note 6A** – if a *firm* indicates that it will be providing *basic advice on stakeholder products* then the first box in section 2 must not be ticked as the *firm* will not be doing so on the basis of *advice on investments* from the whole market.

**Note 7** - if the CIDD is provided by an *appointed representative*, the service described must be that offered by the *appointed representative*, in accordance with *COB 5*, *ICOB 4.2.8R* note 1(e) and *MCOB 4.3.10R*.

**Note 8** – insert “can” if the *firm’s* range of products is determined by any contractual obligation. This does not apply where a *product provider, insurer, lender* or company is selling its own products.

**Note 9** – if the *insurance intermediary* deals with a different *insurance undertaking* for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the CIDD. This only needs to be done in relation to the service it is offering a particular *customer*. For example, “we can only offer products from ABC Insurance for motor insurance and XYZ Insurance for household insurance”.

**Note 10** – if the *firm* selects this box, it will be offering the products of one provider to the *customer* for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*. If the *firm* does not select this box, then the text must follow that set out in note 13 below.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the lender for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the company for home reversion schemes. For example: "We can only offer products from [name of *product provider*]". For *non-investment insurance contracts* the type of insurance offered should also be included. For example: "We only offer XYZ's household insurance and ABC's motor insurance." If the provider has only one product, the *firm* must amend the text to the singular – for example: "We can only offer a mortgage from [name of lender]". If the *firm* does not offer all of the ~~*packaged products*~~ or mortgages or home reversion schemes generally available from that provider, it must insert the words "a limited range of" as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part’s trading name, it should use this alternative text.

**Note 11** – for services provided in relation to *regulated mortgage contracts, regulated lifetime mortgage contracts* and home reversion schemes, this sentence is required only where a *firm* selects this service option. It may also be omitted if a ~~the~~ *firm* chooses to list all of the ~~companies~~ lenders it offers mortgages from instead of the text "a limited number of lenders", in the previous line, so long as the *firm* offers all of the products generally available from each ~~provider~~ lender.

**Note 12** – this sentence is required only where a *firm* selects this service option. For services provided in relation to *packaged products*, the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *customer*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOB 4.2.14R*.

**Note 13** – if the *firm* does not select this box, it must alter the wording to say "a single group of companies" for *packaged products*, "a single insurer" for *non-investment insurance contracts*, "a single lender" for *regulated mortgage contracts* or *regulated lifetime mortgage contracts* and "a single company" for home reversion schemes. For example: "We only offer the products from a single group of companies" should replace the text in the specimen CIDD.

**Note 14** – change “mortgage” to “lifetime mortgage” where the *firm* sells only *regulated lifetime mortgage contracts*. *Firms* must insert the text relating to home reversion schemes and change “mortgage” to “product” and “lender” to “company” if they advise or give personalised information on home reversion schemes in addition to *advising* or giving personalised information on *regulated lifetime mortgage contracts*.

#### **Section 4: What will you have to pay us for our services?**

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate "keyfacts guide to the costs of services" (i.e. a menu) if they propose to give that *customer advice* on *packaged products*. Where a *firm* is not required to provide that *customer* with a menu because the *firm* does not intend to give him advice on packaged products, ~~the firm may omit the part of section 4 of the CIDD that relates to packaged products~~ then it should tick the second box in section 4.

**Note 16** – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* or *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to 'A fee'. If the firm is offering more than one type of service in connection with non-investment insurance contracts, the firm may aggregate the fees over all the services provided, and (if that is the case) identify the services for which there is no fee.

**Note 17** – if the *firm* receives commission instead of, or in addition to, *fees* from the *customer* for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes, it must insert a plain language explanation of this (see specimen for a plain language example). If the firm will pay over to the customer any commission the firm receives, it may refer to that fact here.

**Note 18** – insert a plain language description of when any *fees* are payable for services relating to *regulated mortgage contracts*, *regulated lifetime mortgage contracts* or home reversion schemes. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount must be included. If a *firm* offers more than one pricing option, it may illustrate each with a separate box. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to 'A fee'.

**Note 19** – omit this part of the CIDD on ‘Refund of fees’ if the *firm* has indicated that there will be “No fee” for services in relation to *regulated mortgage contracts, regulated lifetime mortgage contracts* or home reversion schemes or that any fee will be payable only if the product completes.

**Note 20** – *firms* may select as many boxes as appropriate.

**Note 21** – insert a short, plain language description of the circumstances in which the *fee* for services in relation to *regulated mortgage contracts, regulated lifetime mortgage contracts* or home reversion schemes is refundable or not refundable as described.

**Note 22** – a *firm* may delete this line if it does not offer a partial refund for services in relation to *regulated mortgage contracts, regulated lifetime mortgage contracts* or home reversion schemes in any circumstances.

### **Section 5: Who regulates us?**

**Note 23** – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *customer*, provided the *customer* with its *terms of business* which contains that information including the *firm’s permitted business*. This section may be omitted for services relating to *non-investment insurance contracts* if the *firm* provides the information covered by this section where it is required by *ICOB 4.2.8R* to the *customer* by some other means. This section may be omitted for services relating to *regulated mortgage contracts* (including *regulated lifetime mortgage contracts*) and home reversion schemes in accordance with *MCOB 4.4.1R(3)*. If this section is omitted, the other sections of the CIDD must be renumbered accordingly.

**Note 24** – if the *firm’s* address on the *FSA Register* differs from that given on the CIDD under note 5, the address on the *FSA Register* must be given in this section. If the address is the same as that given under note 5 it should be repeated in this section.

**Note 25** – where the *authorised firm* trades under a different name from that under which it is *authorised*, it must include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

**Note 26** - an *incoming EEA firm* will need to modify this section if it chooses to use this CIDD (see *GEN 4 Ann 1R(2)*).

**Note 27** – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

**Note 28** – where the information is provided by an *appointed representative*, the *appointed representative* must use this text instead. The *appointed representative* must give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *customer*.

### **Section 6: Loans and ownership**

**Note 29** – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the CIDD must be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section must be changed to 'Ownership'. Where the information is provided by an appointed representative, it must cover loans made to or by that appointed representative or holdings in, or held by, that appointed representative as appropriate.

**Notes 30, 31 and 32** apply only to a *firm* *advising on, dealing in, or arranging* in relation to *packaged products* ~~for private customers~~.

**Note 30** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider of *packaged products* or by the parent of the provider.

**Note 31** – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider of *packaged products* which is held by the *firm*.

**Note 32** – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

**Notes 33 and 34** apply to an *insurance intermediary* that is not an *insurer* providing services in relation to *non-investment insurance contracts*.

**Note 33** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

**Note 34** – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

### **Section 7: What to do if you have a complaint**

**Note 35** – if different to the address in note 5, give the address and telephone number which is to be used by *customers* wishing to complain.

**Note 36** – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* is aware that a *commercial customer* would not be an *eligible complainant*.

**Note 36A** – if the CIDD is provided by an authorised professional firm which is exclusively carrying on non-mainstream regulated activities, the authorised professional

firm should delete this sentence and refer to the alternative complaints handling arrangements. It should also omit the information required under note 14.

**Note 37** – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it must make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

### **Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?**

**Note 38** – when an *incoming EEA firm* provides the CIDD, it must modify this section as appropriate.

**Note 38A** - when a *firm* which is not a *participant firm* provides the CIDD, it must answer this question 'No' and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained. It should also omit the information required under note 14.

**Note 39** – where the *insurance intermediary* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it must use this alternative text.

**Note 39A** – where the *insurance intermediary* provides a service in relation to a contract which covers both a compulsory class of insurance and a class of insurance which is not compulsory, it should indicate the level of compensation that applies to each class.

### **Section 9: Group personal pensions**

~~**Note 40** – *firms* should only include section 9 if they intend to give information about, or advise on, the opportunity for *employees* to join a *group personal pension scheme* established by their employer. In all other cases it should be omitted entirely.~~

~~**Note 41** – the words in square brackets should be omitted or included, as appropriate, depending upon whether the *firm* is *advising employees* whether or not to join a *group personal pension scheme*, or merely providing them with factual information about the scheme.~~

~~**Note 42** – although *firms* must not use the occasion of a meeting to discuss a *group personal pension scheme* as an opportunity to give *advice on other designated investments*, this does not preclude the provision of *advice on non investment insurance contracts, regulated mortgage contracts or regulated lifetime mortgage contracts*. A *firm* may also, when giving *advice on a group personal pension scheme*, suggest that a further meeting be arranged to discuss *designated investments* and if so must provide a further appropriate IDD or CIDD.~~

### **Lifetime mortgage warning**

**Note 403** - This warning box should be added when the *firm* sells *regulated lifetime mortgage contracts* or home reversion schemes or both.

## Annex E

### Amendments to the Client Assets sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

Money that is not client money: ‘opt outs’ for any business (including ISD business) other than insurance mediation activity

- 4.1.8 G The ‘opt out’ provisions provide a *firm* with the option of allowing an *intermediate customer* or *market counterparty* to choose whether their *money* is subject to the *client money rules* (unless the *firm* is conducting *insurance mediation activity*).
- 4.1.9 R Subject to CASS 4.1.11R, *money* is not *client money* when a *firm* (other than a sole trader) holds that *money* on behalf of, or receives it from, a *market counterparty* or an *intermediate customer*, other than in the course of *insurance mediation activity*, and the *firm* has obtained written acknowledgement from the *market counterparty* or *intermediate customer* that:
- (1) ...
- ‘Opt-outs’ for non-ISD or non-IMD business
- 4.1.10 G For a *firm* whose business is not governed by the *ISD* or the *IMD*, it is possible to ‘opt out’ on a one-way basis. ...
- 4.1.11 R *Money* is not *client money* if a *firm*, in respect of designated investment business which is not a *core investment service*, a *non-core investment service*, ~~or~~ a *listed activity* or *insurance mediation activity* :
- (1) ...

## Annex F

### Amendments to the Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 2.4.3 G In *TC 2.4.2 R (2)* an adequate level of application of knowledge and skills includes:
- (1) specific knowledge of the *firm's* relevant systems and procedures, and of the kinds of *designated investment business* and *regulated mortgage activities* carried on by the *firm* ~~and any other members of its marketing group~~; and
- ...



## Annex G

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Appendix 1: Financial promotion and related activities

1.10.10 G Article 8(3) of the *Financial Promotion Order* also has the effect in broad terms that *financial promotions* made during a visit, call or dialogue will be solicited only if they relate to *controlled activities* or *controlled investments* of the kind to which the recipient envisaged that they would relate. ... For example, a *person* may ask for a visit from a ~~representative~~ representative of an investment product company with a view to receiving advice on an appropriate pension product. ...

5 Ann 3 G

...

#### 2 Table

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
...  <i>COB</i>	<i>COB</i> applies.	Where the activity:  (1) (a) would fall within the <i>overseas persons</i> exclusions in article 72 of the <i>Regulated Activities Order</i> ; or

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
		<p>(b) would not be regarded as carried on in the <i>United Kingdom</i>; or</p> <p>(c) is not carried on with or for a <i>client</i> in the <i>United Kingdom</i>;</p> <p>then only the following apply:</p> <p>(d) <i>COB 3</i> (Financial promotion), but see the territorial scope in <i>COB 3.3</i> (Where?);</p> <p>(e) <i>COB 5.5.7R</i> (Overseas business); <del>and</del></p> <p>(f) certain parts of <i>COB 6</i> (Product disclosure and the customer's right to cancel or withdraw) but only in relation to <i>long-term insurance business</i> carried on with a <i>customer</i> habitually resident in the <i>United Kingdom</i> or if the <i>State of the risk</i> is the <i>United Kingdom</i> (see <i>COB 1.4.7R</i> and <i>COB 1.4.8R</i>); <del>and</del></p> <p><u>(g) (i) <i>COB 4.3.19R</i> to <i>4.3.25R</i> save that the <i>firm</i> must also comply with those <i>rules</i> as if they also applied to a <i>firm</i> carrying out the activities in <i>COB 4.3.19R (1)</i> with or on behalf of all</u></p>

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
		<p><u>private customers;</u></p> <p><u>(ii) COB 5.2.12R to 5.2.14R; and</u></p> <p><u>(iii) COB 5.3.18R (1) and 5.3.18AR to 5.3.18CR;</u></p> <p><u>but only in relation to activities passported under the IMD (see COB 1.4.12R (3));</u></p> <p>(2)...</p>

## Annex H

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

12.2.5 G [deleted]

What is a “network”?

12.2.6 G ~~An independent intermediary~~ A firm is referred to as a ‘network’ if it appoints five or more *appointed representatives* or if it appoints less than five *appointed representatives* which have, between them, twenty-six or more ~~financial advisers~~ representatives. However, a network does not include:

(a) a product provider;

(b) a firm which markets the packaged products of a product provider in the same group as the firm and which does so other than by selecting products from the whole market;

(c) an insurer in relation to a non-investment insurance contract; or

(d) a mortgage lender.

...

Introducers, and representatives and financial advisers: what do these terms mean and what is the relationship with an appointed representative?

12.2.12 G A firm or its *appointed representative* may appoint or employ individuals to act as introducers, or representatives ~~or financial advisers~~ in respect of *designated investment business*.

12.2.13 G (1) An *introducer* is an individual appointed by a ~~provider~~ firm or by an *appointed representative* of such a firm to carry out, in the course of *designated investment business*, either or both of the following activities:

- ...
- 12.2.14 G (1) A *representative* is an individual who is appointed by a *provider firm* or an *appointed representative*...
- ...
- (2) If a *provider firm* appoints an *appointed representative* who is an individual in (1), that *appointed representative* will also be a *representative*...
- 12.2.15 G (1) ~~A *financial adviser* is an individual appointed by an *independent intermediary* or by its *appointed representative* to provide any or all of the following services:~~
- (a) ~~*advising on investments which are designated investments;*~~
- (b) ~~*arranging (bringing about) deals in investments or executing transactions involving, in each case, designated investments with or for clients;*~~
- (c) ~~*managing investments;*~~
- (d) ~~receiving or holding *client money* or other *client assets*;~~
- (e) ~~*safeguarding and administering investments.*~~
- (2) ~~Many of the activities for which an *appointed representative* can be appointed (see SUP 12.2.7G) are also within (1). If an *independent intermediary* appoints an *appointed representative* which is an individual in business on his own account, to perform such activities, that *appointed representative* will also be a financial adviser. The individual may need to be approved to perform the *sole trader function* and other relevant *controlled functions* (see SUP 12.6.8G and SUP 12.6.9G). Further, in these circumstances, in addition to complying with the requirements of SUP 12 and other regulatory requirements, the *firm* should ensure that the rules for financial advisers in COB 5 are complied with. [deleted]~~
- ...
- 12.5.6 G (1) If the *appointed representative* is appointed to give *advice on investments to private customers* concerning *packaged products*, the *firm* should also satisfy itself that:
- (a) the contract requires compliance with the *rules* in COB 5.1 (~~*Polarisation and status disclosure*~~ Advising on packaged products); and.
- ...

- (2) The contractual requirements in SUP 12.5.5R should extend to:
- (a) the activities of the *appointed representative*, if the *appointed representative* is a ~~representative, introducer or financial adviser~~ an individual; ~~or and~~
  - (b) the activities of the *employees* of, ~~or representatives, and introducers and financial advisers~~ appointed by, the *appointed representative*.

...

SUP 20 Ann 1R

Activity groups, tariff bases and valuation dates applicable

...

Part 2

This table indicates the tariff base for each fee block. The tariff base is the means by which we measure the 'amount of business' conducted by a *firm*.

SUP Table

4	Activity group	Tariff-base
	A.1	MODIFIED ELIGIBLE LIABILITIES
	...	
	A.4	ADJUSTED GROSS PREMIUM INCOME AND MATHEMATICAL RESERVES  ...  Notes:  (1) Business conducted through a <del>marketing associate</del> <u>an associated company</u> should be excluded in reporting the <i>product provider's premium income</i> .  ....

## Annex I

### Amendments to the Dispute Resolution: Complaints sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

Transitional provisions, Table 1

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
<u>17</u>	<u>DISP</u> <u>1.4.18R –</u> <u>DISP</u> <u>1.4.20G</u>	<u>R</u>	<u>A firm must apply DISP as it applied before amendment by the Depolarisation Instrument to complaints received before 14 January 2005.</u>	<u>From 14 January 2005.</u>	<u>14 January 2005</u>
...					

#### Purpose

1.1.12

G The purpose of this chapter is to set out the *rules* relating to the internal handling of complaints by *firms*, including the procedures which a *firm* must put in place, the time limits within which a *firm* must deal with a complaint, the referral of complaints, the records of a complaint which a *firm* must make and retain ...

#### Requirement to have internal complaint handling procedures

1.2.1

R A *firm, A*, must have in place and operate appropriate and effective internal complaint handling procedures (which must be written down) for:

(1) handling any expression of dissatisfaction, whether oral or written, and whether justified or not, from or on behalf of an *eligible complainant* about ~~that firm's~~ A's provision of, or failure to provide, a financial service; and

(2) referring to another firm, B, expressions of dissatisfaction about B's services, if A markets (or has marketed) B's financial services or if A's financial services are marketed by B.

...

1.2.4 G The internal complaints handling procedures should provide for:

...

(2) responding to complaints;

(2A) referring complaints to other firms;

(3) the appropriate investigation of complaints; and

...

1.2.6 G (1) *DISP* 1.2.1R does not prevent the use of a third party administrator for the purposes of handling complaints.

(2) It is acceptable for two or more firms to set up arrangements, such as a one-stop shop for complaints handling under a service level agreement, provided that this still secures for complainants an equivalent standard of service and, if appropriate, redress. Any such arrangements should be made clear to an eligible complainant.

...

Internal complaint handling procedures: additional requirements

1.3.3. R *DISP* 1.4 - *DISP* 1.5 do not apply:

(1) where the *firm* has taken reasonable steps to determine, and has determined, that the complaint:

(a) ...

(b) does not relate to an activity of that *firm* (or of any other firm with whom that firm has some connection in marketing financial services) which comes under the jurisdiction of the *Financial Ombudsman Service*; or

(c) ...

...



Written acknowledgement within five business days

1.4.1

R A firm must send a written acknowledgement of a complaint to the complainant within five business days of its receipt, ...

...

Referring complaints

1.4.18

R (1) A firm which has reasonable grounds to be satisfied that another firm may be solely responsible for the fault alleged in a complaint may refer the complaint to that other firm, but if it does so it must:

(a) refer the complaint promptly and in any event within five business days of the date on which it became satisfied that such other firm may be responsible for the subject matter of the complaint;

(b) make the referral using a durable medium; and

(c) inform the complainant of the referral by way of a final response and include the other firm's contact details.

(2) A firm which has reasonable grounds to be satisfied that another firm may be jointly responsible for the fault alleged in a complaint, may refer the complaint to that other firm but if it does so it must:

(a) refer the complaint promptly and in any event with five business days of the date on which it became satisfied that such other firm may be jointly responsible for the subject matter of the complaint;

(b) make the referral on a durable medium;

(c) at the same time inform the complainant of the referral and include the other firm's contact details; and

(d) comply with the obligations in DISP as to the investigation of that part of the complaint that is the firm's responsibility and, as soon as possible, inform the complainant of the outcome by a final response.

Dealing with a referred complaint

1.4.19

R When a firm receives a complaint referred to it under DISP 1.4.18R, the complaint is treated for the purposes of DISP as if made directly to that firm, and as if received by it when the referral was received.

1.4.20 G On receiving a complaint referred by another *firm*, the standard time limits will apply from the date on which the *firm* receives the referral. In particular, *DISP* 1.4.1R requires the *firm* to send a written acknowledgement to the complainant within five *business days*. A *firm* should copy this acknowledgement to the *firm* which made the referral.

...

1.5.2 G The records required by *DISP* 1.5.1R are for the purposes of monitoring by the *FSA* and also to ensure that the *firm* is able to cooperate, as necessary, with the *Financial Ombudsman Service*. They should include:

...

(2) ...; ~~and~~

(3) any correspondence between the *firm* and the complainant including details of any redress offered by the *firm*; ~~and~~

(4) documentation relating to the referral of a complaint under *DISP* 1.4.18R.

...

## Appendix 2 Handling Mortgage Endowment Complaints

2.6.15 G *Product providers* with windfall benefits in the form of *policy* augmentations should tell:

(1) their own relevant *customers* (mortgage endowment complainants);  
and

(2) ~~independent financial advisers~~ other *firms* with such *customers* (and any other interested parties);

that they have excluded windfall augmentation benefits from values used or to be used for loss and redress. ~~Firms~~Firms should provide this information to the *Financial Services Compensation Scheme* when providing them with a value to be used for loss or redress. Should their own relevant *customers*, ~~independent financial advisers~~ other *firms* with such *customers* (and any other interested parties) and the *Financial Services Compensation Scheme* request it, the *firm* should provide the value of these benefits and a description of the method used to exclude them.

## Annex J

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

Transitional provisions, Table 1

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
<u>5</u>	<u>CRED</u> <u>17.4.4 R –</u> <u>CRED</u> <u>17.4.6G</u>	<u>R</u>	<u>A credit union must apply CRED as it applied before amendment by the Depolarisation Instrument with respect to complaints received by a credit union before 14 January 2005</u>	<u>From 14 January 2005</u>	<u>14 January 2005</u>

...

17.1.5 G The purpose of this chapter is to set out the *rules* relating to the internal handling of complaints by a *credit union*, including:

...

(2A) the referral of complaints;

...

...

17.2.1 R A *credit union* must establish, maintain and implement appropriate and effective internal complaint handling procedures (which must be written down) for:

- (1) handling any expression of dissatisfaction whether oral or written, and whether justified or not, from or on behalf of an *eligible complainant* about that *credit union's* provision of, or failure to provide, a financial services activity; and
- (2) referring to another *firm*, A, expressions of dissatisfaction about A's services, if the *credit union* markets (or has marketed) A's financial services or if the *credit union's* financial services are marketed by A.

...

17.2.4 G The internal complaint handling procedures should provide for:

...

- (2A) referring complaints to other *firms*;
- (3) the appropriate investigation of complaints; and

...

17.2.6 G (1) A *credit union* is not prevented from using a third party administrator (for example, an outside organisation) for the purposes of handling complaints.

- (2) It is acceptable for two or more *credit unions* to set up arrangements, such as a one-stop shop for complaints handling under a service level agreement, provided that this still secures for complainants an equivalent standard of service and, if appropriate, redress. Any such arrangements should be made clear to an *eligible complainant*.

...

17.4.1 R The additional requirements in *CRED* 17.5 - *CRED* 17.7 (on time-limits, record-keeping; reporting and co-operation with *Ombudsman*) do not apply:

- (1) where the *credit union* has taken reasonable steps to determine, and has determined, that the complaint:
  - (a) is not made by, or on behalf of, an *eligible complainant*; or
  - (b) does not relate to an activity of that *credit union* (or of any other *firm* with whom that *credit union* has some connection in marketing financial services) which comes under the jurisdiction of the *Financial Ombudsman Service*; or

...

...

#### Referring complaints

17.4.4 R (1) A *credit union* which has reasonable grounds to be satisfied that another *firm* may be solely responsible for the fault alleged in a complaint may refer the complaint to that other *firm* but if it does so it must:

- (a) refer the complaint promptly and in any event within five business days of the date on which it became satisfied that such other firm may be responsible for the subject matter of the complaint;
  - (b) make the referral using a durable medium; and
  - (c) inform the complainant of the referral by way of a final response and include the other firm's contact details.
- (2) A credit union which has reasonable grounds to be satisfied that another firm may be jointly responsible for the fault alleged in a complaint, may refer the complaint to that other firm but if it does so it must:
- (a) refer the complaint promptly and in any event within five business days of the date on which it became satisfied that such other firm may be jointly responsible for the subject matter of the complaint;
  - (b) make the referral using a durable medium;
  - (c) at the same time inform the complainant of the referral and include the other firm's contact details; and
  - (d) comply with the obligations in CRED as to the investigation of that part of the complaint that is the credit union's responsibility and, as soon as possible, inform the complainant of the outcome by a final response.

#### Dealing with a referred complaint

- 17.4.5     R     When a firm receives a complaint referred to it under CRED 17.4.4R, the complaint is treated for the purposes of CRED as if made directly to that firm, and as if received by it when the referral was received.
- 17.4.6     G     On receiving a complaint referred by a firm, the standard time limits will apply from the date on which the credit union receives the referral. In particular, CRED 17.5.1 R requires the credit union to send a written acknowledgement to the complainant within five business days. A credit union should copy this acknowledgement to the firm which made the referral.

...

17.5.1 R A *credit union* must send a written acknowledgement of a complaint to the complainant within five ~~business days~~ *business days* of its receipt, giving the name or job title of the person handling the complaint within the *credit union* (together with details of the *credit union*'s internal complaint handling procedures).

...

17.6.2 G The records required are for the purposes of monitoring by the *FSA* and also to ensure that the *credit union* is able to cooperate, as necessary, with the *Financial Ombudsman Service*. These should include:

- (1) the name of the complainant;
- (2) the substance of the complaint;
- (3) any correspondence between the *credit union* and the complainant including details of any redress offered by the *credit union*; and
- (4) documentation relating to the referral of a complaint under *CRED* 17.4.4R.

## Annex K

### Amendments to the Professional Firms sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

5.3.2 G *COB* 1.2.1R (4) provides that *COB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities*, except for:

(1) *COB* 2.1 (Clear, fair and not misleading communication), ... ; and

(2) (where these are *insurance mediation activities*) the *IMD implementation provisions* and *COB* 4.3.19R to 4.3.25R as if they also applied to a *firm* carrying out the activities in *COB* 4.3.19 R (1)(a)-(c) with or on behalf of *private customers*, unless:

(a) the *designated professional body* of the *firm* has made rules which implement some or all of articles 12 and 13 of the *IMD*;

(b) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and

(c) the *firm* is subject to the rules in the form in which they were approved;

in which case they are disappplied to the extent that articles 12 and 13 of the *IMD* are implemented by the rules of the *designated professional body*.

(3) *COB* 1.2.1AG provides that the effect of *COB* 1.2.1R(4)(d) is that if the relevant *designated professional body* of an *authorised professional firm* does not make rules implementing articles 12 and 13 of the *IMD* applicable to *authorised professional firms*, those *firms* will need to comply with the *IMD implementation provisions* and *COB* 4.3.19R to 4.3.25R as if they also applied to a *firm* carrying out the activities in *COB* 4.3.19 R (1)(a)-(c) with or on behalf of *private customers*.

## Annex L

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text.

<del><i>adopted packaged product</i></del>	<p><del>(in relation to a firm) a stakeholder pension scheme which is a packaged product:</del></p> <p>(a) <del>not produced by the firm or in the firm's marketing group, but by another producer (whether a firm or not); and</del></p> <p>(b) <del>on which the firm is able to advise as a result of a decision taken under COB 5.1.4R(1).</del></p>
<i>adviser</i>	<p>an individual who is:</p> <p>(a) <u>a financial adviser</u>; or</p> <p>(b) <del>a representative</del>; or</p> <p>(c) <u>an appointed representative</u>.</p>
<i>branded fund</i>	<p>a life policy or a regulated collective investment scheme other than a broker fund which is available as an investment only or mainly to the clients of a particular <u>independent intermediary firm other than a provider firm</u>.</p>
<i>broker fund adviser</i>	<p><del>an independent intermediary firm</del> <u>who</u> <del>which</del> has or whose associate being an authorised person has, an arrangement with a long-term insurer, overseas long-term insurer or operator of a regulated collective investment scheme, under which it is to be expected that the long-term insurer, overseas long-term insurer or operator will take into account the advice of that <u>independent intermediary firm</u> or <u>his</u> <u>its</u> associate:</p> <p>(a) ... into which cash contributions of that <u>independent intermediary's firm's</u> customers have been made;</p> <p>(b) ... into which the cash contributions of <u>that independent intermediary's firm's</u> customers have been made;</p> <p>in this definition <i>associate</i> includes any authorised person in respect of whose services the first <u>independent intermediary firm</u> receives any benefit or reward ...</p>
<u><i>combined initial disclosure document</i></u>	<p><u>information about the scope and nature of the services offered by a firm in relation to a combination of two or more of the following:</u></p> <p>(a) <u>packaged products</u>;</p> <p>(b) <u>non-investment insurance contracts</u>;</p>



- (c) regulated mortgage contracts; or
- (d) regulated lifetime mortgage contracts;
- commission*\* any form of commission or remuneration, including a benefit of any kind, offered or given in connection with:
- (a) *designated investment business* (other than *commission equivalent*); ~~or~~
- (b) *insurance mediation activity* in connection with a *non-investment insurance contract*; or
- (c) the sale of a *packaged product*, that is offered or given by the *product provider*.

Note that this definition of commission amends that which has been made by the Board in Instrument 2004/01 and which is due to come into force on 14 January 2005.

*fee* Any payment or remuneration offered or made by a *client* to a *firm* in connection with *designated investment business* or with any other business of the *firm*, including (where applicable) any *mark up or mark down*.

*fees and commission statement* a statement which a *firm* is required to maintain in accordance with COB 4.3.11R.

~~*financial adviser*~~ ~~an individual appointed by an independent intermediary or by its appointed representative to provide any or all of the following services:~~

(a) ~~giving advice on investments to clients;~~

(b) ~~arranging (bringing about) deals in investments or executing transactions involving, in each case, designated investments with or for clients;~~

(c) ~~managing investments;~~

(d) ~~receiving or holding client money or other clients' assets;~~

(e) ~~safeguarding and administering investments~~

~~*independent advice*~~ ~~advice on investments, other than in the form of a direct offer financial promotion, given to a customer by an independent intermediary in relation to packaged products.~~

~~*independent intermediary*~~ a *firm* acting as an intermediary, but excluding:

- (a) a *firm* which is a member of a *marketing group*;
- (b) a *product provider* which sells its own *packaged products*.

IMD minimum implementation provisions

The following provisions in *COB*:

- (1) COB 4.3.19R to COB 4.3.25R;
- (2) COB 5.2.12R to COB 5.2.14R; and
- (3) COB 5.3.14R (1) and COB 5.3.18AR to COB 5.3.18CR.

initial disclosure document

information about the scope and nature of the services offered by a firm in relation to packaged products as required by COB 4.3.9R; or stakeholder products as required by COB 5A.2.1 (1) R.

*inter-professional business*

the business of a *firm*:

- (a) ...
- (b) but excluding the carrying on of the following activities:
  - (i) ...
  - (vi) (vi) activities relating to life policies;

*introducer*

an individual appointed by a ~~*provider firm*~~ or by an *appointed representative of such a firm*, to carry out in the course of *designated investment business* either or both of the following activities:

- (a) *effecting introductions*;
- (b) *distributing non-real time financial promotions*.

*introducer appointed representative*

an *appointed representative* appointed by a ~~*provider firm*~~ whose scope of appointment is limited to:

- (a) *effecting introductions*; and
- (b) *distributing non-real time financial promotions*.

<i>introducing</i>	<p>...</p> <p><u>(in COB) the activity of effecting mere introductions carried on by a firm with permission for making arrangements with a view to deals in investments.</u></p>
<i>investment trust savings scheme</i>	<p>(a) a dealing service (whether or not held within a pension contract) dedicated to the securities of <del>a particular</del> <u>one or more</u> investment trusts, <del>or within a particular marketing group;</del></p> <p>...</p>
<i>marketing group</i>	<p>a group of persons who:</p> <p>(a) are allied together (either formally or informally) for purposes of marketing <del>packaged products</del> of the marketing group; and</p> <p>(b) each of which, if it holds itself out in the <i>United Kingdom</i> as marketing <del>packaged products to private customers</del>, does so only as an <i>investment manager</i> or in relation to <del>packaged products of the marketing group.</del></p>
<i>marketing group associate</i>	<p><del>a firm other than a product provider which is a member of a marketing group.</del></p>
<i>network</i>	<p>an <del>independent intermediary firm:</del></p> <p>(a) which has five or more <i>appointed representatives</i>; or</p> <p>(b) whose <i>appointed representatives</i> (being fewer than five) have, between them, 26 or more <u><i>financial advisers representatives</i></u>;</p> <p><u>but not:</u></p> <p>(i) <u>a product provider; or</u></p> <p>(ii) <u>a firm which markets the packaged products of a product provider which is in the same group as the firm and which does so other than by selecting products from the whole market; or</u></p> <p>(iii) <u>an insurer in relation to a non-investment insurance contract; or</u></p> <p>(iv) <u>a mortgage lender.</u></p>
<i>personal recommendation</i>	<p>a recommendation which is <u>advice on investments</u> given to a specific person.</p>
<i>provider firm</i>	<p>a <del>firm</del> that is:</p> <p>(a) <del>a product provider; or</del></p> <p>(b) <del>a marketing group associate.</del></p>

range of packaged products, range

(in relation to a firm) the range of packaged products on which the firm gives advice on investments to private customers (see COB 5.1.6AR) or if appropriate the list of packaged products in which the firm deals.

Delete existing definition for 'representative' and replace with the following text, which is not underlined:

*representative*

an individual who:

- (a) is appointed by a *firm*, or by an *appointed representative* of a *firm*, to carry on any of the following activities:
  - (i) *advising on investments*;
  - (ii) *arranging (bringing about) deals in investments*;
  - (iii) *dealing in investments*; or
- (b) although not appointed to do so, carries on any of the activities in (i) to (iii) on behalf of a *firm* or its *appointed representative*.

*small personal investment firm*

a *personal investment firm*:

- (a) which is not an *ISD investment firm*;
- (b) which is not a *network*; and
- (c) which has fewer than 26 ~~financial advisers or~~ *representatives*.

## ADDENDUM

### DEPOLARISATION INSTRUMENT 2004

In this Addendum, the underlining should have been in the Depolarisation Instrument 2004 where indicated. Where an entire section of text is being inserted, the place where the change will be made is indicated and the text is not underlined.

Annex L of this instrument is amended as follows:

*commission* any form of commission or remuneration, including a benefit of any kind, offered or given in connection with:

(a) *designated investment business* (other than *commission equivalent*); ...

Insert in the correct alphabetical position the following new definition:

*commission equivalent* (equivalent) the cash payments, benefits and services listed in *COB 5.7.16E* which satisfy the criteria in *COB 5.7.5R(2)*.

Addendum

9 December 2004

**SECOND ADDENDUM**  
**DEPOLARISATION INSTRUMENT 2004**

As a result of this Addendum, Paragraph C (1) of this instrument is amended to replace “Annexes A to F, H and J to M” with “Annexes A to F, H and J to L”. This revision is not shown underlined or struck through.

Elsewhere in this Addendum, underlining indicates new text and striking through indicates deleted text or revisions are explained in narrative.

Annex B of this instrument is amended as follows:

(i) COB 1.3.5G is shown as it should have appeared in the instrument:

1.3.5 G *Firms* are reminded that the definition of *inter-professional business* does not include:

...

(4) ...; ~~or~~

(5) ...; or

(6) *regulated activities relating to life policies.*

...

(ii) The text of COB 2.2.5AE which results following this instrument is further amended as follows:

Financial assistance and product providers

2.2.5A E ...

(2) ...

(a) ...

(b) ...;

unless all the conditions in (4) are satisfied. A product provider should also take reasonable steps to ensure that its associates do not

take any step which would result in it having a holding as in (a) or providing credit as in (b), having regard to (5).

(3) ...

(4) The conditions referred to in (2) and (3) are that:

...

(iii) The text in this instrument dealing with changes to COB 6.2.9R, COB 6.2.11G, COB 6.2.19R, COB 6.2.23G and COB 6.2.25R is deleted from the instrument.

Annex C of this instrument is amended as follows:

(iv) The following text amending ICOB 4 Annex 2R is that which should have appeared in the instrument:

ICOB 4 Annex 2R: Combined initial disclosure document ("CIDD")

...

---

#### 4 What will you have to pay us for our services?

---

##### Investment

Before we provide you with advice, we will give you our keyfacts guide ~~to~~ about the cost of our services'. [Note 15]

...

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate "keyfacts guide ~~to~~ about the costs of our services" (i.e. a menu) if they propose to give that *customer advice on investments on packaged products*.

...

Annex D of this instrument is amended as follows:

- (v) The following text amending MCOB 4 Annex 2R is that which should have appeared in the instrument:

...

MCOB 4 Annex 2R: Combined initial disclosure document ("CIDD")

...

---

#### 4 What will you have to pay us for our services?

---

##### Investment

- Before we provide you with advice, we will give you our keyfacts guide ~~to~~ about the cost of our services'. [Note 15]

...

**Note 15** – *firms* are only required to provide a *private customer* with an appropriate "keyfacts guide ~~to~~ about the costs of our services" (i.e. a menu) if they propose to give that *customer advice* on investments on packaged products.

...

Second Addendum

18 August 2005



## BASIC ADVICE ON STAKEHOLDER PRODUCTS INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making powers);
  - (2) section 145 (Financial promotion rules);
  - (3) section 149 (Evidential provisions);
  - (4) section 156 (General supplementary powers); and
  - (5) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- C. Subject to D, this instrument comes into force on 6 April 2005.
- D. The amendments in Annex A to COB 6.5.15 R and 6.5.37A R will come into force on 1 December 2004.

### Amendments to the Handbook

- E. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below:

(1)	(2)
Principles for Business (PRIN)	Annex A
Conduct of Business sourcebook (COB)	Annex B
Training and Competence sourcebook (TC)	Annex C
Authorisation manual (AUTH)	Annex D
Supervision manual (SUP)	Annex E
Glossary of definitions	Annex F

### Citation

- F. This instrument may be cited as the Basic Advice on Stakeholder Products Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### Amendments to Principles for Business

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Classification: designated investment business

1.2.3 G (1) All firms, except those intending only to provide basic advice on a stakeholder product, are required by COB 4.1.4R (Requirement to classify) ~~requires a firm~~ to classify a client before conducting *designated investment business* with or for him, and that classification will be applicable for the purposes of *Principles 6, 7, 8 and 9*.

(2) The person to whom a firm provides basic advice on a stakeholder product will be a private customer for all purposes including the purposes of Principles 6, 7, 8 and 9.

...

3.4.3 G (1) The whole of *COB 4.1* (Client classification) applies to a firm intending to conduct, or conducting, *designated investment business other than providing basic advice on a stakeholder product*, and *ancillary activities* relating to *designated investment business*. Any *client* classifications established in relation to such business will be applicable for the purposes of *Principles 6, 7, 8 and 9*.

(2) The person to whom a firm provides basic advice on a stakeholder product will be a private customer for all purposes including the purposes of Principles 6, 7, 8 and 9.

## Annex B

### Amendments to the Conduct of Business Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section is inserted, the place that it goes is indicated and the text is not underlined.

#### Contents

Chapter

...

5A Providing basic advice on stakeholder products

...

3.2.8 G ...

- (2) *Firms* are reminded that if in the course of making a *financial promotion* of any kind a *representative* gives specific *advice on investments* to a *private customer*, about the suitability of a product for that individual *or provides basic advice on a stakeholder product*, rules on advising and selling in COB 5 *or, as the case may be, 5A, apply*.

...

Specific non-real time financial promotions: packaged products

3.8.19 R (1) *A firm must not communicate or approve a specific non-real time financial promotion containing or offering advice on packaged products, or providing basic advice on a stakeholder product, unless the promotion discloses information to show whether the scope of the advice which is given or offered is or will be based upon a selection made from:*

- (a) the whole market (or from the whole of a named sector of the market); or

...

- (2) *A firm must not communicate or approve a specific non-real time financial promotion offering packaged products or stakeholder products produced by a person, A:*

... (a) that holds out any *person* other than A as the *packaged product's* producer; or

...

3.8.22 R ...

(7) if applicable acts in conformity with the *rules* in COB 4.3 (Disclosing information about services, fees and commission – packaged products), COB 5A.1 (Providing basic advice on Stakeholder Products) and COB 5.1 (Advising on packaged products).

...

4.1 Client classification

Application

4.1.1 R (1) This section applies to a *firm* intending to conduct, or conducting *designated investment business* or *ancillary business* relating to *designated investment business* (but not to a *firm* which in relation to any customer intends only to provide basic advice on a stakeholder product).

4.3 Disclosing information about services, fees and commission - packaged products

Application

4.3.1 R (1) COB 4.3 applies:

~~(a)~~ to a *firm* when carrying on with or for *private customers* any of the following in relation to *packaged products*:

~~(i)~~ *advising*; or

~~a)~~

~~(ii)~~ *dealing as agent*; or

~~b)~~

~~(iii)~~ *arranging*;

~~e)~~

(b) to a *firm*, other than an *insurer*, that carries on in relation to a *life policy* any of the activities in (1) with or for an *intermediate customer* or a *market counterparty*.

(2) COB 4.3, other than COB 4.3.7R (1) and (2), does not apply to a *firm* when providing basic advice on a stakeholder product.

...

5.1 Advising on packaged products

## Application

- 5.1.1 R This section applies to a *firm* which gives *advice on investments to a private customer on packaged products* but does not apply to a *firm* when providing basic advice on a stakeholder product.

...

## 5.2 Know your customer

### Application

- 5.2.1 R This section applies to a *firm* that:
- (1) gives a *personal recommendation* concerning a *designated investment* to a *private customer*;

...

- (6) is not an *insurer* and *arranges* (but not merely by *introducing*) a *life policy* for an *intermediate customer* or a *market counterparty*;

But this section does not apply to a *firm* when providing basic advice on a stakeholder product.

...

## 5.3 Suitability

### Application

- 5.3.1 R This section applies to a *firm* when it:
- (1) makes a *personal recommendation* concerning a *designated investment* to a *private customer*;

...

- (3) promotes a *personal pension scheme* by means of a *direct offer financial promotion* to a group of *employees*;

but this section does not apply to a *firm* when providing basic advice on a stakeholder product.

...

## 5.4 Customer's understanding of risk

### Application

- 5.4.1 R This section applies to a *firm* that conducts *designated investment business* with or for a *private customer* but does not apply to a *firm* when providing basic advice on a stakeholder product.

...

After Chapter 5 of *COB* insert a new Chapter 5A as follows, the text of this new chapter is not underlined:

## **Chapter 5A**

### **5A.1 Providing basic advice on stakeholder products**

#### **Application and Purpose**

5A.1.1 G This chapter sets out what *firms* must do when *providing basic advice on a stakeholder product*. The *rules* in the chapter are designed to enable *firms* to provide simple, quick and limited advice to *persons* who may be interested in buying a *stakeholder product*. The *rules* assume that *firms* will *provide basic advice* to *persons* who have no practical knowledge of investing in *stakeholder products* or *investments*.

### **5A.2 Disclosure on making first contact : information about services**

- 5A.2.1 R (1) **A *firm* must take reasonable steps to ensure that its *representatives*, on first making contact with a *customer* with a view to *providing basic advice on a stakeholder product*, provide, in a *durable medium*, an *initial disclosure document* that complies with *COB* 4.3.9R (1).**
- (2) **A *firm* must take reasonable steps to ensure that its *representatives* explain the contents of the *initial disclosure document* at the time it is provided to the *customer*.**
- (3) **The requirements in (1) and (2) do not apply:**
- (a) **to the extent that the information has already been given to the *customer* on a previous occasion and it is still likely to be accurate and appropriate for the *customer*; or**
- (b) **if *COB* 5A.2.6R (initial contact by telephone) applies.**
- (4) **A *firm* which is required by this *rule* to provide an *initial disclosure document* to a *private customer* may instead provide the *customer* with a *combined initial disclosure document*, that complies with *COB* 4.3.9R (2), if it has reasonable grounds to be satisfied that the *services* which it is likely to provide to the *customer* will, in addition to *stakeholder products*, relate to one or more of the following:**
- (a) ***regulated mortgage contracts*;**
- (b) ***regulated lifetime mortgage contracts*;**
- (c) ***non-investment insurance contracts*.**

- (5) **A firm must, if requested to do by a customer, provide an explanation of the basis on which it has chosen to market the particular stakeholder products within the range on which basic advice will be given to a customer, including an explanation of why the firm has selected particular product providers.**

#### **Smoothed Products**

- 5A.2.2 **R A firm must not provide basic advice on smoothed linked long term products.**
- 5A.2.3 **G COB 5A.2.2R does not prevent a firm from including smoothed linked long term products in regulated activity that does not involve the provision of basic advice.**

#### **Providing a copy of the range of stakeholder products**

- 5A.2.4 **R A firm must take reasonable steps to ensure that its representatives provide a copy of the appropriate range of stakeholder products on the request of a customer having regard to the services it is providing or may provide to the customer.**

#### **Terms of business and telephone sales**

- 5A.2.5 **R (1) A firm that, pursuant to COB 5A.2.1R, provides a customer with an initial disclosure document containing information that a corresponding rule in COB 4.2 says must be included in terms of business, will satisfy the corresponding rule by providing that information in the initial disclosure document.**
- (2) Any information required by COB 4.2 which is not included in an initial disclosure document provided to a customer in compliance with COB 5A.2.1R can be included at the end of the initial disclosure document provided to the customer or, if provided at the same time, by way of separate items of information.**
- 5A.2.6 **R (1) Where a firm's initial contact with a customer (for a purpose set out in COB 5A.2.1 R) is by telephone, then the firm must provide the following information and satisfy the following requirements before proceeding further:**
- (a) the name of the firm and, if the call is initiated by or on behalf of a firm, the commercial purpose of the call;**
- (b) whether the firm will select from or deal with stakeholder products from a limited number of companies or from a single company;**
- (c) that the firm will provide the customer with only basic advice on stakeholder products and without full assessment of his needs and circumstances;**

(d) that the information given under (a) to (c) will subsequently be confirmed in writing.

- (2) A *firm* which complies with (1) will, subject to (3), satisfy the condition set out in item (1) of *COB 4, Annex 1R*.
- (3) If during the course of a telephone call a *firm* is to conclude a contract (for example for the provision of a mediation services or for the purchase or sale of a *stakeholder product*), it must satisfy the requirements in *COB 4.2.5R* and *COB 4 Annex 1R* as well as comply with (1) and (2) above.

5A.2.7 R If the first contact a *firm* has with a *private customer* with a view to providing basic advice on stakeholder products, is by telephone then the *firm* must send the *customer* an *initial disclosure document* as soon as is reasonably practicable following the conclusion of the call.

5A.3 Scope and range of advice on stakeholder products: general

- 5A.3.1 R
- (1) A *firm* which provides a *private customer* with basic advice on a *stakeholder product* must take reasonable steps to ensure that the scope of the *basic advice* given to a *private customer* is based upon a selection of one of the following:
    - (a) a limited number of providers of *stakeholder products*; or
    - (b) a single provider of a *stakeholder product*.
  - (2) A *firm* which provides a *customer* with basic advice on a *stakeholder product* must do so only on the basis of a *range of stakeholder products* which includes no more than one of each of:
    - (a) a *CIS stakeholder product* or a *linked-life stakeholder product*;  
or
    - (b) a *stakeholder pension*; or
    - (c) a *stakeholder CTF*.
  - (3) A *firm* must take reasonable steps to ensure that any of its *representatives* which give *basic advice on stakeholder products* that offer a choice of funds, do not give *advice on*, or recommend, a particular fund for the *customer*.
  - (4) A *firm* must take reasonable steps to ensure that its *representatives* do not, while they are engaged in providing *basic advice on stakeholder products*, provide *advice* on products other than those within the *range* offered by the *firm*.
  - (5) A *firm* which has commenced the sales process for *stakeholder products* in respect of a particular *customer* may only depart from that process if:



(a) it has taken reasonable steps to ensure its *representatives* advise the *customer* that *basic advice on stakeholder products* within the *range* offered by the *firm* will not be provided during the period of departure; and

(b) it has taken reasonable steps to ensure its *representatives* do not *provide basic advice* during the period of departure.

(6) A *firm* must take reasonable steps to ensure that if its *representatives* return to the sales process for *stakeholder products* after the period of departure referred to in *COB 5A.3.1R (5)*, they first advise the *customer* that the period of departure has ended and the sales process for *stakeholder products* has recommenced.

5A.3.2 G (1) A *firm* can provide a *customer* with *basic advice on a stakeholder product* on the basis of a range of *stakeholder products* which includes more than one *deposit-based stakeholder product*.

G (2) A *firm* can provide advice on a *deposit based stakeholder product* during the period of departure referred to in *COB 5A.3.1R (5)*.

5A.3.3 G (1) A *firm* which *provides basic advice on stakeholder products* is required by *COB 5A.3.1R (2)* to do so, in relation to any particular *customer*, by reference to a *range of stakeholder products* which should include no more than one of each type of *stakeholder product* specified in *COB 5A.3.1R (2)*. A *firm* may however operate with more than one such *range*.

(2) When a *firm* *provides basic advice on a stakeholder product* which is not produced by the *firm*, it is responsible for the advice given. By contrast, the producer is responsible for the relevant terms and conditions of the *stakeholder product*.

#### **Range of stakeholder products: appointed representatives**

5A.3.4 R (1) A *firm* must maintain in writing and keep up to date a statement of:

(a) the scope of *basic advice* (within the meaning of *COB 5A.3.1R (1)*) which each of its *appointed representatives* is, through its contract with the *firm*, permitted to give; and including

(b) the *range (or ranges) of stakeholder products* on which each *appointed representative* advises.

(2) In applying the *rules in COB* to a *firm* in respect of its *appointed representatives*, references to a *firm's* scope or *range of stakeholder products* are to be taken as references to the scope (or scopes) and to the *range (or ranges) of its appointed representatives*.

5A.3.5 G An *appointed representative's range of stakeholder products* should be defined by means of a list of the names or titles of each of the *stakeholder products* which it is permitted to sell.

#### Range of stakeholder products: records

- 5A.3.6 R (1) **A firm must make, and keep up to date, a record of its scope and range (or ranges) of stakeholder products.**
- (2) **The record in (1) must be retained for six years from the date on which it was superseded by a more up-to-date record.**
- (3) **The record for distribution to a customer must be the particular range of stakeholder products which is appropriate for the services provided to that customer and include details of:**
- (a) **the identity of the firms within the range whose stakeholder products the firm may sell; and**
- (b) **a list of the products the firm may sell.**
- (4) **A firm must maintain a record of the particular range of stakeholder products on which its basic advice to each private customer is based and such a record must be kept for six years from the date on which the basic advice is given.**

#### Branding stakeholder products

- 5A.3.7 R **If a firm provides basic advice on a stakeholder product produced by another person, it must not:**
- (1) **hold itself out as the stakeholder product's producer;**
- (2) **do or say anything which might reasonably lead a customer to be mistaken as to the identity of the product's producer.**

#### Staying within the range of advice of stakeholder products

- 5A.3.8 R (1) **A firm must take reasonable steps to ensure that neither it nor any of its representatives provides basic advice on a stakeholder product unless the product is:**
- (a) **within the firm's range (or ranges) of stakeholder products; and**
- (b) **is within the particular range of stakeholder products on which the firm has indicated it will give basic advice to that customer.**

#### "Independence" - restriction on holding out

- 5A.3.9 R (1) **A firm must not in providing basic advice on stakeholder products hold itself out as giving such basic advice on an independent basis.**
- (2) **Notwithstanding (1) a firm may use its facilities and stationery which it may use for other business in respect of which it does hold itself out as acting or advising independently.**

Remuneration structure and referrals

- 5A.3.10 R** A *firm* must take reasonable steps to ensure that none of its *representatives*:
- (1)** is likely to be influenced by the structure of his or her *remuneration* to give unsuitable *basic advice* on *stakeholder products* to a *customer*; and
  - (2)** refers *customers* to another *firm* in circumstances which would amount to the provision of an inducement under *COB 2.2.3R* (Prohibition of inducements).

**5A.4** Providing basic advice on stakeholder products through scripted questions

- 5A.4.1 R**
- (1)** A *firm* which provides *basic advice on a stakeholder product* must do so through a sales process which incorporates pre-scripted questions put to the *customer*.
  - (2)** Unless excluded at the preliminary stage, a *customer* must be sent or given, in a *durable medium*, a copy of the completed scripted questions and answers.

Suitability of stakeholder products

- 5A.4.2 R**
- (1)** A *firm* must only recommend that a *customer* acquire a *stakeholder product* if:
    - (a)** it has taken reasonable steps to assess:
      - (i)** the *customer's* answers to the scripted questions;
      - (ii)** any other facts, circumstances or information disclosed by the *customer* during the sales process.
    - (b)** it has, having due regard to the information in (a), reasonable grounds for believing that the *stakeholder product* is suitable for the *customer*;
    - (c)** the *firm* reasonably believes that the *customer* understands the advice he has been given and the basis on which it was provided.
  - (2)** The requirements in (1)(b) do not apply in the case of a *deposit-based stakeholder product*.

**5A.4.3 G** *COB 5A Annex 1 G* contains *guidance* on the steps a *firm* could take to ensure it complies with the requirements in *COB 5A.4.2R* (1); it also includes *guidance* on providing advice on *stakeholder pensions* that will comply with *COB 5A.4.5R*.

**5A.4.4 R** A *firm* must not recommend or agree that a *customer* make contributions to an *ISA* in excess of the Inland Revenue's *ISA* limits.

**5A.4.5 R** A *firm* must not, in the course of *providing basic advice*, advise a *customer* on the contribution levels to a *stakeholder pension* needed to achieve a specific income in retirement.

**Procedure on making a recommendation**

**5A.4.6 R** On making a recommendation to acquire a *stakeholder product* a *firm* must, subject to *COB* 5A.4.7R, 5A.4.8R and 5A.4.9R, take reasonable steps to ensure that prior to the conclusion of a contract with the *customer* the *representative*:

- (1) explains to the *customer*, if necessary in summary form, the "aims", "risks" and "commitment" sections of the appropriate *key features* together with such other explanation of the *product* as will enable the *customer* to make an informed decision whether to accept the recommendation;
- (2) provides the *customer* with a summary sheet, in a *durable medium*, setting out for each *product* recommended:
  - (a) the specific amounts that the *customer* wishes to pay into each *product*;
  - (b) the reasons for the recommendation, including any information provided by the *customer* on which the recommendation is based, including the *customer's* attitude to risk;
- (3) informs the *customer* that in determining any subsequent complaint the *Ombudsman* may take into account the limited information on which the recommendation is based and that the recommendation is not tailored to take account of those aspects of a *customer's* financial needs and circumstances not covered by its sales process.

**5A.4.7 R** *COB* 5A.4.6R (1) does not apply to a recommendation to acquire a *deposit-based stakeholder product*.

**5A.4.8 R** A *firm* may provide the summary sheet required by *COB* 5A.4.6R (2) subsequent to the conclusion of the contract if requested to do so by the *customer* as long as it completes the steps in *COB* 5A.4.9R (1) and (2) prior to concluding a contract with the *customer*.

**5A.4.9 R** A *firm* which concludes the sale of a *stakeholder product* by telephone must take reasonable steps to ensure that its *representatives*:

- (1) read through the summary sheet required by *COB* 5A 4.6R (2);
- (2) inform the *customer* that in determining any subsequent complaint the *Ombudsman* may take into account the limited information on which the recommendation is based and that the recommendation is not tailored to take account of those aspects of a *customer's* financial needs and circumstances not covered by its sales process;

- (3) send the *customer* as soon as possible after that a copy of the *firm's* summary sheet, and the completed answers and questions, in a *durable medium*.

#### Record of recommendations

- 5A 4.10 R A *firm* must keep in a *durable medium* a record of each recommendation to acquire a *stakeholder product* and the *customer's* summary sheet and such a record must be kept for not less than six years from the date of the recommendation.

#### COB 5A Annex 1G sales processes for stakeholder products

This Annex forms part of COB 5A.4.3G and gives *guidance* on the standards and requirements to which a *firm* may have regard in designing a sales process for *stakeholder products* which meets the requirements of COB 5A.4.2R.

#### General Standards – all sales

1. A sales process for *stakeholder products* may allow the *representative* administering it to depart from scripted questions where this is desirable to enable the *customer* to better understand the points that need to be made provided this is compatible with the *representative's* competence and the degree of support offered by the *firm's* software and other systems. A software based system is more likely to provide an adaptable means of providing prompts and support for *representatives* which may accordingly support a more flexible sales process.
2. Questions, statements and warnings provided to a *customer* should be short, simple and couched in plain language that *customers* will understand. Questions should address one issue at a time.
3. The sales process should enable the *customer* to exit freely and without pressure at any stage and should make provision for the *representative* to terminate the process if at any stage it appears that there is no likelihood of any *product* being suitable for the *customer* (whether by reason of the affordability of *products* for the *customer*, the need to address other financial priorities (see below), the mis-match of risk or otherwise).
4. Where necessary the sales process should incorporate procedures to allow uncertainties in the *customer's* answers to be addressed before proceeding further and should generally reflect caution about proceeding further if clarification or further information cannot be obtained during the process (this would be likely to be the case for example if a *customer* were unable to confirm whether he or she was eligible for membership of an *occupational pension scheme*).

#### Preliminary - all sales

5. The following preliminary information and explanation should be given to the *customer* :

- (a) only *basic advice* will be given about *stakeholder products*;
  - (b) *stakeholder products* are intended to provide a relatively simple and low-cost way of investing and saving;
  - (c) the *range of products* on which the representative will give advice to that *customer*;
  - (d) the *customer* will be asked a series of questions about his or her circumstances and needs and at the end of the procedure he or she may be recommended to acquire a *stakeholder product*;
  - (e) that the assessment of whether a *stakeholder product* is suitable will be made without a detailed assessment of the *customer's* needs but will be based only upon the information disclosed during the questioning process; and
  - (f) the *customer's* answers will be noted and that at the end of the process, if a recommendation to acquire a *stakeholder product* is made, the *customer* will be provided with a copy of the completed questionnaire.
6. Following 5, the *customer* should be asked if he or she wishes to proceed and, if not, the sales process should cease.

#### **Affordability - all sales**

7. If it appears that the *customer* will be likely to be unable to afford a *stakeholder product*, the sale should be terminated at that stage and the *customer* given an explanation together with a copy of the questions and answers completed to that point.

#### **Financial Priorities and Debt - all sales**

8. A *customer* should be assessed to ascertain other possible financial priorities such as the need for insurance protection for self or dependents, the need for access to liquid cash to meet an emergency, or, a need to reduce a level of existing debt and, if appropriate, the *customer* should be given an unambiguous warning about the desirability of meeting those other priorities before making payments to a *stakeholder product*.
9. A stronger warning about the desirability of addressing debt as a priority should be given if it appears that the *customer* is significantly indebted, and particularly where there is a strong indication that such debt commitments may render any new commitment unaffordable in the short-term. For this purpose a *firm* should consider using a threshold or indicator to decide whether a *customer* should be excluded on the basis of affordability. Examples may include where the *customer* has (a) annual unsecured debt repayments in excess of 20% of gross annual income or (b) four or more active forms of unsecured credit or (c) has consistently reached his overdraft limit. A *firm* should review its chosen indicator or threshold regularly to ensure that it reflects prevailing economic conditions and takes account of industry best practice.
10. A *firm* should clearly explain the information it is seeking in respect of a *customer's* 'debt' and consider the use of a range of alternative words, such as 'loans', 'repayable

student loans 'borrowing' or 'other forms of credit', to ensure all relevant information is obtained. A *firm* may use a simple reckoner to assess *customer* debt but should be conscious of the nature of, and not give impression that they are providing anything more than, *basic advice*.

11. After a *firm* has given either or both of the warnings mentioned in 8 and 9 above, the *customer* should be invited to consider whether the sales process should be terminated at that stage.

### **Saving and investment objectives – all sales (except establishing a stakeholder CTF)**

12. A *customer's* savings and investment objectives, including the period over which the *customer* wishes to save or invest, should be ascertained including whether:
  - (a) early access to some or all of the amount saved or invested could be important;
  - (b) the *customer* wishes to save or invest for retirement; or whether
  - (c) the *customer* wants to accumulate a specific sum by a specific date.
13. If the information obtained under 12 above indicates that the *customer's* objective:
  - (a) is as described in 12 (c) then normally no *CIS*, *linked life stakeholder product* or topping up of a *stakeholder CTF* should be recommended; or
  - (b) is to save or invest for the short term only or that early access to the whole accumulated sum may be important, then no *CIS*, *linked life stakeholder product*, *stakeholder pension* or topping up of a *stakeholder CTF* should normally be recommended.

### **Tolerance of risk – all sales**

14. If a *customer* is not, in any circumstances, willing to accept any risk of the capital value of an investment being reduced then normally no *CIS*, *linked life stakeholder product*, or *stakeholder CTF* should be recommended. However a *firm* may, if it is appropriate, explain the effect of inflation on long-term savings especially in relation to pensions and invite the *customer* to consider his attitude to risk in the light of that explanation.
15. If a *customer* is willing to accept the risk of capital reduction in some circumstances but not others then, before any recommendation to acquire a *CIS* or *linked life stakeholder product* is made, the *customer* should be reminded of the other circumstances in which he or she is unwilling to accept risk to capital.

### **Stakeholder pensions**

16. A *stakeholder pension* should not be recommended and instead the *customer* should be advised to seek alternative or further *advice* if it appears that the *customer* :
  - (a) has or will have access to an *occupational pension scheme*; or

- (b) is likely to view income in retirement from state benefits as sufficient; or
- (c) already has a pension to which he or she could make further contributions; or
- (d) wishes to retire within five years.

17. In addition to providing the advice in 16, a *firm* may also want to advise the customer that there may be more beneficial courses of action than buying a *stakeholder pension* (for example joining an *occupational pension scheme*).
18. A *firm* designing a sales process for use in the workplace may take account of the benefits offered by the employer. If a *firm* recommends a *stakeholder pension* on the basis of benefits provided by an employer then it should explain the basis of the recommendation to the *customer* and suggest that the *customer* seek *advice* if he or she has any concerns.
19. A *firm* should design its processes with a view to addressing the risk that *customers* will fail to appreciate the significance of questions about their pension provision and should accordingly incorporate a range of questions and information designed to foster the *customer's* understanding of the issues and to elicit appropriate information.
20. *Customers* should be told that a *stakeholder pension* is life-styled and what this means.
21. A *firm* may provide a copy of the pension table specified in COB 6 Annex 1 R for the *customer's* reference but in doing so should also provide and explain the caveats and assumptions behind the table. A *firm* should make it clear that the decision on how much to invest is the *customer's* responsibility and that he should get further advice if has any concerns.

### **Child Trust Funds**

22. A *firm* is reminded of its obligation to provide a *customer* with the information relating to *stakeholder CTFs* that is specified in COB 6.5.40R (7)(a), (b), (d) and (e).

### **ISAs**

23. It should be ascertained whether the *customer* has already opened an *ISA* (whether a "maxi" or "mini" version) and if so whether it would be appropriate for the *customer* to open a non-*ISA* version of the same *product*.

### Amendment to Chapter 6 of COB

6.3 Post-sale confirmation: life policies

...

Exceptions to post-sale confirmation



6.3.6 R A *long term insurer* need not send or give the post-sale confirmation required by COB 6.3.3R when:

...

- (3) the *life policy* is purchased by the trustees or manager of a *stakeholder pension scheme* or if the *life policy* is otherwise sold as a *stakeholder product*;

...

6.5.15 R A *firm* must include a *projection*, illustrating how the principal terms of the proposed transaction apply to the *private customer*:

- (1) where the proposed transaction is for a *life policy* (other than:

(a) a *long-term care insurance contract* which is a *pure protection contract*); ~~or~~

(b) a *linked life stakeholder product*;

(c) one that relates to a CTF or a stakeholder product sold through basic advice;

- (2) where the proposed transaction does not relate to a CTF or a stakeholder product sold through basic advice and is for a scheme or a linked life stakeholder product;

...

...

6.5.19 R (1) A *life policy projection* within *key features* must be specified to the *private customer*, calculated on the basis of the *private customer's* age and sex, the sum assured, the *premium* and other principal factors of the proposed *life policy* unless:

(a) the *life policy* is a single premium *life policy*; or

...

(d) the *key features* are part of a *direct offer financial promotion*; ~~or~~

(e) the projection is in respect of a stakeholder product (which is not a stakeholder pension);

...

...

6.5.25 R When completing COB 6.5.24R a *firm* must:

- (1) under the heading "the early years" include figures for the first five years of the *life policy* or, if the *life policy* has a fixed term of less than five years, as many of them as fall before the maturity date;

...

- (9) (b) the standard ten-year figure must be used for the reduction in yield and the accompanying words amended accordingly;
- (10) in the case of a stakeholder product (which is not a stakeholder pension) the table may be given on the basis of generic figures and values.

...

6.5.32 R When including the contents of COB 6.5.31R a *firm* must replace the wording in brackets as directed by the instructions in those brackets and:

- (2) when the inclusion of a *scheme projection* within the *key features* is compulsory in accordance with *cob* 6.5.13R (2), include figures calculated in accordance with COB 6.6 (Projections):

...

- (10) in the case of a stakeholder product (which is not a stakeholder pension) the table may be given on the basis of generic figures and values.

...

#### CTFs and stakeholder products: annual charges

6.5.37A R (1) If a *firm* imposes one annual charge including expenses, it need not make the detailed disclosures required by COB 6.5.24R and COB 6.5.30R; but if it does not make those disclosures, it must instead include either:

- (a) the following statement (the last sentence must be included if and only if it is clear at the time of acquisition that the annual charge will reduce to r % after a fixed period):

"There is an annual charge of [y]% of the value of the funds you accumulate. If your fund is valued at £250 throughout the year, this means we deduct [£250 x y/100] that year. If your fund is valued at £500 throughout the year, this means we deduct [£500 x y/100] that year. After ten years these deductions would reduce to [£250 x r/100] and [£500 x r/100] respectively."

or;

- (b) the information required by COB 6.5.20R.

...

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...	...	...	...	...
<u>COB 5A.3.4R</u>	<u>The scope of basic advice which a firm's appointed representative is permitted to give (including the range of stakeholder products on which each appointed representative advises.)</u>	<u>The scope of basic advice each appointed representative is permitted to advise</u>	<u>At the time an appointed representative is permitted to provide basic advice.</u>	<u>6 years from the date on which the record is superseded by a more up-to-date record</u>
<u>COB 5A.3.6R (1)</u>	<u>A firm's scope and range of stakeholder products</u>	<u>A firm's scope and range of stakeholder products</u>	<u>When a firm commences providing basic advice</u>	<u>6 years from the date on which the record is superseded by a more up-to-date record</u>
<u>COB 5A.3.6R (4)</u>	<u>The range of stakeholder products on which a firm's basic advice to a private customer is based</u>	<u>The range of stakeholder products on which a firm's basic advice to a private customer is based</u>	<u>When a firm commences providing basic advice</u>	<u>6 years from the date on which the advice is given</u>

## Annex C

### Amendments to Training and Competence sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### 2.1.4 R Table Activities to which TC 2 Applies

	Activity	Extent of Application
1. <i>Employees</i> engaging in:	<u>Advising and dealing</u>  (a) <i>advising on investments</i> which are, and dealing with or for <i>clients</i> in, <i>securities</i> (other than <i>stakeholder pension schemes</i> or <i>broker funds</i> ) and <i>derivatives</i> ;  ...  (r) <i>advising ... contracts</i> ;  (s) <u><i>providing basic advice on stakeholder products</i> (other than a <i>deposit-based stakeholder product</i>).</u>	If the activity...

...

2.4.2 R (2) (1)(a) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract* or is *providing basic advice on stakeholder products*.

...

2.4.5 R (2) (1)(b) does not apply when this activity is an *insurance mediation activity* in relation to a *non-investment insurance contract* or is *providing basic advice on stakeholder products*.

...

**2.5.1A R The time limits to which TC 2.5.1 R applies**

Activity in TC2.1.4.R	Examination must be passed
1.(a)-(c)	before starting the activity
...	...
(s)	<u>(no examination requirement)</u>

...

2.7.5 R If an *employee* who is not assessed as competent is engaging in the activity of giving advice on *investments* which are *packaged products* (other than *basic advice*) to *private customers*, the *firm* must ensure that the individual supervising that *employee*:

...

## Annex D

### Amendments to the Authorisation manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### Providing basic advice on stakeholder products

- 2.7.14A      G      This activity covers advice in the form of a recommendation given to a retail consumer. The recommendation must relate to a stakeholder product and certain conditions must be met. These conditions are based on the need for the adviser to make an assessment of the consumer's needs based on the answers that the consumer provides to a series of pre-scripted questions. A fuller description of the activity is given in AUTH 2.7.14BG and explains what is meant by "retail customer". This activity is separate to the regulated activity of advising on investments (see AUTH 2.7.15G (Advising on investments)). The existence of this separate advising activity does not prevent a person from giving advice on stakeholder products in circumstances that do not satisfy the conditions set out in AUTH 2.7.14BG. But such advice is likely to amount to advising on investments unless the stakeholder product is a deposit. Neither does the existence of the activity prevent a person from selling stakeholder products in any other manner provided the person has the appropriate permission.
- 2.7.14B      G      A person ('P') carries on the regulated activity of providing basic advice on a stakeholder product when:
- (1) P gives the advice:
    - (a) to a person ('C') who does not receive the advice in the course of a business that he carries on; and
    - (b) in the course of a business that P carries on;
  - (2) the advice is on the merits of C opening or buying a stakeholder product;
  - (3) the following conditions are met:
    - (a) P asks C questions to enable P to assess whether a stakeholder product is appropriate for C;
    - (b) if P, relying solely on the information provided by C in response to the questions referred to in (a), assesses that a stakeholder product is appropriate for C, P:
      - (i) describes that product to C; and
      - (ii) gives a recommendation of that product to C; and

(4) C has indicated to P that he has understood the description and recommendation referred to in (3)(b).

2.7.16A      G      In certain circumstances, the activity of *advising on investments* can also amount to *providing basic advice on a stakeholder product* (see *AUTH 2.7.14A* (Providing basic advice on stakeholder products)).

...

*AUTH 2*      G  
Annex 2

Regulated activities and the permission regime

*AUTH 2* Annex 2 Table 1:

Regulated activity	Specified investment in relation to which the regulated activity (in the corresponding entry in column 1) may be carried on
...	
<b>Designated investment business [see note 1A and 1B to Table 1]</b>	
...	
(p) <i>establishing, operating or winding up a stakeholder pension scheme</i> (article 52)	
(pp) <i>providing advice on a stakeholder product</i> (article 52B)	<u>those <i>specified investments</i> that are also a <i>stakeholder product</i> [see note 7])</u>
...	

...

Note 7:

A stakeholder product is defined in the *Glossary* as:

- an investment of a kind specified in the *Stakeholder Regulations*;
- a stakeholder pension scheme; and
- a stakeholder CTF.

...

3.6.4 G (5) COB 4.1.4R does not apply to a firm which, in relation to any customer, intends only to provide advice on a stakeholder product.

...

App 1.24.3 G Each of the aspects referred to in *AUTH* App 1.24.2G is considered in greater detail in *AUTH* App 1.25 to *AUTH* 1.29. In addition, under article 52A of the *Regulated Activities Order providing advice on a stakeholder product is a regulated activity and under article 56 of the Regulated Activities Order...*



## Annex E

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through indicates deleted text. Where an entire new section is inserted, the place that it goes is indicated and the text is not underlined.

...

12.2.7 G (1) ...

...

- (h) ~~advising on investments (article 53 of the *Regulated Activities Order*) (that is in summary, on any designated investment, funeral plan contract or right to or interest in a funeral plan); providing basic advice on stakeholder products (article 52B of the *Regulated Activities Order*);~~
- (i) ~~advising on regulated mortgage contracts (article 53A of the *Regulated Activities Order*); and advising on investments (article 53 of the *Regulated Activities Order*) (that is in summary, on any designated investment, funeral plan contract or right to or interest in a funeral plan);~~
- (j) ~~agreeing to carry on a regulated activity (article 64 of the *Regulated Activities Order*) where the regulated activity is one of those in (a) to (g);~~ advising on regulated mortgage contracts (article 53A of the *Regulated Activities Order*); and
- (k) agreeing to carry on a regulated activity (article 64 of the *Regulated Activities Order*) where the regulated activity is one of those in (a) to (h).

...

12.2.8 G (2) The permitted scope of appointment of an *introducer appointed representative* does not include in particular:

...

...

(d) *advising on investments, providing basic advice on stakeholder products, advising on regulated mortgage contracts or other activity that might reasonably lead a customer to believe that he had received basic advice or advice on investments or on regulated mortgage contracts or that the introducer appointed representative is permitted to provide basic advice or give advice on investments or on regulated mortgage contracts.*

12.5.2 G (2) ...

(e) *provides basic advice on stakeholder products;*

## Annex F

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

Insert or amend the following definitions in the appropriate alphabetical position:

<u>basic advice</u>	see <u>providing basic advice on a stakeholder product</u>
<u>branded fund</u>	A life policy or a regulated collective investment scheme other than a broker fund which is available as an investment only or mainly to the clients of a particular <del>independent intermediary</del> firm other than a provider firm.  (a) ... into which cash contributions of that <del>independent intermediary's</del> firm's customers have been made;  (b) ... into which the cash contributions of that <del>independent intermediary's</del> firm's customers have been made;
<u>CIS stakeholder product</u>	<u>the stakeholder product specified by regulations 5 (units in certain collective investment schemes) and 7 of the Stakeholder Regulations;</u>
<u>combined initial disclosure document (CIDD)</u>	information about the scope and nature of the services offered by a firm in relation to:  (a) a combination of two or more of the following:  <del>(a)(i)</del> packaged products;  (ii) non-investment insurance contracts;  (iii) regulated mortgage contracts;  (iv) regulated lifetime mortgage contracts;  <u>or</u>  (b) <u>a combination of two or more of the following:</u>  (i) <u>stakeholder products;</u>  (ii) <u>regulated lifetime mortgage contracts;</u>  (iii) <u>regulated mortgage contracts;</u>  (iv) <u>non-investment insurance contracts.</u>

<u>deposit-based stakeholder product</u>	<u>the stakeholder product specified by regulation 4 (certain deposit accounts) of the Stakeholder Regulations;</u>
<u>designated investment business</u>	Any of the following activities, specified in Part II of the <i>Regulated Activities Order</i> (Specified Activities), which is carried on by way of business: <ul style="list-style-type: none"> <li>(a) ...</li> <li>(p) <u>providing basic advice on a stakeholder product (article 52B).</u></li> </ul>
<u>initial disclosure document (IDD)</u>	information about the scope and nature of the services offered by a <i>firm</i> in relation to <u>packaged products</u> as required by COB 4.3.7R; or <u>stakeholder products</u> as required by COB 5A.2.1R (1).
<u>linked life stakeholder product</u>	<u>the stakeholder product specified by regulations 6 and 7 (rights under certain linked long-term contracts) of the Stakeholder Regulations;</u>
<u>packaged product</u>	<ul style="list-style-type: none"> <li>(a) a <i>life policy</i></li> <li>(b) a <i>unit</i> in a <i>regulated collective investment scheme</i>;</li> <li>(c) an interest in an <i>investment trust savings scheme</i>;</li> <li>(d) a <i>stakeholder pension scheme</i></li> </ul> <p>whether or not (in the case of (a), (b) or (c)) held within a <i>PEP</i><del> or</del>, an <i>ISA</i> or a <i>CTF</i> and whether or not the <u>packaged product</u> is also a <u>stakeholder product</u>.</p>
<u>private customer</u>	<ul style="list-style-type: none"> <li>(1) (except in COB 3, COB 4.2 and COB 6.4) a <i>client</i> who is not a <i>market counterparty</i> or an <i>intermediate customer</i>, including: <ul style="list-style-type: none"> <li>...</li> <li>(e) <u>a person to whom a firm provides basic advice on stakeholder products;</u></li> <li>...</li> </ul> </li> </ul>
<u>providing basic advice on a stakeholder product</u>	<u>the regulated activity, specified in article 52B of the Regulated Activities Order (providing basic advice on stakeholder products)], which is in summary, advising on certain relatively low cost products by means of questions.</u>
<u>regulated activity</u>	(in accordance with section 22 of the <i>Act</i> (The classes of activity and categories of investment)) any of the following activities specified in Part II of the <i>Regulated Activities Order</i> (Specified Activities): <ul style="list-style-type: none"> <li>...</li> <li>(oa) <u>providing basic advice on a stakeholder product (article 52B);</u></li> </ul>

(p) ...

range see range of packaged products and range of stakeholder products

range of packaged products, range (in relation to a firm) the range of packaged products on which the firm gives advice on investments to private customers (see COB 5.1.6 A) or if appropriate the list of packaged products in which the firm deals.

range of stakeholder products, range (in relation to a firm) the range of stakeholder products on which the firm gives advice (see COB 5A.3.2R);

Delete the existing definition for ‘representative’ and replace with the following definition:

representative an individual who:

- (a) is appointed by a *firm*, or by an *appointed representative* of a *firm*, to carry on any of the following activities:
  - (i) *advising on investments*;
  - (ii) *providing basic advice on stakeholder products*;
  - (iii) *arranging (bringing about) deals in investments* ;
  - (iv) *dealing in investments*; or
- (b) although not appointed to do so, carries on any of the activities in (i) to (iii) on behalf of a *firm* or its *appointed representative*.

smoothed linked long term stakeholder product the stakeholder product specified by regulations 6, 7 and 8 (smoothed linked long term contracts) of the Stakeholder Regulations;

stakeholder CTF a CTF that has the characteristics and complies with the conditions set out in paragraph 2 of the schedule to the CTF Regulations;

stakeholder product (as defined in article 52B(3) of the Regulated Activities Order):

- (a) a stakeholder CTF; or
- (b) a stakeholder pension scheme; or
- (c) an investment of a kind specified in the Stakeholder Regulations.

Stakeholder Regulations the Financial Services and Markets Act 2000 (Stakeholder Products) Regulations 2004 (SI 2004/2738).

**CLIENT ASSETS (REVISED CFTC PART 30 ORDER)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 139 (Miscellaneous ancillary matters);
  - (3) section 156 (General supplementary powers); and
  - (4) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 1 January 2005.

**Amendments to the Client Assets sourcebook**

- D. The Client Assets sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Supervision manual**

- E. The Supervision manual is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Client Assets (Revised CFTC Part 30 Order) Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### Amendments to the Client Assets sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

Commodity Futures Trading Commission Part 30 exemption order

- 4.3.106A G United States (US) legislation restricts the ability of non-US firms to trade on behalf of US customers on non-US futures and options exchanges. The relevant US regulator (the CFTC) operates an exemption system for firms authorised by the FSA. The FSA sponsors the application from a firm for exemption from Part 30 of the General Regulations under the US Commodity Exchange Act in line with this system. The application forms and associated information can be found on the FSA website in the “Forms” section.
- 4.3.107 ~~R~~ G A firm with a Part 30 exemption order undertakes to the CFTC that it will refuse to allow any US customer to opt not to have ~~must treat~~ his money treated as client money ~~the money of any US resident investor which if it~~ is held or received in respect of transactions on non-US exchanges, unless that US customer is an “eligible contract participant” as defined in section 1a(12) of the Commodity Exchange Act, 7 U.S.C.. In doing so, the firm is representing that it will not make use of the opt-out arrangements in CASS 4.1.8G to CASS 4.1.11R in relation to that business.

...

## **Annex B**

### **Amendments to the Supervision manual**

In this annex an entire section of text is being deleted, the location of this text is indicated and the text is not shown struck through.

The Supervision manual is amended by deleting Chapter 19, SUP 19 (Commodity Futures Trading Commission Part 30 exemption), in its entirety.

SUP 19      [deleted]



**CLIENT ASSETS SOURCEBOOK (AMENDMENT NO 2) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the powers and related provisions in the following sections of the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 139(1) (Miscellaneous ancillary matters); and
  - (3) section 156 (General supplementary powers).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 14 January 2005.

**Amendments to the Handbook**

- D. The Client Assets sourcebook is amended in accordance with Annex A to this instrument.
- E. The Glossary of definitions is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Client Assets Sourcebook (Amendment No 2) Instrument 2004.

By order of the Board  
18 November 2004

Amended by Addendum  
25 November 2004

## Annex A

### Amendments to the Client Assets sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

#### CASS Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision : dates in force	Handbook provision coming into force
<u>3</u>	<u>CASS 5.1 to 5.6</u>	<u>R</u>	<u>Apply in relation to <i>money</i> (and where appropriate <i>designated investments</i>) held by a <i>firm</i> on 14 January 2005 (being <i>money</i> or <i>designated investments</i> to which CASS 5.1 to 5.6 would not otherwise apply) to the extent that any such <i>money</i> (or <i>designated investments</i>) relate to business carried on before 14 January 2005 and which would, if conducted on or after 14 January 2005, be an <i>insurance mediation activity</i>.</u>	<u>Indefinitely</u>	<u>14 January 2005</u>
<u>4</u>	<u>CASS 5.1.5A</u>	<u>R</u>	<u>A <i>firm</i> will satisfy the requirements of this paragraph, and <i>money</i> is <i>client money</i>, notwithstanding that an <i>insurance undertaking</i> which is the <i>firm</i>'s counterparty to an agreement required by CASS 5.1.5AR has not given written consent to its interests under the trusts (or in Scotland agency) in CASS 5.3.2R or CASS 5.4.7R being subordinated to the interests of the <i>firm</i>'s other <i>clients</i>.</u>	<u>14 January 2005 for 6 months</u>	<u>14 January 2005</u>
<u>5</u>	<u>CASS 5.3.2</u>	<u>R</u>	<u>The interests of a <i>firm</i>'s <i>clients</i> which are <i>insurance undertakings</i> will rank equally with the interests of the <i>firm</i>'s</u>	<u>14 January 2005 for 6 months</u>	<u>14 January 2005</u>

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision : dates in force	Handbook provision coming into force
			<u>other clients.</u>		
<u>6</u>	<u>CASS 5.4.7</u>	<u>R</u>	<u>A firm will satisfy the requirements of this rule notwithstanding that the deed referred to in CASS 5.4.6R provides that money (and if appropriate designated investments) are held on terms which provide for the interests of the firm's clients which are insurance undertakings to rank equally with the interests of the firm's other clients.</u>	<u>14 January 2005 for 6 months</u>	<u>14 January 2005</u>
<u>7</u>	<u>CASS 5.5.65</u>	<u>R</u>	<u>A firm may for the purpose of calculating its client money resource disregard any money which the firm had before 14 January 2005 transferred to an intermediate broker in circumstances analogous to those described in CASS 5.5.34R.</u>	<u>14 January 2005 for 12 months</u>	<u>14 January 2005</u>

...

- 5.1.4A     R     (1)     A firm which, in relation to a service charge, receives or holds client money and is required to segregate and account for such money in accordance with section 42 of the Landlord and Tenant Act 1987 ("the 1987 Act") will, if it complies with that provision and with (3), be deemed to comply with CASS 5.3 to 5.6.
- (2)     Paragraph (1) also applies to a firm in Scotland or in Northern Ireland if in acting as a property manager the firm receives or holds a service charge and complies (so far is practicable) with section 42 of the 1987 Act as if the requirements of that provision applied to it.
- (3)     In addition to complying with (1), a firm must ensure that an account in which money held pursuant to the trust fund mentioned in section 42(3) of the 1987 Act satisfies the requirements in CASS 5.5.49R.

- 5.1.5 R Subject to CASS 5.1.5AR ~~M~~money is not *client money*:  
 ...
- 5.1.5 A R CASS 5.1.5R(1)(b) and (2) do not apply, and hence *money is client money*, in any case where:
- (1) in relation to an activity specified in CASS 5.2.3R(1)(a) to (c), the *insurance undertaking* has agreed that the *firm* may treat *money* which it receives and holds as agent of the *undertaking*, as *client money* and in accordance with the provisions of CASS 5.3 to 5.6; and
- (2) the agreement in (1) is in writing and adequate to show that the *insurance undertaking* consents to its interests under the trusts (or in Scotland agency) in CASS 5.3.2R or CASS 5.4.7R being subordinated to the interests of the *firm's* other *clients*.
- 5.1.6 R ~~Except where a *firm* and an *insurance undertaking* have (in accordance with CASS 5.1.5AR) agreed otherwise, for the purposes of CASS 5.1 to 5.6 an *insurance undertaking* (when acting as such) with whom a *firm* conducts *insurance mediation activity* is not to be treated as a *client* of the *firm*.~~
- Purpose
- 5.1.7 G ...
- (2) There are two particular approaches which a *firm* can adopt which reflect options given in article 4.4. The first is to provide by law or contract for a transfer of risk from the *insurance intermediary* to the *insurance undertaking* (CASS 5.2). The second is that *clients' money* is strictly segregated by being transferred to *client accounts* that cannot be used to reimburse other creditors in the event of the *firm's* insolvency (CASS 5.3 and 5.4 provide different means of segregation). CASS 5.1.5AR permits a *firm* subject to certain conditions to treat *money* which it collects as agent of an *insurance undertaking* as *client money*; the principle of strict segregation is, however, satisfied because such *undertakings* must agree to their interests being subordinated to the interests of the *firm's* other *clients*.
- ...
- 5.2.1 G If a *firm* holds *money* as agent of an *insurance undertaking* then the *firm's clients* (who are not *insurance undertakings*) will be adequately protected to the extent that the *premiums* which it receives are treated as being received by the *insurance undertaking* when they are received by the agent and claims *money* and *premium* refunds will only be treated as received by the *client* when they are actually paid over. The *rules* in CASS 5.2 make provision for

agency agreements between *firms* and *insurance undertakings* to contain terms which make clear when *money* should be held by a *firm* as agent of an undertaking. *Firms* should refer to *CASS 5.1.5R* to determine the circumstances in which they may treat *money* held on behalf of *insurance undertakings* as *client money*. *Money* is not *client money* when a *firm* holds *money* as agent for an *insurance undertaking* to which *premiums* are, or will become, payable or from whom claims *money* or *premium* refunds are received for onward payment to the *firm's client*. This is because for the purposes of *CASS 5.1* to *5.6* an *insurance undertaking* with whom a *firm* transacts *insurance mediation activity* is not treated as a *client* of the *firm*. Where a *firm* acts as the agent of an *insurance undertaking* (for the purposes of receiving *premiums*, claims *money* and *premium* refunds) the *firm's clients* will be adequately protected because *premiums* will be treated as being received by the *insurance undertaking* when they are received by the agent and claims *money* and *premium* refunds will only be treated as received by the *client* when they are actually paid over.

- 5.2.2 G (1) Agency agreements between *insurance intermediaries* and *insurance undertakings* ... Accordingly such *money* is not, except where a *firm* and an *insurance undertaking* have in compliance with *CASS 5.1.5AR* agreed otherwise, *client money* for the purposes of *CASS 5*.
- (2) Other introductory agency agreements may also, depending on their precise terms, satisfy some or all of the requirements of the type of written agreement described in *CASS 5.2.3R* which will result in a transfer of risk for the purpose of *CASS 5.2*. It is desirable that an *intermediary* ...
- 5.2.3 R ...
- (3) Where a *firm* holds, or is to hold, *money* as agent for an *insurance undertaking* it must ensure that it informs those of its *clients* which are not *insurance undertakings* and whose transactions may be affected by the arrangement ...
- (4) A *firm* may (subject to the consent of the *insurance undertaking* concerned) include in an agreement in (1) provision for *client money* received by ~~an~~ its appointed representative, *field representatives* and other agents to be held ~~by the representative~~ as agent for the *insurance undertaking* (in which event the *firm* must ensure that the *representative* or agent provides the information to *clients* required by (3)).
- 5.2.4 G *Firms* are reminded that *CASS 5.1.5AR 5.1.5R(1)(b)* provides that, if the *insurance undertaking* has agreed in writing, *money* held in accordance with an agreement made under *CASS 5.2.3R* ~~is not~~ may be treated as *client money* and ~~in accordance with the rules in *CASS 5*, that *money* may (but not otherwise)~~ must not be kept in a *client bank account*.
- 5.2.5 G A *firm* which provides for the protection of a *client* (which is not an

*insurance undertaking*) under CASS 5.2 is relieved of the obligation to provide protection for that *client* under CASS 5.3 or CASS 5.4 to the extent of the items of ~~the~~ *client money* protected by the agency agreement.

5.2.6 G A *firm* may, in accordance with CASS 5.2.3R(4), arrange for an *insurance undertaking* to accept responsibility for the *money* held by its *appointed representatives, field representatives, and other agents*, in which event CASS 5.5.18R to CASS 5.5.25G will not apply.

...

5.3.2 R A *firm* (other than a *firm* acting in accordance with CASS 5.4) receives and holds *client money* as trustee (or in Scotland as agent) on the following terms:

- (1) for the purposes of and on the term of CASS 5.3, CASS 5.5 and the *client money (insurance) distribution rules*;
- (2) subject to ~~(34)~~, for the *clients (other than clients which are insurance undertakings when acting as such)* for whom that *money* is held, according to their respective interests in it;
- (3) after all valid claims in (2) have been met, for *clients* which are *insurance undertakings* according to their respective interests in it;
- ~~(34)~~ on the failure of the *firm*, for the payment of the costs properly attributable to the distribution of the *client money* in accordance with (2) and (3); and
- ~~(45)~~ after all valid claims and costs under (2) ~~and (3)~~ to (4) have been met, for the *firm* itself.

...

5.4.4 R A *firm* may not handle *client money* in accordance with the *rules* in this section unless each of the following conditions is satisfied:

- (1) ...
- (5) in relation to each of the *clients* for whom the *firm* holds *money* in accordance with CASS 5.4, the *firm* must take reasonable steps to ensure that its *terms of business* or other *client agreements* adequately explain, and obtain the *client's* informed consent to, the *firm* holding the *client's money* in accordance with CASS 5.4 (and in the case of a *client* which is an *insurance undertaking* (when acting as such) there must be an agreement which satisfies CASS 5.1.5AR).

...

5.4.6 R Except to the extent that a *firm* acts in accordance with CASS 5.3, A *firm*

must not receive or hold any *client money* unless it does so as trustee (or, in Scotland, as agent) and has properly executed a deed (or equivalent formal document) to that effect.

#### Contents of trust deed

5.4.7 R The deed referred to in CASS 5.4.6R must provide that the *money* (and if appropriate the *designated investments*) are held:

...

(2) subject to ~~(34)~~, for the *clients* (other than *clients* which are *insurance undertakings* when acting as such) for whom that *money* is held, according to their respective interests in it;

(3) after all valid claims in (2) have been met for *clients* which are *insurance undertakings* according to their respective interests in it;

~~(34)~~ on the *failure* of the *firm*, for the payment of the costs properly attributable to the distribution of the *client money* in accordance with (2) and (3); and

~~(45)~~ after all valid claims and costs under (2) ~~and (3)~~ to (4) have been met, for the *firm* itself.

...

5.5.10 R If it is prudent to do so to ensure that *client money* is protected (and provided that doing so would otherwise be in accordance with CASS 5.5.63R~~(2)(b)(1)(b)(ii)~~) ...

...

5.5.11A G When a *firm* acts in accordance with CASS 5.3 (Statutory trust) it should not make a payment from the *client bank account* unless it is satisfied on reasonable grounds that the *client* has provided it with cleared funds. Accordingly, a *firm* should normally allow a reasonable period of time for cheques to clear. If a withdrawal is made and the *client's* cheque is subsequently dishonoured it will be the *firm's* responsibility to make good the *shortfall* in the account as quickly as possible (and without delay whilst a cheque is re-presented).

...

5.5.16 R (1) A *firm* may draw down *commission* from the *client bank account* if:

(a) it has received the *premium* from the *client* (or from a *third party premium* finance provider on the *client's* behalf); and

- (b) this is consistent with the firm's terms of business ~~terms of reference of~~ which it maintains with the relevant client and the insurance undertaking to whom the premium is will become payable;

and the *firm* may draw down *commission* before payment of the *premium* to the *insurance undertaking*, provided that the conditions in (a) and (b) are satisfied.

- (2) If a *firm* receives a *mixed remittance* (that is part *client money* and part other *money*), it must:
- (a) pay the full amount into a *client bank account* in accordance with *CASS 5.5.5R* ; and
- (b) pay the *money* that is not *client money* out of the *client bank account* as soon as reasonably practicable and in any event by not later than twenty five *business days* after the day on which the remittance is cleared (or, if earlier, when the firm performs the client money calculation in accordance with *CASS 5.5.63R(1)*.

- 5.5.17 G (1) As soon as *commission* becomes due to the *firm* (in accordance with *CASS 5.5.16R(1)*) it must be treated as a remittance which must be withdrawn in accordance with *CASS 5.5.16R (2)*. The procedure required by *CASS 5.5.16R* will also apply where ~~money becomes is due and payable~~ to the *firm* in respect of fees due from *clients* (whether to the *firm* or other professionals) ~~and amounts in respect of *commission* which becomes due to the *firm* from an *insurance undertaking*.~~
- (2) *Firms* are reminded that *money* received in accordance with *CASS 5.2* must not, except where a *firm* and an *insurance undertaking* have (in accordance with *CASS 5.1.5AR*) agreed otherwise, be kept in a *client bank account*. *Client money* received from a third party *premium* finance provider should, however, be segregated into a *client bank account*.
- (3) Where a *client* makes payments of *premium* to a *firm* in instalments, *CASS 5.5.16R(1)* applies in relation to each instalment.
- (4) If a *firm* is unable to match a remittance with a transaction it may be unable to immediately determine whether the payment comprises a *mixed remittance* or is *client money*. In such cases the remittance should be treated as *client money* while the *firm* takes steps to match the remittance to a transaction as soon as possible.



Appointed representatives, field representatives and other agents

- 5.5.18 R (1) Subject to (4), a firm must in relation to each of its appointed representatives, field representatives and other agents comply with CASS 5.5.19R to CASS 5.5.21R (Immediate segregation) or with CASS 5.5.23R (Periodic segregation and reconciliation).

...

- (4) (1) to (3) do not apply in relation to an appointed representative, field representative or other agent to which (if it were a firm) CASS 5.1.4AR(1) or (2) would apply, but subject to the representative or agent maintaining an account which satisfies the requirements of CASS 5.5.49R.

...

Client money calculation and reconciliation

- 5.5.62 G ~~The purpose of the client money calculation is to act as a check that the amount of client money (and where appropriate the value of segregated designated investments) that is segregated at banks (and where appropriate third parties) is sufficient to meet the firms obligations to its clients. For this purpose two, alternative, calculation methods are permitted, but a firm must use the same calculation method in relation to both CASS 5.3 and CASS 5.4. The first requires a firm to calculate its client money requirement by reference to individual client money balances. The second permits a firm to carry out the calculation on the basis of information in its business ledgers. In either case, the firm must carry out the calculation at least every 25 business days.~~

- (1) In order that a firm may check that it has sufficient money segregated in its client bank account (and held by third parties) to meet its obligations to clients it is required periodically to calculate the amount which should be segregated (the client money requirement) and to compare this with the amount shown as its client money resource. This calculation is, in the first instance, based upon the firm's accounting records and is followed by a reconciliation with its banking records. A firm is required to make a payment into the client bank account if there is a shortfall or to remove any money which is not required to meet the firm's obligations.

