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Financial Services Authority

# Quarterly consultation

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The Financial Services Authority invites comments on this Consultation Paper.  
Comments on the proposed amendments should reach us by 6 June 2006.

You can submit your comments electronically using the form on our website (at [www.fsa.gov.uk/pubs/cp/cp06\\_06\\_response.html](http://www.fsa.gov.uk/pubs/cp/cp06_06_response.html)).

Or you can respond by email: [cp06\\_06@fsa.gov.uk](mailto:cp06_06@fsa.gov.uk)

If you wish to respond by letter, please send your comments to the person named at the end of each chapter and set out below:

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If you are responding in writing to several chapters, please send your comments to Nick Walker in General Counsel's Division, who will pass your response on as appropriate.

All responses to the above people should be sent to:

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**It is our policy to make all responses to formal consultation available for public inspection, unless the respondent requests otherwise. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure.**

Copies of this Consultation Paper are available to download from our website – [www.fsa.gov.uk](http://www.fsa.gov.uk). Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

# 1 Introduction

1.1 This Consultation Paper (CP) invites comments on miscellaneous amendments to the Handbook. It proposes amendments:

- to the *Glossary of definitions* in respect of Exchange Traded Funds;
- to the *General Provisions*, the *Conduct of Business sourcebook*, the *Insurance: Conduct of Business sourcebook* and the *Mortgages: Conduct of Business sourcebook* following the registration of the FSA's keyfacts logo;
- to the *Integrated Prudential sourcebook*, the *Interim Prudential sourcebook for Investment Businesses* and the *Supervision manual* in respect of a proposed extension of audit exemption in the Companies Act 1985 to small authorised firms and appointed representatives and consequential changes in the capital resources requirements for small authorised firms;
- to the *Conduct of Business sourcebook* in respect of the sale of traded life policies and of third party processors;
- to the *Mortgages: Conduct of Business sourcebook* in order to make some existing waivers permanent and to provide for certain technical changes;
- to the *Complaints against the FSA sourcebook* in respect of one of the qualifications applying to the Complaints Commissioner and other minor amendments; and
- to the *New Collective Investment Schemes sourcebook*.

1.2 We describe each amendment in a separate chapter. Each chapter includes an explanation of the proposed amendment, a statement of purpose, a cost benefit analysis (if necessary) and a compatibility statement. The appendices to this CP contain the actual text of the proposed amendments.

- 1.3 The deadline for comments on these amendments is 6 June 2006.

## **CONSUMERS**

The proposed amendments in Chapters 3, 5, 6 and 8 may be of particular interest to retail consumers and consumer groups.

The remaining amendments are largely technical amendments, clarifications and corrections and are, on the whole, unlikely to have a direct impact on consumers.

# 2 Proposed amendments to the Glossary

## Introduction

- 2.1 This chapter explains our proposal to amend the *Glossary of definitions* to include a definition of an ‘exchange traded fund’ (ETF) and to amend the definition of ‘inter-professional investments’ to include units in ETFs.
- 2.2 We would make these amendments under sections 138 (general rule-making power) and 156 (general supplementary power) of the Financial Services and Markets Act 2000 (FSMA). The text of the proposed amendment is set out at Appendix 2 to this CP.
- 2.3 This change is of primary interest to firms conducting inter-professional business.

## Proposed amendment

- 2.4 The inter-professional regime set out in MAR 3 permits market counterparties to conduct certain regulated activities between themselves without providing certain customer protections. This inter-professional business can only be carried out in respect of a defined list of inter-professional investments.
- 2.5 Article 76(3)(a) of the Regulated Activities Order 2001 (the RAO) specifically excludes shares in an open ended investment company from the definition of ‘share’ set out in Article 76 of the RAO. As a result of this, shares in an open ended investment company do not fall within the definition of ‘share’ set out at item (a) of the definition of ‘inter-professional investments’, which specifically refers back to Article 76 of the RAO. ETFs are generally constituted as open ended investment companies, so units in an ETF do not fall within the FSA Handbook Glossary definition of ‘inter-professional investments’ and transactions in them cannot take place on an inter-professional basis.

- 2.6 This means that firms dealing in units in ETFs are unable to classify other firms that they deal with as market counterparties. Instead, these counterparties (other authorised firms) will need to be classified as intermediate customers with the requisite customer protections. But units in ETFs are traded in the UK like shares, on the LSE using the SETSmm trading platform and OTC. They are also traded on various overseas exchanges. This means the regulatory treatment of these units is not consistent with market practice.
- 2.7 It is inappropriate to require customer protections to be provided in relation to market transactions simply because the instrument being traded is a unit in an ETF and it was not intended that ETFs should be treated in this way under the inter-professional business regime. Furthermore, we do not intend for the inter-professional business regime to place barriers in the way of new market developments by singling out different treatment for new investment types such as ETF units that trade in the same way as shares and are regulated products.
- 2.8 As this was not intended we are making a modification by consent available to firms undertaking inter-professional business so that the Glossary definition of 'inter-professional investments' will be extended to include units in ETFs. The modification by consent will end in December 2006. We are also proposing to amend the Glossary definition to give permanent effect to the modification by consent.

Q1: Do you agree to the definition of 'inter-professional investments' being amended to include units in exchange traded funds?

### **Cost benefit analysis**

- 2.9 This amendment will allow firms that trade in ETFs to conduct their business under the inter-professional business regime.
- 2.10 A benefit of this amendment is that these firms will not be required to provide customer protections to their counterparties which would be time consuming and costly and are unnecessary by virtue of their market expertise and authorised status.
- 2.11 There are no additional costs associated with the proposal and no increased risk, either in terms of consumer detriment or loss of market confidence. So we are satisfied that no formal cost benefit analysis is required.



## **Compatibility statement**

- 2.12 We believe that the proposal outlined in this chapter is compatible with our general duties under section 2 of FSMA, and in particular our statutory objectives of consumer protection under section 5 and market confidence under section 3. We believe this proposal is the most appropriate way of meeting these objectives because it has regard to the principle of good regulation in section 2(3), namely that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction.

### **Contact**

We invite comments on this proposal. Comments should reach us by 6 June 2006. Please send them to:

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# 3 Proposed amendments in respect of the FSA's keyfacts logo

## Introduction

- 3.1 The keyfacts logo has recently been registered as a trade mark of the FSA. To reflect this registration, this chapter proposes changes to the *General Provisions* (GEN), the *Conduct of Business sourcebook* (COB), the *Insurance: Conduct of Business sourcebook* (ICOB) and the *Mortgages: Conduct of Business sourcebook* (MCOB).
- 3.2 These changes would be made under sections 138, 156 and 157 of the Financial Services and Markets Act 2000 (FSMA).
- 3.3 Subject to the outcome of consultation, we intend to make these changes at the September 2006 meeting of the FSA Board. The amended rules would come into force on 6 November 2006. Appendix 3 to this CP contains the text of the proposed amendments.

## CONSUMERS

These proposed changes should benefit consumers by preventing firms using the keyfacts logo in a misleading way.

## Proposed amendments

- 3.4 We have registered the keyfacts logo we use on our Key Facts documents as a Community trade mark of the FSA. We need to add licensing information and terms of use to GEN 5.1 to reflect this registration. There will also be some consequential changes to MCOB, ICOB and COB to add the ® symbol to the keyfacts logo to template and example documents in those sourcebooks.

- 3.5 When consumers receive an Initial Disclosure Document (IDD), Key Facts Illustration (KFI), Policy Summary or Menu bearing the keyfacts logo they know they should be able to rely on the information in the documents. We only allow firms to use this logo where expressly provided for by the rules and it is not a marketing tool. We have registered the logo to prevent firms which we do not regulate from using it for commercial gain or in other ways which are not intended by the rules.
- 3.6 This means that in order to protect the trademark we need to introduce a revised logo including the ® symbol. This will affect the IDD, the Combined IDD, the KFI, Policy Summary and Menu required by the MCOB, ICOB and COB sourcebooks. Contact with trade bodies has suggested that firms do not hold large printed stocks of these documents and that any systems changes required to insert the new logo will be small. We propose a 12 month transitional period from 6 November 2006 for firms to implement these changes to minimise any costs. The new logo is now available on our website.
- 3.7 There will be no change to the rules setting out where firms are required to, or are permitted to, use the keyfacts logo. Aside from the new logo, the content of the disclosure documents will not change.

Q2: Do you agree with our proposed transitional period for this change?

### **Cost benefit analysis**

- 3.8 We believe that the costs resulting from this change will be of no more than minimal significance. Therefore we are not providing a full CBA. To ensure transparency and accountability, we outline our expectations of the costs and benefits below.
- 3.9 Registering this logo as a trade mark is important to protect the keyfacts brand and our reputation as the holder of this brand. This change will bring benefits for consumers by preventing firms from using the logo in a misleading way. There will be some one-off costs to investment, general insurance and mortgage firms from making minor changes to their disclosure documentation displaying the keyfacts logo. Communication with trade bodies has indicated that a 12 month transitional period will allow firms to make these changes as part of their normal business processes. We believe that allowing firms to have this transitional period will result in associated costs of no more than minimal significance. However, we are aware that changes to documentation can impose costs and will consider the views of those we are consulting.

## **Compatibility statement**

- 3.10 We are satisfied that the proposed amendments are compatible with our statutory objectives. If the keyfacts logo were to be misused, this could mislead consumers and diminish the value of the keyfacts brand as a consumer tool. Preventing such misuse by protecting our trade mark will help us to secure the appropriate degree of protection for consumers. Giving a long transitional period to reduce the cost to firms follows our principle of acting proportionately. So we believe that our proposal is the most appropriate way of meeting our regulatory objectives.

### **Contact**

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

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# 4 Proposed extension of audit exemption in the Companies Act 1985

## Introduction

- 4.1 Under the Companies Act 1985 (CA), limited liability companies that are categorised as small<sup>1</sup>, are exempt from the statutory audit requirement unless, among others, they have permission under Part IV of the Financial Services and Markets Act 2000 (FSMA) to carry on one or more regulated activities, or are an appointed representative (AR) within the meaning of section 39 of FSMA.
- 4.2 In September 2005, the Department of Trade and Industry (DTI) amended the CA to enable small authorised firms (and ARs), whose only regulated activities are mortgage and insurance (M&GI) mediation activities, to take advantage of the CA exemption<sup>2</sup>. After the exemption was extended to M&GI firms, we said we would consider extending the exemption to other small authorised firms and ARs<sup>3</sup>. Having undertaken a study we have concluded that the arguments for exempting M&GI firms are also applicable to certain other small authorised firms and ARs within the scope as set out below.
- 4.3 The DTI supports this initiative to reduce burdens on small businesses. If this consultation meets with a favourable response, the DTI and the FSA will work together to implement the necessary changes in companies legislation and in the FSA Handbook.
- 4.4 We considered whether achieving our objectives – in this case, relating principally to consumer protection – would be compromised if we allowed the same audit exemption treatment for firms other than M&GI firms. We do not believe this would be the case for a number of reasons.

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1 Under the CA definition of 'small', companies need to satisfy two criteria from: turnover less than £5.6 million; balance sheet assets of less than £2,8 million and 50 or less employees. Some firms, such as those in groups, cannot use the exemption.

2 The Companies Act 1985 (Investment Companies and Accounting and Audit Amendments) Regulations 2005 (SI 2005/2280).

3 Better Regulation Action Plan published December 2005 p.10.

- First, since most small authorised firms are now subject to the Retail Mediation Activities Return (RMAR), we consider that alternative measures are in place to deal with the relevant risks to our objectives.
- Second, we are not relaxing our quantitative capital resources requirements imposed on these firms.
- Third, consumer protection is also provided by the client money rules applying to firms holding client money. We intend that a firm that holds client money will still be required to have a client money audit whether or not it falls within the category of small firms exempt from statutory audit to ensure the adequacy of systems and controls surrounding the safe keeping of client money satisfy the requirements set out in the Client Assets Sourcebook (CASS). We believe this approach is justified: firms holding client money present more risks to our objectives, as the impact of their failure is likely to be more significant particularly on consumers.

- 4.5 If the extension of the audit exemption is made, we may, in the future, make greater use of skilled persons as a supervisory tool to supplement our supervision and thematic work. This is in addition to the exercise of our existing powers under section 166 of FSMA where we can require a firm to provide us with a report by a skilled person if we believe there is a risk of significant regulatory failure in a firm or Group.
- 4.6 In our opinion, such occasional use of skilled persons will minimise the risks of a reduction in the standard of firm's internal controls because firms will know that they could still be subject to a detailed inspection by an external auditor or FSA staff. Although we do not know the precise numbers, we expect to select approximately 50 firms a year (using a mixture of targeted and random selection) that will be subject to review by a skilled person. We have used this figure when considering the cost and benefits of these proposals later in this chapter.
- 4.7 In developing our proposals, we have also considered the impact that allowing small firms to include unaudited reserves and unverified profits within their capital resources, or to calculate annual expenditure based on unaudited financial statements, may have on the competitive structure of the small authorised firms market. We believe such a step will foster competition because small limited companies compete in the same market as sole traders and partnerships, which are not subject to a requirement to prepare audited statutory accounts (although all categories of firm are potentially subject to a section 166 review).

### **Scope of audit exemption**

- 4.8 We propose that the firms which should benefit from the exemption are those that are neither required to appoint an auditor because of legislation other than the CA nor subject to specific capital requirements as a result of an EEA Directive.

4.9 The types of firms that could benefit from an extension of the audit exemption in the CA are therefore:

- Authorised Professional firms;
- non-ISD<sup>4</sup> Investment Management firms;
- non-ISD Personal Investment firms;
- non-ISD Securities and Futures firms;
- mortgage lenders;
- mortgage administrators; and
- service companies.

