

Cost of Compliance for smaller licenceholders Second progress report

In November 2011 the Commission issued a first progress report on the cost of compliance for small licenceholders. This second progress report summarises the issues which were raised and the action taken to date.

The main change is that licenceholders with an annual turnover of up to £250,000 may apply for an exception from audit of their financial statements.

Instructions on how to apply are on the next page.

We plan to continue this process and would welcome further correspondence on these matters and new suggestions. Please contact:

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Audited financial statements

Two respondents suggested that there should be a minimum threshold below which audited financial statements are not required.

Audit represents an assurance as to the quality of a set of financial statements. However, for many small licenceholders, financial failure *of the licenceholder itself* may not be one of the most significant threats to the Commission's regulatory objectives. This is because:

- A licenceholder must segregate clients' money and investments from its own money and assets;
- Some licenceholders are not permitted to hold clients' money or investments at all;
- In a small owner-managed business there is scope for a "soft landing" in which the principals of the business manage a declining workload themselves, before selling the book of business. This would provide continuity of service to the client base.

We will therefore welcome applications from licenceholders¹, initially with a turnover below £250,000 and will consider each application on its merits against a consistent set of criteria. More than 20% of the Commission's licenceholders will be eligible in this initial stage. An audit letter in respect of client money and clients' investments (if held) would still be required².

In considering applications from licenceholders we will take into account the financial position and compliance record of the licenceholder and the licenceholder's likely ability to wind down its business in an orderly manner if it got into financial difficulties.

If we are satisfied, we will grant the licenceholder an exception from obtaining an audit of its financial statements.

If an exception is granted, we will still require that the licenceholder submits signed (but not audited) annual financial statements and that the financial statements include a confirmation from the directors that the balance sheet and profit & loss account represent a "true and fair view", in accordance with section 3 of the Companies Act 1982. Licenceholders will also continue to prepare quarterly financial resources calculations, and we will continue to sample these as part of the visit programme.

How to apply

Write to us;

- **Describe what steps you might take to protect services to clients, if the business got into financial difficulties;**
- **If you do not submit interim financial resources calculations to the Commission each quarter, you should enclose a copy the past 4 quarterly financial resources calculations; and**
- **If you hold money or investments covered by Part 3 of the Rule Book (Client money, trust money and relevant funds) or Part 4 (Clients' investments), set out how you propose to obtain an auditor's letter in respect of compliance with Part 3 and Part 4³. This might be correspondence with an auditor which confirms its availability.**

¹ We envisage that new licenceholders will be expected to supply audited accounts for at least their first year in business

² Rule 5.20 would still apply, but with an exception from 5.20(1)(b)(i)

³ We expect most applications to be from financial advisers and CSPs/TSPs. We would not rule out an application from other licenceholders, but we might apply additional scrutiny.

AML/CFT

It was suggested that we should review aspects of the AML/CFT regime.

The AML/CFT Handbook includes guidance on situations where business may carry a lower AML/CFT risk and licenceholders are encouraged to take this into account in assessing the AML/CFT risk profile of their business. The revised FATF 40 recommendations, published in February 2012, require jurisdictions to develop their own risk-based approach at a national level. This will create a further opportunity to address those areas where business in the Island may carry a lower AML/CFT risk. For example there might be an opportunity to address the diversified nature of the Island's economy and the local nature of much of its domestic customer base.

The Joint Anti-Money Laundering Advisory Group ("JAMLAG") is an important forum for Government and industry to discuss the Island's approach to the implementation of international AML/CFT standards. We will continue to work closely with JAMLAG.

AML/CFT training for professional officers

It was queried whether professional officers really need AML/CFT training. Training is an FATF requirement and we believe it is relevant for professional officers because of AML/CFT risk in the companies and trusts of which they are directors or trustees. However, the nature of the professional officer's responsibilities should be taken into account – and similar considerations may apply to tailoring training to the roles of other non-executive directors.

We would also welcome feedback on whether licenceholders feel that the availability of AML/CFT training could be more widely publicised. The Commission cannot give an implied endorsement to any training provider, but there could be an opportunity to work with professional bodies and trade associations.

CPD

It was queried whether the CPD hours requirement could be relaxed for part-time staff. However, we believe that the CPD requirement should be maintained at a consistent level, because staff who are in Key Person roles need to be equally capable, whether they work full-time or part-time.

One respondent noted that if a person is required to record CPD in his/her "main" job, it is inefficient to duplicate that record in another licenceholder. This seems reasonable and we will review how we apply rule 8.5A in these circumstances.

External appointments to key person roles

A licenceholder commented that a requirement to use an external person for a specific function had created a situation in which subsequently it was difficult to bring the function in-house, because the in-house staff could not develop the required experience. Where the Commission requires the appointment of an external person in a Key Person role (other than as part of a specific short-term project) it will encourage an in-house person to acquire exposure to the role with a view to being able to assume the responsibility. This should allow some smaller licenceholders to reduce their use of external contractors.

Fees

It was suggested that annual licence fees should be proportionate to the size of the licenceholder. The Commission keeps its fee structure under consideration and this comment has been fed into that process.

The Commission could have a person tasked with representing small firms

We already have a single relationship manager for all the professional officers and believe this has helped improve working relationships. Paul de Weerd, a Deputy Director in Supervision Division has been nominated to take on this role for small firms for the duration of this project.

One person having multiple roles

We were asked whether small licenceholders could dispense with some of the roles required by the Rule Book. We can see the appeal of removing requirements for one person to “wear several hats” under the rules. However we do not think that such a change would reduce costs. We would still require separation of roles in larger licenceholders and wherever we set a threshold (whether based on turnover or number of staff) it would create a problem for any licenceholder which was close to that threshold. Building-in different standards would also make the rules harder to follow. For that reason, we do not propose to make any changes at this point.

Record keeping requirements and registers

It was queried whether all of the record keeping and registers that are required in the financial services legislation (and other legislation) were really necessary in a small licenceholder. Our initial view is that the requirements appear to be relevant even in a small licenceholder. We do appreciate however, that some licenceholders have some of their registers empty.

We have issued guidance and pro-formas but we would welcome feedback on how these could be improved.