- (2) For the purpose of calculating its client money requirement two alternative calculation methods are permitted, but a firm must use the same method in relation to CASS 5.3 and CASS 5.4. The first refers to individual client cash balances; the second to aggregate amounts of client money recorded on a firm's business ledgers.

- 5.5.63 R (1) A *firm* must, as often as is necessary to ensure the accuracy of its records and at least at intervals of not more than 25 *business days*:
- (1) (a) check whether its *client money* resource, as determined by CASS 5.5.65R on the previous *business day*, was at least equal to the *client money* requirement, as determined by CASS 5.5.66R or CASS 5.5.68R, as at the close of business on that day; and
  - (2) (b) ensure that:
    - (a) (i) any *shortfall* is paid into a *client money bank account* by the close of business on the day the calculation is performed; or
    - (b) (ii) any excess is withdrawn within the same time period unless CASS 5.5.9R or CASS 5.5.10R applies to the extent that the *firm* is satisfied on reasonable grounds that it is prudent to maintain a positive margin to ensure the ~~test~~-calculation in (a) is satisfied having regard to any unreconciled items in its business ledgers as at the date on which the calculations are performed; and
  - (3) (c) ~~ensure that it~~ includes in any calculation of its *client money* requirement (whether calculated in accordance with CASS 5.5.66R or CASS 5.5.68R) any amounts attributable to *client money* received by its *appointed representatives*, *field representatives* or other agents and which, as at the date of calculation, it is required to segregate in accordance with CASS 5.5.19R.
- (2) A *firm* must within ten *business days* of the calculation in (a) reconcile the balance on each *client bank account* as recorded by the *firm* with the balance on that account as set out in the statement or other form of confirmation used by the bank with which that account is held.
- (3) When any discrepancy arises as a result of the reconciliation carried out in (2), the *firm* must identify the reason for the discrepancy and correct it as soon as possible, unless the discrepancy arises solely as a result of timing differences between the accounting systems of the party providing the statement or confirmation and those of the *firm*.

- (4) While a firm is unable to resolve a difference arising from a reconciliation, and one record or a set of records examined by the firm during its reconciliation indicates that there is a need to have a greater amount of client money than is in fact the case, the firm must assume, until the matter is finally resolved, that the record or set of records is accurate and either pay its own money into a relevant account or make a withdrawal of any excess.

...

- 5.5.65 R The *client money* resource, for the purposes of CASS 5.5.63R(1)(a), is
- (1) the aggregate of the balances on the *firm's client money bank accounts*, as at the close of business on the previous *business day* and, if held in accordance with CASS 5.4, *designated investments* (valued on a prudent and consistent basis) together with *client money* held by a third party in accordance with CASS 5.5.34 R; and
  - (2) (but only if the firm is comparing the client money resource with its client's money (accruals) requirement in accordance with CASS 5.5.68R) to the extent that *client money* is held in accordance with CASS 5.3 (statutory trust), insurance debtors (which in this case cannot include pre-funded items); and
  - (3) (but only if the firm is comparing the client money resource with its client's money (accruals) requirement in accordance with CASS 5.5.68R) to the extent that *client money* is held in accordance with CASS 5.4 (non-statutory trust):

...

But a firm may treat a transaction with an insurance undertaking which is not a UK domestic firm as complete, and accordingly may (but only for the purposes of the calculation in (1)) disregard any unreconciled items of client money transferred to an intermediate broker relating to such a transaction, if:

- (4) it has taken reasonable steps to ascertain whether the transaction is complete; and
- (5) it has no reason to consider the transaction has not been completed; and
- (6) a period of at least 12 months has elapsed since the money was transferred to the intermediate broker for the purpose of the transaction.

...

- 5.5.67 R The individual *client balance* for each *client* must be calculated as follows:

...

- (4) less the amount paid to *insurance undertakings* for the benefit of the *client* (to include all *premiums* and *commission* due to itself) (i.e. *commissions* that are due but have not yet been removed from the *client account*);

...

5.5.68 R A *firm's client money* (accruals) requirement is the sum of the following:

...

- (2) unearned ~~brokerage~~ *commission* being the amount of ~~brokerage~~ *commission* shown as accrued (but not shown as ~~earned~~ due and payable) as at the date of the calculation (a prudent estimate must be used if the *firm* is unable to produce an exact figure at the date of the calculation).

...

#### Reconciliation of client money: frequency of reconciliation

5.5.70 R ~~A *firm* must perform a reconciliation of the *client money* balances which it holds, or if appropriate perform the *client money* (accruals) calculation, as frequently as is necessary to ensure the accuracy of its record of *money* so held, and no less than once in every 25 *business days*. [deleted]~~

5.5.71 G ~~In determining whether the minimum acceptable frequency is sufficient, a *firm* should consider the risks to which the business is exposed, such as the volume of business, and where and with whom the *client money* is held. [deleted]~~

5.5.72 R ~~A *firm* must complete the reconciliation of *client money* within ten *business days* of the date on which the *client money* resource and *client money* requirements were determined. [deleted]~~

#### Verification of banking records

5.5.73 R ~~A *firm* must for the purpose of the reconciliation required by CASS 5.5.63R compare the balance on each *client bank account* as recorded by the *firm* with the balance on that account as set out in the statement or other form of confirmation used by the bank with which that account is held. [deleted]~~

#### Verification of discrepancies

5.5.74 R ~~When any discrepancy arises as a result of the verification carried out under CASS 5.5.73R, the *firm* must identify the reason for the discrepancy and correct it as soon as possible, unless the discrepancy arises solely as a result of timing differences between the accounting systems of the party providing the statement or confirmation and those of the *firm*. [deleted]~~

5.5.75 R ~~While a *firm* is unable to resolve a difference arising from a reconciliation, and one record or a set of records examined by the *firm* during its reconciliation indicates that there is a need to have a greater amount of *client money* than is in fact the case, the *firm* must assume, until the matter is finally resolved, that the record or set of records is accurate and pay its own *money* into a relevant account. [deleted]~~

Failure to perform calculations or reconciliation

5.5.76 R A *firm's* must notify the *FSA* immediately if it is unable to, or does not, perform the calculation required by *CASS* 5.5.63R(1).

5.5.77 R A *firm* must notify the *FSA* immediately it becomes aware that it may not be able to make good any *shortfall* identified by *CASS* 5.5.63R(1) by the close of business on the day the calculation is performed and if applicable when the reconciliation is completed.

5.5.78 R ~~A *firm* must notify the *FSA* as soon as possible if it is unable to comply with any of the requirements of *CASS* 5.5.70R, *CASS* 5.5.72R, *CASS* 5.5.73R, *CASS* 5.5.74R and *CASS* 5.5.75R. [deleted]~~

...

5.5.80 R *Money* ceases to be *client money* if it is paid:

...

(5) to the *firm* itself, when it is an excess in the *client bank account* as set out in *CASS* 5.5.63R(2)(b)(1)(b)(ii).

...

5.6.5 R A *primary pooling event* occurs:

...

(4) when the *firm* notifies, or is in breach of its duty to notify, the *FSA*, in accordance with *CASS* 5.5.787R ...

...

5.6.22 R *Money* held in each *general client bank account* of the *firm* must be treated as pooled and:

...

(4) the *firm* must use the new *client* entitlements, calculated in accordance with (2), when performing the *client money* calculation in accordance with *CASS* 5.5.63R to *CASS* 5.5.7569R.

...

5.6.24 R For each *client* with a *designated client bank account* held at the *failed* bank:

...

(4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), when performing the periodic *client money* calculation, in accordance with CASS 5.5.63R to CASS 5.5.7569R.

...

5.6.30 R *Money* held in each *general client bank account* of the *firm* must be treated as pooled and:

...

(4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), when performing the periodic *client money* calculation, in accordance with CASS 5.5.63R to CASS 5.5.7569R.

## Annex B

### Amendments to the Glossary of definitions

In this Annex striking through indicates deleted text.

Amend the following definition as shown:

*approved bank* (except in *COLL* and *CIS*) (in relation to a *bank* account opened by a *firm*):

- (a) if the account is opened at a branch in the *United Kingdom*:
  - (i) the Bank of England; or
  - (ii) the central bank of a member state of the *OECD*; or
  - (iii) a *bank*; or
  - (iv) a *building society* ~~which offers unrestrictedly, banking services~~; or

...

## ADDENDUM

### CLIENT ASSETS SOURCEBOOK (AMENDMENT NO 2) INSTRUMENT 2004

Annex A to this instrument is amended by replacing the text shown for the transitional provisions CASS TP 3 and TP 4 with the following text:

#### CASS Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
3	CASS 5.1 to CASS 5.6	R	<del>In CASS 5.1 to CASS 5.6 an insurance undertaking (when acting as such) with whom a firm conducts insurance mediation activity may be treated by the firm as its client.</del> <u>Apply in relation to money (and where appropriate designated investments) held by a firm on 14 January 2005 (being money or designated investments to which CASS 5.1 to CASS 5.6 would not otherwise apply) to the extent that any such money (or designated investments) relate to business carried on before 14 January 2005 and which would, if conducted on or after 14 January 2005, be an insurance mediation activity.</u>	14 January 2005 for 12 months <u>Indefinitely</u>	14 January 2005
4	<del>CASS 5.1 to CASS 5.6</del> <u>CASS 5.1.5AR</u>	R	<del>Money held by a firm in accordance with an agreement made under CASS 5.2.3R may be kept in a client bank account. A firm will satisfy the requirements of this paragraph, and money is client money, notwithstanding that an insurance undertaking which is the firm's counterparty to an agreement required by CASS 5.1.5AR has not given written</del>	14 January 2005 for <del>12</del> <u>6</u> months	14 January 2005



(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			<u>consent to its interests under the trusts (or in Scotland agency) in CASS 5.3.2R or CASS 5.4.7R being subordinated to the interests of the <i>firm's</i> other <i>clients</i>.</u>		

## CONTROLLERS AND CLOSE LINKS INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance); and
  - (4) section 182 (1) (Notification).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- C. This instrument comes into force on 1 December 2004, save for the amendment to SUP 11.2.8G which appears in square brackets, which comes into force on 14 January 2005 pursuant to the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (FSA 2004/01).

### Amendments to the Supervision manual

- D. The Supervision manual is amended in accordance with the Annex to this instrument.

### Citation

- E. This instrument may be cited as the Controllers and Close Links Instrument 2004.

By order of the Board  
18 November 2004

## Annex

### Amendments to the Supervision manual

In this Annex, underlining indicates new text and striking through deleted text. Footnotes do not form part of this instrument, but have been inserted to assist the reader.

- 11.2 Purpose
- ...
- 11.2.2 G The *rules* in SUP 11.4 to SUP 11.6 are aimed at ensuring that the FSA receives information it needs from *firms* to assist the FSA with its responsibility to monitor and, in some cases, give prior approval to *firms' controllers*. ~~These rules also implement certain requirements relating to changes in control that are required under the Investment Services Directive, the Banking Consolidation Directive, the Third Life Directive and the Third Non-Life Directive.~~
- ...
- 11.2.5 G Similarly, the FSA needs to monitor a *firm's* continuing satisfaction of *threshold condition 3* (Close links) (see SUPCOND 2.3), which requires that a *firm's close links* are not likely to prevent the FSA's effective supervision of that *firm*. Accordingly the FSA needs to be notified of any changes in a *firm's close links*. This requirement is contained in SUP 11.9 and implements a requirement of the amending Directive (the *Post BCCI directive*) in relation to *close links*.
- 11.2.6 G Every *firm<sub>2</sub>* other than a *firm* listed in SUP 11.1.1R(1) to (6) or a *firm* excluded from the operation of SUP 16.4 or SUP 16.5 by SUP 16.1.3R, is required to submit an annual report on its *controllers* and *close links* as set out in SUP 16.4 and SUP 16.5.
- 11.2.7 G The requirements in SUP 11 implement certain provisions relating to changes in control and close links required under the Single Market Directives. ~~A summary of the notification requirements in this chapter is given in SUP 11Ann1G.~~
- 11.2.8 G An event described in SUP 11.4.2R(1) to (4) [and SUP 11.4.2AR(1) and (2)]<sup>1</sup> is referred to in this chapter as a "change in control".
- ...

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<sup>1</sup> This amendment will come into force on 14 January 2005 pursuant to the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (FSA2004/01). This amendment was made initially to SUP 11.3.2G but this instrument moves this text to SUP 11.2.8G and so the amendment made by FSA 2004/01 is transposed.

11.3 Requirements on controllers or proposed controllers under the Act

...

Requirement to notify a proposed change in control

11.3.2 G ~~Part XII~~ Sections 178(1) and 190(1) of the *Act* requires a *person* (whether or not he is an *authorised person*) to notify the *FSA* in writing if he proposes to take a step which would result in his acquiring *control* or increasing or reducing his *control* over a UK domestic firm in a way described in SUP 11.4.2R(1) to (4). Failure to notify is an offence under section 191(1) of the *Act* (Offences under this Part). ~~An event described in SUP 11.4.2R(1) to (4) is referred to in this chapter as a “change in control”.~~

...

11.3.3 G ~~The notifications referred to in SUP 11.3.2G may be given jointly with the firm as described in SUP 11.5.8G. [deleted]~~<sup>2</sup>

~~Prior a~~ Approval of required before acquiring or increasing control

11.3.4 G If a *person* proposes to acquire *control* or increase his *control* over a UK domestic firm in a way described in SUP 11.4.2R(1) to (4), he must obtain the *FSA's* approval before doing so. ~~Failure~~ Failure to obtain approval is an offence under section 191(3) of the *Act* (Offences under this Part). The *FSA* has up to three *months* to consider whether to ~~approve~~ approve such a change in *control*; see SUP 11.7 for guidance on the approval procedures. ~~A controller or proposed controller should take this period into account when deciding when to give his notification.~~

11.3.5 G The *FSA's* ~~approval~~ approval is not required before a *controller* reduces his *control* over a UK domestic firm.

Pre-notification and approval for fund managers

11.3.5A G The *FSA* recognises that *firms* acting as *investment managers* may have difficulties in complying with the prior notification requirements in sections 178(1) and 190(1) of the *Act* as a result of acquiring or disposing of listed *shares* in the course of that fund management activity. To ameliorate these difficulties, the *FSA* may accept pre-notification of proposed changes in *control*, made in accordance with SUP 11.3.5BD, and may grant approval of such changes for a period lasting up to a year.

11.3.5B D The *FSA* may treat as notice given in accordance with sections 178(1) and 190(1) of the *Act* a written notification from a *firm*

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<sup>2</sup> Text moved to SUP 11.3.17G

which contains the following statements:

- (1) that the *firm* proposes to acquire and/or dispose of *control*, on one or more occasions, of any *UK domestic firm* whose *shares* or those of its ultimate *parent undertaking* are, at the time of the acquisition or disposal of *control*, listed or which are admitted to listing on a *designated investment exchange*;
- (2) that any such acquisitions and/or disposals of *control* will occur only in the course of the *firm's* business as an *investment manager*; and
- (3) that the level of *control* the *firm* so acquires in the pre-approval period will at all times remain less than 20%.

11.3.5C     G     Where the *FSA* approves changes in *control* proposed in a notice given under *SUP* 11.3.5BD:

- (1) the *controller* remains subject to the requirement to notify the *FSA* when a change in *control* actually occurs; and
- (2) the notification of change in *control* should be made no later than five *business days* after the end of each *month* and set out all changes in the *controller's control* position for each *UK domestic firm* for the *month* in question.

At that stage, the *FSA* may seek from the *controller* further information, including that which would have been supplied under *SUP* 11.3.7D(2).

Change in control without taking any step

11.3.6     G     If a change in *control* occurs without the *person* himself having taken any step (~~for example, because of an increase in the firm's capital~~), he must notify the *FSA* within 14 days of becoming aware of the change (sections 178(2) and 190(2) of the *Act*). Failure to notify is an offence under section 191(2) of the *Act*. Provisions determining when such a notice is treated as being received by the *FSA* are set out in regulation 10(1) of the Financial Services and Markets Act 2000 (Service of Notices) Regulations 2001 (SI 2001/1420).

Custodians obtaining control

11.3.6A     G     The *FSA* considers that a *custodian* or its wholly-owned subsidiary *nominee company*, acting only in that capacity, does not itself take any step for the purposes of sections 178(2) and 190(2) of the *Act* when it becomes the *controller* of a *UK domestic firm*, its *control* of a *UK domestic firm* changes or it ceases to be the *controller* of a *UK domestic firm* as a result of acquiring or disposing of *custody assets* in the form of *shares* in accordance with its *clients'*

instructions.

11.3.6B     D     For the purposes of sections 178(2) and 190(2) of the Act and where there has been more than one change in control for each UK domestic firm in a fortnightly period, a custodian or its wholly-owned subsidiary nominee company to which SUP 11.3.6AG applies need only notify the FSA of its final control position for each UK domestic firm for that fortnight, so long as it also supplies the highest control position for each UK domestic firm it obtained during that period.

11.3.6C     G     Reporting by a custodian or its wholly-owned subsidiary nominee company does not relieve any other person with an interest in any custody assets from its control notification responsibilities under Part XII of the Act.

Form of notification when acquiring or increasing control

11.3.7        D     A notification ("notice of control") given to the FSA by a person who is acquiring control or increasing his control over a UK domestic firm, in a way described in SUP 11.4.2R(1) to (4), must:

(1)        ~~where the in the case of a controller or a proposed controller who~~ is not an authorised person, contain ...

(1A)       ~~where the controller is a custodian or a nominee company notifying under SUP 11.3.6AD, comply with that direction;~~

(2)        ~~where the controller or proposed controller is any other authorised person in all other cases, contain the information required in those sections of Controllers Form A (SUP 11 Annex 4D) which deal with details of the proposed change in control and the persons involved in the notification;~~  
~~sections 1, 5 and 6; and~~

(3)        ...

...

11.3.11       G     The FSA, for administrative reasons, expects notifications within SUP 11.3.7D to be given on Controllers Form A or Controllers Form B, as appropriate. If notifications are not made on these forms the applicant must inform the FSA of the reasons for not using them. ~~Copies of the Controllers Form A and Controllers Form B are available on the FSA's website at [www.fsa.gov.uk](http://www.fsa.gov.uk).~~ Regulations 7 to 9 of the Financial Services and Markets Act 2001 (Services of Notices) Regulations 2001 (SI 2001/1420) govern the manner in which a notice of control may be submitted. In summary, ~~it should be delivered or posted to the FSA's address as shown on the Forms, and will be treated as given when it is received by the FSA. It should not be sent by fax or electronic mail.~~

11.3.12 G If a *controller* or proposed *controller* considers that the requirements in SUP 11.3.7D to SUP 11.3.9D are not appropriate to his circumstances, for example;

- (1) if the *control* is ~~to be held~~ temporary through a trust; or
- (2) if Form B is required (under SUP 11.3.8D) in relation to:
  - (a) an individual who is an *approved person*; ~~or~~
  - (b) a partnership of which one or more of the partners are bodies corporate;

he should consult the *FSA*. The *FSA* has power, under section 182(3) of the *Act* (Notification), to amend those requirements if it considers it appropriate to do so.

...

11.3.14 G ~~If item 1.05 of Controllers Form A is answered in the affirmative,~~ The *FSA* may be obliged to consult regulatory authorities in other *EEA States* before approving the change in *control* or giving a *warning notice* where:

- (1)
  - (a) the "target" UK domestic firm is an investment firm;
  - (b) the controller or proposed controller is an ISD investment firm or the parent undertaking of an ISD investment firm; and
  - (c) as a result of the acquisition or proposed acquisition, the controller or proposed controller would become the parent undertaking of the UK domestic firm; or
- (2)
  - (a) the "target" UK domestic firm has permission to accept deposits;
  - (b) the controller or proposed controller is a BCD credit institution or the parent undertaking of a BCD credit institution; and
  - (c) as a result of the acquisition or proposed acquisition, the controller or proposed controller would become the parent undertaking of the UK domestic firm.

Form of notification when reducing control

11.3.15 G A notification given to the *FSA* by a *person* who is reducing his *control* over a *UK domestic firm*, in a way described in SUP 11.4.2R(1) to (4), must, in accordance with section 190(4) of the *Act* (Notification):

- (1) be in writing; and
- (2) provide details of the extent of *control* (if any) which the *controller* will have following the change in *control*.

Notification when change in control occurs

- 11.3.16 G A *person* who is under a duty to notify the *FSA* of a proposed change in control is also required to notify the *FSA* when the relevant change in *control* has occurred (sections 178(3) and 190(3) of the *Act*). ~~The notification may be given jointly with the firm as described in SUP 11.6.6G. If a person has reduced his control, section 190(4) of the Act requires that the notification should provide details of the extent of control retained (if any).~~

Joint and shared notifications

- 11.3.17 G Notifications to the *FSA* by proposed *controllers* and *controllers* under Part XII of the *Act* may be made on a joint or shared basis outlined in SUP 11.5.8G to SUP 11.5.10G.

...

- 11.5 Form of notification by firms

...

- 11.5.3 G In determining what the *FSA* would reasonably expect notice of in accordance with row (4) in SUP 11.5.1R, a ~~firm~~ *firm* should have regard, in particular, to the following matters set out in items 1.03 to 1.07 and 6.02 of Controllers Form A (SUP 11 Annex 4D) to the extent that the *firm* is aware of such matters them:

- (1) whether the *controller* intends to make any significant changes to the *firm*'s or *firms*' regulated activities, business plan or strategy as a result of the change in *control*;
- (2) whether the *controller* intends any restructuring either in terms of the legal form of the *firm*(s) or in its or their borrowings, capital restructuring or financing arrangements;
- (3) whether the *FSA* is obliged to consult with regulatory authorities in other *EEA States* (see SUP 11.3.14G);
- (4) in the case of a share acquisition or similar, how it is to be financed;
- (5) whether the *controller* has any interests which may conflict with its role as *controller* of the *UK domestic firm*.

*Firms* are also reminded of the circumstances set out in SUP 15.3.8G (Communication with the *FSA* in accordance with



Principle 11) which may arise on a change in *control* and which should also be notified.

...

11.7 Acquisition or increase of control: approval procedures

...

11.7.3 G Alternatively, the *FSA* may decide to approve the proposed acquisition or increase of *control* subject to such conditions as it considers appropriate, having regard to the *FSA's* duty to ensure that the *firm* concerned will satisfy, and continue to satisfy, the *threshold conditions* (section 185 of the *Act*).

(1) If the *FSA* proposes to approve subject to conditions, it must give a *warning notice*.

(2) If the *FSA* decides to proceed to approve subject to conditions, it must give a *decision notice*.

...

11.7.7 G (1) If the *FSA* proposes to object, it must issue a *warning notice*.

(2) If the *FSA* decides to proceed with its proposed objection, it must issue a *decision notice*.

(3) If the *FSA* considers that the approval requirements would be met if a particular step were taken or not taken, the *decision notice* must identify that step (section 186(4) of the *Act*).

11.7.8 G ~~As well as objecting when satisfied that the approval requirements are not met,~~ The *FSA* may also object if it has not received sufficient information from either the *controller* or the *firm* to satisfy itself that the approval requirements are met.

...

The *FSA's* timeframe for responding to a notification

11.7.10 G If the *FSA* receives a valid notification from a *controller* or proposed *controller* (~~whether a joint notification in accordance with SUP 11.5.8G or otherwise~~), the *FSA* must respond within three ~~months~~ ~~regardless of when it receives a notification from the *firm*~~ (section 183(1) of the *Act*). The response from the *FSA* will be either an approval notice or a *warning notice*.

11.7.11 G (1) ~~Alternatively, the *FSA* may receive a notification from the *firm* but not from the *controller* or proposed *controller* or may otherwise become~~ Where the *FSA* becomes aware of a possible breach by the *controller* or proposed *controller* of his

obligations under section 178(1) or (2) of the *Act* (Obligation to notify the Authority); ~~it the FSA~~ may require the *person* concerned to provide additional information or *documents* (section 188(4) of the *Act*).

- (2) If the *FSA* is satisfied that a breach has occurred, but is not satisfied that the approval requirements are met, the *FSA* may give a *warning notice* to the *controller* or proposed *controller* (section 187(1) and 188(1) of the *Act*).
- (3) Alternatively, the *FSA* may retrospectively approve the change ~~of~~ *control* as if a notification had been received from the *controller* or proposed *controller* (section 187(2) of the *Act*).

...

#### The FSA's right to object to existing controllers

- 11.7.14 G If a *controller* fails to give a notification under section 178(3) of the *Act* on acquiring or increasing *control*, ...

...

#### 11.9 Changes in close links

##### Requirement to notify changes in close links

- 11.9.1 R A *firm* must notify the *FSA* ~~immediately it becomes aware~~ that it has become or ceased to be *closely linked* with any *person*. The notification must include the information set out in SUP 16.5.4R(4).

...

##### Timing of notification requirement

- 11.9.4 R The *firm* must make a notification to the *FSA* under SUP 11.9.1R:
  - (1) as soon as reasonably practicable and no later than one *month* after it becomes aware that it has become or ceased to be *closely linked* with any *person*; or
  - (2) where a *firm* has elected to report on a *monthly* basis, within fifteen *business days* of the end of each *month* and:
    - (a) including the information set out in SUP 16.5.4R(4) for that *month*; and
    - (b) if there is no *person* required to be included in the notification for a particular *month*, confirming this fact in the notification.

Electing to notify changes in close links monthly

- 11.9.5 R (1) A firm elects to report changes in close links on a monthly basis by sending a written notice of election to the firm's usual supervisory contact at the FSA.
- (2) An election to report changes in close links on a monthly basis will stand until such time as the firm gives its usual supervisory contact at the FSA at least one month's written notice of its intention to cease reporting changes in close links on a monthly basis.

- 11.9.6 G The FSA considers that monthly reporting of changes in close links will ordinarily only be appropriate for firms forming part of large groups.

...

16.4 Annual Controllers Report

Application

- 16.4.1 G ~~The effect of SUP 16.1.1R is that this~~ This section applies to every firm except those firms excluded from its operation by SUP 16.1.1R and SUP 16.1.3R. ÷

- ~~(1) a credit union;~~
- (1) an ICVC;
- (2) an incoming EEA firm;
- (3) an incoming Treaty firm;
- (4) a non-directive friendly society;
- (5) [deleted];
- ~~(6) a sole trader;~~
- (7) a service company;
- ~~(8) a UCITS qualifier.~~

...

16.5 Annual Close Links Reports

Application

- 16.5.1 G ~~The effect of SUP 16.1.1R is that this~~ This section applies to every firm except those firms excluded from its operation by SUP 16.1.1R

and SUP 16.1.3R. ÷

- ~~(1) a credit union;~~
- (1) an ICVC;
- ~~(2) an incoming EEA firm;~~
- ~~(3) an incoming Treaty firm;~~
- ~~(4) a non-directive friendly society;~~
- ~~(5) [deleted];~~
- ~~(6) a sole trader;~~
- ~~(7) a service company;~~
- ~~(8) a UCITS qualifier.~~

...

#### SUP Schedule 2 – Notification Requirements

Handbook Reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
SUP 11.3.7D	<i>Controllers - person proposing to acquire or increase control - notification from controller or proposed controller</i>	If the <i>controller</i> or proposed <i>controller</i> is an <i>authorised person</i> : <u>those sections of</u> Controllers Form A <u>which deal with details of the proposed change in control, joint notifications and supplementary information sections 1, 5 and 6</u> (see SUP 11 Ann 4D)	Proposing to take a step which would result in acquiring the specified <i>control</i>	Before acquiring <i>control</i> (the FSA has up to <del>three months</del> <u>months</u> to consider whether to <del>approve</del> <u>approve</u> <i>control</i> )

If the controller or proposed controller is an authorised person and a fund manager which satisfies SUP 11.3.5D: notification in accordance with SUP 11.3.5D

In other cases: ...

...

<p>SUP 11.3.15G</p>	<p><i>Controllers - proposing to reduce control - notification from controller</i></p>	<p>Extent of control (if any) which the controller will have following the change in control</p> <p><u>If the controller is a fund manager which satisfies SUP 11.3.5D: notification in accordance with SUP 11.3.5D</u></p>	<p>Reduction in control</p>	<p>Before reducing control <del>(the FSA has up to three months to consider whether to approve change)</del></p>
---------------------	--	---	-----------------------------	--

...

<p>SUP 11.9.1R</p>	<p><i>Close links</i></p>	<p>(a) the name of the person</p> <p>(b) the nature of the close links</p> <p>(c) if the close link is with a body corporate, its country of incorporation, address and</p>	<p>The firm becoming aware that it has become or ceased to be closely linked with any person .</p>	<p><u>Immediately</u>  <u>As soon as reasonably practicable and no later than one month after the firm becomes aware that it has become or ceased to be closely linked or if the firm</u></p>
--------------------	---------------------------	---	--	---

registered  
number; and

(d) if the *close link* is with an individual, his date and place of birth

has elected to report  
monthly,  
within 15  
business days  
of the end of  
each month  
(see  
SUP 11.9.4R)

## SUPERVISION MANUAL (ACTUARIES) INSTRUMENT 2004

### Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 59 (Approval for particular arrangements);
  - (2) section 138 (General rule-making power);
  - (3) section 156 (General supplementary powers);
  - (4) section 157(1) (Guidance); and
  - (5) section 340 (Appointment).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

### Commencement

- C. This instrument comes into force on 31 December 2004.

### Amendments to the Handbook

- D. The modules of the FSA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2) below.

(1)	(2)
The Threshold Conditions (COND)	Annex A
Conduct of Business sourcebook (COB)	Annex B
Authorisation manual (AUTH)	Annex C
Supervision manual (SUP)	Annex D
Enforcement manual (ENF)	Annex E
Glossary of definitions	Annex F

### Citation

- E. This instrument may be cited as the Supervision Manual (Actuaries) Instrument 2004.

By order of the Board  
18 November 2004

Amended by Addendum  
29 July 2005

## Annex A

### Amendments to the Threshold Conditions

In this Annex underlining indicates new text and striking through indicates deleted text.

2.5.7 G (11) where appropriate, the *firm* has appointed auditors and actuaries, who have sufficient experience in the areas of business to be conducted (see *SUP* 3.4 (Auditors' qualifications) and *SUP* 4.3.8G to *SUP* 4.3.1310G (~~Appointed~~ actuaries' qualifications)); and

...

...



## Annex B

### Amendments to the Conduct of Business sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

6.11.11 R ~~Any~~The report to *with-profits policyholders* made under SUP 4.3.16AR (4) by a *with-profits actuary*~~from an *actuary* appointed under SUP 4 (Actuaries)~~ must be annexed to the annual report in COB 6.11.9R.

...

6.11.14 G In preparing the report to *with-profits policyholders* in COB 6.11.9R, a *firm* should take advice from a *with-profits actuary*~~*actuary*~~.

Insert the following new transitional provision in COB TR5.

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
	COB 6.11.9	R	<p>Annual report to <i>with-profits policyholders</i></p> <p><i>A firm</i> must produce its first report to <i>with-profits policyholders</i> under COB 6.11.9R in respect of the part of its financial year that follows the date on which PRU 7.4 (With-profits Insurance Capital Component) comes into force.</p>	From 30 April 2004	30 April 2004

## Annex C

### Amendments to the Authorisation manual

In this Annex underlining indicates new text and striking through indicates deleted text.

- 3.9.19 D If an applicant appoints an actuary, ~~other than an appointed actuary~~, to report on an application for *Part IV permission*, the applicant is directed to take reasonable steps to ensure that the *actuary* satisfies the qualification tests in *SUP 4.3.9R* (~~Appointed actuaries'~~ qualifications).

...

## Annex D

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

Insert the following new transitional provisions in the correct sequential order:

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision: coming into force
...					
4A	<i>SUP</i> 4	R	Anything done before 31 December 2004 for the purposes of an amended provision in <i>SUP</i> 4 has effect as if done under that provision.	From 31 December 2004	31 December 2004
4B	<i>SUP</i> 4.3.1R	R	A <i>firm</i> must notify the <i>FSA</i> immediately of all appointments under <i>SUP</i> 4.3.1R (as amended) which come into, or are in, effect on 31 December 2004, advising the <i>FSA</i> of the name and business address of each <i>actuary</i> appointed and the functions each <i>actuary</i> is to perform.	From 31 December 2004	31 December 2004
4C	<i>SUP</i> 4.5.9R	R	An <i>actuary</i> , who immediately before 31 December 2004 is the <i>appointed actuary</i> of a <i>firm</i> , must notify the <i>FSA</i> under <i>SUP</i> 4.5.9R (as amended) if on that date he is not appointed by the <i>firm</i> under <i>SUP</i> 4.3.1R (as amended).	From 31 December 2004	31 December 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
4D	SUP 4.5.10R	R	<p>An <i>actuary</i>, who immediately before the relevant time in (a) or (b) below is the <i>appointed actuary</i> of a <i>firm</i>, must notify the <i>FSA</i> under SUP 4.5.10R (as amended) if:</p> <p>(a) he is not appointed by the <i>firm</i> under SUP 4.3.1R (as amended) on 31 December 2004;</p> <p>or</p> <p>(b) he is or has been formally notified that he will not be so appointed by the <i>firm</i>.</p>	From 31 December 2004	31 December 2004
4E	SUP 4.3.1R and SUP 4.3.3R	G	<p><i>Firms</i> and the <i>FSA</i> will need to make fresh appointments once these proposed amendments come into effect, even if an <i>actuary</i> has already been appointed under the existing provisions. A <i>firm</i> will not need to seek fresh approval under section 60 of the <i>Act</i> for an existing <i>appointed actuary</i> who continues to perform the <i>actuarial function</i> (CF12) or the</p>	From 31 December 2004	31 December 2004

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
			<p><i>with-profits actuary function</i> (CF12A). This is because both these <i>controlled functions</i> are already covered by an <i>actuary's</i> existing approval to perform the previous <i>appointed actuary function</i>. However, under <i>SUP TP4B firms</i> are required to notify the <i>FSA</i> of any new or continued appointments to perform either or both of these functions. The effect of <i>SUP TP4CR</i> and <i>SUP TP4DR</i> is to require an existing <i>appointed actuary</i> to notify the <i>FSA</i> under <i>SUP 4.5.9R</i> and <i>SUP 4.5.10R</i> if he ceases to hold any appointment at all under <i>SUP 4.3.1R</i>, but not if he is appointed to perform either or both functions.</p>		
...					

...

4.1 Application

4.1.1 R This chapter applies to:

- (1) every *firm* within a category listed in column (1) of the table in *SUP 4.1.3R*; and

- (2) every ~~the appointed actuary or appropriate actuary~~ appointed under this chapter of such a firm;

in accordance with column (2) of that table.

- 4.1.2 G This chapter applies to *long-term insurers* (including *friendly societies*) and other *friendly societies*. This chapter does not apply to the *Society of Lloyd's* or to *Lloyd's underwriting agents*. Requirements dealing with the appointment and duties of *actuaries* in relation to *Lloyd's insurance business* are contained in *LLD*. This chapter does not apply to actuaries advising the auditors of long-term insurers under IPRU(INS) 9.35(1A) or IPRU(FSOC) 5.11(2A), as they are not appointed to act on behalf of the firm.

...

## 4.2 Purpose

- 4.2.1 G Section 340 of the *Act* gives the *FSA* power to make *rules* requiring an *authorised person*, or an *authorised person* falling into a specified class, to appoint an ~~actuary~~ actuary. Section 340 further empowers the *FSA* to make *rules* governing the manner, timing and notification to the *FSA* of such an appointment and, where an appointment is not made, for the *FSA* to make an appointment on the *firm's* behalf. The *FSA's* rule-making powers under section 340 of the *Act* also extend to ~~the an actuary's~~ sactuary's duties and to the cessation of an ~~actuary's~~ sactuary's term of office.

- 4.2.2 G This chapter defines the relationship between ~~a firms~~ a firm's and ~~their~~ its ~~appointed actuaries or appropriate actuaries~~ appointed actuaries and clarifies the role which ~~appointed actuaries and appropriate actuaries~~ appointed actuaries play in the *FSA's* monitoring of *firms'* compliance with the requirements and standards under the *regulatory system*. The chapter sets out *rules* and *guidance* on the appointment of ~~an actuaries~~ an actuary to the position of ~~appointed actuary or appropriate actuary~~ appointed actuary, and the termination of ~~an their actuary's~~ an actuary's term of office, as well as setting out their respective rights and duties. The purpose of the chapter is to ensure that:

- (1) *long-term insurers* (other than certain *friendly societies*) have access to adequate actuarial advice, both in valuing their liabilities to policyholders and in exercising discretion affecting the interests of their with-profits policyholders; and
- (2) other *friendly societies* carrying on *insurance business* (and which have traditionally relied upon actuarial expertise) employ or use an *actuary* of appropriate seniority and experience to evaluate the liabilities of that business.

- 4.2.3 G The functions described by *SUP* 4.2.2G(1) ~~is~~ are performed by one or more ~~the appointed actuaries~~ the appointed actuaries who ~~is~~ are required to hold office continuously

and must be ~~an approved persons~~. The principal duty of ~~the~~ an appointed actuary appointed to perform these functions is to advise the *firm* (see *SUP* 4.3.13R to *SUP* 4.3.1824G for the rights and duties of ~~the~~ such an appointed actuary).

4.2.4 G The function described by *SUP* 4.2.2G(2) is performed by ~~the~~ an appropriate actuary who is appointed to prepare the triennial investigation and interim certificate or statement required by *IPRU(FSOC)* 5.2(1) (see *SUP* 4.4.76R to ~~and~~ *SUP* 4.4.10G 4.5.12G to *SUP* 4.5.14G for the rights and duties of an appropriate actuary).

4.2.5 G ~~Both the appointed actuary and the appropriate actuary~~ Actuaries act as a valuable source of information to the *FSA* in carrying out its functions. For example, in determining whether a *firm* satisfies the *threshold conditions*, the *FSA* has regard to whether the *firm* has appointed an appointed-actuary with sufficient experience in the areas of business to be conducted by the *firm* (*COND* 2.5.7G(11)).

4.2.6 G In making appointments under this chapter and in allocating duties to actuaries, firms are reminded of their obligation under SYSC 2.1.1R to maintain a clear and appropriate apportionment of significant responsibilities so that it is clear who has which of those responsibilities and that the business and affairs of the firm can be adequately monitored and controlled by the directors, relevant senior managers and governing body of the firm.

4.3 Appointedment of actuaries

Appointment by firms

4.3.1 R A *firm* to which this section applies (see *SUP* 4.1) must:

(1) appoint one or more ~~an actuaries~~ (the "appointed actuary") to perform:

(a) the actuarial function (see *SUP* 4.3.13R) in respect of all classes of its *long-term insurance business*; and

(b) the with-profits actuary function (see *SUP* 4.3.16AR) in respect of all classes of its *with-profits business* (if any);

(2) notify the *FSA*, without delay, when it is aware that a vacancy in the office of any such appointed-actuary will arise or has arisen, giving the reason for the vacancy;

(3) appoint an *actuary* to fill any such vacancy ~~in the office of appointed actuary~~ that has arisen; and

(4) ensure ~~the~~ a replacement actuary can take up office at the time the vacancy arises or as soon as is reasonably practicable after that.

4.3.2 G The provisions relating to the duties of an ~~the~~ appointed-actuary appointed

to perform these functions are set out in SUP 4.3.13R to SUP 4.3.1824G. The functions performed by *actuaries* appointed ~~Acting in the capacity of appointed-actuary~~ of by a firm under SUP 4.3.1R ~~is~~ are specified as a *controlled functions* (CF 12, the ~~appointed-actuarial~~ function, and CF 12A, the *with-profits actuary function*) in SUP 10 (*Approved persons*). As a result, an application must be made to the FSA under section 60 of the *Act* (Applications for approval) for approval of the *person* proposing to take up such an appointment ~~as an appointed-actuary~~. Section 61(3) of the *Act* (Determination of applications) gives the FSA three months to grant its approval or give a *warning notice* that it proposes to refuse the application. A firm should not appoint an *actuary* until the FSA has approved the *actuary*. In order to comply with SUP 4.3.1R, a firm should ensure it applies to the FSA as soon as practicable before the date when it needs the *actuary* to take office. The FSA will need time to consider the application before deciding whether to grant approval. See SUP 10 (*Approved persons*).

#### Appointment by the FSA

- 4.3.3 R If a firm, which is required to appoint one or more actuaries ~~an actuary~~ under SUP 4.3.1R, fails to do so within 28 days of a vacancy arising, the FSA may appoint one or more actuaries ~~an actuary~~ to perform the any function corresponding to the actuarial function or the with-profits actuary function ~~of appointed-actuary~~ on the following terms:
- (1) the *actuary* to be remunerated by the firm on the basis agreed between the *actuary* and the firm or, in the absence of agreement, on a reasonable basis; and
  - (2) the *actuary* to hold office until he resigns or the firm appoints another *actuary*.
- 4.3.4 G SUP 4.3.3R allows but does not require the FSA to appoint an *actuary* if the firm has failed to do so within the 28 day period. When it considers whether to use this power, the FSA will take into account the likely delay until the firm can make an appointment and the urgency of any pending duties of the ~~appointed-actuary~~.
- ...
- 4.3.7 G If the FSA appoints an *actuary* under SUP 4.3.3R, he will not be an ~~appointed-actuary~~ approved person (not being appointed under SUP 4.3.1R) ~~and will not therefore need to be an approved person~~. However, the firm is still under an obligation to appoint an *actuary* under SUP 4.3.1R and will need to seek prior approval of that *person* (even if the individual it proposes to appoint is the *person* who has been appointed by the FSA under SUP 4.3.3R).

#### ~~Appointed-actuary's~~ Actuaries' qualifications

- 4.3.8 G The FSA is concerned to ensure that every the appointed-actuary appointed by a firm under this section has the necessary skill and experience to provide



the *firm* with appropriate actuarial advice. *SUP 4.3.9R* to *SUP 4.3.10G* set out the *FSA's rules* and *guidance* aimed at achieving this.

- 4.3.9 R Before a *firm* applies for approval of its ~~proposed~~ the person it proposes to appoint as an appointed-actuary under *SUP 4.3.1R*, it must take reasonable steps to ensure that the *actuary*:
- (1) has the required skill and experience to perform his functions under the *regulatory system*; and
  - (2) is a Fellow of the Institute of Actuaries or of the Faculty of Actuaries.
- 4.3.10 G To comply with *SUP 4.3.9R* and *Principle 3*, before an ~~appointed~~ *actuary* takes up his appointment the *firm* should ensure that the *actuary*:
- (1) has skills and experience appropriate to the nature, scale and complexity of the *firm's* business and the requirements and standards under the *regulatory system* to which it is subject; and
  - (2) has adequate qualifications and experience, which includes holding an appropriate Appointed Actuaries Practising Certificate under the rules of the Institute of Actuaries or the Faculty of Actuaries;
- and seek confirmation of these from the *actuary*, or the *actuary's* current and previous employers, as appropriate.

#### Disqualified actuaries

- 4.3.11 R A *firm* must not appoint under *SUP 4.3.1R* ~~as appointed-actuary~~ an *actuary* who is disqualified by the *FSA* under section 345 of the *Act* (Disqualification) from acting as an *actuary* either for that *firm* or for a relevant class of *firm*.
- 4.3.12 G If it appears to the *FSA* that an ~~appointed~~ *actuary* has failed to comply with a duty imposed on him under the *Act*, it may disqualify him under section 345 of the *Act*. For more detail about what happens when the disqualification of an *actuary* is being considered or put into effect, see *ENF 17 (Disqualification of auditors and actuaries)*. A list of *actuaries* who are disqualified by the *FSA* may be found on the *FSA* website ([www.fsa.gov.uk](http://www.fsa.gov.uk)).

#### Conflicts of interest

- 4.3.12A R A *firm* must take reasonable steps to ensure that an *actuary* who is to be, or has been, appointed under *SUP 4.3.1R*:
- (1) does not perform the function of chairman or chief executive of the *firm*, or does not, if he is to perform the with-profits *actuary* function, become a member of the *firm's* governing body; and
  - (2) does not perform any other function on behalf of the *firm* which

could give rise to a significant conflict of interest.

- 4.3.12B G Both the *actuarial function* and the *with-profits actuary function* may be performed by *employees* of the *firm* or by external consultants, and performing other functions on behalf of the *firm* will not necessarily give rise to a significant conflict of interest. However, being a *director*, or a senior manager responsible, say, for sales or marketing in a *firm* (or for finance in a *proprietary firm*), is likely to give rise to a significant conflict of interest for an *actuary* performing the *with-profits actuary function*. He nevertheless retains direct access to the *firm's governing body* under SUP 4.3.17R(2).

The actuarial function ~~Rights and duties of the appointed actuary~~

- 4.3.13 R An ~~appointed~~ actuary appointed to perform the *actuarial function* must, in respect of those classes of the *firm's long-term insurance business* which are covered by his appointment:
- (1) ~~identify and monitor~~ advise the *firm's* management, at the level of seniority that is reasonably appropriate, on the risks the *firm* runs in so far as they may have a material impact on the *firm's* ability to meet *liabilities* to *policyholders* in respect of *long-term insurance contracts* as they fall due and on the capital needed to support the business, including regulatory capital requirements;
  - (2) monitor those risks and inform the *firm's* management, at the level of seniority that is reasonably appropriate, if he has any material concerns or good reason to believe that the *firm*:
    - (a) is not meeting *liabilities* to *policyholders* under *long-term insurance contracts* as they fall due, or may not be doing so, or might not have done so, or might, in reasonably foreseeable circumstances, not do so;
    - (b) is, or may be, effecting new *long-term insurance contracts* on ~~inadequate terms contrary to IPRU(INS) 3.5A or IPRU(FSOC) 4.13 [number to be inserted later]~~ as applicable; terms under which the resulting income earned is insufficient, under reasonable actuarial methods and assumptions, and taking into account the other financial resources that are available for the purpose, to enable the *firm* to meet its *liabilities* to *policyholders* as they fall due (including reasonable bonus expectations);-
    - (c) does not, or may not, have sufficient financial resources to meet *liabilities* to *policyholders* as they fall due (including reasonable bonus expectations) and the capital needed to support the business, including regulatory capital requirements or, if the *firm* currently has sufficient resources, might, in reasonably foreseeable circumstances, not continue

to have them;

- (3) advise the firm's governing body on the methods and assumptions to be used for the investigations required by IPRU(INS) 9.4R or IPRU(FSOC) 5.1R and the calculation of the with-profits insurance capital component under PRU 7.4 as applicable; perform actuarial investigations and prepare abstracts of those investigations as required by IPRU(INS) 9.4R or IPRU(FSOC) [number to be inserted later] as applicable;
- (4) perform those investigations and calculations in (3), in accordance with the methods and assumptions determined by the firm's governing body; request from the firm such information and explanations as are reasonably considered necessary to enable him to properly perform the duties described in SUP 4.3.13R(1) to (3); and
- (5) report to the firm's governing body on the results of those investigations and calculations in (3); and advise the firm as to the data and systems reasonably needing to be kept and maintained to provide such information and explanations.
- (6) in the case of a friendly society to which this section applies, perform the functions of the appropriate actuary under section 87 (Actuary's report as to margin of solvency) of the Friendly Societies Act 1992.

4.3.14 G IPRU(INS) 9.4R and IPRU(FSOC) 5.1R require firms to which this section applies to cause an investigation to be made at least yearly by the actuary or actuaries appointed to perform the actuarial function, and to report on the result of that investigation. PRU 7.4 requires realistic basis life firms to calculate the with-profits insurance component as part of their capital resources requirements. The firm is responsible for the methods and assumptions used to determine the liabilities attributable to its long-term insurance business. The obligation on friendly societies to obtain a report from the 'appropriate actuary' under section 87 of the Friendly Societies Act 1992 applies to a friendly society which is to receive a transfer of engagements under section 86 (transfer of engagements to or by a friendly society). The 'appropriate actuary' in this context is the actuary appointed to perform the actuarial function, rather than the appropriate actuary under SUP 4.4 (Appropriate actuaries). A liability to a policyholder is defined in the Glossary as any liability or obligation of an insurer to, or in respect of, a policyholder. It includes policyholder's reasonable expectations as to discretionary benefits and charges.

4.3.15 G The appointed actuary's duty to request information does not necessarily require him to undertake continuous monitoring. This depends on the firm's size, financial position, future plans and other circumstances, including the robustness of its systems and controls. If a periodic update or review is sufficient, it should be carried out as often as is reasonably necessary. An annual update may suffice for small, financially sound, well run insurers. Such periodic reviews might also usefully be supplemented by desk based monitoring to identify circumstances where the timing of the next review

~~might need to be brought forward.~~ SUP 4.3.13R is not intended to be exhaustive of the professional advice that a *firm* should take whether from an *actuary* appointed under this chapter or from any other *actuary* acting for the *firm*. *Firms* should consider what systems and controls are needed to ensure that they obtain appropriate professional advice on financial and risk analysis; for example:

- (1) risk identification, quantification and monitoring;
- (2) stress and scenario testing;
- (3) ongoing financial conditions;
- (4) financial projections for business planning;
- (5) investment strategy and asset-liability matching;
- (6) individual capital assessment;
- (7) pricing of business, including unit pricing;
- (8) variation of any charges for benefits or expenses;
- (9) discretionary surrender charges; and
- (10) adequacy of reinsurance protection.

#### The with-profits actuary function

4.3.16 ~~G If a *firm* also carries out general insurance contracts, the appointed actuary should consider the general insurance business to the extent, if any, that this might have an impact on the long term insurance business.~~ ~~[deleted]~~

4.3.16A R An actuary appointed to perform the with-profits actuary function must:

- (1) advise the *firm's* management, at the level of seniority that is reasonably appropriate, on key aspects of the discretion to be exercised affecting those classes of the *with-profits business* of the *firm* in respect of which he has been appointed;
- (2) where the *firm* is a realistic basis life firm advise the *firm's* governing body as to whether the assumptions used to calculate the *with-profits insurance component* under PRU 7.4 are consistent with the *firm's* PPFM in respect of those classes of the *firm's* *with-profits business*;
- (3) at least once a year, in respect of each financial year commencing on or after 1 January 2005, report to the *firm's* governing body on key aspects (including those aspects of the *firm's* application of its *Principles and Practices of Financial Management* on which the advice described in (1) has been given) of the discretion exercised in respect of the period covered by his report affecting those classes of

with-profits business of the firm;

- (4)\* in respect of each financial year commencing on or after 1 January 2005, make a written report addressed to the relevant classes of the firm's with-profits policyholders, to accompany the firm's annual report under COB 6.11.9R, as to whether, in his opinion and based on the information and explanations provided to him by the firm, the annual report and the discretion exercised by the firm in respect of the period covered by the report may be regarded as taking, or having taken, their interests into account in a reasonable and proportionate manner;
- (5) request from the firm such information and explanations as he reasonably considers necessary to enable him properly to perform the duties in (1) to (4);
- (6) advise the firm as to the data and systems that he reasonably considers necessary to be kept and maintained to provide the duties in (5); and
- (7) in the case of a friendly society to which this section applies, perform the function of appropriate actuary under section 12 (Reinsurance) of the Friendly Societies Act 1992 or section 23A (Reinsurance) of the Friendly Societies Act 1974 as applicable, in respect of those classes of its with-profits business covered by his appointment.

4.3.16B\* G In advising or reporting on the exercise of discretion, an actuary performing the with-profits actuary function should cover the implications for the fair treatment of the firm's with-profits policyholders. His opinion on any communication or report to them should also take into account their information needs and the extent to which the communication or report may be regarded as clear, fair and not misleading. Aspects of the business that should normally be included are:

- (1) bonus rates to be applied to policies at maturity or on the death of the policyholder, or when calculating the annual bonus;
- (2) investment policy in the light of product descriptions disclosed to customers;
- (3) surrender value methodology (including market value adjusters);
- (4) new business plans and premium rates;
- (5) allocation of expenses to with-profits business;
- (6) investment fees to be charged to with-profits business;
- (7) changes to the Principles and Practices of Financial Management;  
and
- (8) communication with policyholders or potential policyholders on the

\* See Addendum 29 July 2005 on p. 24

issues in (1) to (7).

- 4.3.16C G The report in SUP 4.3.16AR(3) should be proportionate to the nature of the *with-profits business*. For smaller *firms* with fewer products, the extent of reporting would be proportionately less.
- 4.3.16D G *Firms* should normally obtain advice, from the *actuary* appointed to perform the *with-profits actuary function* in respect of the affected class or classes of *with-profits business*, whenever they are preparing to make key decisions based on the exercise of discretion affecting their *with-profits business*. *Firms* should also have risk management processes in place to ensure that all relevant matters are referred to the *actuary* for advice.
- 4.3.17 R A *firm* must require and allow any ~~its appointed~~ *actuary* appointed to perform the *with-profits actuary function* to perform his duties and, in particular must:
- (1) keep him informed of the *firm's* business and other plans (including, where relevant, those of any related *firm*, to the extent it is aware of these);
  - (2) provide him with sufficient resources (including his own time and access to the time of others);
  - (3) hold such data and establish such systems as he reasonably requires;
  - (4)\* request his advice about the likely effect of material changes in the *firm's* business plans, practices or other circumstances on the fair treatment of *with-profits policyholders* rights and reasonable expectations of *policyholders* in respect of long term insurance contracts; and
  - (5) pay due regard to his advice, whether provided in response to a request under (4) or on the ~~*appointed actuary's*~~ own initiative; this will include, if he requests it, allowing him to present his advice directly to the *firm's governing body* (that is, the board of *directors* or, for a *friendly society*, the committee of management).
- 4.3.18 G A *firm's* duty to keep an ~~its appointed~~ *actuary* appointed to perform the *with-profits actuary function* informed includes providing relevant information, even where the ~~*appointed actuary*~~ does not ask for it. The *firm* needs to appreciate that the ~~*appointed actuary*~~ may be unaware of certain business developments and so unable to request relevant information.
- 4.3.19 G ~~Section 341 of the Act (Access to books etc.) provides that an *appointed actuary*:~~
- (1) ~~has a right of access at all times to the *firm's* books, accounts and vouchers; and~~
  - (2) ~~is entitled to require from the *firm's* officers such information and explanations as he reasonably considers necessary to perform his~~

\* See Addendum 29 July 2005 on p. 24

~~duties as *appointed actuary*.~~[deleted]

- 4.3.20 R ~~When carrying out his duties, an *appointed actuary* must pay due regard to generally accepted actuarial best practice.~~[deleted]
- 4.3.21 G ~~The standards and guidance issued from time to time by the Institute of Actuaries and the Faculty of Actuaries are important sources of actuarial best practice.~~[deleted]
- 4.4 Appropriate actuaries
- ...
- 4.4.5 G If it appears to the *FSA* that an *appropriate actuary* has failed to comply with a duty imposed on him under the *Act*, it may disqualify him under section 345 of the *Act*. For more detail about what happens when the disqualification of an *actuary* is being considered or put into effect, see *ENF 17 (Disqualification of auditors and actuaries)*. A list of *actuaries* who have been disqualified by the *FSA* may be found on the *FSA* website ([www.fsa.gov.uk](http://www.fsa.gov.uk)).

#### Specific Rights and duties of the appropriate actuary

- 4.4.6 R An *appropriate actuary* must carry out the triennial investigation and prepare an abstract of the report as required by *IPRU(FSOC) 5.2(2)* and provide the interim certificate or statement as required by *IPRU(FSOC) 5.2(3)*.
- 4.4.7 G ~~Section 341 of the *Act* (Access to books etc.) provides that an *appropriate actuary*:~~
- (1) ~~has a right of access at all times to the *firm's* books, accounts and vouchers; and~~
  - (2) ~~is entitled to require from the *firm's* officers such information and explanations as he reasonably considers necessary for the performance of his duties as *appropriate actuary*.~~[deleted]
- 4.4.8 R ~~In carrying out his duties an *appropriate actuary* must pay due regard to generally accepted actuarial best practice.~~[deleted]
- 4.4.9 G ~~The standards and guidance issued by the Institute of Actuaries and the Faculty of Actuaries are important sources of actuarial best practice.~~[deleted]
- 4.5 Provisions applicable to ~~both appointed and appropriate~~ all actuaries

#### Objectivity

- 4.5.1 R An ~~*appointed actuary* or *appropriate actuary*~~ appointed under this chapter must be objective in performing his duties.

- 4.5.2 G Objectivity requires the ~~appointed actuary or appropriate actuary~~ to perform his duties in such a manner that he can have an honest belief in his work and does not compromise the quality of his work or his judgment. An ~~appointed actuary or appropriate actuary~~ should not allow himself to be placed in situations where he feels unable to make objective professional judgments.
- 4.5.3 R An ~~appointed actuary or appropriate actuary~~ appointed under this chapter must take reasonable steps to satisfy himself that he is free from bias, or from any conflict of interest from which bias may reasonably be inferred. He must take appropriate action where this is not the case.
- 4.5.4 G The appropriate action may include asking the *firm's governing body* to re-assign temporarily some or all of his duties to another competent *actuary*. Where this is insufficient, the ~~appointed actuary or appropriate actuary~~ should resign his office.
- 4.5.5 G If the ~~appointed actuary or appropriate actuary~~ is an *employee* of the *firm*, the ordinary incentives of employment, including profit-related pay, *share options* or other financial interests in the *firm* or any *associate*, give rise to a conflict of interest only where they are disproportionate, or exceptional, relative to those of other employees of equivalent seniority.

...

#### ~~Appointed and appropriate a~~Actuaries' statutory duty to report

- 4.5.7 G ~~Appointed actuaries and appropriate a~~Actuaries appointed under this chapter are subject to regulations made by the Treasury under section 342(5) and 343(5) of the *Act* (Information given by *auditor* or *actuary* to the Authority). These regulations oblige *actuaries* to report certain matters to the *FSA*. Sections 342(3) and 343(3) of the *Act* provide that an *actuary* does not contravene any duty by giving information or expressing an opinion to the *FSA*, if he is acting in good faith and he reasonably believes that the information or opinion is relevant to any functions of the *FSA*. These provisions continue to have effect after the end of the *actuary's* term of appointment.

#### Termination of term of office

- 4.5.8 G *SUP 4.5.9R* to *SUP 4.5.11G* apply to a *person* who is or has been an ~~appointed actuary or appropriate actuary~~ appointed under this chapter.
- 4.5.9 R An ~~appointed actuary or appropriate actuary~~ appointed under this chapter must notify the *FSA* without delay if he:
- (1) is removed from office by a *firm*; or
  - (2) resigns before his term of office expires; or
  - (3) is not reappointed by a *firm*.



- 4.5.10 R An ~~actuary~~actuary who has ceased to be appointed under this chapter ~~the appointed actuary or appropriate actuary~~, or who has been formally notified that he will cease to be so appointed, ~~the appointed actuary or appropriate actuary~~, of a firm must notify the FSA without delay:
- (1) of any matter connected with the cessation which he thinks ought to be drawn to the FSA's attention; or
  - (2) that there is no such matter.
- 4.5.11 G When an ~~appointed actuary~~ appointed under SUP 4.3.1R ceases to hold office, he ceases to perform a controlled function ~~the appointed actuary function~~. A firm is therefore required under SUP 10.13.6R to tell the FSA within seven *business days* of its ~~appointed actuary~~ ceasing to hold office and to complete a withdrawal form (Form C, SUP 10 Ann 6R). Note also the requirement of SUP 10.13.7R in relation to qualified withdrawals.

Rights and duties

- 4.5.12 G Section 341 of the Act (Access to books etc.) provides that an actuary appointed under or as a result of the Act:
- (1) has a right of access at all times to the firm's books, accounts and vouchers; and
  - (2) is entitled to require from the firm's officers such information and explanations as he reasonably considers necessary to perform his duties as actuary.
- 4.5.13 R When carrying out his duties, an actuary appointed under this chapter must pay due regard to generally accepted actuarial best practice.
- 4.5.14 G The standards and guidance issued from time to time by the Institute of Actuaries and the Faculty of Actuaries are important sources of actuarial best practice.

...

- 10.4.5 R Table: Controlled functions

Type	CF	Description of controlled function
...		
<i>Required functions*</i>	8	<i>Apportionment and oversight</i>
	...	
	12	<del>Appointed actuary</del> Actuarial function
	12A	<del>With-profits actuary</del> function
...		

...

Appointed-actuary Actuarial function (CF12) and With-profits actuary function (CF12A)

- 10.7.17 R The ~~appointed-actuary actuarial function~~ is the function of acting in the capacity of ~~the an appointed-actuary appointed by~~ of a firm under SUP 4.3.1R to perform the duties set out in SUP 4.3.13R.
- 10.7.17A R The with-profits actuary function is the function of acting in the capacity of an actuary appointed by a firm under SUP 4.3.1R to perform the duties set out in SUP 4.3.16AR.
- 10.7.18 G The effect of SUP 4.1.1R (Application) and SUP 4.3.1R (Appointment of an actuary) is that a *long-term insurer* (unless it is a certain kind of *friendly society*) must appoint ~~an actuary~~ one or more actuaries to perform the actuarial function in respect of all classes of its long-term insurance business and the with-profits actuary function in respect of all classes of its with-profits business, defined in SUP 4.3.1R as an appointed-actuary. The kinds of *friendly society* to which the provisions do not apply are:
- (1) a *registered friendly society* which is a *non-directive friendly society*; and
  - (2) an *incorporated friendly society* that is a *flat rate benefits business friendly society*.
- 10.7.19 G The appointment of an actuary to perform either of these functions appointed-actuary is a personal appointment and the appointee is typically either typically is an employee of the firm. However, in many cases or a partner or employee in a firm of actuaries is appointed.
- 10.7.20 G The ~~appointed-actuary actuarial function~~ and the *with-profits actuary function* does not extend to the giving of actuarial advice to a *firm* by an *actuary* who has not been appointed to perform these functions is acting outside the capacity of appointed-actuary. A *person* who gives actuarial advice, whether occasionally or regularly, other than in his capacity the course of his duties as an appointed-actuary appointed to perform these functions would not be performing a controlled-the appointed-actuary function.
- 10.7.21 G The *rules and guidance* concerning the rights and duties of ~~an the appointed actuary~~ appointed to perform either of these functions are set out in SUP 4.3.130R to SUP 4.3.1817G.

...

18.2.58\* G ...

\* See Addendum 29 July 2005 on p. 25

## SUP Schedule 2 Notification requirements

...

SUP Table:

Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
...				
<i>SUP 4.3.1R(2)</i>	Vacancy in the office of <i>appointed actuary</i>	The fact of the vacancy and the reason for it	Vacancy in the office of <i>appointed actuary</i> will arise or has arisen	Without delay
<i>SUP 4.3.1R(3)</i> and <i>SUP 4.3.2G</i>	Appointment of <i>appointed actuary</i>	Matters specified in <i>SUP 10</i> (because <u>the actuarial function and the with-profits actuary function</u> are specified as <del>acting as an appointed actuary</del> is specified as a controlled functions)	Appointment of <i>appointed actuary</i>	Before appointment
...				
<i>SUP 4.5.11G</i>	<i>Appointed actuary</i> : ceasing to hold office	Matters specified in <i>SUP 10.13.6R</i> and <i>SUP 10.13.7R</i> (because <u>the actuarial function and the with-profits actuary function</u> are <del>acting as an appointed actuary</del> is specified as a controlled functions)	<i>Appointed actuary</i> ceasing to hold office	Seven business days; or, if approved persons Form C is qualified, as soon as reasonably practicable

## Annex E

### Amendments to the Enforcement manual

In this Annex underlining indicates new text and striking through indicates deleted text.

- 17.4.2 G ~~Appointed actuaries appointed by~~ of firms under SUP 4.3.1R ~~who are approved persons~~ and as such will be subject to the *Statements of Principle* and *Code of Practice for Approved Persons*. When deciding whether to exercise its power to disqualify an ~~appointed~~ actuary who is an approved person, the *FSA* will consider whether the particular breach of duty can be adequately addressed by the exercise of its disciplinary powers in relation to *approved persons*. These powers and the factors that the *FSA* will take into account when deciding whether to exercise them are set out in *ENF 11* (Discipline of authorised firms and approved persons: the *FSA*'s general approach), *ENF 12* (Discipline of firms and approved persons: public censures and public statements) and *ENF 13* (Discipline of firms and approved persons: financial penalties).

...

## Annex F

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

Insert or delete the following definitions in the appropriate alphabetical position.

<u>actuarial function</u>	<u>controlled function CF12 in the table of controlled functions, described more fully in SUP 4.3.13R and SUP 10.7.17R.</u>
<del>appointed actuary</del>	<del>an actuary appointed under SUP 4.3.1R (Appointment by firms).</del>
<del>appointed actuary function</del>	<del>controlled function CF12 in the table of controlled functions, described more fully in SUP 10.7.17R.</del>
<u>established surplus</u>	<u>has the meaning in IPRU(INS) 3.3(4).</u>
<u>with-profits actuary function</u>	<u>controlled function CF12A in the table of controlled functions, described more fully in SUP 4.3.16AR and SUP 10.7.17AR.</u>
<u>with-profits actuary</u>	<u>an actuary appointed to perform the with-profits actuary function.</u>

## ADDENDUM

### SUPERVISION MANUAL (ACTUARIES) INSTRUMENT 2004

In this Addendum, the text shown is that which results following the making of this instrument, and all other instruments that have taken effect on or before 25 July 2005. That text is then amended. Underlining indicates new text and striking through indicates deleted text. These amendments make the effect and purpose of the rules clearer, so the position and obligations of the with-profits actuary is clearer.

This Addendum contains amendments to SUP 4.3.16AR(4), SUP 4.3.16BG, SUP 4.3.17R(4) and to SUP 18.2.58G.

Annex D (Supervision manual (SUP)) of this instrument is amended as follows:

- 4.3.16A R An *actuary* appointed to perform the *with-profits actuary function* must:
- ...
- (4) in respect of each financial year commencing on or after 1 January 2005, make a written report addressed to the relevant classes of the *firm's with-profits policyholders*, to accompany the *firm's* annual report under COB 6.11.9R, as to whether, in his opinion and based on the information and explanations provided to him by the *firm*, and taking into account where relevant the *rules* and *guidance* in COB 6.12, the annual report and the discretion exercised by the *firm* in respect of the period covered by the report may be regarded as taking, or having taken, ~~their~~ interests of the relevant classes of the *firm's with-profits policyholders* into account in a reasonable and proportionate manner;
- ...
- 4.3.16B G In advising or reporting on the exercise of discretion, an *actuary* performing the *with-profits actuary function* should cover the implications for the fair treatment of the relevant classes of the *firm's with-profits policyholders*. His opinion on any communication or report to them should also take into account their information needs and the extent to which the communication or report may be regarded as clear, fair and not misleading. Aspects of the business that should normally be included are:
- ...
- ...
- 4.3.17 R A *firm* must require and allow any *actuary* appointed to perform the *with-profits actuary function* to perform his duties and must:
- ...
- (4) request his advice about the likely effect of material changes in the *firm's* business plans, practices or other circumstances on the fair treatment of the relevant classes of the *firm's with-*

*profits policyholders; and*

...

...

- 18.2.58 G For *long-term insurance business*, the affidavit evidence to the court would normally include copies of reports on the transfer by the *appointed actuaries* of both *firms*, which should be provided to the *FSA* at an early stage. *SUP* 4.3.17R(4) requires a *firm* to consult its *appointed actuary* about the likely effect of material changes in its business plans on rights and reasonable expectations of ~~*long-term insurance business*~~ the relevant classes of its *with-profits* policyholders. A transfer would be material unless the liabilities transferred were not material relative to the total liabilities of the *firm*. The advice on a transfer would normally be in the form of a formal report by the *appointed actuary*.

...

Addendum  
29 July 2005

**COMPENSATION SOURCEBOOK (AMENDMENT NO 5) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 213 (The compensation scheme); and
  - (4) section 214 (General).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C This instrument comes into force on 1 January 2005.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Compensation Sourcebook (Amendment No 5) Instrument 2004.

By order of the Board  
18 November 2004



## Annex

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text.

12.6 Quantification: trustees, personal representatives, agents, and joint claims  
Trustees

12.6.2 R ...  
If a claimant has a *claim* as a bare trustee or *nominee company* for one or more beneficiaries, the *FSCS* must treat the beneficiary or beneficiaries as having the *claim*, and not the claimant.

**COMPENSATION SOURCEBOOK (INSURANCE MEDIATION AND PROTECTED CONTRACTS OF INSURANCE) (SCOPE AMENDMENT) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 156 (General supplementary powers);
  - (3) section 157(1) (Guidance);
  - (4) section 213 (The compensation scheme); and
  - (5) section 214 (General).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 14 January 2005.

**Amendments to the Compensation sourcebook**

- D. The Compensation sourcebook is amended in accordance with Annex A to this instrument.

**Amendments to the Glossary**

- E. The Glossary is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the Compensation Sourcebook (Insurance Mediation and Protected Contracts of Insurance) (Scope Amendment) Instrument 2004.

By order of the Board  
18 November 2004

## Annex A

### Amendments to the Compensation sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

- 4.2.2 R Table: Persons not eligible to claim unless *COMP* 4.3 applies (see *COMP* 4.2.1R)

This table belongs to *COMP* 4.2.1R

	...
(17)	<u>Where the <i>claim</i> is in relation to a <i>protected contract of insurance</i> or <i>protected non-investment insurance mediation, bodies corporate, partnerships, mutual associations and unincorporated associations which are not small businesses.</i></u>

...

- 4.3.4 R A ~~person coming~~ partnership which falls within category 14 or category 17 or both of *COMP* 4.2.2R is eligible to claim compensation in respect of a *relevant general insurance contract* entered into before *commencement*.

...

- 5.7.1 R *Protected non-investment insurance mediation* is an *insurance mediation activity* where the *investment* concerned is a *relevant general insurance contract* or a *pure protection contract* but ~~*non-investment insurance contract*~~ which is not a *long-term care insurance contract* or a *reinsurance contract*, provided that the condition in *COMP* 5.7.2R is satisfied.

- 5.7.2 R *COMP* 5.7.1R only applies if the conditions in (1) and (2) are satisfied:

(1) the *protected non-investment insurance mediation* was carried on from:

~~(1)~~ an establishment of the *relevant person* in the *United Kingdom*; or  
(a)

~~(2)~~ a *branch* of a *UK firm* established in another *EEA State* in the exercise of an *EEA right* derived from the *IMD*; and  
(b)

(2) the *customer* making the *claim* (or where *COMP* 3.2.4R applies, the *customer* on behalf of whom a *firm* makes a *claim*) was in contact with:

(a) a *firm* carrying on an *insurance mediation activity* in the *United Kingdom*; or

(b) a *branch* of a *UK firm* established in another *EEA State*

which is carrying on an insurance mediation activity in the exercise of an EEA right derived from the IMD.

...

6.2.2 G An incoming EEA firm, which is a credit institution, an IMD insurance intermediary, ~~an IMD reinsurance intermediary~~, an ISD investment firm or a UCITS management company, and its appointed representatives are not relevant persons in relation to the firm's passported activities, unless it has top-up cover (and in the case of a UCITS management company, only in relation to managing investments (other than of a collective investment scheme), advising on investments or safeguarding and administering investments). (See definition of "participant firm").

...

13.3.1A R COMP 13.3.1R does not apply to a participant firm that may be subject to a claim under COMP 3.2.4R.

13.3.1B G A participant firm to which COMP 13.3.1AR applies must report annual eligible income in accordance with COMP 13.6.11R. Such a participant firm may take advantage of the option to report its annual income attributable to business conducted with or on behalf of eligible claimants.

...

13.7.1 R If an incoming EEA firm, which is a BCD credit institution, an IMD insurance intermediary, ~~an IMD reinsurance intermediary~~ or ISD investment firm, is a participant firm, the FSCS must give the firm such discount (if any) as is appropriate on the share of any levy it would otherwise be required to pay, taking account of the nature of the levy and the extent of the compensation coverage provided by the firm's Home State scheme.

...

14.1.2 R This chapter also applies to an incoming EEA firm which is a credit institution, or an ISD investment firm (or both), an IMD insurance intermediary, ~~an IMD reinsurance intermediary~~ or a UCITS management company.

14.1.3 G This chapter provides supplementary rules and guidance for an incoming EEA firm which is a credit institution, an IMD insurance intermediary, ~~an IMD reinsurance intermediary~~, an ISD investment firm or UCITS management company. It reflects in part the implementation of the Deposit Guarantee Directive, Investors Compensation Directive and UCITS Directive. This sourcebook applies in the usual way to an incoming EEA firm which is exercising EEA rights under the Insurance Directives. Such a firm is not affected by the Deposit Guarantee Directive, the Investors Compensation Directive or the UCITS Directive.

14.1.4 G An incoming EEA firm, which is a credit institution, an IMD insurance

*intermediary, an IMD reinsurance intermediary, an ISD investment firm or a UCITS management company* is not a *participant firm* in relation to its *passport activities* unless it obtains the cover of, or ‘tops up’ into, the *compensation scheme*. This reflects section 213(10) of the Act (The *compensation scheme*) and regulation 2 of the *Electing Participants Regulations* (Persons not to be regarded as relevant persons). If an *incoming EEA firm* also carries on *non-passported activities* (or, for a *UCITS management company*, certain *passport activities*) for which the *compensation scheme* provides cover, it will be a *participant firm* in relation to those activities and will be covered by the *compensation scheme* for those activities in the usual way.

...

14.2.3 G A notice under *COMP* 14.2.1R should include details confirming that the *incoming EEA firm* falls within a prescribed category. In summary:

- (1) the *firm* must be a *credit institution, an IMD insurance intermediary, an IMD reinsurance intermediary, an ISD investment firm or a UCITS management company*;

...

## Annex B

### Amendment to the Glossary of definitions

In this Annex underlining indicates new text and striking through indicates deleted text.

*annual eligible income* (in *COMP*) the annual income (as described in Part 2 of *SUP* 20 Ann 1R) for the *firm's* last financial year preceding the date for submission of the information under *COMP* ~~1316.6.11R~~ attributable to the relevant *contribution group*; or if the *firm* prefers, that amount of that annual income attributable to business conducted with or on behalf of *eligible claimants*, but only if the *firm* notifies *FSCS* of the amount in accordance with *FSCS* reporting requirements.

**SENIOR MANAGEMENT ARRANGEMENTS, SYSTEMS AND CONTROLS  
(OPERATIONAL RISK) INSTRUMENT 2004**

**Power exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the power in section 157(1) (Guidance) of the Financial Services and Markets Act 2000.

**Commencement**

- B. This instrument comes into force on 31 December 2004.

**Amendments to the Senior Management Arrangements, Systems and Controls  
sourcebook**

- C. The Senior Management Arrangements, Systems and Controls sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Senior Management Arrangements, Systems and Controls (Operational Risk) Instrument 2004.

By order of the Board  
16 December 2004

## Annex

### Amendments to the Senior Management Arrangements, Systems and Controls sourcebook

In this Annex, underlining indicates new text. Where an entire section of text is being inserted the place where the change will be made is indicated and the text is not underlined.

#### Application and purpose

##### 1.1 Application of SYSC 2 and SYSC 3

...

- 1.1.-1 G The application of SYSC 3A (Operational Risk: Systems and Controls) is set out in SYSC 3A.1.1G and SYSC 3A.1.2G. The application of SYSC 4 (Guidance on Public Interest Disclosure Act: Whistleblowing) is set out in SYSC 4.1.1G (Application).

...

Insert, after SYSC Chapter 3, the following new chapter, SYSC 3A. The text for this new chapter is not underlined.

#### 3A **Operational Risk: Systems and Controls**

##### 3A.1 **Application**

- 3A.1.1 G SYSC 3A applies to an *insurer* unless it is:

- (1) a *non-directive friendly society*; or
- (2) an *incoming EEA firm*; or
- (3) an *incoming Treaty firm*.

- 3A.1.2 G SYSC 3A applies to:

- (1) an *EEA-deposit insurer*; and
- (2) a *Swiss general insurer*;

only in respect of the activities of the *firm* carried on from a *branch* in the *United Kingdom*.

##### 3A.2 **Purpose**

- 3A.2.1 G This chapter provides *guidance* on how to interpret SYSC 3.1.1R and SYSC 3.2.6R, which deal with the establishment and maintenance of systems and



controls, in relation to the management of operational risk. Operational risk has been described by the Basel Committee on Banking Supervision as “the risk of loss, resulting from inadequate or failed internal processes, people and systems, or from external events”. This chapter covers systems and controls for managing risks concerning any of a *firm’s* operations, such as its IT systems and *outsourcing* arrangements. It does not cover systems and controls for managing credit, market, liquidity and insurance risk.

- 3A.2.2 G Operational risk is a concept that can have a different application for different *firms*. A *firm* should assess the appropriateness of the *guidance* in this chapter in the light of the scale, nature and complexity of its activities as well as its obligations as set out in *Principle 3*, to organise and control its affairs responsibly and effectively.
- 3A.2.3 G A *firm* should take steps to understand the types of operational risk that are relevant to its particular circumstances, and the operational losses to which they expose the *firm*. This should include considering the potential sources of operational risk addressed in this chapter: people; processes and systems; external events.
- 3A.2.4 G Operational risk can affect, amongst other things, a *firm’s* solvency, or lead to unfair treatment of consumers or lead to financial crime. A *firm* should consider all operational risk events that may affect these matters in establishing and maintaining its systems and controls.

### 3A.3 Other related Handbook sections

- 3A.3.1 G The following is a non-exhaustive list of *rules* and *guidance* in the *Handbook* that are relevant to a *firm’s* management of operational risk:
- (1) *PRU 1.4* and *PRU 6.1* contain specific *rules* and *guidance* for the establishment and maintenance of operational risk systems and controls in a *prudential context*.
  - (2) *COB* contains *rules* and *guidance* that can relate to the management of operational risk, for example, *COB 2* (Rules which apply to all firms conducting designated investment business), *COB 3* (Financial promotion), *COB 5* (Advising and selling), *COB 7* (Dealing and managing) and *COB 9* (Client assets).

### 3A.4 Requirements to notify the FSA

- 3A.4.1 G Under *Principle 11* and *SUP 15.3.1R* a *firm* must notify the *FSA* immediately of any operational risk matter of which the *FSA* would reasonably expect notice. *SUP 15.3.8G* provides *guidance* on the occurrences that this requirement covers, which include a significant failure in systems and controls and a significant operational loss.
- 3A.4.2 G Regarding operational risk, matters of which the *FSA* would expect notice under *Principle 11* include:

- (1) any significant operational exposures that a *firm* has identified;
- (2) the *firm's* invocation of a business continuity plan; and
- (3) any other significant change to a *firm's* organisation, infrastructure or business operating environment.

### 3A.5 Risk management terms

3A.5.1 G In this chapter, the following interpretations of risk management terms apply:

- (1) a *firm's* risk culture encompasses the general awareness, attitude and behaviour of its *employees* and *appointed representatives* to risk and the management of risk within the organisation;
- (2) operational exposure means the degree of operational risk faced by a *firm* and is usually expressed in terms of the likelihood and impact of a particular type of operational loss occurring (for example, fraud, damage to physical assets);
- (3) a *firm's* operational risk profile describes the types of operational risks that it faces, including those operational risks within a *firm* that may have an adverse impact upon the quality of service afforded to its *clients*, and its exposure to these risks.

### 3A.6 People

3A.6.1 G A *firm* should consult SYSC 3.2.2G to SYSC 3.2.5G for *guidance* on reporting lines and delegation of functions within a *firm* and SYSC 3.2.13G to SYSC 3.2.14G for *guidance* on the suitability of *employees* and *appointed representatives*. This section provides additional *guidance* on management of *employees* and other human resources in the context of operational risk.

3A.6.2 G A *firm* should establish and maintain appropriate systems and controls for the management of operational risks that can arise from *employees*. In doing so, a *firm* should have regard to:

- (1) its operational risk culture, and any variations in this or its human resource management practices, across its operations (including, for example, the extent to which the compliance culture is extended to in-house IT staff);
- (2) whether the way *employees* are remunerated exposes the *firm* to the risk that it will not be able to meet its regulatory obligations (see SYSC 3.2.18G). For example, a *firm* should consider how well remuneration and performance indicators reflect the *firm's* tolerance for operational risk, and the adequacy of these indicators for measuring performance;
- (3) whether inadequate or inappropriate training of *client-facing* services exposes *clients* to risk of loss or unfair treatment including by not

- enabling effective communication with the *firm*;
- (4) the extent of its compliance with applicable regulatory and other requirements that relate to the welfare and conduct of *employees*;
- (5) its arrangements for the continuity of operations in the event of *employee* unavailability or loss;
- (6) the relationship between indicators of ‘people risk’ (such as overtime, sickness, and *employee* turnover levels) and exposure to operational losses; and
- (7) the relevance of all the above to *employees* of a third party supplier who are involved in performing an *outsourcing* arrangement. As necessary, a *firm* should review and consider the adequacy of the staffing arrangements and policies of a service provider.

### **Employee Responsibilities**

- 3A.6.3 G A *firm* should ensure that all *employees* are capable of performing, and aware of, their operational risk management responsibilities, including by establishing and maintaining:
- (1) appropriate segregation of employees' duties and appropriate supervision of *employees* in the performance of their responsibilities (see SYSC 3.2.5G);
  - (2) appropriate recruitment and subsequent processes to review the fitness and propriety of *employees* (see SYSC 3.2.13G and SYSC 3.2.14G);
  - (3) clear policy statements and appropriate systems and procedures manuals that are effectively communicated to *employees* and available for *employees* to refer to as required. These should cover, for example, compliance, IT security and health and safety issues;
  - (4) training processes that enable *employees* to attain and maintain appropriate competence; and
  - (5) appropriate and properly enforced disciplinary and employment termination policies and procedures.
- 3A.6.4 G A *firm* should have regard to SYSC 3A.6.3G in relation to *approved persons*, people occupying positions of high personal trust (for example, security administration, payment and settlement functions); and people occupying positions requiring significant technical competence (for example, *derivatives* trading and technical security administration). A *firm* should also consider the *rules* and *guidance* for *approved persons* in other parts of the *Handbook* (including *APER* and *SUP*) and the *rules* and *guidance* on *senior manager* responsibilities in SYSC 2.1 (Apportionment of Responsibilities).

### 3A.7 **Processes and systems**

- 3A.7.1 G A *firm* should establish and maintain appropriate systems and controls for managing operational risks that can arise from inadequacies or failures in its processes and systems (and, as appropriate, the systems and processes of third party suppliers, agents and others). In doing so a *firm* should have regard to:
- (1) the importance and complexity of processes and systems used in the end-to-end operating cycle for products and activities (for example, the level of integration of systems);
  - (2) controls that will help it to prevent system and process failures or identify them to permit prompt rectification (including pre-approval or reconciliation processes);
  - (3) whether the design and use of its processes and systems allow it to comply adequately with regulatory and other requirements;
  - (4) its arrangements for the continuity of operations in the event that a significant process or system becomes unavailable or is destroyed; and
  - (5) the importance of monitoring indicators of process or system risk (including reconciliation exceptions, compensation payments for *client* losses and documentation errors) and experience of operational losses and exposures.

#### **Internal documentation**

- 3A.7.2 G Internal documentation may enhance understanding and aid continuity of operations, so a *firm* should ensure the adequacy of its internal documentation of processes and systems (including how documentation is developed, maintained and distributed) in managing operational risk.

#### **External documentation**

- 3A.7.3 G A *firm* may use external documentation (including contracts, transaction statements or advertising brochures) to define or clarify terms and conditions for its products or activities, its business strategy (for example, including through press statements), or its brand. Inappropriate or inaccurate information in external documents can lead to significant operational exposure.
- 3A.7.4 G A *firm* should ensure the adequacy of its processes and systems to review external documentation prior to issue (including review by its compliance, legal and marketing departments or by appropriately qualified external advisers). In doing so a *firm* should have regard to:
- (1) compliance with applicable regulatory and other requirements (such as *COB 3* (Financial promotion));

- (2) the extent to which its documentation uses standard terms (that are widely recognised, and have been tested in the courts) or non-standard terms (whose meaning may not yet be settled or whose effectiveness may be uncertain);
- (3) the manner in which its documentation is issued; and
- (4) the extent to which confirmation of acceptance is required (including by *customer* signature or counterparty confirmation).

### **IT systems**

- 3A.7.5 G IT systems include the computer systems and infrastructure required for the automation of processes, such as application and operating system software; network infrastructure; and desktop, server, and mainframe hardware. Automation may reduce a *firm's* exposure to some 'people risks' (including by reducing human errors or controlling access rights to enable segregation of duties), but will increase its dependency on the reliability of its IT systems.
- 3A.7.6 G A *firm* should establish and maintain appropriate systems and controls for the management of its IT system risks, having regard to:
- (1) its organisation and reporting structure for technology operations (including the adequacy of senior management oversight);
  - (2) the extent to which technology requirements are addressed in its business strategy;
  - (3) the appropriateness of its systems acquisition, development and maintenance activities (including the allocation of responsibilities between IT development and operational areas, processes for embedding security requirements into systems); and
  - (4) the appropriateness of its activities supporting the operation of IT systems (including the allocation of responsibilities between business and technology areas).

### **Information security**

- 3A.7.7 G Failures in processing information (whether physical, electronic or known by *employees* but not recorded) or of the security of the systems that maintain it can lead to significant operational losses. A *firm* should establish and maintain appropriate systems and controls to manage its information security risks. In doing so a *firm* should have regard to:
- (1) confidentiality: information should be accessible only to *persons* or systems with appropriate authority, which may require firewalls within a system, as well as entry restrictions;
  - (2) integrity: safeguarding the accuracy and completeness of information

and its processing;

- (3) availability and authentication: ensuring that appropriately authorised *persons* or systems have access to the information when required and that their identity is verified;
- (4) non-repudiation and accountability: ensuring that the *person* or system that processed the information cannot deny their actions.

3A.7.8 G A *firm* should ensure the adequacy of the systems and controls used to protect the processing and security of its information, and should have regard to established security standards such as ISO17799 (Information Security Management).

### **Geographic location**

3A.7.9 G Operating processes and systems at separate geographic locations may alter a *firm's* operational risk profile (including by allowing alternative sites for the continuity of operations). A *firm* should understand the effect of any differences in processes and systems at each of its locations, particularly if they are in different countries, having regard to:

- (1) the business operating environment of each country (for example, the likelihood and impact of political disruptions or cultural differences on the provision of services);
- (2) relevant local regulatory and other requirements regarding data protection and transfer;
- (3) the extent to which local regulatory and other requirements may restrict its ability to meet regulatory obligations in the *United Kingdom* (for example, access to information by the *FSA* and local restrictions on internal or external audit); and
- (4) the timeliness of information flows to and from its headquarters and whether the level of delegated authority and the risk management structures of the overseas operation are compatible with the *firm's* head office arrangements.

### **3A.8 External events and other changes**

3A.8.1 G The exposure of a *firm* to operational risk may increase during times of significant change to its organisation, infrastructure and business operating environment (for example, following a corporate restructure or changes in regulatory requirements). Before, during, and after expected changes, a *firm* should assess and monitor their effect on its risk profile, including with regard to :

- (1) untrained or de-motivated *employees* or a significant loss of *employees* during the period of change, or subsequently;
- (2) inadequate human resources or inexperienced *employees* carrying out

routine business activities owing to the prioritisation of resources to the programme or project;

- (3) process or system instability and poor management information due to failures in integration or increased demand; and
- (4) inadequate or inappropriate processes following business re-engineering.

- 3A.8.2 G A *firm* should establish and maintain appropriate systems and controls for the management of the risks involved in expected changes, such as by ensuring:
- (1) the adequacy of its organisation and reporting structure for managing the change (including the adequacy of senior management oversight);
  - (2) the adequacy of the management processes and systems for managing the change (including planning, approval, implementation and review processes); and
  - (3) the adequacy of its strategy for communicating changes in systems and controls to its *employees*.

#### **Unexpected changes and business continuity management**

- 3A.8.3 G *SYSC* 3.2.19G provides high level *guidance* on business continuity. This section provides additional *guidance* on managing business continuity in the context of operational risk.
- 3A.8.4 G The high level requirement for appropriate systems and controls at *SYSC* 3.1.1R applies at all times, including when a business continuity plan is invoked. However, the *FSA* recognises that, in an emergency, a *firm* may be unable to comply with a particular *rule* and the conditions for relief are outlined in *GEN* 1.3 (Emergency).
- 3A.8.5 G A *firm* should consider the likelihood and impact of a disruption to the continuity of its operations from unexpected events. This should include assessing the disruptions to which it is particularly susceptible (and the likely timescale of those disruptions) including through:
- (1) loss or failure of internal and external resources (such as people, systems and other assets);
  - (2) the loss or corruption of its information; and
  - (3) external events (such as vandalism, war and “acts of God”).
- 3A.8.6 G A *firm* should implement appropriate arrangements to maintain the continuity of its operations. A *firm* should act to reduce both the likelihood of a disruption (including by succession planning, systems resilience and dual processing); and the impact of a disruption (including by contingency

arrangements and insurance).

- 3A.8.7 G A *firm* should document its strategy for maintaining continuity of its operations, and its plans for communicating and regularly testing the adequacy and effectiveness of this strategy. A *firm* should establish:
- (1) formal business continuity plans that outline arrangements to reduce the impact of a short, medium or long-term disruption, including:
    - (a) resource requirements such as people, systems and other assets, and arrangements for obtaining these resources;
    - (b) the recovery priorities for the *firm's* operations; and
    - (c) communication arrangements for internal and external concerned parties (including the *FSA*, *clients* and the press);
  - (2) escalation and invocation plans that outline the processes for implementing the business continuity plans, together with relevant contact information;
  - (3) processes to validate the integrity of information affected by the disruption;
  - (4) processes to review and update (1) to (3) following changes to the *firm's* operations or risk profile (including changes identified through testing).
- 3A.8.8 G The use of an alternative site for recovery of operations is common practice in business continuity management. A *firm* that uses an alternative site should assess the appropriateness of the site, particularly for location, speed of recovery and adequacy of resources. Where a site is shared, a *firm* should evaluate the risk of multiple calls on shared resources and adjust its plans accordingly.
- 3A.9 **Outsourcing**
- 3A.9.1 G As *SYSC* 3.2.4G explains, a *firm* cannot contract out its regulatory obligations and should take reasonable care to supervise the discharge of *outsourced* functions. This section provides additional *guidance* on managing *outsourcing* arrangements (and will be relevant, to some extent, to other forms of third party dependency) in relation to operational risk. *Outsourcing* may affect a *firm's* exposure to operational risk through significant changes to, and reduced control over, people, processes and systems used in outsourced activities.
- 3A.9.2 G *Firms* should take particular care to manage *material outsourcing* arrangements and, as *SUP* 15.3.8G(1)(e) explains, a *firm* should notify the *FSA* when it intends to enter into a *material outsourcing* arrangement.
- 3A.9.3 G A *firm* should not assume that because a service provider is either a regulated *firm* or an intra-group entity an *outsourcing* arrangement with that



provider will, in itself, necessarily imply a reduction in operational risk.

3A.9.4 G Before entering into, or significantly changing, an *outsourcing* arrangement, a *firm* should:

- (1) analyse how the arrangement will fit with its organisation and reporting structure; business strategy; overall risk profile; and ability to meet its regulatory obligations;
- (2) consider whether the agreements establishing the arrangement will allow it to monitor and control its operational risk exposure relating to the *outsourcing*;
- (3) conduct appropriate due diligence of the service provider's financial stability and expertise;
- (4) consider how it will ensure a smooth transition of its operations from its current arrangements to a new or changed *outsourcing* arrangement (including what will happen on the termination of the contract); and
- (5) consider any concentration risk implications such as the business continuity implications that may arise if a single service provider is used by several *firms*.

3A.9.5 G In negotiating its contract with a service provider, a *firm* should have regard to:

- (1) reporting or notification requirements it may wish to impose on the service provider;
- (2) whether sufficient access will be available to its internal auditors, external auditors or *actuaries* (see section 341 of the *Act*) and to the *FSA* (see *SUP 2.3.5R* (Access to premises) and *SUP 2.3.7R* (Suppliers under material outsourcing arrangements));
- (3) information ownership rights, confidentiality agreements and *Chinese walls* to protect *client* and other information (including arrangements at the termination of the contract);
- (4) the adequacy of any guarantees and indemnities;
- (5) the extent to which the service provider must comply with the *firm's* policies and procedures (covering, for example, information security);
- (6) the extent to which a service provider will provide business continuity for *outsourced* operations, and whether exclusive access to its resources is agreed;
- (7) the need for continued availability of software following difficulty at

a third party supplier;

- (8) the processes for making changes to the *outsourcing* arrangement (for example, changes in processing volumes, activities and other contractual terms) and the conditions under which the *firm* or service provider can choose to change or terminate the *outsourcing* arrangement, such as where there is:
  - (a) a change of ownership or *control* (including insolvency or receivership) of the service provider or *firm*;
  - (b) significant change in the business operations (including sub-contracting) of the service provider or *firm*; or
  - (c) inadequate provision of services that may lead to the *firm* being unable to meet its regulatory obligations.

3A.9.6 G In implementing a relationship management framework, and drafting the service level agreement with the service provider, a *firm* should have regard to:

- (1) the identification of qualitative and quantitative performance targets to assess the adequacy of service provision, to both the *firm* and its *clients*, where appropriate;
- (2) the evaluation of performance through service delivery reports and periodic self certification or independent review by internal or external auditors; and
- (3) remedial action and escalation processes for dealing with inadequate performance.

3A.9.7 G In some circumstances, a *firm* may find it beneficial to use externally validated reports commissioned by the service provider, to seek comfort as to the adequacy and effectiveness of its systems and controls. The use of such reports does not absolve the *firm* of responsibility to maintain other oversight. In addition, the *firm* should not normally have to forfeit its right to access, for itself or its agents, to the service provider's premises.

3A.9.8 G A *firm* should ensure that it has appropriate contingency arrangements to allow business continuity in the event of a significant loss of services from the service provider. Particular issues to consider include a significant loss of resources at, or financial failure of, the service provider, and unexpected termination of the *outsourcing* arrangement.

### 3A.10 **Insurance**

3A.10.1 G Whilst a *firm* may take out insurance with the aim of reducing the monetary impact of operational risk events, non-monetary impacts may remain (including impact on the *firm's* reputation). A *firm* should not assume that insurance alone can replace robust systems and controls.

3A.10.2 G When considering utilising insurance, a *firm* should consider:

- (1) the time taken for the *insurer* to pay claims (including the potential time taken in disputing cover) and the *firm's* funding of operations whilst awaiting payment of claims;
- (2) the financial strength of the *insurer*, which may determine its ability to pay claims, particularly where large or numerous small claims are made at the same time; and
- (3) the effect of any limiting conditions and exclusion clauses that may restrict cover to a small number of specific operational losses and may exclude larger or hard to quantify indirect losses (such as lost business or reputational costs).