4.10 The types of firms that would be *outside* this scope, and the reasons they are required to retain a statutory audit, are:

- firms subject to specific capital requirements or to the requirement to appoint an auditor under or as a result of European legislation:
  - banks;
  - insurers;
  - UCITs management companies;
  - ISD investment management firms;
  - ISD personal investment firms;
  - ISD securities and futures firms; and
  - electronic money issuers;
- firms subject to the requirement to appoint an auditor under or as a result of other UK legislation:
  - building societies (Building Societies Act 1986, s.77);
  - credit unions (Credit Unions Act 1979, Schedule 1, para 11);
  - friendly societies (Friendly and Industrial Provident Societies Act 1968, s.4(1)); and
  - ICVC (Open-Ended Investment Companies Regulations 2001, regulation 67 and Schedule 5, paragraph 4);
- firms subject to the requirements of another jurisdiction:
  - incoming EEA firms;

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4 Investment Services Directive.

- incoming treaty firms;
- UCITS qualifiers; and
- lead regulated firms.

4.11 Also, we do not propose to modify the audit requirements imposed on the Society of Lloyd's, underwriting agents or members' advisers.

### **Proposed changes to the Handbook**

- 4.12 In this chapter, we propose amendments to the *Integrated Prudential sourcebook* (PRU), the *Interim Prudential sourcebook for Investment Businesses* (IPRU(INV)) and the *Supervision manual* (SUP) as they apply to the relevant population of small authorised firms.
- 4.13 All these changes are subject to our receiving a favourable response to this consultation and to the DTI then making the necessary legislative amendments.
- 4.14 The text of the proposed amendments to the Handbook is set out in Appendix 4 to this CP.
- 4.15 The proposed amendments to SUP 3 delimit the firms to which the chapter applies and those to SUP 16 set out our rules and guidance on the submission of unaudited annual financial statements to the FSA.
- 4.16 The proposed amendments to PRU 9, and IPRU(INV) 5 and 13, set out rules and guidance on the inclusion of unaudited reserves and interim profits in the capital resources of relevant firms. The proposed amendments to IPRU(INV) 3 set out rules and guidance on calculating annual expenditure with reference to unaudited financial statements.
- 4.17 The proposed amendments are explained in further detail below.

#### *Supervision manual*

- 4.18 We are proposing amendments to Chapter 3 and 16 of SUP.
- 4.19 The changes to SUP 3, unlike those to the other chapters, are not consequential to changes in the CA and represent a change in our policy. We propose to relax the requirement to appoint an auditor for regulatory purposes under SUP 3. As such, firms that are not required to appoint an auditor as a result of a statutory provision (other than under FSMA) and that do not hold client money or client assets, will no longer need to appoint an auditor under SUP 3. (These firms are described in the introduction to this chapter.) We will still require those firms which hold client money or client assets to retain the client assets audit.
- 4.20 The proposed amendments to SUP 16.7 and relevant reporting forms (SUP 16 Annexes) enable small firms not required to appoint an auditor under the CA to submit unaudited financial reports to us.



- Q3: Do you agree with our proposal that those small firms listed in paragraph 4.9 that are only required to appoint an auditor under the CA, by virtue of holding permissions under Part IV of FSMA, should be included in the proposed audit exemption or should the current audit requirement in the CA remain in force?
- Q4: Do you agree with our proposal that firms that do hold client assets or client money should still be required to appoint an auditor under SUP 3 for the purposes of a client assets audit?
- Q5: Do you agree with our proposals to enable firms that are able to benefit from the audit exemption under the CA to submit unaudited financial reports to the FSA?

#### *PRU and IPRU(INV)*

- 4.21 We are proposing amendments to PRU 9.3.52R, IPRU(INV) 3.73(2)R, IPRU(INV) 3.73(3)R, IPRU(INV) 5.2.2(1)R and IPRU(INV) 13.10(2)R and 2AR to allow firms that benefit from the small companies audit exemption to include unaudited reserves and unverified interim profits in their capital resources calculation and, in the case of IPRU(INV) 3.73R, to enable firms to calculate annual expenditure with reference to unaudited financial statements. There would be no change in the requirements for firms that require a statutory audit.
- Q6: Do you agree with our proposal that firms that qualify for the small company audit exemption should be allowed to include unaudited reserves and unverified interim profits within their capital resources calculation and, where relevant, calculate their annual expenditure with reference to unaudited financial statements?

#### **Cost benefit analysis**

- 4.22 In evaluating the proposal to allow unaudited reserves and interim profits to qualify as regulatory capital, and unaudited financial statements to be used in calculating annual expenditure for small authorised firms, we highlight the incremental costs and benefits that arise. In doing so, we take into consideration that, for small authorised firms, neither the quantitative requirements for regulatory capital nor the client money audit requirements where required will change under the proposed rule amendments. We also consider the effect of removing the requirement to appoint an auditor for the small firms and their ARs apart from those required to appoint an auditor under legislation other than the CA.

## *Costs*

- 4.23 The theoretical arguments supporting statutory audit suggest that it can act as an aid to consumer protection (although this is not its primary purpose) because an independent third party verifies that the figures for reserves and interim net profits are accurate. The benefits of audits arise from the control afforded over the inadequate financial resources in small authorised firms.
- 4.24 There are then potentially some disadvantages for consumers if the FSA permits regulated firms to include unaudited reserves and unverified interim profits within their capital resources or use unaudited figures to calculate annual expenditure. It is possible that the quality of the financial information underlying regulatory capital/ annual expenditure could diminish in the absence of statutory audits, and so firms could, intentionally or unintentionally, breach their regulatory requirements – or worse, become insolvent.
- 4.25 In such cases there may be inadequate resources available to deal with claims against the firm (for example, to satisfy a claim for mis-selling where the firm's professional indemnity insurance does not cover the full extent of the firm's liability). As a result, costs might arise both to consumers, in the form of losses from mis-sold products or opportunity costs associated with time spent dealing with the process of collecting redress, and to the industry as a result of funding compensation through a voluntary or statutory compensation scheme.
- 4.26 Measuring the costs associated with removing the statutory audit requirement and allowing firms to use unaudited reserves and unverified interim net profits in capital is complex, but depends on two discreet factors:
- (1) how effective statutory audits are in providing protection; and
  - (2) how often we expect firms to indulge in costly 'mis-behaviour' in the absence of these audits.
- 4.27 Regarding the first, the Professional Oversight Board for Accountancy has indicated that small firms' financial statements filed at Companies House, whether audited or not, were of similar quality. This may indicate that an audit may not provide effective safeguards so consumer detriment, that could occur as a result of removing audit assurance for statutory accounting and verification of eligible capital, may not be as large as immediately apparent.
- 4.28 The extent to which we expect firms to indulge in costly 'mis-behaviour' in the absence of a statutory audit is difficult to quantify, but the risks may be mitigated by changes in our supervisory approach, our use of technology and risk-based supervision.

- 4.29 Further, given that we will be maintaining current quantitative regulatory capital and client money audit requirements, that most small authorised firms are now subject to the RMAR, and that we are also considering commissioning an annual audit for a sample of these firms, the benefits foregone are not expected to be large.
- 4.30 We may also supplement these measures by making greater use of skilled persons as a supervisory tool to supplement our supervision and thematic work. We expect to select approximately 50 firms a year (using a mixture of targeted and random selection) that will be subject to review by a skilled person. The costs of reports by skilled persons, for a sample of around 50 firms, would be in the region of £140,000 (based on the average audit costs for firms that will benefit from this audit exemption), but may be less if the scope of the skilled persons report is on a more restricted basis than a statutory audit. This approach may also require additional FSA staff time to plan and oversee, amounting to a cost to the FSA of approximately £400,000 per year. The costs of a skilled person report under s166 of FSMA would normally be borne by the firm involved.
- 4.31 Since June 2005, all small personal investment firms (those most likely to benefit from the audit exemption) have been required to submit the Retail Mediation Activities Return (RMAR) every six months rather than a single annual return under the old rules. So we now have more data, received in a more timely fashion, and an improved capacity to analyse it better enabling us to target our supervisory resources.

Q7: We invite firms' views on the cost estimates and allocation outlined above.

### *Benefits*

- 4.32 The financial benefit impact for small firms in terms of reduced audit costs are significant. Small authorised firms will benefit by the amount of any audit costs saved. Consumers will benefit by not having indirectly to bear these costs. The average cost of a statutory audit for a small firm or an AR is estimated to be between £2,150 and £3,370. We estimate the total population of affected firms at about 3,200 and a further approximately 1,490 ARs. The annual savings for small authorised firms could therefore be between £6.9 million and £10.8 million, and for their ARs between £3.2 million and £5 million (taking an average cost of audit of £2,760 this represents a saving of £8.9 million for small authorised firms and £4 million for ARs). We believe that this cost saving is likely to be shared between firms and their consumers, as the latter are likely to benefit from lower pricing.

## Compatibility statement

- 4.33 Statutory audits for small authorised firms are relevant to our consumer protection objective. The likely market failures they are meant to address are negative externalities (i.e. firms failing and mis-representing the financial position). As discussed earlier in this chapter, alternative measures are in place to deal with the relevant risks to our objectives and evidence suggests these audits may be relatively ineffective in addressing the relevant market failure. So we believe the exemption proposed should not negatively affect the relevant risks to our objectives.
- 4.34 The proposals described above are aimed at ensuring that the burden imposed on the carrying out of the activity is proportionate to the benefits expected to result from imposing that burden. Given the discussion in the previous paragraph, the added provision of statutory audit may then be an additional cost imposed on firms without appropriate benefit. We think the exemption proposals ensure our principle that burdens imposed be proportionate to resultant benefits is met in the most efficient and effective manner.
- 4.35 We also believe these proposed changes may help facilitate competition between firms. Small authorised firms that are limited companies are likely to compete more directly with sole traders and partnerships as opposed to larger firms. Since sole traders and partnerships are also not subject to statutory audit under the CA, the changes should help to promote competition between these different types of firm.
- 4.36 Overall, given this discussion, we believe that the proposed rule changes are the most appropriate way of meeting our objectives. We do not believe these amendments have any other impact on our aim of meeting the principles of good regulation.

## Contact

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

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# 5 Proposed amendments to the Conduct of Business sourcebook

## Introduction

- 5.1 The depolarisation regime came into force on 1 June 2005. We are committed to an ongoing review of the regime to assess the extent to which the objectives of depolarisation have been met and to assess its effects on the market. At this point, for the reasons apparent below, we are proposing two minor sets of amendments.
- 5.2 The first, which relates to provision of the menu in the sale of traded life policies, would result in a single change to the *Conduct of Business sourcebook* (COB). The second, which relates to the treatment of third party processors, would result in changes to COB as well as to the *Glossary of definitions* and the *General Provisions* (GEN).
- 5.3 The changes would be made under sections 138 and 156 of the Financial Services and Markets Act 2000 (FSMA), and the powers under FSMA listed in Schedule 4 to GEN.

## Sale of traded life policies

### *Background*

- 5.4 A firm gives the consumer documents, including the menu, at the start of the advice process. They contain some of the most important information about the firm, its charges and services, and help the consumer to decide whether to use that firm or adviser.
- 5.5 In CP04/3 *Reforming Polarisation: A menu for being open with consumers – Including feedback on CP166* we selected and placed into groups a number of products for which a firm would need to provide a menu. It is evident that as these groups currently stand, the sale of traded life policies falls within the endowment product group. The sale of traded life policies involves the assignment of pre-existing life policies from the client to the firm or another third party. It was not our original policy intention to capture traded life policies within this group.

### *Proposed amendment*

- 5.6 We propose to make an amendment (within Section 4 of COB Annex 6R) to the endowment product group in COB on the grounds that the market average figures in the menu are calculated on the basis of sales of new policies and do not reflect the sales of traded life policies. The amendment would mean that firms, generally, are not required to provide a menu in the sale of traded life policies.
- 5.7 The text of the proposed amendment is set out in Appendix 5A to this CP.

## **Third Party Processors**

### *Background*

- 5.8 Third Party Processors (TPPs) are authorised firms which carry on mortgage or insurance mediation activities, or both, for another authorised firm (Firm B), under an outsourcing contract. Under the terms of that contract, the TPP (Firm A) acts in the name of Firm B in its dealings with consumers. So the consumer is not aware of its involvement in a transaction: they believe they are dealing with Firm B throughout.
- 5.9 Some activities that Firm A carries out for Firm B (for example general administrative services post-sale) may in fact amount to carrying on regulated activities and may therefore mean that Firm A needs to be authorised in its own right. So, Firm A will be subject to our rules, including those on disclosure. This means that even where it acts on behalf of Firm B, Firm A would need to disclose its existence and involvement in a transaction at various stages, as required by our rules. In particular, it would be required to provide an Initial Disclosure Document.
- 5.10 In CP05/1 *Quarterly consultation No 3* we consulted on proposed amendments to certain MCOB and ICOB rules. These proposals removed the requirement for TPPs to separately disclose their identity in a transaction when they are carrying on regulated mortgage activities or insurance mediation activities in relation to non investment insurance contracts.
- 5.11 At the time we said that we were aware of the difference in the treatment of TPPs in the COB and the MCOB/ICOB rules. This issue only seemed to affect a small number of investment firms and has, up until now, been dealt with by granting individual waivers where appropriate. We have since published a number of waivers with a two-year duration. Taking into account the number of representations we have received, we now consider it appropriate to extend to COB the previous amendments, in a similar way to those made in ICOB/MCOB.

