ISLE OF MAN
FINANCIAL SERVICES AUTHORITY
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Structured Deposits and Structured Products

Structured deposits

Structured deposits are a type of structured product (see below) but can only be offered by banks which are able to accept deposits.

A structured deposit is defined as a deposit which is repayable at maturity on terms under which interest or a premium will be paid or is at risk, according to a formula involving factors such as:-

(a) An index or combination of indices (excluding variable rate deposits whose return is directly linked to one interest rate index such as Euribor or Libor);
(b) A financial instrument or combination of financial instruments;
(c) A commodity or combination of commodities or other physical or non-physical non-fungible assets; or
(d) A foreign exchange rate or combination of foreign exchange rates.

Your money is treated as if it is in a restricted-access bank account but, unlike a traditional savings account, which pays a fixed rate of interest, the return you receive will depend on the performance of a stock market index or asset. The return may therefore be zero.

Structured deposits often involve you having no access to your initial capital amount for a long period of time (e.g. 5 years). Key features / risks of a structured deposit may include:-

- **Liquidity risk** – the benefits offered (such as capital protection) are usually only available if the product is held for the full term. It may be impossible, difficult or expensive to access your money before the end of the deposit term.
- **No dividend income** – even if a product's return is linked to the performance of a stock market index, you will not receive any dividend income from the companies which make up that index.
- **Capped returns** – many products restrict or cap the level of the return you can receive, so if an index or asset price rises above the level of that cap, you do not receive additional returns.
- **Averaging** – the return offered by some products can depend on several measurements of index levels or asset prices during the life of the deposit (and sometimes only in the final year of the term). While this can protect you from short-term falls in an index level or asset value, it may also prevent full exposure to any gains.

- **Limited participation** – many products only offer a proportion (for example 50%) of any gains made by the index or asset to which they are linked.
- **Inflation** – even where a product is marketed as '100% capital protected', the real value of the capital can suffer significant erosion due to inflation over the term of the deposit, as there is no guaranteed minimum return in excess of the initial capital.

The calculation of the return that you may receive from a structured deposit is often complicated. You should seek professional advice if you are in any doubt about the potential risks and returns involved, past performance is not an indicator of future performance.

The Authority requires banks in the Island who offer structured deposits to provide you, the depositor, with certain key information before making the transaction. Banks are also required to have appropriately trained staff who are able to speak with customers about structured deposits. The full details of the requirements are contained in Rules 6.73 and 6.74 of the Financial Services Rule Book.

Structured products (*not deposits*)

Structured products can be any one of a wide range of ***investments*** and can offer income, capital growth, or a combination of both. Most structured products tend to be open to new investment for a short period of time. Your money will then usually need to be tied up for between one and ten years. Some structured products offer full capital protection (for example structured deposits above), but others offer partial or no capital protection, and this is because they are an investment not a deposit. This means you may receive back less than your initial capital.

Structured products offer returns based on the performance of underlying investments. Many products are linked to a stock market index such as the FTSE 100. The underlying investments may involve different firms based in various countries.

Even if a product offers 'capital protection' it can sometimes fail, causing you to lose some or all of your original money. You should always know which financial institution is ultimately responsible for offering any 'capital protection', and if it is not clear then you should seek professional advice.

Structured products offer two broad types of capital protection:-

- **Full** – described as '100% capital protection', 'capital security' or a 'capital guarantee'. This aims to return all the original money invested at the end of its term, regardless of any fall in index level or asset price. Remember, though, that the cost of offering this protection will affect the returns you get, and there is still a chance you could lose some or all of your original money.
- **Partial** – often offered by 'structured capital-at-risk products' (known as 'SCARPs'). This aims to return the original money invested at the end of the term unless the index or asset price to which the product is linked has fallen below a predetermined threshold. If this happens then you can quickly lose your original money.

You should understand the risks before investing in a structured product. The following list is not exhaustive and not all risks or features are applicable to each type of product:-

- **Credit risk** – a product may be designed and marketed by a 'plan manager', but the returns and guarantees are generally provided by a third party. If that third party becomes bankrupt, you could lose some or all of your money, even if a product is called 'protected' or 'guaranteed'.
- **Market or investment risk** – if the return of your original money depends on the performance of a stock market index or asset, and if the level of that index or asset performs outside the parameters of the product during the term of the investment you may lose some or all of your original money.
- **Liquidity risk** – the benefits offered (such as capital protection) are usually only available if the product is held for the full term. It may be impossible, difficult or expensive to access your money before the end of the investment term.
- **No dividend income** – even if a product is linked to the performance of a stock market index, you will not receive any dividend income from the companies which make up that index.
- **Capped returns** – many products restrict or cap the level of the return you can receive, so if an index or asset price rises above the level of that cap, you do not receive additional returns.
- **Averaging** – the return offered by some products can depend on several measurements of index levels or asset prices during the life of the investment. While this can protect you from short-term falls in an index level or asset value, it may also prevent full exposure to any gains.
- **Limited participation** – many products only offer a proportion (for example 50%) of any gains made by the index or asset to which they are linked.
- **Inflation** – even where a product is marketed as '100% capital protected', the real value of the capital can suffer significant erosion due to inflation over the term of the investment.
- **Tax** – the tax treatment of structured products depends on their legal structure and the jurisdiction in which you are liable to pay tax.

Structured products are often complicated. You should seek professional advice if you are in any doubt about the potential risks and returns involved.

You could lose some or all of the money you put in to these products, so make sure you understand the risks before investing.

Other products

Some banks also offer investment products in which your capital may be at risk for other reasons. These products must be sold through a qualified financial advisor.

If you are considering a product, be clear about whether it is a bank account (deposit) or an investment and under what circumstances you might lose some or all of your capital.