**INTEGRATED PRUDENTIAL SOURCEBOOK (INSURERS AND OTHER AMENDMENTS) (CONSEQUENTIAL AMENDMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making power);
  - (2) section 141 (Insurance business rules);
  - (3) section 150(2) (Actions for damages);
  - (4) section 156 (General supplementary powers);
  - (5) section 157(1) (Guidance); and
  - (6) section 340 (Appointment).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) the amendment to rule 5.11(1), and rule 5.11(1A), of IPRU(FSOC) in Annex F come into force on 31 December 2005;
  - (2) the remainder of this instrument comes into force on 31 December 2004.

**Amendments to the Handbook**

- D. The modules of the FSA’s Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Senior Management Arrangements, Systems and Controls (SYSC)	Annex A
Threshold Conditions (COND)	Annex B
General provisions (GEN)	Annex C
Interim Prudential sourcebook for Banks (IPRU(BANK))	Annex D
Interim Prudential sourcebook for Building Societies (IPRU(BSOC))	Annex E
Interim Prudential sourcebook for Friendly Societies (IPRU(FSOC))	Annex F
Interim Prudential sourcebook for Insurers (IPRU(INS))	Annex G
Insurance: Conduct of Business sourcebook (ICOB)	Annex H
Market Conduct sourcebook (MAR)	Annex I
Authorisation manual (AUTH)	Annex J
Supervision manual (SUP)	Annex K
Enforcement manual (ENF)	Annex L
Credit Unions sourcebook (CRED)	Annex M
Electronic Money sourcebook (ELM)	Annex N
Glossary	Annex O

**Citation**

- E. This instrument may be cited as the Integrated Prudential Sourcebook (Insurers and Other Amendments) (Consequential Amendments) Instrument 2004.

By order of the Board  
16 December 2004

Amended by Addendum  
22 December 2004

## Annex A

### Amendments to Senior Management Arrangements, Systems and Controls

In this Annex, underlining indicates new text.

Appendix 1.1 Matters reserved to a Home State regulator (see SYSC 1.1.1R(1)(b) and SYSC 1.1.1R(1)(c))

...

1.1.8 G Examples of how the *FSA* considers that *SYSC 3* will apply in practice to an *incoming EEA firm* (see *SYSC 1.1.4G*) are as follows:

(1) The Integrated Prudential Sourcebook (*PRU*) (with the exception of *PRU 7.6.33R* on the payment of financial penalties) and the Interim Prudential sourcebook (insurers) (*IPRU(INS)*) (with the exception of rules 3.6 and 3.7) does not apply to an *insurer* which is an *incoming EEA firm*. Similarly, *SYSC 3* does not require such a *firm*:

(a) ...

(b) to establish systems and controls for compliance with that Interim Prudential sourcebook or *PRU* (*SYSC 3.2.6R*); or

...

...

## Annex B

### Amendments to the Threshold Conditions

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

2.4.2 G ...

- (3) High level systems and control requirements are in *SYSC*. Detailed financial resources and systems requirements are in the relevant section of *IPRU* or *PRU*, including specific provisions for particular types of *regulated activity*. ...

2.4.3 G (1) ...

- (2) ... The *FSA*'s approach to the consolidated supervision of a *firm* and its *group* is in the relevant part of *IPRU* or *PRU*.

2.4.4 G (1) ...

- (2) Relevant matters may include but are not limited to:
- (a) whether there are any indications that the *firm* may have difficulties if the application is granted (see *COND* 2.4.6G), at the time of the grant or in the future, in complying with any of the *FSA*'s prudential *rules* (see the relevant part of *IPRU* or *PRU*);

...

...

...

2.4.6 G (1) ...

(2) ...

- (a) it has a well constructed business plan or strategy plan for its product or service which demonstrates that it is ready, willing and organised to comply with the relevant requirements in *IPRU*, *PRU* and *SYSC* that apply to the *regulated activity* it is seeking to carry on;

...

...

...

2.6.5 G (1) ...

- (2) A *person* seeking to carry on *insurance business* in the *United*

*Kingdom* must have assets in the *United Kingdom* to a value specified in ~~*IPRU (INS)*~~ *PRU*. ...

- (3) ... This deposit will be subject to provisions in ~~*IPRU (INS)*~~ *PRU 7.6*.



## Annex C

### Amendments to the General provisions

In this Annex, underlining indicates new text.

...

- 2.2.7 R In the *Handbook* (except *IPRU*, unless otherwise indicated):
- (1) an expression in italics which is defined in the *Glossary* has the meaning given there; and
  - (2) an expression in italics which relates to an expression defined in the *Glossary* must be interpreted accordingly.

## Annex D

### Amendments to the Interim Prudential sourcebook for Banks

In this Annex, underlining indicates new text and striking through indicates deleted text.

GN: Section 2

...

## 2 THE PRUDENTIAL SOURCEBOOK FOR BANKS: APPLICATION AND PURPOSE

### APPLICATION

1. ~~The Prudential Sourcebook for banks sets out the Financial Services Authority's ("the FSA's") detailed prudential standards and related notification requirements applying to *banks* authorised under the Financial Services and Markets Act 2000 ("the Act"). The sourcebook sets out material relevant to all *banks* (see definition in section 3.5 of Chapter GN). However, most of the material applies only to *UK banks*. From 31 December 2004 the Financial Services Authority (the FSA) has begun the phased implementation for *banks* of its Integrated Prudential Sourcebook (*PRU*). This will eventually replace the set of sectoral prudential sourcebooks applied on an interim basis, including this one applying to *banks* (*IPRU(BANK)*). Over the transition period until all the provisions of *IPRU(BANK)* have been revoked, the FSA's detailed prudential standards (and some related notification requirements) applying to *banks* authorised under the *Act* are set out in a combination of *PRU* and *IPRU(BANK)*. Where a chapter of *IPRU(BANK)* has been substantively affected by the implementation of *PRU*, the introductory section of that chapter has been amended to indicate in broad terms how the chapter's provisions relate to those in *PRU*. *Banks* are responsible for ensuring that they meet all the prudential standards applying to them in both *PRU* and *IPRU(BANK)* during the transitional period.~~
2. *IPRU(BANK)* sets out material relevant to all *banks* (see definition in section 3.5 of Chapter GN). However, most of the material applies only to *UK banks*. The only parts of the sourcebook *IPRU(BANK)* which apply to *EEA banks* are the rules and guidance on liquidity (Rule 3.3.15 and Chapter LM) and fraud (Chapter FR).

### PURPOSE

3. ...
4. The purpose of the prudential standards ~~set out in this sourcebook~~ applying to *banks* is to ensure that banks maintain capital and other financial resources commensurate with their risks and appropriate systems and controls to enable them to manage those risks. The FSA requires in particular that banks maintain adequate capital against their risks: capital enables banks to absorb losses without endangering customer deposits; that they maintain adequate liquidity; and that they identify and control their large credit exposures - which might otherwise be a source of loss to a bank on a scale that might threaten a bank's

solvency.

5. ~~This sourcebook, The prudential standards applying to banks, together with the separate prudential sourcebook those separately~~ applying to building societies, also implements EC directives setting out prudential standards as these apply to *credit institutions*. Where a bank is part of a financial conglomerate, it will also be subject to additional rules and guidance set out in *PRU* 8.4. A bank with an ultimate non-EEA parent may also be subject to some provisions in *PRU* 8.5. And all banks that are part of a group are subject to the general provisions in *PRU* 8.1.

## POWERS AND GENERAL APPROACH

6. ...
7. The prudential standards in this sourcebook applying to banks are set out in the form either of rules and evidential provisions which the FSA has made under Part X of the Act; or of guidance setting out the FSA's expectation of how *banks* should comply with these rules and with the related Principles for Businesses and how they should meet the relevant Threshold Conditions (see PRIN and COND). Where a *bank* complies with this guidance, the FSA will normally hold it to be in compliance with the relevant rules and to meet the relevant Threshold Conditions. ~~The FSA's~~ *IPRU(BANK)*'s rules and evidential provisions are set out in Section 3 of this chapter.
8. ~~This sourcebook applies to banks on an interim basis pending the preparation and implementation of a single Prudential Sourcebook applying to all firms regulated by the FSA—termed the Integrated Prudential Sourcebook.—In developing the interim sourcebook~~ *IPRU(BANK)*, the FSA has drawn on the standards which formerly applied to *banks* authorised under the Banking Act 1987. The FSA has expressed most of the equivalent standards in ~~this sourcebook~~ *IPRU(BANK)* as guidance, identifying to which rules the guidance refers. Only the requirements set out in Section 3 of this chapter take the form of rules. Each chapter sets out in the opening paragraphs the rules, including the Principles for Businesses and Threshold Conditions, to which the guidance refers.
9. This approach has been adopted, after consultation, as appropriate for material that will apply on an interim basis only. It is the FSA's intention in developing ~~its Integrated Prudential Sourcebook~~ *PRU* to make fuller use of its rule-making powers to express its detailed prudential standards.
10. ~~This sourcebook~~ *IPRU(BANK)* also sets out rules and guidance on the information related to prudential standards which *banks* should notify to the FSA. The FSA needs to be informed of certain information by *banks* if it is to monitor compliance with its requirements. The rules and guidance in ~~this sourcebook~~ *IPRU(BANK)* supplement, in respect to *banks*, the FSA's general notification requirements set out in the Supervision Manual [see SUP 13].

...

GN: Section 3

...

### 3 THE FSA'S PRUDENTIAL RULES FOR BANKS

...

3.4.12R A *bank* must send to the *FSA*:

(a) a copy of the policy statement it has first adopted in compliance with each of *IPRU (BANK)* 3.4.1R, ~~3.4.3R~~, 3.4.5R and 3.4.7R as soon as possible after adopting it; and

(b) ...

...

LM: Section 1

### MISMATCH LIQUIDITY

#### 1 INTRODUCTION

##### 1.1 Legal sources

1 ...

See ch  
GN s3

(c) The rules requiring a bank to maintain adequate liquidity appropriate to the nature and scale of its business, and to ~~provide the FSA with a statement of its liquidity policy~~ set out its policy on liquidity risk management in a written statement.

...

2 As part of the phased implementation of the Integrated Prudential Sourcebook (PRU), provisions in PRU 1.2 and PRU 5.1 relating to a firm's systems and controls for liquidity risk have been introduced, superseding – and leading to the revocation or amendment of – material formerly in this chapter. This chapter and chapter LS sets out the FSA's framework for monitoring the liquidity of banks authorised for the purposes of the Act to determine whether the above requirements are met.

...

...

## 10 POLICY STATEMENTS

See ch  
GN s3

1 In order to provide a framework for monitoring liquidity on a basis appropriate to each bank the FSA has made a rule requiring each bank to maintain ~~provide~~ a statement of its liquidity management policy (see rule 3.4.3).

...

See PRU  
5.1

4 The policy statement should consider the management of liquidity in both normal and abnormal circumstances. In particular, it should include details of the bank's contingency funding plan maintained as required by PRU 5.1.86E. ~~A bank should consider how it would react to severe funding difficulties affecting it:~~

- (a) The statement should also include specifically:
- (i) who is responsible for liquidity management on a day to day basis; ~~and who is responsible for crisis management in the event of a liquidity crisis; and~~
  - (ii) what are likely to be the most reliable sources of funds in normal ~~and crisis~~ circumstances;
  - (iii) ~~what warning indicators are used as signs of an approaching crisis; and~~
  - (iv) ~~what action is planned to pre-empt it.~~

...

LS: Section 1

...

## STERLING STOCK LIQUIDITY

### 1 INTRODUCTION

#### 1.1 Legal sources

1 ...

See ch  
GN(3)

(c) The rules made to require a bank to maintain adequate liquidity appropriate to the nature and scale of its business, and to ~~provide the FSA with a statement of its liquidity policy~~ set out its policy on liquidity risk management in a written statement.

...

2 As part of the phased implementation of the Integrated Prudential Sourcebook (PRU), provisions in PRU 1.2 and PRU 5.1 relating to a firm's systems and controls for liquidity risk have been introduced, superseding – and leading to the revocation or amendment of – material formerly in this chapter. This chapter and chapter LM sets out the FSA's framework for monitoring the liquidity of banks authorised for the purposes of the Act to determine whether the above requirements are met.

...

LS: Section 3

### 3 MAIN FEATURES OF THE POLICY

...

#### 3.1 The main features of the sterling stock liquidity policy

...

2 A sterling stock liquidity bank should include in the statement of its liquidity management policy ~~notified to the FSA~~ its intention to:

...

LS: Section 4

## **4 THE MEASUREMENT OF STERLING STOCK LIQUIDITY**

...

### **4.3 The wholesale sterling net outflow limit and sterling stock 'floor'**

#### **4.3.1 General**

...

6 A bank's limit and 'floor' should be those included in its most recent liquidity policy statement ~~notified to the FSA~~ unless otherwise agreed in writing with the FSA.

...

LS: Section 5

## **5 MONITORING LIQUIDITY**

### **5.1 General**

1 All banks are required to ~~notify~~ maintain a liquidity policy statement ~~to the FSA~~. They should also maintain adequate systems for monitoring liquidity.

...

## Annex E

### Amendments to the Interim Prudential sourcebook for Building Societies

In this Annex, underlining indicates new text and striking through indicates deleted text.

X Introductory Chapter

X.1 Introduction

...

X.1.2 G From 31 December 2004 as part of the programme to implement the Integrated Prudential sourcebook (PRU), rules and guidance on elements of liquidity risk systems and controls located in PRU 1.2 and PRU 5.1, come into effect, and supersede some original material in this sourcebook.

...

X.4.1 G The Interim Prudential Sourcebook for building societies sets out most of the FSA's detailed prudential standards and related notification requirements ~~applying (where these apply only to societies authorised under the Act)~~ and covers the constitutional matters referred to above. Other prudential standards applying to societies are set out in the Act and elsewhere in the Handbook: see, for example, the Threshold Conditions (COND), the Principles for Businesses (PRIN), ~~and~~ Senior Management Arrangements, Systems and Controls (SYSC) and the Integrated Prudential Sourcebook (PRU). Other notification requirements are set out in chapter 15 of the Supervision Manual (SUP).

...

X.4.3 G ~~This sourcebook applies to societies on an interim basis pending the preparation and implementation of a single Prudential Sourcebook applying to all firms regulated by the FSA—termed the Integrated Prudential Sourcebook. In developing the interim sourcebook, the FSA has drawn on the standards which formerly applied to societies authorised under the 1986 Act set out in the Statement of Principles and Prudential Notes issued by the Commission. These standards took the form of the Commission's interpretation of the criteria of prudent management in section 45 of the 1986 Act. The FSA has expressed some of the criteria of prudent management as rules in this Interim Prudential Sourcebook, but the majority of the previous material has now been recast as guidance under the Act. A significant amount of material previously published by the Commission has not been carried forward into the Interim Prudential Sourcebook, particularly descriptive, historical and explanatory material. This has been removed because the FSA considers that it is not appropriate material for prudential rules and guidance under the Act, not because the material is in~~



~~any way incorrect or irrelevant to societies' business.~~ The rules and evidential provisions are distributed throughout the prudential chapters of this sourcebook: rules can be found in paragraphs X.2.1, X.8.2, 1.2.1, 1.2.2, 4.2.1, 4.2.5, 4.2.6, ~~5.2.1, 5.2.7, 5.2.9,~~ 6.2.1, 6.2.2, 6.2.3, 7.6.2, 7.6.3, 7.7.1, 7.7.3, 8.2.1, 9.2.1, 9.2.7 and 9.2.8. Evidential provisions can be found in paragraphs 5.2.4, 9.2.3 and 9.2.5.

...

## 4 FINANCIAL RISK MANAGEMENT

...

- 4.2.3 G Societies should have credit limits in place for all counterparties both for placing liquidity and for transacting derivative contracts (further guidance is also in Chapter 5 (Liquidity) and in PRU 5.1 – stress testing and scenario analysis, and contingency funding plans).

...

### Stress Testing

- 4.7.7 G ... Boards and management should, periodically, review the extent of such stress testing to ensure that any "worst case" scenarios remain valid. Contingency plans should be in place to deal with the consequences should such scenarios become reality. Rules and guidance on stress testing, scenario analysis and contingency funding plans specifically for liquidity risk are in PRU 1.2 and PRU 5.1.

...

## 5 Liquidity

### 5.1 Introduction

- 5.1.1 G This chapter now sets out the FSA's quantitative regime for building societies' prudential liquidity, and further guidance specific to building societies on the management of their liquidity in accordance with the five approaches to financial risk management set out in chapter 4. This chapter complements PRU 5.1 (which contains rules and guidance for a wider range of firms on systems and controls appropriate for liquidity risk). Only certain provisions of PRU 5.1 apply to building societies, by virtue of PRU 5.1.3R and PRU 5.1.4R. Similarly it also complements PRU 1.2 (which sets out the high level requirements for liquidity that apply to deposit takers and own account dealers, as well as insurers). This chapter replaces PN 1998/5 issued by the Commission and contains rules and guidance for societies on the management of liquidity. It contains guidance for societies on what is meant by "adequate resources" in the Threshold Condition set out in paragraph

~~4(1) of Schedule 6 to the Act—see also COND 2.4—and in Principle 4, in respect of liquidity. The chapter explains outlines the FSA’s approach to liquidity for building societies and provides guidance on factors the FSA will take into account in assessing whether a society meets the rules set out in section 5.2 and PRU 1.2 and the guidance in PRU 5.1. A list of types of asset suitable for inclusion in prudential liquidity for societies on each of the approaches to financial risk management is set out in Annex 5A. "Prudential liquidity" has the meaning set out in paragraph 5.3.4G.~~

5.1.2 G Some material on liquidity systems and controls, previously in this chapter and superseded by PRU 5.1, has been deleted, but the original numbering has been retained: where an entire section has been deleted this is noted alongside the original section number. The new material in PRU 5.1 covers requirements for stress testing and scenario analysis, as well as contingency funding plans and their documentation.

5.2 Rules

~~5.2.1 R A society must maintain adequate liquid resources, including prudential liquidity, appropriate to the scale and nature of its business to enable it to meet its obligations as they fall due. [Deleted]~~

~~5.2.2 G “Adequate liquid resources” means of such amount and composition as will at all times enable the society to meet its obligations as they fall due. [Deleted]~~

~~5.2.3 G “Prudential liquidity” has the meaning set out in paragraph 5.3.4. A list of assets suitable for inclusion in prudential liquidity is set out in Annex 5A. [Deleted]~~

~~5.2.4 E (1) ...~~  
~~(2) Contravention of 5.2.4(1) may be relied upon as tending to establish contravention of 5.2.4 PRU 1.2.22R.~~

...

~~5.2.7 R A society must maintain, and submit to the FSA, a board-approved policy statement on liquidity.~~

5.2.8 G Guidance on the content of a liquidity policy statement is set out in paragraphs 5.6.2G to 5.6.4G and in Annex 5B. Societies will also find guidance on the requirements (set out at PRU 1.2.26R, PRU 1.2.27R, PRU 1.2.31R, PRU 1.2.33R, PRU 1.2.35R, PRU 1.2.37R and PRU 1.2.38R) for stress testing and scenario analysis at PRU 5.1.58R to PRU 5.1.62R. Further guidance on the requirements (set out at PRU 1.2.22R, PRU 1.2.35R and PRU 1.2.37R) on contingency funding plans and documentation is provided at PRU 5.1.85G – PRU 5.1.91G). Societies may, for convenience, wish to combine their documentation meeting these requirements with their liquidity policy statement, but need to be clear how any combined document meets

the separate requirements.

5.2.9 R ~~A society making any significant change to its policy statement on liquidity must provide the FSA with a copy of the amended policy statement as soon as possible after it has been adopted. [deleted]~~

...

5.6.2 G Rule 5.2.7 requires each society to have a liquidity policy statement. This should be approved by the society's board and be consistent with the society's strategic plan and its financial risk management policy statement. Societies should also have regard to the rules and guidance in PRU 1.2 and PRU 5.1, set out in more detail at PRU 5.2.8G.

...

5.6.5 G Boards should establish the objectives for liquidity including meeting obligations as they fall due (including any unexpected adverse cash flow), smoothing out the effect of maturity mismatches and the maintenance of public confidence. The need to earn a return may also be recognised as an objective, although this should be secondary to the security of the assets. Societies should also have regard to the rules and guidance in PRU 1.2 and PRU 5.1, set out in more detail at PRU 5.2.8G.

## Annex F

### Amendments to the Interim Prudential sourcebook for Friendly Societies

In this Annex underlining indicates new text and striking through indicates deleted text. Where an entirely new section of text is added, this is indicated and the new text is not underlined. Where an entire section of text is being deleted, the place where the change is made is indicated and the text is not struck through.

#### INTERIM PRUDENTIAL SOURCEBOOK FOR FRIENDLY SOCIETIES

#### GUIDANCE

#### THE PURPOSE OF THE PRUDENTIAL RULES FOR FRIENDLY SOCIETIES AND AN OVERALL DESCRIPTION

...

5. ~~The Interim Prudential Sourcebook for Friendly Societies (IPRU(FSOC)) starts by limiting the risks to which a friendly society may be subject. Rule 1.3 in Chapter 1 requires that the business of a directive friendly society is restricted to insurance business.~~ [deleted]

...

10. Provisions in Chapter 4 also require a liability in any particular currency to be matched by assets in that currency. Further provisions relate to the location of assets. [deleted]

...

15. FSA guidance is set out in the Annexes and friendly societies may also wish to refer to the guidance in IPRU(INS) and PRU.

...

# INTERIM PRUDENTIAL SOURCEBOOK

## FOR FRIENDLY SOCIETIES

### CONTENTS

Chapter 1	Application
Chapter 2	Integrity, skill, care and diligence
Chapter 3	Management and control
Chapter 4	Financial prudence
	1. Margins of solvency
	2. Adequacy of assets
	3. <del>Adequacy of premiums</del> [deleted]
	4. <del>Currency matching and localisation</del> [deleted]
	5. Separation between long-term insurance business assets and other assets
	6. Linked long-term contracts
	7. Liquidity
Chapter 5	Prudential reporting
Chapter 6	<del>Statistical information relating to EEA branches and services operations</del> [deleted]
Chapter 7	Definitions
	Part I Definitions
	Part II General Provisions
	Part III Classes of long-term insurance business
	Classes of general insurance business
Chapter 8	Transitional provisions
...	
<b>List of Annexes</b>	
...	
Annex 7	Guidance on the use of derivative contracts by <del>directive</del> friendly societies
Annex 8	<del>Guidance on the balance sheet (Forms 9 to 17)</del> [deleted]

## Chapter 1

### APPLICATION

---

#### Application

- 1.1 These rules apply to a *non-directive friendly society* which has permission under the *Act* to *effect* or *carry out contracts of insurance*.
- 1.1A The rules in Chapters 1, 2, 3 (with the exception of rule 3.1(7)), rules 4.20 to 4.23, rule 5.1A, Chapters 7, 8 and Appendix 3 also apply to a *directive friendly society* which has permission under the *Act* to *effect* or *carry out* contracts of insurance.

...

#### Restriction of business to insurance

- 1.3 (1) ~~A *directive friendly society* must not carry on any commercial business in the United Kingdom or elsewhere other than *insurance business* and activities directly arising from that business.~~
- (2) (1) does not prevent a *friendly society* which was on 15 March 1979 carrying on *long term insurance business* and a *savings business* in the United Kingdom from continuing to carry on the *savings business*. ~~[deleted]~~

...

## Chapter 3

### MANAGEMENT AND CONTROL

---

#### Accounting records and systems of control

- 3.1 ...
- (7) Every *non-directive friendly society* must within the period of 6 months beginning with the end of each *financial year* make and send to the *FSA* a statement of their opinion whether the requirements of this rule have been complied with in respect of that year by the *friendly society* and the statement must be signed by the chairman on behalf of the *committee* and by the chief executive.

...

## Chapter 4

### FINANCIAL PRUDENCE

---

#### I. MARGINS OF SOLVENCY

##### Basic requirement<sup>1</sup>

- 4.1 (1) Subject to (3), a *friendly society* (other than a *flat rate benefits business friendly society*) must maintain a ~~margin of solvency~~ margin of solvency equal to or greater than the required margin of solvency calculated in accordance with rules 4.2 to 4.10.

...

##### Calculating the required margin of solvency

- 4.2 (1) Subject to (2) to (7), the required margin of solvency must be determined -

...

- (2) For a *contract of insurance* to which rule 7.6(a) applies, the required margin of solvency must be determined by taking the aggregate of the results arrived at by applying-

...

- (3) Where a *friendly society* carries on *long-term insurance business* and owing to the nature of that business more than one required margin of solvency is produced in respect of that business by the operation of these rules, the margins in question must be aggregated.

- (4) Where a *friendly society* carries on both *long-term insurance business* and *general insurance business* and is accordingly required to maintain separate margins of solvency in respect of the two kinds of business-

- (a) the provisions in (1) to (3) apply for determining the required margin of solvency for each kind of business separately; and

...

- (5) Subject to (6), in each case in which (1)(b) applies, if the required margin of solvency under (1)(b) is lower than the required margin of solvency of the preceding *financial year*, then the required margin of solvency must be adjusted so it is at least equal to the required margin of solvency of the preceding *financial year* multiplied by the ratio of the amount of the *technical provisions* for *claims* outstanding at the end of the preceding *financial year* and the amount of the *technical provisions* for *claims* outstanding at the beginning of the preceding *financial year*.

---

<sup>1</sup> The requirement for a plan for the restoration of a sound financial position to be submitted by a *friendly society* which breaches this rule is in SUP, App II, 1.3.1.

(6) ...

#### **The guarantee fund<sup>4</sup>**

4.3 ~~A directive friendly society and a A non-directive incorporated friendly society~~ must ensure that its ~~required margin of solvency~~ margin of solvency does not fall below the *guarantee fund*.

#### **Calculating the guarantee fund**

4.4 (1) Subject to (2) to (5), one-third of the *required margin of solvency* constitutes the *guarantee fund*. ~~A friendly society must ensure that its margin of solvency does not fall below the guarantee fund.~~

(2) In the case of a *friendly society* which is a non-directive incorporated friendly society-

(a) ~~an incorporated friendly society;~~ or

(b) ~~an (unincorporated) friendly society, which is a directive friendly society;~~

the *guarantee fund* must not be less than an amount (the minimum *guarantee fund*) arrived at in accordance with rule 4.5 for *long-term insurance business* and rule 4.6 for *general insurance business*, whether the *required margin of solvency* is greater or less than that amount.

...

#### **Minimum guarantee fund: long-term insurance business**

4.5 (1) ~~Subject to (2) to (4) and to rule 4.6(3), the minimum guarantee fund for long-term insurance business carried on by a directive friendly society is 2,250,000 Euro. [deleted]~~

...

#### **Minimum guarantee fund: general insurance business**

4.6 (1) ~~Subject to (2) and (3), the minimum guarantee fund in respect of general insurance business carried on by a directive friendly society is 1,500,000 Euro. [deleted]~~

...

(3) ~~Subject to (4) and (5), the base amount in Euro specified in (1) and in Appendix 2 will increase each year, starting on the first review date of 20 September 2003 (and annually after that), by the percentage change in the~~

---

<sup>4</sup> The requirement for a short term plan to be submitted by a *friendly society* which breaches this rule is imposed by SUP, App 2



European index of consumer prices (comprising all EU member states as published by Eurostat) from 20 March 2002 to the relevant review date, rounded up to a multiple of 100,000 Euro. [deleted]

- (4) In any year, if the percentage change since the last increase is less than 5%, then there will be no increase. [deleted]
- (5) The increase will take effect 30 days after the EU Commission has informed the European Parliament and Council of its review and the relevant percentage change. [deleted]

...

## II. ADEQUACY OF ASSETS

4.11 Except for rule 4.24, which applies to all *friendly societies*, the remaining rules in this chapter do not apply to ~~non-directive~~ registered friendly societies.

4.12 (1) ...

- (b) without prejudice to the generality of (a), that its investments are appropriately diversified and adequately spread and that excessive reliance is not placed on investments of any particular category or description<sup>6</sup>.

...

The rules 4.13 to 4.19 are deleted in their entirety. The deleted text is not shown struck through.

## III ADEQUACY OF PREMIUMS

4.13 [deleted]

## IV CURRENCY MATCHING AND LOCALISATION

### ~~Matching: general requirement~~

4.14 [deleted]

### ~~Matching: property linked benefits~~

4.15 [deleted]

### ~~Matching: currency of general insurance business liabilities~~

4.16 [deleted]

### ~~Matching: exceptions for certain liabilities~~

---

<sup>6</sup> See Guidance Note P.1 of IPRU (INS).

4.17 [deleted]

### Localisation

4.18 [deleted]

### ~~Exclusions from rules 4.14 to 4.18~~

4.19 [deleted]

...

## Chapter 5

### PRUDENTIAL REPORTING

---

#### Annual actuarial investigation

5.1 (1) A *friendly society* which is

(a) ~~is a *directive friendly society*; or~~

(b) a *non-directive incorporated friendly society* (other than a *flat rate benefits business friendly society*),

must cause an investigation to be made, in accordance with the methods and assumptions determined by the *friendly society*, by the person or persons who for the time being are appointed to perform the *actuarial function* under the rules in SUP ~~appointed actuary~~ into the financial condition of the *friendly society* in respect of its *long-term insurance business* as at the end of each *financial year*.

(2) When such an investigation has been made, or when at any other time an investigation into the financial condition of the *friendly society* in respect of its *long-term insurance business* has been made with a view to the distribution of profits, or the results of which are made public the *friendly society* must-

(a) cause an abstract of the ~~actuary's~~ report of the investigation to be made; and

(b) deposit three copies of that abstract with the *FSA* within 6 months of the end of the *financial year* to which it relates,

and one of those copies must be signed as required by rule 5.12.<sup>8</sup>

...

---

<sup>8</sup> See Sup 16.3.6 to 16.3.10R for rules on submission of periodic reports

5.1A A directive friendly society must comply with rules 9.1 to 9.36, 9.37, and 9.39 of IPRU (INS) as if references to an insurer in those rules included a directive friendly society.

### **Triennial actuarial investigation**

5.2 (1) Subject to (1A) and at least once in every period of 3 years, a friendly society (other than a flat rate benefits business friendly society) which-

(a) ...

(b) is a ~~directive friendly society or a non-directive incorporated friendly society~~ must cause an investigation to be made by the *appropriate actuary* into the financial condition of the *friendly society* in respect of its *general insurance business*.

(1A) (1)(a) does not apply to a partnership pension society.

...

(9) ~~A directive friendly society or non-directive incorporated friendly society~~ (other than a *flat rate benefits business friendly society*) which is carrying on *general insurance business* must complete an abstract in the Form required under rules 5.14 to 5.19 (referred to as the “FSC3 return”).

...

### **The FSC1 return**

...

5.5 (1) The FSC1 return must include:

(a) Form FSC1

(b) a balance sheet;

(c) revenue accounts;

(d) a valuation abstract;

(e) a certificate and a statement that the friendly society consents to the FSC1 return being placed on its public file by the appointed actuary; and

(f) a report of the auditors.

~~(g) a statement that the friendly society consents to the FSC1 return being placed on its public file.~~

(2) Rules 5.6 to 5.12 apply to the preparation of the FSC1 return.

### **Balance sheet**

5.6 ...

~~(1A) Form 9A must be completed by every directive friendly society in respect of its long-term insurance business assets.~~

...

### **Actuary's Certificate**

- 5.10 ~~The appointed actuary must give a~~ A friendly society must ensure that a certificate is given in the terms, as appropriate, of Form 61B.

### **Auditor's Report**

- 5.11 (1) The auditor's report in Form 61C must state whether in his opinion the balance sheet, ~~and revenue accounts, valuation abstract and certificate~~ (Forms 9 to 45, 48, 49, 56, 58 and 60, including any supplementary notes) and information relating thereto have been properly prepared and presented in accordance with the rules in chapters 4 & 5.

(1A) To the extent that the auditor's opinion relates to matters covered by the investigation in rule 5.1

(a) the friendly society must ensure that the auditor takes appropriate advice from a suitably qualified actuary who is independent of the friendly society;

(b) the auditor's report in Form 61C must include a statement that the auditor has taken such advice.

(2) In giving this opinion the auditor must state whether he has relied on -

(a) the certificate ~~of the actuary~~ given in accordance with rule 5.10 with respect to the *mathematical reserves* and the *required minimum margin* of the *friendly society*; and

...

### **Signatures**

- 5.12 (1) ~~The appointed actuary must sign the certificate in Form 61B.~~ [deleted]

(3) The FSC1 Return must be signed, in Form 61B ~~61D~~, by ~~the appointed actuary~~ and the chief executive, the secretary and one *committee* member of the *friendly society* (or two members of the *committee* if the offices of chief executive and secretary are held by the same person).

...

- 5.26 ~~A directive friendly society must provide to any person (or the person who has already been provided with a copy under (a)) within 30 days of the date of request (or, in the case of (b), the date of deposit under rule 5.3):~~

(a) a copy of any of the documents last deposited by the friendly society under rules 5.1 or 5.2; and

~~(b) — a copy of any document deposited under rule 5.3 which corrects or makes good any document provided under (a);~~

~~in printed form, but (in the case of (a)) the *friendly society* may make a charge to cover its reasonable costs, including those of printing and postage.~~

[deleted]

Chapter 6 (Statistical information relating to EEA branches and services operations) is deleted in its entirety; the deleted text is not shown struck through.

**Chapter 6**

[deleted]

Amend or delete the following definitions in Chapter 7 as shown (unchanged definitions are not shown):

**Chapter 7**

**DEFINITIONS**

**Part I Definitions**

7.1 In this Part of the *IPRU(FSOC)*, unless the contrary intention appears, the following definitions apply –

<del><i>Act</i> means Financial Services and Markets Act 2000;</del>
<del><i>appointed actuary</i> means an actuary appointed under SUP 4.13.1R;</del>
<del><i>appropriate actuary</i> means an actuary appointed under SUP 4.4.1R;</del>
<del><i>approved credit institution</i> means an institution recognised or permitted under the law of an <i>EEA State</i> to carry on any of the activities set out in Annex 1 to the <i>Banking Co-ordination Consolidation Directive</i>;</del>
<del><i>approved financial institution</i> means any of the following –</del>
<del>—— the European Central Bank;</del>
<del>—— the central bank of an <i>EEA State</i>;</del>
<del>—— the International Bank for Reconstruction and Development;</del>
<del>—— the European Bank for Reconstruction and Development;</del>
<del>—— the International Finance Corporation;</del>
<del>—— the International Monetary Fund;</del>
<del>—— the Inter-American Development Bank;</del>
<del>—— the African Development Bank;</del>
<del>—— the Asian Development Bank;</del>
<del>—— the Caribbean Development Bank;</del>
<del>—— the European Investment Bank;</del>
<del>—— the European Community;</del>
<del>—— the European Atomic Energy Community;</del>
<del>—— and the European Coal and Steel Community;</del>

<del><i>Banking Co-ordination Directive</i> means Council Directive 2000/12/EC of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions;</del>
<del><i>building society</i> means a building society within the meaning of the Building Societies Act 1986;</del>
<del><i>contract of insurance</i> includes:</del>
<del>(a) fidelity bonds, performance bonds, administration bonds, bail bonds, customs bonds, or similar contracts of guarantee, effected in return for the payment of one or more premiums;</del>
<del>(b) tontines;</del>
<del>(c) when effected or carried out by a body that carries on the business of effecting or carrying out <i>contracts of insurance</i> apart from this paragraph, capital redemption contracts and <i>pension fund management contracts</i>;</del>
<del>(d) contracts to pay <i>annuities on human life</i>;</del>
<del>(e) contracts of a kind referred to in article 1(2)(e) of the <i>first life Directive</i>; and</del>
<del>(f) contracts of a kind referred to in article 1(3) of the <i>first life Directive</i>;</del>
<del><i>directive friendly society</i> means a <i>friendly society</i> other than a <i>non-directive friendly society</i>;</del>
<del><i>designated state or territory</i> means any <i>EEA State</i> (other than the United Kingdom), Switzerland, a state in the United States of America, the District of Columbia, Puerto Rico, Canada or a province of Canada, Australia, South Africa, Singapore and Hong Kong;</del>
<del><i>EEA State</i> means a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992</del>
<del><i>first non-life Directive</i> means Council Directive 73/239/EEC of 24 July 1973 on the co-ordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct insurance other than life assurance;</del>
<del><i>first life Directive</i> means Council Directive 79/267/EEC of 5 March 1979 on the co-ordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct life assurance;</del>
<del><i>flat rate benefits business friendly society</i> means a <i>friendly society</i> whose <i>insurance business</i> is restricted to the provision of benefits which vary according to the resources available and in which the contributions of members are determined on a flat rate basis;</del>
<del><i>friendly society</i> means an <i>incorporated friendly society</i> or a <i>registered friendly society</i>;</del>

<i>FSA</i> means the Financial Services Authority;
<del><i>incorporated friendly society</i> means a <i>friendly society</i> incorporated under the 1992 Act;</del>
<del><i>index linked benefits</i> means benefits—</del>  (a) — provided for under a <i>linked long term contract</i> ; and  (b) — determined by reference to fluctuations in, or an index of, the value of property of any description (whether or not specified in the contract);
<del><i>industrial and provident society</i> means any society registered (or deemed to be registered) under the Industrial and Provident Societies Act 1965 or the Industrial and Provident Societies Act (Northern Ireland) 1969;</del>
<del><i>insurance business</i> means the business of effecting or carrying out <i>contracts of insurance</i> as principal;</del>
<del><i>insurance Directives</i> means –</del>  (a) the <i>first non-life Directive</i> , the <i>second non-life Directive</i> and the <i>third non-life Directive</i> , and such other Directives as make provision with respect to the business of direct insurance other than long-term assurance; and  (b) the <u><i>Consolidated Life Directive</i></u> — <del><i>first life Directive</i>, the <i>second life Directive</i> and the <i>third life Directive</i></del> , and such other Directives as make provision with respect to the business of direct long-term assurance;
<del><i>insurance undertaking</i> has the meaning given in <i>IPRU(INS)</i>;</del>
<del><i>Insurer</i> has the meaning given in <i>IPRU(INS)</i>;</del>
<del><i>IPRU(FSOC)</i> means the Interim Prudential Sourcebook for Friendly Societies;</del>
<del><i>IPRU(INS)</i> means the Interim Prudential Sourcebook for Insurers;</del>
<del><i>life Directives</i> means the <i>first life insurance Directive</i>, the <i>second life Directive</i>, and the <i>third life Directive</i>; <u>Directive 2002/83/EC of 5 November 2002 concerning life assurance</u></del>



*non-directive friendly society* means:

- (1) — a *friendly society* whose *insurance business* is restricted to the provision of benefits which vary according to the resources available and in which the contributions of the members are determined on a flat-rate basis;
- (2) — a *friendly society* whose *long-term insurance business* is restricted to the provision of benefits for employed and self-employed persons belonging to an undertaking or group of undertakings, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the *commitments* arising from such operations are fully covered at all times by *mathematical reserves*);
- (3) — a *friendly society* which undertakes to provide benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind;
- (4) — a *friendly society* (carrying on *long-term insurance business*) —
  - (a) — whose articles of association contain provisions for calling up additional contributions from members or reducing their benefits or claiming assistance from other persons who have undertaken to provide it; and
  - (b) — whose annual *gross premium* income (other than from contracts of reinsurance) has not exceeded 5 million Euro for each of the three preceding *financial years*;
- (5) — a *friendly society* (carrying on *general insurance business*) whose —
  - (a) — registered rules contain provisions for calling up additional contributions from members or reducing their benefits;
  - (b) — *gross premium* income (other than from contracts of reinsurance) for the preceding *financial year* did not exceed 5 million Euro; and
  - (c) — members provided at least half of that *gross premium* income;
- (6) — a *friendly society* whose liabilities in respect of *general insurance contracts* are fully reinsured with or guaranteed by other mutuals (including *friendly societies*);

and whose *insurance business* is limited to that described in paragraphs (1) to (6);

*non-directive incorporated friendly society* means a *non-directive friendly society* which is an *incorporated friendly society*;

*non-directive registered friendly society* means a *non-directive friendly society* which is a *registered friendly society*;

*non-life Directives* means the *first non-life Directive*, the *second non-life Directive*, and the *third non-life Directive*;

*notional required minimum margin* means:

- (a) in the case of an *insurance undertaking* (other than a *pure reinsurer*) that has its head office in a *designated state or territory*, the amount of the *required minimum margin* or *general insurance capital requirement* or the equivalent requirement under the regulatory requirements of that state or territory;
- (b) in the case of a *pure reinsurer* that has its head office in a *designated state or territory*, the amount that would be the *required minimum margin* or *general insurance capital requirement*, or the equivalent requirement under the regulatory requirements of that state or territory, if the regulatory requirements of that state or territory applicable to undertakings carrying on *direct insurance business* were applied to the *pure reinsurer* (whether they are or not); and
- (c) in all other cases, the amount of the *required minimum margin* or *general insurance capital requirement* that would apply if the *insurance undertaking* were an *insurer* (other than a *pure reinsurer*), with its head office in the United Kingdom (whether it is or not)

*participation* means:

- (a) the holding of a participating interest within the meaning of section 421(2)411(2) of the *Act*; or
- (b) the holding, directly or indirectly, of 20% or more of the voting rights or capital;

*partnership pension society* means an unincorporated *friendly society*, which satisfies the following conditions –

- (a) the purpose of the society is to effect or carry out unit-linked contracts to pay annuities on human life, which are approved by the Commissioners of the Inland Revenue under Section 620 of the Income and Corporation Taxes Act 1988;
- (b) the assets of each member of the society are separately identifiable;
- (c) the assets of each member of the society are invested solely or primarily by him or in accordance with his instructions;
- (d) the value of each member of the society's assets is dependent entirely on the performance of those assets;
- (e) no member of the society has a contract which comprises, or includes, a cash guarantee; and
- (f) no member of the society has a contract which is an annuity in payment.

*permitted derivative contract*

(1) for a *directive friendly society*, means a *derivative or quasi derivative* which satisfies the requirements of *PRU 4.3*, with the exception of *PRU 4.3.18R*, as applied in relation to assets covering liabilities in respect of *linked long term contracts*, amended as follows:

- (a) in *PRU 4.3.5R* and *PRU 4.3.36R*, "For the purpose of *PRU 2 Ann 1R (Admissible assets in insurance)*" is replaced by "For the purposes of *IPRU (FSOC) rule 4.21* and Appendix 3";
- (b) in *PRU 4.3.6R (2)* and (3), *PRU 4.3.7R (1)* and (2), *PRU 4.3.17R (1)* and *PRU 4.3.36R (1)* "*admissible assets*" is replaced by "*permitted connected property*";
- (c) *PRU 4.3.12R (2)* and (3) are replaced by:

“(2) (where they are held to cover *index-linked liabilities*) might:

- (a) not be appropriate cover for those liabilities as required by *PRU 4.2.58R*; or
- (b) fall in value; and

(3) (where they are held to cover *property-linked liabilities*) might:

- (a) not be appropriately selected in accordance with contractual and constructive liabilities as required by *PRU 7.6.36R* and appropriate cover for those liabilities as required by *PRU 4.2.57R*; or
- (b) fall in value”.

(2) for a *non-directive incorporated friendly society*, means a *derivative contract* which:

- (a) is covered and –
  - (i) is held in connection with property of the type described in rule 4.22 for the purpose of reduction of investment risk or efficient portfolio management, or
  - (ii) has the effect of a *permitted derivative contract* held in connection with such property for such purpose; and
- (b) satisfies the conditions in 13(6) to 13(8) of Appendix 4 except that the references in 13 of Appendix 4 to "an asset for the valuation of which provision is made in this chapter" is construed as reference to *permitted connected property*;

*policyholder* has the meaning given in *IPRU(INS)*;

<del><i>pure reinsurer</i> has the meaning given in <i>IPRU(INS)</i>;</del>
<del><i>registered friendly society</i> means a <i>friendly society</i> registered within the meaning of the <i>1974 Act</i> by virtue of section 7(1)(a) of that Act or any <i>enactment</i> which it replaced, and includes any <i>registered branches</i> of the <i>friendly society</i>;</del>
<del><i>required margin of solvency</i> has the meaning given in rule 4.1.4.2</del>
<del><i>Second non-life Directive</i> means Council Directive 88/357/EEC of 22 June 1988 on the co-ordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance and laying down provisions to facilitate the effective exercise of freedom to provide services and amending Directive 73/239/EEC;</del>
<del><i>Second life Directive</i> means Council Directive 90/619/EEC of 8 November 1990 on the co-ordination of laws, regulations and administrative provisions relating to direct life assurance, laying down provisions to facilitate the effective exercise of freedom to provide services and amending Directive 79/267/EEC;</del>
<del><i>SUP</i> means the Supervision Manual;</del>
<del><i>third non-life Directive</i> means Council Directive 92/49/EEC of 18 June 1992 on the co-ordination of laws, regulations and administrative provisions relating to direct insurance other than life assurance and amending Directives 73/239/EEC and 88/357/EEC;</del>
<del><i>third life Directive</i> means Council Directive 92/96/EEC of 10 November 1992 on the co-ordination of laws, regulations and administrative provisions relating to direct life assurance and amending Directives 79/267/EEC and 90/619/EEC;</del>
<del><i>UCITS Directive</i> means Council Directive 85/611/EEC of 20 December 1985 on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investments in transferable securities;</del>
<del><i>UK insurer</i> has the meaning given in <i>IPRU(INS)</i>;</del>

...

## Chapter 8

### TRANSITIONAL PROVISIONS

Guidance:

...

Table 1

<b>(1)</b>	<b>(2)</b> <b><u>Material to which the transitional provision applies</u></b>	<b>(3)</b>	<b>(4)</b> <b><u>Transitional provision</u></b>	<b>(5)</b> <b><u>Transitional Provision: Dates in force</u></b>	<b>(6)</b> <b><u>Handbook provision: coming into force</u></b>
1	<u>IPRU(FSOC) 4.12, 4.20, 4.21, 4.22, 4.23, Appendix 4 paragraph 15</u>	<u>R</u>	<u>For the period given in column 5, a <i>non-directive incorporated friendly society</i> need not comply with a <i>rule</i> listed in column 2</u>	<u>From 31 December 2004 to 30 December 2005</u>	<u>31 December 2004</u>
2	<u>Rules in IPRU(FSOC)</u>	<u>G</u>	<u>Further transitional provisions concerning <i>waivers</i> and written concessions are contained in <i>PRU</i></u>	<u>See <i>PRU</i></u>	<u>See <i>PRU</i></u>
3	<u>IPRU(FSOC) Rule 5.1A</u>	<u>R</u>	<u>(1) This paragraph and Table 2 below apply to a <i>directive friendly society</i>. (2) <i>IPRU (FSOC) rule 5.1A</i> is modified so that a <i>directive friendly society</i> must comply with <i>IPRU(INS) rule 9.6(1)</i> varied as set out in Table 2.</u>	<u>From 31 December 2004 to 30 December 2007</u>	<u>31 December 2004</u>
4	<u>IPRU(FSOC) rules 4.21, 4.22, 7.1 (Definitions), Appendix 3 paragraphs 9 and</u>	<u>R</u>	<u>For the period given in column (5), for the purposes of the</u>	<u>31 December 2004 to 30 December</u>	<u>31 December 2004</u>

	<u>12</u>		<u>rules specified in column (2), a directive friendly society must apply the definition of permitted derivative contract as it takes effect in relation to a non-directive incorporated friendly society.</u>	<u>2005</u>	
<u>5</u>	<u>IPRU(FSOC) rules 4.21, 4.22, 7.1 (Definitions), Appendix 3 paragraphs 9 and 12</u>	<u>R</u>	<p><u>(1) This paragraph applies to a contract concluded on or before 30 December 2005 which satisfies the definition of permitted derivative contract as it takes effect in relation to a non-directive incorporated friendly society.</u></p> <p><u>(2) In relation to a contract to which this paragraph applies, for the purposes of the rules specified in column (2), a directive friendly society may continue to apply the definition of permitted derivative contract as it takes effect in relation to a non-directive incorporated friendly society.</u></p>	<u>31 December 2004 until the relevant rule is revoked</u>	<u>31 December 2004</u>

Table 2

This Table belongs to IPRU(FSOC) Chapter 8, Table 1, paragraph 3

	<u>Deposit period following the <i>financial year end</i></u>	
<u><i>Financial year ending on or after</i></u>	<u>Where the deposit is made electronically</u>	<u>Otherwise</u>
<u>31 December 2004</u>	<u>6 months</u>	<u>6 months</u>
<u>31 December 2005</u>	<u>6 months</u>	<u>6 months</u>
<u>31 December 2006</u>	<u>4 months</u>	<u>3 months and 15 days</u>
<u>31 December 2007</u>	<u>3 months</u>	<u>2 months and 15 days</u>

## Appendix 1

### LONG-TERM INSURANCE BUSINESS MARGIN OF SOLVENCY

#### Long-term classes I and II

1. (1) For *long-term insurance business* of class I or II the required margin of solvency~~margin of solvency~~ must be determined by taking the aggregate of the results arrived at by applying the calculation described in (2) ("the first calculation") and the calculation described in (3), (4) and (5) ("the second calculation").

...

## Appendix 4

### ASSET VALUATION RULES

...

#### Assets to be taken into account only to a specified extent

15. (1) Subject to (2) to (6), the aggregate value of the assets of a *non-directive incorporated*~~directive-friendly~~ *society* as determined in accordance with the *asset valuation rules* must, for any of the purposes for which the *asset valuation rules* apply, be reduced by an amount representing the aggregate of:
  - (a) the amount by which the ~~friendly~~ *society* is exposed to assets of any description in excess of the *permitted asset exposure limit* for assets of that description;
  - (b) the amount by which the ~~friendly~~ *society* is exposed to a *counterparty* in excess of the *permitted counterparty exposure limit* for such *counterparty*;
  - (c) the amount by which the ~~friendly~~ *society* has an *excess concentration with a number of counterparties*;
  - (d) the value of any assets transferred to or for the benefit of the ~~friendly~~ *society* in pursuance of a condition in a *derivative contract* to which 13 does not apply or a related contract; and
  - (e) the value of any assets transferred to or for the benefit of the ~~friendly~~ *society* in pursuance of a contract whose effect is that of a *derivative contract* to which 13 does not apply or a related contract,as determined in accordance with Annex B.



- (2) Where a *non-directive incorporated friendly society* is exposed to assets of any description in excess of the *permitted asset exposure limit* for such assets, the reduction required to be made by (1)(a) must be made-
- (a) by deducting (as far as possible) the amount of the excess from the assets of that description held by the *friendly society* society; and
  - (b) where the *friendly society* society does not hold sufficient assets of that description to eliminate the excess (or does not hold any assets of that description) by making an appropriate deduction from the aggregate value of the assets which the *friendly society* society would otherwise be permitted to take into account for any of the purposes for which the *asset valuation rules* apply.
- (3) Where a *friendly society* society is required to make a reduction in accordance with (1) (b), (c), (d) or (e), the reduction must be made by making a deduction from the aggregate value of the assets which the *friendly society* society would otherwise be permitted to take into account for any of the purposes for which the *asset valuation rules* apply.
- (4) Where a *non-directive incorporated friendly society* carrying on *long-term insurance business* has attributed assets partly to a *long-term insurance business* fund and partly to its other assets, any reduction required to be made by this rule must be made in the same proportion as the attribution.

...

## Appendix 10

### Prudential Reporting Forms

Contents	Page	Contents	Page
FSC1 Return	157	FSC1 Form 60 (Sheet 1)	196
FSC1 Contents (Sheet 1)	158	FSC1 Form 60 (Sheet 2)	197
FSC1 Contents (Sheet 2)	159	FSC1 Form 61A	198
FSC1 Form 9	160	FSC1 Form 61B	199
FSC1 Notes to Form 9	161	FSC1 Form 61C	200
<del>FSC1 Form 9A</del>	<del>162</del>	<del>FSC1 Form 61D</del>	<del>201</del>
<del>FSC1 Notes to Form 9A</del>	<del>163</del>	FSC2 Return	202
FSC1 Form 13 (Sheet 1)	165	FSC2 Form 9	203
FSC1 Form 13 (Sheet 2)	166	FSC2 Form 9A	204
FSC1 Form 13 (Sheet 3)	167	FSC2 Form 9B	205
FSC1 Notes to Form 13	168	FSC2 Form 9C	206
FSC1 Form 14 (Sheet 1)	169	FSC3 Return	207
FSC1 Form 14 (Sheet 2)	170	FSC3 Contents	208

...

**Prudential Reporting Forms**

FSC1 Return

Long Term Insurance Business: Annual Investigation

FORM FSC 1

Register Number

Year ended 31 December

Name of  
Society  
(as registered)

Registered  
Office

Post Code:

The information provided in this FSC1 Return (Long Term Insurance Business: Annual Investigation), ~~and the Actuary's certificate and Auditor's report included herein are the form and contents of an abstract under rule 5.1(2) for use by a *directive friendly society or a non-directive incorporated friendly society* (other than a *flat rate benefits business friendly society*) in respect of its *long-term insurance business*.~~

One copy of the Return must be signed by ~~the appointed actuary~~, the chief executive, the secretary and one *committee* member of the society (or two members of the *committee* if the offices of chief executive and secretary are held by the same person).

Three copies of this Return (including the original signed copy) must be submitted as soon as possible after 31 December and not later than the following 30 June to:-

The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

...

Form 9A and notes to Form 9A are deleted in their entirety, the text is not shown struck through.

...

## FSC 1 – FORM 14 (Sheet 2)

### Returns under the Friendly Societies Prudential Rules

Long term insurance business liabilities and margins

Name of Society

Period ended 31 December

	Reg No	Units £/£000
	<input type="text"/>	<input type="text"/>

Category of assets/Total

**1** As at the end of the year

**2** As at the end of the previous year

Excess of the value of net admissible assets (Note 8)

51



Total liabilities and margins

59



Amount included in line 59 attributable to liabilities to associated bodies, other than those under contracts of insurance or re-insurance

61



Amount included in line 59 attributable to liabilities in respect of property linked benefits

62



Amount of any additional mathematical reserves included in line 51 which have been taken into account in the ~~appointed actuary's~~ certificate in Form 61B (Note 9)

63

## FSC 1 – Notes to Form 14

- 1** The entry at lines 11 and 19b must equal the sum of lines 21, 43, 44 and 45 of the corresponding Form or Forms 58.
- 2** The entry at line 12 must equal the total of line 42 of the corresponding Form or Forms 58.
- 3** The entry at line 13 must equal the total of line 49 of the corresponding Form or Forms 58.
- 4** The entry at line 14 must equal the total of line 59 of the corresponding Form or Forms 40.
- 5** The entry at line 19a must equal the entry at line 49 on Form 40B.
- 6** The entry at lines 19b and 19c must equal the sum of the entries at line 59 on Form 40C.
- 7** The entry at line 19d must equal the entry at line 69 on Form 40A.
- 8** The entry at line 51 must be:
  - (a) the value of the admissible assets (as included in line 89 of the appropriate Form 13) representing the long term insurance business funds, fund or group of funds to which the Form relates, less
  - (b) the amount of those funds, fund or group of funds, being the sum of the amounts shown at lines 14 and 49.
- 9** The entry at line 63 must be the amount specified in paragraphs (a)(ii) of the certificate in the appointed actuary's certificate (Form 61B), but only insofar as it relates to the fund, funds or group of funds to which this Form 14 relates.

...

FSC 1 – FORM 61B

**Returns under the Friendly Societies Prudential Rules**

Long term insurance business: Annual Investigation — ~~Actuary's Certificate and Signatures~~

Name of Society

Period ended 31 December

Reg No	
<input type="text"/>	<input type="text"/>

I ~~We~~ certify that:

- (a) (i) ~~in my opinion~~, the information in this Return complies with the rules in IPRU(FSOC) and proper records have been kept by the society adequate for the purpose of the valuation of the liabilities of its long term insurance business;
- (ii) the sum of the mathematical reserves and the deposits received from reinsurers as shown in Form 14 together, if the case so requires, with £..... (being part of the excess of the value of the admissible assets representing the long term insurance business funds over the amount of those funds shown in Form 14) constitute proper provision at the end of the financial year for the long term insurance liabilities (including all liabilities arising from deposit back arrangements, but excluding liabilities which have fallen due before the end of the financial year) including any increase in those liabilities arising from a distribution of surplus as a result of any investigation as at that date into the financial condition of the long term insurance business; and
- (iii) for the purpose of sub-paragraph (ii) above the liabilities have been assessed in accordance with Appendix 5 in the context of assets valued in accordance with Appendix 4, as shown in Form 13;
- (iv) ~~in my opinion~~, premiums for contracts entered into during the financial year and income earned thereon are sufficient, on reasonable actuarial assumptions, and taking into account the other financial resources of the society that are available for the purpose, to enable the society to meet its commitments in respect of those contracts, and, in particular, to establish adequate mathematical reserves; and
- (v) ~~I have complied with the Institute of Actuaries and Faculty of Actuaries professional guidance notes listed below.~~  
In preparing this Return, we have taken and paid due regard to advice from every *actuary* appointed by the society to perform the *actuarial function* in accordance with SUP 4.3.13R
- (b) The amount of the required minimum margin of solvency applicable to the society's long term insurance business immediately following the end of the financial year (including any amounts resulting from any increase in liabilities arising from a distribution of surplus as a result of the investigation into the financial condition of the long term insurance business) is £.....
- (c) I ~~We~~ have the following additional comments (use extra pages).

Signature

*Date*

Name:

Address:

Qualification:

The following new signature box is inserted at the end of FSC1 – Form 61B:

We confirm also that the society consents to a copy of this Return being placed on the public file of the society.

**Chief Executive**

Name (Block Capitals)

**Secretary**

Name (Block Capitals)

**Member of Committee**

Name (Block Capitals)

Additional Committee member if the offices of the Chief Executive and Secretary are held by the same person.

Name (Block Capitals)

Form 61D is deleted in its entirety, the text is not shown struck through.

## FSC 1 – FORM 61D ~~[deleted]~~

...

### Annex 3

#### Part I

#### GUIDANCE ON SYSTEMS OF ACCOUNTING, CONTROL OF BUSINESS AND INSPECTION AND REPORT

1. This Part of the Annex sets out the key issues that the *FSA* considers the *committee* and the management of a *friendly society* need to address if the *friendly society's* systems are to satisfy the principle 3 of the *FSA* Principles for Business. That principle requires a *friendly society* to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems. The *FSA* expects that these issues will have been considered by a *non-directive friendly society's committee* in preparing its reports under rule 3.1.
  
- 1A. ~~A *friendly society* may also wish to have regard to Guidance Note P.3 (Systems and Controls in Insurers) in *IPRU(INS)*. Some of the issues addressed in that Guidance Note are already covered in parts of this sourcebook. Where they are not covered, *friendly societies* should look to the Guidance Note. Not all of the Guidance Note is appropriate for smaller *friendly societies*.~~ ~~[deleted]~~

...

#### Part II

#### GUIDANCE ON SYSTEMS OF CONTROL OVER INVESTMENTS

1. This Part of the Annex provides guidance on the main elements of systems of control over investments in conjunction with Part I of this Annex which provides guidance on Systems of Accounting, Control of Business and Inspection and Report. A and B of this Part of the Annex include guidance of general application to *friendly societies*. C provides guidance to ~~*directive friendly societies*~~ which make use of *derivative contracts*.

...

#### **Applicable to ~~directive~~ non-directive incorporated friendly societies**

9. Rule 4.12(1) requires the assets backing insurance liabilities (other than in respect of *linked benefits*) for a *non-directive incorporated directive friendly society* to satisfy the following conditions:

- (a) “.....of appropriate safety, yield and marketability having regard to the *classes* of business carried on”; and
- (b) “..... investments are appropriately diversified and adequately spread and that excessive reliance is not placed on investments of any particular category or description”.
10. Rule 4.12(2) applies to the *linked long-term contracts* of a ~~directive society~~ *non-directive incorporated friendly society* for which liabilities are covered by the value of assets in an internal fund, or units in a collective investment in transferable *securities*, or by reference to a share index, or by assets of appropriate safety, yield and marketability which correspond, as nearly as may be, to the assets on which the reference value is based.
11. Rule 4.12(3) also applies in respect of the *linked long-term contracts* of a ~~directive society~~ *non-directive incorporated friendly society* and requires the society to secure that its liabilities under the contract in respect of *linked benefits* are covered by assets of a description specified in Appendix 3.
12. 15 of, and Annex B to, Appendix 4 **specify** the reductions that should be applied to the aggregate value of a ~~directive society~~ *non-directive incorporated friendly society*'s assets for the purposes of the determination of the society's *required margin of solvency* taking account, amongst other matters, of *permitted asset* and *counterparty exposure limits* and *excess concentration with a number of counterparties* (see 20 to 22).
13. ~~Rules 4.14 to 4.19, which apply to directive societies, set out the requirements for matching and localisation of assets. [deleted]~~

...

## **B – Systems of control**

### **Importance of adequate controls**

...

16. Additional considerations for ~~directive~~ *friendly societies* which make use of *derivative contracts* are included in C (see 31 and 32).

### **Investment policy - general**

17. It is important that the *committee* gives consideration to documenting the investment policy and takes the necessary steps to ensure that the current investment policy is being applied, and that there are systems of control which would result in the *committee* being consulted before any decision is made which may not be in accordance with the current policy. In establishing the policy a *committee* will need to take account of these rules, any requirements in the society's registered rules and advice from the ~~appointed or~~ appropriate actuary or from the person or persons appointed to perform the actuarial function.

...



## Investment policy of a ~~directive~~ non-directive incorporated society - exposure limits

20. The *committee* of a ~~directive~~ non-directive incorporated *friendly society* should consider whether to include limits in its investment policy on the following matters:
- (a) the society's *exposure* to particular assets, taking the provisions and limits in Annex B to Appendix 4 (see 12) into account; and
  - (b) the society's *exposure* to particular *counterparties* taking the limits in B2 of Annex B to Appendix 4 into account (see also 22).

...

## Exposure limits - additional considerations

23. The *committee* of a non-directive incorporated ~~directive~~ *friendly society*, particularly if it makes use of the powers under section 14 of the *1992 Act*, should consider whether, in addition to any policy limits arising from the *exposure* and concentration provisions in Annex B to Appendix 4 (see 20 to 22), internal policy limits for aggregate exposures to certain categories of assets should be included in the investment policy. The limits for certain categories of assets will need to take account, where applicable, of rule 4.12(1) (see 9). In addition the level of the society's free assets should be taken into account, bearing in mind the possibility that such assets might in future be needed to cover *insurance liabilities* or minimum margin of solvency.

...

## C - Additional considerations for controls over derivative contracts

31. 13 to 15 of, and Annex B to, Appendix 4 includes specific provisions with respect to *derivative contracts* and contracts or assets having the effect of *derivative contracts*. This includes provisions restricting those contracts which may be counted as assets for the purposes of determining a ~~directive~~ *friendly society's required margin of solvency*. Annex 7 refers to PRU 4.3 which discusses the valuation issues surrounding the use of derivative contracts. ~~Annex 7 refers to Guidance Note 4.2 in IPRU(INS) which discusses valuation issues surrounding the use of derivative contracts.~~ That Annex also draws attention to the need for the *committee* and management of a society which uses *derivative contracts* to have sufficient understanding of the nature and risks of the contracts it uses to ensure there are effective systems in place to monitor the use of derivatives.

...

## ANNEX 4

### GUIDANCE ON MARGINS OF SOLVENCY AND THE GUARANTEE FUND

...

- 4A. ~~Guidance Note 2.2 in IPRU(INS)~~ Guidance in PRU 2 Annex 2G (Guidance on applications for waivers relating to implicit items) ~~applies to~~ is relevant to

*friendly societies* applying for a waiver of rule 4.7(3) of *IPRU(FSOC)* under section 148 of the *Act* (Modification or waiver of rules).

- 4B. ~~Guidance Note 2.1 in *IPRU(INS)* (Hybrid capital: Admissibility for solvency) applies to *friendly societies* applying for a waiver of rules 4.7(2) or (4) of *IPRU(FSOC)* under section 148 of the *Act* (Modification or waiver of rules).[deleted]~~

...

### **Guarantee fund**

5. Rules 4.3 to 4.7 provide for the maintenance of the *guarantee fund*. The *guarantee fund* is generally one-third of the calculated *required margin of solvency*. For ~~*directive*~~ and *non-directive incorporated friendly societies*, the *guarantee fund* should be not less than the amount set out in rules 4.5 and 4.6 and this is known as the *minimum guarantee fund*.

...

- 8 There are some important modifications contained in Chapter 4 by way of relaxation of the requirements for *friendly societies* which are *non-directive registered friendly societies* in recognition of their different status or much smaller size. These modifications are:

(a) ...

(b) the requirement to have a *minimum guarantee fund* does not apply to a *non-directive friendly society* which is not incorporated (rule 4.4); and

(c) ~~the matching and localisation provisions in rules 4.14 to 4.19 apply only to *directive friendly societies* (rule 4.11); and [deleted]~~

(d) the limits placed on the extent to which certain assets may be taken into account in determining their value in the insurance fund apply only to *directive non-directive incorporated friendly societies* (15(1) of Appendix 4).

9. In addition to these modifications, the *FSA* has power under section 148 of the *Act* to direct that certain requirements do not apply to any particular *friendly society*, and there may be circumstances where the *minimum guarantee fund* may be varied in the case of certain *non-directive incorporated friendly societies*. ~~In addition, the increases to the *minimum guarantee fund* required by virtue of the Solvency I Directives (2002/12/EC and 2002/13/EC of 5 March 2002) from 1 January 2004 have not been applied to *non-directive incorporated friendly societies*.~~

10. ...

### **11.1 The requirements for the various categories are summarised below:**

#### **Life Directive Friendly Societies**

- 11.2 (1) ~~These would include any *friendly society* which carries on *long-term insurance business* where:~~

- (a) ~~its rules do not contain provision for calling up additional contributions, for reducing benefits or for claiming assistance from other persons who have undertaken to provide it; or~~
  - (b) ~~its annual contribution income from long term insurance business exceeded 5 million Euro for 3 consecutive years.~~
- (2) ~~Valuation is made annually and the rules in chapter 4 and rule 5.1 apply. [deleted]~~

### **Non-life Directive Friendly Societies**

- 11.3 (1) ~~Similarly, these would include any friendly society which carries on general insurance business where:~~
- (a) ~~its rules do not contain provision for calling up additional contributions or for reducing benefits; or~~
  - (b) ~~its annual contribution income from general insurance business in any previous year exceeded 5 million Euro.~~
- (2) ~~Valuation is made triennially and rules in chapter 4 (other than rules 4.5 — minimum guarantee fund and rule 4.12 — adequacy of premiums) and rule 5.2 apply [deleted]~~

...

### **Other non-directive Friendly Societies**

- 11.6.1.1(1) *Non-directive registered friendly societies* which have permission to carry on long-term or general insurance business are within the scope of rule 4.1 and are required to be valued triennially.

...

## **12.1 Resilience Test**

...

- 12.3 *Friendly societies* should, as a minimum, consider the scenario of a fall in the market value of equities of ~~the greater of~~ at least 10%, or, if greater, the lower of:
- (1) 25%, or such lower amount which would not produce a P/E ratio on the FTSE Actuaries All Share Index lower than 75% of the inverse of the long-term gilt yield (as defined in paragraph 10(9) of Appendix 5 of *IPRU(FSOC)*); and
  - (2) ~~40%.~~ 25% less any percentage reduction between the current FTSE Actuaries All Share Index and its average over the last 90 calendar days.

12.4 At the same time, *friendly societies* should make the assumption that the earnings yield on equities will fall by 10% (shortly after the above fall in equity values), but that dividends would remain unaltered when assessing the corresponding rate of interest at which the liabilities should be valued.

In 12.3(2), the current index should be compared to its recent average, based on levels at the close of business. Of the last 90 calendar days, only those on which the London Stock exchange was open for trading should be taken into account in determining the average. Where there has been a fall, such a percentage fall should be deducted from the 25% in arriving at this resilience test.

12.5 The ~~appointed actuary~~, actuary appointed to perform the *actuarial function* under the rules in *SUP* ~~in advising the friendly society~~, would then be expected to apply his or her own professional judgement in advising the management of the friendly society on ~~considering~~ the level of changes in the *market value* of, and yield on, other types of investment held by the society for the purpose of ~~this~~ the resilience test. The prudence concept should be paramount. Reductions in fixed interest yields, or changes in the shape of the yield curve, are among the obvious possibilities.

...

#### ~~Shares in and debts due from a related undertaking~~

13. ~~Annex C of Guidance Note 4.1 (Guidance for insurers and auditors on the Valuation of Assets Rules) in IPRU(INS) applies to friendly societies for the purposes of the valuation of shares held in and debts due, or to become due, from a related undertaking under paragraphs 3 and 4 of Appendix 4. [deleted]~~

## Annex 5

### GUIDANCE ON EXEMPTION FROM TRIENNIAL VALUATION

...

2 Rule 5.1 requires any *friendly society* with permission to carry on *long-term insurance business* which is-

(a) ~~a directive friendly society~~; or

(b) an *incorporated friendly society*,

to cause the ~~appointed actuary~~ appointed to perform the actuarial function under the rules in SUP to carry out an annual investigation into the *friendly society's* financial condition in respect of its *long-term insurance business*.

...

## Annex 7

### GUIDANCE ON THE USE OF DERIVATIVE CONTRACTS BY ~~DIRECTIVE~~ FRIENDLY SOCIETIES

#### Introduction

1. The main purpose of this Annex is to draw attention to the rules which cover whether a *derivative contract* has an admissible value which can count towards a *friendly society's* solvency margin. ~~Guidance Note 4.2 in IPRU(INS) applicable to insurers other than friendly societies discusses the valuation issues surrounding the use of derivative contract. The guidance it gives is also generally applicable to friendly societies.~~

#### Approved derivatives contracts

2. An *approved derivative contract*, if held by a ~~directive-friendly society~~ which maintains the *required margin of solvency*, in accordance with Part I of Chapter 4, may have an admissible value which can count towards a *friendly society's required solvency margin*. However, any *derivative contract* which is a liability to a *friendly society* (whether or not it falls within the definition of an *approved derivative contract* and is held for the purposes specified in 13 of Appendix 4) will count as a liability for solvency purposes.

...

#### Information for the FSA

4. A *friendly society* which proposes to make use of *derivative contracts* for the first time is asked to inform FSA staff of its proposals. Societies should note that they are likely to be strongly discouraged from using *derivative contracts* unless they can demonstrate robust systems and controls and a full understanding of the implications of the arrangement.

...

Annex 8 (Guidance on the balance sheet (forms 9 – 17 )) is deleted in its entirety, the text is not shown struck through.

## Annex 8

[deleted]

## Annex G

### Amendments to the Interim Prudential sourcebook for Insurers

#### Part 1: Amendments to Volume 1

In this part underlining indicates new text and striking through indicates deleted text. Where existing text is replaced by new text, this is indicated and the new text is not underlined. Where an entire section of text is deleted, the place where the change is made is indicated and the text is not struck through.

...

#### INTERIM PRUDENTIAL SOURCEBOOK FOR INSURERS GUIDANCE

##### THE PURPOSE OF THE PRUDENTIAL RULES FOR INSURERS AND AN OVERALL DESCRIPTION

Delete the paragraphs 1 to 18 below in their entirety  
[deleted text]

#### INTERIM PRUDENTIAL SOURCEBOOK FOR INSURERS CONTENTS

##### VOLUME ONE

<b>Guidance:</b>	<del>The purpose of the prudential rules for insurers and an overall description</del> <u>[deleted]</u>
Chapter 1	<del>Application rule and restriction of business to insurance</del>
Chapter 2	<del>Margins of solvency</del> <u>[deleted]</u>
Chapter 3	Long-term insurance business
	Part I Identification and application of assets and liabilities
	Part II Linked long-term contracts
Chapter 4	<del>Valuation of assets</del> <u>[deleted]</u>
Chapter 5	<del>Determination of liabilities</del> <u>[deleted]</u>
Chapter 6	<del>General insurance business: equalisation reserves</del> <u>[deleted]</u>
Chapter 7	<del>Currency matching and localisation</del> <u>[deleted]</u>

Chapter 8	Non-UK insurers
	Part I <del>Deposits—[deleted]</del>
	Part II <del>Location of accounts and records—[deleted]</del>
	Part III        Rules applicable to branches
Chapter 9	Financial reporting
	Part I          Accounts and statements
	Part II         Accounts and statements for a marine mutual
	Part III        Statistical rules
	Part IV        Material connected-party transactions
	<u>Part V</u> <u>Group Capital Adequacy</u>
Chapter 10	<del>Parent undertaking solvency calculation—[deleted]</del>
Chapter 11	Definitions
	Part I          Definitions
	Part II         General Provisions
	Annex 11.1    Classes of long-term insurance business
	Annex 11.2    Classes, and groups of classes, of general insurance business
Chapter 12	Transitional arrangements

## VOLUME TWO

### Appendices to the Rules

Appendix 2.1	<del>General insurance business solvency margin: first method of calculation (premium basis) (rule 2.4(1)(b)) [deleted]</del>
Appendix 2.2	<del>General insurance business solvency margin: second method of calculation (claims basis) (rule 2.4(1)(b)) [deleted]</del>
Appendix 2.3	<del>Minimum guarantee fund (rule 2.9) [deleted]</del>
Appendix 3.1	[deleted]
Appendix 3.2	Permitted links (rule 3.7)
Appendix 4.1	[deleted]
Appendix 4.2	<del>Assets to be taken in to account only to a specified extent (rule 4.14) [deleted]</del>
Appendix 5.1	<del>Relevant co-insurance operations (rule 5.5 and relevant co-insurance</del>

	<del>operation)</del> <u>[deleted]</u>
Appendix 6.1	<del>Methods of calculating the equalisation reserve (rule 6.7)</del> <u>[deleted]</u>
Appendix 6.2	<del>Method of calculating the equalisation reserve for credit insurance business (rule 6.12)</del> <u>[deleted]</u>
Appendix 9.1	Balance sheet and profit and loss account (Forms 9-17) (rules 9.12 and 9.13)
Appendix 9.2	General insurance business: revenue account and additional information (Forms 20 to 39) (rules 9.14 to 9.22)
Appendix 9.3	Long-term insurance business: revenue account and additional information (Forms 40 to 45) (rules 9.14 and 9.23)
Appendix 9.4	Abstract of valuation report prepared by appointed actuary (Forms 46 to 61) (rule 9.31)
<u>Appendix 9.4A</u>	<u>Abstract of valuation report for realistic valuation (rule 9.31)</u>
Appendix 9.5	General insurance business: additional information on business ceded (rule 9.32)
Appendix 9.6	Certificates by directors and actuary and report of auditors (rules 9.34 and 9.35)
Appendix 9.7	Insurance statistics: other EEA States (Forms 91 to 94) (rule 9.37)
Appendix 9.8	Marine mutuals: items to be disregarded, directors' certificates and auditors reports (rule 9.36A)
<u>Appendix 9.9</u>	<u>Group Capital Adequacy (rules 9.40 to 9.42 and guidance 9.43)</u>

## **VOLUME THREE**

### **FSA GUIDANCE NOTES**

Guidance Note P.1	<del>Systems and controls over the investments (and counterparty exposure) with particular reference to the use of derivatives (Principles for business)</del> <u>[deleted]</u>
Guidance Note P.2	<del>Systems and controls over general business claims provisions (Principles for business)</del> <u>[deleted]</u>
Guidance Note P.3	<del>Systems and controls in insurers</del> <u>[deleted]</u>
Guidance Note 2.1	<del>Hybrid capital: admissibility for solvency (rule 6.1 and required</del>



~~margin of solvency) [deleted]~~

Guidance Note 2.2 ~~Guidance on applications for waivers relating to implicit items [deleted]~~

Guidance Note 2.3 ~~Solvency margin: implementation of Solvency I Directives [deleted]~~

Guidance Note 4.1 ~~Guidance for insurers and auditors on the Valuation of Assets Rules [deleted]~~

Guidance Note 4.2 ~~Use of derivative contracts in insurance funds (rule 4.12) [deleted]~~

Guidance Note 4.3 [deleted]

Guidance Note 4.4 ~~Linked contracts [deleted]~~

Guidance Note 5.1 ~~Resilience test [replaced by Guidance Note No.4 (Resilience test for insurers) until the Integrated Prudential Sourcebook comes into force] [deleted]~~

Guidance Note 9.1 ~~Preparation of returns [deleted]~~

Guidance Note 9.2 [deleted]

Guidance Note 10.1 ~~Parent undertaking solvency calculation [deleted]~~

## **GUIDANCE: FSA ‘DEAR DIRECTOR’ LETTERS**

DD1 ~~Use of derivatives—listed products [deleted]~~

## **OTHER MATERIAL: ‘DEAR APPOINTED ACTUARY’ LETTERS**

DAA8 ~~Recommended aids reserving policy [deleted]~~

DAA9 ~~Pensions review: reserving for guarantees [deleted]~~

DAA11 ~~Reserving for guaranteed annuity options [deleted]~~

DAA13 ~~Reserving for guaranteed annuity options [deleted]~~

DAA14 [deleted]

DAA15 [deleted]

## **Chapter 1**

### **APPLICATION RULE AND RESTRICTION OF BUSINESS TO INSURANCE**

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## **CONTENTS**

## Application

1.1 Insurers

1.2 The Society of Lloyd's

## ~~Restriction of business to insurance~~

1.3 ~~[deleted]~~

---

## Chapter 1

### ~~APPLICATION RULE AND RESTRICTION OF BUSINESS TO INSURANCE~~

---

## Application

### Insurers

1.1 An insurer must comply with *IPRU (INS)* unless it is –

(a) a *friendly society*<sup>1</sup>; or

(b) subject to ~~rule 3.5(3) (payment of financial penalties)~~ and rules 3.6 and 3.7 (application of rules to *linked long-term contracts*), an *EEA insurer* qualifying for authorisation under Schedules 3 or 4 to the *Act*.

The Society of Lloyd's<sup>2</sup>

1.2 No provisions of *IPRU (INS)* apply to the *Society of Lloyd's*, or members of the *Society of Lloyd's* except rules 9.37 and 9.38.

---

<sup>1</sup> A *non-directive friendly society* must comply with *IPRU(FSOC)*; a *directive friendly society* must comply with *PRU*; with Chapters 1, 2 and 3, 4 (rules 4.20 to 4.23 only), 5 (rule 5.1A only) 7, 8 and Appendix 3 of *IPRU(FSOC)*. Rule 5.1A of *IPRU(FSOC)* effectively applies most of Chapter 9 of *IPRU(INS)* to *directive friendly societies*, notwithstanding *IPRU(INS)* 1.1(a)

<sup>2</sup> *LLD* applies to the *Society*.

## **Restriction of business to insurance**

1.3 (1) ~~— An *insurer* must not carry on any commercial business in the United Kingdom or elsewhere other than *insurance business* and activities directly arising from that business.~~

### ~~In-house pension funds~~

(2) ~~— If an *insurer* manages assets of a pension fund solely for the benefit of—~~

(a) ~~— its ‘officers’ or ‘employees’; or~~

(b) ~~— its ‘officers’ or ‘employees’ and ‘officers’ or ‘employees’ of its *subsidiary* or *holding company* or a *subsidiary* of its *holding company*,~~

~~that activity is to be treated as directly arising from the *insurer’s insurance business*.~~

(3) ~~— **Officers** or **employees** include their dependants. [deleted]~~

---

Chapter 2 (Margins of solvency) is deleted

## **Chapter 2**

[deleted]

## **Chapter 3**

### **LONG-TERM INSURANCE BUSINESS**

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#### **CONTENTS**

##### **Part I - Identification and application of assets and liabilities**

3.1 Separation of assets and liabilities attributable to long-term insurance business

3.2 Application of assets of insurer with long-term insurance business

- 3.3 Allocations to policy holders
- 3.4 ~~Restriction on transactions with connected persons [deleted]~~
- 3.5 Arrangements to avoid unfairness between separate insurance funds, ~~source of funds~~  
for payment of financial penalties, etc

## **Part II - Linked long-term contracts**

- 3.6 Application
- 3.7 Linked long-term contracts

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## **Chapter 3**

### **LONG-TERM INSURANCE BUSINESS**

---

#### **Part I**

#### **IDENTIFICATION AND APPLICATION OF ASSETS AND LIABILITIES**

##### **Separation of assets and liabilities attributable to long-term insurance business**

- 3.1 (1) ~~Where an insurer carries on ordinary long-term insurance business or industrial assurance business or both –~~
- ~~(a) — it must maintain a separate account in respect of each kind of business; and~~
  - ~~(b) — the receipts of each kind of business must be entered in the account maintained for that business and must be carried to and form a separate long-term insurance fund with an appropriate name. [deleted]~~
- (2) An insurer which carries on ordinary long-term insurance business or industrial assurance business must maintain such accounting and other records as are necessary for identifying -
- (a) the assets representing the ~~fund~~ long-term insurance fund maintained by it for that business ~~under (1)(b)~~ (but without necessarily distinguishing between the ~~funds or~~ funds if more than one); and
  - (b) the liabilities attributable to each kind of business which it carries on.

## Application of assets of insurer with long-term insurance business

### *Limitation on use of assets in long-term insurance fund*

- 3.2 ~~(1) Subject to (2) and (4), long-term insurance business assets must—~~
- ~~(a) be applied only for the purposes of its long-term insurance business; and~~
  - ~~(b) not be transferred so as to be available for other purposes of the insurer except where the transfer constitutes reimbursement of expenditure borne by other assets (in the same or the preceding financial year) in discharging liabilities wholly or partly attributable to long-term insurance business.~~

#### ~~First exception: the use of excess assets~~

- ~~(2) Where an actuarial investigation shows that the value of the assets mentioned in (1) exceeds the amount of the liabilities attributable to the long-term insurance business, the restriction imposed by that rule does not apply to so much of those assets as represents the excess.~~

#### ~~Qualification~~

- ~~(3) (2) does not authorise a transfer or other application of assets by virtue of an actuarial investigation at any time after the date when the abstract of the actuary's report of the investigation has been deposited with the FSA in accordance with rule 9.6(1).~~

#### ~~Second exception: exchanges at fair market value~~

- ~~(4) Nothing in (1) precludes an insurer from exchanging, at fair market value, long-term insurance business assets for other assets of the insurer.~~

#### ~~Further limitation on use of assets in long-term insurance fund~~

- ~~(5) Money from an insurer's long-term insurance fund must not be used for the purposes of any other business of the insurer notwithstanding any arrangement for its subsequent repayment out of the receipts of that other business. [(1) to (5) deleted]~~

#### ~~Restriction in relation to dividends~~

- ~~(6) A long-term insurer must not declare a dividend at any time when the value of the long-term insurance business assets, as determined in accordance with the Valuation of Assets Rules, PRU 1.3 and PRU 3.2 is less than the amount of the long-term insurance business liabilities technical provisions determined in accordance with the Determination of Liabilities Rules and any other~~

liabilities connected with the long-term insurance business.

...

### **Allocations to policy holders**

Allocation of established surplus

3.3 (1) ...

an *insurer* must not by virtue of ~~rule 3.2(2)~~ PRU 7.6.27R transfer or otherwise apply assets representing any part of the surplus mentioned in (a) unless the insurer has –

...

(7) (1) does not authorise the application for purposes other than those mentioned in ~~rule 3.2(1)~~ PRU 7.6.30R of assets representing any part of the surplus mentioned in (1)(a) which the *insurer* has decided to carry forward unappropriated; and for the purposes of (2) the amount of any surplus is treated as reduced by any part of it which the insurer has decided to carry forward unappropriated.

...

Restriction on transactions with connected persons

Rule 3.4 is deleted

3.4 [deleted]

3.5 **Arrangements to avoid unfairness between separate insurance funds, source of funds for payment of financial penalties, etc**

...

~~(3) Where the FSA imposes a financial penalty on a long-term insurer (including an insurer qualifying for authorisation under Schedules 3 or 4 to the Act), which is not a mutual, the insurer must not pay that financial penalty from a long-term insurance fund. [deleted]~~

### **Adequacy of premiums**

3.5A (1) ~~Before entering into a long-term insurance contract, a UK insurer must satisfy itself that the aggregate of~~

~~(a) — the premiums payable under the contract and the income which will be derived from them; and~~

~~(b) — any other resources of the *UK insurer* which are available for the purpose, will be sufficient, on reasonable actuarial assumptions, to meet all *commitments* arising under or in connection with the contract.~~

~~(2) — A *UK insurer* must not rely on other resources for the purposes of (1) — in such a way as to jeopardise its solvency in the long term. [deleted]~~

...

Chapters 4 (Valuation of assets), 5 (Determination of liabilities), 6 (General insurance business: equalisation reserves) and 7 (Currency matching and localisation) are deleted

**Chapter 4**  
[deleted]

**Chapter 5**  
[deleted]

**Chapter 6**  
[deleted]

**Chapter 7**  
[deleted]

**Chapter 8**

**NON-UK INSURERS**

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**CONTENTS**

**Part I - Deposits**

8.1 — ~~Making and amount of deposit~~ [deleted]

**Part II - Location of accounts and records**

8.2 — ~~Location of accounts and records~~ [deleted]

## Part III – Rules applicable to branches

8.3 –8.5

### Part I

#### DEPOSITS

##### ~~Making and amount of deposit~~

8.1 ~~(1) Subject to (2), a non-EEA insurer which has permission under the Act to carry on direct insurance business, other than a Swiss general insurer, must make and maintain a deposit in the United Kingdom with an approved credit institution which is no less than the minimum.~~

~~(2) Where~~

~~(a) the insurer carries on insurance business in the United Kingdom and one or more other EEA States; and~~

~~(b) the FSA and the appropriate supervisory authority or authorities in the EEA States have agreed that this rule should apply;~~

~~the insurer must make and maintain the deposit with such person as may be agreed between the FSA and the other authority or authorities.~~

~~[deleted]~~

### Part II

#### LOCATION OF ACCOUNTS AND RECORDS

8.2 ~~A non-EEA insurer which is not a Swiss general insurer must keep in the United Kingdom proper accounts and records in respect of insurance business carried on in the United Kingdom. [deleted]~~

### Part III

#### RULES APPLICABLE TO BRANCHES

8.3 ~~An insurer which has its head office outside the United Kingdom (other than a pure reinsurer which has a Treaty right under Schedule 4 to the Act, or a Swiss general insurer) must appoint and maintain the appointment of a chief executive (who alone or jointly with one or more others, is responsible for the conduct of its business through an establishment in the United Kingdom) and an authorised UK representative (who is resident in the United Kingdom and is authorised to act generally, and to accept service of any document, on behalf~~



of the *insurer* in the United Kingdom).

8.4 ~~A Swiss general insurer must appoint and maintain the appointment of an authorised UK representative as described above. [deleted]~~

8.5 ~~An insurer which has its head office outside the United Kingdom (other than a pure reinsurer which has a Treaty right under Schedule 4 to the Act) must be entitled to undertake insurance business under its national law. [deleted]~~

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## Chapter 9

### FINANCIAL REPORTING

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#### CONTENTS

##### Part I - Accounts and statements

...

##### 9.3A Half-yearly balance sheet and report for realistic valuation

...

##### 9.22 Additional information on general insurance business (~~other than credit insurance business~~)

...

##### 9.31 ~~Periodic actuarial investigation~~ Valuation reports on long-term insurance business

...

##### 9.34 Certificates of Directors

...

##### 9.36 Information on ~~appointed actuary~~ the actuary who has been appointed to perform the with-profits actuary function

...

##### Part V – Group Capital Adequacy

##### 9.40 – 9.43

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## Chapter 9

### FINANCIAL REPORTING

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#### Part I

#### ACCOUNTS AND STATEMENTS

#### Application

- 9.1 These *Accounts and Statements Rules* apply to every *insurer* other than -
- (a) an *EEA-deposit insurer*, in relation to *insurance business* carried on by it outside the United Kingdom; or
  - ...
- Interpretation
- 9.2 ...
- (3) ...
  - (b) in relation to a *UK-deposit insurer*, to its entire *long-term insurance business* or to its entire *general insurance business* and to any *long-term insurance business* or *general insurance business* carried on by it through a branch in any *EEA State*,
- ...
- (ii) accounts prepared in respect of the *long-term insurance business* or the *general insurance business* carried on, in the case of an *external insurer*, by the branch in the United Kingdom and, in the case of a *UK-deposit insurer*, by the branches in question in the *EEA States* taken together.
- ...

#### **Half-yearly balance sheet and report for realistic valuation**

#### 9.3A

- (1) Every *long-term insurer* which is a *realistic basis life firm* must in respect of each *financial year* prepare **Forms 2, 18 and 19 of Appendix 9.1**, as at the end of the first six months of that *financial year*.

- (2) The Forms in (1) must be prepared in accordance with **Appendix 9.1**, and **Form 2** must be completed in respect of the *long-term insurance business* of the *firm* and **Forms 18 and 19** must be completed in respect of each of the *firm's with-profit funds*.
- (3) The Forms in (1) must be accompanied by a report (instead of the reports required under rule 9.4(1)(b)) identifying any changes to the methods and assumptions used from those set out in the report for the realistic valuation as at the end of the *preceding financial year* .
- (4) Rules 9.4, 9.6, 9.10, 9.11, 9.12, 9.33 and 9.34, **Appendices 9.1** and **9.4A** and **Part I of Appendix 9.6** apply to this rule and to any documents required under this rule as if –
- (a) an additional balance sheet were required under rule 9.3;
  - (b) the documents required by (1), and only those documents, were required by rule 9.12 for the purposes of the balance sheet in (a) above;
  - (c) an additional investigation were required under rule 9.4 in respect of the six-month period covered by this rule;
  - (d) any document required by (3) were a document required by rule 9.31(b) for the purposes of the investigation in (c) above;
  - (e) any reference to the *financial year in question* (however expressed) were a reference to the six-month period referred to in (1);
  - (f) any reference to the *preceding year* were a reference to the end of the *preceding financial year*;
  - (g) the required signatory in each case were any director of the *insurer*;
  - (h) any reference to a particular amount shown in a document not required under (1) or (3) were a reference to the amount which would be shown in that document (subject to any modifications in (a) to (f) above) in accordance with the *Accounts and Statements Rules* if that document were required to be produced; and
  - (i) any requirement (other than in this rule) to refer in the *return* or any certificate annexed to it by virtue of rule 9.34 to a document not required under (1) or (3) were omitted.
- (5) Instead of a valuation report under rule 9.31(a), the report referred to in (3) must include, in an additional numbered answer following the answers to the paragraphs in **Appendix 9.4A**–
- (a) a full description of each of the changes in the methods and assumptions used in the investigation for the purposes of rule 9.4(2)(a) and (b) since the previous investigation at the end of the *preceding financial year*; or

(b) if there has been no such change, a statement to that effect.

Rules 9.3, 9.5, 9.7, 9.13 to 9.30, 9.31, 9.32 and 9.35 to 9.39 do not apply in respect of the documents required under this rule.

### **Periodic actuarial investigation of long-term insurer**

- 9.4 (1) Every *long-term insurer* –
- (a) must, once in every period of 12 months, cause an investigation to be made into its financial condition in respect of its *long-term insurance business*, in accordance with the methods and assumptions determined by the insurer, by the person or persons who for the time being ~~is its appointed-actuary~~ are appointed to perform the actuarial function under the rules in *SUP*; and
  - (b) when such an investigation has been made, or when at any other time an investigation into the financial condition of the *insurer* in respect of its *long-term insurance business* has been made with a view to the distribution of profits, or the results of which are made public, must cause an abstract of the ~~appointed actuary's~~ report or reports of the investigation to be made.
- (2) An investigation to which (1)~~(b)~~ relates must include –
- (a) a determination of the liabilities of the *insurer* attributable to its *long-term insurance business*; ~~and~~
  - (b) a valuation of any excess over those liabilities of the assets representing the *long-term insurance fund* or *funds* and, where any rights of any long-term *policy holders* to participate in profits relate to particular parts of such a fund, a valuation of any excess of assets over liabilities in respect of those parts; and
  - (c) for every long-term insurer which is a realistic basis life firm, a calculation of the with-profits insurance capital component.
- (3) For the purposes of any investigation to which this rule applies, the value of any assets and the amount of any liabilities must be determined in accordance with ~~the Valuation of Assets Rules PRU 1.3, PRU 3.2 and the Determination of Liabilities Rules PRU 7.~~
- (4) The form and contents of any abstract under this rule must be in accordance with ~~the Accounts and Statements Rules~~ rule 9.31.

### **Audit of accounts**

9.5 (1) ...

(2) In (1), the reference to **accounts and balance sheets** includes a reference to any notes or statement or report annexed to them, save for -

(a) the *directors'* certificate annexed pursuant to rule 9.34, and

(b) Forms 46 to 47A, 50 to 55, 57 and 59.

#### **Deposit of accounts etc. with the FSA**

9.6 (1) ~~Subject to (1A), e~~Every 'account', 'balance sheet', abstract or statement required by rules 9.3, 9.4 and 9.36A and any report of the auditor of the *insurer* made in pursuance of rules 9.5 or 9.36E must be printed, and the 'required copies' must be deposited with the *FSA* within the periods set out in the table below.

	<b>deposit period following the <i>financial year end</i></b>	
<b><i>financial year ending on or after</i></b>	<b>where the deposit is made electronically or under rule 9.36A</b>	<b>otherwise</b>
31 December 2001	4 months	3 months and 15 days
31 December 2002 and following years	3 months	2 months and 15 days

~~(1A) For a *financial year* ending on a date from 31 December 2002 to 30 December 2003, the deposit periods for the 'required copies' of **Form 9A** set out in (1) are extended by 1 month.~~

...

#### **Value of assets and amount of liabilities**

9.10 Unless otherwise provided in the *Accounts and Statements Rules*, in the documents which an *insurer* is required to prepare in accordance with the *Accounts and Statements Rules* –

(a) the value or amount given for an asset ~~(other than a *linked asset* not required to be valued in accordance with the *Valuation of Assets Rules* by virtue of rule 4.1(2))~~ or a liability of the *insurer* is the value or amount of that asset or liability as determined in accordance with ~~the PRU 1.3 *Valuation of Assets Rules* and the *Determination of Liabilities Rules*~~ PRU

7 at the end of *the financial year in question*; and

- (b) ~~in the case of a *linked asset* of the *insurer* (other than a *linked asset* required to be valued in accordance with the *Valuation of Assets Rules* by virtue of rule 4.1), the value given is the value of that asset as determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate for *insurers*~~ no value shall be given to exposures in excess of the limits set out in PRU 3.2.22R (3);
- (c) notwithstanding (a) and (b) (but subject to the conditions set out in (d)), an *insurer* may, for the purposes of an *actuarial investigation*, elect to assign to any of its assets the value given to the asset in question in the books or other records of the *insurer*; and
- (d) the conditions referred to in (c) are that –
  - (i) the election does not enable the *insurer* to bring into account any asset that is not an *admissible asset*; and
  - (ii) the value assigned to the aggregate of the *insurer's* assets is not higher than the aggregate of the value of those assets as determined in accordance with (a) and (b), without taking advantage of (c).