### *Proposed amendments*

- 5.12 None of the firms we have seen so far have contracted out any advising activity to TPPs. The services contracted out to these firms have been general administration and post-sale transaction type services. Advising on investments cannot be contracted out in the same way, as it requires the exercise of discretion and cannot be automated. Where a firm is giving investment advice, the consumer should be given accurate information regarding the identity of the firm giving the advice as this is an important factor when considering trustworthiness, reputation and choice. Accordingly, we consider the following amendments to be appropriate as long as no advice is provided by the TPP.
- 5.13 In support of the proposed changes to the rules, TPPs told us the following.
- Where Firm B is responsible for Firm A's activities, Firm A's involvement in a transaction is irrelevant to a consumer – the TPP does not give any advice. If TPPs disclosed their involvement, consumers would be unclear which firm they were dealing with. So, such disclosure is likely to be an unnecessary burden and confusing for the consumer.
  - It is questionable whether there is any benefit to the consumer in knowing they are dealing with a third party since it is the outsourcing firm (Firm B) that will be responsible for the transaction.
  - Requiring the TPP to disclose its identity could deter firms from outsourcing.
  - There is minimal risk to private customers. Conversely, compliance with the current requirements is likely to cause confusion and is of questionable benefit.
- 5.14 We therefore propose amending the definition of a TPP in the Glossary to enable TPPs to carry on insurance mediation activities in relation to any type of contract of insurance. We would do this by removing the requirement that TPPs may carry on insurance mediation activities only in relation to non-investment insurance contracts. We also propose to include a rule in COB relating to TPPs in a similar way that we have done in ICOB and MCOB. However, if the TPP is advising on investments, this rule will not apply.
- 5.15 When the TPP amendments to ICOB/MCOB were made we also amended the statutory status disclosure requirements in GEN. This is so the requirement to disclose a firm's regulatory status (on letterheads etc.) would not apply to TPPs when they are carrying on regulated mortgage activities or insurance mediation activities in relation to non investment insurance contracts. We propose to make corresponding amendments to the statutory status disclosure rules to bring about a similar widening of its application as for COB.



## *Appointed Representatives*

- 5.16 We propose to extend our proposals to cover appointed representatives. We do not believe there is any reason to adopt a different approach on disclosure of the TPP's involvement for the appointed representative. This is primarily because the principal of the appointed representative will be responsible for the appointed representative's acts or omissions anyway. So, in this case, the disclosure rules will apply to the appointed representative rather than the TPP, which will represent itself as the appointed representative in any communication with a consumer.
- 5.17 It should be noted that our proposals do not cover the situation where a TPP is acting on behalf of a non-authorised person who is not an appointed representative.
- 5.18 The proposed amendments are set out in Appendix 5B to this CP.

## **Cost benefit analysis**

- 5.19 The proposed amendments are unlikely to generate incremental costs to firms and customers of more than minimal significance so we are not providing a cost benefit analysis.

## **Compatibility statement**

- 5.20 We do not believe that the proposed amendments have any significant impact on our consumer protection objective and, as a result, the proposals are compatible with our general statutory duties. The reasons we believe this are the same as set out in our previous consultations in this area. The proposals make minor corrections to certain parts of our Handbook where the rules and guidance do not reflect our intention when originally drafted; the corrections merely give effect to our original intentions. Readers should refer to Annex 1 in CP04/3 *A menu for being open with consumers and made text* for more detailed explanations.

## **Contact**

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

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# 6 Proposed amendments to the Mortgages: Conduct of Business sourcebook

## Introduction

- 6.1 We are proposing some minor changes to the *Mortgages: Conduct of Business sourcebook* (MCOB). These are essentially deregulatory measures making existing waivers permanent and dealing with technical amendments to the rules.
- 6.2 The changes we are proposing are to:
- simplify the application of MCOB to financial promotions, including risk warnings and APR requirements in long shelf-life promotions;
  - clarify the application of the Key Facts Illustration (KFI) rules to flexible mortgages;
  - remove the requirement to include details of non-tied insurance policies in offer letters;
  - simplify the annual statements requirements in some circumstances; and
  - amend the disclosure requirements in the KFI for certain post-sale changes to mortgage contracts.
- 6.3 We explain these changes in more detail below. Subject to the outcome of consultation, we intend to make them at the September 2006 meeting of the FSA Board. The amended rules would come into force on 31 October 2006. Appendix 6 to this CP contains the text of the proposed amendments.

## CONSUMERS

The proposed changes to the financial promotions and disclosure rules should benefit consumers by clarifying the information provided to them. The remaining changes should have little impact on consumers, as explained in the cost-benefit analysis.

## Proposed amendments

### *Financial Promotion rules*

- 6.4 We propose four minor changes to the rules on financial promotions in MCOB 3. In two cases, we intend to make existing modifications permanent. The other two proposals have arisen from issues firms have raised with us on the current rules.
- 6.5 We have granted a modification to MCOB 3.6.3R that is available to all firms who promote qualifying credit. We now propose to make this modification permanent. This rule reflects the Comparative Advertising Directive which allows for comparisons in advertisements between “competing goods and services meeting the same needs or intended for the same purpose”. The current (unmodified) rule is more restrictive than this, however, and only allows firms to compare qualifying credit with qualifying credit. The proposed amendment broadens firms’ scope to make comparisons in their promotions, allowing them to compare qualifying credit with other credit meeting the same needs or intended for the same purpose.
- 6.6 Another existing modification that we propose to make permanent is to the risk warning in MCOB 3.6.13R(3). The wording of this warning is not suitable where the security is not the borrower’s home. This may be, for example, where the promotion is for buy-to-let lending or for business lending secured on other land. We have allowed several firms to use a modified warning in these circumstances. We propose to change the rule in a permissive way so firms may continue to use the standard (unmodified) warning if they wish.
- 6.7 Contact with firms has highlighted an overlap of risk warnings where a firm advertises both qualifying credit and Consumer Credit Act (CCA) regulated credit in the same promotion. Currently the two sets of regulations require firms to put two risk warnings on their promotions, both serving the same purpose. The wording of the Consumer Credit (Advertisements) Regulations 2004 warning includes the risk warning required by MCOB 3.6.13R(3). So, we are proposing a rule that would allow firms to use the CCA version in advertisements which include qualifying credit and CCA-regulated credit. This would avoid the unnecessary duplication of the warning. This change illustrates our commitment signalled at the time of the Budget to improve matters for firms regulated under both the Financial Services and Markets Act and the CCA and minimise the administrative burden where possible. Better regulation changes of this kind support the approach set out in the Hampton report.

- 6.8 MCOB 3.6.3R states that non-real time credit promotions should be clear, fair and not misleading. We give guidance in MCOB 3.6.5G(2) that certain information (including APRs) should be relevant and recent. We go on to suggest that firms should, therefore, avoid including this information in promotions which have a long shelf-life. However, we also require (in MCOB 3.6.17R) non-real time qualifying credit promotions which target customers who consider their access to credit restricted to state the APR in the promotion. Although it is only guidance, MCOB 3.6.5G combined with MCOB 3.6.17R has caused firms to avoid promoting such credit in long shelf-life publications. The proposed change to the guidance would allow firms to include APRs (and other information), provided there is a clear and prominent warning that it can become outdated.

Q8: Do you agree with the proposed changes to our rules on financial promotions in MCOB 3? If not, please state your reasons.

#### *Dealing with flexible mortgages in the KFI*

- 6.9 We have had several queries from firms about how they should illustrate flexible mortgages in the KFI. In this particular context, we are using ‘flexible mortgage’ in a narrow sense to refer specifically to those products that allow an initial drawdown together with a linked borrowing facility. Customers can draw down the linked borrowing facility without any further approval from the lender.
- 6.10 The queries we received showed differences in the way firms are interpreting our rules on how to illustrate flexible mortgages in the KFI. Our policy aim for these mortgages has always been for firms to illustrate the initial drawdown in Sections 3, 5 and 6 of the KFI and to use this amount when calculating the APR shown in Section 5. The linked borrowing should be illustrated in Section 12 under ‘Additional Features’. We believe it would be better for customers to receive a KFI based on their initial drawdown as this is likely to reflect the actual monthly payments they will make. The additional cost of the linked borrowing facility, which customers may or may not make use of, can then be illustrated separately.
- 6.11 This has led us to review our rules to see whether they delivered our policy intention. Our conclusion was that they did for flexible mortgages that are not revolving credit agreements (or ‘running-account credit’ agreements), but that they did not for flexible mortgages that are revolving credit agreements.
- 6.12 We are therefore proposing to make changes to our rules that will deliver our policy intention for flexible mortgages that are revolving credit agreements. We propose similar changes to the equivalent rules for lifetime mortgages.
- 6.13 We are proposing to allow a 12 month transitional period from the date the new rules take effect for firms to implement any changes to their systems.

Q9: Do you agree with our proposed rule changes for flexible mortgages that are revolving credit agreements? Do you also agree with the proposed transitional period?

*Requirement to include insurance details in offer letters*

- 6.14 We have granted a waiver by consent for MCOB 6.4.4R(10) since 31 October 2004. The rule requires firms to include in their offer documents details of non-tied insurance policies that customers decide to take out, irrespective of whether these details were in the KFI. In granting the waiver, we agreed that this requirement was unduly burdensome and disproportionate given other disclosure requirements in ICOB and MCOB.
- 6.15 We now propose to delete MCOB 6.4.4R(10) for the same reasons for which we granted the waiver by consent, effectively making the waiver permanent. The original waiver would have run out on 30 April 2006 for most firms, but we have extended this to 31 October 2006 to cover the period of consultation.
- 6.16 There is an equivalent rule for lifetime mortgages (MCOB 9.5.4R(9)). We also propose deleting this rule for the same reasons.
- 6.17 Firms who have not taken advantage of the waiver for MCOB 6.4.4R(10) and currently comply with MCOB 6.4.4R(10) and MCOB 9.5.4R(9) can continue to do so after these rules are deleted since our rules already allow for the inclusion of such additional details within the offer document.

Q10: Do you agree with the proposal to delete these rules?

*Annual statement requirements*

- 6.18 The current rule in MCOB 7.5.1R requires firms to provide customers with a statement at least once a year. Many lenders send all their statements in the same month of the year. This means that if a mortgage completes in the month before this, the customer may receive a statement where the only transaction shown is the release of funds.
- 6.19 Customers will already have received this information in the start of contract disclosure required under MCOB 7.4, and we do not believe there is any benefit in their receiving it again in the statement. We therefore propose to allow firms thirteen months in which to send the first 'annual' statement. (We have already granted a modification to this effect to one firm.) Under the proposed change, the firm can send the statement at any point within this 13 month period. There is no requirement that firms must wait until the thirteenth month if they do not wish to. Firms will still have to send later statements at least every 12 months.

Q11: Do you agree with the proposed change to our annual statement rules? If not please state your reasons.

*Providing KFIs for post-sale variations*

- 6.20 MCOB 7.6.27R provides replacement text for Section 2 of the KFI in cases where a party is added to or removed from an existing regulated mortgage contract (a ‘transfer of equity’). However, the text only covers non-advised cases. Rather than adding more prescribed text to deal with an advised transfer of equity, we are proposing to delete MCOB 7.6.27R and rely on the general provision at MCOB 7.6.25R. This general provision allows the KFI to diverge from the requirements in MCOB 5 “where it is necessary to do so in order to reflect the fact that the illustration is being provided in respect of the addition or removal of a party to the contract”.
- 6.21 This approach would follow the line we have taken for all other forms of variation discussed in MCOB 7, where we have used a general rule allowing firms to amend the illustration as necessary rather than prescribe text. Allowing firms to choose wording which best suits their circumstances follows our stated aim of reducing our detailed requirements and giving firms’ senior management more responsibility for the conduct of their business.

Q12: Do you agree with our proposal to delete this rule? If not please state your reasons.

**Cost-benefit analysis**

- 6.22 The changes we are proposing to make fall into two groups:
- changes which would have no costs or costs of minimal significance; and
  - changes which would result in some extra costs to firms.

*Changes which would have no costs or costs of minimal significance*

- 6.23 The following changes are expected to have no costs or costs of minimal significance for firms and consumers, so we will not provide a full costs benefit analysis (CBA). To ensure transparency and accountability, we have outlined our expectations of the costs and benefits. These changes are all permissive, meaning that the change in rules will allow firms to choose whether to continue with their existing practices or alter them to reflect the amendment. It is anticipated that firms will only change their practices if it is to their advantage. This will limit any costs.

- (1) *Deleting MCOB 6.4.4R(10) and 9.5.4R(9) (Requirement to include insurance details in offer letters)* This change removes a burden from lenders. Most lenders are already taking advantage of the waiver granted to MCOB 6.4.4R(10), so this will not change their current practice. Consumer protection will not be reduced because consumers must still receive information on tied insurance products at the offer stage, and information on all associated insurance products in the start of contract disclosure documentation.
- (2) *MCOB 3.6.3R(2)(a) and (b) (Comparative advertising rules)* The amendment will benefit both firms and consumers by allowing qualifying credit to be compared with a greater range of credit meeting the same needs or intended for the same purpose. Consumer protection will not be reduced as misleading comparisons with services or products which do not meet the same needs will remain prohibited.
- (3) *MCOB 3.6.5G(2) (APRs in long shelf-life publications)* This amendment will remove an unintended barrier to firms wishing to advertise in this type of publication, allowing them greater choice of marketing channel. It will allow credit-impaired consumers to receive more information about their access to credit. The risk that the APR in these adverts may become out of date will be balanced by the required warning to this effect. So we do not believe this change will lead to any increased risk to consumers.
- (4) *MCOB 3.6.13R (Risk warnings in financial promotions)* These changes should make it easier for firms to produce promotions where the risks to consumers are accurately explained, and which avoid unnecessary duplication. A risk warning of some kind must be given whether or not the firm takes advantage of the new rule, and therefore consumer protection will not be diminished.
- (5) *MCOB 7.5.1R (Annual statement requirements)* Consumers will still receive a statement at the earliest point at which it will contain meaningful information, and so there will be no reduction in consumer protection.
- (6) *Deleting MCOB 7.6.27R (Providing for post sale variations)* This change removes the requirement for firms to use prescribed text in Section 2 of KFI provided when a party is being added to or removed from the contract. Firms will be given greater freedom, under the general provision in MCOB 7.6.25R, to provide information tailored to consumers' circumstances. Consumers will benefit from receiving information which is more accurate and meaningful to them. We believe that firms will produce their own compliant description through a one-off, central process. We expect that this will not result in costs of more than minimal significance. In more complex cases this description may not be adequate anyway. Firms currently deal with this situation through a re-mortgage and the proposed change will not affect this.



*Changes which would result in some extra costs for firms*

- 6.24 We are also proposing to clarify the way firms disclose flexible mortgages in the KFI, which may result in some extra costs for firms.
- 6.25 At present MCOB is not clear about how firms should disclose a flexible mortgage product with a pre-defined drawdown facility in the KFI in cases where the flexible mortgage is also a revolving credit facility. Firms are currently adopting different approaches in producing KFIs for these products. In the two variations we have identified some firms are separating the loan amount from the additional draw down facility and therefore illustrating Sections 3, 5 and 6 based on the actual loan amount. Others are illustrating this product using the combined amount of the actual loan and the additional facility which is often much higher and does not represent the repayments consumers will make. This leads to potential difficulty for consumers using the KFI to compare similar products from different providers. It may also make it difficult for consumers to determine the true cost of their mortgage before they commit to it.
- 6.26 These difficulties may lead to consumer confusion. The intended outcome of this change is that customers will receive an illustration based on the amount they are borrowing and not the amount they could potentially borrow, which will be illustrated separately. Illustrating an APR and monthly repayments which reflect the cost of the actual borrowing may better allow customers to assess the suitability of the product and increase their ability to make comparisons. Our informed view is that this will lead to some consumers purchasing products which are more suitable to their needs.
- 6.27 We do not expect any additional direct costs to us resulting from this change.
- 6.28 We do not believe there will be costs of more than minimal significance for firms where they are already producing their KFIs in line with our proposed change. Based on internal and external data, our estimates of the market suggest that up to 35 lenders currently provide this type of flexible product with a pre-defined draw down facility. Of these, 10 lenders account for around 80% of the sales and are typically larger lenders. Our inquiries have shown that these 10 lenders are already producing KFIs in the way we propose.
- 6.29 Some of the 25 remaining lenders may need to make changes to their pre-sale disclosure documentation incurring some limited costs. We do not expect these changes will create ongoing costs, but discussions with a limited number of firms indicate that they will generate one-off costs. These costs will include changes to systems, including testing and possibly communications and training and competence costs. Discussion with firms leads us to believe that these one-off compliance costs will be between £12,500 and £15,000 per firm. If all the remaining firms who offer this product do need to make these changes, we estimate that the upper limit for aggregate compliance costs will not be more than £400,000. However, our initial consultation strongly

suggests that the number of firms affected, and therefore the total costs, will be much lower than this. We would welcome views on these estimates.

- 6.30 Overall, we expect this change to make the features and costs of this type of product more transparent and easier to compare in the pre-sale disclosure. There may be a greater negative impact on smaller firms or firms who do not sell this type of product in large volumes. The cost of this change will be proportionately higher to these firms, who may have fewer resources with which to make the required changes.

### **Compatibility statement**

- 6.31 We believe that changing the rules on how flexible mortgages are illustrated in the KFI will help us to meet our objective of securing the appropriate degree of consumer protection. We also believe that the costs this will impose on firms are proportionate to the resulting benefits to consumers of receiving information that better allows them to purchase products most suitable to their needs.
- 6.32 The changes to the other rules concerning the content of the KFI and to financial promotions will enhance consumer protection by clarifying the information consumers receive. In removing unnecessary burdens placed on firms by the requirement to include insurance details in the offer letter, by the annual statement rules, and by the current duplication of risk warnings in financial promotions, we are acting proportionately. We are promoting senior management responsibility by allowing firms more discretion to tailor their disclosure documentation to the needs and circumstances of their customers. Making clear that firms can use long shelf-life publications to advertise all mortgages follows our principle of facilitating competition between regulated firms. For these reasons, we consider these proposals the most appropriate way of meeting our regulatory objectives.

### **Contact**

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

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# 7 Proposed amendments to the Complaints against the FSA sourcebook

## Introduction

- 7.1 This chapter proposes two sets of amendments to the *Complaints against the FSA sourcebook* (COAF). We would make these amendments under section 157(1) (Guidance) of, and paragraph 7 of Schedule 1 to, the Financial Services and Markets Act 2000 (FSMA).
- 7.2 These amendments are relevant to firms, consumers and any other parties who may wish to make a complaint against the FSA.
- 7.3 The two sets of amendments relate to:
- removal of the requirement that the Complaints Commissioner must vacate his office on reaching the age of 70; and
  - other minor amendments to COAF.
- 7.4 The text of the proposed amendments is set out in of Appendix 7 to this CP, which is divided into two Parts to reflect the two sets of changes described below.

## Part 1: Age disqualification

### *Proposed amendment*

- 7.5 The Employment Directive (2000/78/EC) requires member states to outlaw discrimination on the grounds of religion or belief, disability, age and sexual orientation in the fields of employment and vocational training. The government will implement the parts of the Directive relating to age through Regulations which will come into force on 1 October 2006.

- 7.6 We have reviewed our rules and guidance to identify provisions that affect employment or vocational training and which might be considered to discriminate on grounds of age, either directly or indirectly. Both the Directive and the forthcoming Regulations will allow discriminatory treatment to be maintained where it can be objectively justified. And we have elected to maintain some existing rules and guidance that provide for the experience of certain bodies or persons to be taken into account on this basis.
- 7.7 Our review identified only one provision that discriminates directly. COAF currently provides that a person who reaches the age of 70 is not eligible to be or to remain as the Complaints Commissioner.
- 7.8 On reflection, we feel that we should be in a position to appoint the most suitable candidate for the post, regardless of age, and so we propose to delete this provision from COAF (COAF 1.3.2G(2)).
- 7.9 We are retaining a number of other provisions in relation to the Complaints Commissioner. In particular, appointments must be approved by the Treasury. In addition, COAF will continue to provide that the Complaints Commissioner will be appointed for a three-year fixed term and that he may be dismissed, with the consent of the Treasury, if he is incapacitated by physical or mental illness or is unfit to perform his functions for any other reason.

#### *Cost benefit analysis*

- 7.10 The proposed amendment only affects our selection or retention of a Complaints Commissioner. No additional costs are expected to arise as a result making the proposed change.

#### *Compatibility statement*

- 7.11 We are satisfied that the proposed amendment to COAF is the most appropriate way to meet the requirements of the Employment Directive and the forthcoming government regulations on age discrimination. This is because the upper age limit in COAF discriminates directly against older people and is not justified in the light of new legislation. As a result we consider that the amendment is compatible with and appropriate for meeting our statutory objectives. The complaints scheme is designed to help us meet all our objectives by ensuring that we deal with complaints in a robust and effective way, and the proposed amendment will not compromise the scheme.
- 7.12 We believe the amendment will have no significant impact, and no negative impact, on the principle of good regulation.

## Part 2: Other minor changes

### *Proposed amendments*

- 7.13 We are also proposing other amendments to COAF. We consider these to be part of a constructive development of the Complaints Scheme and think they will help it operate more efficiently for complainants and for us.
- 7.14 These proposals aim to clarify, and make explicit in the rules, the operational practice of the Complaints Scheme, by:
- (1) (COAF 1.4.7G and 2.3.7G) letting complainants know that FSA costs, and any costs of the Complaints Commissioner, incurred investigating a complaint under the processes of the Complaints Scheme, will not be sought from the complainant;
  - (2) (COAF 1.5.2AG and 2.4.2AG) making plain that our procedure for investigating a complaint involves only a review of the complainant's allegations and supplied supporting evidence, subject to any request by us for further information from the complainant;
  - (3) (COAF 1.5.6AG and 2.4.6AG) introducing a time-limit for complainants to refer any FSA decision to the Complaints Commissioner and to give him the discretion to decline to accept a referral from a complainant beyond the time limit: it is in the best interests of the complainant and the FSA that if our decision is disputed then the matter is reviewed promptly by the Complaints Commissioner; and
  - (4) (COAF 1.5.19AG and 2.4.18AG):
    - (a) formally stating the Complaints Commissioner's current practice of issuing a preliminary report of his investigation and his setting of a time-limit for the FSA and complainants to respond to him with any comments; and
    - (b) stating clearly that the Complaints Commissioner's final report will be regarded by the FSA and the Complaints Commissioner as the final action taken in regard to a complaint investigation under the process allowed for by COAF.

### *Cost benefit analysis*

- 7.15 The changes on which we are consulting will give rise to no costs of more than minimal significance by minimising delay between Stage 1 and Stage 2 of the complaints process, and by emphasising the finality of the process at the conclusion of the Stage 2. These changes will help to reduce the administrative costs of dealing with complaints and should improve the quality of the complaints-handling process by ensuring that the speed and effectiveness of the Complaints Scheme operation is preserved in all circumstances.

### *Compatibility statement*

- 7.16 We are satisfied that the proposed amendments to COAF are designed to help us achieve our statutory objectives by ensuring that we deal with complaints in a consistent, speedy and effective manner. In relation to the principles of good regulation, we believe that the proposals are the most appropriate in regard to the need to use our resources in the most efficient and economic way. As for the other principles, we believe there will be no significant impact and no negative impact.

### **Contact**

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

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# 8 Proposed amendments to the New Collective Investment Schemes sourcebook

## Introduction

- 8.1 This chapter proposes amendments to the *New Collective Investment Schemes sourcebook* (COLL).
- 8.2 The proposed amendments:
- make changes to the provisions for determining the end of an authorised fund's initial annual accounting period;
  - clarify requirements for the information to be included in the instrument constituting a non-UCITS retail scheme;
  - clarify the basis on which certain charges and expenses may be taken from the scheme property of an authorised fund; and
  - introduce a new transitional provision for authorised funds that currently comply with the Collective Investment Schemes sourcebook (CIS) and will be in the process of being wound up at 12 February 2007, when CIS will be revoked.
- 8.3 We would make these amendments under sections 138, 140, 156, 157, 238(5), 242, 247 and 248 of the Financial Services and Markets Act 2000 (FSMA) and regulation 6 of the Open-Ended Investment Companies Regulations 2001. The text of the proposed amendments is set out in Appendix 8 to this CP. We propose that the new provisions should come into effect on 6 August 2006.
- 8.4 These proposals are relevant to authorised fund managers (AFMs) and depositaries of authorised collective investment schemes, and to investors in those schemes and prospective purchasers of units in the schemes.

## Changes to accounting periods

- 8.5 Authorised funds are required to have an annual accounting period ending on the same date in each year, and to prepare accounts as at that date which are audited and published. The fund's prospectus states the date on which the accounting period is to end, known as the accounting reference date. Depending on when we first authorise a fund and it begins to be marketed to the public, its first annual accounting period may be of less than a year's duration, in some cases no more than a couple of months long.
- 8.6 CIS, which will be revoked from February 2007, includes a rule permitting the first annual accounting period of a scheme to be extended if it would otherwise be shorter than six months. The AFM, with the agreement of the fund's appointed auditor, may disregard the first accounting reference date and treat the period up to the next accounting reference date as a single accounting period. Therefore, a fund's initial annual accounting period could be nearly 18 months long.
- 8.7 This measure was not reproduced in COLL, which is intended to be a shorter and more principle-based sourcebook than CIS. However, a number of AFMs have argued that the CIS rule is a useful tool which reduces the burden of regulation. If the initial accounting period of a fund is very short, the information in its accounts will be of little value to existing and prospective investors, who are more likely to rely on the fund's prospectus and any marketing materials produced by the AFM. Also, the accounts may not be representative of how the AFM will manage the fund in the longer term; for example, rules about the fund's spread of investments do not apply in full during the first six months of its existence. However, preparing and publishing an audited report and accounts will entail considerable expense which is likely to be borne by investors in the fund (assuming the scheme documents permit such expenses to be taken directly from the fund's property).
- 8.8 We agree that on balance it is not likely to be beneficial to investors for audited reports and accounts to be produced in such circumstances. So we propose to reintroduce the ability for the AFM, with the auditor's agreement, to extend an initial annual accounting period that would otherwise be less than six months long. We are also modifying the rule concerning the half-yearly accounting period, to make clear that the first period may be extended so it ends six months before the end of the annual period.
- 8.9 We propose one condition for AFMs that wish to extend a fund's initial accounting period. We think it is important for retail investors to have access to information about how the AFM is running the fund during this extended period – which, as mentioned above, could run to nearly 18 months (plus a further four months for preparing the report and accounts). Although there is a requirement to issue an interim report and accounts, it will not appear until nearly 14 months after the fund is launched, if the annual period is extended to its limit.

- 8.10 So we propose to introduce new guidance that an AFM should make appropriate information available to unitholders in retail funds during an extended accounting period. We will not prescribe the content or format of such information, or the way in which it is made available. As an example of information likely to meet the needs of the majority of investors in a new fund, we note it is common for AFMs to produce summaries or factsheets of fund data for marketing purposes. These typically set out a fund's broad asset allocation, a list of its most substantial holdings, and information about investment performance such as price movements and a short commentary on the markets in which the fund invests.
- 8.11 We intend for AFMs to be able to make this information available in a cost-effective manner. They might refer to it in promotional material, offer it to customers calling a helpline, publish it on the firm's website, or include it in a mailing sent for other purposes (e.g. with a periodic statement for investors holding units in an ISA).
- 8.12 In modifying these rules, we are taking the opportunity to transfer the provision on the initial accounting period from Chapter 4.5 to Chapter 6.8 of COLL, where it more logically belongs. We propose that the initial accounting periods of a qualified investor scheme (QIS) may be extended in the same way, though without equivalent guidance on making information available to investors.

Q13: Do you support the proposal to allow a fund's initial annual accounting period to be extended?