...

### **Balance sheet**

- 9.12 (1) The balance sheet required to be prepared by an *insurer* under rule 9.3(1) must comply with the requirements of **Appendix 9.1** and must be in **Forms 1 to 3, 9 10 to 15 and 17 to 19** of that Appendix completed (as may be appropriate) as specified in (2) to (89).
- (2) **Form 9 1** must be completed by every *insurer* that carries on *general insurance business*, other than a *Swiss general insurer* or an *EEA-deposit insurer*.
  - (2A) **Form 9A 2** must be completed by every *long-term insurer*, other than an *EEA-deposit insurer* in respect of the ~~*long-term insurance business*~~ carried on by the insurer.
  - (3) **Form 10 3** must be completed by every *insurer* other than a *Swiss general insurer* or an *EEA-deposit insurer*.
  - (3A) **Form 10** must be completed by an *external insurer* (other than a *pure reinsurer*), an *EEA-deposit insurer* or a *Swiss general insurer*.
  - (4) **Forms 11 and 12** must be completed by every *insurer* which carries on *general insurance business*, other than a *Swiss general insurer* or an *EEA*

*deposit insurer and, except when the instructions for completion of **Forms 11 and 12** specify otherwise, by every insurer which carries on long-term insurance business.*

- (5) ...
- (a) ...
- (i) its total *long-term insurance business assets*; and
- (ii) the *long-term insurance business assets* appropriated by it in respect of each *long-term insurance fund* or, where such assets have been appropriated for a group of funds, those assets;
- (b) by every *insurer* in respect of its total assets other than *long-term insurance business assets*;
- (c) by every *external insurer* (other than a *pure reinsurer*) in respect of *long-term insurance business* or *general insurance business* carried on by it through a branch in the United Kingdom in respect of those assets which are -
- (i) deposited under ~~rule 8.1~~ PRU 7.6.54R,
- (ii) maintained in the United Kingdom, and
- (iii) maintained in the United Kingdom and the other *EEA States*; and
- (d) by every *UK-deposit insurer* in respect of *long-term insurance business* or *general insurance business* carried on by it through branches in the *EEA States* in respect of those assets which are -
- (i) deposited under ~~rule 8.1~~ PRU 7.6.54R,
- ...
- (6) **Form 14** must be completed by every *long-term insurer* in respect of -
- (a) its total *long-term insurance business liabilities* and margins; and
- (b) the *long-term insurance business liabilities* and margins for each *long-term insurance fund* or where *long-term insurance business assets*



group. have been appropriated in respect of a group of funds, for the *group*

...

- (9) **Forms 18 and 19** must be completed by every *long-term insurer* which is a realistic basis life firm, in respect of each of its *with profits funds*.

...

**Additional information on general insurance business (~~other than credit insurance business~~)**

- 9.22 (1) This rule applies to ~~Part II business~~ *non-credit insurance business* as defined in PRU 7.5.11R (1) and ~~Part III business~~ *credit insurance business* as defined in PRU 7.5.38R.

- (2) An ~~Part II insurer~~ to which PRU 7.5.11R to PRU 7.5.37G apply (unless PRU 7.5.18R applies) and an ~~Part III insurer~~ to which PRU 7.5.43R applies (unless PRU 7.5.44R applies) must, in accordance with the requirements of **Appendix 9.2**, prepare -

- (a) **Form 37**;
- (b) **Form 38** for business reported on **Forms 21, 22** and **23**; and
- (c) **Form 39** for business reported on **Forms 24** and **25**.

...

**Additional information on general insurance business: major treaty reinsurers**

9.25 ...

- (2) ...
- (b) in relation to which (whether alone or with any *company* which is 'connected' with the other *company*) the aggregate of the amounts referred to in (1)(d) and (f) exceeds the sum of 20,000 Euro and 5% of the insurer's liabilities arising from its general insurance business amount, net of reinsurance ceded.

## Additional information on general insurance business: major facultative reinsurers

9.26 ...

(2) ...

- (b) in relation to which, in respect of any *reinsurer* (a **major facultative reinsurer**) the aggregate of amounts in (1)(d) and (e) exceeds the sum of 4,000 Euro and 1% of the *insurer's* liabilities arising from its general insurance business ~~amount~~, net of reinsurance ceded.

...

## Additional information on derivative contracts

9.29 (1) Every *insurer* must, in respect of the *financial year in question*, annex to the documents referred to in rules 9.12, 9.13 and 9.14 a statement comprising a brief description of -

...

- (h) the circumstances surrounding the use of any '*derivative contract*' held at any time during the *financial year* which ~~did not fall within rule 4.12 (2)~~ required a 'significant' provision to be made for it under PRU 4.3.17R, or (where appropriate) did not fall within the definition of a permitted derivative contract; and

...

(1A) For the purposes of determining in accordance with (1)(h) whether a required provision is 'significant', the *insurer* must have regard to its obligations under the contract and the volatility of the assets identified by the *insurer* as being suitable to cover such obligations; and the required provision in respect of any one *derivative contract* must be treated as **significant** if –

- (a) the aggregate provision required in respect of all contracts having a similar effect is significant; or
- (b) the aggregate provision required in respect of all contracts with which it is connected is significant.

(2) In this rule, **derivative contract** includes a contract or asset which 'has the effect of a *derivative contract*' ~~within the meaning of rule 4.13~~ and, for the purposes of (1)(h), such a contract or asset must be treated as requiring a significant provision or falling within ~~rule 4.12(2)~~, ~~or~~ the definition of *derivative contract* which would require a significant permitted derivative contract, as appropriate, if it has the effect of a provision or fall within that provision definition.

(2A) Subject to (2C), for the purposes of (2), a contract has the effect of a *derivative contract* if it is a contract (other than a *derivative contract*) which provides, whether upon the exercise of a right by the *insurer* or otherwise –

(a) for payment (at any time) of amounts which are determined by fluctuations in –

(i) the value of property of any description;

(ii) an index of the value of property of any description;

(iii) income from property of any description; or

(iv) an index of income from property of any description;

(b) for delivery to or by the *insurer* of an asset other than any office machinery (including computer equipment), furniture, motor vehicles and other equipment; or

(c) for the conversion of an asset held by the *insurer* or another party to –

(i) an asset of a different type, or

(ii) a different asset of the same type.

(2B) Subject to (2C), for the purposes of (2) an asset has the effect of a *derivative contract* if the asset is an asset (other than an *approved security* or a unit, or other beneficial interest, in a scheme falling within the *UCITS Directive*) and the holding of the asset confers contractual rights or imposes contractual obligations to make or accept payment, delivery or conversion as set out in (2A)(a) to (c).

(2C) A contract or asset does not have the effect of a *derivative contract* by reason only that -

(a) it provides for the unconditional delivery of assets, or for the payment for unconditional delivery of assets, such delivery or payment to be made within a period commencing at the date of the contract and extending –

(i) in the case of a *listed security*, for the usual period for delivery or payment as determined by the rules of the stock exchange or *regulated market* on which the *securities* are *listed* or facilities for dealing have been granted, or

- (ii) in any other case, for no more than 20 working days;
  - (b) it is a contract for the conversion of currency in respect of which the conditions set out in (2D) have been satisfied; or
  - (c) it is a *stock lending* transaction which satisfies the conditions of *PRU 4.3.36R*.
- (2D) The conditions referred to in (2C)(b) are that –
- (a) the contract provides –
    - (i) for the conversion into another currency of an amount representing the sale of an asset which has, on the *relevant date*, been sold but not delivered, or
    - (ii) for the purchase of currency for the purpose of settling the purchase of an asset which has, on the *relevant date*, been purchased but not delivered;
  - (b) the conversion is to take place during a period which is –
    - (i) where the contract is in connection with the delivery of a *listed security*, a period commencing on the date of the contract and extending for the usual period of settlement as laid down by the rules of the relevant stock exchange or *regulated market*, or
    - (ii) where the contract is in connection with the delivery of any other asset, a period commencing on the date of the contract and extending for 20 working days thereafter; and
  - (c) the contract is *listed* or has been entered into with an *approved counterparty*.

...

**Periodic actuarial investigation Valuation reports on long-term insurance business**

- 9.31 Save in relation to (b), for the purposes of rule 9.4, *ordinary long-term insurance business* and *industrial assurance business* must be treated separately, and the Every insurer which carries on *long-term insurance business* must prepare and annex to the documents referred to in rules 9.12, 9.13 and 9.14 -

- (a) ~~for the purposes of rule 9.4 other than in relation to the calculation required by rule 9.4(2)(c), a valuation the abstract of the report of the appointed actuary on long-term insurance business which, – treating ordinary long-term insurance business and industrial assurance business separately, must comply complies with the requirements of **Appendix 9.4** and ~~must contain~~ the information ~~(together with such of Forms 46 to 49 and 51 to 58 as may be appropriate)~~ specified in that Appendix; and~~
- (b) ~~except in the case of an EEA deposit insurer, must also include Form 60 and, where appropriate, Form 61~~ for the purposes of rule 9.4 in relation to the calculation required by rule 9.4(2)(c) (if applicable), a valuation report for the realistic valuation which complies with the requirements of **Appendix 9.4A** and contains the information specified in that Appendix.

...

### Signature of documents

- 9.33 (1) In respect of any document relating to the *insurance business* of an *insurer*, wherever it may be carried on, the signatories for the purposes of rule 9.6 are -
- (a) ~~in any case –~~
- (i) ~~a) where there are more than two *directors* of the *insurer*, at least two of those *directors* and, where there are not more than two *directors*, all the *directors*, and~~
- (ii) ~~b) a chief executive, if any, of the *insurer* or (if there is no chief executive) the secretary, if any; and~~
- (b) ~~in the case of an abstract under rule 9.4, the actuary who made the investigation to which the abstract relates.~~
- (2) In respect of any document relating to *insurance business* carried on through a branch in the United Kingdom by a *Swiss general insurer*, an *EEA deposit insurer* or an *external insurer* or through branches in any *EEA State* (taken together) by a *UK deposit insurer*, the signatories for the purposes of rule 9.6(3) are -
- (a) ~~in any case –~~
- (i) ~~a) the authorised UK representative referred to in rule 8.3 or 8.4, as the case may be article 3(1)(a) of The Financial Services and Markets Act 2000 (Variation of Threshold Conditions) Order 2001 (2001/2507), and~~

- (~~ii~~ b) the chief executive appointed under rule 8.3 or, in the case of a *Swiss general insurer*, a person who alone or jointly with one of more others, is responsible for the conduct of its *insurance business* through the branch; ~~and~~

~~(b) in the case of an abstract under rule 9.4, the actuary who made the investigation to which the abstract relates.~~

### **Certificates by Directors**

9.34 There must be annexed to the documents referred to in rules 9.12, 9.13 and 9.14 ~~(a)~~ a certificate in accordance with the requirements of Part I of **Appendix 9.6** which must be signed by the persons required by rule 9.33 to sign the documents to which the certificate relates; ~~and~~

~~(b) in the case of an *insurer* which has at any time during the *financial year in question* carried on *long-term insurance business*, a certificate in accordance with the requirements of Part II of **Appendix 9.6** which must be signed by the *appointed actuary*.~~

### **Audit and auditor's report**

9.35 (1) The documents referred to in rules 9.12, 9.13 and 9.14, together with **Forms 40 to 45, 48, 49, 56, 58 and 60**, and every statement, analysis, ~~or~~ report ~~or~~ certificate annexed pursuant to rules 9.24 to 9.27, 9.29 and ~~9.31~~ 9.34(a) must be audited by a person, in accordance with the rules in *SUP*, who must make and annex to those documents a report in accordance with the requirements of Part ~~II~~ III of **Appendix 9.6**.

~~(1A) For the purposes of rule 9.5 and (1) and **Appendix 9.6**, to the extent that any document, form, statement, analysis or report to be audited under (1) contains amounts or information abstracted from the *actuarial investigation* performed pursuant to rule 9.4, the *insurer* must ensure that the auditor obtains and pays due regard to advice from a suitably qualified *actuary* who is independent of the *insurer*.~~

(2) ...

### **Information on ~~the appointed actuary~~ actuary who has been appointed to perform the with-profits actuary function**

9.36 (1) Subject to the provisions of this rule, there must be annexed to the documents referred to in rules 9.12, 9.13 and 9.14, with respect to every person who, at any time during the *financial year in question*, was the ~~appointed actuary~~ actuary who has been appointed to perform the *with-profits actuary function* ~~to~~ for the *insurer*, a statement of the following information -

(a) particulars of any *shares* in, or debentures of, ‘the *insurer*’ in which the *appointed* ‘actuary’ was ‘interested’ at any time during that year;

...

## **Part II**

### **ACCOUNTS AND STATEMENTS FOR A MARINE MUTUAL**

#### **Returns**

9.36A Subject to rules 9.36B, 9.36C, 9.36D and 9.36E and **Appendix 9.8**, a *marine mutual* may complete an abbreviated *return* which comprises –

- (1) **Forms 1, 3, 11 and 12**; and
- (2) **Forms M1 to M5 in Appendix 9.8**,

and, if so, rules 9.3 to 9.4, 9.12 to 9.28, 9.31 and 9.32 and 9.34 to 9.36 do not apply.

...

## **PART IV**

### **MATERIAL CONNECTED-PARTY TRANSACTIONS**

9.39 (1) If, during the *financial year in question*, an *insurer* has agreed to, or carried out, a *material connected-party transaction*, it must provide a brief description of that transaction by way of a supplementary note to **Form 20 (note 2007)** or **Form 40 (note 4009)**.

...

## **PART V**

### **GROUP CAPITAL ADEQUACY**

9.40 (1) Subject to (2), an *insurer* to which PRU 8.3 applies must, in respect of its *ultimate insurance parent undertaking* and its *ultimate EEA insurance parent undertaking* (if different), submit a report of:

- (a) the group capital resources of that undertaking (as calculated in accordance with PRU 8.3.36R); and
  - (b) the group capital resources requirement of that undertaking (as calculated in accordance with PRU 8.3.33R).
- (2) An insurer is not required to submit the report referred to in (1) where:
- (a) The insurer is an undertaking listed in PRU 8.3.17R (2); or
  - (b) under Article 4(2) of the Insurance Groups Directive, a competent authority of an EEA State other than the United Kingdom has agreed to be the competent authority responsible for exercising supplementary supervision in accordance with PRU 8.3.23R.
- (3) The report required in (1) must:
- (a) comply with the requirements of SUP 16.3;
  - (b) subject to (d), be signed by the persons described in IPRU(INS) 9.33(1);
  - (c) include a statement from the auditors of the insurer (or of an insurer under (d)) that, in their opinion, the report has been properly compiled in accordance with PRU 8.3 from information provided by members of the insurance group and from the insurer's own records; and
  - (d) be provided by either the insurer or on behalf of the insurer (the first insurer) by any other insurer to which PRU 8.3 applies and which is a member of the insurance group (the second insurer) where:
    - (i) it is signed by two directors of the second insurer, and
    - (ii) it contains a statement that it has been copied to the board of directors of the first insurer.

9.41 (1) Subject to (2), an insurer must include, in the report in rule 9.40(1), the details of any regulated related undertaking in the insurance group where the individual capital resources requirement of that undertaking exceeds its



solo capital resources, stating in each case:

- (a) where the undertaking in rule 9.41(1)(a) is a subsidiary undertaking of the ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking (if different), the full amount of the calculation items set out in PRU 8.3.28R of that undertaking in accordance with PRU 8.3.30R and PRU 8.3.31R; or
  - (b) where the undertaking in rule 9.41(1)(a) is not a subsidiary undertaking, the ultimate insurance parent undertaking's or ultimate EEA insurance parent undertaking's relevant proportion, as set out in PRU 8.3.29R, of the calculation items set out in PRU 8.3.28R of that undertaking.
- (2) Subject to paragraph (4) an insurer can exclude a regulated related undertaking where the individual capital resources requirement of that undertaking exceeds its solo capital resources if:
- (a) the group capital resources of the ultimate insurance parent undertaking or the ultimate EEA insurance parent undertaking (as the case may be) exceed its group capital resources requirement;
  - (b) paragraph 3 applies to the regulated related undertaking.
- (3) This paragraph applies to a regulated related undertaking if:
- (a) in respect of the insurance group, it is not;
    - (i) the insurer; or
    - (ii) a parent undertaking of the insurer; or
    - (iii) a participating undertaking in the insurer; or
    - (iv) a related undertaking of the insurer; and
  - (b) the amount by which its individual capital resources requirement exceeds its solo capital resources does not exceed 5% of the amount that the group capital resources exceed the group capital resources requirement referred to in rule (2)(a)

(4) An insurer must include regulated related undertakings to which paragraph (2) would apply if the amount of D less E exceeds 10% of the amount that the group capital resources exceed the group capital resources requirement referred to in rule (2)(a), where:

(a) D is the sum of the individual capital resources requirements of the regulated related undertakings; and

(b) E is the sum of the solo capital resources of the regulated related undertakings.

9.42 (1) The report in rule 9.40(1) must include information and calculations required by 9.40 and 9.41:

(a) as at the end of the financial year of:

(i) the insurer; or

(ii) the ultimate EEA insurance parent undertaking; or

(iii) the ultimate insurance parent undertaking.

(b) subject to (2), as at the same date for every member of the insurance group to which the report relates. Where the financial year end of a member of the insurance group differs from the date chosen for the purposes of 1(a), interim calculations must be prepared for that member as at the date chosen for the purposes of 1(a); and

(c) as at a date no later than 12 months from the day after the end of the financial year by reference to which the information and calculations required in the report were last provided under this chapter or Chapter 10 of IPRU(INS).

(2) If it is not practical to prepare interim calculations for a member of the insurance group whose financial year end differs from the date chosen for the purposes of 1(a), calculations as at the member's last financial year end may be used, provided that:

(a) the member's financial year end is not more than three months

before the date chosen for the purposes of 1(a); and

- (b) the calculations are adjusted to take account of any changes between the *financial year* end and the date chosen for the purposes of 1(a) that materially affect the information and calculations required by rules 9.40 and 9.41.
- (3) If for any reason the end of the *financial year* chosen for the purposes of 1(a) is changed so as to end on a date later than that specified in 1(c):
  - (a) the report after the change takes effect must be as at the later date; but
  - (b) unless the report contains information and calculations that do not materially differ from what they would be as at the date specified in 1(c), the *insurer* must also provide the *FSA* with an interim statement.
- (4) The report in rule 9.40(1) must be provided to the *FSA* no later than 4 months from the end of:
  - (a) The *financial year in question*; or
  - (b) the *financial year* of the relevant parent, where the report is provided as at the end of its *financial year* under 1(a).

#### Guidance

- 9.43
- (1) An *insurer* may use Appendix 9.9 Form 95 for the purposes of the report required by rule 9.40(1).
  - (2) The report required by rule 9.40(1) does not form part of the *insurer's return*.
  - (3) Where several *insurers* to which rule 9.40 applies have the same *ultimate insurance parent undertaking* or *ultimate EEA insurance parent undertaking* or both, rule 9.40 applies to all of them. In these circumstances one *insurer* may submit the report in rule 9.40 on behalf of the other *insurers* in the *insurance group* as set out in rule 9.40(3)(d). This should consist of one package of the relevant information with confirmation that

the insurer submitting the information has made it available to the boards of directors of the other insurers in the insurance group. The purpose of this requirement is to ensure that all the insurers in the insurance group are aware of the relevance of the group information to themselves.

- (4) Where an insurance group consists of an ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking which is itself an insurer whose head office is in the United Kingdom and which has a United Kingdom insurance subsidiary or subsidiaries which is or are themselves insurers, the report in rule 9.40 will cover the same group undertakings. The subsidiary insurer need not in these circumstances deposit the report in rule 9.40. However, this does not affect the requirement to provide information under rule 9.41.

Chapter 10 (Parent undertaking solvency calculation) is deleted

## **Chapter 10**

[deleted]

Amend or delete the following definitions in chapter 11 as shown (unchanged definitions are not shown):

## **Chapter 11**

### **DEFINITIONS**

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#### **PART I**

#### **DEFINITIONS**

- 11.1 For the purposes of *IPRU (INS)*, the term or phrase in the first column has the meaning given to it in the second column unless the context otherwise requires.

Term or phrase	Definition
<i>1980 Regulations</i>	Insurance Companies (Accounts and Statements) Regulations (S.I. 1980 No. 6)

...

<i>Accounts Directives</i>	Council Directives 78/660/EEC for companies, 91/674/EEC for insurance companies, 86/635/EEC for banks and 83/349/EEC for consolidated accounts
<i>accumulating with-profits policy</i>	a <i>with-profits policy</i> which has a readily identifiable current benefit, whether or not this benefit is currently realisable, which is adjusted by an amount explicitly related to the amount of any premium payment and to which additional benefits are added in respect of participation in profits by additions directly related to the current benefit or a <i>policy</i> with similar characteristics
<i>Act</i>	Financial Services and Markets Act 2000
<i>admissible asset</i>	an asset which is not required by rule 4.1(3) to be left out of account for the purposes specified in rule 4.1(1) that falls into one or more categories in <i>PRU 2 Annex 1R</i>
<i>Amortised value</i>	the amortised value as determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate to <i>insurers</i>
<i>ancillary risk</i>	<p>(a) — in relation to an <i>insurer</i> with permission under the <i>Act</i> to insure a principal risk belonging to one <i>class</i> of <i>general insurance business</i>, means a risk included in another such <i>class</i> which is —</p> <ul style="list-style-type: none"> <li>—— connected with the principal risk,</li> <li>—— concerned with the object which is covered against the principal risk, and</li> <li>—— the subject of the same contract insuring the principal risk;</li> </ul> <p>(b) — but, the risks included in <i>classes</i> 14, 15 and 17</p>

	<p>may not be treated as risks ancillary to other <i>classes</i>;</p> <p>(e) — except, the risk included in <i>class 17</i> (legal expenses insurance) may be regarded as an ancillary risk of <i>class 18</i> where the conditions laid down in (a) are fulfilled and where the principal risk relates solely to assistance provided for persons who fall into difficulties while travelling, while away from home or while away from their permanent residence or where it concerns disputes or risks arising out of, or in connection with, the use of sea-going vessels</p>
<i>annuities on human life</i>	does not include superannuation allowances and annuities payable out of any fund applicable solely to the relief and maintenance of persons engaged or who have been engaged in any particular profession, trade or employment, or of the dependants of such persons
<i>appointed actuary</i>	the person appointed as actuary to an <i>insurer</i> under the rules in <i>SUP</i>
<i>approved counterparty</i> <sup>3</sup>	<p>any of the following—</p> <p>(a) — an <i>approved credit institution</i>;</p> <p>(b) — a person permitted under the <i>Act</i> to conduct investment business of a kind which includes entering into <i>unlisted derivative contracts</i> as principal; or</p> <p>(c) — in respect of a transaction involving a new issue of <i>securities</i> which are to be <i>listed</i>, the issuer or an <i>approved investment firm</i> acting on behalf of the issuer</p>
<i>approved credit institution</i>	an institution recognised or permitted under the law of an <i>EEA State</i> to carry on any of the activities set out in Annex 1 to the <i>Banking Co-ordination Directive</i> and, for the purposes of a <i>deposit</i> made before 1 December 2001, the Accountant General of the Supreme Court

<sup>3</sup> For guidance, see paragraph 3 of **Guidance Note 4.1**

<p><i>approved financial institution</i></p>	<p>any of the following—</p> <ul style="list-style-type: none"> <li>● <del>the European Central Bank;</del></li> <li>● <del>the central bank of an <i>EEA State</i>;</del></li> <li>● <del>the International Bank for Reconstruction and Development;</del></li> <li>● <del>the European Bank for Reconstruction and Development;</del></li> <li>● <del>the International Finance Corporation;</del></li> <li>● <del>the International Monetary Fund;</del></li> <li>● <del>the Inter-American Development Bank;</del></li> <li>● <del>the African Development Bank;</del></li> <li>● <del>the Asian Development Bank;</del></li> <li>● <del>the Caribbean Development Bank;</del></li> <li>● <del>the European Investment Bank;</del></li> <li>● <del>the European Community;</del></li> <li>● <del>the European Atomic Energy Community;</del></li> <li>● <del>the European Coal and Steel Community.</del></li> </ul>
<p><i>approved index</i></p>	<p>(a) an index which is -</p> <ul style="list-style-type: none"> <li>(i) calculated independently,</li> <li>(ii) published at least once every week,</li> <li>(iii) based on constituents, each of which is property falling within paragraphs (1) to (8) or (10) of Part I of <b>Appendix 3.2</b>, and</li> <li>(iv) calculated on a basis which is made available to the public and which includes both the rules for including and excluding constituents and the rules for valuation which must use an arithmetic average of the value of the constituents;</li> </ul> <p>(b) a national index of retail prices published by or under the authority of a government of a State belonging to Zone A as defined in the <i>Banking Co-ordination Consolidation Directive</i>; or</p>

	<p>(c) an index which is -</p> <p>(i) based on constituents, each of which is property falling within paragraphs (1) to (8) or (10) of Part I of <b>Appendix 3.2</b>, and</p> <p>(ii) in respect of which a <i>derivative contract</i> is listed</p>
<i>approved securities</i>	<p>any of the following -</p> <p>(a) any <i>securities</i> issued or guaranteed by, or the repayment of the principal of which, or the interest on which is guaranteed by, and any loans to or deposits with, any of the following, namely, any government, public or local authority or nationalised industry or undertaking, which belongs to Zone A as defined in the <i>Banking Co-ordination Consolidation Directive</i>;</p> <p>(b) any loan to, or deposit with, an <i>approved financial institution</i>; and</p> <p>(c) debentures issued prior to 31 December 1994 by the Agricultural Mortgage Corporation Ltd or the Scottish Agricultural Securities Corporation Ltd</p>
<del><i>assessable mutual</i></del>	<p><del>a mutual association—</del></p> <p><del>(a) where the <i>insurance business</i> carried on by the association is limited to the provision of insurance to its members; and</del></p> <p><del>(b) whose articles of association, rules or bye laws provide for the calling of additional contributions from members to meet claims</del></p>
<i>Asset Identification Rules</i>	the rules in Part I of Chapter 3
<i>authorised person</i>	a person who is authorised for the purposes of the <i>Act</i>
<i>AUTH</i>	<del>the Authorisation manual</del>



<i>available assets</i>	the excess of an <i>insurer's</i> assets (other than <i>implicit items</i> ) over its liabilities, in each case valued in accordance with the <i>Valuation of Assets Rules</i> and the <i>Determination of Liabilities Rules</i> and rule 2.10- <u>PRU 1.3</u> , <u>PRU 3.2</u> and <u>PRU 7</u>
<i>Banking Co-ordination Directive</i>	Council Directive of 20 March 2000, relating to the taking up and pursuit of the business of credit institutions (2000/12/EC)
<i>body corporate</i>	includes a body corporate constituted under the law of a country or territory outside the United Kingdom
<i>building society</i>	a building society within the meaning of the Building Societies Act 1986
<i>business amount</i>	(a) — for a company carrying on only <i>general insurance business</i> , the <i>general insurance business amount</i> ;  (b) — for a company carrying on only <i>long term insurance business</i> , the <i>long term insurance business amount</i> ; and  (c) — for a company carrying on both <i>general insurance business</i> and <i>long term insurance business</i> , in the case of its <i>general business assets</i> , the <i>general insurance business amount</i> and in the case of its <i>long term insurance business assets</i> , the <i>long term insurance business amount</i>
<i>business group</i>	a group comprising descriptions of <i>general insurance business</i> determined in accordance with rule 6.6
<i>business group maximum</i>	has the meaning given in Part III of <b>Appendix 6.1</b>
<i>charges for management</i>	amounts chargeable in respect of the management of an <i>internal linked fund</i> in accordance with the conditions of those <i>contracts of insurance</i> under which <i>property linked benefits</i> are linked to the value of the fund or units of the fund
<i>collective investment scheme</i>	has the meaning given in section 235 of the <i>Act</i>

<i>commission payable</i>	in relation to <del>long-term insurance business</del> , the amounts recorded during a <i>financial year</i> of the <i>insurer</i> as due to <del>intermediaries and cedants</del> in respect of the <i>inception</i> , amendment or renewal of <i>contracts of insurance</i> , whether or not paid during that year
<i>company</i>	(a) for the purposes of the <i>Accounts and Statements Rules</i> means an <i>insurance undertaking</i> ; and  (b) <del>otherwise for the purposes of the <i>Valuation of Assets Rules</i> and the <i>Determination of Liabilities Rules</i></del> , includes any <i>body corporate</i>
<i>contract for differences</i>	a contract for differences or any other contract the purpose or pretended purpose of which is to secure a profit or avoid a loss by reference to fluctuations in—  (a) <del>the value or price of property of any description; or</del>  (b) <del>an index or other factor designated for that purpose in the contract</del>
<i>contracts of insurance</i>	includes:  (a) <del>fidelity bonds, performance bonds, administration bonds, bail bonds, customs bonds, or similar contracts of guarantee effected in return for the payment of one or more premiums;</del>  (b) <del>tontines;</del>  (c) <del>when effected or carried out by a body that carries on the business of effecting or carrying out <i>contracts of insurance</i> apart from this paragraph, capital redemption contracts and <i>pension fund management contracts</i>;</del>  (d) <del>contracts to pay <i>annuities on human life</i>;</del>  (e) <del>contracts of a kind referred to in article 1(2)(e) of the <i>First Life Directive</i>; and</del>  (f) <del>contracts of a kind referred to in article 1(3) of the <i>First Life Directive</i></del>

<i>contractually based investment</i>	(a) — right under a <i>qualifying contract of insurance</i> ;  (b) — any investment of the kind specified by any of articles 83, 84, 85 of the <i>Regulated Activities Order</i> ; or  (c) — any investment of the kind specified by article 89 of the <i>Regulated Activities Order</i> so far as relevant to an investment falling within (a) or (b)
<i>credit insurance business</i>	<i>Insurance business</i> falling within <i>general insurance business class 14</i> that is not <i>reinsurance</i>
<i>Currency Matching and Localisation Rules</i>	the rules in Chapter 7
<i>dealings with or by a counterparty</i>	see <i>counterparty</i>
<i>debt security</i>	includes bonds, notes, debentures and debenture stock
<i>deferred acquisition costs</i>	those items shown at GII under the heading ‘Assets’ set out in paragraph 9 of Schedule 9A to the <i>Companies Act</i>
<i>dependant</i>	a <i>subsidiary undertaking</i> the value of whose <i>shares</i> is taken to be the value of its <i>surplus assets</i> under rule 4.2(1) or (1A)(a) a dependant is: (a) for a <i>firm</i> that is not a <i>participating insurance undertaking</i> (and so is not subject to <i>PRU 8.3.9R</i> ), any <i>subsidiary undertaking</i> that is valued in accordance with <i>PRU 1.3.35R</i> ; or (b) for a <i>firm</i> that is a <i>participating insurance undertaking</i> (and so is subject to <i>PRU 8.3.9R</i> as referred to in <i>PRU 2.1.9R(2)</i> ), any <i>subsidiary undertaking</i> that is either (1) a <i>regulated related undertaking</i> in respect of which no election has been made in accordance with <i>PRU TR 25R</i> , or (2) a <i>subsidiary undertaking</i> of the <i>firm</i> , not referred to in (1), that is valued in accordance with <i>PRU 1.3.35R</i> .
<i>deposit, and</i>	the deposit mentioned in rule 8.1, and

<i>depositor</i>	depositor means an <i>insurer</i> making (or intending to make) such a deposit
<i>deposit ——— back arrangement</i>	in relation to any contract of <i>reinsurance</i> , means an arrangement whereby an amount is deposited by the <i>reinsurer</i> with the <i>cedant</i>
<i>designated state or territory</i>	any <i>EEA State</i> (other than the United Kingdom), Switzerland, a state in the United States of America, the District of Columbia, Puerto Rico, Canada or a province of Canada, Australia, South Africa, Singapore and Hong Kong
<i>derivative contract</i>	a <i>contract for differences</i> , a <i>futures contract</i> or an <i>option</i> and includes a contract under which the amount payable by either party is calculated by reference to the <i>amortised value</i> of any property  has the meaning given to <i>derivative</i> in the <i>Glossary</i>
<i>Determination of Liabilities Rules</i>	the rules in Chapter 5
<i>Directive</i>	see—  <i>Investment Services Directive</i> <i>First Life Directive</i> <i>First Non-Life Directive</i> <i>Banking Co-ordination Directive</i> <i>Third Life Directive</i> <i>Third Non-Life Directive</i> <i>Life Assurance Directive</i>
<i>director</i>	in relation to a <i>body corporate</i> , includes—  (a) — person occupying in relation to it the position of a director (by whatever name called); and  (b) — a person in accordance with whose directions or instructions (not being advice given in a professional capacity) the directors of that body are accustomed to act
<i>EEA deposit insurer</i>	a <i>non-EEA insurer</i> which has made a <i>deposit</i> in an <i>EEA State</i> (other than the United Kingdom) in accordance with rule 8.1(2)

<i>EEA insurer</i>	an <i>insurer</i> , other than a <i>pure reinsurer</i> or a <i>non-directive insurer</i> , whose head office is in any <i>EEA State</i> except the United Kingdom and which has received authorisation under article 6 of the <i>First Life Directive</i> or of the <i>First Non-Life Directive</i> from its home state regulator
<i>EEA insurance parent undertaking</i>	an <i>insurance parent undertaking</i> that has its head office in the United Kingdom or another <i>EEA State</i>
<i>EEA margin of solvency</i>	the <i>margin of solvency</i> of an <i>insurer</i> computed by reference to the assets and liabilities of the business carried on by the <i>insurer</i> in <i>EEA States</i> (taken together) in accordance with rule 2.4(2)(b)
<i>EEA State</i> <sup>4</sup>	a State which is a contracting party to the agreement on the European Economic Area signed at Oporto on 2 May 1992 as it has effect for the time being
<i>equalisation reserve</i>	a reserve to be maintained under the <i>Equalisation Reserves Rules</i>
<i>Equalisation Reserves Rules</i>	the rules in Chapter 6
<i>equity share capital</i>	in relation to a <i>company</i> , its issued <i>share capital</i> excluding any part which, neither as respects dividends nor as respects capital, carries any right to participate beyond a specified amount in a distribution
<i>excess concentration with a number of counterparties</i>	is determined in accordance with paragraph 17 of <b>Appendix 4.2</b>
<i>exposure</i>	(a) — in relation to assets, means an amount determined in accordance with rule 4.14 and paragraphs 4 to 11A of <b>Appendix 4.2</b> ; and  (b) — in relation to a <i>counterparty</i> , means an amount terminated in accordance with rule 4.14 and paragraphs 13 to 15A of <b>Appendix 4.2</b>
<i>external insurer</i>	an <i>insurer</i> whose head office is outside the United

<sup>4</sup> These comprise the 15 EU states (ie the United Kingdom, Portugal, Spain, France, Italy, Ireland, Belgium, Luxembourg, the Netherlands, Denmark, Germany, Greece, Austria, Sweden and Finland) plus Norway, Iceland and Liechtenstein.

	Kingdom, other than an <i>EEA-insurer</i> , a <i>Swiss general insurer</i> or an <i>insurer</i> to which rule 8.1(2) applies <u>UK- or EEA-deposit insurer</u> .
<i>financial year</i>	(a) — for the purposes of the <i>Equalisation Reserves Rules</i> , a period of account; and  (b) — for all other purposes, each period at the end of which the balance of the accounts of the <i>insurer</i> is struck or, if no such balance is struck, the calendar year
<i>firm</i>	an <i>authorised person</i>
<i>first calculation</i>	in relation to the <i>Margins of Solvency Rules</i> , is the calculation described in rules 2.5(1) and (2)
<i>First Life Directive</i>	Council Directive (79/267/EEC) of 5 March 1979 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct life assurance
<i>First Non-Life Directive</i>	Council Directive (73/239/EEC) of 24 July 1973 on the coordination of laws, regulations and administrative provisions relating to the taking up and pursuit of the business of direct insurance other than life insurance
<i>fixed interest securities</i>	<i>securities</i> which under their terms of issue provide for fixed amounts of interest
<i>friendly society</i>	an <i>incorporated friendly society</i> or <i>registered friendly society</i>
<i>futures contract</i>	a contract for the sale or delivery of a commodity or property of any other description under which delivery is to be made at a future date and at a price agreed on when the contract is made
<i>FSA</i>	Financial Services Authority
<i>general insurance business</i>	the business of effecting or carrying out <i>general insurance contracts</i>
<i>general insurance business amount</i>	is the higher of—  (a) — the total of:

	<p>(i) — <del>the insurer's insurance liabilities (net of reinsurance ceded) in respect of general insurance business less debts –</del></p> <p style="padding-left: 40px;">(A) — <del>which are due from dependants to which paragraph 11C of Part I of Appendix 4.2 relates;</del></p> <p style="padding-left: 40px;">(B) — <del>which are not reinsurance which has already been netted off the insurer's insurance liabilities; and</del></p> <p style="padding-left: 40px;">(C) — <del>which are included in general insurance business assets;</del></p> <p style="padding-left: 40px;"><del>which amount is to be zero where the debts are greater than the insurer's insurance liabilities; and</del></p> <p>(ii) — <del>an amount equal to whichever is the greater of 400,000 Euro or 20% of the general premium income; or</del></p> <p>(b) — <del>such other amount as the insurer may select not exceeding:-</del></p> <p style="padding-left: 40px;">(i) — <del>the value of its general insurance business assets as determined in accordance with the Valuation of Assets Rules;</del></p> <p style="padding-left: 40px;">(ii) — <del>excluding debts due from dependants to which paragraph 11C of Part I of Appendix 4.2 relates and reinsurance recoveries; and</del></p> <p style="padding-left: 40px;">(iii) — <del>less debts due to dependants of the insurer included in general insurance business liabilities (excluding reinsurance recoveries, other than amounts due or that relate to claims already paid by the dependant) except that for a dependant to which paragraph 11C of Part I of Appendix 4.2 does not relate, the amount deducted will not exceed the dependant's surplus assets (or proportional share)</del></p>
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<i>general insurance business assets, and general insurance business liabilities</i>	respectively assets and liabilities of an <i>insurer</i> which are not <i>long-term insurance business assets</i> or <i>long-term insurance business liabilities</i>
<i>general insurance contract</i>	any <i>contract of insurance</i> falling within Part I of <b>Annex 11.2</b>
<i>general insurer</i>	an <i>insurer</i> whose business includes effecting or carrying out <i>general insurance contracts</i>
<i>general policy</i>	a policy evidencing a contract the effecting or carrying out of which constitutes the carrying on of <i>general insurance business</i>
<i>general premium income</i>	in any year, the net amount, after deduction of any premiums payable for <i>reinsurance</i> , of the premiums receivable in that year in respect of all <i>insurance business</i> other than <i>long-term insurance business</i>
<i>gross premiums</i>	in relation to an <i>insurer</i> and a <i>financial year</i> —  (a) — means premiums after deduction of discounts, refunds and rebates of premium but before deduction of premiums for <i>reinsurance ceded</i> and before deduction of <i>commission payable</i> by the <i>insurer</i> ; and  (b) — includes premiums receivable by the <i>insurer</i> under <i>reinsurance</i> contracts accepted by the <i>insurer</i>
<i>gross premiums earned</i>	in respect of a <i>financial year</i> , such proportion of <i>gross premiums written</i> or <i>gross premiums receivable</i> , as the case may be, as is attributable to risk borne by the <i>insurer</i> during that <i>financial year</i> .
<i>gross premiums written</i>	the amounts required by the <i>insurance accounts rules</i> to be shown in the <i>profit and loss account</i> of a <i>company</i> at general business technical account item I.1.(a), or for <i>class IV insurance business</i> , at <i>long-term business</i> technical account item II.1(a).



<i>group undertaking</i>	any of:  (a) — the <i>insurer</i> ;  (b) — its <i>related undertakings</i> ;  (c) — its <i>participating undertakings</i> ; and  (d) — the <i>related undertakings</i> of its <i>participating undertakings</i>
<i>guarantee fund</i>	has the meaning given in rule 2.9
<i>holding company</i>	is construed in accordance with section 736 of the <i>Companies Act</i> or Article 4 of the <i>1986 Order</i>
<i>hybrid linked contract</i>	<del>a contract of insurance</del> the effecting of which constitutes the carrying on of <i>long term insurance business</i> and which contains an option such that at some future time the contract may, according to how such option is exercised, constitute either a <i>linked contract</i> or a <i>non-linked contract</i>
<i>implicit item</i>	has the meaning given in rule 2.10(5)
<i>incorporated friendly society</i>	a society incorporated under the Friendly Societies Act 1992
<i>index linked benefits</i>	<del>benefits—</del>  (a) — provided for under a <i>linked long-term contract</i> ; and  (b) — determined by reference to an index of the value of property of any description (whether specified in the contract or not)
<i>index linked contract</i>	a <i>linked long-term contract of insurance</i> conferring <i>index-linked benefits</i>
<i>index linked liabilities</i>	<i>insurance liabilities</i> in respect of <i>index-linked benefits</i>

<i>industrial and provident society</i>	a society registered or deemed to be registered under the Industrial and Provident Societies Act 1965 or the Industrial and Provident Societies Act (Northern Ireland) 1969
<i>insurance accounts rules</i>	Schedule 9A to the <i>Companies Act</i> and Schedule 9A to the <i>1986 Order</i> for the preparation of accounts by <i>insurance undertakings</i>
<i>Insurance Accounts Directive</i>	Council Directive 91/674/EEC of 19 December 1991 on annual accounts and consolidated accounts of insurance undertakings
<i>insurance business</i>	the business of effecting or carrying out <i>contracts of insurance</i> as principal
<i>insurance group</i>	an <i>insurance parent undertaking</i> and its <i>related undertakings</i> that are—  (a) — <i>insurance undertakings</i> ; or  (b) — <i>insurance holding companies</i>
<i>Insurance Groups Directive</i>	Directive of the European Parliament and of the Council of 27 October 1998 on the supplementary supervision of insurance undertakings in an insurance group (1998/78/EC)
<i>insurance holding company</i>	an undertaking whose main business is to acquire and hold <i>participations in subsidiary undertakings</i> , where those <i>subsidiary undertakings</i> are exclusively or mainly <i>insurance undertakings</i>
<i>insurance liabilities</i>	amounts calculated in accordance with the <i>Determination of Liabilities Rules-PRU 1.3 (Valuation)</i> in respect of those items shown at C and D under the heading ‘Liabilities’ set out in paragraph 9 of the <i>insurance accounts rules</i>
<i>insurance parent undertaking</i>	in relation to an <i>insurer</i> , is a <i>parent undertaking</i> of that <i>insurer</i> which is either itself an <i>insurance undertaking</i> or an <i>insurance holding company</i>
<i>insurance undertaking</i>	an undertaking, whether or not an <i>insurer</i> , which carries on <i>insurance business</i>

<i>insurer</i>	a <i>firm</i> with permission under the <i>Act</i> to effect or carry out <i>contracts of insurance</i> , other than a bank
<i>intermediary</i>	a person who in the course of any business or profession invites other persons to make offers or proposals or to take other steps with a view to entering into <i>contracts of insurance</i> with an <i>insurer</i> , other than a person who only publishes such invitations on behalf of, or to the order of, some other person
<i>Investment Services Directive</i>	Council Directive of 10 May 1993 on investment services in the securities field (93/22/EEC)
<i>IPRU (INS)</i>	Interim Prudential Sourcebook for Insurers
<i>IPRU (FSOC)</i>	Interim Prudential Sourcebook for Friendly Societies
<i>issuer</i>	in respect of a <i>collective investment scheme</i> , means the manager or operator of the scheme and in respect of an interest in a limited partnership, means the partnership
<i>leading insurance undertaking</i>	in relation to a <i>relevant co-insurance operation</i> , means an <i>insurance undertaking</i> which—  (a) — is recognised as the leading insurance undertaking by the other <i>insurance undertakings</i> involved in the operation; and  (b) — determines the terms and conditions of insurance for the operation
<i>linked long-term contract</i>	a contract of the kind described in rule 2.3(4), and  linked contract and non-linked contract are construed accordingly
<i>LLD</i>	the Lloyd's Sourcebook
<i>localisation</i>	existence of assets, whether moveable or immovable, in a State
<i>long-term insurance business</i>	the business of effecting or carrying out <i>long-term insurance contracts</i>

<i>long-term insurance business amount</i>	<p>is the higher of—</p> <p>(a) — the total of—</p> <p style="padding-left: 40px;">(i) — the <i>insurer's insurance liabilities</i> in respect of <i>long-term insurance business</i> (net of <i>reinsurance ceded</i>) and the amount of any deposit back under a <i>deposit back arrangement</i> in relation to a contract of <i>reinsurance</i> in respect of <i>long-term insurance business</i>;</p> <p style="padding-left: 80px;">(A) — <i>excluding property linked liabilities</i>, and</p> <p style="padding-left: 80px;">(B) — less the amount of any <i>debt</i>, that is a <i>long-term insurance business asset</i> (excluding <i>reinsurance</i> that has already been netted off the <i>insurer's insurance liabilities</i>), due from a <i>dependant</i> to which paragraph 11C of Part I of Appendix 4.2 relates, and</p> <p style="padding-left: 80px;">(C) — less the amount of any <i>implicit item</i> valued in accordance with a waiver under section 148 of the <i>Act</i>,</p> <p style="padding-left: 40px;">adjusted to zero where the result is negative; and</p> <p style="padding-left: 40px;">(ii) — the amount of the <i>required margin of solvency</i> for its <i>long-term insurance business</i> (or the amount of the <i>minimum guarantee fund</i> if greater) determined in accordance with rules 2.5 to 2.9 and 2.4(3) (or, in the case of an <i>insurer</i> whose head office is not in the United Kingdom, that amount which would apply if its head office were in the United Kingdom) or</p> <p>(b) — such other amount as the <i>insurer</i> may select not exceeding the value of its assets valued in accordance with the <i>Valuation of Assets Rules</i>:</p>
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(i) — ~~excluding:~~

(A) — ~~reinsurance recoveries;~~

(B) — ~~assets required to match property linked liabilities;~~

(C) — ~~debts due from dependants of the insurer to which paragraph 11C of Part I of Appendix 4.2 relates; and~~

(D) — ~~if the insurer is a general insurer, general insurance business assets, and~~

(ii) — ~~less:~~

(A) — ~~if the insurer is a general insurer, debts due to dependants of the insurer included in long-term insurance business liabilities (excluding reinsurance recoveries (other than amounts due or that relate to claims already paid by the dependant)), or~~

(B) — ~~if the insurer is not a general insurer, debts due to dependants of the insurer (excluding reinsurance recoveries (other than amounts due or that relate to claims already paid by the dependant)),~~

~~but for the purposes of (ii) above, for dependants to which paragraph 11C of Part I of Appendix 4.2 does not relate, the amount deducted will not exceed the dependant's surplus assets (or proportional share);~~

~~except that for the purposes of determining the permitted asset exposure limit under paragraph 2 of Part 1 of **Appendix 4.2**, index linked liabilities must also be excluded from (a)(i) and assets~~

	required to match such liabilities must be also excluded from (b)
<del>long-term insurance business assets, and long-term insurance business liabilities</del>	respectively assets of an <i>insurer</i> which are, for the time being, identified as representing the <i>long-term insurance fund or funds</i> , and liabilities of an <i>insurer</i> arising under or in connection with its <i>long-term insurance business</i> , including arising from <i>deposit back arrangements</i>
<del>long-term insurance contract</del>	any <i>contract of insurance</i> falling within <b>Annex 11.1</b>
<del>long-term insurance fund</del>	a fund maintained under rule 3.1
<del>long-term insurer</del>	an <i>insurer</i> whose business includes effecting or carrying out <i>long-term insurance contracts</i>
<del>majority shareholder controller</del>	a <i>shareholder controller</i> whose shareholding is such that the <i>insurer</i> is his <i>subsidiary undertaking</i>
<del>margin of solvency</del>	is the excess of the value of assets over the amount of liabilities, that value and amount being determined in accordance with the <i>Valuation of Assets Rules</i> , the <i>Determination of Liabilities Rules</i> and rule 2.10
<del>Margins of Solvency Rules</del>	the rules in Chapter 2
<del>market value</del>	in Appendix 3.2 the market value as determined in accordance with generally accepted accounting concepts, bases and policies or other generally accepted methods appropriate to <i>insurers</i>
<del>material connected-party transaction</del>	a <i>connected-party transaction</i> for which (together with any similar transactions): <ul style="list-style-type: none"> <li>(a) the price actually paid or received for the transfer of assets or liabilities or the performance of services; or</li> <li>(b) the price which would have been paid or received had that transaction been negotiated at arm's length between unconnected parties,</li> </ul>

	<p>exceeds:</p> <p>(c) in the case of an <i>insurer</i> that carries on either <del><i>general insurance business or long-term insurance business</i></del>, but not both, 5% of the <del><i>general insurance business amount or long-term business insurance amount</i></del>, as applicable – <u><i>long-term insurance business</i></u> but not <u><i>general insurance business</i></u>, 5% of the <u><i>insurer's liabilities arising from its long-term insurance business, excluding property-linked liabilities and net of reinsurance ceded</i></u>; or</p> <p>(d) in the case of an <i>insurer</i> that carries on <u><i>general insurance business</i></u>, but not <u><i>long-term insurance business</i></u>, the sum of Euro 20,000 and 5% of the <u><i>insurer's liabilities arising from its general insurance business, net of reinsurance ceded</i></u>; or</p> <p><del>(d)</del>(e) in the case of an <i>insurer</i> that carries on both types of business either –</p> <p>(i) 5% of the <del><i>long-term insurance business amount</i></del> of the <u><i>insurer's liabilities arising from its long-term insurance business, excluding property-linked liabilities, net of reinsurance ceded</i></u> where the transaction is in connection with the <u><i>insurer's long-term insurance business</i></u>, or</p> <p>(ii) in other cases, <u>the sum of Euro 20,000 and 5% of the <i>insurer's liabilities arising from general insurance business net of reinsurance ceded</i> 5% of the <i>general insurance business amount</i></u></p>
<i>maximum reserve</i>	For the purposes of the <i>Equalisation Reserves Rules</i> , the aggregate value of the <i>business group maxima</i> calculated in accordance with Part III of <b>Appendix 6.1</b>
<i>the minimum</i>	in relation to a <i>deposit</i> , means one half of the <i>minimum guarantee fund</i> appropriate to the <i>margin of solvency</i> which the <i>insurer</i> is required to maintain under rule 2.1(2)(b) or 2.1(3)(e)

<i>minimum-guarantee fund</i>	has the meaning given in rule 2.9
<i>mutual</i>	An <i>insurer</i> which—  (a) — if it is a <i>body corporate</i> has no share capital; or  (b) — a <i>registered society</i>
<i>net claims incurred</i>	in respect of a <i>financial year</i> means <i>claims</i> arising from incidents occurring during that <i>financial year</i> (including direct <i>claims</i> handling expenses), net of <i>reinsurance</i> and other recoveries but excluding <i>claims management costs</i>
<i>net claims paid</i>	in respect of a <i>financial year</i> means <i>claims</i> paid during that <i>financial year</i> (including direct <i>claims</i> handling expenses), net of <i>reinsurance</i> and other recoveries but excluding <i>claims management costs</i> , regardless of whether incidents giving rise to such <i>claims</i> occurred during that <i>financial year</i> or any preceding <i>financial year</i>
<i>net operating expenses</i>	the net amount paid in a <i>financial year</i> in respect of commissions, other acquisition expenses, administrative expenses, <i>reinsurance</i> commissions and profit participations
<i>net premiums earned, and net premiums written</i>	respectively, <i>gross premiums earned</i> , net of <i>reinsurance</i> premiums earned and <i>gross premiums written</i> , net of <i>reinsurance</i> premiums payable under <i>reinsurance ceded</i>
<i>non-directive insurer</i>	(1) — an <i>insurer</i> whose <i>insurance business</i> is restricted to the provision of benefits which vary according to the resources available and in which the contributions of the members are determined on a flat-rate basis;  (2) — an <i>insurer</i> whose <i>long-term insurance business</i> is restricted to the provision of benefits for employed and self-employed persons belonging to an undertaking or group of undertakings, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the <i>commitments</i> arising from such operations are fully covered at all times)



	<p>by <i>mathematical reserves</i>);</p> <p>(3) — an <i>insurer</i> which undertakes to provide benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind;</p> <p>(4) — a <i>mutual</i> (carrying on <i>long term insurance business</i>) —</p> <p>(a) — whose articles of association contain provisions for calling up additional contributions from members or reducing their benefits or claiming assistance from other persons who have undertaken to provide it; and</p> <p>(b) — whose annual <i>gross premium</i> income (other than from contracts of <i>reinsurance</i>) has not exceeded 5 million Euro for each of the <i>financial year in question</i> and the two <i>previous financial years</i>;</p> <p>(5) — a <i>mutual</i> (carrying on <i>general insurance business</i>) whose —</p> <p>(a) — articles of association contain provisions for calling up additional contributions from members or reducing their benefits;</p> <p>(b) — business does not cover liability risks, other than <i>ancillary risks</i>, or credit or suretyship risks;</p> <p>(c) — <i>gross premium</i> income (other than from contracts of <i>reinsurance</i>) for the <i>financial year in question</i> did not exceed 5 million Euro; and</p> <p>(d) — members provided at least half of that <i>gross premium</i> income;</p> <p>(6) — an <i>insurer</i> whose <i>insurance business</i> (other than <i>reinsurance</i>) is —</p>
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	<p>(a) <del>restricted to the provision of assistance for persons who get into difficulties while travelling, while away from home or while away from their permanent residence;</del></p> <p>(b) <del>carried out exclusively on a local basis and consists only of benefits in kind; and</del></p> <p>(c) <del>such that the gross premium income from the provision of assistance in the financial year in question did not exceed 200,000 Euro; or</del></p> <p>(7) <del>a mutual whose liabilities in respect of general insurance contracts are fully reinsured with or guaranteed by other mutuals (including friendly societies); and</del></p> <p><del>whose insurance business is limited to that described in paragraphs (1) to (7)</del></p>
<i>non-EEA insurer</i>	An insurer, other than a pure reinsurer, whose head office is not in an EEA State
<i>non-linked contract</i>	see <i>linked long-term contract</i>
<i>notional group solvency margin</i>	<p>in relation to an <i>ultimate insurance parent undertaking</i> or an <i>ultimate EEA insurance parent undertaking</i>, the sum of:</p> <p>(a) <del>the notional required minimum margin (if any) of that parent; and</del></p> <p>(b) <del>the sum of that parent's proportional shares of the notional required minimum margins of its related insurance undertakings</del></p>

<i>notional required minimum margin</i>	<p>(a) — in the case of an <i>insurance undertaking</i> (other than a <i>pure reinsurer</i>) that has its head office in a <i>designated state or territory</i>, the amount of the <i>required minimum margin</i>, or the equivalent requirement under the regulatory requirements of that state or territory;</p> <p>(b) — in the case of a <i>pure reinsurer</i> that has its head office in a <i>designated state or territory</i>, the amount that would be the <i>required minimum margin</i>, or the equivalent requirement under the regulatory requirements of that state or territory, if the regulatory requirements of that state or territory applicable to undertakings carrying on <i>direct insurance business</i> were applied to the <i>pure reinsurer</i> (whether they are or not); and</p> <p>(c) — in all other cases, the amount of the <i>required minimum margin</i> that would apply if the <i>insurance undertaking</i> were an <i>insurer</i> (other than a <i>pure reinsurer</i>), with its head office in the United Kingdom (whether it is or not)</p>
<i>nuclear installation</i>	any installation prescribed by the Nuclear Installations Regulations 1971
<i>nuclear matter, and nuclear reactor</i>	have the same meanings as in the Nuclear Installations Act 1965
<i>nuclear risks</i>	risks falling within any <i>class of general insurance business</i> and arising in connection with the construction or use of any <i>nuclear reactor</i> or <i>nuclear installation</i> or the carriage of any <i>nuclear matter</i>

<i>option</i>	<p>an option to acquire or dispose of—</p> <p>(a) — an investment falling within any of articles 76 to 82 or, so far as relevant to those articles, within article 89 of the <i>Regulated Activities Order</i>;</p> <p>(b) — a <i>contractually based investment</i>;</p> <p>(c) — currency of the United Kingdom or of any other country or territory;</p> <p>(d) — palladium, platinum, gold or silver; or</p> <p>(e) — an investment falling within this definition by virtue of (a), (b), (c) or (d);</p> <p>or a <i>warrant</i></p>
<i>parent undertaking</i>	is construed in accordance with section 258 of the <i>Companies Act</i> and article 266 of the <i>1986 Order</i>
<i>parent undertaking solvency calculation</i>	the calculation required under rule 10.2(3)(a)
<i>participating undertaking</i>	an undertaking which holds a <i>participation</i> in the undertaking in question
<i>participation</i>	<p>(a) — the holding of a participating interest within the meaning of section 421(2) of the <i>Act</i>; or</p> <p>(b) — the holding, directly or indirectly, of 20% or more of the voting rights or capital</p>
<i>Part II business, and Part III business</i>	the <i>insurance business</i> to which Part II and Part III, respectively, of the <i>Equalisation Reserves Rules</i> applies
<i>Part II insurer, and Part III insurer</i>	an <i>insurer</i> to which <i>Part II</i> and <i>Part III</i> , respectively, of the <i>Equalisation Reserves Rules</i> applies

<i>pension fund management contract</i>	means a contract to manage the investments of pension funds (other than funds solely for the benefit of the officers or employees of the person effecting or carrying out the contract and their dependants or, in the case of a <i>company</i> , partly for the benefit of officers or employees and their dependants of its <i>subsidiary</i> or <i>holding company</i> or a <i>subsidiary</i> of its <i>holding company</i> )
<i>period of risk</i>	the period for which a <i>contract of insurance</i> provides cover
<i>permanent health contract</i>	a contract falling within <i>class IV</i> of <i>long term insurance contracts</i>
<i>permitted asset exposure limit</i>	has the meaning given in paragraph 2 of <b>Appendix 4.2</b>
<i>permitted connected property</i>	property of any of the descriptions in paragraphs 1 to 8 or 10 of Part I of <b>Appendix 3.2</b> , which is not property falling within rule 3.7(3)
<i>permitted counterparty exposure limit</i>	has the meaning set out in paragraph 3 of <b>Appendix 4.2</b>
<i>permitted derivative contract</i>	for the purpose of <b>Appendix 3.2</b> , a <i>derivative contract</i> or <i>quasi-derivative</i>  (a) — which is 'covered' and  (i) — which is held in connection with 'property' for the purposes of reduction of investment risk or efficient portfolio management, or  (ii) — which has the effect of a <i>permitted derivative contract</i> held in connection with 'property' for such purposes; and  (b) — which satisfies the conditions in rules 4.12(6) to (8) except that the references in rule 4.12 to 'an

asset for the valuation of which provision is made in the *Valuation of Assets Rules* is construed as a reference to *permitted connected property*;

which satisfies the requirements of PRU 4.3 with the exception of PRU 4.3.18R, as applied in relation to assets covering liabilities in respect of linked long- term contracts of insurance, amended as follows:

(a) in PRU 4.3.5R and PRU 4.3.36R, "For the purpose of PRU 2 Ann 1R (Admissible assets in insurance)" is replaced by "For the purposes of IPRU (INS) rules 3.6 and 3.7 and Appendix 3.2";

(b) in PRU 4.3.6R (2) and (3), PRU 4.3.7R (1) and (2), PRU 4.3.17R (1) and PRU 4.3.36R (1) "admissible assets" is replaced by "permitted connected property";

(c) PRU 4.3.12R (2) and (3) are replaced by:

"(2) (where they are held to cover index-linked liabilities) might:

(a) not be appropriate cover for those liabilities as required by PRU 4.2.58R; or

(b) fall in value; and

(3) (where they are held to cover property-linked liabilities) might:

(a) not be appropriately selected in accordance with contractual and constructive liabilities as required by PRU 7.6.36R and appropriate cover for those liabilities as required by PRU 4.2.57R; or

	(b) <u>fall in value</u> ".
<i>permitted securities</i>	<del>securities in which cash under the control of or subject to the order of the Supreme Court may be invested pursuant to the relevant rules of court</del>
<i>policy</i>	<p>(a) <del>in relation to <i>long-term insurance business</i> and <i>industrial assurance business</i>, includes an instrument evidencing a contract to pay an <i>annuity upon human life</i>;</del></p> <p>(b) <del>in relation to <i>insurance business</i> of any other kind, includes any policy under which there is for the time being an existing liability already accrued or under which a liability may accrue; and</del></p> <p>(c) <del>in relation to capital redemption <i>insurance business</i>, includes any policy, bond, certificate, receipt or other instrument evidencing the <i>contract of insurance</i> with the <i>insurer</i></del></p>
<i>Policy holder</i>	<p>the person who for the time being is the legal holder of the <i>policy</i> for securing the contract with the <i>insurer</i>, and—</p> <p>(a) <del>in relation to such <i>long-term insurance business</i> or <i>industrial assurance business</i> as consists in the granting of <i>annuities upon human life</i>, includes an annuitant; and</del></p> <p>(b) <del>in relation to <i>insurance business</i> of any other kind, includes a person to whom, under a <i>policy</i>, a sum is due or a periodic payment is payable</del></p>
<i>proper valuation</i>	<del>in relation to land, a valuation made by a <i>qualified valuer</i> not more than three years before the <i>relevant date</i> which determined the amount which would be realised at the time of the valuation on an open market sale of the land free from any <i>mortgage</i> or charge</del>
<i>property linked benefits</i>	benefits other than <i>index linked benefits</i> provided for under a <i>linked long-term contract of insurance</i> .

<i>property linked contract</i>	a linked long-term contract <i>of insurance</i> conferring <i>property linked benefits</i> .
<i>proportional share</i>	in relation to a <i>related undertaking</i> , the percentage which is the percentage holding (directly or indirectly) in the <i>related undertaking's</i> capital
<i>pure reinsurer</i>	an <i>insurer</i> whose <i>insurance business</i> is as a matter of fact restricted to effecting or carrying out contracts of <i>reinsurance</i>
<i>qualified valuer</i>	<p>in relation to any particular type of land in any particular area, means—</p> <p>(a) — a person who is a fellow or professional associate of the Royal Institution of Chartered Surveyors or a fellow or associate of the Incorporated Society of Valuers and Auctioneers or a fellow or associate of the Rating and Valuation Association and either—</p> <p>(i) — has knowledge of and experience in the valuation of that particular type of land in that particular area; or</p> <p>(ii) — has knowledge of and experience in the valuation of land and has taken advice from a valuer who he is satisfied has knowledge of and experience in the valuation of that particular type of land in that particular area; or</p> <p>(b) — a person who conforms with (a)(i) or (ii) and immediately before 15 June 1981 was recognised as a qualified valuer by virtue of an approval by the Secretary of State under the Insurance Companies (Valuation of Assets) Regulations 1976 (and for these purposes an approval given under the Insurance Companies (Valuation of Assets) Regulations 1974 is deemed to have been given under the 1976 Regulations)</p>
<i>qualifying contract of insurance</i>	<p>means a <i>long-term insurance contract</i> which is not</p> <p>(a) — a <i>reinsurance contract</i>; or</p> <p>(b) — a contract in respect of which the following</p>



	<p><del>conditions are met—</del></p> <p><del>(i) the benefits under the contract are payable only on death or in respect of incapacity due to injury, sickness or infirmity;</del></p> <p><del>(ii) the contract provides that benefits are payable on death (other than death due to an accident) only where the death occurs within ten years of the date on which the life of the person in question was first insured under the contract, or where the death occurs before that person attains a specified age not exceeding seventy years;</del></p> <p><del>(iii) the contract has no surrender value, or the consideration consists of a single premium and the surrender value does not exceed that premium; and</del></p> <p><del>(iv) the contract makes no provision for its conversion or extension in a manner which would result in it ceasing to comply with any of the above conditions</del></p>
<p><i>readily realisable</i></p>	<p>in <u>Appendix 3.2</u>, in relation to an investment:</p> <p>(a) an investment which, had negotiations for the assignment or transfer of the investment commenced not more than seven working days before the <i>relevant date</i>, it is reasonable to assume could have been assigned or transferred on the <i>relevant date</i> for an amount not less than 97.5% of the <i>market value</i> to a person other than the <i>issuer</i> or an <i>associate</i> or <i>associated company</i> of the <i>issuer</i> or of the <i>insurer</i>; or</p> <p>(b) a <i>listed</i> investment with respect to which (a) does not apply by reason only that -</p> <p>(i) the listing of the investment has been temporarily suspended following receipt of price sensitive information received by the stock exchange on which the investment is <i>listed</i> or the <i>regulated market</i> on which facilities for dealing have been granted, or</p>

	(ii) the extent of the holding would prevent an orderly disposal of the investment for an amount equal to or greater than 97.5% of <i>market value</i>
<i>recoverable</i>	in relation to an <i>insurer</i> and a <i>financial year</i> , means recorded in the <i>insurer's</i> books as due in that year, whether or not the <i>insurer</i> has received any payment
<i>registered friendly society</i>	a society which is—  (a) a friendly society within the meaning of section 7(1)(a) of the Friendly Societies Act 1974; and  (b) registered within the meaning of that Act
<i>registered society</i>	a society registered or deemed to be registered under the Industrial and Provident Societies Act 1965 or the Industrial and Provident Societies Act (Northern Ireland) 1969
<i>Regulated Activities Order</i>	Financial Services and Markets Act (Regulated Activities) Order (S.I. 2001 No. 544)
<i>regulated activity</i>	is construed in accordance with the <i>Regulated Activities Order</i>
<i>regulated institution</i>	any of the following—  (a) an <i>EEA insurer</i> or <i>UK insurer</i> ;  (b) an <i>approved credit institution</i> ;  (c) a <i>friendly society</i> which is authorised to carry on <i>insurance business</i> ; and  (d) an <i>approved investment firm</i>
<i>reinsurance, and reinsurer</i>	include retrocession and retrocessionaire respectively
<i>related undertaking</i>	an undertaking in which a <i>participation</i> is held by another undertaking or which is a <i>subsidiary undertaking</i>

<i>relevant co-insurance operation</i>	has the meaning given in <b>Appendix 5.1</b>
<i>relevant date</i>	in relation to the valuation of any asset or liability, the date at which the value of the asset or liability falls to be determined for the purposes of reporting under the <i>Accounts and Statements Rules</i> any purpose for which the <i>Valuation of Assets Rules</i> apply, the date when the asset falls to be valued for that purpose and in relation to the determination of any liability for any purpose for which the <i>Determination of Liabilities Rules</i> apply, the date when the liability falls to be determined for that purpose
<i>relevant insurer</i>	in relation to a <i>relevant co-insurance operation</i> , an <i>insurer</i> which is concerned in the operation but is not the <i>leading insurance undertaking</i>
<i>relevant regulatory requirements</i>	<p>(a) — in the case of a <i>group undertaking</i> that is an <i>insurance undertaking</i>, <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> established in a <i>designated state or territory</i>, at the option of the <i>insurer</i>:</p> <p>(i) — the regulatory requirements of that state or territory applicable to an undertaking carrying on <i>direct insurance business</i> (even if it only carries on <i>reinsurance business</i> or is an <i>insurance holding company</i>), or</p> <p>(ii) — the requirements referred to in (b); and</p> <p>(b) — in the case of any other <i>insurance undertaking</i> or <i>insurance holding company</i>, the rules in <i>IPRU (INS)</i> applicable to an <i>insurer</i> (other than a <i>pure reinsurer</i>) with its head office in the United Kingdom (whether or not it is such an <i>insurer</i>)</p>
<i>required margin of solvency</i>	a <i>margin of solvency</i> required by rule 2.1
<i>required minimum margin</i>	the greater of the appropriate <i>required margin of solvency</i> and the amount of the appropriate <i>guarantee fund</i> ; and  ‘required EEA minimum margin’ and ‘required United

	Kingdom minimum margin' are construed accordingly
<i>salvage right</i>	any right of an <i>insurer</i> under a <i>contract of insurance</i> to take possession of and to dispose of property by virtue of the fact that the <i>insurer</i> has made a payment or has become liable to make a payment in respect of a loss under the contract
<i>second calculation</i>	is the calculation described in rule 2(5)(1) and 2.5(3) to (6)
<i>secured debt</i>	<p>(1) — a <i>debt</i> owed to (or an obligation to be fulfilled for the benefit of) an <i>insurer</i> to the extent it is—</p> <p>(a) — secured by—</p> <p style="padding-left: 40px;">(i) — a letter of credit established with an <i>approved credit institution</i>, or</p> <p style="padding-left: 40px;">(ii) — a guarantee provided by an <i>approved credit institution</i>;</p> <p>where the sum of the aggregate amount available under all letters of credit established for the benefit of the <i>insurer</i> with the same <i>counterparty</i>; the aggregate amount of all guarantees issued for the benefit of the <i>insurer</i> by that <i>counterparty</i> and the amount of any <i>exposure</i> of the <i>insurer</i> to that <i>counterparty</i> does not exceed the <i>permitted counterparty exposure limit</i> for that <i>counterparty</i>; or</p> <p>(b) — secured by assets for the valuation of which provision is made in the <i>Valuation of Assets Rules</i> and—</p> <p style="padding-left: 40px;">(i) — the value of such assets (after deducting reasonable expenses of sale and the amount of any other <i>debt</i> or obligation secured by the assets having priority to in ranking equally with the <i>debt</i> or obligation) is sufficient to enable the <i>debt</i> or obligation to be discharged in full,</p>

(ii) — the value of the assets when aggregated with the *insurer's exposure* to assets of the same description does not exceed the *permitted exposure limit* for assets of that description (as calculated under rule 4.14 of **Appendix 4.2**); and

(iii) — where the assets give rise to *exposure to a counterparty*, the exposure of the *insurer* to that *counterparty*, when added to the aggregate amount available under all letters of credit established for the benefit of the *insurer* with that *counterparty*, and to the aggregate amount of all guarantees issued for the benefit of the *insurer* by that *counterparty*, does not exceed the *permitted counterparty exposure limit* for that *counterparty*;

(2) — for the purpose of (1) —

(a) — the aggregate amount available under letters of credit established with a *counterparty* must be taken not to exceed the sum of the aggregate amount of all *debts* and the aggregate value of all obligations in respect of which those letters of credit were established;

(b) — the aggregate amount of guarantees issued by a *counterparty* must be taken not to exceed the sum of the aggregate amount of all *debts* and the aggregate value of all obligations so guaranteed; and

(c) — assets which are securing any other *debt* owed to (or obligation to be fulfilled for the benefit of) the *insurer* must be treated as if they were assets of the *insurer*;

and unsecured debt is construed accordingly

	<p>a debt fully secured on:</p> <p>(a) <u>assets whose value at least equals the amount of debt; or</u></p> <p>(b) <u>a letter of credit or guarantee from an <i>approved counterparty</i>.</u></p>
<i>settlement date</i>	any date on which the fulfilment of an obligation under a <i>derivative contract</i> is or may be required
<i>share</i>	has the meaning given in the <i>Companies Act</i> or the <i>1986 Order</i> Part VII of the <i>Companies Act</i> or Part VIII of the <i>Companies (Northern Ireland) Order 1986</i>
<i>shareholder controller</i>	see rule 11.2 for <i>controller</i>
<i>short term deposit</i>	a sum of money which may be withdrawn at the discretion of the lender without penalty or loss of accrued interest by giving notice of withdrawal of one month or less
<i>Society</i>	the society incorporated by Lloyd's Act 1871 by the name of Lloyd's
<i>solvency deficit</i>	deficit in the assets available to cover the undertaking's liabilities and represent its <i>notional required minimum margin</i> (if any)
<i>subordinated debt</i>	any <i>debt</i> which, on a winding up of the debtor, ranks for payment after the claims of general creditors and is not to be repaid until the claims of all the general creditors outstanding at the time have been settled
<i>subsidiary</i>	is construed in accordance with section 736 of the <i>Companies Act</i> or Article 4 of the <i>1986 Order</i>
<i>SUP</i>	Supervision manual
<i>surplus assets</i>	has the meaning given in rule 4.2(2)
<i>Swiss general insurer</i>	a <i>non-EEA insurer</i> which has its head office in Switzerland and which has permission under the <i>Act</i> to effect or carry out <i>general insurance contracts</i> in

	accordance with the Swiss Treaty Agreement of 10 October 1989
<i>Third Life Directive</i>	Council Directive of 10 November 1992 on the co-ordination of laws, etc and amending Directives 79/267/EEC and 90/619/EEC (92/96/EEC)
<i>Third Non-Life Directive</i>	Council Directive of 18 June 1992 on the co-ordination of laws, etc, and amending Directives 73/239/EEC and 88/357/EEC (92/49/EEC)
<i>total capital resources</i>	the sum calculated at stage O of the calculation in <i>PRU</i> 2.2.14R
<i>ultimate EEA insurance parent undertaking</i>	an <i>EEA insurance parent undertaking</i> that is not itself the <i>subsidiary undertaking</i> of another <i>EEA insurance parent undertaking</i>
<i>ultimate insurance parent undertaking</i>	an <i>insurance parent undertaking</i> that is not itself the <i>subsidiary undertaking</i> of another <i>insurance parent undertaking</i>
<i>UCITS</i>	is an undertaking for collective investments in transferable <i>securities</i>
<i>UCITS Directive</i>	Council Directive 85/611/EEC of 20 December 1985 on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investments in transferable <i>securities</i>
<i>UK deposit insurer</i>	a <i>non-EEA insurer</i> which has made a <i>deposit</i> in the United Kingdom in accordance with rule 8.1
<i>UK insurer</i>	an <i>insurer</i> , other than a <i>pure reinsurer</i> or a <i>non-directive insurer</i> , whose head office is in the United Kingdom
<i>UK margin of solvency</i>	an <i>insurer's margin of solvency</i> computed by reference to the assets and liabilities of the business carried on by that <i>insurer</i> in the United Kingdom under rule 2.4
<i>Unsecured debt</i>	see <i>secured debt</i>
<i>used notional group solvency margin</i>	in relation to an <i>ultimate insurance parent undertaking</i> or an <i>ultimate EEA insurance parent undertaking</i> , the sum of:  (a) — in the case of a parent which is itself an <i>insurance</i>

	<p><del>undertaking:</del></p> <p>(i) <del>all liabilities in respect of cumulative preference shares left out of account by it in accordance with rule 2.10(3), and</del></p> <p>(ii) <del>all liabilities in respect of subordinated debt left out of account by it in accordance with a direction under section 148 of the Act,</del></p> <p><del>or, in either case, in accordance with the relevant regulatory requirements of the state or territory where the head office of the parent is situated, as the case may be;</del></p> <p>(b) <del>the parent's proportional shares of all liabilities in respect of cumulative preferences shares left out of account by its related insurance undertakings in accordance with rule 2.10(3) or the relevant regulatory requirements of the state or territory where the head office of the relevant insurance undertaking is situated, as the case may be; and</del></p> <p>(c) <del>the parent's proportional shares of all liabilities in respect of subordinated debt left out of account by its related insurance undertakings in accordance with a direction under section 148 of the Act or the relevant regulatory requirements in the state or territory where the head office of the relevant insurance undertaking is situated, as the case may be</del></p>
<i>Valuation of Assets Rules</i>	the rules in Chapter 4
<i>Warrant</i>	an instrument which falls within article 79 of the <i>Regulated Activities Order</i>



<i>zillmerising</i>	in relation to the <i>Margins of Solvency Rules</i> , means the method known by that name for modifying the net premium reserve method of valuing a long term <i>policy</i> by increasing the part of the future premiums for which credit is taken so as to allow for initial expenses
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...

## PART 2

### GENERAL PROVISIONS

#### Powers under which the rules are made

...

#### Use of definitions

- 11.5 A word or phrase which is printed in italics is used in the defined sense. Where a word or phrase is printed in italics and is not given a meaning in Part 1 of Chapter 11, that word or phrase has the meaning given to it in the *Glossary*.

...

## Chapter 12

### TRANSITIONAL ARRANGEMENTS

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#### Guidance:

GEN (the part of the *FSA Handbook* in High Level Standards which has the title General Provisions) contains some technical transitional provisions that apply throughout the Handbook and which are designed to ensure a smooth transition at commencement of the *Act*. These include transitional provisions relevant to record keeping and notification rules.

*SUP* contains transitional provisions which carry forward written concessions relating to pre-commencement provisions.

Table

<u>(1)</u>	<u>(2)</u> <b><u>Material to which the transitional provision applies</u></b>	<u>(3)</u>	<u>(4)</u> <b><u>Transitional provision</u></b>	<u>(5)</u> <b><u>Transitional Provision:</u></b> <b><u>Dates in force</u></b>	<u>(6)</u> <b><u>Handbook provision:</u></b> <b><u>coming into force</u></b>
1	<u>IPRU (INS) rules 3.7 and 11.1 (Definitions), Appendix 3.2 paragraph 9</u>	R	For the period specified in column (5), for the purposes of the <i>rules</i> specified in column (2), an <i>insurer</i> must apply the definition of <i>permitted derivative contract</i> as it had effect immediately prior to the date specified in column (6)	From 31 December 2004 to 30 December 2005	31 December 2004
2	<u>IPRU(INS) rules 3.7 and 11.1 (Definitions), Appendix 3.2 paragraph 9</u>	R	(1) This paragraph applies to a contract concluded on or before 30 December 2005 which satisfies the definition of <i>permitted derivative contract</i> as it had effect immediately prior to the date specified in column (6).  (2) In relation to a contract to which this paragraph applies, for the purposes of the rules specified in	From 31 December 2004 until the relevant <i>rule</i> is revoked	31 December 2004

			<u>column (2), an insurer may continue to apply the definition of permitted derivative contract as it had effect immediately prior to the date specified in column (6)</u>		
<u>3</u>	<u>IPRU(INS) rules 9.3A (1), 9.3A (2), 9.12 (2), 9.12(2A), 9.12(3), 9.12(9), Forms 1, 2, 3, 18 and 19</u>	<u>R</u>	<u>In relation to its financial year ending on or before 30 December 2005, an insurer is not required to complete column 2 ("As at end of the previous year") of Forms 1, 2, 3, 18 and 19</u>	<u>From 31 December 2004 to 30 December 2005</u>	<u>31 December 2004</u>
<u>4</u>	<u>IPRU(INS), Volume 1, Ch. 9 Part I, rules 9.5 and 9.35</u>	<u>R</u>	<u>In respect of the report annexed pursuant to IPRU(INS) rule 9.31(a) to the return for an insurer's financial year ending on or before 30 December 2005, the scope of the audit required by IPRU(INS) Volume 1, Ch.9 rules 9.5 and 9.35 is limited to audit of:</u>  <u>(a) Forms 48, 49, 56, 58 and 60; and</u>	<u>From 31 December 2004 to 30 December 2005</u>	<u>31 December 2004</u>

			<p><u>(b) the methods and assumptions determined by the insurer and used to perform the actuarial investigation.</u></p>		
5	<p><u>IPRU (INS), Volume 2, Appendix 9.6 Part II, paragraph 4</u></p>	R	<p><u>In respect of the report annexed pursuant to IPRU(INS) rule 9.31(a) to the return for an insurer's financial year ending on or before 30 December 2005, the audit opinion required by IPRU(INS) rule 9.5 and 9.35 is limited to the statement whether, in the auditor's opinion,:</u></p> <p><u>(a) Forms 48, 49, 56, 58 and 60 have been properly prepared in accordance with the Accounts and Statements Rules and</u></p>	<p><u>From 31 December 2004 to 30 December 2005</u></p>	<p><u>31 December 2004</u></p>

			<p><u>PRU</u>; and</p> <p>(b) the methods and assumptions determined by the <u>insurer</u> and used to perform the <u>actuarial investigation</u> appropriately reflect the requirements of <u>PRU 7.3</u>.</p>		
<u>7</u>	<u>IPRU(INS) rules 9.5 and 9.35, Appendix 9.4A, paragraphs 4(2), 4(6), 6(3) and 13</u>	<u>R</u>	<p>In respect of the valuation report annexed to the <u>return for an insurer's financial year ending on or before 30 December 2005</u> pursuant to <u>IPRU(INS) rule 9.31(b)</u>, the scope of the audit required by <u>IPRU(INS) rules 9.5 and 9.35</u> does not include:</p> <p>(a) the omitted information (as defined in <u>IPRU(INS) TR 6</u>); or</p> <p>(b) the information required by paragraph 4(6) of <u>Appendix 9.4A to IPRU(INS)</u>.</p>	<u>From 31 December 2004 to 30 December 2005</u>	<u>31 December 2004</u>
<u>8</u>	<u>IPRU (INS) Chapter 9 and Appendices 9.1 to</u>	<u>R</u>	<p>In relation to an <u>insurer's financial year ending on or before 30 December 2004</u>, the</p>	<u>From 31 December 2004 to 30</u>	<u>31 December</u>

	<u>9.9</u>		<u>insurer must comply with IPRU(INS) Chapter 9 and Appendices 9.1 to 9.9 as if the Integrated Prudential Sourcebook (Insurers and Other Amendments) (Consequential Amendments) Instrument 2004 had not been made.</u>	<u>April 2005</u>	<u>2004</u>
<u>9</u>	<u>IPRU (INS) Chapter 9, 9.40 to 9.43 and Appendix 9.9</u>	<u>R</u>	<u>In relation to an insurer's financial year ending on or before 30 December 2004, the insurer must comply with IPRU(INS) Chapter 10 (Parent undertaking solvency calculation) as it was in force on 30 December 2004, as if the Integrated Prudential Sourcebook (Insurers and Other Amendments) (Consequential Amendments) Instrument 2004 had not been made.</u>	<u>From 31 December 2004 to 30 June 2005</u>	<u>31 December 2004</u>

## Part 2: Amendments to Volume 2

In this part underlining indicates new text and striking through indicates deleted text. Where existing text is replaced by new text or entirely new text is added, this is indicated and the new text is not underlined. Where an entire section of text is deleted the place where the change is made is indicated and the text is not struck through.

# INTERIM PRUDENTIAL SOURCEBOOK FOR INSURERS

## CONTENTS

### VOLUME TWO

#### Appendices to the Rules

- |              |  |
|--------------|--|
| Appendix 2.1 | <del>General insurance business solvency margin: first method of calculation (premium basis) (rule 2.4(1)(b))</del> <u>[deleted]</u> |
| Appendix 2.2 | <del>General insurance business solvency margin: second method of calculation (claims basis) (rule 2.4(1)(b))</del> <u>[deleted]</u> |
| Appendix 2.3 | <del>Minimum guarantee fund (rule 2.9)</del> <u>[deleted]</u>  |
| Appendix 3.1 | [deleted]  |
| Appendix 3.2 | Permitted links (rule 3.7)   |
| Appendix 4.1 | [deleted]  |
| Appendix 4.2 | <del>Assets to be taken in to account only to a specified extent (rule 4.14)</del> <u>[deleted]</u>                                  |
| Appendix 5.1 | <del>Relevant co-insurance operations (rule 5.5 and relevant co-insurance operation)</del> <u>[deleted]</u>                          |
| Appendix 6.1 | <del>Methods of calculating the equalisation reserve (rule 6.7)</del> <u>[deleted]</u>   |
| Appendix 6.2 | <del>Method of calculating the equalisation reserve for credit insurance business (rule 6.12)</del> <u>[deleted]</u>                 |
| Appendix 9.1 | Balance sheet and profit and loss account (Forms 9-17) (rules 9.12 and 9.13)   |
| Appendix 9.2 | General insurance business: revenue account and additional information (Forms 20 to 39) (rules 9.14 to 9.22)                         |
| Appendix 9.3 | Long-term insurance business: revenue account and additional information (Forms 40 to 45) (rules 9.14 and 9.23)                      |

Appendix 9.4	Abstract of valuation report <del>prepared by appointed actuary</del> (Forms 46 to 61) (rule 9.31)
<u>Appendix 9.4A</u>	<u>Abstract of valuation report for realistic valuation (rule 9.31(b))</u>
Appendix 9.5	General insurance business: additional information on business ceded (rule 9.32)
Appendix 9.6	Certificates by directors <del>and actuary</del> and report of auditors (rules 9.34 and 9.35)
Appendix 9.7	Insurance statistics: other EEA States (Forms 91 to 94) (rule 9.37)
Appendix 9.8	Marine mutuals: items to be disregarded, directors' certificates and auditors reports (rule 9.36A)
<u>Appendix 9.9</u>	<u>Group Capital Adequacy (rule 9.40 to rule 9.42 and guidance 9.43)</u>

The following appendices are deleted:

Appendix 2.1	General insurance business solvency margin: first method of calculation (premium basis) (rule 2.4(1)(b))
Appendix 2.2	General insurance business solvency margin: second method of calculation (claims basis) (rule 2.4(1)(b))
Appendix 2.3	Minimum guarantee fund (rule 2.9)
Appendix 4.2	Assets to be taken in to account only to a specified extent (rule 4.14)
Appendix 5.1	Relevant co-insurance operations (rule 5.5 and relevant co-insurance operation)
Appendix 6.1	Methods of calculating the equalisation reserve (rule 6.7)
Appendix 6.2	Method of calculating the equalisation reserve for credit insurance business (rule 6.12)
<b>Appendix 2.1</b>	<u>[deleted]</u>
<b>Appendix 2.2</b>	<u>[deleted]</u>
<b>Appendix 2.3</b>	<u>[deleted]</u>



...

**APPENDIX 3.2 (rule 3.7)**

**PERMITTED LINKS**

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**PART I**

**DESCRIPTIONS OF PROPERTY BY WHICH BENEFITS MAY BE DETERMINED<sup>1</sup>**  
**APPENDIX 3.2 (rule 3.7)**

...

**PART II**

**INDICES BY REFERENCE TO WHICH BENEFITS MAY BE DETERMINED<sup>2</sup>**

...

**Appendix 4.2**      [deleted]

**Appendix 5.1**      [deleted]

**Appendix 6.1**      [deleted]

**Appendix 6.2**      [deleted]

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<sup>1</sup> See ~~Guidance Note 4.1~~ and ~~Guidance Note 9.1~~

<sup>2</sup> See ~~Guidance Note 4.1~~ and ~~Guidance Note 9.1~~

**APPENDIX 9.1** (rules 9.12 and 9.13)

**BALANCE SHEET AND PROFIT AND LOSS ACCOUNT  
(FORMS 1 TO 3 AND 109 TO 179)**

---

**Introduction**

1. (1) All the forms included in the part of the *return* to which this Appendix relates (**Forms 1 to 3 and 109 to 179**) are to be laid out as shown in this Appendix, except that the instructions for the completion of the forms need not be reproduced.

...

5 ...

- (2) The bases of conversion adopted must be stated by way of supplementary note (code 1601) to **Form 16** or, if there is no Form 16, by way of supplementary note (code 4005) to **Form 40**.

...

8. (3) If amounts shown include amounts calculated on the basis set out in (2), a supplementary note to **Form 13** (code 1304 for other than *long-term insurance business* and code 1310 for *long-term insurance business*) to that effect must be provided.

...

**Premiums**

10. (1) Notwithstanding the requirements of the *insurance accounts rules*, amounts included in **Forms 11 and 12** in respect of -

- (a) *gross premiums receivable*;
- (b) *claims paid*;
- (c) *claims outstanding*; and
- (d) *reinsurance recoveries*,

must be determined in accordance with ~~**Appendices 2.1 to 2.3**~~ PRU 7.2.66R and PRU 7.2.71R.

...

**Counterparty exposure**

11. (1) There must be given by way of a supplementary note to **Form 13** (code 1305 for other than long-term insurance business and code 1311 for long-term insurance business) -

...

- (2) In each case where the *exposure* of the *insurer* to a *counterparty* at the end of the *financial year in question* exceeds:

(a) 5% of the sum of its base capital resources requirement and its long-term insurance business ~~amount~~ liabilities, excluding property linked liabilities and net of reinsurance ceded, or

(b) the sum of 20,000 Euro and 5% of its liabilities arising from its general insurance business ~~amount~~, net of reinsurance ceded,

as appropriate -

(a) the amount of that *exposure*; and

(b) the nature of the assets held which give rise to that *exposure*,

must be stated by way of a supplementary note to **Form 13** (code 1306 for other than long-term insurance business and code 1312 for long-term insurance business).

- (3) There must be stated by way of supplementary note to **Form 13** (code 1307 for other than long-term insurance business and code 1313 for long-term insurance business) the aggregate value of any rights to which PRU 3.2.35R or PRU 3.2.36R and PRU 3.2.37R relates paragraph 14 of Part I of Appendix 4.2.

#### **Provision for ~~adverse changes~~ reasonably foreseeable adverse variations**

12. There must be stated by way of supplementary note to **Form 14** (code 1401) or **15** (code 1501) the methods and assumptions used to determine the amount of any adjustment or provision made pursuant to PRU 1.3.26R to PRU 1.3.29R or PRU 4.3.17R to PRU 4.3.18R ~~rule 5.3~~ or, if there is no such adjustment or provision, the methods and assumptions used to determine that no adjustment or provision is required.

#### **Liabilities**

13. (1) Subject to (3), the following information must be given by way of a supplementary note to **Form 14** (code 1402) or **15** (code 1502) -

...

...

- (3) (1)(a) and (c) may be disregarded by an *insurer* in the case of -

- (a) one or more 'charges' over assets which are attributable to either the *long-term insurance assets* or the 'other general insurance business assets' and whose aggregate value (as shown on **Form 13**) does not exceed 2.5% of the *long-term insurance assets (other than reinsurance recoveries and assets required to match property linked liabilities)* or the 'other assets (other than reinsurance recoveries)' ~~or general insurance business amount~~, as the case may be; or
  - (b) one or more contingent liabilities whose aggregate value does not exceed 2.5% of the *long-term insurance assets (other than reinsurance recoveries and assets required to match property linked liabilities)* or the 'other assets (other than reinsurance recoveries)' ~~or general insurance business amount~~, as the case may be.
- (4) (1)(d) may be disregarded by an *insurer* in respect of one or more guarantees, indemnities or contractual commitments where the aggregate of the maximum liabilities specified in such guarantees, indemnities or contractual commitments does not exceed 2.5% of the *long-term insurance assets (other than reinsurance recoveries and assets required to match property linked liabilities)* or the 'other assets (other than reinsurance recoveries)' ~~or general insurance business amount~~, as the case may be.
- (5) For the purposes of this paragraph, **charge** includes any arrangement whatsoever, whether contractual or otherwise, which operates to secure the prior claim of any person over general creditors to any assets on a winding up of the *insurer*, and other assets means assets that are not *long-term insurance assets*.

### Reconciliation

14. (1) ~~For an *insurer* (other than a *company* incorporated outside the United Kingdom) an explanation must be given by way of supplementary note to **Form 10** reconciling—~~
- (a) ~~line 99 of **Form 13** (category of assets '1') less line 59 of **Form 15**; and~~
  - (b) ~~the amount shown under balance sheet item A 'capital and reserves' in the *insurer's* accounts prepared pursuant to the insurance accounts rules for the financial year in question.~~
- ~~(2) Where for an *insurer* (other than a *company* incorporated outside the United Kingdom) there are no accounts pursuant to 1(b) (or the accounts have not yet been prepared), this must be stated by way of supplementary note to **Form 10**.~~

A reconciliation of the *capital resources* of the *insurer* to the net *admissible assets* of the *insurer* must be provided in accordance with instruction 66 to **Form 3**.

...

16 Where, in respect of any *derivative contract* included in **Form 17**, assets have been transferred to or for the benefit of the *insurer* by way of *variation margin* there must be stated by way of supplementary note (code 1701) to **Form 17** –

...

17 If –

...

the corresponding value, if not zero, must be stated (by way of supplementary note (code 1702) to **Form 17**) for each line in **Forms 13, 14** or **15** and paragraph 16 applies to the insurer as if such assets had been included in **Form 17**.

---

## FORMS

[**Forms 1-3 and 10-179** to follow]

Forms 1, 2 and 3 of Appendix 9.1 (Balance sheet and profit and loss account) are inserted as follows:

**Statement of solvency – general insurance business**

Name of insurer

Global business/UK branch business/EEA branch

Financial year ended

Solo solvency calculation / Group solvency calculation

	Company registration number	GL/ UK/ CM	day	month	year	units
R1						£000
					<b>As at end of this financial year 1</b>	<b>As at end of the previous year 2</b>

**Capital resources**

Capital resources arising outside the long-term insurance fund	11		
Capital resources allocated towards long-term insurance business arising outside the long-term insurance fund	12		
Capital resources available to cover general insurance business capital resources requirement (11-12)	13		

**Guarantee fund**

Guarantee fund requirement	21		
Excess (deficiency) of available capital resources to cover guarantee fund requirement	22		

**Minimum capital requirement (MCR)**

General insurance capital requirement	31		
Base capital resources requirement	33		
Minimum capital requirement	34		
Excess (deficiency) of available capital resources to cover 50% of MCR	35		
Excess (deficiency) of available capital resources to cover 75% of MCR	36		

**Capital resources requirement (CRR)**

Capital resources requirement	41		
Excess (deficiency) of available capital resources to cover general insurance business CRR (13-41)	42		

**Contingent liabilities**

Quantifiable contingent liabilities in respect of other than long-term insurance business as shown in a supplementary note to Form 15	51		
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## Instructions for completion of Form 1

1. An *insurer* (other than a *Swiss general insurer* or an *EEA-deposit insurer*) carrying on *general insurance business* must complete Form 1 in respect of its entire *general insurance business*. An *external insurer* (other than a *pure reinsurer*) that is carrying on *general insurance business* must complete Form 1 in respect of business carried on through a *branch* in the *United Kingdom*. An *UK-deposit insurer* that is carrying on *general insurance business* must complete Form 1 in respect of business carried on through its *branches* in *EEA States* taken together. Form 1 is not required for *Swiss general insurers* or *EEA-deposit insurers*.
2. In the case of a *marine mutual* completing an abbreviated *return* under rule 9.36A, units must be the same as those used in Form M1.
3. For *financial years* commencing on or before 31 December 2004 lines 11 to 42, column 2 must be blank.
4. The entry at line 13 must be equal to the *total capital resources* after deductions at line 79, column 1 on Form 3. The entry at line 11 includes also *capital resources* allocated towards the *long-term insurance business* (and included in column 2 on Form 3) that arise outside the *long-term insurance fund*. For a *branch* the entry at line 11 is equal to Form 10 line 29.
5. For a *firm* carrying on *long-term insurance business* the entry at line 12 on Form 1 must equal the entry at line 12 on Form 2. For a *firm* not carrying on *long-term insurance business* the entry at line 12 on Form 1 is nil.