### **Other amendments to COLL**

- 8.13 We are making two proposals to modify rules in COLL in order to clarify their application.
- 8.14 The first concerns investment in government and public securities (GAPS), where the AFM wishes to take the power to invest more than 35% of the fund's assets in one or more GAPS issued by the same issuer. Where a UCITS scheme is invested in this way, in order to meet the requirements of the UCITS Directive<sup>5</sup> both the instrument constituting the scheme and the prospectus must list individually the issuers of GAPS that the AFM may invest in.
- 8.15 For a non-UCITS retail scheme (NURS) invested in this way, we consider that publishing the list of GAPS issuers in the fund prospectus provides adequate disclosure to investors. It is onerous for the AFM to make changes to a fund's instrument each time it wishes to add or remove an issuer, but since investors rarely if ever ask to see a copy of the instrument, reproducing the information there is of little advantage to them. Consequently, we do not believe that applying this Directive requirement to funds outside the scope of the Directive would enhance investor protection.

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5 Directive 85/611/EEC as amended.



- 8.16 However, COLL 5.6.8R currently requires the AFM of a NURS to follow in full the disclosure provisions that apply to a UCITS scheme invested in GAPS. So we propose to disapply this provision from a NURS as it relates to the instrument constituting the scheme, while maintaining full disclosure in the fund's prospectus.
- 8.17 The second change modifies the rule (COLL 6.7.12R) that bans promotional payments being taken from the property of a retail fund, except for permitted payments to the AFM. We explain in guidance (COLL 6.7.13G) that costs for preparing the simplified prospectus or the key features of the fund are exempted from this general prohibition. However, the current drafting of the sourcebook is not satisfactory, because guidance cannot relieve an authorised person from a duty imposed by a rule in the Handbook.
- 8.18 We therefore propose to recast the relevant rule and guidance so as to achieve the same purpose while giving legal certainty to AFMs. Please note that the only expenses chargeable to the fund are those which are set out in the fund's prospectus, and they may include preparation and printing costs but not distribution costs.

Q14: Do you agree that these changes are appropriate?

### **Transitional provisions**

- 8.19 Authorised funds that currently comply with CIS are required instead to comply with COLL by no later than 12 February 2007. There are likely to be a considerable number of funds at that date which, although retaining their authorised status, will be in the process of being wound up in line with the rules of CIS. They will have no unitholders, and the property of the fund (other than a provision for outstanding expenses) will have been distributed to unitholders, or transferred to another fund under a scheme of arrangement approved by unitholders.
- 8.20 The reason for retaining the authorised status of these funds is to carry out an orderly winding-up and to ensure that any outstanding liabilities due to or from the fund, such as overseas tax payments, are settled as efficiently as possible. In such circumstances, no useful purpose would be achieved by requiring the AFM and depositary of the fund to carry out changes to ensure compliance with COLL, incurring costs which would have to be taken from the remaining assets of the fund.
- 8.21 We propose that funds that are winding-up will be deemed compliant with COLL, provided they continue to comply instead with the relevant rules of CIS as if those rules still applied to them, until the winding-up is complete and their authorised status is revoked. The transitional provision will apply to:



- any authorised unit trust whose manager or trustee has applied for the revocation of the authorisation order of the scheme under section 256 of FSMA, which the FSA has granted before 12 February 2007 on condition that the winding-up of the scheme is first completed;
- any authorised unit trust subject to a scheme of arrangement effected under section 251 (4) of FSMA before 12 February 2007; and
- any ICVC that has applied under regulation 21(1)(d) of the OEIC Regulations<sup>6</sup> to be wound up, where the proposal has been effected under regulation 21(3) before 12 February 2007.

8.22 This provision is not intended as an extension to the period available to AFMs to undertake the process of making their range of funds compliant with COLL. AFMs should consider carefully what steps they need to take, which may include the convening of unitholder meetings, and should plan a suitable timetable to meet the 12 February 2007 deadline.

Q15: Will the proposed transitional provision give sufficient flexibility to AFMs and depositaries of schemes in the process of being wound up at 12 February 2007?

## **Cost benefit analysis**

8.23 Our proposals are permissive and deregulatory in nature, and do not impose requirements that differ significantly from existing policy. Either they generate costs of no more than minimal significance for firms, or they enable a net saving in costs to be achieved (for example, through AFMs providing focused information about a new fund's investment and performance, instead of publishing audited reports and accounts). We think these proposals will benefit firms and consumers without generating additional risk. For these reasons, we are satisfied that a full cost benefit analysis of the proposals is not necessary.

## **Compatibility statement**

8.24 We believe that the proposals outlined in this chapter are compatible with our general duties under section 2 of FSMA, and in particular with our statutory objective of consumer protection under section 5. We have had regard to the principles of good regulation in section 2(3), especially the following:

*The principle that a burden or restriction which is imposed on a person, or on the carrying out of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction*

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<sup>6</sup> The Open-Ended Investment Companies Regulations 2001 (SI 2001 no. 1228) as amended.

- 8.25 The proposals are intended to remove prescriptive measures where we do not consider the benefits sufficient to justify such prescription. Producing audited accounts for a very recently-launched fund is of limited use to investors, but the costs are a burden on either the AFM or the fund itself. Other types of information can meet investors' needs at a lesser cost, and we consider it right in this situation to rely on firms' duty to treat their customers fairly in the way they provide it. In proposing to relieve funds that are to be wound up from the obligation to convert to COLL, we are likewise seeking to remove a cost burden that will result in no appreciable benefit to markets or consumers.

*Acting in a way which we consider most appropriate for the purpose of meeting our statutory objectives*

- 8.26 In proposing these changes we have sought to allow greater flexibility where it is possible to do so, in one case recommending appropriate disclosure to retail investors as a balance to the removal of a regulatory obligation. In this way, we aim to maintain authorised funds as vehicles which offer appropriate degrees of protection to different categories of consumers, according to their experience and needs. Other changes are intended to remove ambiguity from our rules and to facilitate cost-saving. These measures should maintain confidence in UK authorised funds as an attractive and efficient investment vehicle, thus helping to promote confidence in the UK financial system as a whole. For these reasons, we consider that our proposals are the most appropriate way of acting to meet our statutory objectives.

## **Contact**

We invite comments on the proposed amendments. Comments should reach us by 6 June 2006. Please send them to:

Mark Glibbery  
Retail Policy Division  
Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

Telephone      020 7066 0594  
Fax:              020 7066 0595  
Email:           cp06\_06@fsa.gov.uk

## List of specific consultation questions

### Chapter 2

- Q1 Do you agree to the definition of ‘inter-professional investments’ being amended to include units in exchange traded funds?

### Chapter 3

- Q2 Do you agree with our proposed transitional period for this change?

### Chapter 4

- Q3 Do you agree with our proposal that those small firms listed in paragraph 4.8 that are only required to appoint an auditor under the CA, by virtue of holding permissions under Part IV of FSMA, should be included in the proposed audit exemption or should the current audit requirement in the CA remain in force?
- Q4 Do you agree with our proposal that firms that do hold client assets or client money should still be required to appoint an auditor under SUP 3 for the purposes of a client assets audit?
- Q5 Do you agree with our proposals to enable firms that are able to benefit from the audit exemption under the CA to submit unaudited financial reports to the FSA?
- Q6 Do you agree with our proposal that firms that qualify for the small company audit exemption should be allowed to include unaudited reserves and unverified interim profits within their capital resources calculation and, where relevant, calculate their annual expenditure with reference to unaudited financial statements?
- Q7 We invite firms’ views on the cost estimates and allocation outlined above.

### Chapter 6

- Q8 Do you agree with the proposed changes to our rules on financial promotions in MCOB 3? If not, please state your reasons.
- Q9 Do you agree with our proposed rule changes for flexible mortgages that are revolving credit agreements? Do you also agree with the proposed transitional period?
- Q10 Do you agree with the proposal to delete these rules (MCOB 6.4.4R(10) and MCOB 9.5.4R(9))?

- Q11 Do you agree with the proposed change to our annual statement rules? If not please state your reasons.
- Q12 Do you agree with our proposal to delete this rule (MCOB 7.6.27R)? If not please state your reasons.

### **Chapter 8**

- Q13 Do you support the proposal to allow a fund's initial annual accounting period to be extended?
- Q14 Do you agree that these changes are appropriate?
- Q15 Will the proposed transitional provision give sufficient flexibility to AFMs and depositaries of schemes in the process of being wound up at 12 February 2007?

**INTER-PROFESSIONAL INVESTMENTS (EXCHANGE TRADED FUNDS)  
INSTRUMENT 2006**

**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 powers);
  - (2) section 156 (General supplementary powers).

**Commencement**

- B. This instrument comes into force on 6 August 2006.

**Amendments to the Handbook**

- C. The Glossary of definitions is amended in accordance with the Annex to this instrument.

**Citation**

- D. This instrument may be cited as the Inter-Professional Investments (Exchange Traded Funds) Instrument 2006.

By order of the Board  
20 July 2006

## Annex

### Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text. Where new definitions are being inserted, the text is not underlined.

<i>inter-professional investment</i>	<p>any of the following investments specified in Part III of the <i>Regulated Activities Order</i> (Specified investments) <u>or, in the case of units in an exchange-traded fund, defined in the <i>Glossary</i>:</u></p> <ul style="list-style-type: none"> <li>(a) <i>share</i> (article 76);</li> <li>(b) <i>debenture</i> (article 77);</li> <li>(c) <i>government and public security</i> (article 78);</li> <li>(d) <i>warrant</i> (article 79);</li> <li>(e) <i>certificate representing certain securities</i> (article 80);</li> <li>(f) <i>option</i> (article 83); for the purposes of the <i>permission</i> regime, this is sub-divided into: <ul style="list-style-type: none"> <li>(i) <i>option</i> (excluding a <i>commodity option</i> and an <i>option on a commodity future</i>);</li> <li>(ii) <i>commodity option</i> and <i>option on a commodity future</i>;</li> </ul> </li> <li>(g) <i>future</i> (article 84); for the purposes of the <i>permission</i> regime, this is sub-divided into: <ul style="list-style-type: none"> <li>(i) <i>future</i> (excluding a <i>commodity future</i> and a <i>rolling spot forex contract</i>);</li> <li>(ii) <i>commodity future</i>;</li> <li>(iii) <i>rolling spot forex contract</i>;</li> </ul> </li> <li>(h) <i>contract for differences</i> (article 85); for the purposes of the <i>permission</i> regime, this is sub-divided into: <ul style="list-style-type: none"> <li>(i) <i>contract for differences</i> (excluding a <i>spread bet</i> and a <i>rolling spot forex contract</i>);</li> <li>(ii) <i>spread bet</i>;</li> <li>(iii) <i>rolling spot forex contract</i>;</li> </ul> </li> </ul>
--------------------------------------	---

- (i) *rights to or interests in investments* in (a) to (h) (article 89);
- (j) *units in an exchange traded fund.*

Insert the following new definition in the appropriate alphabetical position:

*exchange  
traded fund*

a fund:

- (a) which is an *open-ended investment company*; and
- (b) the *units* in which are traded on a *regulated market* or *designated investment exchange*.





## KEYFACTS LOGO INSTRUMENT 2006

### 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 powers);
  - (2) section 156 (General supplementary powers); and
  - (3) section 157(1) (Guidance); and
- 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 [6 November] 2006.

### 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).

General amendment to Handbook forms	Annex A
General Provisions (GEN)	Annex B
Conduct of Business sourcebook (COB)	Annex C
Insurance: Conduct of Business sourcebook (ICOB)	Annex D
Mortgages: Conduct of Business sourcebook (MCOB)	Annex E



### Citation

- E. This instrument may be cited as the Keyfacts Logo Instrument 2006.

By order of the Board  
[28 September] 2006

**Annex A****General amendment to Handbook forms**

All instances in the Handbook of the keyfacts logo in column (1) of the table below are replaced with the keyfacts logo and regulatory mark in column (2) of the table.

(1)	(2)
	

## Annex B

## Amendments to the General Provisions sourcebook

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

...

GEN 5 The FSA logo and the keyfacts logo

...

~~Purpose~~ The FSA logo

5.1.2 G ...

...

The keyfacts logo

5.1.4A G The keyfacts logo is a registered Community trade mark, with the number 3866688, and is the property of the FSA. It is also subject to copyright and may be used or reproduced with permission of the FSA only. If the keyfacts logo is reproduced or otherwise used by any person without such permission the FSA may seek to enforce its rights over its property through the courts.

5.1.4B G GEN 5 Annex 2G is a general licence which sets out the circumstances in which the FSA permits firms and their appointed representatives to reproduce the keyfacts logo.

5.1.5 R A firm must not use the keyfacts logo other than as and when it is required or permitted to be used by the rules, and in accordance with the general licence in GEN 5 Annex 2G.

...

After GEN 5 Ann 1G insert the following new annex, GEN 5 Ann 2G. The inserted text is not underlined.

Annex 2 G Licence for use of the keyfacts logo by authorised firms and appointed representatives

Application

1.1 The FSA grants this licence to *firms* and *appointed representatives*.

## The keyfacts logo

- 2.1 The keyfacts logo is made up of two elements:
  - (1) the symbol (the rectangular speech bubble); and
  - (2) the word 'keyfacts'.
- 2.2 Together, these elements make up the registered Community trade mark, with number 3866688.
- 2.3 There are two versions of the keyfacts logo, a low resolution version and a high resolution version.
- 2.4 Copyright subsists in the keyfacts logo.
- 2.5 Copies of the keyfacts logo that are capable of being reproduced for printing can be found on the *FSA's* website at [http://www.fsa.gov.uk/Pages/Library/Other\\_publications/Logos\\_and\\_Photos/index.shtml](http://www.fsa.gov.uk/Pages/Library/Other_publications/Logos_and_Photos/index.shtml).