### **Instructions 6-12 only apply to firms that do not meet the conditions specified in PRU 2.1.9R(2), i.e. that are not required to perform an adjusted solo calculation under PRU 8.3.**

6. The *guarantee fund* requirement at line 21 is calculated by reference to PRU 2.2.18R as the higher of line 33 and 1/3 of line 31.
7. The excess (deficiency) of available *capital resources* to cover the *guarantee fund* requirement at line 22 is equal to line 81 on Form 3 less line 21. For a *branch* this is equal to line 13 less line 21 less an adjustment because assets held to cover the *guarantee fund* must be held in the *United Kingdom* (or for *UK-deposit insurers*, in the *EEA States* where the *firm* carries on *insurance business*); the adjustment is the difference between form 13 line 89 for categories 4 and 3 (or 5), except for *branches* carrying on both *long-term insurance business* and *general insurance business* (composite *branches*); composite *branches* will need to state how the difference is allocated between *general insurance business* and *long-term insurance business* in a note to the Form.
8. The *general insurance capital requirement* at line 31 must be equal to the amount shown at line 43 of Form 12, which is calculated in accordance with PRU 2.1.30R.
9. The *base capital resources requirement* at line 33 must be taken from PRU 2.1.26R.
10. The excess (deficiency) of available *capital resources* to cover 50% of the *minimum capital requirement* at line 35 is equal to line 82, column 1 on Form 3 less 50% of line 34. For a *branch*, line 35 is to be left blank.
11. The excess (deficiency) of available *capital resources* to cover 75% of the *minimum capital requirement* at line 36 is equal to line 83, column 1 on Form 3 less 75% of line 34. For a *branch*, line 36 is to be left blank.
12. The *capital resources requirement* at line 41 is calculated in accordance with PRU 2.1.14R and is equal to line 34.

### **Instructions 13-20 only apply to firms that meet the conditions specified in PRU 2.1.9 R(2), i.e. that perform the adjusted solo solvency calculation in accordance with PRU 8.3.**

13. The *guarantee fund* requirement at line 21 is calculated as the share of the *general insurance business*

of  $\frac{1}{3}X + (R - S - U - X)$  by reference to *PRU* 8.3.45R.

14. The excess (deficiency) of available *capital resources* to cover the *guarantee fund* requirement at line 22 is equal to line 81, column 1 on Form 3 less line 21.
15. Line 31 is not applicable.
16. Line 33 is not applicable.
17. The entry at line 34 must equal the amount represented by (R-S) with reference to *PRU* 8.3.45R in relation to the *general insurance business*.
18. The excess (deficiency) of available *capital resources* to cover 50% of the *minimum capital requirement* at line 35 is equal to line 82, column 1 on Form 3 less 50% of line 34.
19. The excess (deficiency) of available *capital resources* to cover 75% of the *minimum capital requirement* at line 36 is equal to line 83, column 1 on Form 3 less 75% of line 34.
20. The entry at line 41 must equal the amount represented by R with reference to *PRU* 8.3.45R in relation to the *general insurance business*.

**Instructions 21 onwards apply to all firms**

21. The entry at line 51 must not include provision for any liability to tax on capital gains referred to in paragraph 13(1)(b) of Appendix 9.1. Amounts in *related undertakings* must not be included.
22. Where a direction under section 148 of the *Act* has been issued disapplying or modifying any of the provisions of the *Accounts and Statements Rules*, a note to **Form 1** explaining the effect of the order is usually required. The requirement for such a note would be specified in the direction itself. [Code 0101].



**Statement of solvency – long-term insurance business**

Name of insurer

Global business/UK branch business/EEA branch

Financial year ended

Solo solvency calculation / Group solvency calculation

	Company registration number	GL/ UK/ CM	day	month	year	units
R2						£000
					<b>As at end of this financial year 1</b>	<b>As at end of the previous year 2</b>

**Capital resources**

Capital resources arising within the long-term insurance fund	11		
Capital resources allocated towards long-term insurance business arising outside the long-term insurance fund	12		
Capital resources available to cover long-term insurance business capital resources requirement (11+12)	13		

**Guarantee fund**

Guarantee fund requirement	21		
Excess (deficiency) of available capital resources to cover guarantee fund requirement	22		

**Minimum capital requirement (MCR)**

Long-term insurance capital requirement	31		
Resilience capital requirement	32		
Base capital resources requirement	33		
Minimum capital requirement	34		
Excess (deficiency) of available capital resources to cover 50% of MCR	35		
Excess (deficiency) of available capital resources to cover 75% of MCR	36		

**Enhanced capital requirement**

With-profits insurance capital component	37		
Enhanced capital requirement	38		

**Capital resources requirement (CRR)**

Capital resources requirement (greater of 34 and 38)	41		
Excess (deficiency) of available capital resources to cover long-term insurance business CRR (13-41)	42		

**Contingent liabilities**

Quantifiable contingent liabilities in respect of long-term insurance business as shown in a supplementary note to Form 14	51		
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## Instructions for completion of Form 2

1. An *insurer* (other than an *EEA-deposit insurer*) carrying on *long-term insurance business* must complete Form 2 in respect of its entire *long-term insurance business*. An *external insurer* (other than a *pure reinsurer*) or *EEA-deposit insurer* that is carrying on *long-term insurance business* must complete Form 2 in respect of business carried on through a *branch* in the *United Kingdom*. An *UK-deposit insurer* that is carrying on *long-term insurance business* must complete Form 2 in respect of business carried on through its *branches* in *EEA States* taken together.
2. The entry at line 13 must be equal to the *total capital resources* after deductions at line 79, column 2 on Form 3. The entry at line 11 represents items relating to the *long-term insurance fund*, and that at line 12 represents amounts arising outside the *long-term insurance fund*. For a *branch*, line 11 is equal to the sum of any *implicit items* plus form 10 line 11 less the sum of lines 11, 12 and 49 in Form 14: when there are *implicit items* it would be appropriate for note 0202 (see instruction 26) to include an analysis of line 11; if the *insurer* is not carrying on *general insurance business* through the *branch*, line 12 will be equal to Form 10 line 29.
3. For *financial years* commencing on or before 31 December 2004 lines 11 to 42, column 2 must be blank.
4. For *EEA-deposit insurers*, lines 21 to 42 must be blank.

**Instructions 5-14 only apply to firms that do not meet the conditions specified in PRU 2.1.9 R(2), i.e. that are not required to perform an adjusted solo calculation under PRU 8.3.**

5. The *guarantee fund* requirement at line 21 is calculated by reference to *PRU 2.2.17R* as the higher of line 33 and 1/3 of line 31.
6. The excess (deficiency) of available *capital resources* to cover the *guarantee fund* requirement at line 22 is equal to line 81, column 2 on Form 3 less line 21. For a *branch* this is equal to line 13 less line 21 less an adjustment because assets held to cover the *guarantee fund* must be held in the *United Kingdom* (or for *UK-deposit insurers*, in the *EEA States* where the *firm* carries on *insurance business*) and cannot include *implicit items*; an analysis would be appropriate in a note (code 0203) to the Form.
7. The *long-term insurance capital requirement* at line 31 must be equal to the amount shown at line 51 of Form 60, which is calculated in accordance with *PRU 2.1.32R*.
8. The *resilience capital requirement* at line 32 is calculated in accordance with the *rules* in *PRU 4.2*.
9. The *base capital resources requirement* at line 33 must be taken from *PRU 2.1.26R*.
10. The excess (deficiency) of available *capital resources* to cover 50% of the *minimum capital requirement* at line 35 is equal to line 82, column 2 on Form 3 less 50% of line 34. For a *branch*, line 35 must be blank.
11. The excess (deficiency) of available *capital resources* to cover 75% of the *minimum capital requirement* at line 36 is equal to line 83, column 2 on Form 3 less 75% of line 34. For a *branch*, line 36 must be blank.
12. The *with-profits insurance capital component* at line 37 must be the total of the amounts shown at line 64 on Forms 18, calculated in accordance with the *rules* in *PRU 7.4*.
13. The *enhanced capital requirement* at line 38 is calculated as the sum of lines 31, 32 and 37.
14. The *capital resources requirement* at line 41 is calculated in accordance with *PRU 2.1.15R*.

**Instructions 15-23 only apply to firms that meet the conditions specified in PRU 2.1.9R(2), i.e. that perform the adjusted solo solvency calculation in accordance with PRU 8.3.**

15. The *guarantee fund* requirement at line 21 is calculated as the share of the *long-term insurance*

*business of  $\frac{1}{3}X + (R - S - U - X)$  by reference to PRU 8.3.45R.*

16. The excess (deficiency) of available *capital resources* to cover the *guarantee fund* requirement at line 22 is equal to line 81, column 2 on Form 3 less line 21.
17. Lines 31, 32 and 33 are not applicable.
18. The entry at line 34 must include the amount represented by (R-S) with reference to PRU 8.3.45R in relation to the *long-term insurance business*.
19. The excess (deficiency) of available *capital resources* to cover 50% of the *minimum capital requirement* at line 35 is equal to line 82, column 2 on Form 3 less 50% of line 34.
20. The excess (deficiency) of available *capital resources* to cover 75% of the *minimum capital requirement* at line 36 is equal to line 83, column 2 on Form 3 less 75% of line 34.
21. The *with-profits insurance capital component* at line 37 must be the total of 'S' with reference to PRU 8.3.45R.
22. The entry at line 38 must be the sum of lines 34 and 37.
23. The entry at line 41 must equal the amount represented by R with reference to PRU 8.3.45R in relation to the *long-term insurance business*.

**Instructions 24 onwards apply to all firms**

24. The entry at line 51 must not include provision for any liability to tax on capital gains referred to in paragraph 13(1)(b) of Appendix 9.1. Amounts in *related undertakings* must not be included.
25. Where a direction under section 148 of the *Act* has been issued disapplying or modifying any of the provisions of the *Accounts and Statements Rules*, a note to **Form 2** explaining the effect of the direction is usually required. The requirement for such a note would be specified in the direction itself. (Code 0201).
26. Where a direction under section 148 of the *Act* has been issued to an *insurer* permitting it to take into account *implicit items* on *long-term insurance business*, that direction may specify that a note is to be included in the *return* explaining such items. That note should be included as a note to **Form 2**. (Code 0202).

Components of capital resources

Name of insurer  
Global business  
Financial year ended

	Company registration number	GL/UK/CM	day	month	year	units
	R3					£000
		General insurance business	Long-term insurance business	Total as at the end of this financial year	Total as at the end of the previous year	
		1	2	3	4	
<b>Core tier one capital</b>						
Permanent share capital	11					
Profit and loss account and other reserves	12					
Share premium account	13					
Positive valuation differences	14					
Fund for future appropriations	15					
Core tier one in related undertakings	16					
Core tier one capital (sum of 11 to 16)	19					
<b>Tier one waivers</b>						
Unpaid share capital / unpaid initial funds and calls for supplementary contributions	21					
Implicit items	22					
Tier one waivers in related undertakings	23					
Total tier one waivers as restricted (21+22+23)	24					
<b>Other tier one</b>						
Perpetual non-cumulative preference shares as restricted	25					
Perpetual non-cumulative preference shares in related undertakings	26					
Innovative tier one capital as restricted	27					
Innovative tier one capital in related undertakings	28					
<b>Total tier one capital before deductions (19+24+25+26+27+28)</b>	31					
Investments in own shares	32					
Intangible assets	33					
Amounts deducted from technical provisions for discounting	34					
Other negative valuation differences	35					
Deductions in related undertakings	36					
Deductions from tier one (32 to 36)	37					
<b>Total tier one capital after deductions (31-37)</b>	39					

Components of capital resources

Name of insurer  
Global business  
Financial year ended

	Company registration number	GL/UK/CM	day	month	year	units
R3						£000
		General insurance business		Long-term insurance business	Total as at the end of this financial year	Total as at the end of the previous year
		<b>1</b>		<b>2</b>	<b>3</b>	<b>4</b>

**Tier two capital**

Implicit items, (tier two waivers and amounts excluded from line 22)	41				
Perpetual non-cumulative preference shares excluded from line 25	42				
Innovative tier one capital excluded from line 27	43				
Tier two waivers, innovative tier one capital and perpetual non-cumulative preference shares treated as tier two capital (41 to 43)	44				
Perpetual cumulative preference shares	45				
Perpetual subordinated debt and securities	46				
Upper tier two capital in related undertakings	47				
<b>Upper tier two capital (44 to 47)</b>	<b>49</b>				

Fixed term preference shares	51				
Other tier two instruments	52				
Lower tier two capital in related undertakings	53				
<b>Lower tier two capital (51+52+53)</b>	<b>59</b>				

<b>Total tier two capital before restrictions (49+59)</b>	<b>61</b>				
Excess tier two capital	62				
Further excess lower tier two capital	63				
<b>Total tier two capital after restrictions, before deductions (61-62-63)</b>	<b>69</b>				

Components of capital resources

Name of insurer  
Global business  
Financial year ended

	Company registration number	GL/UK/CM	day	month	year	units
R3						£000
		General insurance business	Long-term insurance business	Total as at the end of this financial year	Total as at the end of the previous year	
		<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	

**Total capital resources**

Positive adjustments for regulated non-insurance related undertakings	71				
<b>Total capital resources before deductions (39+69+71)</b>	72				
Inadmissible assets other than intangibles and own shares	73				
Assets in excess of market risk and counterparty limits	74				
Deductions for related ancillary services undertakings	75				
Deductions for regulated non-insurance related undertakings	76				
Total deductions of ineligible surplus	77				
<b>Total capital resources after deductions (72-73-74-75-76-77)</b>	79				

**Available capital resources for PRU tests**

Available capital resources for guarantee fund requirement	81				
Available capital resources for 50% MCR requirement	82				
Available capital resources for 75% MCR requirement	83				

**Financial engineering adjustments**

Implicit items	91				
Financial reinsurance – ceded	92				
Financial reinsurance – accepted	93				
Outstanding contingent loans	94				
Any other charges on future profits	95				
<b>Sum of financial engineering adjustments (91+92-93+94+95)</b>	96				

### Instructions for completion of Form 3

1. An *insurer* (other than a *Swiss general insurer* or an *EEA-deposit insurer*) must complete Form 3 in respect of its entire business. An *external insurer* (other than a *pure reinsurer*), an *EEA-deposit insurer* or a *Swiss general insurer* must complete Form 10 in respect of business carried on through a *branch* in the *United Kingdom*. An *UK-deposit insurer* must complete Form 10 in respect of business carried on through its *branches* in *EEA States* taken together.
2. An *insurer* that is carrying on *long-term insurance business*, other than a *mutual* not carrying on *general insurance business*, that includes within its *capital resources* any capital instruments issued by its *long-term insurance fund*, must include a supplementary note (code 0302) analysing those instruments.
3. In the case of a *marine mutual* completing an abbreviated *return* under rule 9.36A, units must be the same as those used in Form M1. If units are in US\$ or US\$000, then the bases of conversion used in determining the *base capital resources requirement* must be those used in Forms 11 and 12.
4. Amounts in columns 1 and 2 refer to capital supporting the *general insurance business* and the *long-term insurance business* respectively. For a *firm* carrying on only *general insurance business* column 2 should be blank. For a *firm* carrying on only *long-term insurance business* column 1 should be blank. All items relating to the *long-term insurance fund* should be included in column 2. For a *composite firm* capital items arising outside the *long-term insurance fund* should be allocated between *general insurance business* and *long-term insurance business* in a manner consistent with the *firm's* view of what business that capital supports. Where there is a material change in way capital items are allocated from one year to the next, the *firm* should explain the change in a supplementary note (code 0303).
5. Column 3 is the sum of columns 1 and 2.
6. For *financial years* commencing on or before 31 December 2004 column 4 must be blank.
7. Amounts at lines 11-13 should be taken from the *firm's* stand-alone accounts prepared under the Companies Act 1985 or (for *firms* not preparing accounts under the Companies Act) equivalent overseas legislation or the applicable UK legislation.
8. The entry at line 15.2 must be the FFA taken from the *firm's* stand-alone accounts prepared under the Companies Act 1985 or (for *firms* not preparing accounts under the Companies Act) equivalent overseas legislation or the applicable *United Kingdom* legislation. The entry at line 15 column 1 must be blank.
9. *PRU 2.2.78R* and *2.2.79G* explain how to calculate the valuation differences for inclusion at line 14 or 35. Inadmissible assets or assets in excess of *market risk* and *counterparty* limits are not to be included in the valuation differences. Net valuation differences are shown at line 14 if positive or in line 35 if negative. The *firm* must state in a supplementary note (code 0308) to this form -
  - (a) The amount of positive valuation differences included within line 14 or 35 in respect of assets where valuation in *PRU* exceeds the valuation that the *firm* uses for external financial reporting purposes, together with a brief explanation indicating the nature of those assets;
  - (b) The amount of positive valuation differences included within line 14 or 35 in respect of liabilities where valuation in *PRU* is lower than the valuation that the *firm* uses for external financial reporting purposes, together with a brief explanation indicating the nature of those liabilities;
  - (c) The amount of negative valuation included within line 14 or 35 in respect of assets where valuation in *PRU* is lower than the valuation that the *firm* uses for external financial reporting purposes (excluding inadmissible assets and assets in excess of *market risk* and *counterparty* limits), together with a brief explanation indicating the nature of those assets; and
  - (d) The amount of negative valuation included within line 14 or 35 in respect of liabilities where valuation in *PRU* exceeds the valuation that the *firm* uses for external financial reporting

purposes (excluding amounts deducted from *technical provisions* for discounting shown at line 34), together with a brief explanation indicating the nature of those liabilities.

The amount in (a) plus the amount in (b) less the amount in (c) less the amount in (d) should equal the amount shown at line 14 if positive or at line 35 if negative."

**Instructions 10-32 only apply to firms that do not meet the conditions specified in PRU 2.1.9R(2), i.e. that are not required to perform an adjusted solo calculation under PRU 8.3.**

10. The entries at line 16 must be nil.
11. Amounts may only appear in lines 21 and 22 if the *FSA* has issued a *waiver* permitting these amounts to count as *tier one capital* (tier one waivers). These amounts are restricted by *PRU 2.2.20R* (1), so that amounts in line 24 may not be greater than corresponding amounts in line 19. If the *FSA* has issued a *waiver* permitting amounts to count as *tier two capital* (tier two waivers), these are to be included at line 41, together with any amounts that arise from the restriction at *PRU 2.2.20R*(1).
12. The entries at line 23 must be nil.
13. The entries at lines 25 and 27 must be restricted to comply with *PRU 2.2.20R*, so that the total of the amounts in lines 24, 25 and 27 is not greater than the amount in line 19 and the amount in line 27 is not greater than 15/85 of the total of the amounts in lines 19, 24 and 25. Amounts in excess of the limits are entered at lines 42 and 43 respectively.
14. The entries at lines 26 and 28 must be nil.
15. The entries at line 32 for investments in own *shares* should, in the majority of cases, be zero.
16. For the purpose of completing line 33, the *firm* should refer to *PRU 2.2.84R* and *PRU 2.2.85G*.
17. The amounts in line 34 must be calculated in accordance with *PRU 2.2.80R* and *PRU 2.2.81R*.
18. The entries at line 36 must be nil.
19. The entries at lines 45 and 46 for perpetual cumulative *preference shares*, *subordinated debt* and *securities* must be the total, unrestricted, amounts that the *firm* can include in *upper tier two capital* in accordance with *PRU 2.2.100G* to *PRU 2.2.106G*.
20. The entries at line 47 must be nil.
21. The types of capital instrument that a *firm* can include within its *lower tier two capital* are set out at *PRU 2.2.107G* to *PRU 2.2.115G*. These should be split between fixed term *preference shares* and other *tier two instruments* and entered at lines 51 and 52 respectively.
22. The entries at line 53 must be nil.
23. The effect of the restrictions at *PRU 2.2.23R* applying to *tier two capital* are shown at lines 62 and 63. Line 62 relates to *tier two capital* as a whole and equals the excess (if any) of line 61 over line 39. Line 63 relates to *lower tier two capital* and equals the excess (if any) of line 59 over the sum of line 62 and 1/2 line 39.
24. Line 71 must show positive adjustments for *related undertakings* that are *regulated related undertakings* (other than *insurance undertakings*) required by *PRU 2.2.90R*.
25. Line 73 must show the deductions for assets that are not *admissible assets* required by *PRU 2.2.86R*.
26. Line 74 must show the assets in excess of *market risk* and *counterparty* limits in *PRU 3.2.22R*.
27. Line 75 must show negative adjustments for *related undertakings* that are *ancillary services*



*undertakings* required by PRU 2.2.89R.

28. Line 76 must show negative adjustments for *related undertakings* that are *regulated related undertakings* (other than *insurance undertakings*) required by PRU 2.2.90R.
29. The entries at line 77 must be nil.
30. The entry at line 81 is determined as the amount of the *firm's capital resources* available to meet its *guarantee fund* requirement, having regard to PRU 2.2.17R and PRU 2.2.18R. Line 81 must be either:
  - line 79; or
  - (if less) the sum of lines 19, 25, 42, 45, 46 and 59 less the sum of lines 37, 62 and 63.
31. The entry at line 82 is determined as the amount of the *firm's capital resources* available to meet 50% of its *minimum capital requirement*, having regard to PRU 2.2.16R. Line 82 must be either:
  - line 79; or
  - (if less) the sum of lines 19, 24, 25 and 42 less line 37.
32. The entry at line 83 is determined as the amount of the *firm's capital resources* available to meet 75% of its *minimum capital requirement*, having regard to PRU 2.2.24R. Line 83 must be either:
  - line 79; or
  - (if less) the sum of lines 19, 24, 25, 41, 42, 45 and 46 less the sum of line 37 and any excess of line 62 over line 59.

**Instructions 33-57 only apply to firms that meet the conditions specified in PRU 2.1.9 R(2), i.e. that perform the adjusted solo solvency calculation in accordance with PRU 8.3.**

33. *Tier one capital resources* must be calculated in accordance with the *rules* in PRU 8.3.41R in relation to restricted assets.
34. The entries at line 16 must equal the net contribution to core *tier one capital resources* of the *firm's related undertakings* in accordance with the calculation in PRU 8.3.55R (2).
35. Amounts may only appear in lines 21-23 if the *FSA* has issued a *waiver* permitting these amounts to count as *tier one capital* (tier one waivers). These amounts are restricted by PRU 8.3.45R (1)(c), so the amounts in line 24 may not be greater than corresponding amounts in line 19. If the *FSA* has issued a *waiver* permitting amounts to count as *tier two capital* (tier two waivers), these are to be included at line 41, together with any amounts that arise from the restriction at PRU 8.3.45R (1)(c).
36. The entries at line 26 must include the net contribution to the *firm* of perpetual non-cumulative *preference shares* issued by the *firm's related undertakings* – ie. the capital represented by perpetual non-cumulative *preference shares* of each of the *firm's related undertakings* that is a *regulated related undertaking* after deduction of the sum of the book value of the investments by the *firm* in the perpetual non-cumulative *preference shares* of each of its *related undertakings* that is a *regulated related undertaking* and the book value of the investments by *related undertakings* of the *firm* in the perpetual non-cumulative *preference shares* of each of its *related undertakings* that is a *regulated related undertaking* – in a manner consistent with the calculation of *GCR* in PRU 8.3.
37. The entries at line 28 must equal the net contribution to innovative *tier one capital resources* of the *firm's related undertakings* in accordance with the calculation in PRU 8.3.53R (2).
38. The entries at lines 25-28 must be restricted to comply with PRU 8.3.45R, so that the total of the amounts in lines 24-28 is not greater than the amount in line 19, and the total amount in lines 27 and 28 is not greater than 15/85 of the total of the amounts in lines 19, 24, 25, 26. Amounts in excess of the limits are entered at lines 42 and 43 as appropriate. If line 42 or 43 includes amounts excluded from line 26 or 28, these amounts must be stated in a supplementary note (code 0304).
39. The entries at line 32 for investments in own *shares* should, in the majority of cases, be zero.
40. For the purpose of completing line 33, the *firm* should refer to PRU 2.2.84R and 2.2.85G.

41. The amounts in line 34 must be calculated in accordance with *PRU 2.2.80R* and *2.2.81R*.
42. The entries at line 36 must equal the total of any of the deductions of the type specified in lines 32-35 that apply to the *firm's related undertakings*.
43. The entries at lines 45 and 46 for perpetual cumulative *preference shares*, subordinated *debt* and *securities* must be the total, unrestricted, amounts that the *firm* can include in *upper tier two capital* in accordance with *PRU 2.2.100G* to *PRU 2.2.106G*.
44. The entries at line 47 must equal the net contribution to *upper tier two capital resources* of the *firm's related undertakings* – ie. the sum of the *firm's* share of the *upper tier two capital resources* of each *related undertaking* less the book value of the *firm's* investment in the *upper tier two capital* of its *related undertakings* – in a manner consistent with the calculation of *GCR* in *PRU 8.3*.
45. The types of capital instrument that a *firm* can include within its *lower tier two capital* are set out at *PRU 2.2.107G* to *PRU 2.2.115G*. These should be split between fixed term *preference shares* and other *tier two instruments* and entered at lines 51 and 52 respectively.
46. The entries at line 53 must equal the net contribution to *lower tier two capital resources* of the *insurer's related undertakings* in accordance with the calculation in *PRU 8.3.57R(2)*.
47. The effect of the restrictions at *PRU 8.3.45R* applying to *tier two capital* are shown at lines 62 and 63. Line 62 relates to *tier two capital* as a whole and equals the excess (if any) of line 61 over line 39. Line 63 relates to *lower tier two capital* and equals the excess (if any) of line 59 over the sum of line 62 and 1/2 line 39.
48. The entries at line 71 must be nil.
49. Line 73 must show the deductions for inadmissible assets required by *PRU 8.3.59R*.
50. Line 74 must show the assets in excess of *market risk* and *counterparty* limits in *PRU 8.3.70R*.
51. Line 75 must show negative adjustments for *related undertakings* that are *ancillary services undertakings* required by *PRU 8.3.62R*.
52. The entries at line 76 must be nil.
53. The entries in line 77 must show the total amount calculated in respect of ineligible surplus in accordance with *PRU 8.3.65R*.
54. The entry at line 81 is determined as the amount of the *firm's capital resources* available to meet its *guarantee fund* requirement, having regard to *PRU 8.3.45R(2)*. Line 81 must be either:
  - line 79; or
  - (if less) the sum of lines 19, 25, 26, 42, 45, 46, 47 and 59 less the sum of lines 37, 62 and 63.
55. The entry at line 82 is determined as the amount of the *firm's capital resources* available to meet 50% of its *minimum capital requirement*, having regard to *PRU 8.3.45R(1)(a)*. Line 82 must be either:
  - line 79; or
  - (if less) sum of lines 19, 24, 25, 26 and 42 less line 37.
56. The entry at line 83 is determined as the amount of the *firm's capital resources* available to meet 75% of its *minimum capital requirement*, having regard to *PRU 8.3.45R(1)(b)*. Line 83 must be either:
  - line 79; or
  - (if less) the sum of lines 19, 24, 25, 26, 41, 42, 45, 46 and 47 less line 37 and any excess of line 62 over line 59.
57. Amounts relating to financial engineering shown in lines 91-96 must not include amounts in *related undertakings*.

### Instructions 58 onwards apply to all firms

58. Any arrangement relating to *long-term insurance business* which is not entered in lines 91 to 95, but which falls within the definition of financing arrangement in paragraph 12(4) of Appendix 9.4 (Abstract of valuation report) must be disclosed in a supplementary note (code 0305) to this Form.
59. The entry at line 91 (implicit items) must equal the sum of the entries at lines 22 and 41. Lines 92 to 95 do not apply to *general insurance business* and line 91 is only likely to apply to *long-term insurance business*.
60. The entry at line 92 must equal the gross amount of any contingent liability to repay a *debt* to or recapture a liability from a *reinsurer* not already recognised in Form 14. The *firm* must provide in a supplementary note (code 0306) to this Form the following information on each material *reinsurance* arrangement:
- the amount of any *reinsurance* offset (i.e. the amount of the difference between the *mathematical reserves* at the end of the *financial year in question* were that *reinsurance* to be ignored and the amount of the *mathematical reserves* after deducting the *mathematical reserves* reinsured);
  - the amount of the contingent liability for payment to the *reinsurer*; and
  - the commutation value at the end of the *financial year in question* of the *reinsurance* arrangement.
61. The entry at line 93 must equal the amount of any contingent asset receivable from a *cedant* not already recognised in Form 13 or 14. The *firm* must provide in a supplementary note (code 0307) to this Form the following information on each material outgoing *reinsurance* arrangement:
- the amount of any *reinsurance* liability (i.e. the amount of the difference between the *mathematical reserves* at the end of the *financial year in question* including the *mathematical reserves* reinsured 'in', and the amount of the *mathematical reserves* were that *reinsurance* to be ignored);
  - the amount of the contingent asset for payments from *cedants*; and
  - the commutation value at the end of the *financial year in question* of the *reinsurance* arrangement.
62. The amount to be shown for contingent loans at line 94 must be the amount, including any interest accrued, still to be repaid from future profits under the arrangements, as at the end of the *financial year in question*, not already recognised in Form 14.
63. Line 95 must include the potential charge against future profits in respect of any other types of financial engineering not included in lines 91 to 94 where the gross amount of any contingent liability is not already recognised in Form 14.
64. The *firm* must provide an explanation of the nature of the adjustments in line 94 and 95 in a supplementary note (code 0308) to this Form, together with the amount of the adjustment for each material arrangement. As part of this note, the commutation value of each of the items included at lines 94 and 95, to the extent that value is not already a component of line 79, must be disclosed.
65. Details of any promises to *long-term insurance business policyholders* conditional upon future profits (other than bonuses not yet declared), or other charges to future profits not already disclosed, must be provided in a supplementary note (code 0309) to this Form.
66. A reconciliation of net *admissible assets* to *total capital resources* after deductions (line 79) must be provided as a supplementary note (code 0301). The reconciliation must contain the following items:
- (i) Net *admissible assets* [Form 13 line 89 (other than long-term business) plus Form 13 line 89 (long-term) less the sum of lines 11, 12 and 49 in Form 14 less Form 15 line 69]
  - (ii) Any components of *capital resources* that are treated as a liability in Form 14 or 15 (each to be specified and identified to the entries on Forms 3 and 14/15). (In particular this would include any subordinated loan capital.) [These items would be added to net *admissible assets*

in the reconciliation]

- (iii) Any components of *capital resources*, not included in (ii), that arise as a result of a *waiver* and are not represented by *admissible assets* included in Form 13 (each to be specified and identified to the entries on Form 3). (In particular this would include any *implicit items* included as a result of a *waiver* within *capital resources*.) [These items would be added to net *admissible assets* in the reconciliation]
- (iv) Any other items, each such item to be separately specified. An explanation of each such item is to be provided together with, if applicable, the reference to where the item is included elsewhere in the *return* or in the *firm's* stand-alone accounts prepared under the Companies Act 1985 or (for *firms* not preparing accounts under the Companies Act) equivalent overseas legislation or the applicable *United Kingdom* legislation). [These items would be added to or deducted from net *admissible assets* in the reconciliation as appropriate.]

The net *admissible assets* in item (i) plus or minus the additions and deductions in items (ii) to (iv), should equal line 79 (Total capital resources after deductions).

Forms 9 and 9A of Appendix 9.1 (Balance sheet and profit and loss account) are deleted.

The instructions for completion of Form 10 are amended as follows:

### **Instructions for completion of Form 10**

1. An external insurer (other than a pure reinsurer), an EEA-deposit insurer or a Swiss general insurer must complete Form 10 in respect of business carried on through a branch in the United Kingdom. An UK-deposit insurer must complete Form 10 in respect of business carried on through its branches in EEA States taken together.
2. Lines 24-27, 51 and 52 should be blank.
- ~~1. Amounts included at lines 24 to 27 must be as determined in accordance with Rule 2.10.~~
- ~~3.2.~~ Line 63 must be equal to lines 13.92.2 to 13.95.2 less lines 13.92.1 to lines 13.95.1 of the Form for the total other than *long-term insurance business assets* category.
- ~~4. 3.~~ Line 64 must be Form 15.61.2 less 15.61.1.
5. Line 65 should include transfers from or to head office. (note 1002).

Form 11 of Appendix 9.1 (Balance sheet and profit and loss account) is amended, and Form 12 and the instructions to Forms 11 and 12 are replaced as follows:

**Calculation of general insurance capital requirement – premiums amount and brought forward amount****General insurance business : Calculation of required margin of solvency – first method and brought forward**

Name of insurer

Global business / UK branch business / EEA branch business

Financial year ended

General/long-term insurance business

			Company registration number	GL/ UK/ CM	day	month	year	units
			R11					£000
						This financial year 1		Previous year 2
Gross premiums receivable			11					
Premiums taxes and levies (included in line 11)			12					
Premiums receivable net of taxes and levies (11-12)			13					
Premiums for classes 11, 12 or 13 (included in line 13)			14					
Premiums for "actuarial health insurance" (included in line 13)			15					
<b>Sub-total A</b> (13 + $\frac{1}{2}$ 14 - $\frac{2}{3}$ 15)			<b>1516</b>					
<b>Adjusted Sub-total A</b> if financial year is not a 12 month period to produce an annual figure			<b>16</b>					
Division of Sub-total A (or adjusted Sub-total A if appropriate)	Other than health insurance	Up to and including sterling equivalent of 50M EURO x 0.18	17					
		Excess (if any) over 50M EURO x 0.16	18					
	Health insurance	Up to and including sterling equivalent of 50M EURO x 0.06	19					
		Excess (if any) over 50M EURO x 0.16 /3	20					
<b>Sub-total B</b> (17+18+19+20)			<b>21</b>					
Gross premiums earned			<b>2221</b>					
Premium taxes and levies (included in line 2221)			<b>2322</b>					
Premiums <u>earned receivable</u> net of taxes and levies (21-22) (22-23)			<b>2423</b>					
Premiums for classes 11, 12 or 13 (included in line 2325)			<b>2524</b>					
Premiums for "actuarial health insurance" (included in line 23)			<b>25</b>					
<b>Sub-total H</b> (23 + $\frac{1}{2}$ 24 - $\frac{2}{3}$ 25) (24 + $\frac{1}{2}$ 25)			<b>26</b>					
<b>Adjusted Sub-total F</b> if financial year is not a 12 month period to produce an annual figure			<b>27</b>					
Division of Sub-total H	Other than health insurance	Up to and including sterling equivalent of 50M EURO x 0.18	28					
		Excess (if any) over 50M EURO x 0.16	29					
	Health insurance	Up to and including sterling equivalent of 50M EURO x 0.06	30					
		Excess (if any) over 50M EURO x 0.16 /3	31					
<b>Sub-total I</b> (higher of sub-total A and sub-total H) (28+29+30+31)			<b>3230</b>					
<b>Adjusted sub-total I</b> if financial year is not a 12 month period to produce an annual figure			<b>31</b>					
Division of <u>gross adjusted premiums amount</u> : sub-total I (or adjusted sub-total I if appropriate)	Up to and including sterling equivalent of 50M EURO x 0.18		32					
	Excess (if any) over 50M EURO x <u>0.02 0.16</u>		33					
<b>Sub-total J</b> (32-33) (32+33)			<b>34</b>					

**Calculation of general insurance capital requirement – premiums amount and brought forward amount**

**General insurance business : Calculation of required margin of solvency – first method and brought forward**

Name of insurer

Global business / UK branch business / EEA branch business

Financial year ended

General/long-term insurance business

		Company registration number	GL/ UK/ CM	day	month	year	units
		R11					£000
						This financial year 1	Previous year 2
<b>Sub-total J</b> (greater of sub-total B and Sub-total I)						<b>40</b>	
Claims paid in period of 3 financial years						<b>41</b>	
Claims outstanding carried forward at the end of the 3 year period	For insurance business accounted for on an underwriting year basis					<b>42</b>	
	For insurance business accounted for on an accident year basis					<b>43</b>	
Claims outstanding brought forward at the beginning of the 3 year period	For insurance business accounted for on an underwriting year basis					<b>44</b>	
	For insurance business accounted for on an accident year basis					<b>45</b>	
<b>Sub-total C</b> (41+42+43-44-45)						<b>46</b>	
Amounts recoverable from reinsurers in respect of claims included in Sub-total C						<b>47</b>	
<b>Sub-total D</b> (46-47)						<b>48</b>	
<b>Reinsurance ratio</b> (Sub-total D / sub-total C or, if more, 50% or, if less, 100%)						<b>49</b>	
<b>Premiums amount First result</b>							
Sub-total J x reinsurance ratio						<b>5049</b>	
$\frac{G \times \text{Sub-total D}}{\text{Sub-total C}}$ (or, if $\frac{1}{2}$ is a greater fraction, $\times \frac{1}{2}$ )							
Provision for claims outstanding (before discounting and net of reinsurance)						<b>5150</b>	
<b>Brought forward amount</b> (12.43.2 x 51.1 / 51.2 50.1 / 50.2 or, if less, 12.43.2)						<b>5254</b>	
Greater of lines 50 and 52 49 and 54						<b>5352</b>	

**Calculation of general insurance capital requirement– claims amount and result**

Name of insurer

Global business / UK branch business / EEA branch business

Financial year ended

General/long-term insurance business

		Company registration number	GL/ UK/ CM	day	month	year	units
		R12					£000
						This financial year 1	Previous year 2
Reference period (No. of months) See <i>PRU 7.2.63R</i>							
Claims paid in reference period							
Claims outstanding carried forward at the end of the reference period	For insurance business accounted for on an underwriting year basis						
	For insurance business accounted for on an accident year basis						
Claims outstanding brought forward at the beginning of the reference period	For insurance business accounted for on an underwriting year basis						
	For insurance business accounted for on an accident year basis						
Claims incurred in reference period (21+22+23-24-25)							
Claims incurred for classes 11, 12 or 13 (included in 26)							
Claims incurred for "actuarial health insurance" (included in 26)							
<b>Sub-total E</b> (26 + $\frac{1}{2}$ 27 - $\frac{2}{3}$ 28)							
<b>Sub-total F</b> – Conversion of sub-total E to annual figure (multiply by 12 and divide by number of months in the reference period)							
Division of sub-total F (gross adjusted claims amount)	x 0.26						
	Excess (if any) over 35M EURO x 0.03						
<b>Sub-total G</b> (32 - 33)							
<b>Claims amount</b> Sub-total G x <b>reinsurance ratio</b> (11.49)							
Higher of <b>premiums amount</b> and <b>brought forward amount</b> (11.53)							
<b>General insurance capital requirement</b> (higher of lines 41 and 42)							



## Instructions for completion of Forms 11 and 12

### Long-term insurance business

1. For a *composite firm*, Forms 11 and 12 must be completed separately for the total *general insurance business* and for the total *long-term insurance business* which is *class IV* or supplementary accident and sickness insurance business. For other *firms*, the forms must be completed for the total *general insurance business* or for the total *long-term insurance business* which is *class IV* or supplementary accident and sickness insurance business, as appropriate.
2. Notwithstanding instruction 1, if the gross annual office premiums for *class IV* business and supplementary accident and sickness insurance in force on the 'valuation date' do not exceed 1% of the gross annual office premiums in force on that date for all *long-term insurance business*, Forms 11 and 12 need not be completed for *long-term insurance business* as long as it can be stated that the entry in line 21 of Form 60 exceeds the amount that would be obtained if Forms 11 and 12 were to be completed for *long-term insurance business*. In this circumstance, the method of estimating the entry in line 21 of Form 60, together with a statement of the gross annual office premiums in force at the 'valuation date' in respect of *Class IV* business and supplementary accident and sickness insurance, must be given.
3. When completing Forms 11 and 12 for *long-term insurance business* the accounting conventions for *general insurance business* should be followed, but reasonable approximations may be used if they are unlikely to result in an underestimate of the *insurance health risk capital component*.

### Marine mutuals

4. In the case of a *marine mutual* completing an abbreviated *return* under rule 9.36A, units must be the same as those used in Form M1. If units are in US\$ or US\$000, then references to the sterling equivalent of Euro in line 33 of Form 11 and lines 33 of Form 12 must be taken to be references to the US\$ equivalent of the specified amount of Euro and the Forms must be amended to reflect the use of US\$. The bases of conversion adopted must be stated by way of a supplementary note to Form 11 (code 1101).

### Pure reinsurers

5. Lines 14 and 24 of Form 11 and line 27 of Form 12 must be left blank for a *pure reinsurer* that does not have *permission* under the *Act* to effect *contracts of insurance*.

### Prior year figures

6. *PRU 7.2.71R* requires recalculation of the *gross adjusted premiums amount* and the *gross adjusted claims amount* (but not during *financial years* beginning before 31 December 2004, because of the transitional provisions) if there has been a significant change to the business portfolio. This may alter the *claims amount* or the *premiums amount* used in calculating the *general insurance capital requirement* for the *financial year* in question. For this reason, entries in column 2 (but not the *brought forward amount*: this should (errors excepted) equal the *brought forward amount* calculated in the previous year's return) may differ from the corresponding entries from the previous year. Any restatement of the figures should be explained by way of a supplementary note to Form 11 (code 1102) and Form 12 (code 1202).
7. If the *financial year* began before 1 January 2004: then
  - 11.14.2, 11.24.2, 11.52.2 and 12.27.2 should be left blank;
  - lines 21 to 41, column 2, of Form 12 relating to *long-term insurance business*, should be left blank; and
  - no amounts should be included in column 2 of Form 11 that relate to *class IV* business.
8. Where the *financial year* began between 1 January 2004 and 31 December 2004 (inclusive), the previous *financial year's* figures would normally be those sent to the *FSA* under rule 9.6(1B) and may be unaudited.
9. If the *financial year* began before 1 January 2005:
  - the treatment of "actuarial health insurance" in the calculation will have changed and prior year figures in lines 32 and 33 of Form 11 and lines 32 and 33 of Form 12 may be inappropriate because the form does not represent the calculation at the time. If so, these figures should be left blank and an

explanation should be provided by way of a supplementary note to Form 11 (code 1103) and Form 12 (code 1203).

- the *firm* would not have had a reference period in relation to the *previous financial year* if it had been in existence for less than 3 or 7 *financial years* (as appropriate). If it had no reference period, then lines 11 to 41, column 2, of Form 12 should be left blank.

#### Premiums and claims

10. *PRU 7.2.66R* requires amounts of *premiums* and *claims* to be determined in accordance with *PRU 1.3* and so (by virtue of *PRU 1.3.5R*) normal accounting conventions will generally apply. However, *premiums* and *claims* are defined by references to *contracts of insurance* and these themselves are defined by the *Regulated Activities Order* so that *premiums* or *claims* may be included for contracts that would not be treated as insurance under normal accounting conventions.

#### Euro

11. The Euro amounts in the calculation of line 33 of Form 11 and line 33 of Form 12 will change from time to time as the result of indexation in accordance with *PRU 7.2.49R*. The conversion rate to be used is described in *PRU 7.2.50R*. Changes in the Euro amounts or conversion rates will not affect prior year figures.

#### Actuarial health insurance

12. "Actuarial health insurance" refers to health insurance business that meets the conditions of *PRU 7.2.72R* or for *class IV insurance business* those conditions as modified by *PRU 7.2.86R*.

#### **Instructions for completion of Form 11**

1. Line 30 represents the *gross adjusted premiums amount* calculated in accordance with *PRU 7.2.56R*, if the *financial year* has 12 months. Otherwise line 31 represents the *gross adjusted premiums amount*.
2. In accordance with *PRU 7.2.54R*, the reinsurance ratio calculated at line 49 must be:
  - 100% if sub-total D / sub-total C exceeds 100%;
  - 50% if sub-total D / sub-total C is less than 50%; and
  - sub-total D / sub-total C, otherwise.
3. The provisions in line 51 must be net of *reinsurance* and must not be discounted or reduced to take account of investment income, except for:
  - risks in *classes 1 or 2*;
  - reductions to reflect the discounting of annuities; and
  - a *pure reinsurer* that does not have *permission* under the *Act* to effect *contracts of insurance*.For these exceptions, the discount must be calculated in accordance with *PRU 1.3.5R* and, if any amounts in line 51 are discounted, a supplementary note to the Form 11 (code 1104) must describe the items that are discounted.

#### **Instructions for completion of Form 12**

1. The reference period in line 11 is specified in *PRU 7.2.63R*.
2. Statistical methods may be used to allocate the *claims*, provisions and recoveries in respect of *classes 11, 12 and 13* in line 27.
3. Line 31 represents the *gross adjusted claims amount* calculated in accordance with *PRU 7.2.60R*.

Line 43 represents the *general insurance capital requirement* that relates to the following *financial year*: that is the year commencing on the day after the year end to which the *returns* relate.

...

Forms 13, 14, 15 and 16 of Appendix 9.1 (Balance sheet and profit and loss account) are amended as follows:

**Analysis of admissible assets**

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

Category of assets

		Company registration number	GL/UK/CM	Period ended			Units	Category of assets
				day	month	year		
		<b>R13</b>					<b>£000</b>	
<b>Debtors</b>						As at the end of this financial year	As at the end of the previous year	
<b>Other assets</b>						<b>1</b>	<b>2</b>	
Debtors arising out of direct insurance operations	Policyholders					<b>71</b>		
	Intermediaries					<b>72</b>		
Salvage and subrogation recoveries						<b>73</b>		
Debtors arising out of reinsurance operations	Due from ceding insurers and intermediaries under reinsurance business accepted					<b>74</b>		
	Due from reinsurers and intermediaries under reinsurance contracts ceded					<b>75</b>		
Other debtors	Due from dependants	Due in 12 months or less after the end of the financial year				<b>76</b>		
		Due more than 12 months after the end of the financial year				<b>77</b>		
	Other	Due in 12 months or less after the end of the financial year				<b>78</b>		
		Due more than 12 months after the end of the financial year				<b>79</b>		
Tangible assets						<b>80</b>		
Cash at bank and in hand	Deposits not subject to time restriction on withdrawal, with approved credit institutions and approved financial institutions and local authorities					<b>81</b>		
	Cash in hand					<b>82</b>		
Other assets (particulars to be specified by way of supplementary note)						<b>83</b>		
Prepayments and accrued income	Accrued interest and rent					<b>84</b>		
	Deferred acquisition costs					<b>85</b>		
	Other prepayments and accrued income					<b>86</b>		
Deductions (under rules 4.14(2)(b) and 4.14(3)) from the aggregate value of assets						<b>87</b>		
Total sheet 3 (71 to 86 less 87)						<b>88</b>		
Grand total of admissible assets after deduction of market risk and counterparty limits (39+69+88)						<b>89</b>		

**Reconciliation to asset values determined in accordance with the insurance accounts rules**

Total admissible assets after deduction of market risk and counterparty limits (as per line 89 above)	<b>91</b>		
Total assets in excess of the admissibility limits of Appendix 4.2 (as valued in accordance with those rules before applying admissibility limits) – Assets in excess of market and counterparty limits	<b>92</b>		
Solvency margin deduction for subsidiary undertakings which are insurance undertakings. Capital resources requirement deduction for subsidiary undertakings which are insurance undertakings.	<b>93</b>		
Other differences in the valuation of assets (other than for assets not valued above)	<b>94</b>		
Assets of a type not valued above (as valued in accordance with the insurance accounts rules). Other inadmissible assets	<b>95</b>		
Total assets determined in accordance with the insurance accounts rules (91 to 95)	<b>99</b>		

Amounts included in line 89 attributable to debts due from related insurers, other than those under contracts of insurance or reinsurance	<b>100</b>		
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### Instructions for completion of Form 13

1. Form 13 must be completed for the total *long-term insurance business assets* of the *insurer* or *branch* and for each fund or group of funds for which separate assets are appropriated. The words "total *long-term insurance business assets*" or the name of the fund must be shown against the heading "Category of assets". The corresponding code box must contain "10" for the total assets and, in the case of separate funds, code numbers allocated sequentially beginning with code "11".
2. Form 13 must be completed in respect of the total assets of the *insurer* or *branch* other than any *long-term insurance business assets*. The words "total other than *long-term insurance business assets*" must be shown against the heading "Category of assets", and the corresponding code box must contain "1".
3. (a) In the case of the *United Kingdom branch return* of an *external insurer* (other than a *pure reinsurer*) Form 13 must be completed for the following categories of assets -

Category	Code - other than <i>long-term insurance business assets</i>	Code - <i>long-term insurance business assets</i>
In the case of a <i>non-EEA insurer</i> , assets deposited under <del>rule 8.1(1)</del> <u>PRU 7.6.54R</u>	2	6
Assets maintained in the <i>United Kingdom</i>	3	7
Assets maintained in the <i>United Kingdom</i> and the other <i>EEA States</i>	4	8

- (b) In the case of an *EEA branch return* of a *UK-deposit insurer* which has made a *deposit* under ~~rule 8.1(2)~~ PRU 7.6.54R, Form 13 must be completed for the following categories of assets -

Category	Code – other than <i>long-term insurance business assets</i>	Code – <i>long-term insurance business assets</i>
Assets deposited under <del>rule 8.1(2)</del> <u>PRU 7.6.54R</u>	2	6
Assets maintained in the <i>United Kingdom</i> and the other <i>EEA States</i>	4	8
Assets maintained in the <i>United Kingdom</i> and the <i>EEA States</i> where <i>insurance business</i> is carried on	5	9

4. In lines 11 to 86 -
  - (a) for the purpose of classifying (but not valuing) assets, headings and descriptions used above, wherever they also occur in the balance sheet format in Schedule 9A to the *Companies Act*, must have the same meaning as in that Schedule,
  - (b) *dependants* of the *firm* must be valued in accordance with PRU 1.3.35R,
  - (c) a *related undertaking* that is not a *dependant* of the *firm* must be valued in accordance with PRU 1.3.35R unless:
    - It is an *ancillary services undertaking* which must be valued at zero;

- It is a *related undertaking* that is not a *regulated related undertaking* which must be valued in accordance with *PRU 1.3.11R*; or
- It is a *regulated related undertaking* which the *firm* has made an election to value in accordance with *PRU TR 25R*

~~(b)~~(d) other assets must be valued in accordance with rule 9.10, and

~~(e)~~(e) assets of any particular description must be shown after deduction of assets of that description which (for any reason) fall to be left out of account under ~~rule 4.14(2)(a)~~ *PRU 3.2.22R(3)(a)*, (b), (c), (g) and (h). Negative amounts should not be shown at lines 11 to 86. If a deduction is more than the value of the assets to which it relates, the excess element of the deduction should be shown at line 87; and

(f) deductions in respect of *market risk* and *counterparty risk* are to be shown in line 87, to the extent that (e) does not require them to be recognised in other lines.

5. The aggregate value of those investments which are:

- (a) *unlisted* investments falling within any of lines 41, 42, 46 or 48 which have been valued in accordance with ~~the rules in rule 4.8~~ *PRU 1.3*;
- (b) *listed* investments falling within any of lines 41, 42, 46 or 48 which have been valued in accordance with ~~rule 4.8~~ the rules in *PRU 1.3* and which are not *readily realisable*;
- (c) units or other beneficial interests in *collective investment schemes* ~~falling within rule 4.9(1)(e)~~ that:
  - (i) are not schemes falling within the *UCITS Directive*;
  - (ii) are not authorised unit trust schemes or recognised schemes within the meaning of *Part XVII of the Act*;
  - (iii) do not employ *derivative contracts* unless they meet the criteria in *PRU 4.3.5R*;
  - (iv) do not employ contracts or assets having the effect of *derivative contracts* unless they have the effect of *derivative contracts* that meet the criteria in *PRU 4.3.5R*; and
  - (v) do not include assets other than *admissible assets* among their property; or
- (d) reversionary interests or remainders in property other than land or buildings,

must be stated by way of a supplementary note (code 1301 for other than *long-term insurance business* and code 1308 for *long-term insurance business*) to this Form, together with a description of such investments.

6. The aggregate value of those investments falling within lines 46 or 48 which are *hybrid securities* are to be stated by way of a supplementary note (code 1302 for other than *long-term insurance business* and code 1309 for *long-term insurance business*) to this Form.

7. Amounts in respect of salvage or subrogation included above other than at line 73 are to be stated by way of a supplementary note (code 1303) to this Form.

8. The entry at line 85 must be equal to the sum of lines 22.29.3 and lines 25.24.99-99.

9. In line 93 "*Solvency margin deduction for subsidiary undertakings which are insurance undertakings*" refers to deductions under rule 4.2. The amount to be shown in line 93 shall represent the total of the relevant proportions in accordance with *PRU 1.3.37R* and *PRU 1.3.38R* of the *individual capital*

resources requirements of the regulated related undertakings.

10. In line 95 "Assets of a type not valued above" refers to assets left out of account under rule 4.1(3). In line 95 "inadmissible assets" refers to those assets described at PRU 2.2.86R that are not assets listed in PRU 2 Annex 1R.
11. Lines 60 to 63 and 85 relate only to *general insurance business*.
12. Lines 60 to 63 and 85 must be left blank for "Category of assets" codes "2", "3", "4" and "5".
13. Since the *technical provisions* for *claims* outstanding shown in **Form 15** may only be discounted or reduced to take account of investment income in limited circumstances, the amount shown at line 12 of **Form 15** may need to be increased (see instruction 4 to **Form 15**). In such cases, the *reinsurers'* share shown at line 61 must be adjusted to be consistent with the amount shown in line 12.
14. It would be appropriate to state the amount of any tangible leased asset included at line 80 by way of a supplementary note (code 1314 for other than *long-term insurance business* and code 1316 for *long-term insurance business*) to this Form.
15. Particulars of any other assets included at line 83 must be stated by way of a supplementary note (code 1315 for other than *long-term insurance business* and code 1317 for *long-term insurance business*) to this Form.

The source column of Form 14 is deleted.

Form 14

**Long term insurance business liabilities and margins**

Name of insurer

Global business/UK branch business/EEA branch

Financial year ended

Category of assets

		Company registration number	GL/UK/CM	day	month	year	units	Category of assets	
R14							£000		
						As at end of this financial year 1	As at end of the previous year 2		
Mathematical reserves, after distribution of surplus						11			
Cash bonuses which had not been paid to policyholders prior to end of the financial year						12			
Balance of surplus / (valuation deficit)						13			
Long term insurance business fund carried forward (11 to 13)						14			
Claims outstanding which had fallen due for payment before the end of the financial year		Gross amount				15			
		Reinsurers' share				16			
		Net (15-16)				17			
Provisions for other risks and charges		Taxation				21			
		Other				22			
Deposits received from reinsurers						23			
Creditors and other liabilities	Arising out of insurance operations	Direct insurance business				31			
		Reinsurance accepted				32			
		Reinsurance ceded				33			
	Debenture loans	Secured				34			
		Unsecured				35			
	Amounts owed to credit institutions						36		
	Other creditors	Taxation				37			
		Other				38			
Accruals and deferred income						39			
Provisions for adverse changes (calculated in accordance with rule 5.3) Provision for "reasonably foreseeable adverse variations"						41			
Total other insurance and non-insurance liabilities (17 to 41)						49			
Excess of the value of net admissible assets						51			
Total liabilities and margins						59			
Amounts included in line 59 attributable to liabilities to related companies, other than those under contracts of insurance or reinsurance						61			
Amounts included in line 59 attributable to liabilities in respect of property linked benefits						62			
Amount of any additional mathematical reserves included in line 51 which have been taken into account in the appointed actuary's certificate						63			



## Instructions for completion of Form 14

1. The Form must be completed for the total *long-term insurance business liabilities* and margins of the *insurer* or *branch* and for each fund or group of funds for which separate assets are appropriated. The words “total *long term insurance business assets*” or the name of the fund must be shown against the heading “Category of assets”. The corresponding code box must be completed with the same entries as were used on the corresponding Form 13.
  2. The entry at line 11 must equal the sum of lines 21, 43, 44 and 45 of the appropriate Form or Forms 58.
  3. The entry at line 12 must equal line 42 of the appropriate Form or Forms 58.
  4. The entry at line 13 must equal line 49 of the appropriate Form or Forms 58.
  5. The entry at line 14 must equal line 59 of the appropriate Form or Forms 40.
  6. Where the provision required by PRU 4.3.17R(3) is implicit (i.e. the obligation to pay the monetary amount is recognised under the rules in PRU 1.3), it would be appropriate to state, in a supplementary note (code 1404) to this Form, the amount of the provision.
- 67 The entry at line 51 must be:
- (a) the value of the *admissible assets* (as included in line 89 of the appropriate Form 13) representing the *long-term insurance funds*, fund or group of funds to which the Form relates, less
  - (b) the amount of those funds, fund or group of funds, being the sum of the amounts shown at lines 14 and 49.
- 7-8 The entry at line 63 must be zero for financial years ending on or after 31 December 2004. the amount specified in the appointed actuary's certificate in accordance with paragraph 8(a)(ii) of Appendix 9.6, but only insofar as it relates to the fund, funds or group of funds to which this Form 14 relates.
9. It would be appropriate to state, in a supplementary note (code 1403) to this Form, the amount of each provision, included in line 22, in respect of a deficit in a regulated related undertaking and the identity of the undertaking.

**Liabilities (other than long term insurance business)**

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

		Company registration number	GL/UK/CM	Period ended		Units	
		R15		day	month	£000	
				As at the end of this financial year	1	As at the end of the previous year	
				2			
Technical provisions (gross amount)	Provision for unearned premiums	11					
	Claims outstanding	12					
	Provision for unexpired risks	13					
	Equalisation provisions	Credit business	14				
		Other than credit business	15				
	Other	16					
	Total (11 to 16)	19					
Provisions for other risks and charges	Taxation	21					
	Other	22					
Deposits received from reinsurers		31					
Creditors	Arising out of insurance operations	Direct insurance business	41				
		Reinsurance accepted	42				
		Reinsurance ceded	43				
	Debenture loans	Secured	44				
		Unsecured	45				
	Amounts owed to credit institutions		46				
	Other creditors	Taxation	47				
		Recommended dividend	48				
Other		49					
Accruals and deferred income		51					
Total (19 to 51)		59					
Provision for "reasonably foreseeable adverse variations" adverse changes calculated in accordance with Rule 5.3 [Regulation 61 of the Insurance Companies Regulations 1994]		61					
Cumulative preference share capital		62					
Subordinated loan capital		63					
Total (59 to 63)		69					
Amounts included in line 69 attributable to liabilities to related insurers, other than those under contracts of insurance or reinsurance		71					

## Instructions for completion of Form 15

1. Amounts in lines 11 to 13 and 16 must be stated gross of *reinsurers'* share.
2. The aggregate amount of any accrued dividend in respect of cumulative *preference shares* issued by the *insurer* must be shown by way of a supplementary note (code 1503) to this Form.
3. Only equalisation provisions that are created as a result of a regulatory requirement are to be included at lines 14 and 15
4. The amount shown in line 12 may only be discounted or reduced to take account of investment income:
  - (a) for *Class 1* or *2* business; or
  - (b) in respect of annuities; or
  - (c) if the *insurer* is a *pure reinsurer* which does not have permission under the *Act* to effect *contracts of reinsurance*.

So, if the *technical provisions* for *claims* outstanding for other business are discounted or reduced to take account of investment income, then they must be increased by the difference between the undiscounted and the discounted provisions. If the *technical provisions* are increased the amount of the increase must be shown by way of a supplementary note (code 1505) to this Form, together with the corresponding increase in the *reinsurers'* share shown in line 61 of **Form 13**.

5. It would be appropriate to state the amount of each provision, included in line 22, in respect of a deficit in a regulated related undertaking and the identity of the undertaking in a supplementary note (code 1504) to this Form.
6. Where the provision required by PRU 4.3.17R(3) is implicit (i.e. the obligation to pay the monetary amount is recognised under the rules in PRU 1.3), it would be appropriate to state, in a supplementary note (code 1506) to this Form, the amount of the provision.

...

### **Instructions for completion of Form 16**

1. In addition to the supplementary note (code 1601) required under **Appendix 9.1** paragraph 5(2), where any brought forward amounts on any Form are restated due to currency reconversion it would be appropriate to briefly state this fact in a supplementary note (code 1602) to this Form in order to facilitate the FSA's computerised validation of the return. This fact may be stated by a simple statement, e.g. 'Some of the brought forward amounts shown in the forms xx to xx have been restated from the corresponding carried forward amounts included in the previous year's return due to the reconversion of foreign currency amounts at a different rate of exchange'. No further details need be given.
2. Particulars of any amounts included at lines 21 must be stated by way of a supplementary note (code 1603) to this Form.
3. Particulars of any amounts included at lines 41 must be stated by way of a supplementary note (code 1604) to this Form.

...

Forms 18 and 19 of Appendix 9.1 (Balance sheet and profit and loss account) are inserted as follows:

**With-profits insurance capital component for the fund**

Name of insurer  
 With-profits fund  
 Financial year ended  
 Units

	<b>As at end of this financial year 1</b>	<b>As at end of the previous year 2</b>
--	---	---

**Regulatory excess capital**

Regulatory value of assets	Long-term admissible assets of the fund	11		
	Implicit items allocated to the fund	12		
	Mathematical reserves in respect of non-profit insurance contracts written in the fund	13		
	Long-term admissible assets of the fund covering the long-term insurance capital requirement allocated in respect of non-profit insurance contracts written in the fund	14		
	Long-term admissible assets of the fund covering the resilience capital requirement allocated in respect of non-profit insurance contracts written in fund	15		
	Total (11+12-(13+14+15))	19		
Regulatory value of liabilities	Mathematical reserves (after distribution of surplus) in respect of the fund's with-profit insurance contracts	21		
	Regulatory current liabilities of the fund	22		
	Total (21+22)	29		
Long-term insurance capital requirement in respect of the fund's with-profits insurance contracts		31		
Resilience capital requirement in respect of the fund's with-profits insurance contracts		32		
Sum of regulatory value of liabilities, long-term insurance capital requirement and resilience capital requirement (29+31+32)		39		
Regulatory excess capital (19-39)		49		

**Realistic excess capital**

Realistic excess capital	51		
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**Excess assets allocated to with-profits insurance business**

Excess (deficiency) of assets allocated to with-profits insurance business in fund (49-51)	61		
Face amount of capital instruments attributed to the fund and included in capital resources (unstressed)	62		
Realistic amount of capital instruments attributed to the fund and included in capital resources (stressed)	63		
With-profits insurance capital component for fund (if 62 exceeds 63, greater of 61+62-63 and zero; else greater of 61 and zero)	64		

**Instructions for completion of Form 18**

1. The entries at lines 11, 12, 13, 14 and 15 must equal the values determined in accordance with *PRU 7.4.24R*.
2. The entry at line 19 must equal the value determined in accordance with *PRU 7.4.23R(1)*.
3. The entries at lines 21 and 22 must equal the values determined in accordance with *PRU 7.4.29R*.
4. The entries at lines 29, 31 and 32 must equal the values determined in accordance with *PRU 7.4.23R(2)(a)*, (b) and (c) respectively.
5. The entry at line 39 must equal the value determined in accordance with *PRU 7.4.23R(2)*.
6. The entry at line 49 must equal the value determined in accordance with *PRU 7.4.23R*.
7. The entry at line 51 must equal the value at Form 19, Line 66.
8. The entry at line 62 must equal C, determined in accordance with *PRU 7.4.7R(3)(a)*.
9. The entry at line 63 must equal D, determined in accordance with *PRU 7.4.7R(3)(b)*.
10. The entry at line 64 must equal the contribution in respect of the fund to the aggregate value determined in accordance with *PRU 7.4.7R(1)*.

**Realistic balance sheet**

Name of insurer  
With-profits fund  
Financial year ended  
Units

	As at end of this financial year 1	As at end of the previous year 2
--	---	---

**Realistic value of assets available to the fund**

Regulatory value of assets	11	
Implicit items allocated to the fund	12	
Value of shares in subsidiaries held in fund (regulatory)	13	
Excess admissible assets	21	
Present value of future profits (or losses) on non-profit insurance contracts written in the fund	22	
Value of derivatives and quasi-derivatives not already reflected in lines 11 to 22	23	
Value of shares in subsidiaries held in fund (realistic)	24	
Prepayments made from the fund	25	
Realistic value of assets of fund (11+21+22+23+24+25-(12+13))	26	
Support arrangement assets	27	
Assets available to the fund (26+27)	29	

**Realistic value of liabilities of fund**

With-profits benefit reserve	31		
Future policy related liabilities	Past miscellaneous surplus attributed to with-profits benefits reserve	32	
	Past miscellaneous deficit attributed to with-profits benefits reserve	33	
	Planned enhancements to with-profits benefits reserve	34	
	Planned deductions for the costs of guarantees, options and smoothing from with-profits benefits reserve	35	
	Planned deductions for other costs deemed chargeable to with-profits benefits reserve	36	
	Future costs of contractual guarantees (other than financial options)	41	
	Future costs of non-contractual commitments	42	
	Future costs of financial options	43	
	Future costs of smoothing (possibly negative)	44	
	Financing costs	45	
	Any other liabilities related to regulatory duty to treat customers fairly	46	
	Other long-term insurance liabilities	47	
	Total (32+34+41+42+43+44+45+46+47-(33+35+36))	49	
Realistic current liabilities of the fund	51		

Realistic value of liabilities of fund (31+49+51)	59		
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**Realistic balance sheet**

Name of insurer  
With-profits fund  
Financial year ended  
Units

	As at end of this financial year 1	As at end of the previous year 2
--	---	---

**Realistic excess capital and additional capital available**

Value of relevant assets before applying the most adverse scenario other than present value of future profits arising from business outside with-profits funds	62		
Amount of present value of future profits (or losses) on long-term insurance contracts written outside the fund included in the value of relevant assets before applying most adverse scenario	63		
Value of relevant assets before applying the most adverse scenario (62+63)	64		
Risk capital margin for fund (62-59)	65		
Realistic excess capital for fund (26-(59+65))	66		
Realistic excess available capital for fund (29-(59+65))	67		
Working capital for fund (29-59)	68		
Working capital ratio for fund (68/29)	69		

**Other assets potentially available if required to cover the fund's risk capital margin**

Additional amount potentially available for inclusion in line 62	81		
Additional amount potentially available for inclusion in line 63	82		

## Instructions for completion of Form 19

1. The entry at line 11 must equal the value at Form 18, Line 19.
2. The entry at line 12 must equal the value at Form 18, Line 12.
3. The entry at line 13 must be the amount determined in accordance with *PRU* 1.3 and excluded from the amount calculated in accordance with *PRU* 7.4.33R(1)(a).
4. The entry at line 21 must be the amount of the fund's excess *admissible assets*, determined in accordance with *PRU* 7.4.33R(1)(b).
5. The entry at line 22 must be the present value of future profits (or losses) on any *non-profit insurance contracts* written in the *with-profits fund*, determined in accordance with *PRU* 7.4.33R(1)(c).
6. The entry at line 23 must be the market value of any *derivative* or *quasi-derivative* determined in accordance with *PRU* 7.4.33R(1)(d).
7. The entry at line 24 must be the amount determined in accordance with *PRU* 7.4.33R(1)(e).
8. The entry at line 25 must be the amount determined in accordance with *PRU* 7.4.33R(1)(f).
9. The entry at line 26 must be the amount determined in accordance with *PRU* 7.4.32R(1).
10. The entry at line 27 must be any other amount providing capital support to the fund under a support arrangement, included with the prior agreement of the *FSA*.
11. The entry at line 31 must be the amount determined in accordance with *PRU* 7.4.40R(1).
12. The entries at lines 32, 33, 34, 35, 36, 41, 42, 43, 44, 45, 46 and 47 must be the amounts determined in accordance with *PRU* 7.4.137R(1) to (11).
13. The entry at line 32 is the (positive) amount determined in accordance with *PRU* 7.4.137R(1) if this represents a surplus.
14. The entry at line 33 is the (positive) amount determined in accordance with *PRU* 7.4.137R(1) if this represents a deficit.
15. The entries at lines 34, 35, 36, 41, 42, 43, 44 and 45 are the amounts determined in accordance with *PRU* 7.4.137R(2) to (9) respectively.
16. The entries at lines 46 and 47 are the values determined in accordance with *PRU* 7.4.137R(10) and (11).
17. The entry at line 49 must be the amount determined in accordance with *PRU* 7.4.40R(2).
18. The entry at line 51 must be the amount determined in accordance with *PRU* 7.4.40R(3).
19. The entry at line 59 must be the amount determined in accordance with *PRU* 7.4.32R(2)(a).
20. The entry at line 62 must be the amount described as A and determined in accordance with *PRU* 7.4.43R(3)(a) adjusted to exclude any amount taken into consideration under *PRU* 7.4.45R(2)(c).
21. The entry at line 63 must be any amount taken into consideration under *PRU* 7.4.45R(2)(c) in determining the amount described as A in accordance with *PRU* 7.4.43R(3)(a).
22. The entry at line 64 must be the amount described as A and determined in accordance with *PRU* 7.4.43R(3)(a).
23. The entry at line 65 must be the amount determined in accordance with *PRU* 7.4.32R(2)(b).
24. The entry at line 66 must be the amount determined in accordance with *PRU* 7.4.32R.
25. The entry at line 81 must be an amount not exceeding the sum of the value of the net shareholders assets of the *firm* and the surplus assets of the *firm's non-profit funds*, to the extent not included at any Form 19 line 27 or at any Form 19 line 62 and to the extent not required to meet regulatory capital requirements in respect of any business written outside the fund.
26. The entry at line 82 must be an amount not exceeding 50% of the present value of future profits arising from insurance contracts written by the *firm* outside its *with-profits funds* reduced by the sum of any amounts included at any Form 19 line 63.

APPENDIX 9.2 (rules 9.14 and 9.22)

**GENERAL INSURANCE BUSINESS:  
REVENUE ACCOUNT AND ADDITIONAL INFORMATION  
(FORMS 20 TO 39)**

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...

7. Where an *insurer* includes *insurance business* in another *accounting class* under 6(1) or 6(2)(a), the following information must be stated by way of a supplementary note (code 2001) to **Form 20** -

...

...

**Presentation of amounts**

- 8A Where in any Form an amount which is shown brought forward from a previous year differs from the corresponding amount shown as carried forward from that year and the difference is not due solely to the use of a different rate to express other currencies in sterling, an explanation of the reason for the difference must be given by way of a supplementary note to that Form in accordance with **Appendix 9.1** paragraph 7. For **Forms 21, 22, 23, 24, 26, 27, 28, 31, 32, 33, 34** or **35**, the code for the supplementary note is 2101, 2201, 2301, 2401, 2601, 2701, 2801, 3101, 3201, 3301, 3401 or 3501 respectively.

...

**UK and overseas business**

16. (1) For each *accounting class* there must be stated separately for business accounted for on an accident year and on an underwriting year basis the following by way of a supplementary note (code 2002) to **Form 20** –

...

...

**Transfers of general insurance business**

17. (1) If, during the *financial year*, *policies* already effected by another *insurer* have been transferred to the *insurer*, an *insurer* must state, in respect of each *accounting class*, the following by way of a supplementary note to **Form 23** (code 2302) and **Form 24** (code 2403) -

...

...

**Unearned premiums**

18. In **Forms 21** and **25**, the basis on which unearned premiums are calculated and the reason for adopting this basis must be stated by way of supplementary note

(code 2102 in the case of Form 21 and code 2501 in the case of Form 25).

...

### **Provision for unexpired risks**

...

20. (1) Where the amount included at column 3 line 19 (provision for unexpired risks) in any **Form 22** or at column 99-99 of line 23 (provision for unexpired risks) in any **Form 25** has been determined after taking into account expected investment return, the following must be stated by way of supplementary note (code 2205 in the case of Form 22 and code 2502 in the case of Form 25) –

...

...

### **Cessation of business**

21. (1) If the *insurer* has effected no 'new contracts of insurance' of any one or more *classes* of *general insurance business* during the financial year in question, the date on which the last 'new contract' of each such *class* was effected must be stated by way of a supplementary note (code 2003) to Form 20.

...

### **Claims management costs**

22. (1) In **Forms 22** and **24**, the basis used for the determination of amounts for *claims management costs* payable in the *financial year in question* and carried forward to the following financial year must be stated by way of a supplementary note (code 2202 in the case of Form 22 and code 2404 in the case of Form 24).

...

- (4) Where the amount in respect of *claims management costs* carried forward and included in any Form 22 or 24 has been determined after taking into account expected investment return, there must be stated by way of supplementary note to ~~that~~ Form 22 (code 2203) or Form 24 (code 2405)-

...

### **Acquisition costs**

23. The basis used for determination of the amounts for acquisition costs (other than commission) payable in the *financial year in question* and carried forward to the next *financial year*, as shown at line 22 of **Form 22** and line 42 of **Form 24**, must be stated by way of a supplementary note to ~~these~~ Forms 22 (code 2204) and Form 24 (code 2406).

### **Underwriting year accounting**

24. (1) With reference to the *financial year in question* and in respect of each *accounting class*, the following information must be stated by way of a supplementary note (code 2402) to **Form 24** –

...

**Business managed together**

...

25. ...  
(2) Where any amount is shown on **Form 25** or **29** for the transfer of anticipated surplus, the following must be stated by way of supplementary note to ~~that Form~~ **Form 25** (code 2504) or **Form 29** (code 2901) –

...

**Application of accounting practice**

26. ...  
(2) Where amounts of in respect of an inwards or outwards *contract of insurance* have been excluded from the revenue account, the following must be shown by way of a supplementary note (code 2004) to **Form 20** –

...

...

27. ...  
(5) The following must be stated by way of supplementary note (code 3003) to **Form 30** –

...

28. Where the *reinsurers'* share of *claims* incurred (as stated in any Form 22 or **25**) includes amounts expected to be covered from *reinsurers* more than 12 months after the payment of the underlying gross *claims* by the *insurer*, the following must be stated by way of supplementary note to **Form 22** (code 2206) or **25** (code 2503) (as appropriate) –

...

...

29. ...  
(2) Where the name required by (1) is not sufficient to identify the nature of the objects exposed to such risks and the nature of the cover provided against such risks, the information must be stated by way of a supplementary note to **Form 31** (code 3102), **32** (code 3202) or **34** (code 3402) as the case may be.

...

...

### **Country codes**

31. The country codes required for **Forms 31, 32 and 34** must be in accordance with the following Table:

<b><u>COUNTRY</u></b>	<b><u>CODE</u></b>
<u>Afghanistan</u>	<u>QS</u>
<u>Albania</u>	<u>CE</u>
<u>Algeria</u>	<u>KA</u>
<u>Andorra</u>	<u>CG</u>
<u>Angola</u>	<u>MT</u>
<u>Anguilla</u>	<u>GY</u>
<u>Antigua And Barbuda</u>	<u>GP</u>
<u>Argentina</u>	<u>JA</u>
<u>Armenia</u>	<u>RB</u>
<u>Aruba</u>	<u>GM</u>
<u>Australia</u>	<u>EA</u>
<u>Austria</u>	<u>BL</u>
<u>Azerbaijan</u>	<u>RC</u>
<u>Bahamas</u>	<u>GD</u>
<u>Bahrain</u>	<u>PN</u>
<u>Bangladesh</u>	<u>QA</u>
<u>Barbados</u>	<u>GA</u>
<u>Belarus</u>	<u>RD</u>
<u>Belgium</u>	<u>BD</u>
<u>Belize</u>	<u>HH</u>
<u>Benin</u>	<u>LK</u>
<u>Bermuda</u>	<u>GE</u>
<u>Bhutan</u>	<u>QX</u>
<u>Bolivia</u>	<u>JL</u>
<u>Bosnia and Herzegovina</u>	<u>CH</u>
<u>Botswana</u>	<u>MG</u>
<u>Brazil</u>	<u>JC</u>
<u>Brunei</u>	<u>QY</u>
<u>Bulgaria</u>	<u>CD</u>
<u>Burkina Faso</u>	<u>LL</u>
<u>Burundi</u>	<u>MW</u>
<u>Cambodia</u>	<u>QU</u>
<u>Cameroon</u>	<u>MV</u>
<u>Canada</u>	<u>FA</u>
<u>Cape Verde</u>	<u>LM</u>
<u>Central African Republic</u>	<u>MY</u>
<u>Chad</u>	<u>NA</u>
<u>Channel Islands</u>	<u>BA</u>
<u>Chile</u>	<u>JB</u>
<u>China (Taiwan)</u>	<u>QQ</u>
<u>China, Peoples Rep.Of</u>	<u>QJ</u>
<u>Colombia</u>	<u>JD</u>
<u>Comoros</u>	<u>MX</u>

<u>Congo, Democratic Republic of</u>	<u>MM</u>
<u>Congo (Republic of)</u>	<u>MU</u>
<u>Costa Rica</u>	<u>HF</u>
<u>Croatia</u>	<u>CJ</u>
<u>Cuba</u>	<u>GJ</u>
<u>Curacao</u>	<u>GL</u>
<u>Cyprus</u>	<u>DA</u>
<u>Czech Republic</u>	<u>CP</u>
<u>Denmark</u>	<u>BE</u>
<u>Djibouti</u>	<u>NB</u>
<u>Dominica</u>	<u>GR</u>
<u>Dominican Republic</u>	<u>GF</u>
<u>Ecuador</u>	<u>JF</u>
<u>Egypt</u>	<u>KE</u>
<u>El Salvador</u>	<u>HB</u>
<u>England</u>	<u>AC</u>
<u>Equatorial Guinea</u>	<u>NC</u>
<u>Eritrea</u>	<u>NK</u>
<u>Estonia</u>	<u>RE</u>
<u>Ethiopia</u>	<u>MP</u>
<u>European Currencies, Weighted Average Of</u>	<u>CZ</u>
<u>European Currency Unit</u>	<u>CY</u>
<u>Fiji</u>	<u>EC</u>
<u>Finland</u>	<u>BR</u>
<u>France</u>	<u>BF</u>
<u>French Guiana</u>	<u>JK</u>
<u>Gabon</u>	<u>ND</u>
<u>Gambia, The</u>	<u>LA</u>
<u>Georgia</u>	<u>RF</u>
<u>Germany</u>	<u>BK</u>
<u>Ghana</u>	<u>LB</u>
<u>Gibraltar</u>	<u>DB</u>
<u>Grand Cayman Islands</u>	<u>GW</u>
<u>Greece</u>	<u>BN</u>
<u>Grenada</u>	<u>GQ</u>
<u>Guam</u>	<u>RW</u>
<u>Guatemala</u>	<u>HD</u>
<u>Guinea</u>	<u>LN</u>
<u>Guinea-Bissau</u>	<u>LP</u>
<u>Guyana</u>	<u>JH</u>
<u>Haiti</u>	<u>GK</u>
<u>Home Foreign-United Kingdom</u>	<u>AB</u>
<u>Honduras</u>	<u>HC</u>
<u>Hong Kong</u>	<u>QE</u>
<u>Hungary</u>	<u>CC</u>
<u>Iceland</u>	<u>BU</u>
<u>India</u>	<u>QB</u>
<u>Indonesia</u>	<u>QM</u>
<u>Iran</u>	<u>PB</u>
<u>Iraq</u>	<u>PJ</u>

<u>Irish Republic</u>	<u>BC</u>
<u>Isle Of Man</u>	<u>BB</u>
<u>Israel</u>	<u>PC</u>
<u>Italy</u>	<u>BG</u>
<u>Ivory Coast</u>	<u>LH</u>
<u>Jamaica</u>	<u>GB</u>
<u>Japan</u>	<u>QK</u>
<u>Jordan</u>	<u>PL</u>
<u>Kazakhstan</u>	<u>RG</u>
<u>Kenya</u>	<u>MA</u>
<u>Kiribati</u>	<u>ED</u>
<u>Kirjhzia (alternate name for Kyrgystan)</u>	<u>RV</u>
<u>Korea, South</u>	<u>QR</u>
<u>Korea, North</u>	<u>QP</u>
<u>Kuwait</u>	<u>PD</u>
<u>Kyrgyzstan</u>	<u>RV</u>
<u>Laos</u>	<u>RT</u>
<u>Latvia</u>	<u>RJ</u>
<u>Lebanon</u>	<u>PE</u>
<u>Lesotho</u>	<u>MH</u>
<u>Liberia</u>	<u>LG</u>
<u>Libya</u>	<u>KD</u>
<u>Liechtenstein</u>	<u>CK</u>
<u>Lithuania</u>	<u>RK</u>
<u>Luxembourg</u>	<u>BH</u>
<u>Macedonia</u>	<u>BZ</u>
<u>Madagascar</u>	<u>MS</u>
<u>Malawi</u>	<u>MD</u>
<u>Malaysia</u>	<u>QF</u>
<u>Maldives</u>	<u>RU</u>
<u>Mali</u>	<u>LE</u>
<u>Malta</u>	<u>DC</u>
<u>Marshall Islands</u>	<u>EM</u>
<u>Mauritania</u>	<u>LS</u>
<u>Mauritius</u>	<u>ML</u>
<u>Mexico</u>	<u>HA</u>
<u>Micronesia</u>	<u>EN</u>
<u>Moldova</u>	<u>RL</u>
<u>Monaco</u>	<u>CF</u>
<u>Mongolia</u>	<u>RM</u>
<u>Monserrat</u>	<u>GS</u>
<u>Morocco</u>	<u>KB</u>
<u>Mozambique</u>	<u>MR</u>
<u>Myanmar</u>	<u>QH</u>
<u>Namibia</u>	<u>NE</u>
<u>Nauru</u>	<u>EE</u>
<u>Nepal</u>	<u>QT</u>
<u>Netherlands</u>	<u>BJ</u>
<u>Netherlands Antilles</u>	<u>GX</u>
<u>New Zealand</u>	<u>EB</u>



<u>Nicaragua</u>	<u>HE</u>
<u>Niger</u>	<u>NF</u>
<u>Nigeria</u>	<u>LC</u>
<u>Northern Ireland</u>	<u>AF</u>
<u>Norway</u>	<u>BS</u>
<u>Oman</u>	<u>PP</u>
<u>Pakistan</u>	<u>QC</u>
<u>Palau</u>	<u>EP</u>
<u>Panama</u>	<u>HG</u>
<u>Papua New Guinea</u>	<u>EF</u>
<u>Paraguay</u>	<u>JM</u>
<u>Peru</u>	<u>JG</u>
<u>Philippines</u>	<u>QL</u>
<u>Poland</u>	<u>BV</u>
<u>Portugal</u>	<u>BP</u>
<u>Puerto Rico</u>	<u>GG</u>
<u>Qatar</u>	<u>PG</u>
<u>Romania</u>	<u>BW</u>
<u>Russia</u>	<u>RN</u>
<u>Rwanda</u>	<u>NG</u>
<u>San Marino</u>	<u>CL</u>
<u>Sao Tome And Principle</u>	<u>LQ</u>
<u>Saudi Arabia</u>	<u>PF</u>
<u>Scotland</u>	<u>AE</u>
<u>Senegal</u>	<u>LJ</u>
<u>Seychelles</u>	<u>NH</u>
<u>Sierra Leone</u>	<u>LD</u>
<u>Singapore</u>	<u>QG</u>
<u>Slovakia</u>	<u>CQ</u>
<u>Slovenia</u>	<u>CM</u>
<u>Solomon Islands</u>	<u>EG</u>
<u>Somalia</u>	<u>MQ</u>
<u>South Africa</u>	<u>MK</u>
<u>Spain</u>	<u>BQ</u>
<u>Sri Lanka</u>	<u>QZ</u>
<u>St Helena And Dependencies</u>	<u>NJ</u>
<u>St Kitts-Nevis</u>	<u>GT</u>
<u>St Lucia</u>	<u>GV</u>
<u>St Martin</u>	<u>GN</u>
<u>St Vincent and The Grenadines</u>	<u>GU</u>
<u>Sudan</u>	<u>MN</u>
<u>Surinam</u>	<u>JJ</u>
<u>Swaziland</u>	<u>MJ</u>
<u>Sweden</u>	<u>BT</u>
<u>Switzerland</u>	<u>BM</u>
<u>Syria</u>	<u>PK</u>
<u>Tahiti</u>	<u>QV</u>
<u>Tajikistan</u>	<u>RP</u>
<u>Tanzania</u>	<u>MC</u>
<u>Thailand</u>	<u>QN</u>

<u>Togo</u>	<u>LR</u>
<u>Tonga</u>	<u>EH</u>
<u>Trinidad And Tobago</u>	<u>GC</u>
<u>Tunisia</u>	<u>KC</u>
<u>Turkey</u>	<u>PA</u>
<u>Turkmenistan</u>	<u>RQ</u>
<u>Turks &amp; Caicos Islands</u>	<u>GZ</u>
<u>Tuvalu</u>	<u>EJ</u>
<u>Uganda</u>	<u>MB</u>
<u>Ukraine</u>	<u>RR</u>
<u>United Arab Emirates</u>	<u>PH</u>
<u>United Kingdom</u>	<u>AA</u>
<u>Uruguay</u>	<u>JN</u>
<u>USA</u>	<u>FB</u>
<u>Uzbekistan</u>	<u>RS</u>
<u>Vanuatu</u>	<u>EK</u>
<u>Vatican City</u>	<u>CN</u>
<u>Venezuela</u>	<u>JE</u>
<u>Vietnam</u>	<u>QW</u>
<u>Virgin Islands</u>	<u>GH</u>
<u>Wales</u>	<u>AD</u>
<u>Western Samoa</u>	<u>EL</u>
<u>Yemen, South</u>	<u>PM</u>
<u>Yugoslavia</u>	<u>BY</u>
<u>Zambia</u>	<u>ME</u>
<u>Zimbabwe</u>	<u>MF</u>

...

Forms 20, 21, 25, 26, 28, 30, 37, 38 and 39 of Appendix 9.2 (General Insurance Business: revenue account and additional information) are amended as follows:

**Instructions for completion of Form 20**

- Particulars of any amounts included at lines 16, 25 or 32 ('other technical income or charges') are required to be stated by way of a supplementary note (code 2005) to the form.

...

**Instructions for completion of Form 21**

- Lines 13 to 15 of **Form 21** should include *premiums* actually received prior to the *financial year*, but relating to risks incepted in the *financial year* and exclude *premiums* received during the *financial year*, but relating to risks incepting after the end of the *financial year*. In **Forms 13** and **15** the accounting treatment adopted for *premiums* received in respect of risks incepting in future *financial years* should be the same as that adopted in the shareholder accounts, or, if there are no shareholder accounts, should be in accordance with generally accepted accounting practice. If this results in different amounts for the provision of unearned premium (either gross or the *reinsurers'* share) being shown in **Forms 13** or **15** as compared to **Form 21**, it would be appropriate to identify, and provide an explanation, of the difference in a supplementary note (code 2103) to the form.

...

#### Instructions for completion of Form 25

...

8. Particulars of any amounts included at line 25 on must be stated in a supplementary note (code 2505) to the form.

...

#### Instructions for completion of Form 26

...

11. Where the allocation or apportionment to business categories of any *reinsurance* treaties accepted which have previously been reported differs from that adopted previously, rule 9.17(3)(a) requires an explanation of the nature of the change and the reasons for it in a supplementary note (code 2603) to this form.
12. Where the allocation or apportionment to business categories of any *reinsurance* treaties accepted differs from that adopted previously for *reinsurance* treaties relating to similar risks, rule 9.17(3)(a) requires an explanation of the nature of the change and the reasons for it in a supplementary note (code 2604) to this form.

...

#### Instructions for completion of Form 28

...

8. Where the allocation or apportionment to business categories of any *reinsurance* treaties accepted which have previously been reported differs from that adopted previously, rule 9.17(3)(a) requires an explanation of the nature of the change and the reasons for it in a supplementary note (code 2803) to this form.
9. Where the allocation or apportionment to business categories of any *reinsurance* treaties accepted differs from that adopted previously for *reinsurance* treaties relating to similar risks, rule 9.17(3)(a) requires an explanation of the nature of the change and the reasons for it in a supplementary note (code 2804) to this form.

...

**Instructions for completion of Form 30**

...

5. The methods and assumptions used in determining the yield in accordance with instruction 4 must be stated by way of a supplementary note (code 3001) to this Form.

...

7. The treatment of expected income payments from any asset where such payment is in default must be stated by way of a supplementary note (code 3002) to this Form.

...

**Equalisation provisions**

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

Company registration number	GL/UK/CM	Period ended			Units
		day	month	year	
<b>R37</b>					<b>£000</b>

	Business group grouping A (property)	Business group grouping B (business interruption)	Business group grouping C (marine and aviation)	Business group grouping D (nuclear)	Business group grouping E (non-proportional treaty)	All business groups	Credit insurance business
	1	2	3	4	5	6	7
<b>Calculation of the maximum provision</b>							
Total net premiums written in the previous 4 years	11						
Net premiums written in the current year	12						
Maximum provision	13						

**Calculation of the transfer to/from the provision**

Equalisation provision brought forward	21						
Transfers in	22						
Total abnormal loss	23						
Provisional transfers out	24						
Excess of provisional transfer out over fund available	25						
Provisional amount carried forward (21+22-24+25)	26						
Excess, if any, of 26 over 13	27						
Equalisation provision carried forward (26-27)	28						
Transfer in/(out) for financial year (28-21)	29						

### Instructions for completion of Form 37

1. Lines 11 & 12, columns 1 to 5, must include net written premium from ~~the~~ Form 21 (accident year *insurance business*) and/or Form 24 (underwriting year *insurance business*) that in whole or in part covers each ~~business group~~ insurance business grouping.
2. Only premium for *financial years* covered by the scheme may be included in lines 11 & 12, columns 1 to 5 (see ~~Appendix 6.1, Part 11~~ see PRU 7.5.20R). Adjustments in respect of prior years must be included at line 12.
3. Any *insurance business* that has been transferred must be excluded from lines 11 & 12, columns 1 to 5 (see ~~rules 6.8 and 6.9~~ see PRU 7.5.32R to PRU 7.5.37G).
4. Line 13, columns 1 to 5 must show the maximum provision for each ~~business group~~ insurance business grouping calculated in accordance with ~~Appendix 6.1~~ PRU 7.5.24R. If *insurance business* in a group has been written for less than 5 years, the average of the qualifying years must be used.
5. If all rights and obligations in an ~~business group~~ insurance business grouping have been transferred, line 13 columns 1 to 5 must be left blank at the appropriate column.
6. Line 22, columns 1 to 5 must be calculated by multiplying the figure at line 12 for each ~~business group~~ insurance business grouping by the % in ~~paragraph 3 of Part 1 of Appendix 6.1~~ PRU 7.5.27R.
7. Line 23 must be, for each ~~business group~~ insurance business grouping, the total of abnormal losses, if any, brought forward from Forms 38 and 39, line 19. These must be entered in the same columns as they were on Forms 38 and 39.
8. The transfer out for each ~~business group~~ insurance business grouping at line 24, columns 1 to 5 must not exceed the line 13 maximum provision for that group.
9. The sum of columns 1 to 5 of lines 13, 22 and 24 must be entered in column 6 of the relevant line.
10. In the first year of the scheme, line 21 column 6 must be left blank. In subsequent years this figure must be brought forward from the previous year's figure (normally the figure at Form 15, line 15). Only equalisation provisions required by ~~the rules in the Equalisation Reserves Rules~~ PRU 7.5.11R to PRU 7.5.37G may be included.
11. The calculations for lines 25 to 29, column 6 must be carried out and the net transfer in or out for the year must be entered at Form 16, line 12, and the provision carried forward entered at Form 15, line 15.
12. Line 13, column 7 must be 150% of the highest annual amount of net premiums written in the last 5 years.
13. Line 21, column 7 must equal the statutory credit equalisation provision, if any, brought forward from the previous year at Form 15, line 14.
14. Line 22, column 7 must be 75% of the technical surplus, if any, brought forward from Forms 38 and/or 39, line 29, subject to a limit of 12% of line 12.
15. Line 24, column 7 must equal the technical deficit, if any, brought forward from Forms 38 and/or 39, line 29.
16. The calculations for lines 25 to 29, column 7 must be carried out and the net transfer in or out for the year must be entered at Form 16, line 12, and the provision carried forward entered at Form 15, line 14.

**Equalisation provisions technical account : Accident year accounting**

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

	Company registration number	GL/UK/CM	Period ended			Units
			day	month	year	
	<b>R38</b>					<b>£000</b>
<b>Other than credit business</b>	Business group grouping A (property)	Business group grouping B (business interruption)	Business group grouping C (marine and aviation)	Business group grouping D (nuclear)	Business group grouping E (non-proportional treaty)	
	1	2	3	4	5	
Net premiums earned	11					
Claims incurred net of reinsurance	12					
Trigger claims value	13					
Abnormal loss	19					
Trigger claims ratio	72.5%	72.5%	95%	25%	100%	

**Credit business**

Net premiums earned	21	
Claims incurred net of reinsurance	22	
Claims management costs	23	
Net operating expenditure	24	
Technical surplus/(deficit) (21-22-23-24)	29	

### Instructions for completion of Form 38

1. Apart from *credit insurance business*, any *insurance business* transferred to an *insurer* by novation or under Part VII of the *Act* (or the *1982 Act*) must be accounted for in accordance with ~~rule 6.9~~ PRU 7.5.34R.
2. The entries at line 11 must be derived from Form 21, that in whole or in part covers the *insurance business ~~group~~ grouping*, at line 11, column 5 and line 19, column 5.
3. The entries at line 12 must be derived from Form 22, that in whole or part covers the *insurance business ~~group~~ grouping*, at line 13 and 17, column 4.
4. The entries at line 13 must be line 11 (or nil if line 11 is negative) multiplied by the trigger *claims* ratio for the *insurance business ~~group~~ grouping*.
5. For each *insurance business ~~group~~ grouping* the entry at line 19 must be the amount, if any, by which the entry at line 12 for that *insurance business ~~group~~ grouping* exceeds the entry at line 13. If the entry at line 12 does not exceed the entry at line 13, line 19 must be left blank.
6. The entry at line 21 must be derived from Form 21 for *accounting class 8*, at line 11, column 5 and line 19, column 5, to include only *insurance business* in *general insurance business class 14*.
7. The entry at line 22 must be derived from Form 22 for *accounting class 8*, at lines 13 and 17, column 4, to include only *insurance business* in *general insurance business class 14*.
8. The entry at line 23 must be derived from Form 22 for *accounting class 8*, at lines 14 and 18, column 4, to include only *insurance business* in *general insurance business class 14*.
9. The entry at line 24 must be derived from Form 22 for *accounting class 8*, at lines 19 and 29, column 4, to include only *insurance business* in *general insurance business class 14*.