## Permission to use the keyfacts logo

- 3.1 A *firm* and its *appointed representatives* are permitted to use the keyfacts logo as and when it is required or permitted to be used by the *rules*.
- 3.2 The following are examples of places where the *rules* require or permit the keyfacts logo to be used:
  - (1) In *COB*:
    - (a) in an initial disclosure document or combined initial disclosure document (*COB* 4.3.9R); and
    - (b) in a fees and commission statement (*COB* 4.3.11R).
  - (2) In *ICOB*:
    - (a) in an initial disclosure document or combined initial disclosure document (*ICOB* 4.2.4G to *ICOB* 4.2.7R);
    - (b) in a *policy summary* (*ICOB* 5.5.5R); and

- (c) in a *key features* as an alternative to a *policy summary* (ICOB 5.5.4R).
- (3) In *MCOB*:
  - (a) in an initial disclosure document or combined initial disclosure document (*MCOB* 4.4.1R, *MCOB* 4.4.7R, *MCOB* 8.3.1R and *MCOB* 8.4.1R); and
  - (b) in an *illustration* (*MCOB* 5.6.2R and *MCOB* 9.4.2R).

#### Conditions on appearance of the keyfacts logo

- 4.1 The permission in paragraph 3.1 is subject to the following conditions:
  - (1) the regulatory mark is attached to the keyfacts logo;
  - (2) the keyfacts logo and regulatory mark appear:
    - (a) in black type;
    - (b) reversed out white on a coloured background; or
    - (c) in colour provided that this does not diminish their prominence;
  - (4) the two elements of the keyfacts logo appear together in the same way, and in the same proportion, as in the Community trade mark;
  - (5) the keyfacts logo is not redrawn in any way, or matched by a typesetter;
  - (6) the low resolution version of the keyfacts logo is used only in documents intended to be read on a computer, television or other screen; and
  - (7) if the keyfacts logo is reproduced electronically, no hyperlink is incorporated.

#### Further conditions on the use of the keyfacts logo

- 5.1 The permission in paragraph 3.1 is also subject to the conditions that any material, whether produced on paper or electronically, on which

the keyfacts logo is displayed does not:

- (1) in any way imply that the *FSA* is endorsing the *firm* or its *appointed representatives* or products, services or communications (see also *GEN* 1.2.2R(1)); or
- (2) misrepresent the *firm's* or its *appointed representative's* relationship with the *FSA* or present false information about the *FSA*; or
- (3) contain content that could be construed as distasteful, offensive or controversial; or
- (4) infringe any intellectual property or other rights of any *person* or otherwise not comply with any relevant law or regulation.

#### Commencement and duration

- 7.1 This licence comes into effect on 6 November 2006 with the exception of paragraph 4.1(1) which comes into effect on 6 November 2007.
- 7.2 The *FSA* may alter or revoke this licence at any time, by giving at least two months' notice on the *FSA's* website.

#### Interpretation

- 8.1 This licence is to be interpreted in accordance with chapter 2 of the General provisions (Interpreting the Handbook) of the *FSA's* Handbook of Rules and Guidance. In particular, expressions in italics are defined in the Handbook Glossary.

#### Governing law and jurisdiction

- 9.1 This licence is governed by and interpreted in line with English law. The courts of any jurisdiction in the United Kingdom have the exclusive jurisdiction to settle any dispute in connection with this licence.

## Annex C

## Amendments to the Conduct of Business sourcebook

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

...

4.3.10 G ~~Firms can obtain from the FSA website <http://www.fsa.gov.uk> a specimen of the initial disclosure document.~~ Further requirements regarding the use of the logo and the location of specimens are set out in *GEN 5.1* and *GEN 5 Annex 2G*. ...

...

COB 4 Annex 4R: Initial disclosure document required by COB 4.3.9R(1) ("IDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in *GEN 5.1* and *GEN 5 Annex 2G*. ~~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).~~

...

COB 4 Annex 5R: Combined initial disclosure document required by COB 4.3.9R(2) ("CIDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in *GEN 5.1* and *GEN 5 Annex 2G*. ~~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).~~

...

COB TP 4 Miscellaneous transitional provisions applying to all firms

TP 4.4

(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
...	...	...	...	...	...
18	<u>COB 4 Annex 4R</u> , <u>COB 4 Annex 5R</u> and <u>COB 4</u>	<u>R</u>	<u>Key facts logo</u> <u>A firm may continue to use a keyfacts logo</u>	<u>From 6 November 2006 to 6</u>	<u>6 November 2006</u>

	<u>Annex 6R</u>		<u>which is not accompanied by a registered trademark symbol.</u>	<u>November 2007</u>	
--	-----------------	--	---	--------------------------	--



## Annex D

## Amendments to the Insurance: Conduct of Business sourcebook

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

...

'Key facts' logo

- 2.2.2 R ~~A firm must not use the key facts logo unless it is required by a rule.~~[deleted]

...

Clear, fair and not misleading: comparisons ~~and restrictions on the use of the~~  
key facts logo

- 3.8.1 R ...

(3) ~~A non-investment financial promotion must not contain the key facts logo unless it is required by a rule.~~[deleted]

...

- 5.5.11 R ... The logo may be a different size from that in *ICOB* 4 Annex 1 ~~but its proportions must not be distorted.~~

- 5.5.12 G The *FSA* has developed a common 'key facts'keyfacts logo to be used on significant pieces of information directed to *customers*. Further requirements regarding the use of the logo and the location of specimens are set out in GEN 5.1 and GEN 5 Annex 2G. ~~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).~~

...

ICOB 4 Annex 1G: Initial disclosure document ("IDD")

...

**Note 2** – ... *ICOB* 4.2.6R sets out the principal requirements on the use of the key factskeyfacts logo. Further requirements are set out in GEN 5.1 and GEN 5 Annex 2G. ~~A specimen of the key facts~~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).~~

...

## ICOB 4 Annex 2R: Combined initial disclosure document ("CIDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in *GEN 5.1* and *GEN 5 Annex 2G*. ~~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).~~

...

## ICOB TP 1 Transitional provisions

## TP 1.1

(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
...	...	...	...	...	...
<u>11</u>	<u>ICOB 4 Annex 1G</u>	<u>G</u>	Key facts logo <u>A firm may continue to use a keyfacts logo which is not accompanied by a registered trademark symbol.</u>	From <u>6 November 2006</u> to <u>6 November 2007</u>	<u>6 November 2006</u>
<u>12</u>	<u>ICOB 4 Annex 2R</u>	<u>R</u>	Key facts logo <u>A firm may continue to use a keyfacts logo which is not accompanied by a registered trademark symbol.</u>	From <u>6 November 2006</u> to <u>6 November 2007</u>	<u>6 November 2006</u>

## Annex E

## Amendments to the Mortgages: Conduct of Business sourcebook

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

...

'Key facts' logo

- 2.2.4 R ~~In MCOB, a firm must only use the 'key facts' logo where it is required by a rule.~~[deleted]

...

- 5.6.2 R An illustration provided to a customer must:

(1) ...

(2) follow the layout of the template in MCOB 5 Annex 1 with:

...

- (a) prominent use of the ~~'key facts'~~keyfacts logo followed by the text 'about this mortgage' ~~(if a firm resizes the logo it must ensure that the proportions remain consistent with the original design, so as not to distort it in any way);~~

...

...

- 5.6.4 G (1) ~~Firms can obtain from the FSA website <http://www.fsa.gov.uk> a specimen of the 'key facts' logo. When reproducing the logo firms may use colour providing this does not diminish the prominence of the logo. Further requirements regarding the use of the keyfacts logo and the location of specimens are set out in GEN 5.1 and GEN 5 Annex 2G.~~

...

- 9.4.2 R An illustration provided to a customer must:

(1) ...

(2) follow the format of the template in MCOB 9 Annex 1 with:

- (a) prominent use of the ~~'key facts'~~keyfacts logo followed by the text 'about this lifetime mortgage' ~~(if a firm resizes the logo it must ensure that the proportions remain consistent with the original design, so as not to distort it in any way);~~

...

- 9.4.3 G (1) ~~*Firms can obtain from the FSA website <http://www.fsa.gov.uk> a specimen of the 'key facts' logo. When reproducing the logo firms may use colour providing this does not diminish the prominence of the logo. Further requirements regarding the use of the keyfacts logo and the location of specimens are set out in GEN 5.1 and GEN 5 Annex 2G.*~~

...

MCOB 4 Annex 1R: Initial disclosure document ("IDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in GEN 5.1 and GEN 5 Annex 2G.

...

MCOB 4 Annex 2R: Combined initial disclosure document ("CIDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in GEN 5.1 and GEN 5 Annex 2G. 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).

...

MCOB 8 Annex 1R: Initial disclosure document ("IDD")

...

**Note 2** – ... Further requirements regarding the use of the keyfacts logo are set out in GEN 5.1 and GEN 5 Annex 2G.

...

MCOB TP 1 Transitional provisions

MCOB TP 1.1 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>9</u>	<u>MCOB 4 Annex 1R, MCOB 4 Annex 2R,</u>	<u>R</u>	<u>Key facts logo</u> <u>A firm may continue to</u>	<u>From 6 November 2006 to 6</u>	<u>6 November 2006</u>

	<u>MCOB 5 Annex 1R, MCOB 8 Annex 1R and MCOB 9 Annex 1R</u>		<u>use a keyfacts logo which is not accompanied by a registered trademark symbol.</u>	<u>November 2007</u>	
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## **CAPITAL RESOURCES FOR SMALL FIRMS INSTRUMENT 2006**

### **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);
  - (3) section 157(1) (Guidance); and
  - (4) section 340 (Appointment of auditors and actuaries).
- 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 [6 October] 2006.

### **Amendments to the Handbook**

- D. The Integrated Prudential sourcebook (PRU) is amended in accordance with Annex A to this instrument.
- E. The Interim Prudential sourcebook for Investment Businesses (IPRU(INV)) is amended in accordance with Annex B to this instrument.
- F. The Supervision manual (SUP) is amended in accordance with Annex C to this instrument.

### **Citation**

- G. This instrument may be cited as the Capital Resources for Small Firms Instrument 2006.

By order of the Board  
[28 September] 2006

## Annex A

## Amendments to the Integrated Prudential sourcebook

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

...

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

Item	Additional explanation
1. ...	
...	
3. Reserves (Notes 1 <del>and 2</del> )	...
4. Interim net profits (Notes 1 <del>and 2</del> )	...
...	
6. General/ collective provisions ( <u>Note 1</u> )	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. <u>Subject to Note 1, G-general/collective provisions must be verified by external auditors and disclosed in the <i>firm's</i> annual report and accounts.</u>
...	
Notes	
1	<del>In general, small insurance intermediaries which only carry on insurance mediation activities in relation to non-investment insurance contracts and small mortgage intermediaries, may be</del> <u>Reserves must be audited and interim net profits, general provisions and collective provisions must be verified by the <i>firm's</i> external auditor unless the <i>firm</i> is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)). If so, the <i>firm</i> may include unaudited reserves and unverified interim net profits in the calculation of its capital resources.</u>
2	<del>Mortgage lenders and mortgage administrators to which the Companies Act 1985 applies are required to appoint an auditor under that Act (section 249B (Cases where exemptions not available)). These firms will only be able to include audited reserves and verified interim net profits in the calculation of its capital resources.</del>

...



## Annex B

## 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

...

## Calculation of relevant annual expenditure

- 3-73(2) R Subject to (3) and (4) below, a *firm* must calculate its *relevant annual expenditure* with reference to the *firm's* most recent ~~audited~~ *annual financial statements* submitted to the *FSA*, as follows:

- (a) ...

Absence of ~~audited~~ annual financial statements

- 3-73(3) R If a *firm* does not have ~~audited~~ *annual financial statements*, it must:
- (a) where it has just commenced trading or has not been authorised long enough to have submitted ~~audited~~ *annual financial statements* to the *FSA* (or to the *FSA's* predecessor), base its *relevant annual expenditure* on budgeted or other accounts which it submitted to the *FSA* (or to the *FSA's* predecessor) as part of its application; or
- (b) ...

## Appendix 1 – Glossary of Terms for IPRU(INV) 3

...

*annual accounting reference date* means the date as at which the ~~audited~~ *annual financial statements* are prepared as initially notified by the *firm* to the *FSA* or as subsequently notified under rule 3-31 for all other purposes and which may not be more than 55 weeks since the previous *annual accounting reference date* or, if applicable, the date on which the *firm* commenced trading;

...

~~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~~ and, where required, an *auditor's report* ~~thereon~~;

*auditor's report* means a report drawn up in the format required by the *Supervision manual* which a *firm* must submit to the *FSA* in conjunction with the *firm's* ~~audited~~ *annual financial statements*;

...

*reporting statement*

means any one or more of the following types of report as required by the *Supervision manual*:

- (a) ~~audited~~ *annual financial statements*;
- (b) ...
- (j) the ~~audited~~ accounts of a *subsidiary* of the *firm*;

...

#### Appendix 43 - Guidance Notes on the financial resources and accounting treatment of soft commission agreements

1. ...
2. The *FSA* is of the view that it is not responsible for setting accounting policies in relation to a *firm's* ~~audited~~ *annual financial statements*. However, the *FSA* considers that it is preferable for all *firms* participating in "soft commission agreements" to have consistent accounting policies. Without such consistency, certain *firms* would have a competitive advantage in terms of their *financial resources*. Therefore, for the purposes of completing *financial reporting statement* submitted to the *FSA*, appropriate accounting policies should be used. The guidance and interpretations made in this Appendix should be considered in this context.
3. ...

...

## Chapter 5: Interim Prudential Requirements for Former IMRO Firms

...

TABLE 5.2.2(1) CALCULATION OF OWN FUNDS AND LIQUID CAPITAL

## PART I

## METHOD OF CALCULATION

A *firm* must calculate its *own funds* and *liquid capital* as shown below, subject to the detailed requirements set out in Part II.

Financial resources	Category	Part II Para
Tier 1		
(1) Paid-up share capital (excluding preference shares)	A	2
(2) Share premium account		
(3) <del>Audited</del> Reserves		2A
(4) Non-cumulative preference shares		
...		

...

## PART II

## DETAILED REQUIREMENTS

1 Ratios

...

(Items 10, 11 and 15)

...

2A ~~Audited~~ Reserves

...

**Note 1**A *firm* should keep a record ...**Note 2**

Reserves must be audited unless the *firm* is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).

...

8 Net trading book profits ...	
(Item 14)	<p><b>Note</b></p> <p><i>Non-trading book</i> interim profits may only be included in Tier 1 of the calculation if they have been independently verified by the <i>firm's</i> external auditors, <u>unless the <i>firm</i> is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).</u></p>
...	

## Chapter 13: Financial Resources Requirements for Personal Investment Firms

...

## Calculation

- 13.10.2 R A *Category B firm's own funds* must be calculated in accordance with table 13.10(2).

Table 13.10(2)

This table forms part of *rule* 13.10.2

OWN FUNDS	
Companies	Sole Traders: Partnerships
Paid-up <i>share</i> capital (excluding preference <i>shares</i> redeemable by shareholders within 2 years) <i>Share</i> premium account <del>Audited</del> + Retained profits (see 13.10.2AR) and <del>verified</del> interim net profits ( <u>Note 1</u> ) ...	...
<p><b><u>Note 1</u></b></p> <p><u>Retained profits must be audited and interim net profits must be verified by the <i>firm's</i> external auditor, unless the <i>firm</i> is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).</u></p>	

- 13.10.2A R For the purpose of calculating a *Category B firm's own funds*, the following adjustments apply to ~~audited~~ retained profits or, (for non-corporate entities), current accounts figures:

(1) ...

...

...

## Annex C

## Amendments to the Supervision manual

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

...

3.1.1A    G    For the avoidance of doubt, this chapter does not apply to the following firms if they do not hold *client money* or client assets and do not appoint an auditor under or as a result of a statutory provision other than in the *Act*:

- (1)    *authorised professional firms*;
- (2)    *energy market participants, including oil market participants, to whom IPRU(INV) 3 does not apply*;
- (3)    *exempt insurance intermediaries*;
- (4)    *insurance intermediaries not subject to SUP 3.1.2R(10)*;
- (5)    *investment management firms*;
- (6)    *mortgage administrators*;
- (7)    *mortgage intermediaries*;
- (8)    *mortgage lenders*;
- (9)    *personal investment firms, including small personal investment firms*;
- (10)    *securities and futures firms*; and
- (11)    *service companies*.

3.1.2        R    Applicable sections (see SUP 3.1.1R)

(1) Category of firm		(2) Sections applicable to the firm	(3) Sections applicable to its auditor
(1)	<i>Authorised professional firm</i> which is required by <i>IPRU(INV)</i> 2.1.2R to comply with chapters 3, 5, 10 or 13 of <i>IPRU(INV)</i> <u>and which has an auditor appointed under or as a result of a statutory provision other than in the <i>Act</i> (Note 1)</u>	<i>SUP</i> 3.1 – <i>SUP</i> 3.7	<i>SUP</i> 3.1, <i>SUP</i> 3.2, <i>SUP</i> 3.8 – <i>SUP</i> 3.10
...			
(7)	<i>Investment management firm, personal investment firm (other than a small personal investment firm), <del>UCITS management company</del>, or securities and futures firm (Note 3) which, in each case, has an auditor</i>	<i>SUP</i> 3.1 – <i>SUP</i> 3.7	<i>SUP</i> 3.1, <i>SUP</i> 3.2, <i>SUP</i> 3.8 – <i>SUP</i> 3.10

	<u>appointed under or as a result of a statutory provision other than in the Act</u>		
(7A)	<u>Investment management firm, personal investment firm (other than a small personal investment firm), or securities and futures firm not within (7) to which either or both of CASS 2 (Client assets) and CASS 4 (Client money and mandates: designated investment business) applies</u>	<u>SUP 3.1 – SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8, SUP 3.10</u>
(7B)	<u>UCITS management company</u>	<u>SUP 3.1 – SUP 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8 – SUP 3.10</u>
...			
(9)	<u>Mortgage lender 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 3.7</u>	<u>SUP 3.1, SUP 3.2, SUP 3.8</u>
...			

...

#### Limited application for certain types of firm and their auditors

- 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;~~
  - ~~(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 firms are not required, under this chapter, to appoint an auditor because SUP 3.3 (Appointment of auditors) does not apply. If such firms appoint 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 3.1.2 R, Note 4, for further clarification concerning insurance intermediaries and~~

~~those which qualify as exempt insurance intermediaries. [deleted]~~

Insurance intermediaries and their auditors

- 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.

...

- 16.7.21 R Financial reports required from *service companies* (see SUP 16.7.20R)

Report	Frequency	Due Date
Annual <del>audited</del> financial statements ( <u>Note 1</u> )	Annually	6 months after the <i>firm's accounting reference date</i>

Note 1 = The *firm's* annual financial statement must be audited unless the *firm* is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).

...

- 16.7.29 R Financial reports from a *securities and futures firm* which is an adviser, local or a traded options market maker (see SUP 16.7.28R)

Report	Frequency	Due Date
...		
<del>Audited a</del> Annual financial statements ( <i>partnerships and bodies corporate</i> only) ( <u>Note 1</u> )	Annually	3 months after the <i>firm's accounting reference date</i>
<del>Audited a</del> Accounts of any <i>subsidiary</i> unless the <i>rules</i> in this chapter require that <i>subsidiary</i> to submit accounts to the <i>FSA</i> ( <u>Note 2</u> )	Annually	3 months after the <i>firm's accounting reference date</i>

Note 1 = The *firm's* annual financial statement must be audited unless the *firm* is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).

Note 2 = The *subsidiary's* accounts must be audited unless both the *firm* and the *subsidiary* are exempt from the requirement to appoint an auditor under the Companies Act 1985.

...

- 16.7.33 R (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;

(b) ...

...

16.7.34 G The *FSA* expects the ~~audited~~ annual financial statements to be submitted together with the auditor's report required by *SUP* 3.9.4R.

...

16.7.77 R Reports from a *firm* not subject to other reporting requirements in *SUP* 16.7.1G - *SUP* 16.7.75R

Report	Return (Note 1)	Frequency	Due Date
...			
If the <i>firm</i> is a <i>mortgage lender</i> or <i>mortgage administrator</i> , annual report and <del>audited</del> accounts (Note 10).			
...			

Note 10 = The *firm's* annual report and accounts must be audited unless the *firm* is exempt from the requirement to appoint an auditor under the Companies Act 1985 (section 249A (Exemptions from audit)).

...

SUP 16 Annex SUP 16 Ann 5R: Investment management firms' reporting forms and requirements applying to their completion

Annual Financial Return

...

Financial Resources

...

TIER 1

Paid up share capital (excluding preference shares) (*Item 1*) (36)

Share premium account (*Item 2*) (37)

~~Audited~~ ~~+~~ Reserves (*Item 3*) (38)

...

Declaration

...

It is accompanied by the Annual Accounts and the report of the auditor to the FSA as if required by the rules.

...



## Quarterly Financial Return

...

## Financial Resources

...

## TIER 1

Paid up share capital (excluding preference shares) (*Item 1*) (36)Share premium account (*Item 2*) (37)~~Audited~~ Reserves (*Item 3*) (38)

...

## Monthly Financial Return

...

## Financial Resources

...

## TIER 1

Paid up share capital (excluding preference shares) (*Item 1*) (36)Share premium account (*Item 2*) (37)~~Audited~~ Reserves (*Item 3*) (38)

...

## SUP 16 Annex 10R: Securities and Futures Firms' Reporting Forms and Requirements Applying to their Completion

...

## Section 6: Securities and Futures Firms: Form and content of report

...

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 as at the *firm's accounting reference date*.

## SUP 16 Annex 11G: Guidance notes on completion of Securities and Futures firms' reporting forms

...

## Section 3

Guidance Notes: standard reporting statement for Securities and Futures Firms which are not ISD firms

...

## SUP 16 Ann 10R Accounting policies

The accounting policies which are required to be used for the reporting statements are not necessarily the same as the accounting policies used in the ~~audited~~ annual financial statements (i.e. statutory accounts). A firm must give particulars of any departure from the requirements in SUP 16 Ann 10R. A firm must use the correct accounting policy for each case.

...

SUP 16 Annex 18 AR: Retail Mediation Activities Return ('RMAR')

...

Section D2: Financial Resources - Non-ISD Personal Investment Firms

Own Funds (Test 1)

1. ...

3. ~~Audited~~ Retained profits

4. ~~Verified interim~~ Interim profits (~~audited~~)

...

...

...
RR0255
RR0256
...

SUP 16 Annex 18 BG: Notes for Completion of the Retail Mediation Activities Return ('RMAR')

...

Section D2: non-ISD *personal investment firms*

...

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. If the *firm* is exempt from the requirement to appoint an auditor under the Companies Act 1985, the *firm's* expenditure does not need to be audited.

...

SUP 16 Annex 19 BG: Notes for Completion of the Mortgage Lending & Administration Return ('MLAR')

...

C1-2 CAPITAL RESOURCES

...

(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. Reserves must be audited unless the *firm* is eligible to include unaudited reserves in its capital resources calculation under PRU 9.3.52R.

The ~~audited~~ reserves figure is subject to the following adjustments, where appropriate:

(a) ...

...

(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 unless the *firm* is eligible to include unverified interim net profits in its capital resources calculation under PRU 9.3.52R.

...

(6) General /collective provisions

*Firms* should report general/collective 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/collective provisions must be verified by external auditors and disclosed in the *firm*'s annual report and accounts unless the *firm* is eligible to include unaudited general and collective provisions in its capital resources calculation under PRU 9.3.52R.

...

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

...

C5 Capital requirements

...

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.

...



**CONDUCT OF BUSINESS SOURCEBOOK (MENU ON ASSIGNMENT OF  
LIFE POLICIES) INSTRUMENT 2006**

**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); 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 6 October 2006.

**Amendments to the Handbook**

- D. The Conduct of Business sourcebook (COB) is amended in accordance with the Annex to this instrument.

**Citation**

- E. This instrument may be cited as the Conduct of Business Sourcebook (Menu on Assignment of Life Policies) Instrument 2005.

By order of the Board  
[28 September 2006]

## Annex

### Amendments to the Conduct of Business Sourcebook

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

...

COB 4      Annex 6R (Fees and Commission Statement required by *COB* 4.3.11R(1) and (2))

...

Section    - Commission (or equivalent)  
4

...

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)    ...

(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 other than a *traded life policy*.

...

**CONDUCT OF BUSINESS SOURCEBOOK (DISCLOSURE REQUIREMENTS FOR  
THIRD PARTY PROCESSORS) INSTRUMENT 2006**

**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) the other rule-making powers listed in Schedule 4 to the General Provisions.
- 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 6 October 2006.

**Amendments to the Handbook**

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The General Provisions (GEN) are amended in accordance with Annex B to this instrument.
- F. The Conduct of Business sourcebook (COB) is amended in accordance with Annex C to this instrument.

**Citation**

- G. This instrument may be cited as the Conduct of Business (Disclosure Requirements for Third Party Processors) Instrument 2006.

By order of the Board  
[28 September 2006]

## Annex A

## Amendments to the Glossary of definitions

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

Amend the following definition as shown:

...

*Third party processor* (1) A firm ("Firm A") which carries on *regulated mortgage activities* or *insurance mediation activities* other than advising on life policies ~~in relation to non-investment insurance contracts~~, or both, for another firm (or an appointed representative) ("Firm B") under a properly documented *outsourcing* agreement, the terms of which provide that when Firm A carries on any of these activities ("the outsourced activities") for Firm B:

...

(2) A firm ("Firm C") which carries on *regulated mortgage activities* or *insurance mediation activities* other than advising on life policies ~~in relation to non-investment insurance contracts~~, or both, for a *third party processor* within (1) ("Firm A"), where:

...

...



## Annex B

## Amendments to the General Provisions

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

...

Exception: use of third party processors in mortgage and ~~non-investment~~  
insurance-business mediation activities

- 4.3.6 R (1) Where a *firm* has outsourced activities to a *third party processor* other than *advising on life policies*, GEN 4.3.1R does not apply to that *third party processor* when acting as such, so long as the outsourcing *firm* ensures that the *third party processor* and its *employees* comply with that *rule* as if it was the *firm* and they were *employees* of the *firm*.
- (2) Where an *appointed representative* has outsourced *insurance mediation activities* other than *advising on life policies* ~~in relation to *non-investment insurance contracts*~~ or mortgage mediation activities to a *third party processor*, GEN 4.3.1R does not apply to that *third party processor* when acting as such, so long as the *appointed representative's principal* ensures that the *third party processor* and its *employees* comply with that *rule* as if it was the *appointed representative* and they were the *employees* of the *appointed representative*.
- (3) Where an *appointed representative* of a *firm* is carrying on:
- (a) *insurance mediation activities* other than *advising on life policies* ~~in relation to *non-investment insurance contracts*~~; or
- (b) ...

...

## Annex C

## Amendments to the Conduct of Business sourcebook

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

...

Use of third party processors in life insurance mediation activities

- 1.2.6 R (1) Where a *firm* (or its *appointed representative*) has outsourced *insurance mediation activities* to a *third party processor*, any rule in *COB* which requires the *third party processor*, when acting as such, to disclose its identity to a *customer* must be read as requiring disclosure of the identity of the *firm* (or *appointed representative*, as appropriate) which is taking responsibility for the acts and omissions of the *third party processor* when carrying on the outsourced activities.
- (2) If the *third party processor* is *advising on investments*, (1) does not apply.

...

**MORTGAGES: CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT NO X)  
INSTRUMENT 2006**

**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 referred to 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 2006.