**Equalisation provisions technical account : Underwriting year accounting**

Name of insurer

Global business/UK branch business/EEA branch business

Financial year ended

	Company registration number	GL/UK/CM	Period ended			Units
			day	month	year	
	<b>R39</b>					<b>£000</b>
	Business group grouping A (property) 1	Business group grouping B (business interruption) 2	Business group grouping C (marine and aviation) 3	Business group grouping D (nuclear) 4	Business group grouping E (non-proportional treaty) 5	
<b>Other than credit business</b>						
Net premiums written	11					
Claims net of reinsurance	12					
Trigger claims value	13					
Abnormal loss	19					
Trigger claims ratio		72.5%	72.5%	95%	25%	100%

**Credit business**

Net premiums written	21	
Claims net of reinsurance	22	
Claims management costs	23	
Net operating expenditure	24	
Technical surplus/(deficit) (21-22-23-24)	29	

### Instructions for completion of Form 39

1. Apart from *credit insurance business*, any *insurance business* transferred to an *insurer* by novation or under Part VII of the *Act* (or the *1982 Act*) must be accounted for in accordance with ~~rule 6.9~~ PRU 7.5.34R.
2. The entries at line 11 must be derived from Form 24, that in whole or in part covers the ~~*business group insurance business grouping*~~, at line 19, column 99-99.
3. The entries at line 12 must be derived from column 99-99 of Forms 24 and 25, that in whole or part covers the ~~*business group insurance business grouping*~~, as follows:  
  
line 29 on Form 24 plus line 29 less line 15 plus line 24 on Form 25 less line 29 plus line 15 less line 24 on Form 25 for the *preceding financial year*.
4. The entries at line 13 must be line 11 (or nil if line 11 is negative) multiplied by the trigger *claims* ratio for the ~~*business group insurance business grouping*~~.
5. For each ~~*business group insurance business grouping*~~ the entry at line 19 must be the amount, if any, by which the entry at line 12 for that ~~*business group insurance business grouping*~~ exceeds the entry at line 13. If the entry at line 12 does not exceed the entry at line 13, line 19 must be left blank.
6. The entry at line 21 must be derived from Form 24 for *accounting class* 8, at line 19, column 99-99, to include only *insurance business* in *general insurance business class* 14.
7. The entry at line 22 must be derived from Form 24 for *accounting class* 8, at line 29, column 99-99, plus line 53, column 99-99 less line 51, column 99-99, to include only *insurance business* in *general insurance business class* 14.
8. The entry at line 23 must be derived from Form 24 for *accounting class* 8, at line 39, column 99-99, to include only *insurance business* in *general insurance business class* 14.
9. The entry at line 24 must be derived from Form 24 for *accounting class* 8, at line 49 column 99-99, to include only *insurance business* in *general insurance business class* 14.
- ...

Forms 40, 43 and 44 of Appendix 9.3 (Long-term Insurance business: revenue account and additional information) are amended as follows:

#### Instructions for completion of Form 40

...

2. Any item of income which cannot properly be allocated to lines 11, 12, 13 or 14 must be entered in line 15, and similarly, any item of expenditure which cannot properly be allocated to lines 21, 22, 23 or 24 must be entered in line 25. Particulars of such items must be specified in a supplementary note (Code 4002).
3. Where an *insurer* decides to allocate to the *long-term insurance business* the whole or any part of investment income and/or net capital gains arising from assets not attributable to its *long-term insurance business*, the amounts in question must be shown as a transfer in line 26 and particulars must be specified in a supplementary note (Code 4003).
4. Where a transfer is made to the non-technical account, the entry at line 26 must show amounts which have been included in line 47 of Form 58. Transfers from or to other funds must be included in line 15 or 25, with transfers to reserves associated with a transfer of contracts from one fund to another specified in a supplementary note (Code 4004).

...

8. If any of the brought forward amounts differs from the corresponding carried forward amounts in the previous return, the reason must be stated in a supplementary note as specified in paragraph 7 of Appendix 9.1 (Code 4001).
9. If the bases of conversion adopted in respect of foreign currency for income and expenditure have not already been stated in a note to Form 16, the bases should be stated in a supplementary note as specified in paragraph 5(2) of Appendix 9.1 (Code 4005).
10. Where an insurer maintains more than one long-term insurance fund, the principles and methods applied to apportioning the investment income, the increase or decrease in the value of assets brought into account, expenses and taxation between the different funds must be stated in a supplementary note as specified in paragraph 4(1) of Appendix 9.3 (Code 4006).
11. Where arrangements have been in force during the financial year for the provision either by or to the insurer of management services, this fact must be stated in a supplementary note (Code 4008) together with the name of the other party (to whom or from whom such services were provided or received) - see paragraph 5 of Appendix 9.3. This statement is only needed where a substantial part of the day-to-day administration of an insurer is undertaken by another company or vice versa. Note that where the arrangement is between two insurers, the directors will need to consider very carefully the form of their certificate under Appendix 9.6, Part I paragraph 4(e).
12. Details of any material connected-party transactions as required under rule 9.39 must be stated in a supplementary note (Code 4009).

...

#### Instructions for completion of Form 43

1. The basis on which the assets have been valued must be stated in a supplementary note (Code 4301).
2. The aggregate value of rights (gross of *variation margin*) and the aggregate amount of liabilities (gross of *variation margin*) under *derivative contracts* (or in respect of contracts or assets which have the effect of a *derivative contract*) must each be stated in a supplementary note (Code 4302). The corresponding figures net of *variation margin* must also be stated. For this purpose, rights and liabilities must not be set off against one another unless

- (i) such rights and liabilities may be set off against each other in accordance with generally accepted accounting practice, and
  - (ii) such set off results (in whole or in part) from the closing out of obligations under a contract.
3. Where there is a liability to repay *variation margin* and there are no arrangements for netting of amounts outstanding or the arrangements would not permit the accounting of such amounts on a net basis in accordance with generally accepted accounting practice, it must be so stated in a supplementary note (Code 4303).

...

#### **Instructions for completion of Form 44**

...

2. Any item of income which cannot properly be allocated to lines 11, 12, or 13 must be entered in line 14, and similarly, any item of expenditure which cannot properly be allocated to lines 21, 22, 23, 24 or 25 must be entered in line 26. Particulars of such items must be specified in a supplementary note (Code 4402).

...

4. If any of the brought forward amounts differs from the corresponding carried forward amounts in the previous *return* the reason must be stated in a supplementary note as specified in paragraph 7 of **Appendix 9.1** (Code 4401).

...

...

#### APPENDIX 9.4 (rule 9.31)

### ABSTRACT OF VALUATION REPORT ~~PREPARED BY APPOINTED ACTUARY~~ (FORMS 46 to 60)

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...

(c) references to **Form 57** are to either of the versions of that Form set out in this Appendix and an insurer is free to use either version; and

~~(e)~~ (d) boxes marked 'UK/OS' must be completed by the insertion of 'UK' for 'UK contracts' and 'OS' for 'overseas contracts'.

...

3. A statement that the valuation has been made in conformity with PRU 7.3.10R ~~rule 5.6~~ or, where this was not the case, such qualification, amplification or explanation as necessary.

...

6. (1) The general principles and methods adopted in the valuation, including specific reference to the following –

...

(b) the method by which due regard has been given to the duty to treat customers fairly ~~the reasonable expectations of policy holders~~, as required by PRU 7.3.10 R(6) ~~rule 5.6~~, and by which account has been taken of the custom and practice of the insurer in the manner and timing of the distribution of profits or the grant of discretionary additions over the duration of each policy, as required by PRU 7.3.10R(5) ~~rule 5.7(6)~~;

(c) where the net premium method has been used, whether and to what extent it has been modified, for what purposes any such modification has been made and whether any modifications on account of *zillmerising* conform to PRU 7.3.43R ~~rule 5.10~~;

(d) whether any negative reserves arose and the steps taken to ensure that *no contract of insurance* was treated as an asset, as required by PRU 7.3.24R ~~rule 5.15~~;

...

7. ...

- ~~(6) — A description of all the scenarios of future changes in the value of assets which have been tested in order to take account of the nature (including currency) and terms of the assets held in determining the amount of the *long term insurance business liabilities* in accordance with rule 5.17 identifying that scenario which produces the most onerous requirement (whether or not a reserve is required).~~
- ~~(7) — The amount of any reserve made pursuant to rule 5.17(a), together with a brief description of the method used and assumptions made to calculate any such reserve.~~
- ~~(8) — In respect of that scenario described under (6) which produces the most onerous requirement (whether or not a reserve is required), the amount of any reserve made pursuant to rule 5.17(b), together with—~~
- ~~(a) — a description of the changed assumptions made (other than the changed interest rate stated in **Form 57**) in calculating such requirement;~~
- ~~(b) — a brief description of the method used to calculate such requirement; and~~
- ~~(c) — resulting from the application of such changed assumptions—~~
- ~~(i) — the change in the aggregate amount of the *long term insurance business liabilities*, and~~
- ~~(ii) — the aggregate amount by which the assets allocated to match such liabilities in the scenario have changed in value from the amount of those assets shown in **Form 13**.~~
- (6) A statement of the most onerous scenario under PRU 4.2.16R for assets invested in the *United Kingdom* and other assets that fall under PRU 4.2.16R for the purposes of calculating the resilience capital requirement in PRU 4.2.10R.
- (7) A statement of the most onerous scenario under PRU 4.2.23R for each significant territory in which assets are invested outside the *United Kingdom* for the purposes of calculating the resilience capital requirement in PRU 4.2.10R.
- (8) In respect of the scenarios described under (6) and (7) which produce the most onerous requirement (whether or not a resilience capital requirement is required),
- (a) the amount of the *resilience capital requirement* if such a requirement arises,
- (b) the change in the aggregate amount of the *long-term insurance liabilities*, and
- (c) the aggregate amount by which the assets allocated to match such liabilities in the scenario have changed in value from the amount of those assets shown in Form 13.

8. In respect of non-linked contracts –

...

- (d) where, in valuing contracts falling within the circumstances described in PRU 7.3.38R ~~rule 5.9(1)~~, future *premiums* brought into account are not in accordance with that rule, such additional information as is necessary to demonstrate whether the *mathematical reserves* determined in the aggregate for each of the main categories of contract are greater than an amount for each such category calculated in accordance with PRU 7.3.24R to PRU 7.3.91G ~~rules 5.8 to 5.17~~,

...

9. For each category of linked contract –

...

- (b) where an explicit reserve has not been made for meeting the expenses likely to be incurred in future in fulfilling the existing contracts on the basis of specific assumptions in regard to the relevant factors, details of the basis used in testing the adequacy of the reserves to satisfy PRU 7.3.50R ~~rule 5.13(1)~~.

...

12. ...

(4) In this paragraph -

- (a) **financing arrangement** means any contract entered into by the *insurer*, in respect of *contracts of insurance* of the *insurer*, which has the effect of increasing the ~~amount of assets included at long term capital resources in line 13 34 of Form 9 2, representing assets of the insurer which are available to meet its required minimum margin for long term insurance business,~~ and which includes terms for -

...

20. ...

- (3) In the event that the liability for a specific fund link is wholly reinsured so that entries in columns 8 and 9 of **Form 55** are omitted in accordance with paragraph 7 of the instructions for the completion of that form a statement, if such be the case, to the effect that the provisions of PRU 4.2.57R ~~rule 7.2~~ have been complied with in accordance with any published guidance in relation to the liabilities so reinsured.

21. . . .
- (2) A general description of the method by which the yield on assets other than equity *shares* and land was adjusted in accordance with PRU 4.2.41R rule 5.11(7).
- (3) For assets which are equity *shares* or land, a description of the categories into which such assets were divided for the purposes of PRU 4.2.33R rule 5.11(7), together with the method and basis by which the yield on such assets was adjusted in accordance with that rule.

23. (1) A statement of the *long term insurance capital requirement required minimum margin for long term insurance business* in the form set out in **Form 60** and of the *required margin of solvency for Class IV business and supplementary accident and sickness insurance* in the form set out in **Forms 11 and 12**, in accordance with instruction 8 for completion of **Form 60**. When completing Forms 11 and 12, the accounting conventions for *general insurance business* should be followed, but reasonable approximations may be used if they are unlikely to result in an underestimate of the *required margin of solvency*.

The instructions for the completion of Forms 48, 49, 56 and 57 of Appendix 9.4 (Abstract of valuation report) are amended as follows:

**Instructions for completion of Form 48**

4. The expected income must be the amounts before deduction of tax which would be received in the next *financial year* on the assumption that the assets will be held throughout the year and that the factors which affect income will remain unchanged, but account must be taken of any changes in those factors known to have occurred by the *relevant date* (in particular changes of the type (a), (b), (c) or (d) ~~denoted in rule 5.11(5)(1), (2), (3), (4), (5) and (6) in PRU 4.2.33R~~). The expected income shown in this Form must be that determined before any adjustments considered necessary because of ~~rule 5.11(7)PRU 4.2.41R and PRU 4.2.44R~~.

7. The entries at 48.12.3, 48.13.3, 48.14.3 and 48.15.3 must be equal to 49.19.2, 49.29.2, 49.19.5 and 49.29.5 respectively. Subject to paragraphs 10 and 11, the yields to be inserted in column 3 for other categories of asset must be the running yields determined in accordance with ~~rules 5.11(3) to (6A)PRU 4.2.33R to PRU 4.3.34R~~ before any allowance for tax required by PRU 4.2.29R. The entry at 48.29.3 must be the weighted average of the yields in column 3, where the weight given to each asset is the value of that asset applicable for entry into column 1. Assets not producing income must be included in the calculation.

8. Where the yield in column 3 for a type of asset shown in line 17, 18 or 19 above (assumed to be zero for assets in line 19) is significantly different from the weighted average of the yields for each asset of that type determined in accordance with ~~rule 5.11(6)PRU 4.2.34R(2)~~ before any allowance for tax required by PRU 4.2.29R, then the latter yield figure must be shown in a supplementary note. For this purpose, the weighted average of the yields means an average yield weighted by the value of each



asset of that type as entered in column 1.

....

10. To the extent that ~~rule 5.11(5A)~~ PRU 4.2.34R (2) has not been, or would otherwise not be required to be, applied to calculate the yield on ~~equity shares or~~ holdings in *collective investment schemes*, that rule may be ignored (in which case ~~rule 5.11(5)~~ PRU 4.2.33R and PRU 4.2.34R(1) will apply, before any allowance for tax required by PRU 4.2.29R) for an amount up to the higher of £5 million or 5% of the value of equity *shares* and holdings in *collective investment schemes* required to be reported in Form 48.
11. To the extent that a yield greater than zero on equity *shares* or holdings in *collective investment schemes* is not needed for the purpose of determining rates of interest under ~~rule 5.11~~PRU 4.2.28R, rules 5.11(5) and (5A) PRU 4.2.33R and PRU 4.2.34R may be ignored for an amount of up to 1% of the value of equity *shares* and holdings in *collective investment schemes* required to be reported in Form 48, and the relevant yield will be taken as zero.

...

#### Instructions for completion of Form 49

...

2. The gross redemption yield in columns 2 and 5 for each asset must be calculated as in ~~rule 5.11(3), (4) and (6)~~ PRU 4.2.34R(2) before any allowance for tax required by PRU 4.2.29R, leaving out of account any adjustment considered necessary because of ~~rule 5.11(7)~~ PRU 4.2.41R and PRU 4.2.46R. Where a number of assets with different gross redemption yields are held, the weighted average gross redemption yield must be calculated using as weights the value of the asset applicable for entry into columns 1 and 4 respectively.

...

#### Instructions for completion of Form 56

...

7. Any provision for ~~adverse changes~~ "reasonably foreseeable adverse variations" must be determined in accordance with ~~rule 5.3~~ PRU 4.3.17R(3) and shown in a supplementary note.

...

#### Instructions for completion of Form 57

...

5. Separate Forms must be prepared for each separate asset mix determined by the notional allocation of assets to contracts ~~rate of interest used in the valuation in pursuance of rule 5.11(12)~~ and may include all contracts valued at the same rate, subject to 2 and 3. Contracts valued at a lower rate of interest but subject to the same apportionment of assets may also be included as long as the rationale for such inclusion is given in a supplementary note. Each of the valuation rates of interest used must be itemised against the heading "Valuation rate(s) of interest". The highest valuation rate of interest used must be shown in line 31 or 32 as appropriate and in the code box headed "Valuation rate of interest".

...

8. The risk adjusted yield in columns 2 and 6 for each asset included in column 1 and 5 respectively must be that calculated as in ~~rules 5.11(3) to (6)~~ PRU 4.2.34R before any allowance for tax required by PRU 4.2.29R, taking account of any adjustment considered necessary because of ~~rule 5.11(7)~~PRU 4.2.41R

and PRU 4.2.46R. Where a number of assets with different risk adjusted yields are held, the weighted average risk adjusted yield must be calculated using as weights the value of the asset applicable for entry into columns 2 and 6.

...

Alternative version of Form 57 of Appendix 9.4 (Abstract of valuation report) is inserted as follows:

**Long-term insurance business – analysis of valuation interest rate**

Name of insurer  
 Financial year ended  
 Category of surplus

Company registration number	GL/UK/CM	day	month	year	units	Category of surplus	
R57					£000		
Product group				Net mathematical reserves	Net valuation interest rate	Gross valuation interest rate	Risk adjusted yield on matching assets
1				2	3	4	5
<b>Total</b>					n/a	n/a	n/a

### Instructions for completion of Form 57

1. This Form must be completed for each separate fund or part of a fund for which a surplus is determined where *mathematical reserves* for non-linked business exceed £100m. The name of the fund or part of a fund is to be shown against the heading "Category of surplus". The corresponding code box must contain the code numbers consistent with Forms 51-54.
2. Separate lines are required for UK and overseas liabilities, for life assurance and annuity business, pension business, permanent health business and other business and for with-profits and non-profit business.
3. Separate lines are required for each separate asset mix determined by the notional allocation of assets to contracts.
4. Separate lines are required for each valuation interest rate.
5. The product group in column 1 must be a narrative description of the products included in the line sufficient to give an easy cross reference to Forms 51-54, e.g. 'UK L&GA WP Form 51 assurances'.
6. The *mathematical reserves* in column 2 must include any increase in reserves resulting from the bonus declaration for the year and must be net of *reinsurance ceded*.
7. Up to 10% of the total relevant liabilities for the fund may be shown in a line labelled 'Misc' in column 1. In this case columns 3 and 4 must be 'n/a'. The relevant liabilities are the total *mathematical reserves* including cost of bonus plus any deposit back, less property linked unit liabilities and index linked investment liabilities.
8. The risk adjusted yield in column 5 must allow for the adjustments from PRU 4.2.41R.

...

Form 60 of Appendix 9.4 (Abstract of valuation report) is replaced as follows:

## Long term insurance capital requirement

Name of insurer

Global business / UK branch / EEA branch

Financial year ended

	Company registration number	GL/UK/CM	day	month	year	units
	R60					£000
	LTICR factor	Gross reserves / capital at risk	Net reserves / capital at risk	Reinsurance factor	LTICR Financial year	LTICR Previous year
	1	2	3	4	5	6
<b>Insurance death risk capital component</b>						
Classes I, II and IX	11	0.1%				
Classes I, II and IX	12	0.15%				
Classes I, II and IX	13	0.3%				
Classes III, VII and VIII	14	0.3%				
<b>Total</b>	15					
<b>Insurance health risk capital component</b>						
Class IV and supplementary classes 1 and 2	21					
<b>Insurance expense risk capital component</b>						
Classes I, II and IX	31	1%				
Classes III, VII and VIII (investment risk)	32	1%				
Classes III, VII and VIII (expenses fixed 5 yrs +)	33	1%				
Classes III, VII and VIII (other)	34	25%				
Class IV	35	1%				
Class V	36	1%				
Class VI	37	1%				
<b>Total</b>	38					
<b>Insurance market risk capital component</b>						
Classes I, II and IX	41	3%				
Classes III, VII and VIII (investment risk)	42	3%				
Classes III, VII and VIII (expenses fixed 5 yrs +)	43	0%				
Classes III, VII and VIII (other)	44	0%				
Class IV	45	3%				
Class V	46	0%				
Class VI	47	3%				
<b>Total</b>	48					
<b>Long term insurance capital requirement</b>	51					

## Instructions for completion of Form 60

1. The *insurance death risk capital component* in lines 11-14 column 5 is based on capital at risk for those contracts where it is not negative. Capital at risk is the benefit payable as a result of death less the *mathematical reserves* after distribution of surplus. Business in classes I, II and IX must be split between lines 11, 12 and 13 in accordance with *PRU 7.2.82R*. Line 11 is for temporary insurance on death where the original term of the contract is 3 years or less or for a *pure reinsurer*. Line 12 is for temporary insurance where the original term is 5 years or less but more than 3 years. Line 13 is for other *class I, II or IX* business. For a *pure reinsurer* the factor of 0.3% in column 1 of line 14 should be replaced by 0.1%.
2. In lines 11-14 columns 2 and 3 are the gross and net capital at risk in accordance with *PRU 7.2.83R*. For lines 11-13 the reinsurance factor is calculated in aggregate, so column 4 is the sum of lines 11-13 column 3 divided by the sum of lines 11-13 column 2, subject to a minimum of 0.5 in accordance with *PRU 7.2.81R*. For line 14 column 4 is column 3 divided by column 2, subject to a minimum of 0.5 in accordance with *PRU 7.2.81R*. Column 5 is column 1 x column 2 x column 4.
3. The *insurance health risk capital component* in line 21 column 5 must be equal to the entry at line 43 in Form 12 for *long-term insurance business*.
4. For the purpose of calculating the *insurance expense risk capital component* and the *insurance market risk capital component* linked contracts should be allocated to:
  - lines 32 and 42 where the *firm* bears an investment risk,
  - lines 33 and 43 where the *firm* does not bear an investment risk but where the allocation to cover *management expenses* is fixed for a period exceeding 5 years from the commencement of the contract, and
  - lines 34 and 44, otherwise.
5. The *insurance expense risk capital component* for linked contracts where the *firm* bears no investment risk and the allocation to cover *management expenses* does not have a fixed upper limit for a period exceeding 5 years from the commencement of the contract in line 34 is 25% of net *administrative expenses* in accordance with *PRU 7.2.88R(1)*.
6. The *insurance expense risk capital component* for *class V* in line 36 column 5 is 1% of the assets of the tontine in accordance with *PRU 7.2.88R(2)*.
7. The *insurance expense risk capital component* for other business in lines 31, 32, 33, 35 and 37 column 5 is 1% of adjusted *mathematical reserves* after distribution of surplus in accordance with *PRU 7.2.88R(3)*. Column 4 is column 3 divided by column 2, subject to a minimum of 85% (50% for a pure reinsurer) in accordance with *PRU 7.2.90R*. Column 5 is column 1 x column 2 x column 4.
8. The *insurance market risk capital component* in lines 43 and 44 column 5 for class III, VII and VIII contracts where the *firm* does not bear any investment risk and in line 45 for class V contracts is nil in accordance with *PRU 7.2.89R*.
9. The *insurance market risk capital component* in line 41, 42, 45 and 47 column 5 is 3% of adjusted *mathematical reserves* after distribution of surplus in accordance with *PRU 7.2.89R*. Column 4 is column 3 divided by column 2 subject to a minimum of 85% (50% for a pure reinsurer) in accordance with *PRU 7.2.90R*. Column 5 is column 1 x column 2 x column 4.
10. The *long term insurance capital requirement* in line 51 column 5 is the sum of column 5 in lines 15, 21, 38 and 48.
11. For *financial years* starting before 1 January 2005 lines 11 to 48 of column 6 must be blank.

Appendix 9.4A is inserted as follows:

#### **APPENDIX 9.4A** (rule 9.31(b))

### **ABSTRACT OF VALUATION REPORT FOR REALISTIC VALUATION**

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The following information must be provided in the abstract of the report required under rule 9.31(b), the answers being numbered to accord with the numbers of the corresponding paragraphs of this Appendix. For the purposes of this Appendix, the “report period” means the period from the date to which the previous calculation of the *with-profits insurance capital component* under rule 9.4(2)(c) related to the ‘valuation date’ (as defined in 1).

#### **Introduction**

1. (1) The date to which the actuarial investigation relates, namely, the **valuation date**.
- (2) The date of the previous valuation.
- (3) The dates of any interim valuations carried out since the previous ‘valuation date’.

#### **Assets**

2. (1) For each *with-profits fund* in which any *non-profit insurance contracts* are written, a table of the economic assumptions used to determine the value of future profits (or losses) on those contracts, showing the economic assumptions used at the end of the *financial year in question*, and used at the end of the *preceding financial year*.
- (2) For each *with-profits fund* in respect of which the *realistic value of the assets* includes an amount determined under *PRU 7.4.33R(2)*, a table of the economic assumptions used to determine any additional amount by reference to the value of future profits (or losses) on *non-profit insurance contracts* according to *PRU 7.4.33R(3)(b)(iii)*.
- (3) For each *with-profits fund* in respect of which an asset not exceeding 50 % of the present value of future profits arising from insurance contracts written outside the *with-profits funds* is included in the relevant assets for the purpose of *PRU 7.4.43R* in accordance with *PRU 7.4.45R(2)(c)* and *PRU 7.4.45R(5)*, a table of the economic assumptions used to determine that present value.
- (4) Where the valuation of the future profits (or losses) on *non-profit insurance contracts* in (1) or of any additional amount in (2) or of any present value in

- (3) involves more than one set of economic assumptions, (for example, different sets of economic assumptions are used for different *with-profits funds*), each different set of economic assumptions must be shown.
- (5) The separate disclosure of economic assumptions used to determine the valuation of future profits (or losses) on *non-profit insurance contracts* in (1) or of any additional amount in (2) or of any present value in (3) is not required to the extent the total of the values derived by reference to assumptions which are not disclosed is less than £20 million.

### **With-Profits Benefits Reserve Liabilities**

3. (1) For each *with-profits fund*, a table of the retrospective methods (see *PRU 7.4.119R*) and/or prospective methods (see *PRU 7.4.128R*) used to calculate the *with-profits benefits reserve* for that fund, showing:
- (a) the types of product or classes of *with-profits insurance contracts* to which each of the retrospective methods and/or prospective methods applies;
  - (b) for each type of product or class of *with-profits insurance contracts* and method, the corresponding amounts of the *with-profits benefits reserve* and the *future policy related liabilities*; and
  - (c) the aggregate amount of the *with-profits benefits reserve* and the *future policy related liabilities* for those types of product or classes of *with-profits insurance contracts* which are not required to be disclosed separately (in accordance with 3(3)).
- (2) If the total of the amounts of the *with-profits benefits reserve* and *future policy related liabilities* shown in the table under (1) do not correspond to the respective amounts shown at lines 31 and 49 of the appropriate **Form 19**, an explanation and reconciliation must be provided.
- (3) The separate disclosure of the retrospective methods and prospective methods used to calculate the *with-profits benefits reserve* of a *with-profits fund* is not required for types of products and/or classes of *with-profits insurance contracts* to the extent the aggregate amount of the *realistic value of liabilities* for all types of products and/or classes of *with-profits insurance contracts* in respect of which the valuation methods are not disclosed is less than the higher of 5% of the *realistic value of liabilities* for that fund and £20 million.
- (4) References in paragraph 3 of this Appendix to types of product and/or classes should be taken as meaning the constituent elements of a division of the portfolio of *with-profits insurance contracts* by grouping those contracts having regard to materially different guarantees and options such as pension contracts with minimum bonuses and annuity rate options, pension



contracts with minimum bonuses, pension contracts with no minimum bonuses, life bonds issued with no Market Value Reduction / Market Value Adjustment type clauses (MVR/MVAs), life bonds with spot MVR/MVA free dates (dates on which the MVR/MVAs do not apply), life bonds with no MVR/MVA free dates, etc.. The extent of disclosure should be sufficient to permit an identification of material groupings of contracts which offer significant variance in terms of the nature of benefits provided to *policyholders*.

#### **With-profits benefits reserve – Retrospective method**

4. (1) For each *with-profits fund*, a table of the retrospective methods used to calculate the *with-profits benefits reserve* showing for each retrospective method:
  - (a) the proportion of the *with-profits benefit reserve* calculated using that retrospective method for which contracts have been valued on an individual basis;
  - (b) the proportion of the *with-profits benefit reserve* calculated using that retrospective method for which contracts have been valued on a grouped basis; and
  - (c) in relation to any *with-profits insurance contracts* that have been grouped:
    - (i) a statement of the basis used to group contracts;
    - (ii) the number of individual contracts and the number of model points used to represent them; and
    - (iii) the nature of the validations made to ensure that significant attributes of the contract groupings have not been lost.
- (2) For each *with-profits fund*:
  - (a) a description of any significant changes to the valuation method for any types of product or classes of *with-profits insurance contracts* written in that fund compared to the previous valuation; and
  - (b) where the changes in (a) have resulted in any types of product or classes of *with-profits insurance contracts* written in that fund being valued using approaches more approximate than used for the previous valuation, a statement of the types of product or classes of *with-profits insurance contracts* affected.
- (3) For each *with-profits fund*, a description of the basis of allocating expenses to that fund during the *financial year in question* identifying:

- (a) the date of the previous expense investigation;
  - (b) the frequency of expense investigations;
  - (c) a table of the total expenses allocated to the *with-profits benefits reserve* during the *financial year in question* showing:
    - (i) the nature and amount of expenses identified as initial expenses;
    - (ii) the nature and amount of expenses identified as maintenance expenses;
    - (iii) how expenses are charged to the *with-profits benefits reserve* in respect of individual contracts (for example, by way of an average expense charge deducted from all contracts); and
    - (iv) the nature and amount of any expenses charged other than to the *with-profits benefits reserve*.
- (4) For each *with-profits fund*, a description of the nature and amount of any significant charges (for example for the costs of guarantees or the use of capital) deducted from the *with-profits benefits reserve* during the *financial year in question* and a comparison to the charges in the *preceding financial year*.
- (5) For each *with-profits fund*, a description of the nature and amount of any charges deducted from that fund for non-insurance risk (for example, charges deducted from investment only accumulating with-profit business).
- (6) For each *with-profits fund*, a statement of the average (expressed as a percentage) of the ratio of A to B for each of the three *preceding financial years* where:
- A is the total *claims* paid during the financial year on *with-profits insurance contracts* written in that fund; and
  - B is the sum of:
    - (i) *with-profits benefits reserve* for those *claims*; plus
    - (ii) any past miscellaneous surplus attributed to the *with-profits benefits reserve* in respect of those *claims*; less

- (iii) any past miscellaneous deficit attributed to the *with-profits benefits reserve* in respect of those *claims*;

Where there has been a change in procedures such that the ratio of A to B would not be directly comparable with that ratio disclosed at the end of the *preceding financial year*, details should be disclosed as to the change in procedures.

- (7) For each *with-profits fund*, the investment return before tax and expenses allocated to the *with-profits benefits reserve* in respect of the *financial year in question*. If the investment return allocated to the *with-profits benefits reserve* in respect of any types of product or classes of *with-profits insurance contracts* differs materially from that allocated to the *with-profits benefits reserve* in respect of other types of product or classes of *with-profits insurance contracts*, other than because of tax, an explanation and reconciliation must be provided.

#### **With-profits benefits reserve – Prospective method**

- 5. (1) For each *with-profits fund*, a table of the key assumptions used in the prospective method(s) of calculating the *with-profits benefits reserve* showing:
  - (a) the discount rate, together with an explanation of any difference between this rate and the risk free rates denoted "r" in the table required by 6(4)(a)(iii) below;
  - (b) the investment returns and risk adjustments made to assets (categorised as in **Form 48**);
  - (c) expense inflation;
  - (d) future assumed *annual* and *final bonus* rates for major types of products and/or classes of *with-profits insurance contracts*;
  - (e) assumptions as to future expenses and future charges for expenses for major types of products and/or classes of *with-profits insurance contracts*; and
  - (f) any significant persistency assumptions at quinquennial durations.
- (2) Where any of the prospective methods in (1) involves more than one set of key assumptions, each different set of key assumptions must be shown.

## Costs of guarantees, options and smoothing

6. (1) For each *with-profits fund*, where the costs of guarantees, options and smoothing do not exceed the lesser of £50m and 0.5% of the total *realistic value of liabilities*, disclosure of the valuation methods in accordance with the following sub-paragraphs is not required.
- (2) For each *with-profits fund*, a table of the valuation methods used to calculate the costs of guarantees, options and smoothing showing:
- (a) the types of product and/or classes of *with-profits insurance contracts* to which each valuation method applies;
  - (b) for each valuation method and each type of product and/or class of *with-profits insurance contract*:
    - (i) the proportion, measured by reference to the underlying asset shares, of the *with-profits insurance contracts* being valued for which costs have been valued on an individual basis;
    - (ii) the proportion, measured by reference to the underlying asset shares, of the *with-profits insurance contracts* being valued for which costs have been valued on a grouped basis; and
    - (iii) in relation to any *with-profits insurance contracts* that have been grouped,
      - a statement of the basis used to group contracts;
      - the number of individual contracts and the number of model points used to represent them; and
      - the nature of the validations made to ensure that significant attributes of the contract groupings have not been lost;
  - (c) if applicable to the disclosures in (a) and (b), a description of any significant approximations in method used for any residual types of product or classes of *with-profits insurance contracts*.
- (3) A description of any significant changes to the valuation methods for valuing the costs of guarantees, options or smoothing since the previous valuation.
- (4) For each of the valuation methods under (2)(b), the following information must be disclosed:
- (a) for each of the costs of guarantees, options and smoothing which have

been valued using a full stochastic approach:

- (i) the nature of the guarantee, option or smoothing being valued, including a description of the extent to which the guarantee or option is in or out of the money at the valuation date;
- (ii) a description of the nature of the asset model(s), including the choice of parameters for each model (including the assumed volatility of assets both short term and long term) and any assumed correlations between asset classes and/or between asset classes and economic indicators (such as inflation), and a justification for these assumptions;
- (iii) completion of the following table showing the annualised compound equivalent of the risk free rate(s) assumed for each duration (n) and values derived from the asset model(s) of specified assets/options as shown in the table:

		Asset type (all UK assets)	K=0.75				K=1				K=1.5			
			5	15	25	35	5	15	25	35	5	15	25	35
	n													
	r	Annualised compound equivalent of the risk free rate assumed for the period. (to two decimal places)					x	x	x	x	x	x	x	x
1		Risk-free zero coupon bond					x	x	x	x	x	x	x	x
2		FTSE All Share Index (p=1)												
3		FTSE All Share Index (p=0.8)												
4		Property (p=1)												
5		Property (p=0.8)												
6		15 year risk free zero coupon bonds (p=1)												



## Notes to Table

Row 1 should be completed showing the value of cash payments of £1,000,000 due  $n$  years after the valuation date.

Rows 2 to 15 inclusive should be completed for the appropriate asset classes showing the value of a put option on a portfolio worth £1,000,000 on the valuation date exercisable  $n$  years after the valuation date with strike price of  $K * £1,000,000 * (1+r*p)^n$ .

All references to 15 year bonds mean rolling bonds traded to maintain the 15 year duration at all future dates. The corporate bonds should be assumed to be rolling AA rated zero coupon bonds.

Row 16 should be completed showing the value of sterling receiver swaptions with a strike of 5% exercisable  $n$  years after the valuation date with swap durations on exercise of  $L$  years. The values should be expressed as a percentage of nominal.

In carrying out the calculations required to complete the table above firms should assume, where appropriate, that the underlying asset portfolios are continuously rebalanced to the stated proportions. The property put options should be assumed to relate to a well diversified portfolio of *United Kingdom* commercial property.

A zero trend growth in property prices should be assumed where this is relevant.

In each case the options should be valued with reinvestment of any dividend income into the FTSE All Share index and reinvestment of any rental or other property income into *United Kingdom* property.

Tax should be ignored in all calculations.

All options should be assumed to be European-style.

A *firm* may consider that its model does not need to be calibrated to produce a reasonable value for a particular entry in the table because that entry is insignificant to the valuation of its assets and liabilities. In such circumstances the *firm* may leave an entry in the table blank, but must give an explanation as a note to the table.

- (iv) a statement of the initial equity and property rental yields assumed for the *United Kingdom* and each significant territory as applicable;
- (v) for each significant territory other than the *United Kingdom* a statement of the entries that would be appropriate (for  $K=1$  only) for the risk free rate and lines 1 and 2;

- (vi) a table showing the outstanding durations of significant guarantees within material types of products and/or classes of *with-profits insurance contracts* together with the details of the fit of the asset model(s) to specimen relevant market-traded instruments at these durations;
  - (vii) a statement of the nature of the validations of the asset model(s) by projecting future income, gains and losses on asset values and comparing the net present value of these amounts to the current asset values;
  - (viii) a statement of the number of projections of assets and liabilities carried out and the nature of the validations to ensure reasonable convergence of the model results;
- (b) for each of the costs of guarantees, options and smoothing which have been valued using the market costs of hedging:
- (i) a description of the method and assumptions used to determine the option points and amounts implied by the underlying guarantee or option or smoothing;
  - (ii) a description of the method and assumptions used to value the implied options and hence to determine the costs of the underlying guarantee, option or smoothing (including the assumed volatility of assets both short term and long term and any assumed correlations between asset classes and/or between asset classes and economic indicators (such as inflation) and also including a description as to how those assumptions relate to available market traded instruments and have been assumed to apply in respect of non-available instruments);
  - (iii) completion of a table as at 6(4)(a)(iii) above showing the risk free rate(s) assumed and values derived from the asset model(s) of assets/options as shown in the table;
  - (iv) a statement of the equity and property rental yields assumed for the *United Kingdom* and each significant territory as applicable;
  - (v) a table showing the outstanding durations of significant guarantees within material types of products and/or classes of *with-profits insurance contracts*;
- (c) for each of the costs of guarantees, options and smoothing which have been valued using a series of deterministic projections using attributed probabilities:



- (i) a description of the number of projections of assets and liabilities carried out, the attributed probability to each projection and the range of key assumptions underlying the projections of assets and liabilities;
  - (ii) a description of how the range of projections was selected and how the attributed probabilities were determined;
  - (iii) completion of a table as at 6(4)(a)(iii) above showing the risk free rate(s) assumed and values derived from the asset model(s) of assets/options as shown in the table;
  - (iv) a table showing the outstanding durations of significant guarantees within material types of products and/or classes of *with-profits insurance contracts*.
- (5) Where management actions have been assumed in the projection of assets and liabilities used to determine the costs in (4) (a), (b) and (c):
- (a) a description of the nature of the management actions assumed in the projection of assets and liabilities; and
  - (b) a table of the *firm's* best estimates as to the future proportions of the assets backing the *with-profits benefits reserve* which would consist of equities (whether UK or non-UK) and as to future bonus rates, in each case as at the end of the *financial year in question*, in 5 years time and in 10 years time, making the three sets of assumptions described in this paragraph as to annual investment returns over the periods in question. The table must show, in addition to the specimen equity backing ratios (for the fund), *annual bonus* rates on significant accumulating with-profits business (for each of life and pensions business separately). Calculations should be made assuming that the annual investment return on all assets over the period in question is (i) based on forward rates derived from the risk free interest rate curve as calibrated at the valuation date (ii) based on forward rates derived from the risk free interest rate curve increased across the period by 17.5 % of the long-term gilt yield and (iii) based on forward rates derived from the risk free interest rate curve reduced across the period by 17.5 % of the long-term gilt yield. The effect of any significant assumed equity *derivative contracts* or contracts having the effect of *derivative contracts* on the values disclosed in the table should be described by note. The long-term gilt yield is as defined in *PRU 7.4.11R*.
- (6) For material types of product or classes (as identified in 3 above) a statement of the persistency assumptions used to determine the costs in (4) (a), (b) and (c), and where appropriate the assumed take-up rates of guaranteed annuity

options and the rates of annuitant mortality assumed.

- (7) A statement of the assumptions made, regarding the foreseeable actions that would be taken by *policyholders*, in the projection of assets and liabilities in (4) (a), (b) and (c).

#### **Financing costs**

7. Where financing arrangements exist in connection with any *with-profits fund(s)*, a statement of the type of financing, the sources available for repayment of capital and interest, the extent to which repayments are subordinated to *policyholders'* interests, the face amount outstanding, the rate of interest payable, the level of fees payable, the expected amount to be repaid and the expected time period for such repayment (or, in the case of *reinsurance* arrangements, recapture).

#### **Other long-term insurance liabilities**

8. For each *with-profits fund*, a statement of the nature and amount of *long-term insurance liabilities* which have been included within the amounts of 'any other liabilities related to regulatory duty to treat customers fairly' and 'any other long-term insurance liabilities' shown at lines 46 and 47 of **Form 19**, including disclosure of any value attributed to future tax relief.

#### **Realistic current liabilities**

9. A statement of the nature and amount of current liabilities which have been included within the amount of the *realistic current liabilities* shown at line 51 of **Form 19** together with a reconciliation to the amount of the *regulatory current liabilities*.

#### **Risk capital margin**

10. For the calculation of the *risk capital margin* for each *with-profits fund*:
- (a) a statement of the amount of the *risk capital margin* and of information relating to the individual scenarios in *PRU 7.4.44R* which comprise the most adverse scenario for the purposes of calculating that margin in accordance with *PRU 7.4.43R*, including:
- (i) the percentage change assumed in accordance with *PRU 7.4.68R* for each of the market values of equities and real estate for the purpose of the *market risk* scenario for *United Kingdom* assets and each significant territory in *PRU 7.4.62R(1)(a)*, and a statement as to whether a rise or fall was the most onerous in each case;

- (ii) the nominal change in yields assumed in accordance with *PRU 7.4.68R* for fixed interest securities for the purpose of the *market risk* scenario for *United Kingdom* assets and each significant territory in *PRU 7.4.62R(1)* together with a statement of the percentage change in and level of the long-term gilt yield or nearest equivalent assumed in each case and a statement as to whether a fall or rise in yields is the more onerous in each case);
  - (iii) the average change in spread for bonds (weighted by value) and the total percentage change in asset value separately for (a) bonds, (b) debts, (c) *reinsurance* (d) analogous non-*reinsurance* financing agreements and (e) other assets (by reference to *PRU 7.4.78R*), where the total percentage change is, in each case, calculated as the overall percentage change that results from applying the credit risk scenario to the actual assets of each type held by a *firm*;
  - (iv) the overall percentage change in the *realistic value of liabilities* that results from applying the persistency risk scenario according to *PRU 7.4.100R*, that is, the impact of the persistency risk scenario assuming the market and credit risk stress scenarios have occurred; and
  - (v) to the extent any change in asset value in (iii) is not materially independent of the change in liability values in (iv), a description of the approach to deriving the disclosed changes in asset and liability values;
- (b) a statement of the nature of any management actions assumed in the *risk capital margin* calculation that are in addition to those set out in 6(5)(a) above; and any material changes to other assumptions;
  - (c) (i) a statement of the nature of the assets (categorised as in **Form 48**) and location of assets held to cover the *risk capital margin*;
  - (ii) if any of the assets to cover the *risk capital margin* are located outside of the *with-profits fund*, a statement as to the way the *firm* would intend to make such assets available to the *with-profits fund* should the need arise.

## Tax

11. A statement of the *firm's* treatment of tax included on assets backing (i) the *with-profits benefits reserve(s)*, (ii) any *future policy related liabilities* and (iii)

any *realistic current liabilities*, including any simplifying assumptions.

### **Derivatives**

12. A full description of any major positions in relation to *derivative contracts* or contracts having the effect of *derivative contracts* held by the *with-profits fund* or located outside the *with-profits fund* to cover the *risk capital margin* in part or in full at the valuation date.

### **Analysis of working capital**

13. For each *with-profits fund*, a reconciliation of the significant movements in the working capital of the *with-profits fund* from that shown at line 68 of **Form 19** at the end of the *preceding financial year* and that same entry shown for the *financial year in question*. Such movements must at least include investment return, tax, significant costs (of expenses, guarantees or smoothing) and enhancements or charges to retrospective reserve(s).

### **Optional disclosure**

14. At the option of the *firm*, a statement may be made for each *with-profits fund* of the amount of the *realistic value of liabilities* which relates to contractual obligations to *policyholders*, with a description of the approach taken to distinguishing contractual and non-contractual obligations to *policyholders*.

## **Instructions to the report**

Adhere to numbering above, enter ‘not applicable’ or ‘de minimis’ for sections where there is nil or de minimis data.

## **APPENDIX 9.5 (rule 9.32)**

### **GENERAL INSURANCE BUSINESS ADDITIONAL INFORMATION ON BUSINESS CEDED**

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For the purposes of rule 9.32~~5~~, an *insurer* which carries on *general insurance business* must, in respect of the *financial year in question*, prepare a statement of the following information.

...

## APPENDIX 9.6 (rules 9.34 and 9.35)

Appendix 9.6 is amended as follows:

- (i) paragraphs 1 to 4 are replaced by the new paragraphs 1 to 4 set out below;
- (ii) paragraphs 5 to 11 and the associated headings are deleted; and
- (iii) otherwise as shown using underlining and strike through.

### **CERTIFICATES BY DIRECTORS ~~AND ACTUARY~~ AND REPORTS OF THE AUDITORS**

#### **Part I**

#### **Certificate by directors etc.**

- (1) Subject to 3, the certificate required by rule 9.34 must state -
    - (a) that the *return* has been properly prepared in accordance with the requirements in *IPRU(INS)* and *PRU*; and
    - (b) that the *directors* are satisfied that:
      - (i) throughout the *financial year in question*, the *insurer* has complied in all material respects with the requirements in *SYSC* and *PRIN* as well as the provisions of *IPRU(INS)* and *PRU*; and
      - (ii) it is reasonable to believe that the *insurer* has continued so to comply subsequently, and will continue so to comply in future.
  - (2) An *insurer* does not comply in all material respects with the requirements specified in (1)(b) if it commits a breach of any of those requirements which is significant, having regard to the potential financial loss to *policyholders* or to the *insurer*, frequency of the breach, implications for the *insurer's* systems and controls and if there were any delays in identifying or rectifying the breach.
2. Subject to 3, if the *insurer* carries on *long-term insurance business*, the certificate required by rule 9.34 must also state that -
- (a) in the *directors' opinion*, *premiums* for contracts entered into during the *financial year* and the resulting income earned are sufficient, under reasonable actuarial methods and assumptions, and taking into account the other financial resources of the *insurer* that are available for the purpose, to enable the *insurer* to meet its obligations in respect of those contracts and, in particular, to establish adequate *mathematical reserves*;
  - (b) the sum of the *mathematical reserves* and the deposits

received from *reinsurers* as shown in **Form 14**, together with any amount specified at line 63 of **Form 14** (being part of the excess of the value of the *admissible assets* representing the *long-term insurance funds* over the amount of those funds shown in **Form 14**), constitute proper provision at the end of the *financial year in question* for the *long-term insurance business liabilities* (including all liabilities arising from *deposit back arrangements*, but excluding other liabilities which had fallen due before the end of the *financial year*) including any increase in those liabilities arising from a distribution of surplus as a result of an *actuarial investigation* as at that date into the financial condition of the *long-term insurance business*;

- (c) the *with-profits fund* has been managed in accordance with the *Principles and Practices of Financial Management*, as established, maintained and recorded under *COB 6.10*; and
- (d) the *directors* have, in preparing the *return*, taken and paid due regard to-
  - (i) advice in preparing the *return* from every *actuary* appointed by the *insurer* to perform the *actuarial function* in accordance with *SUP 4.3.13R*; and
  - (ii) if applicable, advice from every *actuary* appointed by the *insurer* to perform the *with-profits actuarial function* in accordance with *SUP 4.3.16R*.

- 3. (1) Where, in the opinion of those signing the certificate, the circumstances are such that any of the statements required by 1 and 2 cannot truthfully be made, the relevant statements must be omitted.
- (2) Where, by virtue of (1), any statements have been omitted from the certificate, this fact, and the reasons for omission must be stated in a note to the certificate.

### **Part III-II**

#### **Auditor's report**

- 4. The report required by rule 9.35 must, in addition to any statement required under rule 9.35, state:
  - (a) whether, in the auditor's opinion:
    - (i) the documents referred to in rules 9.12, 9.13 and 9.14, together with **Forms 40 to 45, 48, 49, 56, 58 and 60** and the statements, analyses and reports annexed pursuant to rules 9.24 to 9.27,

9.29 and 9.31 have been properly prepared in accordance with the *Accounts and Statements Rules* and *PRU*; and

(ii) the methods and assumptions determined by the *insurer* and used to perform the *actuarial investigation* (as set out in the valuation reports) appropriately reflect the requirements of *PRU* 7.3 and *PRU* 7.4.

(b) that, in accordance with rule 9.35(1A), to the extent that any document, Form, statement, analysis or report to be audited under rule 9.35(1) contains amounts or information abstracted from the *actuarial investigation* performed pursuant to rule 9.4, the auditor has obtained and paid due regard to advice from a suitably qualified *actuary* who is independent of the *insurer*.

5. [deleted]

6. [deleted]

7. [deleted]

8. [deleted]

9. [deleted]

10. [deleted]

11. [deleted]

12. Where the auditor refers in the report or in any note attached to it to any uncertainty, the report must state whether, in the auditor's opinion, that uncertainty is material to determining whether the *insurer* has available assets in excess of its ~~*required minimum margin, required EEA minimum margin or required UK minimum margin*~~, as the case may be. *capital resources requirement*.

...

#### **APPENDIX 9.8 (rule 9.36A)**

#### **MARINE MUTUALS: ITEMS TO BE DISREGARDED, DIRECTORS' CERTIFICATES AND AUDITORS REPORTS**

. . . .

## Part II

### Directors' certificates

2. Subject to 4, every *return* provided by a *marine mutual* under rule 9.36A must include a certificate signed by the persons required by rule 9.33 to sign the documents to which the certificate relates –

- (a) confirming that –
  - (i) the *return* has been prepared in accordance with the requirements in *IPRU(INS)* and *PRU Accounts and Statements Rules*,
  - (ii) proper accounting records have been maintained and adequate information on which to base the *return* has been obtained the directors are satisfied that throughout the *financial year in question*, the *marine mutual* has complied in all material respects with the requirements in *SYSC* and *PRIN* as well as the provisions of *IPRU(INS)* and *PRU*, and that it is reasonable to believe that the *marine mutual* has continued so to comply subsequently, and will continue so to comply in future,
  - ~~(iii) appropriate systems and controls have been established and maintained by the *marine mutual* with respect to its transactions and records,~~
  - ~~(iv) the value or amount given for an asset or liability of the *marine mutual* has been determined in accordance with the *Valuation of Assets Rules* and the *Determination of Liabilities Rules*,~~
  - ~~(v) in respect of the *marine mutual's* insurance business not excluded by rule 7.6, throughout the *financial year in question* the *marine mutual* complied with rules 7.1 to 7.5 (currency matching and localisation),~~
  - ~~(vi) the *marine mutual* maintained the *required margin of solvency* throughout the *financial year in question*,~~
  - (viii) each member of the *marine mutual* which is subject to them has accepted those parts of the *marine mutual's* rules which oblige members to pay their share of any supplementary calls for the year and of calls to meet the *required minimum capital requirement margin* (including any sum needed to make good failure by other members to pay calls made on them), and
  - (iviii) the *marine mutual* is empowered to make supplementary calls



on its members which, if met, would produce sufficient assets to meet the ~~required minimum~~ capital requirement margin; and

...

3. Subject to 4, where the *directors* are satisfied that –
- (a) ~~the systems and controls established and maintained by the *marine mutual* in respect of its *insurance business* complied, at the end of the *financial year in question*, with the relevant guidance in **Guidance Notes P.1 and P.2** and it is reasonable to believe that those systems and controls continue so to comply and will continue so to comply in future; or~~
  - (b) ~~the *return* has been prepared in accordance with the relevant guidance in **Guidance Note 9.1**,~~
- ~~it must be so stated in the certificate. [deleted]~~
4. (1) Where, in the opinion of the *directors*, the circumstances are such that any of the matters specified in 2 and 3 cannot be confirmed or provided, the relevant statements or information must be omitted.
- (2) Where any statements or information have been omitted from the certificate in accordance with (1), this fact, and the reasons for omission, must be explained in a note to the certificate.

### Part III

#### Auditor's reports

5. Every *marine mutual* must procure an auditor's report, pursuant to *SUP*, stating whether, in the auditors' opinion –
- (a) the Forms, information and statements required have been properly prepared in accordance with the *Accounts and Statements Rules*; and
  - (b) where the auditors refer in their report or in any note to any uncertainty, that uncertainty is material to determining whether the *marine mutual* has *available assets* in excess of its *capital resources requirement required minimum margin, required EEA minimum margin, or required UK minimum margin*, as the case may be; and
  - (c) ~~subject to 6, it was or was not reasonable for the persons giving the *directors'* certificate to have made the statements in it.~~
- ~~6. Where the information or explanations given to the auditors is insufficient to allow them to be able to express an opinion on the reasonableness of the statements made in the *directors'* certificate, the report must include such~~

~~qualification, amplification or explanation as may be appropriate.~~

...

**Marine mutuals: Statement of solvency assets and liabilities**

Name of insurer

Financial year ended

	Company registration number	Period ended			Units		
		day	month	year	(See instruction 1)		
	M2						
		As at the end of the financial year	As at the end of the previous financial year	Source			
		1	2	Form	Line	Column	

**ASSETS**

Admissible assets	11			M3	. 89
Calls approved by the Board but unmade at the end of the financial year	12				
Total (11+12)	19				

**LIABILITIES**

Unexpended contributions and unearned premiums and any additional amounts set aside for unexpired risks, gross of reinsurance and deferred acquisition costs	21				See instruction 2
Gross provision for outstanding claims	22				See instruction 3
Creditors	23				
Taxation	24				
Other liabilities	25				See instruction 4
Total (21 to 25)	29				

**REQUIRED MINIMUM MARGIN**

<b>Not admissible assets (19-29)</b>	<b>31</b>				
<b>Calls unapproved by the Board at the end of the financial year</b>	<b>32</b>				<b>See instruction 5</b>
<b>Available net assets (31+32)</b>	<b>33</b>				
<b>Required minimum margin</b>	<b>34</b>				
<b>Excess (deficiency) of available net assets over the required minimum margin (33-34)</b>	<b>39</b>				

Appendix 9.9 is inserted as follows

**Appendix 9.9** (rule 9.40 to guidance 9.43)

**Group capital adequacy**

(Form 95)

This appendix contains guidance as to how the report to be provided under rule 9.40 may be set out .

FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING FORM

Form 95

**INSURANCE GROUP CAPITAL ADEQUACY (page 1)**

Name of reporting insurance firm:

Name of insurance parent undertaking:


Calculation of Consolidated Position:

**Limits on capital  
(see notes)**

		£'000	
1. TIER 1			
Group core tier one	Sum of column G1 (page 4)	<input type="text"/>	H1
Group perpetual non-cumulative preference shares	Sum of column G2 (page 4)	<input type="text"/>	H2
Group innovative tier one	Sum of column G3 (page 4)	<input type="text"/>	H3
Deductions from tier one	Sum of column C (page 2)	<input type="text"/>	H4
2. Total group tier one capital	= H1 + H2 + H3 – H4	<input style="border: 2px solid black;" type="text"/>	TT1
3. TIER 2			
Group upper tier two	Sum of column G4 (page 4)	<input type="text"/>	H5
Group lower tier two	Sum of column G5 (page 4)	<input type="text"/>	H6
4. Total group tier two capital	= H5 + H6	<input style="border: 2px solid black;" type="text"/>	TT2
5.			
6. Group capital resources before deductions	= TT1 + TT2	<input style="border: 2px solid black;" type="text"/>	TCR
Total group capital resources deductions	Sum of column D1 & D2 (page 2)	<input type="text"/>	H7
Group capital resources:	= TCR – H7	<input style="border: 2px solid black;" type="text"/>	GCR
Group capital resources requirement:	Sum of column B (page 2)	<input style="border: 2px solid black;" type="text"/>	GCCR
Group surplus/ (deficit)	= GCR – GCCR	<input style="border: 2px solid black;" type="text"/>	I

FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING FORM

**INSURANCE GROUP CAPITAL ADEQUACY (page 2)**

Name of reporting insurance firm:

--

Name of insurance parent undertaking:

--

A	A1	A2	B	C	D1	D2
Name of related undertaking	% interest	Type of firm	CRR	Deductions from Tier 1	Inadmissible assets	Ancillary services undertakings deduction

Related undertaking 1						
Related undertaking 2						
Related undertaking 3						

Parent:						
---------	--	--	--	--	--	--

Totals:						
---------	--	--	--	--	--	--

FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING FORM

Name of reporting insurance firm:

Name of insurance parent undertaking:


<b>A</b> Name of related undertaking
---

E1	E2	E3	E4	E5	F1	F2	F3	F4	F5
<b>Group's investment in the capital resources of related undertaking</b>					<b>Components of the capital resources of related undertakings</b>				
Core tier 1	Perpetual non-cumulative preference shares	Innovative tier 1	Upper tier 2	Lower tier 2	Core tier 1	Perpetual non-cumulative preference shares	Innovative tier 1	Upper tier 2	Lower tier 2

Related undertaking 1
Related undertaking 2
Related undertaking 3


FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING FORM

**INSURANCE GROUP CAPITAL ADEQUACY (page 4)**

Name of reporting insurance firm:


Name of insurance parent undertaking:

<b>A</b>
Name of related undertaking

G1	G2	G3	G4	G5
<b>Net Contribution to Group Capital Resources</b>				
Core tier 1	Perpetual non-cumulative preference shares	Innovative tier 1	Upper tier 2	Lower tier 2
=F1-E1	=F2-E2	=F3-E3	=F4-E4	=F5-E5

Related undertaking 1
Related undertaking 2
Related undertaking 3


Parent's Capital Resources (by class of capital)
--

--	--	--	--	--

Totals
--------

--	--	--	--	--



## FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS

### Insurance Group Capital Adequacy

<i>Ref</i>	<i>Instructions</i>
A (pages 2, 3 & 4)	<p>List the name of each <i>related undertaking</i> of the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> (as applicable) which is a <i>regulated related undertaking</i> or an <i>ancillary services undertaking</i>.</p> <p>Pursuant to <i>PRU</i> 8.3.18R to 8.3.22R, several entities may be combined where these are not material in relation to the <i>insurance group</i>. The <i>firm</i> should list the relevant entities in a note to the return and should be able to demonstrate the contribution of the individual entities to the group calculation.</p>
A1 (page 2)	<p>List the percentage interest in the <i>regulated related undertaking</i> listed in A held by the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> (as applicable).</p> <p>For the purposes of calculating the percentage interest in accordance with <i>PRU</i> 8.3.28R and 8.2.29R, if the interest is not held directly by the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> but by another member of the <i>insurance group</i>, enter the effective percentage interest of the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> in that <i>undertaking</i> (e.g. where a <i>parent</i> has a 50% holding in a <i>subsidiary</i> which in turn has a 50% holding in another <i>subsidiary</i>, the <i>ultimate parent undertaking's</i> effective percentage interest in the second <i>subsidiary</i> is 25% etc.).</p> <p>Where the entity is a <i>subsidiary</i> of a <i>subsidiary</i> of the <i>parent undertaking</i> (etc.), indicate (S) after the effective percentage interest. Such an entity should be treated as a <i>subsidiary</i> of the <i>parent undertaking</i> and will be included in the calculations in proportion to the <i>parent undertaking's</i> effective percentage interest (or in full if there is a capital resources deficit) (see <i>PRU</i> 8.3.30R and 8.3.31R).</p>

**FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS**

<i>Ref</i>	<i>Instructions</i>
A2 (page 2)	<p>State if the <i>related undertaking</i> listed in A is a <i>regulated insurance entity, pure reinsurer, insurance undertaking</i> that is not a <i>regulated insurance entity, insurance holding company, investment firm, credit institution, financial institution</i> which is not either a <i>credit institution or investment firm, financial holding company, asset management company or ancillary services undertaking</i>.</p> <p>For <i>related undertakings</i> which are <i>ancillary services undertakings</i> entries should only be made in this column and column D2 on page 2.</p>
B (page 2)	<p>State the <i>ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking's</i> share (i.e multiplied by the percentage in A1) of the <i>individual capital resources requirement</i> of the <i>regulated related undertaking</i>, or the full amount if there is a capital resources deficit. This is the requirement set out in <i>PRU 8.3.34R</i>.</p>
C (page 2)	<p>State the <i>ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking's</i> share (or the full amount if there is a capital resources deficit) of the <i>regulated related undertaking's</i> Tier 1 deductions calculated under the <i>sectoral rules</i> that apply to it.</p>
D1 (page 2)	<p>State the <i>ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking's</i> share (or the full amount if there is a capital resources deficit) of any inadmissible assets held by the <i>regulated related undertaking</i> (see <i>PRU 8.3.60R</i>)</p>
D2 (page 2)	<p>This column should be completed only for <i>related undertakings</i> which are <i>ancillary services undertakings</i>. The entry is the higher of: the book value of the direct or indirect investment by the <i>ultimate insurance parent undertaking or ultimate EEA insurance parent undertaking</i> in the <i>ancillary services undertaking</i>; and the <i>ancillary services undertaking's</i> notional capital resources requirement (see <i>PRU 8.3.62R to 8.3.64R</i>)</p>

**FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS**

<i>Ref</i>	<i>Instructions</i>
E1 E2 E3 E4 E5 (page 3)	<p>The entries in E1 to E5 should be the book value of the investments of all members of the <i>insurance group</i> in the <i>solo capital resources</i> of each <i>regulated related undertaking</i> listed in A (this represents internal group holdings of the <i>solo capital resources</i> of each <i>regulated related undertaking</i> to be excluded from <i>group capital resources</i> under <i>PRU</i> 8.3.49R, 8.3.51R, 8.3.54R, 8.3.56R and 8.3.58R).</p> <p>The book value of the group’s investment in <i>core tier one capital resources*</i> should be shown in E1; investments in perpetual non-cumulative <i>preference shares*</i> should be shown in E2; and investments in <i>innovative tier 1 capital resources*</i> should be shown in E3.</p> <p>The book value of the group’s investment in <i>tier two capital resources</i> should be shown in E4 (<i>upper tier two capital resources*</i>) and E5 (<i>lower tier two capital resources*</i>).</p> <p>[* these terms should be applied in accordance with <i>PRU</i> 8.3.37R to the <i>undertaking</i> in question].</p>
F1 F2 F3 F4 F5 (page 3)	<p>The entries in F1 to F5 should be the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking's</i> share (or the full amount if there is a capital resources deficit) of the components of the <i>solo capital resources</i> of the <i>regulated related undertaking</i> (see <i>PRU</i> 8.3.48R(2), 8.3.50R(2), 8.3.53R(2), 8.3.55R(2) and 8.3.57R(2)).</p>

**FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS**

<i>Ref</i>	<i>Instructions</i>
G1 G2 G3 G4 G5 (page 4)	<p>These entries represent the contribution to <i>group capital resources</i> of the <i>regulated related undertaking</i>. G1 is calculated as the difference between column F1 and E1. (G1 can be positive or negative. A negative figure would principally represent goodwill on acquisition).</p> <p>Similarly G2 is the difference between F2 and E2, G3 is the difference between F3 and E3 etc. (G2, G3, G4 &amp; G5 would normally be positive).</p> <p>The totals of columns G1, G2 and G3 respectively represent the group's <i>core tier one capital</i>, perpetual non-cumulative <i>preference shares</i> and <i>innovative tier one capital resources</i> (see H1 to H3 on page 1).</p> <p>The sum of columns G4 and G5 represent the group's <i>tier two capital resources</i> (see H5 and H6).</p>
Parent's capital resources (page 4)	<p>The entries in this line represent the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking's capital resources</i>, after deduction of the book value of the investments taken together of the individual members of the <i>insurance group</i> in those <i>capital resources</i>. The deduction excludes any holding by the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> (as applicable) of its own <i>shares</i>; such holdings are deducted in calculating the parent's <i>tier one capital resources</i>.</p>
H1 H2 H3 H4 (page 1)	<p>H1 to H3 represent the total contribution of the <i>regulated related undertakings</i> and the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> to <i>total group tier one capital</i>. H4 represents the sum of the Tier 1 deductions for all members of the <i>insurance group</i>.</p>

**FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS**

<i>Ref</i>	<i>Instructions</i>
TT1 (page 1)	<p>This entry is <i>total group tier one capital</i> (see stage A of PRU 8.3.43R) after application of limits 1, 2 and 3 below:</p> <p>Limit 1: <i>Total group tier one capital</i>, less <i>innovative tier one capital resources</i> included in <i>total group tier one capital</i>, must account for at least 50% of the <i>group capital resources requirement</i> less any <i>with-profits insurance capital components</i> included in the <i>group capital resources requirement</i> (see PRU 8.3.45R(1)(a)).</p> <p>Limit 2: <i>Core tier one capital resources</i> included in <i>total group tier one capital</i> must account for at least 50% of <i>total group tier one capital</i> (see PRU 8.3.45R(1)(c)).</p> <p>Limit 3: <i>Innovative tier one capital resources</i> included in <i>total group tier one capital</i> must not exceed 15% of <i>total group tier one capital</i> (see PRU 8.3.45R(1)(d)).</p> <p>Any capital item excluded by limit 3 may form part of <i>total group tier two capital</i> (see PRU 8.3.46G).</p>
H5 H6 (page 1)	<p>These entries represent the total contribution of the <i>regulated related undertakings</i> and the <i>ultimate insurance parent undertaking</i> or <i>ultimate EEA insurance parent undertaking</i> to <i>total group tier two capital</i>.</p>
TT2 (page 1)	<p>This entry is calculated as the sum of H5 and H6 which represents <i>total group tier two capital</i> (stage B in PRU 8.3.43R) after application of limits 4 and 5 as follows:</p> <p>Limit 4: <i>Total group tier two capital</i> must not exceed <i>total group tier one capital</i> (see PRU 8.3.45R(1)(e)).</p> <p>Limit 5: <i>Lower tier two capital resources</i> calculated in accordance with PRU 8.3.57R included in <i>total group tier two capital</i> must not exceed 50% of <i>total group tier one capital</i> (see PRU 8.3.45R(1)(f)).</p>

**FORM 95: INSURANCE GROUP CAPITAL ADEQUACY REPORTING INSTRUCTIONS**

<i>Ref</i>	<i>Instructions</i>
TCR (page 1)	<p>This entry is calculated as the sum of TT1 and TT2 and represents group capital resources before deductions (stage C in <i>PRU</i> 8.3.43R) after application of limit 6 as follows:</p> <p>Limit 6: <i>Total group tier one capital less innovative tier one capital resources included in total group tier one capital, plus total group tier two capital less any lower tier two capital resources included in total tier two capital must account for at least 75% of the group capital resources requirement less any with-profits insurance capital components included in the group capital resources requirement (PRU 8.3.45R(1)(b)).</i></p>
H7 (page1)	<p>This entry is the sum of columns D1 and D2 on page 2 which represent deductions to be made from total <i>group capital resources</i> in respect of the group's interest in inadmissible assets (see 8.3.59R), and <i>ancillary services undertakings</i> (see <i>PRU</i> 8.3.62R).</p>
GCR (page1)	<p>This entry is calculated as TCR less H7. This represents <i>group capital resources</i> (stage H in <i>PRU</i> 8.3.43R).</p>
GCCR (page 1)	<p>This entry is calculated as the sum of column B on page 2 which represents the <i>group capital resources requirement (PRU</i> 8.3.33R).</p>
I (page 1)	<p>This is calculated as total <i>group capital resources</i> less total <i>group capital resources requirement (GCR – GCRR)</i>. This represents the amount by which <i>group capital resources</i> exceed or fail to exceed the <i>group capital resources requirement</i>.</p>

### **Part 3: Amendments to volume 3 of the Interim Prudential sourcebook for insurers**

In this part underlining indicates new text and striking through indicates deleted text. Where an entire section is deleted, the place where the change will be made is indicated and the text is not struck through.

## **INTERIM PRUDENTIAL SOURCEBOOK FOR INSURERS**

### **CONTENTS**

#### **VOLUME THREE**

#### **FSA GUIDANCE NOTES**

- Guidance Note P.1 ~~Systems and controls over the investments (and counterparty exposure) with particular reference to the use of derivatives (Principles for business) [deleted]~~
- Guidance Note P.2 ~~Systems and controls over general business claims provisions (Principles for business) [deleted]~~
- Guidance Note P.3 ~~Systems and controls in insurers [deleted]~~
- Guidance Note 2.1 ~~Hybrid capital: admissibility for solvency (rule 6.1 and required margin of solvency) [deleted]~~
- Guidance Note 2.2 ~~Guidance on applications for waivers relating to implicit items [deleted]~~
- Guidance Note 2.3 ~~Solvency margin: implementation of Solvency 1 Directives [deleted]~~
- Guidance Note 4.1 ~~Guidance for insurers and auditors on the Valuation of Assets Rules [deleted]~~
- Guidance Note 4.2 ~~Use of derivative contracts in insurance funds (rule 4.12) [deleted]~~
- Guidance Note 4.4 ~~Linked contracts [deleted]~~
- Guidance Note 5.1 ~~Resilience test [replaced by Guidance Note No.4 (Resilience test for insurers) until the Integrated Prudential Sourcebook comes into force] [deleted]~~
- Guidance Note 9.1 ~~Preparation of returns [deleted]~~
- Guidance Note 9.2 [deleted]
- Guidance Note 10.1 ~~Parent undertaking solvency calculation [deleted]~~

## **GUIDANCE: FSA ‘DEAR DIRECTOR’ LETTERS**

DD1 ~~Use of derivatives—listed products~~ [deleted]

## **OTHER MATERIAL: ‘DEAR APPOINTED ACTUARY’ LETTERS**

DAA8 ~~Recommended aids-reserving policy~~ [deleted]  
DAA9 ~~Pensions review: reserving for guarantees~~ [deleted]  
DAA11 ~~Reserving for guaranteed annuity options~~ [deleted]  
DAA13 ~~Reserving for guaranteed annuity options~~ [deleted]  
DAA14 ~~[deleted]~~  
DAA15 ~~[deleted]~~

The following guidance notes are deleted:

Guidance Note P.1 Systems and controls over the investments (and counterparty exposure) with particular reference to the use of derivatives (Principles for business)

Guidance Note P.2 Systems and controls over general business claims provisions (Principles for business)

Guidance Note P.3 Systems and controls in insurers

Guidance Note 2.1 Hybrid capital: admissibility for solvency (rule 6.1 and required margin of solvency)

Guidance Note 2.2 Guidance on applications for waivers relating to implicit items

Guidance Note 2.3 Solvency margin: implementation of Solvency 1 Directives

Guidance Note 4.1 Guidance for insurers and auditors on the Valuation of Assets Rules

Guidance Note 4.2 Use of derivative contracts in insurance funds (rule 4.12)

Guidance Note 4.4 Linked contracts

Guidance Note 5.1 Resilience test

Guidance Note 9.1 Preparation of returns

Guidance Note 10.1 Parent undertaking solvency calculation



The following 'Dear Director' letter is deleted

DD1 Use of derivatives – listed products

The following 'Dear appointed actuary' letters are deleted

DAA8 Recommended aids reserving policy

DAA9 Pensions review: reserving for guarantees

DAA11 Reserving for guaranteed annuity options

DAA13 Reserving for guaranteed annuity options

**Guidance Note P.1** [deleted]

**Guidance Note P.2** [deleted]

**Guidance Note P.3** [deleted]

**Guidance Note 2.1** [deleted]

**Guidance Note 2.2** [deleted]

**Guidance Note 2.3** [deleted]

**Guidance Note 4.1** [deleted]

**Guidance Note 4.2** [deleted]

**Guidance Note 4.4** [deleted]

**Guidance Note 5.1** [deleted]

**Guidance Note 9.1** [deleted]

**Guidance Note 10.1** [deleted]

**DD1** [deleted]

**DAA8** [deleted]

**DAA9** [deleted]

**DAA11**      [deleted]

**DAA13**      [deleted]

## Annex H

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

1.2.2 G (1) ...

(2) In relation to (1), *insurers* should note that ~~*IPRU(INS) 1.3R*~~ *PRU 7.6.13R* prevents an *insurer* from carrying on an *insurance mediation activity* ...

...

1 Annex 2G – Summary of Handbook provisions for insurance intermediaries

2. Table

...		
Business Standards	Interim Prudential sourcebooks	
	...	...
	Prudential sourcebook <i>PRU 9.1 – PRU 9.3</i>	Applies in respect of (1).
	<del><i>PRU 9.4</i></del>	Applies in respect of (1) where the <i>insurance intermediary</i> is also an <i>insurer</i> <del>or a mortgage lender</del> .
	<u><i>PRU 9.4</i></u>	<u>Applies in respect of (1) where the <i>insurance intermediary</i> is also a <i>mortgage lender</i>.</u>
...		

...

4.2.13 G (1) ...

(2) ~~*IPRU(INS) 1.3R*~~ *PRU 7.6.13R* (Restriction of business to insurance) in practice restricts the business which an *insurer* can carry on.

...

## Annex I

### Amendments to the Market Conduct sourcebook (MAR)

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

3.3.2 G ... *Firms* should also consider the other provisions of the *Handbook*, especially but not exclusively *ML*, ~~and~~ *IPRU* and *PRU*.

...

## Annex J

### Amendments to the Authorisation manual (AUTH)

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.5.3 G ...

- (1) Prudential requirements:
  - (a) ...
  - (b) the detailed prudential requirements in the Interim Prudential Sourcebooks (collectively referred to as *IPRU*) and in the Integrated Prudential Sourcebook (*PRU*) in the Business Standards part of the *Handbook*. In addition to *PRU* there are five interim sourcebooks that apply, respectively, to *banks (IPRU(BANK))*, *building societies (IPRU(BSOC))*, *friendly societies (IPRU(FSOC))*, *insurance companies (IPRU(INS))* and *investment business firms (IPRU(INV))*. *Guidance* is given to applicants in *AUTH 3 Annex 2G* on determining which prudential category, and which sourcebook of *IPRU* or section of *PRU* will apply.

...

- (2) Systems, controls and internal arrangements:
  - (a) ...
  - (b) the detailed requirements, many of which are *regulated activity* specific, in the sourcebooks in the Business Standards part of the *Handbook*; for example, in *IPRU*, *PRU*, the Training and Competence Sourcebook (*TC*), the Money Laundering Sourcebook (*ML*) and Conduct of Business Sourcebook (*COB*); ...

...

...

3.8.4 G (1) ...

- (2) The *Single Market Directives*, the *Capital Adequacy Directive* and the *E-Money Directive* set out minimum financial requirements for all *firms* which carry on banking, issuing e-money, insurance or investment services within the scope of the *Single Market Directives* and the *E-Money Directive*, that is, most *firms* that are *credit institutions*, *financial institutions*, *insurance undertakings* or *investment firms* as defined in these Directives. These requirements are reflected in *PRU* or in the

relevant *IPRU* for each type of *firm*.

...

3.8.6 G An applicant in the prudential category of *bank* or *insurer* should note that the *FSA* will give it individual guidance on its likely capital requirements: for example, the individual capital ratios for a *bank* (see *IPRU(BANK)* CO 4.1.1 (Individual capital ratios)) or the ~~capitalisation or solvency margin~~ *capital resources requirements* of an *insurer* (see ~~*IPRU(INS)* 2 (Margins of Solvency)~~ *PRU* 2.1)) during pre-application discussions (see *AUTH* 3.9.2G).

3.8.7 G Applicants should note that the prudential category and, where relevant, sub-category, not only determines which provisions in the relevant *IPRU* or *PRU* will apply, but which provisions on auditors, financial reporting and transaction reporting in ~~the~~ *SUP* will apply.

3.8.8 G An applicant that is a member of a *group* should note that the *FSA* may take into consideration the impact of other members of the *group* on the adequacy of its resources (see the relevant sections of *PRU* or *IPRU*).

...

3.12.2 G An applicant seeking to carry on *insurance business* should note the restrictions in ~~*IPRU(INS)* 1.3R(1) and *IPRU(FSOC)* 1.3R~~ *PRU* 7.6.13R which relate to the carrying on of other commercial business.

3.12.3 G (1) As a result of these restrictions, the *FSA* will grant an applicant seeking to carry on *insurance business Part IV permission* for *insurance business*, and any other *regulated activities*, only to the extent they are not restricted under ~~*IPRU(INS)* and *IPRU(FSOC)*~~ *PRU*.

(2) ... If the *FSA* gives an applicant *Part IV permission* for *insurance business* and other *regulated activities*, these other *regulated activities* will be subject to *limitations*, as appropriate, so as to comply with ~~*IPRU(INS)* 1.3R(1) and *IPRU(FSOC)* 1.3R~~ *PRU* 7.6.13R.

...

3.12.15 G An applicant which has its head office outside the *United Kingdom* (other than an *EEA firm*, *Treaty firm* or a *Swiss general insurance company*) should note the requirement in ~~*IPRU(INS)* 8.403R~~ to appoint a *chief executive* ...

3.12.16 G A *Swiss general insurance company* seeking to establish a *branch* in the *United Kingdom* should note the requirement referred to in ~~*IPRU(INS)* 18.11R~~ *COND* 2.6.1G to appoint an *authorised UK representative* for the *United Kingdom*.

3.12.17 G An applicant with its head office outside the *United Kingdom* (other than an *EEA firm* or a *Treaty firm*) seeking *permission* to carry on direct or both direct and reinsurance business in the *United Kingdom* should note that specific prudential requirements apply (see ~~*IPRU(INS)*~~*PRU*).

...

3.18.3 G The *FSA's* regulatory requirements, including *PRU* and *IPRU*, will apply to a *firm* in full and worldwide, unless otherwise stated. ...

...

Auth 5 Annex 3

2 G

(1) Module of Handbook	(2) Potential application to an incoming EEA firm with respect to activities carried on from an establishment of the firm (or its appointed representative) in the United Kingdom	(3) Potential application to an incoming EEA firm with respect to activities carried on other than from an establishment of the firm (or its appointed representative) in the United Kingdom
...		
<u><i>PRU</i></u>	... <u><i>PRU</i></u> 9.4...does not apply unless the <i>firm</i> has a <i>top-up permission</i> . <u>Otherwise, <i>PRU</i> does not apply unless the <i>firm</i> is an <i>insurer</i> to which <i>PRU</i> 7.6.33R applies</u>	
...		

## Annex K

### Amendments to the Supervision manual

#### Part 1: Amendments to SUP App 2

In this part, where existing text is replaced by new text, this is indicated and the new text is not underlined.

SUP App 2 is deleted and re-made, with amendments, as follows:

- 2 Insurers: Regulatory intervention points
  - 2.1 Application
    - 2.1.1 R This appendix applies to an *insurer* unless it is:
      - (1) a *Swiss general insurer*; or
      - (2) an *EEA-deposit insurer*; or
      - (3) an *incoming EEA firm*; or
      - (4) an *incoming Treaty firm*.
    - 2.1.2 G This appendix applies to every *friendly society* as a *friendly society* is an *insurer*.
  - 2.2 Interpretation
    - 2.2.1 R For the purpose of SUP App 2:
      - (1) “capital resources”:
        - (a) in relation to a *non-directive friendly society*, has the meaning given to “margin of solvency” in *rule 4.1(4) of IPRU(FSOC)*;
        - (b) in relation to a *participating insurance undertaking*, means P+T, where P and T have the meanings given by *PRU 8.3.45R(3)(a) and (e)* respectively, as calculated in accordance with *PRU 8.3.43R*; and
        - (c) in relation to any other *firm*, means the *firm’s capital resources* as calculated in accordance with *PRU 2.2.12R*;
      - (2) “guarantee fund”:
        - (a) in relation to a *non-directive friendly society*, has the meaning given to that term in *IPRU(FSOC)*;



- (b) in relation to a *participating insurance undertaking*, means the amount of capital resources which that *firm* must hold to comply with *PRU 8.3.45R(2)*;
  - (c) in relation to a *firm* which is not covered by (a) or (b), carrying on *general insurance business*, means the amount of capital resources which that *firm* must hold to comply with *PRU 2.2.18R*; and
  - (d) in relation to a *firm* which is not covered by (a) or (b), carrying on *long-term insurance business*, means the amount of capital resources which that *firm* must hold to comply with *PRU 2.2.17R*;
- (3) “material transaction” means a transaction (when aggregated with any similar transactions) in which:
- (a) the price actually paid or received for the transfer of assets or liabilities or the performance of services; or
  - (b) the price which would have been paid or received had that transaction been negotiated at arm’s length between unconnected parties;

exceeds:

- (c) in the case of a *firm* which carries on *long-term insurance business*, but not *general insurance business*, the sum of €20,000 and 5% of the *firm*’s liabilities arising from its *long-term insurance business*, excluding *property-linked liabilities* and net of *reinsurance ceded*; or
- (d) in the case of a *firm* which carries on *general insurance business*, but not *long-term insurance business*, the sum of €20,000 and 5% of the *firm*’s liabilities arising from its *general insurance business*, net of *reinsurance ceded*; or
- (e) in the case of a *firm* which carries on both *long-term insurance business* and *general insurance business*:
  - (i) where the transaction is in connection with the *firm*’s *long-term insurance business*, the sum of €20,000 and 5% of the *firm*’s liabilities arising from its *long-term insurance business*, excluding *property-linked liabilities* and net of *reinsurance ceded*; and
  - (ii) in all other cases, the sum of €20,000 and 5% of the *firm*’s liabilities arising from its *general insurance business*, net of *reinsurance ceded*; and

- (4) “required margin of solvency”:
- (a) in relation to a *non-directive friendly society*, has the meaning given to that term in *IPRU(FSOC)*;
  - (b) in relation to a *participating insurance undertaking*, means R-S-U, where R, S and U have the meanings given by *PRU* 8.3.45R(3)(c), (d) and (f) respectively;
  - (c) in relation to a *firm* which is not covered by (a) or (b), carrying on *general insurance business*, means the *general insurance capital requirement* applicable to that *firm*; and
  - (d) in relation to a *firm* which is not covered by (a) or (b), carrying on *long-term insurance business*, means the *long-term insurance capital requirement* applicable to that *firm*.

2.2.2 G The calculation of each of the *base capital resources requirement*, the *long-term insurance capital requirement* and the *general insurance capital requirement* is set out in *PRU* 2.1. The calculation of each of the “guarantee fund” and “required margin of solvency” for *non-directive friendly societies* is set out in chapter 4 of *IPRU(FSOC)*.

### 2.3 Purpose

2.3.1 G To fulfil its obligations under the *Insurance Directives*, and as part of the *FSA*’s risk-based approach to supervision, there are certain times when the *FSA* needs to monitor a *firm* more closely than it normally would. This is so the *FSA* can fulfil its function of supervising *firms* properly and meet the *regulatory objective* of securing an appropriate degree of protection for *consumers*.

2.3.2 G The *rules* in this appendix require a *firm* to submit reports and information to the *FSA* when:

- (1) a *firm* is failing to satisfy *threshold condition* 4 (Adequate resources) (see *COND* 2.2), and its capital resources have fallen below its required margin of solvency, or its guarantee fund; or
- (2) the capital resources of a *firm* have fallen below its *capital resources requirement*; or
- (3) a *firm* has decided to cease to *effect new contracts of insurance*; or
- (4) a *firm* is going through periods of potential uncertainty, for example, when it has come under the *control* of a new *parent undertaking* or following the grant or variation of *permission*.

2.3.3 G The *FSA* may also ask a *firm* to submit reports and information to it

when the *firm's* capital resources fall below the level advised in individual capital *guidance* given to the *firm*.

- 2.3.4 G In accordance with the *Insurance Directives*, a *firm* whose capital resources have fallen below its required margin of solvency, or its guarantee fund, is required, by the *rules* set out in this appendix, to submit a *scheme of operations*, together with an explanation of how its capital resources will be adequately restored. In order to secure an appropriate degree of protection for *consumers*, the *FSA* applies the *rules* in this appendix to *firms* to which the provisions of the *Insurance Directives* would not otherwise apply.
- 2.3.5 G A *firm* which is entering into run-off is required to submit a *scheme of operations*, including an explanation of how its *liabilities to policyholders* will be met in full. Where the capital resources of such a *firm* subsequently fall below its required margin of solvency, the *firm* is required to submit a plan for restoration.
- 2.3.6 G Following a change in *control*, or the grant or variation of *permission*, the reports submitted help the *FSA* to identify when a *firm* departs from the *scheme of operations* submitted as part of the notification of a change in *control*, or an application for the grant or variation of *permission*, and on which basis such notification or application was approved.
- 2.3.7 G *Principle 4* of the *FSA's* Principles for Businesses provides that *firms* should hold adequate financial resources, while *PRU 1.2.22R* requires a *firm* to maintain overall financial resources which are adequate to ensure that there is no significant risk that it cannot meet its liabilities as they fall due. In considering these requirements, a *firm* may decide to maintain capital resources above the level advised in individual capital *guidance* given by the *FSA*, or, if no individual capital *guidance* has been given, above its *capital resources requirement*. The amount of any such additional capital resources held is at the discretion of the *firm*. However, the extent to which a *firm* matches these additional capital resources to the volatility of its capital base, in conjunction with the strength of its systems and controls environment, is likely to affect the frequency with which it is subject to intervention under this appendix.
- 2.3.8 G In relation to a *firm* carrying on *with-profits insurance business*, action which it takes either to restore its capital resources to the levels set by the intervention points in this appendix, or to prevent its capital resources falling below those points, should be consistent with *Principle 6* of the *FSA's* Principles for Businesses. *Principle 6* requires a *firm* to pay due regard to the interests of its *customers* and treat them fairly.
- 2.3.9 G These *rules* are in addition to the other *rules* and *guidance* in *SUP*, in particular *SUP 2* (Information gathering by the *FSA* on its own

initiative), *SUP* 15 (Notifications to the *FSA*), *SUP* 16 (Reporting requirements) and the Principles for Businesses (*PRIN*).

## 2.4 Capital resources below guarantee fund

2.4.1 R If a *firm*'s capital resources fall below its guarantee fund, it must, within 14 days of the *firm* becoming aware of this event, submit to the *FSA* a short-term financial plan, including:

- (1) a *scheme of operations* (see *SUP* App 2.12); and
- (2) an explanation of how, if at all, and by when, it expects its capital resources to be adequately restored to the guarantee fund.

2.4.2 G See *SUP* App 2.11.2G for *guidance* on the period that the *scheme of operations* should cover.

## 2.5 Capital resources below required margin of solvency

2.5.1 R Unless *SUP* App 2.5.3R applies:

- (1) if a *firm*'s capital resources are such that they no longer equal or exceed its required margin of solvency; or
- (2) if a *firm* no longer complies with *PRU* 2.2.16R and *PRU* 2.2.24R, or *PRU* 8.3.45R(1)(a) and *PRU* 8.3.45R(1)(b), as applicable;

it must, within 28 days of becoming aware of this event, submit to the *FSA* a plan for the restoration of a sound financial position, including:

- (3) a *scheme of operations*; and
- (4) an explanation of how, if at all, and by when:
  - (a) it expects its capital resources to be restored to the required margin of solvency; or
  - (b) as the case may be, it expects to comply with *PRU* 2.2.16R and *PRU* 2.2.24R, or *PRU* 8.3.45R(1)(a) and *PRU* 8.3.45R(1)(b), as applicable.

2.5.2 G See *SUP* App 2.11.2G for *guidance* on the period that the *scheme of operations* should cover.

2.5.3 R If a *firm*:

- (1) falls into *SUP* App 2.5.1R(1) or (2); and
- (2) it has previously submitted either a run-off plan in accordance

with *SUP* App 2.8.1R or a *scheme of operations* in accordance with *SUP* App 2.5.1R;

it must, within 28 days of becoming aware that it falls into *SUP* App 2.5.1R(1) or (2):

- (3) notify the *FSA*; and
- (4) submit a plan for restoration which:
  - (a) explains why the *firm's* capital resources have fallen below its required margin of solvency or, as the case may be, it no longer complies with *PRU* 2.2.16R or *PRU* 2.2.24R, or *PRU* 8.3.45R(1)(a) and *PRU* 8.3.45R(1)(b), as applicable; and
  - (b) demonstrates how, if at all, and by when, the *firm* will restore it or, as the case may be, resume compliance with *PRU* 2.2.16R and *PRU* 2.2.24R, or *PRU* 8.3.45R(1)(a) and *PRU* 8.3.45R(1)(b), as applicable.

## 2.6 Capital resources below capital resources requirement

2.6.1 R Unless any of *SUP* App 2.4.1R, 2.5.1R or 2.5.3R applies, if a *firm's* capital resources fall below its *capital resources requirement*, it must, within 28 days of becoming aware of this event:

- (1) notify the *FSA*; and
- (2) submit a plan for restoration, which:
  - (a) explains why the *firm's* capital resources have fallen below its *capital resources requirement*; and
  - (b) demonstrates how, if at all, and by when, the *firm* will restore it.

## 2.7 Capital resources below the level of individual capital guidance

2.7.1 G Unless any of *SUP* App 2.4.1R, 2.5.1R, 2.5.3R or 2.6.1R applies, if a *firm's* circumstances change, such that its capital resources have fallen, or are expected to fall, below the level advised in individual capital *guidance* given to the *firm* by the *FSA*, then, consistent with *PRIN* 2.1.1R *Principle* 11 (Relations with regulators), a *firm* should inform the *FSA* of this fact as soon as practicable, explaining why capital resources have fallen, or are expected to fall, below the level advised in individual capital *guidance*, and:

- (1) what action the *firm* intends to take to increase its capital resources; or

- (2) what modification the *firm* considers should be made to the individual capital *guidance* which it has been given.
- 2.7.2 G In the circumstance set out in *SUP* App 2.7.1G, the *FSA* may ask a *firm* for alternative or more detailed proposals and plans or further assessments and analyses of capital adequacy and risks faced by the *firm*. The *FSA* will seek to agree with the *firm* appropriate timescales and scope for any such additional work, in light of the circumstances which have arisen.
- 2.7.3 G In relation to a *firm* carrying on *with-profits insurance business*, if it intends either (a) to remedy a fall in the level of capital resources advised in its individual capital *guidance*, or (b) to prevent a fall in the level advised in that *guidance*, for example, in either case, by taking management action to de-risk a *with-profits fund* or by reducing non-contractual benefits for *policyholders*, it should explain to the *FSA* how such proposed actions are consistent with the *firm's* obligations under *PRIN* 2.1 Principle 6 (Customers' interests).
- 2.7.4 G If a *firm's* capital resources fall below the level advised in individual capital *guidance* given to the *firm* and, at the same time, any one or more of *SUP* App 2.4.1R, 2.5.1R, 2.5.3R or 2.6.1R applies, the *firm* should first comply with those *rules*. Those *rules* are concerned with circumstances where capital resources are likely to have fallen to levels much lower than the level advised in individual capital *guidance* and are, in some cases, requirements imposed by the *Insurance Directives*.
- 2.7.5 G If a *firm* has not accepted individual capital *guidance* given by the *FSA* it should, nevertheless, inform the *FSA* as soon as practicable if its capital resources have fallen below the level suggested by that individual capital *guidance*. In such circumstances, the *FSA* may ask the *firm* for further explanation as to why it does not consider the individual capital *guidance* to be appropriate. The *FSA* may also consider using its powers under section 45 of the *Act* to, on its own initiative, vary a *firm's* Part IV *permission*, so as to require it to hold such capital as the *FSA* considers is necessary for the *firm* to comply with *PRU* 1.2.22R.
- 2.8 Ceasing to effect contracts of insurance
- 2.8.1 R If a *firm* decides to cease to *effect* new *contracts of insurance*, it must, within 28 days of that decision, submit a run-off plan to the *FSA* including:
- (1) a *scheme of operations*; and
  - (2) an explanation of how, or to what extent, all *liabilities to policyholders* (including, where relevant, liabilities which arise

from the regulatory duty to treat *customers* fairly in setting discretionary benefits) will be met in full as they fall due.

- 2.8.2 G *SUP* App 2.8.1R only applies if a *firm* ceases to *effect* new *contracts of insurance* in respect of the whole of its *insurance business*.
- 2.8.3 G For the purposes of *SUP* App 2.8.1R, a new *contract of insurance* excludes contracts effected under a term in a subsisting *contract of insurance*.
- 2.8.4 G Under *Principle 11*, the *FSA* normally expects to be notified by a *firm* when it decides to cease *effecting* new *contracts of insurance* in respect of one or more *classes of contract of insurance* (see *SUP* 15.3.8G). At the same time, the *FSA* would normally expect the *firm* to discuss with it the need for the *firm* to apply to vary its *permission* (see *SUP* 6.2.6G and *SUP* 6.2.7G) and, if appropriate, to submit a *scheme of operations* in accordance with *SUP* App 2.8.1R.
- 2.8.5 G See *SUP* App 2.11.2G for *guidance* on the period that the *scheme of operations* should cover.
- 2.9 Under control of a new parent undertaking
- 2.9.1 G A *firm* that has notified the *FSA* of a new *parent undertaking* may be requested to submit a *scheme of operations* (see *SUP* 11.5.5G). A *scheme of operations* would be requested if the significance and circumstances of the change were considered to be sufficient to merit that level of scrutiny. This is normally only likely to be necessary when there has been an ultimate change in *control*, or when, as a result of the change in *control*, significant changes are proposed to the *firm's regulated activities*, business plan or strategy. A *firm* which has submitted a *scheme of operations* under *SUP* 11.5.5G, is not required to submit a further *scheme of operations* under this appendix unless *SUP* App 2.4, 2.5 or 2.8 applies. *SUP* App 2.13 does, however, apply to such a *firm*.
- 2.10 Grant or variation of permission
- 2.10.1 G The *FSA* may ask a *firm* seeking a grant or variation of *permission* to provide a *scheme of operations* as part of the application process (see *AUTH* 3.9.9G(1) and *SUP* 6.3.25G). Such a *firm* is not required to submit a further *scheme of operations* under this appendix unless *SUP* App 2.4, 2.5 or 2.8 applies. *SUP* App 2.13 and *SUP* 6 Ann 4G do, however, apply to such a *firm*.
- 2.11 Submission of a scheme of operations or a plan for restoration
- 2.11.1 G A *firm* should discuss its plan in draft with the *FSA* before submitting it. If a plan is submitted which does not satisfy the *FSA* that the *firm* can restore its capital resources (as appropriate), or meet its liabilities

as they fall due, the *FSA* may use its *own-initiative power* to vary or cancel the *firm's permission*. If a *firm* submitting a plan is part of a *group of companies*, the *FSA* may ask that *firm* to provide additional information in relation to other *companies* in the *group*, if this is necessary to establish how the *firm* will restore its own sound financial position. The *firm* should agree in discussion with the *FSA* the nature of such additional information.

2.11.2 G The *schemes of operations* required when a *firm's* capital resources have fallen below its required margin of solvency or its guarantee fund (see *SUP App 2.5.1R* and *SUP App 2.4.1R*, respectively) should cover a period which is sufficient to demonstrate that the *firm's* capital resources will be adequately restored. Typically this would be a period of at least three years. However, if a *scheme of operations* has expired, but *SUP App 2.4.1R* or *2.5.1R* continues to apply, the *firm* should submit a new *scheme of operations*. The *scheme of operations* required by *SUP App 2.8.1R*, when a *firm* ceases to *effect new contracts of insurance*, should cover the run-off period until all *liabilities to policyholders* are met.