**Amendments to the Handbook**

- D. The Mortgages: Conduct of Business sourcebook (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 No X) Instrument 2006.

By order of the Board  
28 September 2006

## Annex

## Amendments to the Mortgages: Conduct of Business sourcebook

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

...

- 3.6.3 R (1) ...
- (2) *A non-real time qualifying credit promotion* which includes a comparison or contrast must:
- (a) compare ~~qualifying credit~~ credit meeting the same needs or which is intended for the same purpose;
  - (b) objectively compare one or more material, relevant, verifiable and representative features of ~~the qualifying credit~~ that credit, which may include price;

...

...

- 3.6.5 G In relation to MCOB 3.6.3R:
- ...
- (2) if a *non-real time qualifying credit promotion* includes information on the performance of the *firm*, on conditions in the market, interest rates, *APRs* or other *price information* this information should be relevant and recent. *Firms* should therefore avoid including this information in *qualifying credit promotions* which have a long shelf-life, ~~and where the information can become outdated; and~~ without a clear and prominent warning that the information can become outdated; and

...

...

- 3.6.13 R *A non-real time qualifying credit promotion* must, unless MCOB 3.6.15R (Transient advertising) applies, prominently contain one or more of the following statements in the circumstances described:

...

- (3) in all cases except (1) and (2):

'Your home may be repossessed if you do not keep up repayments on your mortgage.'; or if the *qualifying credit promotion* refers in whole or in part to *qualifying credit* secured on property which is not the *customer's* home the statement may be amended but only to the extent

necessary in order to reflect that fact.

...

3.6.13A R Where a *non-real time financial promotion* relates to both *qualifying credit* and *credit* which is not *qualifying credit* it may contain the statement in *MCOB 3.6.13AR(1)* as an alternative to the statement required by *MCOB 3.6.13R(2)* or the statement in *MCOB 3.6.13AR(2)* as an alternative to the statement required by *MCOB 3.6.13R(3)*:

- (1) 'Think carefully before securing other debts against your home. Your home may be repossessed if you do not keep up repayments on a mortgage or any other debt secured on it.'; or
- (2) 'Your home may be repossessed if you do not keep up repayments on a mortgage or any other debt secured on it.'

...

5.6.9 R The amount referred to in *MCOB 5.6.6R(2)* is:

- (1) ...
- (2) where the *regulated mortgage contract* is a revolving credit agreement such as a secured overdraft or *mortgage credit card*, unless (2A) applies the total borrowing that the *firm* is willing to provide under the *regulated mortgage contract*; ~~or~~
- (2A) where the *regulated mortgage contract* is a revolving credit agreement that provides for an initial drawdown and provides *linked borrowing facilities* that would allow the *customer* to increase the amount of the loan without any further approval from the *mortgage lender*, the amount of the initial drawdown; or
- (3) ...

...

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:

...

- (10) ~~details of insurance which the *customer* has chosen to take out through the *firm*, whether or not this insurance was included in the *illustration* provided in accordance with *MCOB 5* (Pre-application disclosure), must be included in Section 9 of the *illustration* that is part of the *offer document*;~~[deleted]

- ...
- ...
- 7.5.1 R Subject to *MCOB 7.5.2R*, a *firm* must provide the *customer* with a statement at least once a year (or, in relation to the first statement, within the first 13 months):
- (1) ...
- ...
- 7.6.27 R ~~For the purposes of *MCOB 7.6.22R*, *MCOB 5.6.17R* is replaced with the following:~~"Section 2: 'Which service are we providing you with?' Under the section heading 'Which service are we providing you with?' the following text should be included: 'We are providing you with an illustration for the [addition/removal] of [a party/parties] to this mortgage. You must make your own choice about whether changing the parties to this mortgage is right for you.'"~~[deleted]~~
- ...
- 9.4.13 R The amount referred to in *MCOB 9.4.6R(2)* is:
- (1) ...
- (2) where the *regulated lifetime mortgage contract* is a revolving credit agreement such as a secured overdraft or *mortgage credit card*, unless (2A) applies the total borrowing that the *firm* is willing to provide under the *regulated lifetime mortgage contract*; ~~or~~
- (2A) where the *regulated lifetime mortgage contract* is a revolving credit agreement that provides for an initial drawdown and provides *linked borrowing* facilities that would allow the *customer* to increase the amount of the loan without any further approval from the *mortgage lender*, the amount of the initial drawdown; or
- (3) ...
- ...
- 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:
- ...
- (9) ~~details of insurance which the *customer* has chosen to take out through the *firm*, whether or not this insurance was included in the *illustration* provided in accordance with *MCOB 9*, must be included in Section 12~~

~~of the illustration that is part of the offer document;~~[deleted]

...

...

## MCOB TP 1

### MCOB Transitional Provisions

#### 1 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
...	...	...	...	...	...
[10] <sup>1</sup>	<u>MCOB 5.6.9R and MCOB 9.4.13R</u>	<u>R</u>	<u>A firm may continue to comply with MCOB 5.6.9R and MCOB 9.4.13R as they applied before amendment by the Mortgages: Conduct of Business Sourcebook (Amendment No X) Instrument 2006</u>	<u>31 October 2006 to 31 October 2007</u>	<u>31 October 2006</u>

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<sup>1</sup> The FSA is consulting on a separate MCOB transitional provision in Chapter 3 of this Consultation Paper.





**COMPLAINTS AGAINST THE FSA SCHEME (AMENDMENT NO [...])  
INSTRUMENT 2006**

**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 157(1) (Guidance); and
  - (2) paragraph 7 of Schedule 1.

**Commencement**

- B. This instrument comes into force on [...] 2006.

**Amendments to the Handbook**

- C. The Complaints against the FSA sourcebook (COAF) 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 No [...]) Instrument 2006.

By order of the Board  
[...] 2006

## Annex

## Amendments to the Complaints against the FSA Sourcebook

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

## Part 1

- 1.3.2 G (1) The *Complaints Commissioner* is appointed for a period of three years and may be dismissed from office only for reason of becoming:
- (a) incapacitated by physical or mental illness; or
  - (b) otherwise unfit to discharge the functions of his office;
- and subject in either event to the approval of the Treasury.
- (2) ~~No person who has attained the age of 70 years is eligible to be or to remain a *Complaints Commissioner*.~~[deleted]
- (3) The *Complaints Commissioner* must not be an employee of the *FSA* and is required to act independently of, and without favouring, the *FSA*.

## Part 2

- 1.4.7 G The *FSA* will not make any charge to complainants in ~~relation to the~~ operation of the complaints scheme.

...

- 1.5.2A G In carrying out the investigation, the suitably senior member of staff will undertake a paper-based review of the complaint, by considering any documents supplied initially by the complainant or following communications from the *FSA* under *COAF* 1.5.1CG. The investigation will not involve an interview of the complainant.

...

Time limit for the referral of a matter to the *Complaints Commissioner*

- 1.5.6A G (1) When the *FSA* writes to a complainant with its final report of its investigation, or explaining that it will not investigate a complaint under the *complaints scheme* under *COAF* 1.5.1BG, the *FSA* will inform the complainant that, if he is dissatisfied, he must refer the *FSA's* decision to the *Complaints Commissioner* within three months of the date of that letter.
- (2) If the *Complaints Commissioner* receives a referral of a matter

outside of the three *months* time limit, it will be the *Complaints Commissioner's* decision whether there is a good reason why the matter should be considered out of time.

...

- 1.5.19A    G    (1)    The *Complaints Commissioner* will send a preliminary report, setting a time limit within which the *FSA* and the complainant may indicate in writing any disagreement(s) with or comments on the preliminary report.
- (2)    At the end of the set time limit, the *Complaints Commissioner* will produce a final report taking into account, at his discretion, any disagreements or comments notified to him. The final report will be the conclusion of the investigation procedure set out in *COAF* 1.5 and the complaint will be regarded as closed by the *Complaints Commissioner* and the *FSA*.

2                      Transitional complaints scheme

...

2.3                      Coverage and scope of the scheme

...

2.3.7            G    The *FSA* will not make any charge to complainants in relation to the operation of the *transitional complaints scheme*.

2.4                      Procedure

...

2.4.2A        G    In carrying out the investigation, the suitably senior member of staff will undertake a paper-based review of the complaint, by considering any documents supplied initially by the complainant or following communications from the *FSA* under *COAF* 2.4.1BG. The investigation will not involve an interview of the complainant.

...

Time limit for the referral of a matter to the *Complaints Commissioner*

- 2.4.6A        G    (1)    When the *FSA* writes to a complainant with its final report of its investigation, or explaining that it will not investigate a complaint under the *complaints scheme* under *COAF* 2.4.1AG, the *FSA* will inform the complainant that, if he is dissatisfied, he must refer the *FSA's* decision to the *Complaints Commissioner* within three *months* of the date of that letter.
- (2)    If the *Complaints Commissioner* receives a referral of a matter

outside of the three *months* time limit, it will be the *Complaints Commissioner's* decision whether there is a good reason why the matter should be considered out of time.

...

- 2.4.18A    G    (1)    The *Complaints Commissioner* will send a preliminary report, setting a time limit within which the *FSA* and the complainant may indicate in writing any disagreement(s) with or comments on the preliminary report.
- (2)    At the end of the set time limit, the *Complaints Commissioner* will produce a final report taking into account, at his discretion, any disagreements or comments notified to him. The final report will be the conclusion of the investigation procedure set out in *COAF 2.4* and the complaint will be regarded as closed by the *Complaints Commissioner* and the *FSA*.

**NEW COLLECTIVE INVESTMENT SCHEMES SOURCEBOOK  
(AMENDMENT NO X) INSTRUMENT 2006**

**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) section 138 (General rule-making power);
    - (b) section 140 (Restriction on managers of authorised unit trust schemes);
    - (c) section 156 (General supplementary powers);
    - (d) section 157(1) (Guidance);
    - (e) section 238(5) (Restrictions on promotion);
    - (f) section 242 (Applications for authorisation of unit trust schemes);
    - (g) section 247 (Trust scheme rules); and
    - (h) section 248 (Scheme particulars rules); and
  - (2) regulation 6 (FSA rules) of the Open-Ended Investment Companies Regulations 2001 (SI 2001/1228).
- B. The rule-making powers and related provisions 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 [     ] 2006.

**Amendments to the Handbook**

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The New Collective Investment Schemes sourcebook (COLL) is amended in accordance with Annex B to this instrument.

**Citation**

- F. This instrument may be cited as the New Collective Investment Schemes sourcebook (Amendment No X) Instrument 2006.

By order of the Board  
[             ] 2006

## Annex A

### Amendments to the Glossary of definitions

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

Amend the following definition as shown:

...

*annual  
accounting  
period*

...

(in *COLL*) the ~~12-month~~ period of 12 months (or, in the case of a *scheme's* first accounting period, the period determined in accordance with *COLL* (6.8.2R (Accounting periods )) which ends on the accounting reference date stipulated in the *prospectus* ~~which ends on the accounting reference date~~).

...

## Annex B

## Amendments to the New Collective Investment Schemes sourcebook

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

## 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
...					
<u>1A</u>	<u>Each and every rule in <i>COLL</i></u>	<u>R</u>	<u>The <i>rules</i> in <i>COLL</i> do not apply to any relevant party in relation to an <i>authorised fund</i> where the winding up of the <i>fund</i> has commenced before 12 February 2007, provided that each relevant party shall continue to comply with the provisions of <i>CIS</i> as if they still applied to them.</u>	<u>From 12 February 2007</u>	<u>12 February 2007</u>

...

## Preparation of long and short reports

4.5.3 R ...

- (4) ~~[deleted] 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*.~~

...

## Spread: government and public securities

5.6.8 R ...

- (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*, except for *COLL 5.2.12R(4)* which will apply to such a *scheme* only to the extent that it concerns the most recently published *prospectus* of the *scheme*.

...

## Prohibition on promotional payments

6.7.12 R (1) No payment may be made from *scheme property* to any *person* ...

- (2) Paragraph (1) shall not apply to the costs of preparing and printing the *simplified prospectus* or *key features* of the *authorised fund*, provided the *prospectus* of the *fund* states in accordance with *COLL 4.2.5R(13)* and (14) (Table: contents of prospectus) that these costs are properly payable to the *authorised fund manager* from *scheme property*.

## Prohibition on promotional payments: guidance

6.7.13 G Examples of payments which are not permitted by *COLL 6.7.12R* include:

...

- (2) payments or costs in relation to the preparation or dissemination of *financial promotions* (other than ~~the preparation of *key features* or the *simplified prospectus*~~ costs allowed under *COLL 6.7.12R(2)*); and



## Accounting periods

- 6.8.2 R ...
- (2) *A half-yearly accounting period begins with the first day of an annual accounting period and ends:*
- (a) *on the day which is six months ~~later~~ before the next accounting reference date; or*
- (b) *~~ends~~ on some other reasonable date as set out in the prospectus of the scheme;*
- unless the first annual accounting period has been extended in accordance with (4), in which case the first half-yearly accounting period ends on the day which is six months before that subsequent accounting reference date.*
- (3) *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;*
- and in either case must end on the next accounting reference date, except where (4) applies.*
- (4) *When the accounting reference date of a scheme falls less than 6 months after the beginning of the first annual accounting period, the authorised fund manager may, after consulting the scheme's auditor, extend that annual accounting period until the subsequent accounting reference date.*
- 6.8.2A G *When the annual accounting period of a scheme is extended under COLL 6.8.2R(4), the authorised fund manager should, in accordance with Principles 6 (Customers' interests) and 7 (Communications with clients), make appropriate information available to unitholders during the period about the investment activities and performance of the scheme.*

...

## Report and accounts

- 8.3.5 R ...
- (2) *[Deleted] 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.~~

The provisions in COLL 6.8.2R(2) to (4) (Accounting periods) also apply to the first annual accounting period of a qualified investor scheme.

...



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