2.11.3 G The period to be covered by, and the details to be included in, the plan for restoration required by *SUP App 2.5.3R* will depend on the circumstances of the *firm*, why its capital resources have fallen below its required margin of solvency and the degree of risk that that fall will be repeated, even if the *firm* restores its capital resources in accordance with its plan.

2.11.4 G In relation to a *firm* which carries on *with-profits insurance business* and which submits a plan, the *FSA* would expect an explanation of how any actions it plans to take to restore capital resources to the level of the guarantee fund, required margin of solvency or *capital resources requirement* are consistent with the *firm's* obligations under *Principle 6* (Customers' interests).

2.12 Content of a scheme of operations

2.12.1 R A *scheme of operations* must:

- (1) describe the *firm's* business strategy;
- (2) include financial projections (including appropriate scenarios and stress-tests) as follows:
  - (a) a forecast summary profit and loss account in accordance with *SUP App 2.12.7R*;
  - (b) a forecast summary balance sheet in accordance with *SUP App 2.12.8R*; and
  - (c) a forecast statement of capital resources in accordance



with *SUP* App 2.12.9R; and

- (3) as at the end of each *financial year* which falls (in whole or part) within the period to which the *scheme of operations* relates:
- (a) describe the assumptions which underlie those forecasts and the reasons for adopting those assumptions; and
  - (b) identify any material transactions proposed to be effected or carried out with, or in respect of, any *associate*.
- 2.12.2 G The business strategy referred to at *SUP* App 2.12.1R(1) should include a description of the nature of the risks which the *firm* is underwriting, or intends to underwrite. It should also give an explanation of the *firm's* strategy for managing the risks associated with carrying on *insurance business* (including, in particular, *reinsurance*).
- 2.12.3 G The amount of detail to be given on the *firm's* business strategy required by *SUP* App 2.12.1R(1) should be appropriate to the scale and complexity of the *firm's* operations and the degree of risk involved.
- 2.12.4 R The information required by *SUP* App 2.12.1R must reflect the nature and content of the *rules* relating to capital resources applicable to a *firm*.
- 2.12.5 G In relation to *firms* covered by this appendix, *IPRU(FSOC)* 4.1 sets out the *rules* relating to capital resources for *non-directive friendly societies* and *PRU* 2.1, 2.2 and 8.3 set out the *rules* relating to capital resources for every other *firm*. The capital resources which a *firm* is required to maintain vary according to whether the *firm* has its head office in the *United Kingdom* or overseas, and depending on the nature of the *insurance business* it carries on. The information which a *firm* is required to submit under *SUP* App 2.12.1R should reflect the nature and content of the *rules* relating to capital resources identified above. For example, in order to satisfy *SUP* App 2.12.1R, a *firm* with its head office outside the *United Kingdom* which is carrying on direct *insurance business* in the *United Kingdom* should submit separate information concerning its world-wide activities and its *UK* activities.
- 2.12.6 G To reflect its obligations under *PRU* 2.1.10R or *IPRU(FSOC)* 4.1(2) (as applicable), in order to comply with *SUP* App 2.12.1R, a *firm* which carries on both *long-term insurance business* and *general insurance business* should submit separate information for each type of *insurance business*.
- 2.12.7 R Summary profit and loss account (see *SUP* App 2.12.1R(2)(a))

(1)	<i>Premiums and claims</i> (gross and net of <i>reinsurance</i> ) analysed by accounting <i>class of insurance business</i>
(2)	Investment return
(3)	Expenses
(4)	Other charges and income
(5)	Taxation
(6)	Dividends paid and accrued

2.12.8 R Summary balance sheet (see SUP App 2.12.1R(2)(b))

(1)	Investments analysed by type
(2)	Assets held to cover linked liabilities
(3)	Other assets and liabilities separately identifying cash at bank and in hand
(4)	Capital and reserves analysed into called up <i>share</i> capital or equivalent funds, <i>share</i> premium account, revaluation reserve, other reserves and profit and loss account
(5)	Subordinated liabilities
(6)	The fund for future appropriations
(7)	Technical provisions gross and net of <i>reinsurance</i> analysed by accounting <i>class of insurance business</i> and separately identifying the provision for linked liabilities, <i>unearned premiums</i> , unexpired risks and equalisation
(8)	Other liabilities and credits

2.12.9 R A forecast statement of capital resources (under SUP App 2.12.1R(2)(c)) must include the forecast capital resources and the forecast required margin of solvency at the end of each *financial year* or part *financial year*.

2.13 Obligations on firms which have previously submitted a scheme of operations

2.13.1 R A *firm* which has submitted a *scheme of operations* to the FSA, whether required by SUP App 2.4, 2.5 or 2.8, or as part of an application under SUP 6.3 (see SUP 6.3.25G), SUP 6.4 (see SUP 6 Ann 4G), AUTH 3.9 (see AUTH 3.9.9G(1)), or SUP 11.5 (see SUP 11.5.5G), or an amended *scheme of operations*, must during the period covered by that *scheme of operations*:

- (1) notify the FSA at least 28 days before entering into or carrying out any material transaction with, or in respect of, an *associate*, unless that transaction is in accordance with a *scheme of operations* which has been submitted to the FSA;

- (2) submit a quarterly financial return to the *FSA* which must include for, or as at the end of, each quarter:
  - (a) a summary profit and loss account prepared in accordance with *SUP* App 2.12.7R;
  - (b) a summary balance sheet prepared in accordance with *SUP* App 2.12.8R; and
  - (c) a statement of capital resources prepared in accordance with *SUP* App 2.12.9R;

and which must identify and explain differences between the actual results and the forecasts submitted in the *scheme of operations*; and

- (3) notify the *FSA* promptly of any matter which has either happened or is likely to happen and which represents a significant departure from the *scheme of operations*; the *firm* must either:
  - (a) explain the nature of the departure and the reasons for it and provide revised forecast financial information in the *scheme of operations* for its remaining term; or
  - (b) include an amended *scheme of operations* and explain the amendments and the reasons for them.

2.13.2 R A report under *SUP* App 2.13.1R(2) must be submitted in accordance with the *rules* in *SUP* 16.3.6R to *SUP* 16.3.13R.

2.13.3 G For the purpose of *SUP* App 2.13.1R(1), the *FSA* considers that transactions with, or in respect of, *associates* include:

- (1) contracting (as either party), advancing, repaying, writing off or agreeing to change the terms of any loan;
- (2) entering into (in any capacity), releasing, calling upon or agreeing to change the terms of any guarantee, pledge, security, charge or any off-balance-sheet transaction;
- (3) entering into agreements to acquire or dispose of property or which otherwise affect the nature or value of the *firm's* assets;
- (4) making an investment (directly or indirectly) in an *associate*;
- (5) entering into (as either party), commuting or agreeing to change the terms of, any contract of *reinsurance*; and

- (6) entering into, or changing the terms of, any agreement to give or provide services or to share costs.

2.13.4 G The *FSA* considers that a significant departure referred to in *SUP* App 2.13.1R(3) includes:

- (1) entry or withdrawal from a line of *insurance business*;
- (2) significant revision of the *firm's* strategy for managing risks, in particular the basis upon which risks are reinsured;
- (3) forecast *premiums* being exceeded, by more than 10%, for a single *financial year* (or part year if the period covered by the *scheme of operations* is or includes part of a *financial year*);
- (4) *claims* experience being significantly worse than forecast for a single *financial year* (or part year if the period covered by the *scheme of operations* is or includes part of a *financial year*);
- (5) the actual level of capital resources being significantly worse than forecast;
- (6) paid or proposed dividends being greater than those forecast; and
- (7) any other transaction or circumstance which is likely to have a material effect upon available assets (as defined in *IPRU(INS)* 11.1).

2.14 Financial Recovery Plan

2.14.1 G When:

- (1) the *FSA* has required a financial recovery plan within the meaning of article 20a of the *First Non-Life Directive*;
- (2) the *FSA* is of the view that *policyholders'* rights are threatened because the financial position of the *firm* is deteriorating; and
- (3) the *FSA* decides to require the *firm* to hold more capital than would otherwise be required under the *Handbook* to ensure that the *firm* will be able to fulfil the required margin of solvency in the near future;

any such higher capital requirement will be based on the financial recovery plan.

## Part 2: Other amendments to the Supervision manual

In this part, underlining indicates new text and striking through indicates deleted text.

4.5.13 R When carrying out his duties, an *actuary* appointed under this chapter must pay due regard to generally accepted actuarial ~~best~~ practice.

4.5.14 G The standards and guidance issued from time to time by the Institute of Actuaries and the Faculty of Actuaries are important sources of generally accepted actuarial ~~best~~ practice.

...

8.2.7 G Table Rules which can be waived (see *SUP* 8.2.6G)

Rules	Section of the Act or other provision under which rules are made	Chapters of the Handbook where such rules appear (Note 1)
...		
Insurance business rules	Section 141	<del>IPRU(INV)</del> <u>PRU</u>
...		

9.3.2 G The *FSA* may give individual *guidance* to a *firm* on its own initiative if it considers it appropriate to do so. For example:

...

(5) in relation to the maintenance of adequate financial resources, the *FSA* may give a *firm* individual *guidance* on the amount or type of financial resources the *FSA* considers appropriate, for example on individual capital ratios for *banks* and *building societies*; further *guidance* on how and when the *FSA* may give individual *guidance* on financial resources is contained in the Interim Prudential sourcebooks and in *PRU*:

...

(c) for a *securities and futures firm* (or other *firm* required to comply with *IPRU(INV)* 3 or *IPRU(INV)* 10): *IPRU(INV)* 10-74R and *IPRU(INV)* App 48-; and

(d) for an *insurer*: *PRU* 2.3.13G and *PRU* 2.3.14G.

...

10.12.3 G In accordance with section 60 of the *Act* (Applications for approval), applications must be submitted by, or on behalf of, the *firm* itself, not by the *candidate*. Usually this will be the *firm* that is employing the *candidate* to perform the *controlled function*. Where a *firm* has outsourced the performance of a *controlled function*, the details of the outsourcing determine where responsibility lies and whom the *FSA* anticipates will submit *approved persons* forms. *SUP* 10.12.4G describes some common situations. The *firm* which is outsourcing is referred to as "A" and the *person* to whom the performance of the function has been outsourced, or which makes the *arrangement* for the function to be performed, is referred to as "B". In each situation, A must take reasonable care to ensure that, in accordance with section 59(2) of the *Act*, no *person* performs a *controlled function* under an *arrangement* entered into by its contractor in relation to the carrying on by A of a *regulated activity*, without approval from the *FSA*. See also *SYSC* 3.2.4G and if applicable *IPRU(BANK)* OS<sub>2</sub> and *IPRU(BSOC)* OS<sub>2</sub> and for *insurers* *SYSC* 3A.9.

...

15.3.8 G Compliance with *Principle* 11 includes, but is not limited to, giving the *FSA* notice of:

- (1) any proposed restructuring, reorganisation or business expansion which could have a significant impact on the *firm's* risk profile or resources, including, but not limited to:

...

- (e) entering into, or significantly changing, a *material outsourcing* arrangement (a bank should also see *IPRU(BANK)* OS 4.2, and a building society should also see *IPRU(BSOC)* 4.2.11 OS 4.2, and an *insurer* should also see *SYSC* 3A.9 for further details); or

...

...

## Annex L

### Amendments to the Enforcement manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

...

- 13.6.3 G ~~*IPRU(INS) rule 3.5(3)*~~ *PRU 7.6.33R* prohibits a *long-term insurer* (including a *firm* qualifying for authorisation under Schedule 3 or 4 to the *Act*), which is not a mutual, from paying a financial penalty from a long-term insurance fund.

## Annex M

### Amendments to the Credit Unions sourcebook

In this Annex, underlining indicates new text.

#### Appendix 1

##### 1.1.1 Table

...		
Business Standards	5 Interim Prudential sourcebooks	<i>IPRU</i>
	<u>Integrated Prudential Sourcebook</u>	<u><i>PRU</i></u>
	...	
...		



## Annex N

### Amendments to the Electronic Money sourcebook

In this Annex, underlining indicates new text.

1.5.2 G Application of other parts of the *Handbook* to *ELMIs*

...

Block	Module	Application
...		
Block 2 (Business Standards)	Interim Prudential sourcebooks: <i>IPRU(INS)</i> , <i>IPRU(FSOC)</i> , <i>IPRU(BANK)</i> , <i>IPRU(BSOC)</i> and <i>IPRU(INV)</i> <u>Integrated Prudential Sourcebook (PRU)</u>	<i>ELM 7</i> (Consolidated financial supervision) applies <i>IPRU(BANK)</i> , <i>IPRU(BSOC)</i> and <i>IPRU(INV)</i> to certain <i>ELMIs</i> who are members of a <i>group</i> . Chapter NE of <i>IPRU(BANK)</i> is relevant to <i>ELM 3.5.16R</i> , as described in <i>ELM 3.5.20G</i> . Otherwise, these sourcebooks do not apply to <i>ELMIs</i> .
...		

## Annex O

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text. Where new definitions are being inserted, the text is not underlined.

#### Part 1: New definitions

Insert the following new definitions in the appropriate alphabetical position:

<i>accumulating with-profits policy</i>	a <i>with-profits insurance contract</i> which has a readily identifiable current benefit, whether or not this benefit is currently realisable, which is adjusted by an amount explicitly related to the amount of any <i>premium</i> payment and to which additional benefits are added in respect of participation in profits by additions directly related to the current benefit or a <i>policy</i> with similar characteristics.
<i>actuarial investigation</i>	an investigation to which <i>IPRU(INS)</i> rule 9.4 applies.
<i>actuarial valuation date</i>	(in <i>PRU</i> ) the date as at which the <i>mathematical reserves</i> are calculated.
<i>administrative expenses</i>	has the meaning set out in the <i>insurance accounts rules</i> .
<i>ancillary risk</i>	(in relation to an <i>insurer</i> with <i>permission</i> under the <i>Act</i> to insure a principal risk belonging to one <i>class</i> (as defined for the purposes of <i>AUTH, PRU, LLD</i> and <i>SUP</i> ) of <i>general insurance business</i> ) a risk included in another such <i>class</i> which is:  (a) connected with the principal risk, (b) concerned with the object which is covered against the principal risk, and (c) the subject of the same contract insuring the principal risk.  However, the risks included in <i>classes</i> 14, 15 and 17 may not be treated as risks ancillary to other <i>classes</i> , except that the risk included in <i>class</i> 17 (legal expenses insurance) may be regarded as an ancillary risk of <i>class</i> 18 where:  (d) the conditions laid down in (a) to (c) are fulfilled, and (e) the principal risk relates solely to assistance provided for <i>persons</i> who fall into difficulties while travelling, while away from home or while away from their permanent residence or where it concerns disputes or risks arising out of, or in connection with, the use of sea-going vessels.
<i>ancillary services undertaking</i>	an <i>ancillary insurance services undertaking</i> , an <i>ancillary banking services undertaking</i> or an <i>ancillary investment services undertaking</i> .
<i>Annual Accounts</i>	the Council Directive of 19 December 1991 concerning the annual

<i>Directive</i>	accounts and consolidated accounts of <i>insurance undertakings</i> (No. 91/674/EEC).
<i>annual bonus</i>	(in relation to a <i>with-profits insurance contract</i> ) a discretionary addition to <i>policy</i> benefits under a <i>with-profits insurance contract</i> made by a <i>long-term insurer</i> as a result of the annual <i>actuarial investigation</i> .
<i>annualised net written premiums</i>	(for the purposes of <i>PRU 7.5</i> ) in relation to a <i>financial year</i> , the <i>net written premiums</i> received during that <i>financial year</i> , except that in relation to a <i>financial year</i> that has been validly extended beyond, or shortened from, a period of 12 months, the amount of <i>net written premiums</i> is the amount determined in accordance with the formula: <div style="text-align: center; margin: 10px 0;"> <math display="block">\frac{NWP \times 365}{D}</math> </div> <p style="text-align: center;">D</p> <p>where:</p> <p>(1) NWP is the amount of <i>net written premiums</i> received in the <i>financial year</i>; and</p> <p>(2) D is the number of days in that <i>financial year</i>.</p>
<i>approved quasi-derivative</i>	a <i>quasi-derivative</i> in respect of which the conditions in <i>PRU 4.3.5R</i> are met.
<i>approved stock lending transaction</i>	a <i>stock lending</i> transaction in respect of which the conditions in <i>PRU 4.3.36R</i> have been met.
<i>assessable mutual</i>	(for the purposes of <i>PRU 7.5</i> ) a <i>mutual</i> where the <i>insurance business</i> carried on by the <i>mutual</i> is limited to the provision of <i>insurance business</i> to its members and whose articles of association, rules or by-laws provide for the calling of additional contributions from members to meet <i>claims</i> .
<i>asset-related capital requirement</i>	a component of the calculation of the <i>ECR</i> for a <i>firm</i> carrying on <i>general insurance business</i> as set out in <i>PRU 3.3</i> .
<i>base capital resources requirement</i>	an amount of <i>capital resources</i> that a <i>firm</i> must hold as set out in <i>PRU 2.1.26R</i> .
<i>basis risk</i>	the risk that the relationship between two financial variables will change, particularly between two sorts of interest rate or between a hedge and the position it ostensibly hedges.
<i>brought forward amount</i>	an amount, as defined in <i>PRU 7.2.51R</i> , used in the calculation of the <i>general insurance capital requirement</i> .
<i>capital resources</i>	in relation to a <i>firm</i> , the <i>firm's</i> capital resources as calculated in accordance with <i>PRU 2.2.12R</i> .
<i>capital resources requirement</i>	an amount of <i>capital resources</i> that a <i>firm</i> must hold as set out in <i>PRU 2.1.14R</i> to <i>PRU 2.1.20R</i> .

<i>claims amount</i>	an amount, as defined in <i>PRU 7.2.47R</i> , used in the calculation of the <i>general insurance capital requirement</i> .
<i>commitment</i>	a commitment represented by <i>insurance business</i> of any of the <i>classes</i> (as defined for the purposes of <i>AUTH, PRU, LLD</i> and <i>SUP</i> ) of <i>long-term insurance business</i> .
<i>compensation fund</i>	any <i>policyholder</i> compensation scheme in any <i>EEA State</i> .
<i>composite firm</i>	a <i>firm</i> that carries on both <i>long-term insurance business</i> and <i>general insurance business</i> .
<i>contingency funding plan</i>	a plan for taking action to ensure that a <i>firm</i> has adequately liquid financial resources to meet its liabilities as they fall due, prepared under <i>PRU 5.1.86E</i> .
<i>core tier one capital</i>	an item of capital that is stated in stage A of the table in <i>PRU 2.2.14R</i> to be core tier one capital.
<i>coupon</i>	a dividend, interest payment or any similar payment.
<i>credit equalisation provision</i>	the provision required to be established by <i>PRU 7.5.43R</i> .
<i>CRR</i>	<i>capital resources requirement</i> .
<i>deposit back arrangement</i>	(in relation to any contract of <i>reinsurance</i> ) an arrangement whereby an amount is deposited by the <i>reinsurer</i> with the cedant.
<i>ECR</i>	<i>enhanced capital requirement</i> .
<i>EEA-deposit insurer</i>	a <i>non-EEA insurer</i> that has made a deposit in an <i>EEA State</i> (other than the <i>United Kingdom</i> ) under article 23 of the <i>First Non-Life Directive</i> (as amended) in accordance with article 26 of that Directive or under article 51 of the <i>Consolidated Life Directive</i> in accordance with article 56 of that Directive.
<i>EEA insurance parent undertaking</i>	an <i>insurance parent undertaking</i> that has its head office in the <i>United Kingdom</i> or another <i>EEA State</i> .
<i>EEA MCR</i>	the <i>MCR</i> in relation to business carried on in all <i>EEA States</i> , taken together, calculated by a <i>UK-deposit insurer</i> in accordance with <i>PRU 7.6.46R</i> .
<i>enhanced capital requirement</i>	<ol style="list-style-type: none"> <li>(1) (in relation to a <i>firm</i> carrying on <i>general insurance business</i>) the amount calculated in accordance with <i>PRU 2.3.11R</i>.</li> <li>(2) (in relation to a <i>firm</i> carrying on <i>long-term insurance business</i>) an amount of <i>capital resources</i> that a <i>firm</i> must hold as set out in <i>PRU 2.1.34R</i>.</li> </ol>
<i>equalisation provision</i>	a provision required to be established under the <i>rules</i> in <i>PRU 7.5</i> .

<i>equity market adjustment ratio</i>	<p>(1) (in relation to the <i>resilience capital requirement</i>) has the meaning set out in <i>PRU 4.2.19R</i>.</p> <p>(2) (in relation to the <i>market risk</i> scenario for the <i>risk capital margin</i> of a <i>with-profits fund</i>) has the meaning set out in <i>PRU 7.4.71R</i>.</p>
<i>final bonus</i>	(in relation to a <i>with-profits insurance contract</i> ) a discretionary payment which might be made by a <i>long-term insurer</i> , in addition to the guaranteed benefits, when the benefits under the <i>with-profits insurance contract</i> become payable.
<i>financial instrument</i>	<p>as defined in Annex B of the <i>Investment Services Directive</i>, the following instruments:</p> <ul style="list-style-type: none"> <li>(a) (i) transferable securities;</li> <li style="padding-left: 2em;">(ii) units in collective investment undertakings;</li> <li>(b) money-market instruments;</li> <li>(c) financial futures contracts, including equivalent cash-settled instruments;</li> <li>(d) forward interest rate agreements (FRAs);</li> <li>(e) interest rate, currency and equity swaps; and</li> <li>(f) options to acquire or dispose of any of the instruments in (a) to (e), including equivalent cash-settled instruments (including in particular options on currency and options on interest rates).</li> </ul>
<i>financial year in question</i>	(for the purposes of <i>PRU 7.2</i> and of the definition of <i>non-directive insurer</i> ) the last <i>financial year</i> to end before the date on which the latest accounts of the <i>insurer</i> are required to be deposited with the <i>FSA</i> ; the preceding <i>financial year</i> and previous <i>financial years</i> are construed accordingly.
<i>financing cost amount</i>	(in relation to a <i>share</i> , <i>debenture</i> or other investment in, or external contribution to the capital of, a <i>firm</i> ) an amount that represents a reasonable estimate of the part of the <i>coupon</i> on that instrument that reflects the cost of financing generally but excludes costs reflecting factors relating to the issuer, guarantor or other person to whom the instrument creates an exposure.
<i>firm in run-off</i>	a <i>firm</i> whose <i>Part IV permission</i> has been varied so as to remove the <i>regulated activity</i> of <i>effecting contracts of insurance</i> .
<i>future policy-related liabilities</i>	(in relation to a <i>with-profits fund</i> ) the future <i>policy-related liabilities</i> of the <i>with-profits fund</i> calculated in accordance with the <i>rules</i> in <i>PRU 7.4.137R</i> to <i>PRU 7.4.189G</i> .
<i>GCR</i>	<i>group capital resources</i> .

<i>GCCR</i>	<i>group capital resources requirement.</i>
<i>general insurance capital requirement</i>	the highest of the <i>premiums amount</i> , <i>claims amount</i> and <i>brought forward amount</i> as set out in <i>PRU 7.2</i> .
<i>general insurance liabilities</i>	insurance liabilities arising from <i>general insurance business</i> .
<i>GICR</i>	<i>general insurance capital requirement.</i>
<i>gross adjusted claims amount</i>	(for the purposes of <i>PRU 7.2</i> ) an amount, as defined in <i>PRU 7.2.60R</i> to <i>PRU 7.2.65G</i> , used in calculating the <i>claims amount</i> .
<i>gross adjusted premiums amount</i>	(for the purposes of <i>PRU 7.2</i> ) an amount as defined in <i>PRU 7.2.56R</i> to <i>PRU 7.2.59G</i> , used in calculating the <i>premiums amount</i> .
<i>gross earned premiums</i>	(in relation to a <i>financial year</i> ) such proportion of <i>gross written premiums</i> as is attributable to risk borne by the <i>insurer</i> during that <i>financial year</i> .
<i>gross leverage</i>	the ratio of total assets to total equity.
<i>gross written premiums</i>	the amounts required by the <i>insurance accounts rules</i> to be shown in the profit and loss account of an <i>insurer</i> at general business technical account item I.1.(a), or for <i>class IV insurance business</i> , at long-term business technical account item II.1(a).
<i>group capital resources</i>	in relation to an <i>undertaking</i> in <i>PRU 8.3.17R</i> , that <i>undertaking's</i> group capital resources as calculated in accordance with <i>PRU 8.3.36R</i> .
<i>group capital resources requirement</i>	in relation to an <i>undertaking</i> in <i>PRU 8.3.17R</i> , that <i>undertaking's</i> group capital resources requirement as calculated in accordance with <i>PRU 8.3.33R</i> .
<i>IBNR</i>	(in relation to <i>claims</i> (as defined for the purposes of <i>PRU</i> , <i>LLD</i> , <i>SUP</i> and <i>TC</i> )) <i>claims</i> that have been incurred but not reported arising out of events that have occurred by the balance sheet date but have not been reported to the <i>insurance undertaking</i> at that date.
<i>implicit items</i>	(in relation to <i>long-term insurance business</i> ) economic reserves arising in respect of future profits, <i>zillmerising</i> or hidden reserves as more fully described in <i>PRU 2 Ann 2G</i> .
<i>index-linked benefits</i>	benefits: <ul style="list-style-type: none"> <li>(a) provided for under a <i>linked long-term contract of insurance</i>; and</li> <li>(b) determined by reference to an index of the value of property of any description (whether specified in the contract or not).</li> </ul>
<i>index-linked liabilities</i>	insurance liabilities in respect of <i>index-linked benefits</i> .

<i>individual capital resources requirement</i>	has the meaning in <i>PRU 8.3.34R</i> .
<i>initial coupon rate</i>	(in relation to a <i>tier one instrument</i> ) the <i>coupon rate</i> of the instrument at the time it is issued.
<i>initial credit spread</i>	(in relation to a <i>tier one instrument</i> ) the <i>initial coupon rate</i> less the <i>original financing cost amount</i> , and where the resulting amount is a negative figure, the initial credit spread is deemed to be zero.
<i>initial fund</i>	the items of capital which are available to a <i>mutual</i> at <i>authorisation</i> .
<i>innovative tier one capital</i>	an item of capital that is stated in stage C of the table in <i>PRU 2.2.14R</i> to be innovative tier one capital.
<i>innovative tier one capital resources</i>	the amount of <i>capital resources</i> at stage C of the table in <i>PRU 2.2.14R</i> .
<i>innovative tier one instrument</i>	a <i>potential tier one instrument</i> that is stated in <i>PRU 2.2.52R</i> to <i>PRU 2.2.69R</i> to be an innovative instrument.
<i>insurance business grouping</i>	a grouping comprising descriptions of <i>general insurance business</i> determined in accordance with <i>PRU 7.5.12R</i> .
<i>insurance death risk capital component</i>	one of the components of the <i>long-term insurance capital requirement</i> as set out in <i>PRU 7.2.81R</i> to <i>PRU 7.2.83R</i> .
<i>insurance expense risk capital component</i>	one of the components of the <i>long-term insurance capital requirement</i> as set out in <i>PRU 7.2.88R</i> .
<i>insurance group</i>	<p>(1) an <i>insurance parent undertaking</i> and its <i>related undertakings</i>; or</p> <p>(2) a <i>participating insurance undertaking</i> (not within (1)) and its <i>related undertakings</i>.</p>
<i>insurance health risk capital component</i>	one of the components of the <i>long-term insurance capital requirement</i> as set out in <i>PRU 7.2.85R</i> and <i>PRU 7.2.86R</i> .
<i>insurance market risk capital component</i>	one of the components of the <i>long-term insurance capital requirement</i> as set out in <i>PRU 7.2.89R</i> .
<i>insurance parent undertaking</i>	<p>a <i>parent undertaking</i> which is:</p> <p>(a) a <i>participating insurance undertaking</i> which has a <i>subsidiary undertaking</i> that is an <i>insurance undertaking</i>; or</p> <p>(b) an <i>insurance holding company</i> which has a <i>subsidiary undertaking</i> which is an <i>insurer</i>; or</p> <p>(c) an <i>insurance undertaking</i> (not within (a)) which has a <i>subsidiary undertaking</i> which is an <i>insurer</i>.</p>
<i>insurance-related capital</i>	a component of the calculation of the <i>ECR</i> for a <i>firm</i> carrying on

<i>requirement</i>	<i>general insurance business</i> as set out in <i>PRU 7.2.76R</i> to <i>PRU 7.2.79R</i> .
<i>liquidity risk</i>	the risk that a <i>firm</i> , although solvent, either does not have available sufficient financial resources to enable it to meet its obligations as they fall due, or can secure such resources only at excessive cost.
<i>long-term admissible asset</i>	a <i>long-term insurance asset</i> which is an <i>admissible asset</i> .
<i>long-term insurance asset</i>	has the meaning set out in <i>PRU 7.6.21R</i> .
<i>long-term insurance capital requirement</i>	(in relation to a <i>firm</i> carrying on <i>long-term insurance business</i> ) an amount of <i>capital resources</i> that the <i>firm</i> must hold calculated in accordance with <i>PRU 2.1.32R</i> .
<i>long-term insurance fund</i>	has the meaning set out in <i>PRU 7.6.22R</i> .
<i>long-term insurance liabilities</i>	insurance liabilities arising from <i>long-term insurance business</i> .
<i>lower tier two capital resources</i>	the sum calculated at stage H of the calculation in <i>PRU 2.2.14R</i> .
<i>lower tier two instrument</i>	an item of capital that meets the conditions in <i>PRU 2.2.108R</i> and is eligible to form part of a <i>firm's lower tier two capital resources</i> .
<i>LTICR</i>	<i>long-term insurance capital requirement</i> .
<i>market risk</i>	(in relation to a <i>firm</i> ) the risks that arise from fluctuations in values of, or income from, assets or in interest or exchange rates.
<i>MCR</i>	<i>minimum capital requirement</i> .
<i>member contribution</i>	any paid up contribution by a member of a <i>mutual</i> where the members' accounts meet the following criteria: <ul style="list-style-type: none"> <li>(a) the memorandum and articles of association or other constitutional documents must stipulate that payments may be made from these accounts to members only in so far as this does not cause the <i>firm's capital resources</i> to fall below the required level, or, if after dissolution of the <i>firm</i>, all the <i>firm's</i> other debts have been settled;</li> <li>(b) the memorandum and articles of association or other constitutional documents must stipulate, with respect to the payments referred to in (a) made for reasons other than the individual termination of membership, that the <i>FSA</i> must be notified at least one month in advance of the intended date of such payments; and</li> <li>(c) the <i>FSA</i> must be notified of any amendment to the relevant provisions of the memorandum and articles of association or other constitutional documents.</li> </ul>



<i>minimum capital requirement</i>	an amount of <i>capital resources</i> that a <i>firm</i> must hold as set out in <i>PRU 2.1.21R</i> and <i>PRU 2.1.22R</i> .
<i>mutual</i>	an <i>insurer</i> which: <ul style="list-style-type: none"> <li>(a) if it is a <i>body corporate</i> has no <i>share</i> capital (except a wholly owned <i>subsidiary</i> with no <i>share</i> capital but limited by guarantee); or</li> <li>(b) is a <i>registered friendly society</i> or <i>incorporated friendly society</i>; or</li> <li>(c) is a society registered or deemed to be registered under the Industrial and Provident Societies Act 1965 or the Industrial and Provident Societies (Northern Ireland) Act 1969.</li> </ul>
<i>net earned premiums</i>	<i>gross earned premiums</i> , less <i>reinsurance premiums</i> earned.
<i>net leverage</i>	the ratio of total assets, less those bought under reverse <i>repo</i> arrangements, to total equity.
<i>net premium</i>	the <i>premium</i> that is calculated to provide the basic sum assured under a <i>with-profits insurance contract</i> taking into consideration only the mortality and interest rate risks and using the same assumptions as used in the calculation of the <i>mathematical reserves</i> .
<i>netting</i>	a process by which the claims and obligations between two counterparties are offset against each other to leave a single net sum.
<i>net written premiums</i>	<i>gross written premiums</i> , less <i>reinsurance premiums</i> payable under <i>reinsurance ceded</i> .
<i>non-credit equalisation provision</i>	the provision required to be established under <i>PRU 7.5.17R</i> .
<i>non-directive mutual</i>	a <i>mutual</i> that falls into (d), (e) or (g) of the definition of a <i>non-directive insurer</i> .
<i>non-EEA direct insurer</i>	an <i>insurer</i> , other than a <i>pure reinsurer</i> , whose head office is not in an <i>EEA State</i> .
<i>non-EEA insurer</i>	an <i>insurer</i> whose head office is not in an <i>EEA State</i> .
<i>non-profit fund</i>	a <i>long-term insurance fund</i> which is not a <i>with-profits fund</i> .
<i>non-profit insurance business</i>	the business of <i>effecting</i> or <i>carrying out non-profit insurance contracts</i> .
<i>non-profit insurance contract</i>	a <i>long-term insurance contract</i> which is not a <i>with-profits insurance contract</i> .
<i>non-proportional</i>	see <i>proportional reinsurance treaty</i> .

<i>reinsurance treaty</i>	
<i>nuclear risks</i>	risks falling within any <i>class</i> of <i>general insurance business</i> and arising in connection with the construction and use of any nuclear reactor or nuclear installation or the carriage of any nuclear matter.
<i>original financing cost amount</i>	(in relation to a <i>share</i> , <i>debenture</i> or other investment in, or external contribution to the capital of, a <i>firm</i> that is subject to a <i>step-up</i> ) the <i>financing cost amount</i> for the instrument for a period beginning on or near the date of issue of the instrument and ending on or near the date of the first <i>step-up</i> .
<i>participating insurance undertaking</i>	an <i>insurer</i> which: <ul style="list-style-type: none"> <li>(a) has a <i>subsidiary undertaking</i> that is an <i>insurance undertaking</i>; or</li> <li>(b) holds a <i>participation</i> in an <i>insurance undertaking</i>; or</li> <li>(c) is linked to an <i>insurance undertaking</i> by a <i>consolidation Article 12(1) relationship</i>.</li> </ul>
<i>permanent share capital</i>	an item of capital that is stated in <i>PRU 2.2.36R</i> to be permanent share capital.
<i>potential tier one instrument</i>	an item of capital that falls into <i>PRU 2.2.27R</i> .
<i>preference share</i>	(in <i>PRU</i> ) a <i>share</i> with rights, in respect of capital or dividends, superior to those of ordinary <i>shares</i> .
<i>premiums amount</i>	(for the purposes of <i>PRU 7.2</i> ), an amount, as defined in <i>PRU 7.2.45R</i> , used in the calculation of the <i>general insurance capital requirement</i> .
<i>property-linked benefits</i>	benefits other than <i>index-linked benefits</i> provided for under a <i>linked long-term contract of insurance</i> .
<i>property-linked liabilities</i>	insurance liabilities in respect of <i>property-linked benefits</i> .
<i>proportional reinsurance treaty</i>	a <i>reinsurance treaty</i> under which a pre-determined proportion of each <i>claim</i> payment by the cedant under <i>policies</i> subject to the treaty is recoverable from the <i>reinsurer</i> ;
	<i>non-proportional reinsurance treaty</i> is construed accordingly.
<i>proxy capital resources requirement</i>	the <i>minimum capital requirement</i> to which an <i>undertaking</i> would have been subject if it had <i>permission</i> for each activity it carries on anywhere in the world, so far as that activity is a <i>regulated activity</i> .
<i>real estate market adjustment ratio</i>	has the meaning set out, in relation to the <i>resilience capital requirement</i> , in <i>PRU 4.2.21R</i> .
<i>realistic basis life firm</i>	a <i>firm</i> to which <i>PRU 2.1.15R</i> applies (and which is therefore required to calculate a <i>with-profits insurance capital component</i> in accordance with <i>PRU 7.4</i> ).

<i>realistic current liabilities</i>	(in relation to a <i>with-profits fund</i> ) the realistic current liabilities of the <i>with-profits fund</i> calculated in accordance with <i>PRU 7.4.190R</i> .
<i>realistic excess capital</i>	(in relation to a <i>with-profits fund</i> ) the excess, if any, of the <i>realistic value of assets</i> for the <i>with-profits fund</i> over the sum of the <i>realistic value of liabilities</i> and the <i>risk capital margin</i> for that fund, calculated in accordance with <i>PRU 7.4.32R</i> .
<i>realistic value of assets</i>	(in relation to a <i>with-profits fund</i> ) has the meaning set out in <i>PRU 7.4.33R</i> .
<i>realistic value of liabilities</i>	(in relation to a <i>with-profits fund</i> ) the sum of the <i>with-profits benefit reserve</i> , the <i>future policy related liabilities</i> and the <i>realistic current liabilities</i> for the <i>with-profits fund</i> .
<i>regulated related undertaking</i>	a <i>related undertaking</i> that is any of the following: <ul style="list-style-type: none"> <li>(a) a <i>regulated entity</i>; or</li> <li>(b) an <i>insurance undertaking</i> which is not a <i>regulated insurance entity</i>; or</li> <li>(c) an <i>asset management company</i>; or</li> <li>(d) a <i>financial institution</i> which is neither a <i>credit institution</i> nor an <i>investment firm</i>; or</li> <li>(e) a <i>financial holding company</i>; or</li> <li>(f) an <i>insurance holding company</i>.</li> </ul>
<i>regulatory basis only life firm</i>	a <i>firm</i> carrying on <i>long-term insurance business</i> which is not a <i>realistic basis life firm</i> .
<i>regulatory current liabilities</i>	(in relation to a <i>with-profits fund</i> ) the regulatory current liabilities of the <i>with-profits fund</i> calculated in accordance with <i>PRU 7.4.30R</i> .
<i>regulatory excess capital</i>	(in relation to a <i>with-profits fund</i> ) has the meaning set out in <i>PRU 7.4.23R</i> .
<i>regulatory surplus value</i>	has the meaning set out in <i>PRU 1.3.36R</i> .
<i>regulatory value of assets</i>	(in relation to a <i>with-profits fund</i> ) has the meaning set out in <i>PRU 7.4.24R</i> .
<i>regulatory value of liabilities</i>	(in relation to a <i>with-profits fund</i> ) has the meaning set out in <i>PRU 7.4.29R</i> .
<i>reinsurance</i>	includes retrocession.
<i>reinsurer</i>	an <i>insurer</i> whose business includes effecting or carrying out contracts of <i>reinsurance</i> ; includes a retrocessionnaire.
<i>related undertaking</i>	in relation to an <i>undertaking</i> ("U"): <ul style="list-style-type: none"> <li>(a) any <i>subsidiary undertaking</i> of U; or</li> <li>(b) any <i>undertaking</i> in which U or any of U's <i>subsidiary</i></li> </ul>

- (c) *undertakings* holds a *participation*; or any *undertaking* linked to U by a *consolidation Article 12(1) relationship*; or
- (d) any *undertaking* linked by a *consolidation Article 12(1) relationship* to an *undertaking* in (a), (b) or (c).

*relevant capital sum* for the purposes of PRU 7.3.43R, the sum under a *contract of insurance* which is:

- (a) unless (b) applies:
    - (i) for whole life assurances, the sum assured;
    - (ii) for *contracts of insurance* where a sum is payable on maturity (including contracts where a sum is also payable on earlier death), the sum payable on maturity;
    - (iii) for deferred annuities, the capitalised value of the annuity at the vesting date (or the cash option if it is greater);
    - (iv) for *capital redemption* contracts, the sum payable at the end of the contract period; and
    - (v) for *linked long-term contracts of insurance*, notwithstanding (i) to (iv), the lesser of:
      - (A) the amount for the time being payable on death; and
      - (B) the aggregate of the value for the time being of the units allocated to the contract (or, where entitlement is not denoted by means of units, the value for the time being of any other measure of entitlement under the contract equivalent to units) and the total amount of the *premiums* remaining to be paid during such of the term of the contract as is appropriate for *zillmerising* or, if such *premiums* are payable beyond the age of seventy-five, until that age;
- but excluding in all cases any vested reversionary bonus; and
- (b) for temporary assurances, the sum assured on the *actuarial valuation date*.

*relevant insurer* in relation to a *community co-insurance operation*, an *insurer* which is concerned in the operation but is not the *leading insurer*.

*resilience capital requirement* the capital component for *long-term insurance business* calculated in accordance with the *rules* in PRU 4.2.9G to PRU 4.2.26R.

*return* the documents required (taken together) to be deposited under *IPRU(INS) rule 9.6(1)*.

<i>risk capital margin</i>	the risk capital margin for a <i>with-profits fund</i> calculated in accordance with the <i>rules</i> in <i>PRU 7.4.43R</i> to <i>PRU 7.4.103G</i> .
<i>Solvency I Directive</i>	the Directive of the European Parliament and of the Council of 5 March 2002 amending Council Directive 79/267/EEC as regards the solvency margin requirements for life assurance undertakings (No. 2002/12/EC).
<i>specific risk</i>	unique risk that is due to the individual nature of an asset and can potentially be diversified.
<i>spread risk</i>	the risk that a spread (that is, the difference in price or yield) between two variables will change.
<i>step-up</i>	(1) (in relation to a <i>tier one instrument</i> ) has the meaning set out in <i>PRU 2.2.74R</i> ; and (2) (in relation to a <i>tier two instrument</i> ) has the meaning set out in <i>PRU 2.2.118R</i> .
<i>Swiss general insurer</i>	a <i>Swiss general insurance company</i> which has <i>permission</i> to <i>effect</i> or <i>carry out contracts of insurance</i> of a kind which is subject to the <i>Swiss Treaty Agreement</i> .
<i>tier one capital resources</i>	the sum calculated at stage F of the calculation in <i>PRU 2.2.14R</i> .
<i>tier one instrument</i>	an item of capital that falls into <i>PRU 2.2.27R</i> and is eligible to form part of a <i>firm's tier one capital resources</i> .
<i>tier two instrument</i>	an item of capital that meets the conditions in <i>PRU 2.2.101R</i> or <i>PRU 2.2.108R</i> and is eligible to form part of a <i>firm's tier two capital resources</i> .
<i>tier two capital resources</i>	the sum calculated at stage I of the calculation in <i>PRU 2.2.14R</i> .
<i>total group tier one capital</i>	the sum calculated at stage A of the calculation in <i>PRU 8.3.43R</i> .
<i>total group tier two capital</i>	the sum calculated at stage B of the calculation in <i>PRU 8.3.43R</i> .
<i>UK MCR</i>	the <i>MCR</i> calculated in accordance with <i>PRU 7.6.44R</i> by a <i>non-EEA direct insurer</i> (except a <i>UK-deposit insurer</i> , an <i>EEA-deposit insurer</i> or a <i>Swiss general insurer</i> ) in relation to business carried on by the <i>firm</i> in the <i>United Kingdom</i> .
<i>ultimate EEA insurance parent undertaking</i>	an <i>EEA insurance parent undertaking</i> that is not itself the <i>subsidiary undertaking</i> of another <i>EEA insurance parent undertaking</i> .
<i>ultimate insurance parent undertaking</i>	an <i>insurance parent undertaking</i> that is not itself the <i>subsidiary undertaking</i> of another <i>insurance parent undertaking</i> .

<i>unearned premium</i>	the amount set aside by a <i>firm</i> at the end of its <i>financial year</i> out of <i>premiums</i> in respect of risks to be borne by the <i>firm</i> after the end of the <i>financial year</i> under <i>contracts of insurance</i> entered into before the end of that year.
<i>unpaid initial fund</i>	part of the <i>initial fund</i> of a <i>mutual</i> which the <i>mutual</i> is prevented from including in its <i>tier one capital resources</i> as <i>permanent share capital</i> by reason of <i>PRU 2.2.29R</i> because it is not fully paid.
<i>unsecured debt</i>	debt that does not fall within the definition of <i>secured debt</i> .
<i>upper tier two capital resources</i>	the sum calculated at stage G of the calculation in <i>PRU 2.2.14R</i> .
<i>upper tier two instrument</i>	an item of capital that meets the conditions in <i>PRU 2.2.101R</i> and is eligible to form part of a <i>firm's upper tier two capital resources</i> .
<i>volatility risk</i>	the potential loss due to fluctuations in implied <i>option</i> volatilities.
<i>with-profits benefits reserve</i>	(in relation to a <i>with-profits fund</i> ) the with-profits benefits reserve for the <i>with-profits fund</i> calculated in accordance with the <i>rules</i> in <i>PRU 7.4.116R</i> to <i>PRU 7.4.135G</i> .
<i>with-profits insurance business</i>	the business of <i>effecting</i> or <i>carrying out with-profits insurance contracts</i> .
<i>with-profits insurance capital component</i>	the capital component for <i>with-profits insurance business</i> of a <i>realistic basis life firm</i> calculated in accordance with <i>PRU 7.4</i> .
<i>with-profits insurance contract</i>	a <i>long-term insurance contract</i> which provides for the <i>policyholder</i> to be eligible to participate in any surplus arising on the whole of, or any part of, the <i>insurer's long-term insurance business</i> .
<i>with-profits insurance liabilities</i>	insurance liabilities arising from <i>with-profits insurance business</i> .
<i>WPICC</i>	<i>with-profits insurance capital component</i> .
<i>zillmerising</i>	the method known by that name for modifying the <i>net premium</i> reserve method of valuing a <i>long-term insurance contract</i> by increasing the part of the future <i>premiums</i> for which credit is taken so as to allow for initial expenses.

## Part 2: Amended definitions

Amend the following definitions as shown:

<i>actuarial health insurance</i>	(1)	<u>(in LLD) ...</u>
	(2)	<u>(in PRU) (in the context of the rules in PRU 7.2 concerning the calculation of the general insurance capital requirement), health insurance which meets all the conditions set out in PRU 7.2.72R.</u>
<i>admissible asset</i>	(1)	<u>(in LLD) ...</u>
	(2)	<u>(in PRU) an asset that falls into one or more categories in PRU 2 Ann 1R.</u>
<i>approved counterparty</i>		<del>an approved counterparty as defined in IPRU(INS).</del> <u>any of the following:</u> (a) <u>an approved credit institution; or</u> (b) <u>a firm whose permission includes dealing in investments as principal with respect to derivatives which are not listed; or</u> (c) <u>an ISD investment firm whose authorisation (as referred to in article 3 of the ISD) authorises it to carry on activities of the kind referred to in (b); or</u> (d) <u>in respect of a transaction involving a new issue of securities which are to be listed, the issuer or an ISD investment firm acting on behalf of the issuer.</u>
<i>approved credit institution</i>		<del>an approved credit institution as defined in IPRU(INS).</del> <u>an institution recognised or permitted under the law of an EEA State to carry on any of the activities set out in Annex 1 to the Banking Consolidation Directive.</u>
<i>approved derivative</i>	(1)	<del>(in COLL and CIS COLL and CIS) ...</del>
	(2)	<u>(in PRU) a derivative in respect of which the conditions in PRU 4.3.5R are met.</u>
<i>approved financial institution</i>		<del>an approved financial institution as defined in IPRU(INS).</del> <u>any of the following:</u>

- (a) the European Central Bank;
- (b) the central bank of an EEA State;
- (c) the International Bank for Reconstruction and Development;
- (d) the European Bank for Reconstruction and Development;
- (e) the International Finance Corporation;
- (f) the International Monetary Fund;
- (g) the Inter-American Development Bank;
- (h) the African Development Bank;
- (i) the Asian Development Bank;
- (j) the Caribbean Development Bank;
- (k) the European Investment Bank;
- (l) the European Community; and
- (m) the European Atomic Energy Community.

*approved security*

- (1) (in *COLL* and *CIS*) ...
- (2) (in *LLD and PRU*) any of the following: ...

*broker*

(in *MAR and PRU*) any person when dealing as agent.

*capital at risk*

~~Capital at risk as defined in *IPRU(INS)* 2.5R(7).~~

*claim*

- (1) (in *COMP*)...
- (2) (in *PRU, LLD, SUP* and *TC*) ...

*class*

- (1) (in *AUTH, IPRU(FSOC), IPRU(INS), PRU, LLD* and *SUP*) (in relation to a *contract of insurance*) any class of *contract of insurance* listed in Schedule 1 to the *Regulated Activities Order (Contracts of insurance)* and references to:
  - (a) *general insurance business class 1, 2, 3, etc.*  
are references to *contracts of insurance* of



the kind mentioned in the corresponding numbered paragraph in Part I of Schedule 1 to that Order or, as the context may require, to the *effecting or carrying out of contracts of insurance* of that kind; and

(b) long-term insurance business class I, II, III, etc. are references to *contracts of insurance* of the kind mentioned in the corresponding numbered paragraph in Part II of Schedule 1 to that Order or, as the context may require, to the *effecting or carrying out of contracts of insurance* of that kind.

- collateral*
- (2) (in *COLL* and *CIS*): ...
  - (3) (in *COB*) ...
  - (1) (in *COLL* and *CIS*) ...
  - (2) (in *COB* and *CASS*) ...
  - (3) (in *PRU*) an asset that is subject to a mortgage, charge, pledge or other security interest.
- counterparty*
- (1) (in *LLD*) ...
  - (2) (in *PRU*) (in relation to an *insurer*):
    - (a) any one individual; or
    - (b) any one unincorporated body of *persons*; or
    - (c) any *company* which is not a member of a *group*; or
    - (d) any *group of companies* excluding any *companies* within the *group* which are *subsidiary undertakings* of the *insurer*; or
    - (e) any government of a State together with all the public bodies, local authorities or nationalised industries of that State,

in which the *insurer*, or any of its *subsidiary undertakings*, has made *investments* or against whom, or in respect of whom, it, or any of its *subsidiary undertakings*, has rights or obligations under a contract entered into by the *insurer* or any of its *subsidiary undertakings*.

<i>defined benefits pension scheme</i>	<p>(1) <u>(except in PRU) a pension policy or pension contract under which the only money-purchase benefits are benefits ancillary to other benefits which are not money-purchase benefits.</u></p> <p>(2) <u>(in PRU) an occupational pension scheme under which the only money-purchase benefits are benefits ancillary to other benefits which are not money-purchase benefits.</u></p>
<i>discounting</i>	(in LLD and in PRU) discounting or deductions to take account of investment income as set out in paragraph 48 of the <i>insurance accounts rules</i> .
<i>EEA insurer</i>	<del>(in COB)</del> an insurer, other than a pure reinsurer or a non-directive insurer, whose head office is in any EEA State except the United Kingdom and which has received authorisation under article 6 of the <i>First Life Directive</i> or article 4 of the <i>Consolidated Life Directive</i> or article 6 of the <i>First Non-Life Directive</i> from its Home State Regulator.
<i>financial year</i>	<p>(1) (in DISP) ...</p> <p>(2) (in LLD) ...</p> <p>(3) <u>(in PRU) the period at the end of which the balance of the accounts of the insurer is struck, or, if no balance is struck, the calendar year.</u></p>
<i>guarantee fund</i>	<p><del>(in relation to an insurer)</del> an amount equal to the greater of one third of the <i>required margin of solvency</i> and the <i>minimum guarantee fund</i>, as set out in <i>IPRU(INS) 2.9R</i>.</p> <p>(1) (a) <u>subject to (1)(b), in relation to a firm carrying on general insurance business, the higher of one third of the general insurance capital requirement and the base capital resources requirement applicable to that firm;</u></p> <p style="padding-left: 40px;">(b) <u>where the firm is required to calculate a UK MCR or an EEA MCR under PRU 7.6, for the purposes of that section the reference in (1)(a) to the general insurance capital requirement is replaced by UK MCR or EEA MCR, as appropriate.</u></p> <p>(2) (a) <u>subject to (2)(b), in relation to a firm carrying on long-term insurance business, the higher of one third of the long-term insurance capital requirement and the base capital resources requirement applicable to that firm;</u></p>

	(b)	<u>where the firm is required to calculate a UK MCR or an EEA MCR under PRU 7.6, for the purposes of that section the reference in (2)(a) to the long-term insurance capital requirement is replaced by UK MCR or EEA MCR, as appropriate.</u>
<i>Insurance Directives</i>		<del>the First Life Directive, Second Life Directive, and Third Life Directive and Consolidated Life Directive</del> and the <i>First Non-Life Directive, Second Non-Life Directive and Third Non-Life Directive</i> .
<i>listed</i>	(1)	(except in <i>LLD</i> and <i>PRU</i> ) included in an <i>official list</i> .
	(2)	(in <i>LLD</i> and <i>PRU</i> ) <ul style="list-style-type: none"> <li>(a) included in an <i>official list</i>; or</li> <li>(b) in respect of which facilities for <i>dealing</i> on a <i>regulated market</i> have been granted.</li> </ul>
<i>lower tier two capital</i>	(1)	(in <i>ELM</i> ) ...
	(2)	<u>(in <i>PRU</i>) an item of capital that is specified in stage H of the table in PRU 2.2.14R.</u>
<i>management expenses</i>	(1)	(except in <i>PRU</i> ) ...
	(2)	<u>(in <i>PRU</i>) in relation to long-term insurance business, means all expenses, other than commission, incurred in the administration of an insurer or its business.</u>
<i>margin of solvency</i>		<del>the excess of the value of an insurer's assets over the amount of its liabilities, that value and amount being determined in accordance with IPRU(INS) and IPRU(FSOC).</del>
<i>mathematical reserves</i>	(1)	(in <i>LLD</i> ) ...
	(2)	<u>(in <i>PRU</i>) the provision made by an insurer to cover liabilities (excluding liabilities which have fallen due and liabilities arising from deposit back arrangements) arising under or in connection with long-term insurance contracts.</u>
<i>minimum guarantee fund</i>		(in <i>LLD</i> ) a minimum guarantee fund as defined in <i>IPRU(INS)</i> 2.9 <u>as that rule was in force on 30 December 2004.</u>

*non-directive friendly society*

...

- (f) (i) *a friendly society* whose liabilities in respect of *general insurance contracts* are fully reinsured with or guaranteed by other ~~mutuals~~ mutuals (including *friendly societies*); and
- (ii) the mutuals providing the reinsurance or the guarantee are subject to the rules of the *First Non-Life Directive*;

...

*non-directive insurer*

~~a non-directive insurer as defined in *IPRU(INS)*.~~

- (a) an insurer whose insurance business is restricted to the provision of benefits which vary according to the resources available and in which the contributions are determined on a flat-rate basis; or
- (b) an insurer whose long-term insurance business is restricted to the provision of benefits for employed and self-employed persons belonging to an undertaking or group of undertakings, or a trade or group of trades, in the event of death or survival or of discontinuance or curtailment of activity (whether or not the commitments arising from such operations are fully covered at all times by mathematical reserves); or
- (c) an insurer which undertakes to provide benefits solely in the event of death where the amount of such benefits does not exceed the average funeral costs for a single death or where the benefits are provided in kind; or
- (d) a mutual (carrying on long-term insurance business) whose:
  - (i) articles of association contain provisions for calling up additional contributions from members or reducing their benefits or claiming assistance from other persons who have undertaken to provide it; and
  - (ii) annual gross premium income (other than from contracts of reinsurance) has not exceeded 5 million Euro for each of the financial year in question and the two previous financial years;

or

- (e) a mutual (carrying on general insurance business) whose:
  - (i) articles of association contain provisions for calling up additional contributions from members or reducing their benefits;
  - (ii) business does not cover liability risks, other than *ancillary risks*, or credit or suretyship risks;
  - (iii) gross premium income (other than from contracts of *reinsurance*) for the *financial year in question* did not exceed 5 million Euro; and
  - (iv) members provided at least half of that gross premium income; or
- (f) an insurer whose insurance business (other than *reinsurance*) is:
  - (i) restricted to the provision of assistance for persons who get into difficulties while travelling, while away from home or while away from their permanent residence;
  - (ii) carried out exclusively on a local basis and consists only of benefits in kind; and
  - (iii) such that the gross premium income from the provision of assistance in the *financial year in question* did not exceed 200,000 Euro; or
- (g) (i) a mutual whose liabilities in respect of general insurance contracts are fully reinsured with or guaranteed by other *mutuals* (including *friendly societies*); and
  - (ii) the *mutuals* providing the *reinsurance* or the guarantee are subject to the rules of the *First Non-Life Directive*.

*premium*

(1) ...

(2) (except in *ICOB* and *CASS 5*) (in relation to a *long-term insurance contract*) ~~a payment under the contract~~ the consideration payable under the contract by the *policyholder* to the *insurer*; ...

*prescribed pricing basis*

...  
(in relation to a *derivative contract*, or *quasi-derivative contract*), the pricing basis set out in *IPRU(INS) 4.12R(8)* (*Derivative contracts*) as that rule was in force on 30 December 2004.

*quasi-derivative contract or quasi-derivative*

a contract or asset having the effect of a *derivative contract*.

*regulated institution*

~~subject to the requirements of *IPRU* and as more fully defined in *IPRU*, an *insurance undertaking*, *credit institution*, *friendly society* or *investment firm*.~~

any of the following:

- (a) an *EEA insurer* or *UK insurer*; or
- (b) an *approved credit institution*; or
- (c) a *friendly society* (not within (a)) which is authorised to carry on *insurance business*; or
- (d) a *firm* whose *permission* includes *dealing in investments as principal* with respect to *derivatives* which are not *listed*; or
- (e) an *ISD investment firm* whose authorisation (as referred to in article 3 of the *ISD*) authorises it to carry on activities of the kind referred to in (d).

*regulated market*

- (1) (a) (as defined in article 1 of the *ISD*) ... ; and
- (b) (in *SUP 17* and, unless the context otherwise requires, elsewhere in the Handbook) ...
- (2) (in *PRU*) a market which is characterised by:
  - (a) regular operation;
  - (b) the fact that regulations issued or approved by the appropriate authority of the state where the market is situated:
    - (i) define the conditions for the operation of and access to the market;
    - (ii) define the conditions to be satisfied by a *financial instrument* in order for

	<u>it to be dealt in on the market; and</u>
	(iii) <u>require compliance with reporting and transparency requirements comparable to those laid down in articles 20 and 21 of the <i>Investment Services Directive</i>; and</u>
	(c) <u>in the case of a market situated outside the <i>EEA States</i>, the fact that the <i>financial instruments</i> dealt in are of a quality comparable to those in a regulated market in the <i>United Kingdom</i>.</u>
<i>required margin of solvency</i>	a <i>margin of solvency</i> required by <i>IPRU(INS)</i> or <i>IPRU(FSOC)</i> .
<i>required minimum margin</i>	for an <i>insurer</i> , the minimum margin required by <i>IPRU(INS)</i> .
<i>scheme of operations</i>	a scheme which: <ul style="list-style-type: none"> <li>(a) ...</li> <li>(b) contains the information required under <i>SUP App 2.9.1R</i> <del>2.12.1R</del>(Content of a scheme of operations).</li> </ul>
<i>secured debt</i>	(1) (in <i>LLD</i> ) ... <ul style="list-style-type: none"> <li>(2) (in <i>PRU</i>) a debt fully secured on: <ul style="list-style-type: none"> <li>(a) <u>assets whose value at least equals the amount of debt; or</u></li> <li>(b) <u>a letter of credit or guarantee from an <i>approved counterparty</i>.</u></li> </ul> </li> </ul>
<i>technical provision</i>	(1) (in <i>LLD</i> ) a technical provision as defined in the <i>insurance accounts rules</i> . <ul style="list-style-type: none"> <li>(2) (in <i>PRU</i>) a technical provision established: <ul style="list-style-type: none"> <li>(a) <u>for <i>general insurance business</i>, in accordance with <i>PRU 7.2.12R</i>; and</u></li> <li>(b) <u>for <i>long-term insurance business</i>, in accordance with <i>PRU 7.2.16R</i>.</u></li> </ul> </li> </ul>
<i>tier one capital</i>	(1) (in <i>ELM</i> ) ...

	(2)	<u>(in PRU) an item of capital that is specified in stages A, B or C of the table in PRU 2.2.14R.</u>
<i>tier two capital</i>	(1)	(in ELM) ...
	(2)	<u>(in PRU) an item of capital that is specified in stages G or H of the table in PRU 2.2.14R.</u>
<i>UK-deposit insurer</i>		<del>a UK deposit insurer as defined in IPRU(INS), which is in summary: a non-EEA insurer which has made a deposit in the United Kingdom in accordance with IPRU(INS) 8.1.</del>  <u>a non-EEA insurer that has made a deposit in the United Kingdom under article 23 of the First Non-Life Directive in accordance with article 26 of that Directive or under article 51 of the Consolidated Life Directive in accordance with article 56 of that Directive.</u>
<i>UK insurer</i>		<del>a UK insurer, as defined in IPRU(INS), which is in summary: an insurer, other than a pure reinsurer or a non-directive insurer, whose head office is in the United Kingdom.</del>  <u>an insurer, other than a pure reinsurer or a non-directive insurer, whose head office is in the United Kingdom.</u>
<i>upper tier two capital</i>	(1)	(in ELM) ...
	(2)	<u>(in PRU) an item of capital that is specified in stage G of the table in PRU 2.2.14R.</u>
<i>with-profits fund</i>	(1)	for the purposes of COB: ...
	(2)	<u>for the purposes of PRU, a long-term insurance fund in which policyholders are eligible to participate in any established surplus.</u>



## ADDENDUM

### INTEGRATED PRUDENTIAL SOURCEBOOK (INSURERS AND OTHER AMENDMENTS) (CONSEQUENTIAL AMENDMENTS) INSTRUMENT 2004

In Annex G to this instrument:

IPRU(INS) rule 9.29(2) is amended as follows, rather than as shown in the instrument:

- (2) In this rule, **derivative contract** includes a contract or asset which has the effect of a *derivative contract* ~~within the meaning of rule 4.13~~ and, for the purposes of (1)(h), such a contract or asset must be treated as requiring a significant provision or falling within rule 4.12 (2), ~~or the definition of permitted derivative contract~~, as appropriate, if it has the effect of a *derivative contract* which would require a significant provision or fall within that provision definition.

The definition of "permitted derivative contract" in IPRU(INS) Chapter 11, Part I is amended as follows, rather than as shown in the instrument:

<i>permitted derivative contract</i>	<p>(1) for the purpose of <b>Appendix 3.2</b>, a <i>derivative contract</i> or <u>quasi-derivative</u></p> <p>(a) which is 'covered' and—</p> <p>(i) which is held in connection with 'property' for the purposes of reduction of investment risk or efficient portfolio management, or</p> <p>(ii) which has the effect of a <i>permitted derivative contract</i> held in connection with 'property' for such purposes; and</p> <p>(b) which satisfies the conditions in rules 4.12(6) to (8) except that the references in rule 4.12 to 'an asset for the valuation of which provision is made in the <i>Valuation of Assets Rules</i>' is construed as a reference to <i>permitted connected property</i>;</p> <p><u>which satisfies the requirements of PRU 4.3 with the exception of PRU 4.3.18R, as applied in relation to assets covering liabilities in respect of linked long-term contracts of insurance, amended as follows:</u></p> <p>(a) in <u>PRU 4.3.5R and PRU 4.3.36R</u>, "For the purpose of PRU 2 Ann 1R (Admissible assets in</p>
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	<p>insurance)" is replaced by "For the purposes of <u>IPRU(INS) rules 3.6 and 3.7 and Appendix 3.2</u>";</p> <p>(b) in <u>PRU 4.3.6R(2) and (3), PRU 4.3.7R(1) and (2), PRU 4.3.17R(1) and PRU 4.3.36R(1)</u> "<u>admissible assets</u>" is replaced by "<u>permitted connected property</u>";</p> <p>(c) <u>PRU 4.3.12R(2) and (3)</u> are replaced by:  <u>"(2) (where they are held to cover index-linked liabilities) might:</u></p> <p style="padding-left: 40px;">(a) <u>not be appropriate cover for those liabilities as required by PRU 4.2.58R; or</u></p> <p style="padding-left: 40px;">(b) <u>fall in value; and</u></p> <p><u>(3) (where they are held to cover property-linked liabilities) might:</u></p> <p style="padding-left: 40px;">(a) <u>not be appropriately selected in accordance with contractual and constructive liabilities as required by PRU 7.6.36R and appropriate cover for those liabilities as required by PRU 4.2.57R; or</u></p> <p style="padding-left: 40px;">(b) <u>fall in value".</u></p> <p>(2) <b>property is—</b></p> <p style="padding-left: 40px;">(a) <del>permitted connected property, not being a contract or asset having the effect of a derivative contract; or</del></p> <p style="padding-left: 40px;">(b) <del>a permitted derivative contract or contract or asset having the effect of a permitted derivative contract either of which when taken together with the permitted derivative contract mentioned in (1), has the effect that the insurer holds either permitted connected property or a permitted derivative contract in connection with such property; and</del></p> <p>(3) <del>a derivative contract is covered if it would not require a significant provision to be made in respect of it pursuant to rule 5.3 if it were a derivative contract to which the Valuation of Asset Rules applied</del></p>
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Insert as new text in IPRU(INS), Chapter 12, between TR5 and TR7, the following transitional provision, TR6:

6	IPRU(INS) rule 9.31(b) and Appendix 9.4A, paragraphs 4(2), 6(3) and 13	R	<p>(1) Subject to compliance with (2), in relation to an <i>insurer's financial year</i> ending on or before 29 June 2005, the <i>insurer</i> is not required to include in the valuation report required by IPRU(INS) rule 9.31(b), and forming part of its <i>return</i> for that <i>financial year</i>, the information (the "omitted information") required by paragraphs 4(2), 6(3) and 13 of Appendix 9.4A to IPRU(INS).</p> <p>(2) The <i>insurer</i> must instead report the omitted information to the <i>FSA</i>, at the same time as it deposits its <i>return</i> for that <i>financial year</i> with the <i>FSA</i> in accordance with IPRU(INS) rule 9.6(1)(b), in a way that:</p> <p>(a) complies with the requirements for written notifications to the <i>FSA</i> in SUP 15.7.4R and SUP 15.7.5R; and</p> <p>(b) otherwise complies with the relevant paragraphs of Appendix 9.4A to IPRU(INS).</p>	From 31 December 2004 until 29 June 2005	31 December 2004
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Addendum  
22 December 2004

**CONDUCT OF BUSINESS SOURCEBOOK  
(AMENDMENT NO 19) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of its general rule-making power under section 138 of the Financial Services and Markets Act 2000 (the "Act").
- B. The rule-making power listed above is specified for the purposes of section 153(2) of the Act (Rule-making instruments).

**Commencement**

- C. This instrument comes into force on 1 January 2005.

**Amendments to the Conduct of Business sourcebook**

- D. The Conduct of Business sourcebook is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Conduct of Business Sourcebook (Amendment No 19) Instrument 2004.

By order of the Board  
16 December 2004

## Annex

### Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 5.2.9R      (1)      Unless (2) applies, a ~~A~~ *firm* must make and retain a record of a *private customer's* personal and financial circumstances that it has obtained in satisfying COB 5.2.5R. The *firm* must retain ~~the record must be retained~~ for a minimum period after the information is obtained, as follows:
- (1) (a)            ...
- (2) (b)            ...
- (3) (c)            ...
- (2)      A *firm* need not retain the record where following a *personal recommendation* to a *private customer* in connection with a *designated investment*, the *private customer* does not proceed with the recommendation or any part of it.

**INSURANCE MEDIATION (MISCELLANEOUS AMENDMENTS)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 138 (General rule-making powers);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157 (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 14 January 2005.

**Amendments to the Handbook**

- D. The Integrated Prudential sourcebook is amended in accordance with Annex A to this instrument.
- E. The Insurance: Conduct of Business sourcebook is amended in accordance with Annex B to this instrument.
- F. The Client Assets sourcebook is amended in accordance with Annex C to this instrument.
- G. The Supervision manual is amended in accordance with Annex D to this instrument.
- H. The Professional Firms sourcebook is amended in accordance with Annex E to this instrument.

**Citation**

- I. This instrument may be cited as the Insurance Mediation (Miscellaneous Amendments) Instrument 2004.

By order of the Board  
16 December 2004

## Annex A

### Amendments to the Integrated Prudential sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (2004/1).)

Insert a transitional rule as follows:

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provisions coming into force
5A	<u>PRU 9.4.5 R</u> and <u>PRU 9.4.7R</u>	R	<u>PRU 9.4.5R and PRU 9.4.7R have effect in respect of the use by a firm of the services of another person consisting of insurance mediation and provided from an establishment in an EEA State that has not implemented Article 3 (Registration) of the IMD, as if the condition in paragraph (4) of PRU 9.4.5R and the condition in paragraph (2) of PRU 9.4.7R were a condition that the firm has no reason to doubt the good repute, competence and financial standing of that person.</u>	<u>14 January 2005 to 14 January 2006</u>	<u>14 January 2005</u>

...

9.4.7 R The second condition in *PRU 9.4.4R* is that the *firm* takes all reasonable steps to ensure that the person in *PRU 9.4.5R* in relation to the activity, is not, directly or indirectly, carrying out the activity as a consequence of the activities of another person which:

...

(1) contravene section 19 of the *Act* (The general prohibition); or

(2) in the case of activities provided from an establishment in an EEA State, contravene the IMD registration requirements.

...

## Annex B

### Amendments to the Insurance: Conduct of Business sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Insurance: Conduct of Business Sourcebook Instrument 2004 (2004/6).)

Amend ICOB transitional rules as follows:

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision: coming into force
...					
7	<i>ICOB 5</i>	R	<p>(1) ...</p> <p>(2) If a <i>non-investment insurance contract</i> is concluded before 14 January 2005 and the <i>customer</i> has not previously received a <i>policy document</i>, the <i>insurer</i> or <i>insurance intermediary</i> (as the case may be) must ensure that the <i>customer</i> is provided with a copy of the <i>policy document</i> in good time prior to the commencement of any <i>renewal</i> of or mid-term change to the <i>policy</i> <u>but in respect of any mid-term change requested by a commercial customer on or before 30 April 2005, the insurer or insurance intermediary (as the case may be) may provide the commercial customer with the policy document promptly after the mid-term change.</u></p>	...	...
...					
9	<u><i>ICOB 5.5.5R (12)</i></u>	<u>R</u>	<u><i>A firm may comply with ICOB 5.5.5.R(12) without including in the policy summary, if it be the case, the fact that there is no compensation scheme.</i></u>	<u>14 January 2005 to 31 July 2005</u>	<u>14 January 2005</u>
...					



...

1.2.10 R *ICOB* does not apply to an *authorised professional firm* with respect to its *non-mainstream regulated activities* except for:

...

(4) those sections in *ICOB* which implement articles 12 and 13 of the *IMD*, unless:

(a) the *designated professional body* of the *firm* has made rules which implement some or all of the provisions of articles 12 and 13 of the *IMD*;

(b) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and

(c) the *firm* is subject to the rules in the form in which they were approved;

in which case those sections of *ICOB* which implement articles 12 and 13 of the *IMD* are disapplied to the extent that these articles are implemented by the rules of the *designated professional body*.

...

5.5.5 R Table: Policy summary content

(1) ...

(12) that, should the *insurance undertaking* be unable to meet its liabilities, the *retail customer* may be entitled to compensation from the *compensation scheme*, or from any other applicable named compensation scheme, or that there is no compensation scheme, should the *insurance undertaking* be unable to meet its liabilities; and

...

...

5.5.15A G If the *non-investment insurance contract* contains optional elements of cover, the total amount of *premium*, or the basis for the calculation of the *premium*, required under requirements of *ICOB* 5.5.14R(1) should include all also apply to each optional elements of cover selected by the *retail customer*.

...

## Annex C

### Amendments to the Client Assets sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Client Assets sourcebook (Amendment No 2) Instrument 2004 (2004/92).)

...

- 5.1.4A R (1) ~~A firm which, in relation to service charge, receives or holds *client money* and is required to segregate and account for such *money* in accordance with section 42 of the Landlord and Tenant Act 1987 ("the 1987 Act") will, if it complies with that provision and with (3), be deemed to comply with CASS 5.3 to 5.6.~~
- A firm will, subject to (3), be deemed to comply with CASS 5.3 to CASS 5.6 if it receives or holds *client money* and it either:
- (a) in relation to a service charge, complies with the requirement to segregate such money in accordance with section 42 of the Landlord and Tenant Act 1987 ("the 1987 Act"); or
- (b) in relation to money which is clients' money for the purpose of the Royal Institution of Chartered Surveyors' Rules of Conduct ("RICS rules") in force as at 14 January 2005, it complies with the requirement to segregate and account for such money in accordance with the RICS Members' Accounts rules.
- (2) Paragraph (1)(a) also applies to a *firm* in Scotland or in Northern Ireland if in acting as a property manager the *firm* receives or holds a service charge and complies (so far as practicable) with section 42 of the 1987 Act as if the requirements of that provision applied it.
- (3) In addition to complying with (1), a *firm* must ensure that an account in which *money* held pursuant to the trust fund mentioned in section 42(3) of the 1987 Act or an account maintained in accordance with the RICS rules satisfies the requirements in CASS 5.5.49R to the extent that the *firm* will hold money as trustee or otherwise on behalf of its clients.

...

- 5.5.18 R ...
- (4) (1) to (3) do not apply in relation to an *appointed representative, field representative* or other agent to which (if it were a *firm*) CASS 5.1.4AR(1) or (2) would apply, but subject to the *representative* or agent maintaining an account which satisfies the requirements of CASS 5.5.49R to the extent that the *representative* or agent will hold *client money* on trust or otherwise on behalf of its clients.

...

## Annex D

### Amendments to the Supervision manual

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Insurance Mediation and Mortgage Mediation, Lending and Administration (Prudential Provisions) Instrument 2004 (2004/01).)

...

13.3.2B G *An appointed representative appointed by a firm to carry on insurance mediation activity on its behalf may establish a branch in another EEA State under the Insurance Mediation Directive. In this case, the notice of intention in SUP 13.3.2G(1) should be given to the FSA by the firm on behalf of the appointed representative.*

...

13.4.2A G *An appointed representative appointed by a firm to carry on insurance mediation activity on its behalf may provide cross border services in another EEA State under the Insurance Mediation Directive. In this case, the notice of intention in SUP 13.4.2G(1) should be given to the FSA by the firm on behalf of the appointed representative.*

SUP Appendix 3 Guidance on passporting issues

...

3.10.11 G *Although the Insurance Directives are concerned with the regulated activities of effecting and carrying out contracts of insurance, an incoming EEA firm passported under the Insurance Directives ~~Consolidated Life Directive~~ will be entitled to carry on certain other regulated activities without the need for top-up permission. This is where the regulated activities are carried on for the purposes of or in connection with ~~the~~ the incoming EEA firm's insurance business. These regulated activities may include:*

...

## Annex E

### Amendments to the Professional Firms sourcebook

In this Annex underlining indicates new text and striking through indicates deleted text.

(This Annex amends in part the text made in the Distance Marketing Directive Instrument 2004 (2004/39).)

...

- 5.4.1 R (1) ...
- (2) Paragraph (1) does not apply in relation to regulations 6 to 7 and 14 to 15(2) if the *designated professional body* of the *authorised professional firm* has rules equivalent to some or all of those regulations and:
- (a) those rules have been approved by the *FSA* under section 332(5) of the *Act*; and
  - (b) the *authorised professional firm* is subject to those rules in the form in which they have been approved;
- in which case those regulations are disapplied to the extent that they are implemented by the rules of the *designated professional body*.

...

**MORTGAGE FIRMS AND INSURANCE INTERMEDIARIES FEES (2004/2005)  
INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 156 (General supplementary powers); and
  - (2) paragraph 17(1) of Schedule 1 (Fees).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force on 17 December 2004 (in part) and 14 January 2005 (in part) as follows:
- (1) SUP 20 Ann 2R part 1 A2 and A18 come into force on 17 December 2004;
  - (2) SUP 20 Ann 2R part 1 A19 comes into force on 17 December 2004 insofar as it relates to any regulated activity in relation to a long-term care insurance contract; and
  - (3) SUP 20 Ann 2R part 1 A19 comes into force on 14 January 2005 insofar as it relates to any regulated activity except in relation to a long-term care insurance contract.

**Amendments to the Supervision manual**

- D. The Supervision manual is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Mortgage Firms and Insurance Intermediaries Fees (2004/2005) Instrument 2004.

By order of the Board  
16 December 2004

## Annex

### Amendments to the Supervision manual

In this Annex underlining indicates new text, striking through indicates deleted text.

SUP 20 Ann 2R

Fee tariff rates, permitted deductions and EEA/Treaty firm modifications for the period from 1 April 2004 to 31 March 2005

Part 1

This table shows the tariff rates applicable to each fee-block.

Activity group	Fee payable	
...	...	...
A.2	<del>{to be made later}</del>  <u>Minimum fee (£)</u>  <u>No. of mortgages</u> <u>0 – 50</u> <u>51 – 500</u> <u>501 – 1,000</u> <u>1,001 – 50,000</u> <u>50,001 – 500,000</u> <u>&gt;500,000</u>	  <u>200</u>  <u>Fee (£/mortgage)</u> <u>0</u> <u>2.08</u> <u>0.83</u> <u>0.62</u> <u>0.21</u> <u>0.04</u>
...	...	...
A.18	<del>{to be made later}</del>  <u>Minimum fee (£)</u>  <u>£ thousands of Annual Income (AI)</u> <u>0 – 100</u> <u>&gt;100 – 1,000</u> <u>&gt;1,000 – 5,000</u> <u>&gt;5,000 – 10,000</u> <u>&gt;10,000 – 20,000</u> <u>&gt;20,000</u>	  <u>300</u>  <u>Fee (£/£ thousand or part £ thousand of AI)</u> <u>0</u> <u>2.50</u> <u>2.08</u> <u>1.67</u> <u>1.25</u> <u>1.04</u>
A.19	<del>{to be made later}</del>  <u>Minimum fee (£)</u>  <u>£ thousands of Annual Income (AI)</u> <u>0 – 100</u> <u>&gt;100 – 1,000</u> <u>&gt;1,000 – 5,000</u> <u>&gt;5,000 – 15,000</u> <u>&gt;15,000 – 100,000</u> <u>&gt;100,000</u>	  <u>100</u>  <u>Fee (£/£ thousand or part £ thousand of AI)</u> <u>0</u> <u>0.84</u> <u>0.74</u> <u>0.53</u> <u>0.21</u> <u>0.08</u>
...	...	...

**LLOYD'S SOURCEBOOK (INTEGRATED PRUDENTIAL AND AUDITING AND  
ACTUARIAL REQUIREMENTS) INSTRUMENT 2004**

**Powers exercised**

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 138 (General rule-making power);
  - (2) section 141 (Insurance business rules);
  - (3) section 150(2) (Actions for damages);
  - (4) section 156 (General supplementary powers);
  - (5) section 157(1) (Guidance);
  - (6) section 316 (Direction by Authority); and
  - (7) section 340 (Appointment).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

**Commencement**

- C. This instrument comes into force as follows:
- (1) the amendments in Annex G, Part 2 come into force on 1 January 2006;
  - (2) LLD 18.2.1R(1) as it applies PRU 1.2.22R to managing agents in Annex M comes into force on 1 January 2006;
  - (3) the amendment to the Glossary definition of "IPRU(INS)" in Annex V comes into force on 31 December 2004;
  - (4) the remainder of this instrument comes into force on 1 January 2005.

**Amendments to the Lloyd's sourcebook**

- D. The Lloyd's sourcebook is amended as follows:
- (1) the chapters of the Lloyd's sourcebook listed in column (1) of the following table are amended in accordance with the Annexes in column (2):

(1)	(2)
LLD Table of Contents	Annex A and Annex G, Part 2
LLD 1	Annex B
LLD 2	Annex C
LLD 9	Annex D
LLD 10	Annex E
LLD 11	Annex F
LLD 12	Annex G, Part 1 and Part 2
LLD 13	Annex H
LLD 14	Annex I
LLD 15	Annex J

(2) by inserting as new chapters and sections as listed in column (1) of the following table the provisions in the Annex listed in column (2):

(1)	(2)
LLD 16	Annex K
LLD 17	Annex L
LLD 18	Annex M
LLD 19	Annex N
LLD 20	Annex O
LLD 21	Annex P
LLD 22	Annex Q
LLD 23	Annex R
LLD 24	Annex S
LLD 25	Annex T

**Amendments to the Supervision manual**

E. The Supervision manual is amended in accordance with Annex U to this instrument.

**Amendments to the Glossary**

F. The Glossary is amended in accordance with Annex V to this instrument.

**Citation**

G. This instrument may be cited as the Lloyd's Sourcebook (Integrated Prudential and Auditing and Actuarial Requirements) Instrument 2004.

By order of the Board  
16 December 2004



## Annex A

### Amendments to the Lloyd's sourcebook, Table of Contents

In this Annex, underlining indicates new text and striking through indicates deleted text.

#### LLD Contents

Lloyd's			
	LLD TP	1	Lloyd's sourcebook – Transitional provisions
	LLD 1		The Society's regulatory functions
		1.1	Application and purpose
		1.2	Carrying out the Society's regulatory functions
		1.3	<del>Conflicts of interest</del> [deleted]
		1.4	<del>Confidential regulatory information</del> [deleted]
	LLD 2		Provision of information
		2.1	Application and purpose
		2.2	Specification of objective
		2.3	Information on matters likely to be of material concern to the FSA
		2.4	Information on investigations and disciplinary proceedings
		2.5	Co-operations between the FSA and the Society
		2.6	<del>Information about the Society's byelaws</del> [deleted]
	LLD 3		The Central Fund
			...
	LLD 4		Capacity transfer market
			...
	LLD 5		Former underwriting members
			...
	LLD 6		Complaints from policyholders
			...
	LLD 7		Complaints from members
			...
	LLD 8		Compensation arrangements for individual members
			...

	LLD 8A		Compensation arrangements for policyholders
			...
	LLD 9		<del>Prudential requirements for the Society</del>
		9.1	Application and purpose
		9.2	General prudential requirements
		9.3	General guidance on financial resources
		9.4	Accounting principles and records
	LLD 10		<del>Insurance operational risk</del>
		10.1	Application and purpose
		10.2	Systems and controls
		10.3	Carrying of insurance receivables to trust funds
		10.4	Changes in approved trust deeds
		10.5	Requirement to maintain risk-based capital system
		10.6	Requirements relating to monitoring aggregations of risk
		10.7	Requirements relating to syndicate business plans
		10.8	Managing agents systems and controls
		10.9	Requirements relating to the role of actuaries
		10.10	Limitation of business
		10.11	Monitoring of transactions between members
	LLD 11		<del>Required margins of solvency</del>
		11.1	Application and purpose
		11.2	Solvency requirement
		11.3	Member's margin
		11.4	General insurance
		11.5	Society margin
	LLD 12		Determination of liabilities
		12.1	Application and purpose
		12.2	<del>Requirement to determine liabilities</del>
		12.3	Members' liabilities
		12.4	<del>General insurance business technical provisions</del>
		12.5	<del>Long term liabilities</del>
	LLD 13		<del>Assets: valuation and realisability risk</del>
		13.1	Application and purpose
		13.2	Identification and valuation of assets
		13.3	Maturity and marketability of assets
		13.4	Admissible assets
		13.5	Restriction of value to realisable amounts
		13.6	Derivatives

		13.7	Stock lending agreements
		13.8	Debts and other rights
		13.9	Land
		13.10	Equipments
		13.11	Securities and beneficial interests in limited liability partnerships
		13.12	Collective investment schemes
		13.13	Deferred acquisition costs
		13.14	Reversionary interests
		13.15	Related and subsidiary undertakings
		13.16	Debts due or to become due from a related undertaking
	LLD 14		<del>[deleted]</del> Assets: market and credit risk
		14.1	Application and purpose
		14.2	Limitation of general market risk
		14.3	Currency matching and localisation
		14.4	Assets to be taken into account only to a specified extent
		14.5	Permitted asset exposure limits
		14.6	Counterparty exposure limits
	LLD 15		Reporting by the Society
		15.1	Application and purpose
		15.2	Requirement to report to the FSA
		15.3	Content and form of the Lloyd's return
		15.4	Risk groups for general insurance business
		15.5	Major treaty reinsurers
		15.6	Major facultative reinsurers
		15.7	Major reinsurance cedants
		15.8	Additional information
		15.9	Certificates and audit report
		15.10	The Lloyd's global account
		15.11	Public disclosure
		15.12	Other requirements
		15.13	<u>Syndicate-level reporting</u>
	LLD 16		<u>General provisions applying PRU to the Society and managing agents</u>
		16.1	<u>Section 150 of the Act (Actions for damages)</u>
		16.2	<u>Application</u>
		16.3	<u>Application of PRU to Lloyd's</u>
		16.4	<u>Summary of application of PRU to Lloyd's</u>
	LLD 17		<u>Special provisions for Lloyd's</u>
		17.1	<u>Section 150 of the Act (Actions for damages)</u>

	<u>17.2</u>	<u>Management of insurance business</u>
	<u>17.3</u>	<u>Obligations under PRU</u>
	<u>17.4</u>	<u>Management of risk</u>
	<u>17.5</u>	<u>Approved reinsurance to close</u>
	<u>17.6</u>	<u>Provision of information by managing agents</u>
	<u>17.7</u>	<u>Insurance receivables to be carried to trust funds</u>
	<u>17.8</u>	<u>Amendments to byelaws, trust deeds and standard form letters of credit and guarantees</u>
	<u>LLD 18</u>	<u>Application of PRU 1 to Lloyd's</u>
	<u>18.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>18.2</u>	<u>Adequacy of financial resources</u>
	<u>18.3</u>	<u>Valuation and recognition</u>
	<u>18.4</u>	<u>Prudential risk management and associated systems and controls</u>
	<u>LLD 19</u>	<u>Application of PRU 2 to Lloyd's</u>
	<u>19.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>19.2</u>	<u>Calculation of capital resources requirements</u>
	<u>19.3</u>	<u>Capital resources</u>
	<u>19.4</u>	<u>Individual capital assessment</u>
	<u>LLD 20</u>	<u>Application of PRU 3 to Lloyd's</u>
	<u>20.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>20.2</u>	<u>Credit risk management systems and controls</u>
	<u>20.3</u>	<u>Credit risk in insurance funds</u>
	<u>20.4</u>	<u>Asset-related capital requirements</u>
	<u>LLD 21</u>	<u>Application of PRU 4 to Lloyd's</u>
	<u>21.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>21.2</u>	<u>Market risk management systems and controls</u>
	<u>21.3</u>	<u>Market risk in insurance</u>
	<u>21.4</u>	<u>Derivatives in insurance</u>
	<u>LLD 22</u>	<u>Application of PRU 5 to Lloyd's</u>
	<u>22.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>22.2</u>	<u>Liquidity risk systems and controls</u>
	<u>LLD 23</u>	<u>Application of PRU 6 to Lloyd's</u>
	<u>23.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
	<u>23.2</u>	<u>Operational risk: prudential systems and controls</u>

	<u>LLD 24</u>		<u>Application of PRU 7 to Lloyd's</u>
		<u>24.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
		<u>24.2</u>	<u>Insurance risk systems and controls</u>
		<u>24.3</u>	<u>Capital resources requirements and technical provisions for insurance business</u>
		<u>24.4</u>	<u>Mathematical reserves</u>
		<u>24.5</u>	<u>Equalisation provisions</u>
		<u>24.6</u>	<u>Internal-contagion risk</u>
	<u>LLD 25</u>		<u>Regulatory intervention points for Lloyd's</u>
		<u>25.1</u>	<u>Section 150 of the Act (Actions for damages)</u>
		<u>25.2</u>	<u>Application of SUP App 2</u>
		<u>25.3</u>	<u>Interpretation</u>
		<u>25.4</u>	<u>Purpose</u>
		<u>25.5</u>	<u>Capital resources below guarantee fund</u>
		<u>25.6</u>	<u>Capital resources below required margin of solvency</u>
		<u>25.7</u>	<u>Capital resources below capital resources requirement</u>
		<u>25.8</u>	<u>Capital resources below the level of individual capital guidance</u>

## Annex B

### Amendments to the Lloyd's sourcebook, Chapter 1

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 Society's regulatory functions

...

1.2 Carrying out the Society's regulatory functions

Delegation

...

Disciplinary arrangements

...

Dealing with the FSA

1.2.7 G [deleted]

[Delete *LLD* 1.2.7G in its entirety; the deleted text is not shown struck through.]

1.2.8 G [deleted]

[Delete *LLD* 1.2.8G in its entirety; the deleted text is not shown struck through.]

1.2.9 G [deleted]

[Delete *LLD* 1.2.9G in its entirety; the deleted text is not shown struck through.]

1.3 ~~Conflicts of interest~~ [deleted]

[Delete *LLD* 1.3 in its entirety; the deleted text is not shown struck through.]

1.4 Confidential regulatory information

1.4.1 G [deleted]

[Delete *LLD* 1.4.1G in its entirety; the deleted text is not shown struck through.]

## Annex C

### Amendments to the Lloyd's sourcebook, Chapter 2

In this Annex, underlining indicates new text and striking through indicates deleted text.

2 Provision of information

...

2.6 ~~Information about the Society's byelaws~~[deleted]

[Delete *LLD* 2.6 in its entirety; the deleted text is not shown struck through.]

## **Annex D**

### **Amendments to the Lloyd's sourcebook, Chapter 9**

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 9      ~~Prudential requirements for the Society [deleted]~~  
[Delete *LLD* 9 in its entirety; the deleted text is not shown struck through.]



## Annex E

### Amendments to the Lloyd's sourcebook, Chapter 10

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 10      ~~Insurance operational risk~~ [deleted]  
[Delete *LLD* 10 in its entirety; the deleted text is not shown struck through.]

## Annex F

### Amendments to the Lloyd's sourcebook, Chapter 11

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 11      ~~Required margins of solvency~~ [deleted]  
[Delete *LLD* 11 in its entirety; the deleted text is not shown struck through.]

## Annex G

### Part 1

#### Amendments to the Lloyd's sourcebook, Chapter 12

In this Part, underlining indicates new text and striking through indicates deleted text.<sup>1</sup>

12 Determination of liabilities

12.1 Application and purpose

...

12.2 ~~Requirement to determine liabilities [deleted]~~

[Delete LLD 12.2 in its entirety; the deleted text is not shown struck through.]

...

12.3 Members' liabilities

12.3.1 R ~~For open syndicate years, a member's liabilities are the aggregate of:~~

~~(1) his proportionate share of the liabilities of each open syndicate year in which he participates, including:~~

~~(a) liabilities associated with earlier syndicate years that have been closed into that year; and~~

~~(b) any equalisation reserve allocated to him for the syndicate year by the Society under LLD 12.2.5G; and~~

~~(2)~~

At stage (e) of PRU 2.2.14R the Society must deduct from a member's capital resources a negative valuation difference being, for each member, (for open syndicate years through which the member carries on general insurance business taken together), if A+B exceeds C, A+B-C, where:

(1)(a) A is the total of his the member's proportionate shares for each syndicate year of the accumulated excess of income over outgoings;

(2)(b) B is the amount of any unpaid additional contributions the

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<sup>1</sup> The amendments to LLD 12 set out in this Part 1 take effect on 1 January 2005 until 31 December 2005. Further amendments taking effect on 1 January 2006 are set out in Part 2.

*member* is required to make to the funds maintained for the *syndicate years* by the *managing agents*; and

(3)(e) C is the total of his ~~the~~ *member's* proportionate shares of the liabilities net of reinsurance recoveries.

12.3.2 R For the purpose of ~~LLD 14.3~~ *PRU 4.2.52G to 4.2.56G* (Currency matching of assets and liabilities) and *PRU 7.2.30R* (Localisation (UK firms only)), the amounts in:

(1) ~~LLD 12.3.1R~~(2) *LLD 12.3.1R*, which are intended to prevent the premature release of profits,; and

(2) ~~LLD 12.2.4R~~ (the equalisation reserve);

may be left out of account.

12.3.3 R ~~[deleted]~~

[Delete *LLD 12.3.3R* in its entirety; the deleted text is not shown struck through.]

12.3.4 R ~~[deleted]~~

[Delete *LLD 12.3.4R* in its entirety; the deleted text is not shown struck through.]

12.4 ~~General insurance business technical provisions~~ ~~[deleted]~~

[Delete *LLD 12.4* in its entirety; the deleted text is not shown struck through.]

12.5 ~~Long term liabilities~~ ~~[deleted]~~

[Delete *LLD 12.5* in its entirety; the deleted text is not shown struck through.]

## Annex G

### Part 2

#### Amendments to the Lloyd's sourcebook, Table of Contents and Chapter 12

In this Part, underlining indicates new text and striking through indicates deleted text.<sup>2</sup>

The Lloyd's sourcebook, Table of Contents is amended as follows:

LLD Contents

Lloyd's

...

LLD12	<del>Determination of liabilities</del> [ <del>deleted</del> ]
12.1	<del>Application and purpose</del>
12.2	[ <del>deleted</del> ]
12.3	<del>Members' liabilities</del>
12.4	[ <del>deleted</del> ]
12.5	[ <del>deleted</del> ]

...

The Lloyd's sourcebook, Chapter 12 is amended as follows:

- 12 ~~Determination of liabilities~~ [~~deleted~~]  
[Delete *LLD* 12 in its entirety; the deleted text is not shown struck through.]

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<sup>2</sup> The amendments to LLD 12 set out in this Part 2 take effect on 1 January 2006.

## Annex H

### Amendments to the Lloyd's sourcebook, Chapter 13

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 13      ~~Assets: valuation and realisability risk~~ [deleted]  
[Delete *LLD* 13 in its entirety; the deleted text is not shown struck through.]

## Annex I

### Amendments to the Lloyd's sourcebook, Chapter 14

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 14      ~~Assets: market and credit risk~~ [deleted]  
[Delete *LLD* 14 in its entirety; the deleted text is not shown struck through.]

## Annex J

### Amendments to the Lloyd's sourcebook, Chapter 15

In this Annex, underlining indicates new text and striking through indicates deleted text.

LLD 15: Reporting by the Society

[Change to title of the chapter]

LLD 15: Reporting ~~by the Society~~

15.1 Application and purpose

Application

15.1.1 R This chapter applies to the *Society* and to *managing agents*.

...

15.1.4 G This chapter requires the *Society* to report on the *insurance business* carried on by *members* and on the assets and liabilities of *members* and the *Society*. It also requires *managing agents* to report on the *insurance business* carried on through each *syndicate* they manage. Reporting at *syndicate* level is required to enable the *Society* to prepare the *Lloyd's Return*.

15.1.5 G The *Lloyd's Return* is made annually and contains the statement required from the *Society* that it has maintained ~~the margin of solvency required under LLD 11 (Required margin of solvency)~~ *capital resources* equivalent to its *capital resources* requirement under PRU. This does not absolve the *Society* from the obligation to maintain ~~the required margin of solvency~~ *capital resources* equivalent to its *capital resources* requirement at all times.

...

15.2 Requirement to report to the FSA

...

15.2.2 R The report in LLD 15.2.1R must be prepared in accordance with ~~LLD 9.4.1R~~ PRU 1.3.5R and this chapter.

15.3 Content and form of the Lloyd's Return

15.3.1 R In preparing the *Lloyd's Return*, the *Society* must:

(1) complete the forms in LLD 15 Ann 1R, subject to ~~LLD 9 to LLD 15~~ to LLD 25,

(a) following the requirement of and making the disclosures required under Appendices 9.1, 9.2, 9.3 and 9.4 of



~~IPRU(INS); and,~~

~~(b) — having regard to Guidance Note 9.1 of IPRU(INS);~~

~~as if in the documents referred to in (a) and (b) those Appendices references to an insurer were references to the Society and members, and adapting the requirements in (a) and the guidance in (b) those Appendices where necessary;~~

(2) ...

...

15.4.7 G ~~Further guidance on risk groups and country classification is in IPRU(INS), Guidance Note 9.1, paragraph 9.4. [deleted]~~

15.8 Additional information

...

15.8.1 R

...  
(8) the circumstances surrounding the use of any *derivative* contract held at any time during the *financial year* which did not fall within ~~LLD 13.6.1R~~; fulfil the criteria outlined in PRU 4.3.5R; and

15.8.5 R

...  
(2) for each of the realistic disaster scenarios set by the *Society* ~~under LLD 10.6~~ when fulfilling its obligation under PRU to monitor aggregation of risk within the Lloyd's market of the contribution it is assumed each such reinsurer would provide in the event of that disaster occurring.

15.9 Certificates and audit report

...

15.9.1 R

(4) an abstract from the *syndicate actuary* of each *syndicate* which carries on *long-term insurance business* of the *actuary's* report made under ~~LLD 10.9.4R(2)(b)~~ SUP 4.6.14R(2).

New text to be inserted into LLD Chapter 15 after LLD 15.12

15.13 Syndicate-level reporting

15.13.1 R Each managing agent must:

(1) prepare a return for each financial year in respect of the insurance business carried on through each syndicate managed by it; and

(2) provide the return in (1) to the *Society* as soon as practicable after the end of the *financial year* but in any event in time to enable the *Society* to report to the *FSA* in accordance with *LLD 15.2.1R*.

15.13.2 R      The *Society* must:

(1) issue instructions to *managing agents* setting out the form and content of the return under *LLD 15.13.1R*; and

(2) issue the instructions in (1) as soon as practicable but in any event in time to enable *managing agents* to comply with *LLD 15.13.1R*.

15.13.3 R      A *managing agent* must annex to each return which it prepares under *LLD 15.13.1R*, a certificate signed by the persons referred to in *LLD 15.13.4R*, including the statements required by *LLD 15.13.5R*.

15.13.4 R      The certificate in *LLD 15.13.3R* must be signed by:

(1) where there are more than two *directors* of the *managing agent*, at least two of those *directors* and, where there are not more than two *directors*, all the *directors*; and

(2) a *chief executive*, if any, of the *managing agent* or (if there is no *chief executive*) the secretary.

15.13.5 R      Table

<u>1</u>	<u>The certificate in <i>LLD 15.13.3R</i> must state that:</u>	
	<u>(1)</u>	<u>the return has been properly prepared in accordance with the instructions referred to in <i>LLD 15.13.2R</i>;</u>
	<u>(2)</u>	<u>proper accounting records have been maintained and adequate information has been obtained by the <i>managing agent</i>;</u>
	<u>(3)</u>	<u>an appropriate system of control has been established and maintained by the <i>managing agent</i> over the <i>syndicate's</i> transactions and records;</u>
	<u>(4)</u>	<u>in relation to the statement by the <i>syndicate actuary</i> of a <i>syndicate</i> carrying on <i>long-term insurance business</i> required by <i>LLD 15.9.1R(3)</i>:</u>
	<u>(a)</u>	<u>proper accounts and records have been maintained for the purpose of preparing the statement; and</u>
	<u>(b)</u>	<u>the information given has been ascertained in</u>

			conformity with <i>LLD</i> 15 Annex 4R.
--	--	--	---

15.13.6 R *A managing agent must ensure for each syndicate managed by it that the return required under LLD 15.13.1R is examined and reported on by the syndicate auditor.*

15.13.7 R *A managing agent must annex to each return required under LLD 15.13.1R an audit certificate provided by the syndicate auditor including the statements required by LLD 15.13.8R.*

15.13.8 R Table

<u>1</u>	<u>The certificate in <i>LLD</i> 15.13.7R must state:</u>		
	<u>(1)</u>	<u>that in the auditors' opinion, the return has been properly prepared in accordance with the instructions referred to in <i>LLD</i> 15.13.2R;</u>	
	<u>(2)</u>	<u>that according to the information and explanations that the auditors have received:</u>	
		<u>(a)</u>	<u>in their opinion, the certificate required to be signed in accordance with <i>LLD</i> 15.13.3R (other than statements to which paragraph 1(3) relates) has been properly prepared in accordance with the instructions; and</u>
		<u>(b)</u>	<u>it was or was not unreasonable for the persons giving the certificate to have made the statements in it (other than statements to which paragraph 1(3) relates);</u>
	<u>(3)</u>	<u>the extent to which, in giving their opinion, the auditors have relied, in respect of <i>long-term insurance business</i>, on the work of the <i>syndicate actuary</i>.</u>	
<u>2</u>	<u>The audit opinion required by paragraph 1 does not extend to cover information on major treaty reinsurers or major facultative reinsurers.</u>		
<u>3</u>	<u>To the extent that the information and explanations they have received do not allow the auditors to express an opinion as to whether it was or was not unreasonable for the persons giving the certificate required to be signed in accordance with <i>LLD</i> 15.13.3R to have made the statements therein, the auditors must add to their report such qualification, amplification or explanation as may be appropriate.</u>		

## Annex K

### Amendments to the Lloyd's sourcebook, Chapter 16

In this Annex, all the text is new and is not underlined.

- 16 General provisions applying PRU to Lloyd's
- 16.1 Section 150 of the Act (Actions for damages)
- 16.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 16.2 Application
- 16.2.1 R This chapter applies to:
- (1) the *Society*; and
  - (2) *managing agents*.
- Purpose
- 16.2.2 G The purpose of this chapter is to:
- (1) set out specific requirements for the prudential management of the *insurance business* of Lloyd's *members*, including management of the assets supporting that business; and
  - (2) clarify how *PRU rules* and *guidance* are to apply to the *insurance business* of Lloyd's *members*.
- 16.2.3 G *Members* bear the risk in respect of their *insurance business* and so it is their responsibility to hold financial resources to support that business. A *member* participates on a several basis, for its own account. In practice *managing agents* manage the business and the *Society* manages the market. Should a *member* hold insufficient financial resources, the *Society's* own assets may be used to support that *member's* business.
- 16.3 Application of PRU to the Society and managing agents
- 16.3.1 R If a provision in *PRU* applies to the *Society* "in accordance with" this *rule*, the *Society* must:
- (1) manage each *member's funds at Lloyd's*;

- (2) manage its *central assets*; and
- (3) supervise the *insurance business* carried on by each *member* at Lloyd's;

so as to achieve in relation to those assets and that *insurance business* the same effect as the relevant *PRU* provision would have (that is, conforming with the requirements of any *rule* and taking appropriate account of any applicable *guidance*.) when applied to a *firm* or to the *insurance business* of a *firm*.

16.3.2 G The *Society* is subject to *PRU rules* in respect of the *insurance business* of each Lloyd's *member*. These include *rules* in respect of:

- (1) the calculation of the *capital resources requirements* for each *member*;
- (2) the financial resources it manages on behalf of *members*; and
- (3) the *Society's* own financial resources.

16.3.3 R If a provision in *PRU* applies to a *managing agent* "in accordance with" this *rule*, the *managing agent* must, in relation to each *syndicate* managed by it and for each *syndicate year*, manage:

- (1) the *syndicate assets*; and
- (2) the *insurance business* carried on by the *members* of the *syndicate* through that *syndicate*;

so as to achieve in relation to those assets and that *insurance business* the same effect as the relevant *PRU* provision would have (that is, conforming with the requirements of any *rule* and taking appropriate account of any applicable *guidance*.) when applied to a *firm* or to the *insurance business* of a *firm*.

16.3.4 G *Syndicate* membership may change from year to year or it may remain constant. *Managing agents* are required to apply *PRU* to the *insurance business* carried on through each *syndicate* for each *syndicate year*. This should ensure that *PRU* is applied to Lloyd's in a way that is consistent with the provision of capital to support the *insurance business* underwritten.

16.3.5 G Where common systems and controls or processes are appropriate for all the *insurance business* carried on through more than one *syndicate year*, a single response may be adequate for all *syndicate years*. However, in some cases it will be important to consider the business of each *open syndicate year* separately, particularly for quantitative *rules*. For example, it is important that *managing agents* separately assess the financial resources (including capital) that are required and are available to support the *insurance business* carried on through each *syndicate year*, where the *syndicate* membership changes from year to year. This is because each *member's* assets are only available to support its own business, so the assets

supporting one year of account may not be available to support another. For example, if a *managing agent* were to assess the financial requirements of two or more *syndicate years* together where the capital structure had changed, there would be a risk that the *managing agent* might take account of diversification effects that were not reflected in the capital supporting the *insurance business*.

- 16.3.6 G There is no requirement on *managing agents* to carry out separate individual capital assessments for *syndicates* for each *syndicate year*. *Managing agents* are required to carry out individual capital assessments for each *syndicate* as if that *syndicate* were a *firm*; this would normally be on the basis of a going concern but, just as in a *firm*, account needs to be taken of any restrictions on the availability of assets (e.g. deposits with cedants), and some account needs to be taken of changes in the capital participation in the *syndicate*. The *Society* is responsible for the individual capital assessment for each *member*, which must take into account the assessments made by *managing agents* of any *syndicates* on which the *member* participates. *PRU 2.3* contains *rules and guidance* on the assessment of capital adequacy for *firms* and *LLD 19.4.1R to LLD 19.4.24R* provide for the application of *PRU 2.3* to the *Society* and *managing agents*.

#### 16.4 Summary of application of PRU to Lloyd's

- 16.4.1 G Table: Key *PRU* requirements for Lloyd's

Key PRU requirements	<i>PRU</i>	<i>LLD</i>
Risk management, systems and controls		
The <i>Society</i> to establish and maintain systems and controls to address risks affecting the Lloyd's market		17.4
The <i>Society</i> to establish and maintain systems and controls for the management of prudential, credit, market, liquidity and operational risks affecting <i>funds at Lloyd's</i> and <i>central assets</i>	1.4, 3.1, 4.1, 5.1 & 6.1	17.4, 18.4, 20.2, 21.2, 22.2 & 23.2
<i>Managing agents</i> to establish and maintain systems and controls for the management of prudential, credit, market, liquidity, operational, and insurance risks affecting each <i>syndicate</i>	1.4, 3.1, 4.1, 5.1, 6.1 & 7.1	17.4, 18.4, 20.2, 21.2, 22.2, 23.2 & 24.2
Adequacy of financial resources		
The <i>Society</i> to ensure that <i>members'</i> financial resources are adequate	1.2	18.2

<i>Members</i> taken together to maintain adequate financial resources in respect of the <i>insurance business</i> conducted at Lloyd's		18.2
<i>Managing agents</i> to ensure that financial resources are adequate for each <i>syndicate</i>	1.2	18.2
Valuation		
The <i>Society</i> and <i>managing agents</i> to apply generally accepted accounting principles to valuing assets, liabilities, equity and income statement items for the purposes of the <i>rules</i> and <i>guidance</i> in <i>LLD</i> and <i>PRU</i> unless the contrary is expressly stated	1.3 & 4.3	18.3 & 21.4
Capital resources requirements		
The <i>Society</i> to calculate the <i>MCR</i> in respect of the <i>general insurance business</i> of each <i>member</i>	2.1	19.2
The <i>Society</i> to calculate the <i>CRR</i> (higher of <i>MCR</i> and <i>ECR</i> ) in respect of the <i>long-term insurance business</i> of each <i>member</i>	2.1	19.2
Capital resources		
The <i>Society</i> and <i>managing agents</i> to calculate <i>capital resources</i> in accordance with the <i>rules</i> and <i>guidance</i> in <i>LLD</i> and <i>PRU</i>	2.2	19.3
Adequacy of capital resources		
<i>Managing agents</i> to assess the adequacy of <i>capital resources</i> held at <i>syndicate</i> level in respect of <i>insurance business</i> carried on through each <i>syndicate</i> (annual <i>ICA</i> for each <i>syndicate</i> )	2.3	19.4
The <i>Society</i> to assess the adequacy of <i>capital resources</i> available to support each <i>member's insurance business</i> ( <i>ICA</i> for each <i>member</i> ), both at <i>syndicate</i> level (taking account of <i>syndicate ICAs</i> ), and as <i>funds at Lloyd's</i>	2.3	19.4

## Annex L

### Amendments to the Lloyd's sourcebook, Chapter 17

In this Annex, all the text is new and is not underlined.

- 17 Special provisions for Lloyd's
  - 17.1 Section 150 of the Act (Actions for damages)
    - 17.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
  - 17.2 Management of insurance business
    - 17.2.1 R Neither the *Society* nor *managing agents* may permit a *member* to carry on any *insurance business* except as a participant on one or more *syndicates*.
    - 17.2.2 G *LLD 17.2.1R* ensures that any *insurance business* carried on by *members* is subject to appropriate *FSA* requirements.
  - 17.3 Obligations under PRU
    - 17.3.1 R The *Society* must ensure that all participants in the Lloyd's market are made aware of their obligations under *PRU*.
    - 17.3.2 G The application of *PRU* to Lloyd's is effected in *LLD 16* to *LLD 24*. *SUP Appendix 2* is applied to Lloyd's in *LLD 25*. Further requirements relevant to the *Society's* general responsibilities with regard to the market are contained in *LLD 1* to *LLD 8A* and *LLD 17*. Requirements relevant to *managing agents* and other participants and advisers in relation to the Lloyd's market are contained elsewhere in the *Handbook*.
  - 17.4 Management of risk
    - 17.4.1 R The *Society* must establish and maintain systems and controls to enable it appropriately to address the risks to which the Lloyd's market is exposed.
    - 17.4.2 G As well as the risks that are common to other *firms*, there are significant risks in the Lloyd's market arising out of its structure and the inter-relationships between the entities involved. The risks include aggregations of risk in the market. The *Society* should ensure that the systems and controls required by *LLD 17.4.1R* enable it to identify, monitor and manage those risks.
    - 17.4.3 R The systems and controls in *LLD 17.4.1R* must include systems and controls to enable the *Society* to ensure that any assumptions made in calculating a



*member's capital resources* or in determining the individual capital assessment for each *member* are regularly reviewed and that appropriate action is taken if any assumption is no longer valid.

- 17.4.4 R The *Society* must take all reasonable steps, including establishing and maintaining adequate systems and controls to enable it:
- (1) to manage the risks to which *funds at Lloyd's* and *central assets* are exposed; and
  - (2) to ensure that *funds at Lloyd's* and *central assets* are adequate to support all *balancing amounts*.
- 17.4.5 G In complying with LLD 17.4.4R the *Society* should take appropriate account of effects such as diversification and concentrations.
- 17.4.6 R A *managing agent* must establish and maintain adequate systems and controls to manage the risks to which the *insurance business* carried on through each *syndicate* it manages is exposed.
- 17.4.7 R In complying with LLD 17.4.6R a *managing agent* need not take account of risks associated with assets that are not *syndicate assets*.
- 17.4.8 R The *Society* must take reasonable steps to ensure that systems and controls established and maintained by *managing agents* are adequate to ensure that risks to which the *insurance business* carried on through each *syndicate* is exposed do not have a detrimental effect on *funds at Lloyd's* or *central assets*.
- 17.4.9 G *Managing agents* and the *Society* each hold and manage some of the financial resources held to support the *insurance business* carried on through *syndicates*. In particular:
- (1) the *Society* holds and manages *funds at Lloyd's* and *central assets* which must be held to support *balancing amounts*. The *Society* is required to manage the risks that affect *funds at Lloyd's* and *central assets* directly, once the effects of any aggregation and diversification have been taken into account;
  - (2) *managing agents* hold and manage some of the financial resources in respect of the *insurance business* carried on through each *syndicate* that they manage. *Managing agents* are required to manage all risks affecting a *syndicate* except for the risk that *funds at Lloyd's* and *central assets* are not available to support the *balancing amount*.
- 17.4.10 G Should the *Society* intend to exercise any power it may have to prescribe a course of action for a *managing agent* which the *managing agent* might reasonably consider to be inconsistent with the interests of any *member* whose *insurance business* it manages, the *Society* should:
- (1) consult any affected *member*, where practical in advance; and

- (2) in accordance with *PRIN* 11 (Relations with regulators), *LLD* 2 and, to enable the *FSA* to comply with section 314 of the *Act* (Authority's general duty), consider whether it should notify the *FSA*.

Group risk and conflicts of interest

- 17.4.11 G Many entities operating within the Lloyd's market are part of a corporate group, including the *Society*, certain *managing agents* and *members*. Those entities are subject to group risk arising from their own corporate group and, depending on the relationships within their own group, may be subject to *FSA* systems and controls requirements or group risk requirements. The *rules* and *guidance* in this section are intended to ensure that sufficient systems and controls are in place to protect *policyholders* and potential *policyholders* from such risks. The *Society* is also subject to the risk of wider conflicts of interest or the appearance of conflicts of interest in carrying out the *Society's regulatory functions*. *LLD* 17.4.13R(1) requires the *Society* to monitor and manage those risks.
- 17.4.12 G In complying with *LLD* 17.4.6R, *managing agents* should have particular regard to:
- (1) transactions which may give rise to a conflict of interest, such as those to which the counterparties are:
    - (a) other members of the *managing agent's* own group;
    - (b) any *members* of any *syndicates* managed by the *managing agent*; or
    - (c) any entity that is part of a *group* to which one or more *members* of any *syndicates* managed by the *managing agent* belong; and
  - (2) transactions involving:
    - (a) the provision of capital;
    - (b) the provision of *reinsurance*; or
    - (c) the provision of other services.
- 17.4.13 R The *Society* must establish and maintain effective arrangements to monitor and manage risk arising from:
- (1) conflicts of interest (including in relation to (2) to (4));
  - (2) inter-*syndicate* transactions, including *reinsurance to close* and *approved reinsurance to close*;
  - (3) related party transactions; and

- (4) transactions between *members* and itself.
- 17.4.14 R The arrangements in *LLD 17.4.13R* must enable the *Society* to identify any significant overstatement of financial resources resulting from any transaction falling within *LLD 17.4.13R (2) to (4)*, including as a result of:
- (1) any differences in the amounts recorded as due or payable by each party to any such transaction; or
  - (2) any actual or likely disputes between the parties to any such transaction.
- 17.4.15 R If the *Society* identifies a significant overstatement of the kind referred to in *LLD 17.4.14R*, it must ensure that an appropriate adjustment is made, including if appropriate by a deduction from or reduction in the value attributed to:
- (1) the *capital resources* of any *member* concerned; or
  - (2) the *Society's capital resources*.
- 17.4.16 G In complying with *LLD 17.4.14R* and *LLD 17.4.15R*, the *Society* should consider the significance of any overstatement with regard to the value of the *Society's capital resources* that are not required to cover shortfalls in a *member's capital resources*.
- 17.5 Approved reinsurance to close
- 17.5.1 G As defined in the *Glossary*, "approved reinsurance to close" excludes:
- (1) *reinsurance* between parties other than *members*; and
  - (2) balance transfers between *syndicate years* of *syndicates* having only one *member*, which have no effect on the overall liabilities of that *member*.
- 17.5.2 G The "approved" status of an *approved reinsurance to close* does not alter the legal status or effect of the original *contract of insurance*, or the liability of a reinsured *member* to the *policyholder* under or in respect of the original *contract of insurance*.
- 17.5.3 R Notwithstanding that the liability of a reinsured *member* to a *policyholder* is unaffected by an *approved reinsurance to close* as described in *LLD 17.5.2G*, for the purposes of *PRU* only:
- (1) a *contract of insurance* reinsured under an *approved reinsurance to close* must be treated as if the reinsuring *member* and not the reinsured *member* had effected the original *contract of insurance*; and
  - (2) any payment received by a *member* as consideration for or in connection with an *approved reinsurance to close* must be treated as

a *Lloyd's member's contribution* and not as *premium* or as a reinsurance recovery.

- 17.6 Provision of information by managing agents
- 17.6.1 R A *managing agent* must, as soon as possible, give the *Society* any information the *managing agent* has concerning material risks to *funds at Lloyd's* or *central assets*.
- 17.6.2 R A *managing agent* need not comply with *LLD 17.6.1R* if the *managing agent* knows that the *Society* already has the relevant information.
- 17.7 Insurance receivables to be carried to trust funds
- 17.7.1 R The *Society* must take all reasonable steps to ensure that each *member*:
- (1) executes the appropriate *Lloyd's trust deeds*; and
  - (2) carries to the appropriate *Lloyd's trust fund* all amounts received or receivable by the *member*, or on its behalf, in respect of any *insurance business* carried on by it.
- 17.7.2 R The *Society* must carry all amounts it receives on behalf of any *member* in respect of that *member's insurance business* to the appropriate *Lloyd's trust fund*.
- 17.7.3 R A *managing agent* must carry all amounts it receives on behalf of any *member* in respect of that *member's insurance business* to the appropriate *Lloyd's trust fund*.
- 17.7.4 R In complying with *LLD 17.7.1R* to *LLD 17.7.3R*, the *Society* and *managing agents* must take all reasonable steps to ensure that amounts received or receivable by a *member* in respect of *general insurance business* and *long-term insurance business* are carried to separate *Lloyd's trust funds*.
- 17.7.5 G The requirement in *LLD 17.7.4R* should be read in conjunction with the requirements of *PRU 7.6* as applied to the *Society* and *managing agents* in *LLD 24.6.1R* to *LLD 24.6.5G*.
- 17.8 Amendments to byelaws, trust deeds and standard form letters of credit and guarantees
- 17.8.1 R The *Society* must, as soon as it is practical to do so, notify the *FSA* of its intention to approve the form of any new *Lloyd's trust deed*.
- 17.8.2 R The *Society* must, as soon as it is practical to do so, notify the *FSA* of its intention to make any amendment which may alter the meaning or effect of any *byelaw*, including:
- (1) any *Lloyd's trust deed*;
  - (2) any standard form letter of credit prescribed by the *Society* from time

to time; or

- (3) any standard form guarantee agreement prescribed by the *Society* from time to time.

- 17.8.3 R The *Society* must provide the *FSA* with full details of:
- (1) the form of any new *Lloyd's trust deed* it intends to approve, as described in *LLD 17.8.1R*; and
  - (2) any amendments falling within *LLD 17.8.2R*.
- 17.8.4 R The *Society* must consult interested parties in relation to any new *Lloyd's trust deed* and in relation to any amendment falling within *LLD 17.8.2R*.
- 17.8.5 G Except in urgent cases, the *Society* should consult in relation to any new *Lloyd's trust deed* or amendments before the new deed or amendments take effect.
- 17.8.6 R The information provided to the *FSA* by the *Society* under *LLD 17.8.3R* must include:
- (1) a statement of the purpose of any proposed amendment or new *Lloyd's trust deed* and the expected impact, if any, on *policyholders, managing agents, members, and potential members*; and
  - (2) a description of the consultation undertaken under *LLD 17.8.4R* including a summary of any significant responses to that consultation.
- 17.8.7 G The *FSA* would normally expect to receive the information required under *LLD 17.8.3R* and *LLD 17.8.6R* not less than three months in advance of the proposed change.

## Annex M

### Amendments to the Lloyd's sourcebook, Chapter 18

In this Annex, all the text is new and is not underlined.

- 18 Application of PRU 1 to Lloyd's
- 18.1 Section 150 of the Act (Actions for damages)
- 18.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 18.2 Adequacy of financial resources
- Application of PRU 1.2
- 18.2.1 R *PRU 1.2* applies to *managing agents* and to the *Society* in accordance with:
- (1) for *managing agents*, *LLD 16.3.3R*; and
  - (2) for the *Society*, *LLD 16.3.1R*.
- 18.2.2 R *LLD 18.2.7R* applies to *members*, pursuant to the *insurance market direction* in *LLD 18.2.5D*.
- Insurance market direction
- 18.2.3 G The *insurance market direction* in *LLD 18.2.5D* is given under section 316(1) of the *Act* (Direction by Authority) and applies to *members*.
- 18.2.4 G The purpose of the *insurance market direction* in *LLD 18.2.5D* is to enable the *FSA* to make the rule in *LLD 18.2.7R* applying to *members*, in order to:
- (1) protect *policyholders* against the risk that *members* may not have adequate financial resources to meet liabilities under or in respect of *contracts of insurance* as they fall due;
  - (2) promote confidence in the market at Lloyd's by requiring *members* to maintain financial resources which are adequate to meet their liabilities.
- 18.2.5 D With effect from 1 January 2005, Part X of the *Act* (Rules and Guidance) applies to the *members* of the *Society* taken together in relation to the *insurance market activities* of *effecting* and *carrying out contracts of insurance* written at Lloyd's, for the purpose of applying the *rules* and *guidance* in *LLD 18.2.7R* to *LLD 18.2.9G*.
- 18.2.6 G Part X of the *Act* is a *core provision* specified in section 317(1) of the *Act*

(The core provisions). Section 317(2) provides that references in an applied *core provision* to an *authorised person* are to be read as references to a *person* in the class to which the *insurance market direction* applies. From 1 January 2005, references in Part X of the *Act* are to be read as references to *members* for the purposes of *LLD 18.2.7R* to *LLD 18.2.9G*.

#### Members' obligation to maintain adequate financial resources

18.2.7 R The *members* taken together must at all times maintain overall financial resources, including capital and liquidity resources, that are adequate, both as to amount and quality, to ensure that there is no significant risk that liabilities under or in respect of *contracts of insurance* written at Lloyd's will not be met as they fall due.

18.2.8 G Under *PRU*:

(1) *managing agents* must ensure that adequate financial resources are available to support the *insurance business* carried on through each *syndicate* that they manage; and

(2) the *Society* must, having regard to the availability and value of the *central assets*, ensure that the financial resources supporting the *insurance business* of each *member* are adequate at all times.

18.2.9 G In practice compliance with the requirements described in *LLD 18.2.8G* are likely to have the effect that *members* comply with *LLD 18.2.7R*.

#### 18.3 Valuation and recognition

##### Application of *PRU 1.3*

18.3.1 R *PRU 1.3* applies to *managing agents* and to the *Society* in accordance with:

(1) for *managing agents*, *LLD 16.3.3R*; and

(2) for the *Society*, *LLD 16.3.1R*.

##### Amounts receivable but not yet received

18.3.2 R When recognising and valuing assets that are available to meet liabilities arising from a *member's insurance business*, neither the *Society* nor *managing agents* may attribute any value to any amounts receivable but not yet received from that *member* or another *member*, except for:

(1) timing differences provided that a corresponding amount has been deducted from *syndicate assets* or *funds at Lloyd's*;

(2) the *Society's callable contributions*, which are valued according to *LLD 18.3.10G* to *LLD 18.3.12R*; and

- (3) debts owed by a *member* to another *member* of the *Society* where the debt is a liability arising out of the *insurance business* he carries on at Lloyd's.

Letters of credit, guarantees and life assurance policies

- 18.3.3 G Letters of credit, guarantees and life assurance policies are admissible assets in respect of *insurance business* at Lloyd's and qualify as *capital resources* under *PRU 2.2*, subject to *LLD 18.3.4R* to *LLD 18.3.9G*.
- 18.3.4 R When recognising and valuing assets held as *members' funds at Lloyd's* the *Society* may, if the conditions in *LLD 18.3.5R* are satisfied, attribute a value to letters of credit and guarantees that it holds in respect of a *member's insurance business*.
- 18.3.5 R The conditions referred to in *LLD 18.3.4R* are that letters of credit and guarantees must be:
- (1) in the form prescribed by the *Society* from time to time and notified to the *FSA*; and
- (2) issued by a *credit institution* or an *insurance undertaking*.
- 18.3.6 R When recognising and valuing assets held as *members' funds at Lloyd's* the *Society* may attribute a value to verifiable sums arising out of life assurance policies.
- 18.3.7 R The *Society* must value any letter of credit, guarantee or life assurance policy at its net realisable value. The *Society* must make all appropriate deductions, including those in respect of:
- (1) the expenses of realisation; and
- (2) any reduction in value that would be likely to occur if the asset needed to be realised at short notice to meet liabilities falling due earlier than expected.
- 18.3.8 R If a *member* relies on a value attributed to a letter of credit or guarantee to meet any applicable *capital resources requirement* and that letter of credit or guarantee will expire in less than one month, the *Society* must take appropriate steps to ensure that the applicable *capital resources requirement* will continue to be met, including taking steps to ensure that sums due under the letter of credit or guarantee are drawn down when due and carried to the appropriate *Lloyd's trust fund*.
- 18.3.9 G In *LLD 18.3.8R*, the expiry date includes the date on which the instrument will terminate if not renewed, and the date on which any notice to terminate will or would take effect.

The *Society's* callable contributions

- 18.3.10 G Under *LLD 19.3.7R(2)* and *LLD 19.3.9R*, the *Society* may recognise and



value *callable contributions* in its calculation of its own *capital resources*. *LLD 18.3.11R* specifies the maximum value that may be attributed to *callable contributions*.

- 18.3.11 R For the purposes of *LLD 19.3.7R(2)* and *LLD 19.3.9R*, the amount assumed to be callable from a *member* must not exceed the lower of:
- (1) the maximum *callable contribution* that *member* is or may be liable to make in that *financial year*; and
  - (2) the amount by which the *member's* own *capital resources* exceed the *member's* own *capital resources requirement*.
- 18.3.12 R The *Society* must value *callable contributions* taking appropriate account of any legal, constructive or other limits on its ability to call for contributions from *members* or to realise the amount called.
- 18.3.13 R The *Society* must give the *FSA* adequate advance notice if it proposes to change the maximum amount of the *callable contribution* that *members* may be liable to make in any *financial year*.
- 18.3.14 G The *FSA* would normally expect not less than six months' notice under *LLD 18.3.13R*.

#### Liabilities

- 18.3.15 R Subject to *LLD 18.3.16R*, the *Society* must recognise and value all of a *member's* liabilities in respect of its *insurance business*.
- 18.3.16 R The *Society* need not recognise or value a *member's* liabilities that are recognised and valued at *syndicate* level by *managing agents* in accordance with *PRU 1.3*.
- 18.3.17 R For the purposes of calculating a *member's* *capital resources*, when valuing a *member's* funds at *Lloyd's* the *Society* must deduct the value of a *member's* liabilities determined under *LLD 18.3.15R*.
- 18.3.18 G The liabilities to be valued under *LLD 18.3.15R* and deducted under *LLD 18.3.17R* include:
- (1) amounts owing to *members' agents*;
  - (2) amounts owing to the *Society*;
  - (3) an appropriate accrual for tax payable on any profits;
  - (4) (where required under any applicable accounting principle in accordance with *PRU 1.3.5R*), any contingent liability relating to liabilities reinsured into Equitas Reinsurance Ltd; and
  - (5) amounts apportioned to *members* in respect of the credit equalisation

reserve under *PRU 7.5*.

18.3.19 R In recognising and valuing a *member's* liabilities, the *Society* and *managing agents* may, to the extent permitted by applicable accounting principles, leave out of account the liabilities in respect of 1992 and prior *general insurance business* reinsured by Equitas Reinsurance Limited.

18.3.20 G There may be contingent liabilities associated with the reinsurance into Equitas. *PRU 1.3* requires *managing agents* and the *Society* to treat those contingent liabilities in accordance with applicable accounting principles: see *PRU 1.3.5R*. Depending on the circumstances, *managing agents* or the *Society* may need to disclose or account for such a liability.

18.4 Prudential risk management and associated systems and controls

Application of *PRU 1.4*

18.4.1 R Subject to *LLD 18.4.2R*, *PRU 1.4* applies to *managing agents* and to the *Society* in accordance with:

(1) for *managing agents*, *LLD 16.3.3R*; and

(2) for the *Society*, *LLD 16.3.1R*.

18.4.2 R The requirement in *PRU 1.4.18R* to take reasonable steps to ensure the establishment and maintenance of a business plan does not apply to the *Society*.

## Annex N

### Amendments to the Lloyd's sourcebook, Chapter 19

In this Annex, all the text is new and is not underlined.

- 19 Application of PRU 2 to Lloyd's
- 19.1 Section 150 of the Act (Actions for damages)
- 19.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 19.2 Calculation of capital resources requirements
- Application of PRU 2.1
- 19.2.1 R *PRU 2.1* applies to the *Society* in accordance with *LLD 16.3.1R*.
- 19.2.2 R *PRU 2.1.34R* to *PRU 2.1.35G* apply to *managing agents* in accordance with *LLD 16.3.3R*.
- 19.2.3 G *PRU 2.1.9R* requires the *Society* to ensure, in relation to each *member's insurance business*, that *capital resources* equal to or in excess of the *member's capital resources requirement (CRR)* are maintained. *PRU 2.1* sets out the overall framework of the *CRR*. *PRU 7.2* sets out the calculation of the components of the *general insurance capital requirement* and the *long-term insurance capital requirement*.
- 19.2.4 G *Managing agents* are required to calculate the *ECR* for the purposes of carrying out *syndicate ICAs* under *PRU 2.3*. As *with-profits insurance business* is not carried on through any *syndicate*, the calculation of the *with-profits insurance capital component* will not be applicable. *PRU 7.4* is not applied to Lloyd's.
- Calculation of the MCR
- 19.2.5 R For the purposes of *PRU 2.1.21R*, the *Society* must calculate the *MCR* in respect of the *general insurance business* of each *member* as the higher of:
- (1) the *member's share of the base capital resources requirement* in respect of *general insurance business* for the *members* in aggregate; and
  - (2) the *general insurance capital requirement* for the *member*, calculated according to *LLD 19.2.11R*.

- 19.2.6 R For the purposes of *LLD 19.2.5R(1)*, the *Society* must determine the *member's* share by apportioning the *base capital resources requirement* in respect of *general insurance business* for the *members* in aggregate between *members* in proportion to the result for each *member* of *LLD 19.2.11R*.
- 19.2.7 R For the purposes of *PRU 2.1.22R*, the *Society* must calculate the *MCR* in respect of the *long-term insurance business* of each *member* as the higher of:
- (1) the *member's* share of the *base capital resources requirement* in respect of *long-term insurance business* for the *members* in aggregate; and
  - (2) the sum of, for each *member*:
    - (a) the *long-term insurance capital requirement*; and
    - (b) the *resilience capital requirement*.
- 19.2.8 R For the purposes of *LLD 19.2.7R(1)*, the *Society* must determine the *member's* share by applying to the aggregate *long-term business base capital resources requirement* the ratio of the result for the *member* of *LLD 19.2.7R(2)* to the aggregate of the results of *LLD 19.2.7R(2)* for all *members*.

#### Calculation of the base capital resources requirement

- 19.2.9 R Subject to *PRU 2.1.27R*, the amount of the *base capital resources requirement* for the *members* in aggregate is:
- (1) for *general insurance business*, €3 million; and
  - (2) for *long-term insurance business*, €3 million.

#### Calculation of the general insurance capital requirement

- 19.2.10 R For the purposes of *PRU 2.1.30R*, the *Society* must calculate the *general insurance capital requirement* for the *members* in aggregate as the higher of:
- (1) the aggregate for all *members* of the higher of, for each *member*, the result of the *premiums amount* and the *claims amount*; and
  - (2) the *brought forward amount*.
- 19.2.11 R The *Society* must determine the *general insurance capital requirement* for each *member* by apportioning the result of *LLD 19.2.10R* between *members* on a fair and reasonable basis, provided that the *general insurance capital requirement* for a *member* must not be less than the higher of the result of the *premiums amount* and the *claims amount* for that *member*.
- 19.2.12 G The *Society* should calculate the *premiums amount* and the *claims amount* for each *member* on the basis of the *member's* own *general insurance business*, including *insurance business* that attaches to the reinsuring

*member* for the purposes of *PRU* following an *approved reinsurance to close* (see *LLD 17.5.3R*).

- 19.2.13 R The *Society* must calculate the *general insurance capital requirement* it would have to determine under *PRU 2.1.30R* if it were an *insurer* carrying on all the *general insurance business* carried on by its *members*, but eliminating *inter-syndicate reinsurance* (the *Society GICR*).
- 19.2.14 G For the purpose of *LLD 19.2.13R* the *Society* may make appropriate approximations, taking reasonable care to avoid underestimating the *Society GICR*.
- 19.2.15 R The *Society* must determine each *member's* share of the *Society GICR* by allocating the *Society GICR* between the *members* in proportion to the result for each *member* of *LLD 19.2.11R*.

### 19.3 Capital resources

#### Application of *PRU 2.2*

- 19.3.1 R Subject to *LLD 19.3.3R*, *LLD 19.3.4R* and *LLD 19.3.6R*, *PRU 2.2* applies to *managing agents* and to the *Society* in accordance with:
- (1) for *managing agents*, *LLD 16.3.3R*; and
  - (2) for the *Society*, *LLD 16.3.1R*.
- 19.3.2 G *PRU 2.1* sets out minimum *capital resources requirements* for a *firm* and for *Lloyd's members*. *PRU 2.2* sets out how, for the purpose of these requirements, *capital resources* are defined and measured. *PRU 2.2* applies:
- (1) to *managing agents* for their calculation of the *capital resources* managed by them in respect of each *syndicate* they manage (by reference, where there is a change in the underlying capital provision, to each *open syndicate year*); and
  - (2) to the *Society* for its calculation of:
    - (a) each *member's capital resources*; and
    - (b) its own *capital resources*.
- 19.3.3 R *PRU 2.2.15G* to *PRU 2.2.26R* (Limits on the use of different forms of capital) do not apply to *managing agents*.
- 19.3.4 R *PRU 2.2.15G* to *PRU 2.2.26R* (Limits on the use of different forms of capital) apply to the *Society* with respect to:
- (1) the *capital resources requirements* for the *members* in aggregate;

and

- (2) the aggregate *capital resources* supporting the *insurance business* of all the *members*.

19.3.5 R *PRU 2.2.72R* does not apply to the *Society* or to *managing agents*.

19.3.6 R In this Chapter *LLD 19*, "the aggregate *capital resources* supporting the *insurance business* of all the *members*" are:

- (1) the aggregate of all the *members' capital resources* calculated under *LLD 19.3.10R*; and
- (2) the *Society's capital resources* excluding *callable contributions*.

#### Calculation of capital resources

19.3.7 R Table *PRU 2.2.14R* applies with the modifications that:

- (1) (A) CORE TIER ONE CAPITAL includes *Lloyd's members' contributions* in accordance with *LLD 19.3.19R*, subject, in the case of letters of credit, guarantees and verifiable sums arising out of life assurance policies, to compliance with *LLD 18.3.3G* to *LLD 18.3.9G*; and
- (2) the *Society* may also recognise and value *callable contributions*, pursuant to *LLD 19.3.9R*.

19.3.8 G *Lloyd's member's contributions* are *admissible assets* under *LLD 19.3.19R* and include letters of credit, guarantees and verifiable sums arising out of life assurance policies held as *funds at Lloyd's*. Assets that may be valued as part of *capital resources* under *PRU* are not necessarily, however, permitted investments for *members* under the terms of any *Lloyd's trust deed*.

19.3.9 R In calculating its *capital resources*, the *Society* may, subject to *LLD 18.3.10G* to *LLD 18.3.12R*, recognise and value *callable contributions*.

19.3.10 R The *Society* must calculate each *member's capital resources* as the sum of:

- (1) a *member's* proportionate share of the *capital resources* held at *syndicate* level for each *syndicate* in which the *member* participates; and
- (2) the value of a *member's funds at Lloyd's* after deducting liabilities in compliance with *LLD 18.3.17R*.

19.3.11 R In order to comply with *PRU 2.1.9R* the *Society* must ensure at all times that:

- (1) each *member's capital resources requirement* is covered by:
  - (a) that *member's capital resources*, calculated according to *LLD*

19.3.10R; and

(b) to the extent that (a) is insufficient, by the *Society's* own *capital resources*; and

(2) the *Society GICR* is covered by the aggregate *capital resources* supporting the *insurance business* of all the *members*.

19.3.12 R For the purposes of *LLD* 19.3.11R(1)(b), the *Society* must maintain at all times *capital resources* sufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's capital resources* fall short of the *member's capital resources requirement*.

19.3.13 R The *Society* must calculate each *member's* share of the amount of *capital resources* required to comply with *PRU* 2.2.17R as the higher of:

(1) 1/3 of the *long-term insurance capital requirement* for the *members* in aggregate; and

(2) the *base capital resources requirement*;

allocated between the *members* in proportion to the result for each *member* of *LLD* 19.2.7R(2).

19.3.14 R For the purposes of *PRU* 2.2.18R, the *Society* must ensure that the aggregate *capital resources* supporting the *insurance business* of all the *members* meet the higher of:

(1) 1/3 of the *general insurance capital requirement* for the *members* in aggregate; and

(2) 1/3 of the *Society GICR*; and

(3) the *base capital resources requirement*;

with the sum of the items listed in *PRU* 2.2.18R.

19.3.15 R The *Society* must calculate each *member's* share of the amount of *capital resources* required to comply with *PRU* 2.2.18R as the higher of:

(1) 1/3 of the *general insurance capital requirement* for the *members* in aggregate; and

(2) 1/3 of the *Society GICR*; and

(3) the *base capital resources requirement*;

allocated between the *members* in proportion to the result for each *member* of *LLD* 19.2.11R.

#### Characteristics of tier one capital

19.3.16 R A *Lloyd's member's* contribution may be included in *tier one capital*

*resources* to the extent that:

- (1) the proceeds are immediately and fully available in respect of the *member's insurance business* at Lloyd's;
- (2) (except in relation to letters of credit), it complies with *PRU 2.2.29R(3)* or cannot be repaid to a *member* until all of the *member's* liabilities in respect of its *insurance business* at Lloyd's have been extinguished, covered or reinsured by an *approved reinsurance to close*;
- (3) it otherwise complies with *PRU 2.2.29R(5)* to (8).

#### Adjustments for related undertakings

- 19.3.17 R *PRU 2.2.90R* applies to the *Society* with the modification that the *Society* must also value its *insurance undertakings* in accordance with *PRU 2.2.90R*.
- 19.3.18 R If a *related undertaking* is an *insurance undertaking* which has a deficit in the *capital resources* available to cover its *capital resources requirement*, the *Society* must make provision for:
- (1) its proportionate share of that deficit; or
  - (2) in the case of a *subsidiary undertaking*, the whole of that deficit.

#### Modification of Annex 1R for Lloyd's

- 19.3.19 R In the case of *members*, *Lloyd's members' contributions* are included in *PRU 2 Annex 1R* and include:
- (1) letters of credit;
  - (2) guarantees; and
  - (3) verifiable sums arising out of life assurance policies;
- held as *funds at Lloyd's*.
- 19.3.20 G The effect of *LLD 19.3.19R* is that *Lloyd's members' contributions*, including letters of credit, guarantees and life assurance policies, are *admissible assets*.

#### 19.4 Individual capital assessment

##### Application of *PRU 2.3*

- 19.4.1 R Subject to *LLD 19.4.2R*, *PRU 2.3* applies to *managing agents* and to the *Society* in accordance with:



- (1) for *managing agents*, LLD 16.3.3R; and
- (2) for the *Society*, LLD 16.3.1R.

19.4.2 R *Managing agents* must carry out assessments of capital adequacy for each *syndicate* they manage by reference to all *open syndicate years* taken together.

Assessment of adequacy of capital resources for syndicates and members

19.4.3 G *PRU 1.2* requires *firms* to carry out assessments of the adequacy of their financial resources. Financial resources include *capital resources* and liquidity resources. *PRU 5* contains *guidance* on liquidity stress tests. *Managing agents* should manage *liquidity risk* affecting each *syndicate* they manage and the *Society* should manage *liquidity risk* affecting *funds at Lloyd's* and *central assets*, including the risk that it cannot make liquid assets available to support *syndicates* on a timely basis.

19.4.4 G *PRU 2* sets out provisions that deal specifically with the adequacy of that part of a *firm's* financial resources that consists of *capital resources*. *PRU 2.3* sets out *guidance* on how *firms* should assess the adequacy of their *capital resources*. The relevant requirements for Lloyd's are that:

- (1) the *Society* should carry out regular assessments of the adequacy of the *capital resources* available to support each *member's insurance business*; and
- (2) *managing agents* should carry out regular assessments of the adequacy of *capital resources* held at *syndicate* level in respect of the *insurance business* carried on through each *syndicate*.

19.4.5 G Responsibility for:

- (1) managing the risks associated with the *insurance business*; and
- (2) holding the *capital resources* that support those risks;

is divided between *managing agents* and the *Society*. To clarify the respective responsibilities of *managing agents* and the *Society* for ensuring the adequacy of financial resources, the *FSA* distinguishes between the *managing agents'* responsibility to carry out capital adequacy assessments for each *syndicate* that they manage, and the *Society's* responsibility to carry out an assessment for each *member*.

19.4.6 R In carrying out capital adequacy assessments in respect of the *insurance business* carried on through each *syndicate* (the *syndicate ICA*), *managing agents* must consider the risks, controls and the financial resources relevant to each *syndicate*.

19.4.7 R When carrying out the *syndicate ICA*, *managing agents* must not take into account risks to which a *member* may be exposed or controls from which a

*member* may benefit:

- (1) because that *member* carries on *insurance business* through another *syndicate* or more than one *syndicate year* (whether or not managed by the same *managing agent*); or
- (2) because that *member's* financial resources include *funds at Lloyd's* or *central assets*.

19.4.8 R The *Society* must have regard to *syndicate ICAs* in arriving at its own capital assessment for each *member*.

19.4.9 G In assessing the adequacy of the *capital resources* supporting the *insurance business* of each *member*, the *Society* should consider the risks, controls and financial resources relevant to the totality of the *member's insurance business*, including:

- (1) the adequacy of *syndicate ICAs*;
- (2) the *member's* share of *syndicate ICAs*;
- (3) adjustments in respect of risks and controls relating to *funds at Lloyd's, central assets* and the interaction of risks underwritten by the *member* through different *syndicates* and in respect of different *syndicate years*; and
- (4) the ongoing validity of any relevant assumptions it makes.

19.4.10 G The *Society* should be able to justify any reliance it places on a *syndicate ICA*, for example by being able to demonstrate that it has carried out appropriate checks.

19.4.11 G In taking account of a *syndicate ICA* under *LLD 19.4.8R*:

- (1) if the *Society* considers a *syndicate ICA* to be adequate, it should use the *managing agent's* risk and capital assessments in carrying out its individual capital assessment in relation to any *member* of that *syndicate*, or it should be able to justify why it will not; and
- (2) if the *Society* considers a *syndicate ICA* to be less than adequate, the *Society* should increase the *syndicate ICA* so that it is adequate for the purpose of carrying out its individual capital assessment in relation to the *members* of that *syndicate*.

19.4.12 G The assessment of capital adequacy for a *member* will rarely equal the proportionate share of a *syndicate ICA* (or sum of those shares, where the *member* participates on more than one *syndicate*) as attributed to that *member*, because, in determining the capital assessments for each *member*, the *Society* may make adjustments to take account of:

- (1) risks and controls associated with *funds at Lloyd's* and *central assets*,

- which can increase the *member's* individual capital assessment;
- (2) diversification effects, including as a result of *members'* participations on more than one *syndicate year*, which can reduce the *member's* individual capital assessment; and
- (3) its own assessment of *syndicate* risks, which can be higher than the *managing agent's* and so increase the *member's* individual capital assessment.

The balancing amount

- 19.4.13 G *Capital resources* to meet each *syndicate ICA* could be:
- (1) held within a *syndicate* and managed by the *managing agent*; or
  - (2) held and managed by the *Society*; or
  - (3) not needed in full, because of effects such as diversification that the *Society* takes into account.
- 19.4.14 G The *balancing amount* is a function of the relationship between the *syndicate ICA* and the amount of assets held within the *syndicate*. As illustrations:
- (1) if the *syndicate* holds no *capital resources* (but its liabilities are fully covered by relevant assets), the *balancing amount* equals the *syndicate ICA* (as there are no *capital resources* at *syndicate* level, all the *capital resources* must be held as *funds at Lloyd's* or *central assets*);
  - (2) if *capital resources* held at *syndicate* level are negative (i.e. if relevant assets do not fully cover liabilities for the *syndicate*), the *balancing amount* should be higher than the *syndicate ICA* by an amount corresponding to the negative *capital resources* held by *managing agents* on behalf of the *syndicate*; and
  - (3) conversely, if a *syndicate* holds positive *capital resources* for the *syndicate*, the *balancing amount* should be lower than the *syndicate ICA* by a corresponding amount.
- 19.4.15 R *Managing agents* must periodically notify the *Society* of the *syndicate ICA* and the *balancing amount* in respect of each *syndicate*.
- 19.4.16 R For the purpose of assessing the adequacy of *capital resources* held as *funds at Lloyd's* and *central assets*, the *Society* must have regard to *balancing amounts* notified to it by *managing agents*.
- 19.4.17 R After notification of a *balancing amount* by a *managing agent*, the *Society* must:
- (1) confirm to the *managing agent* that *capital resources* held as *funds*

*at Lloyd's and central assets* are adequate to support the *balancing amount*; or

(2) notify the *managing agent* that it cannot give that confirmation.

- 19.4.18 G *Managing agents* should submit *syndicate ICAs* and notify *balancing amounts* to the *Society* as part of the annual capital-setting process at Lloyd's. The submission of the *syndicate ICA* and notification of the *balancing amount* should be made in good time for the *Society* to review them and place appropriate reliance on them when it determines the capital assessments for each *member*.
- 19.4.19 G When communicating the *syndicate ICA* and *balancing amount* for each *syndicate* to the *Society*, *managing agents* should agree with the *Society* an allocation of the *syndicate ICA* between *syndicate years*. The purpose of the allocation is to ensure that there is an appropriate matching of assets to risk and liabilities and an equitable treatment between the *members* reflecting the provision of capital in each *syndicate year*.
- 19.4.20 G Under LLD 19.4.23R, a *managing agent* has a continuing obligation to communicate to the *Society* a revised *syndicate ICA* and, where appropriate, a revised *balancing amount*, if it considers that the *syndicate ICA* and *balancing amount* communicated in the capital-setting process are no longer adequate in the light of the risks to which the *syndicate* business is exposed.

#### Monitoring of capital resources

- 19.4.21 G For the purposes of complying with their obligations under PRU, *managing agents* may assume that any *balancing amount* confirmed by the *Society* under LLD 19.4.17R is supported by *capital resources* held as *funds at Lloyd's and central assets*.
- 19.4.22 G Following initial confirmation of a *balancing amount* by the *Society*, assumptions made about risks and controls may change or risks may crystallise, affecting:
- (1) the *syndicate ICA* (and hence, possibly, the *balancing amount*); or
  - (2) the relationship between a *syndicate ICA* and a *member's* individual capital assessment; or
  - (3) the amount of *capital resources* available.
- 19.4.23 R If a *managing agent* has, at any time, a significant doubt about the adequacy of a *syndicate ICA* or *balancing amount* with respect to *syndicate* risks and controls, it must notify the *Society* immediately.
- 19.4.24 R If the *Society* has, at any time, a significant doubt about the adequacy of any *member's capital resources* held by it in support of any *balancing amount*, it must notify the relevant *managing agent* immediately.

## Annex O

### Amendments to the Lloyd's sourcebook, Chapter 20

In this Annex, all the text is new and is not underlined.

- 20 Application of PRU 3 to Lloyd's
- 20.1 Section 150 of the Act (Actions for damages)
  - 20.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 20.2 Credit risk management systems and controls
  - Application of PRU 3.1
  - 20.2.1 R Subject to *LLD 20.2.2R*, *PRU 3.1* applies to *managing agents* and to the *Society* in accordance with:
    - (1) for *managing agents*, *LLD 16.3.3R*; and
    - (2) for the *Society*, *LLD 16.3.1R*.
  - 20.2.2 R In accordance with *LLD 18.4.2R*, the *rules* and *guidance* in *PRU 3.1* relating to the establishment and maintenance of a business plan do not apply to the *Society*.
- 20.3 Credit risk in insurance funds
  - Application of PRU 3.2
  - 20.3.1 R Subject to *LLD 20.3.2R*, *PRU 3.2* applies to *managing agents* and to the *Society* in accordance with:
    - (1) for *managing agents*, *LLD 16.3.3R*; and
    - (2) for the *Society*, *LLD 16.3.1R*.
  - 20.3.2 R *PRU 3.2.23R* to *PRU 3.2.32G* (Large exposure calculation for reinsurance exposures) do not apply to the *Society*.
  - Overall limitation of credit risk
  - 20.3.3 G For Lloyd's, *counterparty* exposure is:

- (1) for *managing agents*, the amount by which the net assets managed by or under the direction of a *managing agent* in respect of a *syndicate* together with any relevant *balancing amount* would decrease if the *counterparty* were to default;
- (2) for the *Society*, the amount by which its net assets (which include those of its *subsidiary undertakings*) would decrease if the *counterparty* were to default; and
- (3) for the *Society's* management of each *member's funds at Lloyd's*, the amount by which the *member's* net assets would decrease if the *counterparty* were to default.

Large exposures

- 20.3.4 R For the purposes of *PRU 3.2.20R* (Large exposure limits: counterparty exposure and asset exposure), the *Society* may determine the exposure to any letters of credit, guarantees or *members' life assurance policies* as an exposure of the *members* in aggregate.
- 20.3.5 R For the purposes of *PRU 3.2.22R* (Large exposure limits: market risk and counterparty limits), the *Society* must calculate the amount of and deduct from *capital resources*:
- (1) an exposure (expressed as a percentage of the relevant *member's capital resources* held as *funds at Lloyd's*), other than to the assets identified in *LLD 20.3.5R(2)(a) to (c)*, of a *member's capital resources* held as *funds at Lloyd's* to a *counterparty*, in excess of the limits in *PRU 3.2.22R*;
  - (2) an exposure in excess of 20% (expressed as a percentage of the aggregate of *capital resources* held as *funds at Lloyd's*) of the aggregate of *capital resources* held as *funds at Lloyd's* to a single issuer of:
    - (a) letters of credit;
    - (b) guarantees; or
    - (c) *members' life assurance policies*;
  - (3) an exposure of its own to a *counterparty*, in excess of the limits in *PRU 3.2.22R*, expressed as a percentage of the *Society's* own assets.
- 20.3.6 R For the purposes of *PRU 3.2.22R* (Large exposure limits: market risk and counterparty limits), *managing agents* must calculate the amount of and deduct from *capital resources* an exposure (expressed as a percentage of the *admissible assets* held in respect of the relevant *syndicate*) of *admissible assets* held in respect of a *syndicate* to a *counterparty* in excess of the limits in *PRU 3.2.22R*.
- 20.3.7 R If the exposures of *capital resources* held as *funds at Lloyd's* for *members* in

the aggregate do not exceed the limits in *PRU 3.2.22R(3)(c)*, then, for each *individual member*, that limit may be replaced by 10%.

Exposures excluded from the large exposure limits

20.3.8 R For *managing agents*, in *PRU 3.2.33R* and *PRU 3.2.35R*, references to an exposure do not include exposure arising from *balancing amounts*.

20.4 Asset-related Capital Requirement

Application of *PRU 3.3*

20.4.1 R *PRU 3.3* applies to *managing agents* and to the *Society* in accordance with:

(1) for *managing agents*, *LLD 16.3.3R*; and

(2) for the *Society*, *LLD 16.3.1R*.

20.4.2 G This chapter applies to the *Society* for each *member*, including the capital charge relating to *central assets*, to the extent that those assets are held to support a particular *member*.

## Annex P

### Amendments to the Lloyd's sourcebook, Chapter 21

In this Annex, all the text is new and is not underlined.

- 21 Application of PRU 4 to Lloyd's
- 21.1 Section 150 of the Act (Actions for damages)
- 21.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 21.2 Market risk management systems and controls
- Application of PRU 4.1
- 21.2.1 R *PRU 4.1* applies to *managing agents* and to the *Society* in accordance with:
- (1) for *managing agents*, *LLD 16.3.3R*; and
- (2) for the *Society*, *LLD 16.3.1R*.
- 21.2.2 R In accordance with *LLD 18.4.2R*, the *rules* and *guidance* in *PRU 4.1* relating to the establishment and maintenance of a business plan do not apply to the *Society*.
- 21.3 Market risk in insurance
- Application of PRU 4.2
- 21.3.1 R *PRU 4.2* applies to *managing agents* and to the *Society* in accordance with:
- (1) for *managing agents*, *LLD 16.3.3R*, subject to *LLD 21.3.4R* below; and
- (2) for the *Society*, *LLD 16.3.1R*.
- Resilience capital requirement (applicable to long-term business only)
- 21.3.2 R *Managing agents* must calculate the amount of the *resilience capital requirement* for the *long-term insurance business* carried on through the *syndicates* they manage.
- 21.3.3 R The *Society* must determine the *resilience capital requirement* for the



*insurance business* of each *member* under *PRU 4.2.10R* as the *member's* proportionate share of the *resilience capital requirement* calculated by the *managing agent* for the *long-term insurance business* carried on through the *syndicate*.

#### Currency risk: matching of assets and liabilities

- 21.3.4 R For the purposes of *PRU 4.2.53R*, a *managing agent* must ensure that:
- (1) *syndicate* liabilities are covered by matching *syndicate assets* as required by *PRU 4.2.53R*; or that
  - (2) it immediately notifies to the *Society* the nature and extent of any *syndicate* liabilities not covered by matching assets under (1).
- 21.3.5 G Notwithstanding the terms of *PRU 4.2.53R*, a *managing agent* may comply with *PRU 4.2.53R* by notifying unmatched currency liabilities to the *Society*.
- 21.3.6 R On receipt of a notification by a *managing agent* under *LLD 21.3.4R(2)*, the *Society* must ensure that the liabilities in respect of the *insurance business* of the *members* in aggregate are covered with matching assets complying with *PRU 4.2.53R*.
- 21.3.7 G The *Society* should consider the need to cover the unmatched currency liabilities notified under *LLD 21.3.4R(2)* with assets in the same currency held as *funds at Lloyd's* for any relevant *member* or, if necessary, with *central assets* meeting the currency matching requirements.

#### 21.4 Derivatives in insurance

##### Application of *PRU 4.3*

- 21.4.1 R *PRU 4.3* applies to *managing agents* and to the *Society* in accordance with:
- (1) for *managing agents*, *LLD 16.3.3R*; and
  - (2) for the *Society*, *LLD 16.3.1R*.

## Annex Q

### Amendments to the Lloyd's sourcebook, Chapter 22

In this Annex, all the text is new and is not underlined.

- 22 Application of PRU 5 to Lloyd's
- 22.1 Section 150 of the Act (Actions for damages)
- 22.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 22.2 Liquidity risk systems and controls
  - Application of PRU 5.1
  - 22.2.1 R *PRU 5.1* applies to *managing agents* and to the *Society* in accordance with:
    - (1) for *managing agents*, *LLD 16.3.3R*; and
    - (2) for the *Society*, *LLD 16.3.1R*.
  - 22.2.2 R In accordance with *LLD 18.4.2R*, the *rules* and *guidance* in *PRU 5.1* relating to the establishment and maintenance of a business plan do not apply to the *Society*.

## Annex R

### Amendments to the Lloyd's sourcebook, Chapter 23

In this Annex, all the text is new and is not underlined.

- 23 Application of PRU 6 to Lloyd's
- 23.1 Section 150 of the Act (Actions for damages)
- 23.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 23.2 Operational risk: prudential systems and controls
- Application of PRU 6.1
- 23.2.1 R *PRU 6.1* applies to *managing agents* and to the *Society* in accordance with:
  - (1) for *managing agents*, *LLD 16.3.3R*; and
  - (2) for the *Society*, *LLD 16.3.1R*.
- 23.2.2 R In accordance with *LLD 18.4.2R*, the *rules* and *guidance* in *PRU 6.1* relating to the establishment and maintenance of a business plan do not apply to the *Society*.

## Annex S

### Amendments to the Lloyd's sourcebook, Chapter 24

In this Annex, all the text is new and is not underlined.

- 24 Application of PRU 7 to Lloyd's
- 24.1 Section 150 of the Act (Actions for damages)
- 24.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 24.2 Insurance risk systems and controls
- Application of PRU 7.1
- 24.2.1 R *PRU 7.1* applies to *managing agents* in accordance with *LLD 16.3.3R*.
- 24.3 Capital resources requirements and technical provisions for insurance business
- Application of PRU 7.2
- 24.3.1 R *PRU 7.2* applies to the *Society* in accordance with *LLD 16.3.1R*.
- 24.3.2 R The following *rules* and *guidance* apply to *managing agents* in accordance with *LLD 16.3.3R*:
- (1) *PRU 7.2.13R* to *PRU 7.2.20G* (except *PRU 7.2.13R(1)*);
- (2) *PRU 7.2.42R* to *PRU 7.2.43G*; and
- (3) *PRU 7.2.74G* to *PRU 7.2.80R*.
- Establishing technical provisions
- 24.3.3 G *Managing agents* are advised by the *syndicate actuary* in relation to the *long-term insurance business* carried on through *long-term insurance business syndicates*. The standards and guidance issued by the Faculty and Institute of Actuaries to assist *syndicate actuaries* are important sources of evidence as to generally accepted actuarial best practice, as referred to in *PRU 7.2.16R(1)*.
- General insurance capital requirement
- 24.3.4 G *PRU 2.1.30R* and *LLD 19.3.10R* to *LLD 19.3.12G* set out the calculation of

the *general insurance capital requirement* for Lloyd's.

- 24.3.5 R The *Society* must calculate the *brought forward amount* for the *members* in aggregate in accordance with *PRU 7.2.51R*, using the result of *LLD 19.2.6R* for the prior *financial year* and the aggregate of all *members' technical provisions* for the relevant periods.

Accounting for premiums and claims

- 24.3.6 R For the purposes of *PRU 7.2.66R* and further to that *rule*, in the case of Lloyd's *members*, amounts of *premiums* and *claims* must be adjusted for *approved reinsurance to close* to exclude any amount included in, or adjustment made to, *premiums* and *claims* to reflect the consideration for an *approved reinsurance to close*.

- 24.3.7 G *Members* of Lloyd's can effect contracts of *approved reinsurance to close* with other *members* in accordance with *LLD 17.5*. For the purposes of *PRU* as it applies to Lloyd's, the capital requirement relating to business transacted through an *approved reinsurance to close* is calculated for the reinsuring and not the reinsured *member* under the contract.

## 24.4 Mathematical reserves

Application of *PRU 7.3*

- 24.4.1 R *PRU 7.3* applies to *managing agents* in accordance with *LLD 16.3.3R*.

Approved reinsurance to close

- 24.4.2 R In respect of business that has been subject to an *approved reinsurance to close*, *managing agents* must calculate *mathematical reserves* (before and after deduction of reinsurance cessions) for the reinsuring and not for the reinsured *member*.

## 24.5 Equalisation provisions

Application of *PRU 7.5*

- 24.5.1 R *PRU 7.5* applies to the *Society* in accordance with *LLD 16.3.1R*:

- (1) with the modification set out in *LLD 24.5.2R*; and
- (2) except *PRU 7.5.11R* to *PRU 7.5.37G*.

- 24.5.2 R The *Society* must calculate a *credit equalisation provision* for the aggregate *insurance business* of all *members*; it is not required to calculate a *credit equalisation provision* separately for the business of each *member*.

24.5.3 R The *Society* must allocate the result of *LLD* 24.5.2R between itself and each of the *members* on a fair and reasonable basis.

## 24.6 Internal-contagion risk

### Application of PRU 7.6

24.6.1 R *PRU* 7.6 applies to *managing agents* and to the *Society* in accordance with:

- (1) for *managing agents*, *LLD* 16.3.3R; and
- (2) for the *Society*, *LLD* 16.3.1R.

### Restriction of business to insurance

24.6.2 R The *Society* and *managing agents* must take all reasonable steps to ensure that:

- (1) a *corporate member* does not carry on any commercial business other than *insurance business* and activities arising directly from that business; and
- (2) *individual members* do not, in their capacity as *underwriting members*, carry on any commercial business other than *insurance business* and activities arising directly from that business.

### Syndicates not to carry on both general and long-term business

24.6.3 R A *managing agent* must not permit both *general insurance business* and *long-term insurance business* to be carried on together through any *syndicate* managed by it.

24.6.4 G *PRU* 7.6.17G contains *guidance* setting out the *FSA* policy (reflecting requirements of the *Insurance Directives*) in relation to the carrying on together of *general* and *long-term insurance business*.

## Annex T

### Amendments to the Lloyd's sourcebook, Chapter 25

In this Annex, all the text is new and is not underlined.

- 25 Regulatory intervention points for Lloyd's
- 25.1 Section 150 of the Act (Actions for damages)
- 25.1.1 R A contravention of the *rules* in this chapter does not give rise to a right of action by a *private person* under section 150 of the *Act* (Actions for damages) and each of those *rules* is specified under section 150(2) of the *Act* as a provision giving rise to no such right of action.
- 25.2 Application
- 25.2.1 R The *rules* and *guidance* in *SUP App 2* apply to the *Society*:
- (1) with the modifications set out in *LLD 25.3.1R* to *LLD 25.8.1G*; but
  - (2) except *SUP App 2.8.1R* to *SUP App 2.8.5G*, *SUP App 2.9.1G*, *SUP App 2.10.1G*, *SUP App 2.12.1R(2)(a)*, *SUP App 2.12.2G* and *SUP App 2.12.7R*.
- 25.3 Interpretation
- 25.3.1 R For the purpose of this Chapter *LLD 25* and the application of *SUP App 2* to the *Society*:
- (1) "capital resources", as the context requires:
    - (a) in relation to the *Society's* own capital resources, means its own *capital resources* calculated in accordance with *PRU 2.2.12R*;
    - (b) in relation to a *member's* capital resources, means the *member's capital resources* calculated in accordance with *LLD 19.3.10R*;
    - (c) in relation to the aggregate capital resources of the *Society* and the *members* supporting the *insurance business* of the *members*, means the aggregate of the *capital resources* in (1)(a) and (b) but excluding the *Society's callable contributions*.
  - (2) "guarantee fund":
    - (a) in relation to the *general insurance business* carried on by *members*, means the amount of capital resources required in

order to comply with *PRU 2.2.18R*, *LLD 19.3.4R* and *LLD 19.3.14R*; and the "*member's share of the guarantee fund*" for *general insurance business* means the result of the calculation set out in *LLD 19.3.15R*;

(b) in relation to the *long-term insurance business* carried on by *members*, means the amount of capital resources required in order to comply with *PRU 2.2.17R* and *LLD 19.3.4R*; and the "*member's share of the guarantee fund*" for *long-term insurance business* means the result of the calculation set out in *LLD 19.3.13R*;

(3) "required margin of solvency":

(a) in relation to the *general insurance business* carried on by *members*, means the higher of the *Society GICR* and the *general insurance capital requirement* for the *members* in aggregate; and

(b) in relation to the *long-term insurance business* carried on by *members*, means the *long-term insurance capital requirement* for the *members* in aggregate.

25.3.2 G The calculations of the *base capital resources requirement*, the *long-term insurance capital requirement* and the *general insurance capital requirement* for *members* and for the *members* in aggregate are set out in *PRU 2.1* and in *LLD 19*. *LLD 19.2.13R* requires the *Society* to calculate the *Society GICR*. *PRU 2.2.17R* and *PRU 2.2.18R*, as applied to Lloyd's and modified by *LLD 19.3.4R* and *LLD 19.3.13R* to *LLD 19.3.15R*, contain requirements for the calculation of the guarantee fund and the *member's share of the guarantee fund*.

25.4 Purpose

25.4.1 G Under *PRU* and *LLD 19* the *Society* must, separately in respect of the *general insurance business* and *long-term insurance business* carried on by *members*, ensure:

(1) its own capital resources are sufficient to cover the aggregate of, for each *member*, any amount by which the *member's* capital resources are inadequate to meet the *member's CRR*; and

(2) that the aggregate capital resources of the *Society* and the *members* supporting the *insurance business* of the *members* comply with the requirements of *PRU 2.2.15G* to *PRU 2.2.26R*.

The *PRU* provisions as applied to Lloyd's reflect requirements under the *Insurance Directives*.



- 25.4.2 G Regulatory intervention is triggered under *SUP App 2* if:
- (1) the capital resources of the *Society* are insufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the guarantee fund (the guarantee fund required by Article 17, *First Non-Life Directive* and Article 29, *Consolidated Life Directive*);
  - (2) the capital resources of the *Society* are insufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the required margin of solvency (the solvency margin required by Article 16a, *First Non-Life Directive* and Article 28, *Consolidated Life Directive*);
  - (3) the capital resources of the *Society* and of each of the *members* supporting their own *insurance business*, in the aggregate, no longer comply with *PRU 2.2.16R* and *PRU 2.2.24R*. *PRU 2.2.16R* and *PRU 2.2.24R* prescribe limits on the forms of capital resources which a firm must hold. (For Lloyd's, the *Society* must comply with *PRU 2.2.16R* and *PRU 2.2.24R* in relation to the aggregate of its own capital resources and the capital resources of the *members* supporting their own business: see *LLD 19.3.4R*);
  - (4) the capital resources of the *Society* are insufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the *CRR* for the *members* in aggregate.
- 25.4.3 G *PRU* requires the *Society* to ensure that the financial resources supporting the *insurance business* of each *member* are adequate at all times. Under *PRU 2.3.13G*, the *FSA* may give individual capital *guidance* to the *Society* stating the amount and quality of capital resources that it considers ought to be held to meet *PRU 1.2.22R*. If the *Society's* own capital resources fall below individual capital *guidance* given to the *Society* in respect of those resources, the *FSA* may take further action as set out in *SUP App 2.7.1.G* to *SUP App 2.7.5G*.
- 25.5 Capital resources below guarantee fund
- 25.5.1 R For the purposes of *SUP App 2.4.1R* and *SUP App 2.4.2G*, capital resources will have fallen below the guarantee fund if the *Society's* own capital resources are such that they are no longer sufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the guarantee fund.
- 25.6 Capital resources below required margin of solvency

25.6.1 R For the purposes of *SUP* App 2.5.1R to *SUP* App 2.5.3R, capital resources will be such that they no longer equal or exceed the required solvency margin if the *Society's* own capital resources are insufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the required solvency margin.

25.7 Capital resources below capital resources requirement

25.7.1 R For the purposes of *SUP* App 2.6.1R, capital resources will have fallen below the *capital resources requirement* if the *Society's* own capital resources are insufficient to meet the aggregate of, for each *member*, the amount, if any, by which the *member's* capital resources fall short of the *member's* share of the *capital resources requirement* for the *members* in aggregate.

25.8 Capital resources below the level of individual capital guidance

25.8.1 G For the purposes of *SUP* App 2.7.1G to *SUP* App 2.7.5G, capital resources will have fallen below the level of individual capital *guidance* if the *Society's* own capital resources have fallen below the level advised in individual capital *guidance* given to the *Society* in respect of those capital resources.

## Annex U

### Part 1

#### Amendments to the Supervision manual, Chapter 3

In this Part, underlining indicates new text and striking through indicates deleted text.

### 3 Auditors

#### 3.1 Application

##### 3.1.2 R Table: Applicable sections

...			
(6)	<i>Insurer, the Society of Lloyd's, underwriting agent or members' adviser (Note 5)</i>	<i>SUP 3.1 – SUP 3.7</i>	<i>SUP 3.1, SUP 3.2, SUP 3.8</i>
...			
	<u>Note (5) = In row (6):</u>		
(a)	<u>SUP 3.1 – SUP 3.7 applies to a managing agent in respect of its own business and in respect of the insurance business of each syndicate which it manages; and</u>		
(b)	<u>SUP 3.1, SUP 3.2 and SUP 3.8 apply to the auditors of a managing agent and the auditors of the insurance business of each syndicate which the managing agent manages.</u>		

...

3.1.9 G A firm which is a bank, building society, friendly society or other insurer, investment management firm, personal investment firm, securities and futures firm, ~~or the Society of Lloyd's;~~ or a Lloyd's managing agent in respect of each syndicate managed by it, should see the Interim Prudential sourcebooks for further provisions as set out in SUP 3.1.10G. For the categorisations employed in SUP 3.1.2R and SUP 3.1.10G see SUP App 1.

##### 3.1.10 G Table: other relevant sections of the handbook

....	
<i>Investment management firm, personal investment firm, securities and futures firm</i>	<i>IPRU (INV)</i>
<i>Society of Lloyd's <u>and Lloyd's managing agents</u></i>	<i>LLD</i>

Lloyd's

Enabling provision and application

- 3.1.11 G The *insurance market direction* in this chapter is given under section 316(1) of the *Act* (Direction by Authority) and applies to *members*.

Purpose

- 3.1.12 G The *insurance market direction* in this chapter is intended to enable the *rules* in *SUP 3* and *SUP 4* to be applied to a *managing agent* in respect of the *insurance business* of each *syndicate* which it manages.

Insurance market direction on rules concerning auditors and actuaries

- 3.1.13 D (1) With effect from 1 January 2005, Part XXII of the *Act* (Auditors and Actuaries) applies to the carrying on of *insurance business* by *members* as modified by paragraph (3).

(2) For the purposes of (1) "*insurance business*" means the *regulated activities of effecting or carrying out contracts of insurance* written at Lloyd's.

(3) Regulations made by the Treasury under section 342(5) and section 343(5) of Part XXII of the *Act* apply only to *actuaries* appointed by a *managing agent* in respect of the *insurance business* of a *syndicate*, in relation to the *long-term insurance business* of that *syndicate*.

(4) In Part XXII of the *Act* (Auditors and Actuaries) as applied by this *insurance market direction*:

(a) a reference to an auditor of an *authorised person* is to be read as including an auditor appointed by a *managing agent* in respect of the *insurance business* of a *syndicate*; and

(b) a reference to an *actuary* acting for an *authorised person* is to be read as including an *actuary* appointed by a *managing agent* in respect of the *insurance business* of a *syndicate*.

- 3.1.14 G Part XXII (Auditors and Actuaries) is a *core provision* mentioned in section 317(1) of the *Act* (The core provisions).

- 3.1.15 G Section 317(2) of the *Act* (The core provisions) provides that references in an applied *core provision* to an *authorised person* are to be read as references to a *person* in the class to which the *insurance market direction* applies. The effect of this, and of the *insurance market direction* set out at *SUP 3.1.13D*, is that Part XXII of the *Act* (Auditors and Actuaries), applies also to auditors and *actuaries* who

are appointed to report on the underwriting business of *members*. Part XXII is modified in its application to *members* by paragraph (3) of SUP 3.1.13D with the effect that the regulations made under sections 342(5) and 343(5) of the *Act* relating to communications by *actuaries* will only apply where the *actuary* is appointed to evaluate the *long-term insurance business* of the *syndicate*. The regulations made under sections 342(5) and 343(5) in relation to communications by auditors will apply in relation to both *general insurance business* and *long-term insurance business*.

3.1.16 G SUP 3.3 sets out rules the effect of which is to require a *managing agent* to appoint an auditor in respect of its own business and the *insurance business* of each *syndicate* which it manages.

3.1.17 G References in SUP 3, as applied by SUP 3.1.2R, to a *firm* include, where appropriate:

(1) a *managing agent*; and

(2) one or more *members* carrying on *insurance business* at Lloyd's through a *syndicate*.

and references to an *actuary* of a *firm* should be read accordingly.

3.1.18 G SUP 4.6 sets out rules the effect of which is to require a *managing agent* to appoint an *actuary* in respect of the *insurance business* of each *syndicate* which it manages.

...

3.3 Appointment of auditors

...

The Society of Lloyds

3.3.4 D ~~[deleted]~~

~~With a view to achieving the objectives of promoting confidence in the market at Lloyd's and protecting the interests of *policyholders* and potential *policyholders*, the *Society* is directed under section 318 of the *Act* (Exercise of powers through Council), to take reasonable steps to ensure that:~~

~~(1) every *managing agent* appoints an auditor for every *syndicate* which it manages; and~~

~~(2) the auditor of every *syndicate* has the skill, resources and experience required to perform his duties.~~

3.3.5 R ~~(1) [deleted]~~

~~Paragraph (2) applies if the notifications required by SUP 3.3.2~~

~~R (2) or (5) are within the scope of any arrangements made by the FSA with the Society of Lloyd's under paragraph 6 (2) of Schedule 1 to the Act.~~

~~(2) An underwriting agent must submit a notification in (1) to the Society of Lloyd's rather than to the FSA.~~

3.3.6 G ~~[deleted]~~

~~An underwriting agent should see SUP 15.7.13G and SUP 15.7.14G for further guidance on the arrangements in SUP 3.3.5R.~~

...

3.7 Notification of matters raised by an auditor

...

3.7.3 G ~~[deleted]~~

~~An underwriting agent should submit any notifications under this section in accordance with the arrangements made between the FSA and the Society of Lloyd's. For guidance on those arrangements see SUP 15.7.13G and SUP 15.7.14G.~~

...

3.8 Rights and duties of auditors

...

3.8.10 G Auditors are subject to regulations made by the Treasury under sections 342(5) and 343(5) of the *Act* (Information given by auditor or actuary to the *FSA*). These regulations oblige auditors to report certain matters to the *FSA*. Sections 342(3) and 343(3) of the *Act* provide that an auditor does not contravene any duty by giving information or expressing an opinion to the *FSA*, if he is acting in good faith and he reasonably believes that the information or opinion is relevant to any functions of the *FSA*. These provisions continue to have effect after the end of the auditor's term of appointment. In relation to Lloyd's, an effect of the *insurance market direction* set out at SUP 3.1.13D is that sections 342(5) and 343(5) of the *Act* (Information given by an auditor or actuary to the *Authority*) apply also to auditors appointed to report on the *insurance business of members*.

...

3.8.13 R ~~[deleted]~~

~~(1) An auditor of an underwriting agent must submit a notification under SUP 3.8.11R or SUP 3.8.12R to the Society of Lloyd's~~

rather than to the *FSA* if (2) applies.

- (2) ~~This paragraph applies if the notification is within the scope of any arrangements made by the *FSA* with the *Society of Lloyd's* under paragraph 6(2) of Schedule 1 to the *Act*.~~

3.8.14 G [deleted]

~~For *guidance* on these arrangements, see *SUP* 15.7.13G and *SUP* 15.7.14G. Notification to the *Society* acting on behalf of the *FSA* in accordance with *SUP* 3.8.13R also satisfies the obligation to notify the *FSA* in accordance with section 344 of the *Act* (Duty of auditor or actuary resigning etc. to give notice).~~

...

## Annex U

### Part 2

#### Amendments to the Supervision manual, Chapter 4

In this Part, underlining indicates new text and striking through indicates deleted text.

#### 4 Actuaries

##### 4.1 Application

...

- 4.1.2 G This chapter applies to *long-term insurers* (including *friendly societies*) and other *friendly societies* and to the *Society of Lloyd's* and *managing agents* at Lloyd's ~~This chapter does not apply to the *Society of Lloyd's* or to Lloyd's *underwriting agents*. Requirements dealing with the appointment and duties of *actuaries* in relation to Lloyd's *insurance business* are contained in *LLD*.~~ This chapter does not apply to *actuaries* advising the auditors of *long-term insurers* under *IPRU(INS)* 9.35(1A) or *IPRU(FSOC)* 5.11(2A), as they are not appointed to act on behalf of the *firm*.

##### 4.1.3 R Table: applicable sections

(1) Category of firm	(2) Applicable sections
...	
<u>(3) A Lloyd's <i>managing agent</i>, in respect of each <i>syndicate</i> it manages</u>	<u><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6</u>
<u>(4) The <i>Society of Lloyd's</i></u>	<u><i>SUP</i> 4.1, <i>SUP</i> 4.2, <i>SUP</i> 4.5, <i>SUP</i> 4.6</u>

...

##### 4.2 Purpose

...

- 4.2.2 G This chapter...purpose of this chapter is to ensure that:

- (1) *long-term insurers* (other than...
- (2) other *friendly societies* carrying on...the liabilities of that



business; and

- (3) managing agents of Lloyd's syndicates employ or use an actuary of appropriate seniority and experience to evaluate the liabilities associated with insurance business carried on at Lloyd's.

...

4.5.7 G .....These provisions continue to have effect after the end of the actuary's term of appointment. In relation to Lloyd's, an effect of the insurance market direction set out at SUP 3.1.13D is that sections 342(5) and 343(5) of the Act (Information given by auditor or actuary to the FSA) apply also to actuaries who are appointed to evaluate the long-term insurance business of a syndicate.

...

4.6 Lloyd's

Appointment of the Lloyd's actuary and syndicate actuaries

4.6.1 R The Society must:

- (1) appoint an actuary to perform the Lloyd's actuary function;
- (2) notify the FSA, without delay, when it is aware that a vacancy in the office of Lloyd's actuary will arise or has arisen, giving the reason for the vacancy;
- (3) appoint an actuary to fill any vacancy in the office of Lloyd's actuary that has arisen; and
- (4) ensure that the replacement actuary can take up office at the time the vacancy arises or as soon as reasonably practicable after that.

4.6.2 G The functions performed by the actuary appointed as the Lloyd's actuary under SUP 4.6.1R are specified as controlled functions in SUP 10 (Approved persons).As a result, an application must be made to the FSA under section 60 of the Act (Applications for approval) for approval of the person proposing to take up such an appointment. Section 61(3) of the Act (Determination of applications) gives the FSA three months to grant its approval or give a warning notice that it proposes to refuse the application. An actuary should not be appointed until the FSA has approved the actuary. In order to comply with SUP 4.6.1R, the Society should ensure it applies to the FSA as soon as practicable before the date when it needs the actuary to take office. The FSA will need time to consider the application before deciding whether to grant approval.

### Qualifications

4.6.3    R    Before the *Society* applies for approval of its proposed appointment of the *Lloyd's actuary* under SUP 4.6.1R, it must take reasonable steps to ensure that the *actuary*:

(1) has the required skill and experience to perform his functions under the *regulatory system*; and

(2) is a Fellow of the Institute of Actuaries or of the Faculty of Actuaries.

4.6.4    G    To comply with SUP 4.6.3R and *Principle 3*, before the *Lloyd's actuary* takes up his appointment the *Society* should ensure that the *actuary*:

(1) has skills and experience appropriate to the nature, scale and complexity of the *Society's* business and the requirements and standards under the *regulatory system* to which it is subject; and

(2) has adequate qualifications and experience, which includes holding an appropriate practising certificate under the rules of the Institute of Actuaries or the Faculty of Actuaries;

and seek confirmation of these from the *actuary*, or the *actuary's* current and previous employers, as appropriate.

### Disqualified actuaries

4.6.5    R    The *Society* must not appoint under SUP 4.6.1R as *Lloyd's actuary* an *actuary* who is disqualified by the *FSA* under section 345 of the *Act* (Disqualification) from acting:

(1) as an *actuary* for the *Society*; or

(2) as a *syndicate actuary*; or

(3) as an *actuary* for any other relevant class of *firm*.

4.6.6    G    If it appears to the *FSA* that an *actuary* has failed to comply with a duty imposed on him under the *Act*, it may disqualify him under section 345 of the *Act*. For more detail about what happens when the disqualification of an *actuary* is being considered or put into effect, see ENF 17. A list of *actuaries* who are disqualified by the *FSA* may be found on the *FSA* website.

### Conflicts of interest

4.6.7    R    The *Society* must take reasonable steps to ensure that an *actuary* who is to be, or has been, appointed under SUP 4.6.1R:

- (1) does not perform the function of chairman or *chief executive* of the *Society*; and
- (2) does not perform any other function on behalf of the *Society* which could give rise to a significant conflict of interest.

The Lloyd's actuary function

4.6.8 R An *actuary* who has been appointed to perform the *Lloyd's actuary* function must:

- (1) prepare the statement required under *LLD* 15.9.1R(2) to be annexed to the *Lloyd's Return*; and
- (2) take reasonable steps to ensure that the *general insurance business technical provisions* for each *syndicate year* have been reviewed by the *syndicate actuary* and that an appropriate opinion has been obtained under *SUP* 4.6.15R; and
- (3) where a *syndicate actuary's* opinion has not been provided, sets appropriate *technical provisions* and, within six months of the end of the *financial year*, submits a report to the *FSA* on the setting of those *technical provisions*.

Appointment of syndicate actuaries

4.6.9 R Each *managing agent* must, in respect of each *syndicate* it manages:

- (1) appoint an *actuary* (the "*syndicate actuary*") to carry out the duties described in *SUP* 4.6.15R or *SUP* 4.6.16R; and
- (2) appoint a replacement for that *actuary* if he ceases to hold office before he has carried out the duties described in *SUP* 4.6.15R or *SUP* 4.6.16R; and
- (3) ensure that the replacement *syndicate actuary* can take up office at the time the vacancy arises or as soon as reasonably practicable after that.

4.6.10 G (1) The *insurance market direction* and guidance set out in *SUP* 3.1.4G to *SUP* 3.1.15G is relevant to *actuaries* appointed to report on the *insurance business of members*.

(2) References in *SUP* 4, as applied by *SUP* 4.1.3R, to a *firm* include, where appropriate:

- (a) a *managing agent*; and
- (b) one or more *members* carrying on *insurance business* at Lloyd's through a *syndicate*;

and references to an *actuary* of a *firm* should be read accordingly.

#### Syndicate actuaries' qualifications

- 4.6.11 R Before a *managing agent* appoints a *syndicate actuary*, it must take reasonable steps to ensure that the *syndicate actuary*:
- (1) has the required skill and experience to perform his duties; and
  - (2) is a fellow of an *actuarial body* or (except for a *syndicate actuary* of a *long-term insurance business syndicate*) is a fellow of the Casualty Actuarial Society who is a member of an *actuarial body*.

- 4.6.12 G To comply with SUP 4.6.11R and Principle 3, before a *syndicate actuary* takes up his appointment a *managing agent* should ensure that the *syndicate actuary*:

- (1) has skills and experience appropriate to the nature, scale and complexity of a *syndicate's* business and the requirements and standards under the *regulatory system* applicable to the activities of *managing agents* in relation to each *syndicate* which they manage; and
- (2) has adequate qualifications and experience, which includes holding an appropriate practising certificate under the rules of the Institute of Actuaries or the Faculty of Actuaries;

and seeks confirmation of these from the *syndicate actuary*, or the *syndicate actuary's* current and previous employers, as appropriate.

#### Disqualified actuaries

- 4.6.13 R A *managing agent* must not appoint under SUP 4.6.9R as *syndicate actuary* an *actuary* who is disqualified by the FSA under section 345 of the *Act* (Disqualification) from acting:

- (1) as a *syndicate actuary*; or
- (2) as a *Lloyd's actuary*; or
- (3) as an *actuary* for a relevant class of *firm*.

- 4.6.14 G If it appears to the FSA that an *actuary* has failed to comply with a duty imposed on him under the *Act*, it may disqualify him under section 345 of the *Act*. For more detail about what happens when the disqualification of an *actuary* is being considered or put into effect, see ENF 17. A list of *actuaries* who are disqualified by the FSA may be found on the FSA website.

Duties of syndicate actuaries

- 4.6.15 R The syndicate actuary of a long-term insurance business syndicate must:
- (1) make an investigation at the end of each financial year into the financial condition of the business carried on through each syndicate year (other than a closed year);
  - (2) make an abstract of his report of the investigation; and
  - (3) prepare the certificate required under LLD 15.9.1R(3) to be annexed to the Lloyd's Return.
- 4.6.16 R The syndicate actuary of a general insurance business syndicate must:
- (1) review the technical provisions (both gross and net of reinsurance recoveries) of each syndicate year (other than a closed year); and
  - (2) provide his opinion confirming that the technical provisions for each syndicate year are no less prudent than his best estimate of the amounts required.
- 4.6.17 R If a managing agent becomes aware that the syndicate actuary of a general insurance business syndicate will or may be unable to produce an unqualified opinion under SUP 4.6.16R, the managing agent must promptly inform the FSA that this is the case.
- 4.6.18 R In carrying out his duties a syndicate actuary must pay due regard to generally accepted actuarial best practice.
- 4.6.19 G The standards and guidance issued by the Institute of Actuaries and the Faculty of Actuaries are important sources of actuarial best practice.

## Annex U

### Part 3

#### Amendments to the Supervision manual, Chapter 10

In this Part, underlining indicates new text and striking through indicates deleted text.

#### 10.4 Specification of functions

##### 10.4.5 R Table: controlled functions

Type	CF	Description of controlled function
...		
Required functions*	... <u>12B</u> ...	... <u>Lloyd's actuary function</u> ...
...		

...

Appointed actuary function (CF12)

...

Lloyd's actuary function (CF12B)

10.7.22 R The *Lloyd's actuary* function is the function of acting in the capacity of the *actuary* appointed under SUP 4.6.1R to perform the duties set out in SUP 4.6.7R.

10.7.23 G The effect of SUP 4.6.1R is that the *Society of Lloyd's* must appoint an *actuary* (the "*Lloyd's actuary*").

## Annex U

### Part 4

#### Amendments to the Supervision manual, Schedule 2

In this Part, underlining indicates new text and striking through indicates deleted text.

2	Table				
	...				
	<i>SUP 3.3.5R</i>	Vacancy in the office of auditor to a Lloyd's <i>underwriting agent</i> <u>or the auditor of the insurance business of a Lloyd's syndicate.</u>	The fact of the vacancy and the reason for it. <del>(NB— notification to be made to the Society of Lloyd's).</del>	Vacancy in the office of auditor will arise or has arisen.	Without delay
		Appointment of auditor by Lloyd's <i>underwriting agent</i>	The fact of the appointment, name and business address of the auditor and the date the appointment takes effect. <del>(NB— notification to be made to the Society of Lloyd's).</del>	Appointment of auditor	Not specified
	...				

## Annex V

### Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text. New definitions are to be inserted at the appropriate alphabetical position.

approved  
reinsurance to  
close

- (a) a reinsurance to close effected before 1 January 2005; or
- (b) an agreement under which members of a syndicate in one syndicate year ("the reinsured members") agree with the members of that syndicate in a later syndicate year or the members of another syndicate ("the reinsuring members") that the reinsuring members will discharge, or procure the discharge of, or indemnify the reinsured members against, all known and unknown insurance business liabilities of the reinsured members arising out of the insurance business carried on by the reinsured members in that syndicate year that is:
- (i) effected after 1 January 2005; and
- (ii) not a balance transfer between two syndicate years where the syndicate has only one member and the member is the same in each of those years.

balancing  
amount

in respect of a syndicate, any part of the capital resources that:

- (a) the managing agent of the syndicate has assessed to be necessary to support the insurance business carried on by the members of the syndicate through the syndicate, including those capital resources required to support the risks arising at syndicate level that affect that business; but
- (b) are not managed by or at the direction of the managing agent of the syndicate.

callable  
contribution

amounts that members are liable to pay to the Society (or may by resolution of the Society be liable to pay) as contributions to the Central Fund.

central assets

(in LLD)-assets that the Society owns and amounts that members are liable to pay to the Society (or may by resolution of the Council be liable to pay) as contributions to the central fund excluding amounts which, if paid by a member, would cause his assets to fall short (or shorter) of the required amount); the Society's own assets that are available at its discretion to meet a member's liabilities in respect of insurance business.

corporate  
member

a member that is a body corporate or a Scottish Limited partnership.

Council

the governing body of the Society, (in LLD) the Council constituted by section 3 of Lloyd's Act 1982.



<i>funds at Lloyd's</i>	assets ( <u>not being <i>syndicate assets</i></u> ) provided by or on behalf of a <i>members</i> to meet the liabilities arising from the <i>member's insurance business</i> at <u>Lloyd's</u> which are held in a <i>Lloyd's trust fund</i> and managed by the <i>Society</i> as trustee, <del>held by the <i>Society</i>, not being part of their <i>premium trust funds</i>, to meet the liabilities arising from their</del> <u>the <i>member's insurance business</i> at Lloyd's</u>
<i>IPRU(INS)</i>	(1) (except in <i>LLD</i> ) the Interim Prudential Sourcebook for insurers;  (2) (in <i>LLD</i> ) the version of IPRU(INS) in force immediately prior to the coming in to force of the Interim Prudential Sourcebook (Insurers and Other Amendments) Instrument 2004.
<i>Lloyd's actuary</i>	the <i>actuary</i> appointed by the <i>Society</i> under <del><i>LLD</i> 10.9.1R</del> <u><i>SUP</i> 4.6.1R.</u>
<u><i>Lloyd's member's contribution</i></u>	assets:  (a) <u>provided to a <i>managing agent</i> in response to a cash call; or</u>  (b) <u>held by the <i>Society</i> as <i>funds at Lloyd's</i>.</u>
<u><i>Lloyd's trust fund</i></u>	a fund held on the terms of a <i>Lloyd's trust deed</i> .
<u><i>Lloyd's trust deed</i></u>	a trust deed in the form prescribed by the <i>Society</i> and notified to the <i>FSA</i> , for execution by a <i>member</i> in respect of his <i>insurance business</i> .
<u><i>managing agent's agreement</i></u>	an agreement in the form prescribed by the <i>Society</i> , between a <i>managing agent</i> and a <i>member</i> , under which the <i>managing agent</i> manages the <i>insurance business</i> of that <i>member</i> .
<i>secured debt</i>	(1) (in <i>LLD</i> ) a debt owed to (or an obligation to be fulfilled for the benefit of) a <i>member</i> , secured by an <i>admissible asset</i> .  (2) (in <i>PRU</i> ) ...
<u><i>Society GICR</i></u>	the <u><i>general insurance capital requirement</i> calculated by the <i>Society</i> as if it were an <i>insurer</i> under <i>LLD</i> 19.2.13R.</u>
<i>syndicate actuary</i>	an <i>actuary</i> appointed to a <i>syndicate</i> as required by <del><i>LLD</i> 10.9.4R(1)</del> <u><i>SUP</i> 4.6.9R(1)</u>
<u><i>syndicate assets</i></u>	assets managed by or at the direction of a <i>managing agent</i> in respect of <i>insurance business</i> carried on through a <i>syndicate</i> and overseas business regulatory deposits funded from those assets.
<u><i>syndicate ICA</i></u>	the capital assessment performed by a <i>managing agent</i> under <i>PRU</i> 1.2.26R, <i>LLD</i> 18.2.1R(1), <i>PRU</i> 2.3 and <i>LLD</i> 19.4.1R(1) in respect of each <i>syndicate</i> managed by it.