



Isle of Man Financial Supervision Commission

# Annual Report 2013/14



## Regulatory Objectives

The Commission's regulatory objectives are to:

- secure an appropriate degree of protection for the customers of persons carrying on a regulated activity,
- reduce financial crime, and
- support the Island's economy and its development as an international financial centre.

## The Commissioners



Geoff Karran MBE (Chairman)



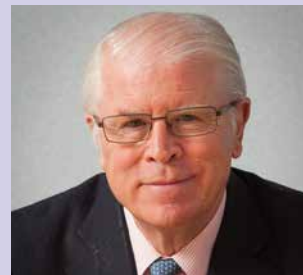
John Aspden (Chief Executive)



Bryan Stott (Deputy Chairman)



Roger Butler



Tim Cullen MBE



Sir David Lewis



Alan Smith



Paul Wright

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# Chief Executive's Report

It gives me great pleasure to present the Annual Report and Accounts of the Financial Supervision Commission for the year ended 31 March 2014.

This Report on the Commission's activities has been prepared for submission to Treasury and to be laid before Tynwald in fulfilment of the Commission's obligation under Schedule 1 to the Financial Services Act 2008.

Through much of the year there was discussion about whether a recovery from the recent external economic turbulence was beginning to take hold. The indications have become more positive, but it will still be some while before they translate into heightened activity for the finance sector locally.



**John Aspden**  
Chief Executive

In this environment the Commission's objective is to use effectiveness of its regulatory role to encourage quality business and growth in the economy.

One of the important interfaces which the Commission has with new businesses coming to the Island is through the licensing process. The Commission needs to strike a difficult balance between being welcoming and facilitative, but at the same time making sure that the public position is protected. In the Regulatory and Supervisory Approach section of this report will be seen a brief analysis of how newly licensed businesses have fared in their early years, in terms of whether or not they have survived. The statistics show an overall majority success rate, but with demise at a level showing that entrepreneurs are also being encouraged to introduce new ideas and services.

Continuing international regulatory reform presented challenges. It has furthered a climate of change, especially in the banking sector where the requirements of Basel III are placing an additional focus on capital and liquidity. It still remains unclear how the proposals of the Independent Commission on Banking will finally affect the structure of UK banking, and particularly what it means for the model of banking activities carried on in the Isle of Man and other Crown Dependencies. Further clarity is needed to help banks plan for any reorganisation, and to continue with the important role which they undertake in the local economy.

The low interest rate environment continued. This has had a number of effects, one of which is on depositors and those needing income from their savings. The temptation is for savers to look for other, possibly higher-yielding opportunities but perhaps forgetting that higher risk will also be incurred.

Mindful of retail consumer vulnerability, the Commission worked with the Office of Fair Trading to publicise some of the key principles which private investors in particular should consider when selecting investments - diversification, and a balance of risk and reward, being two of the most important. Some easily-understood investor guidance was issued shortly after the end of the period.

At the beginning of the year, new requirements came into force regarding minimum qualifications for financial advisers. There was a very positive result in advisers attaining the new level, which now underpins an all-important understanding of investors' needs and the suitability of investments sold to them. Unfortunately there remain a few cases of complaints of mis-selling which the Commission is investigating in the public interest. Investigations have to be fair and consider all the facts, so this can take time to complete before any action is known.

With economic recovery more protracted than many planned, this has also meant that a number of investment funds have still not recovered previous values and in some cases remain suspended or unable to dispose of

illiquid assets. This has required the Commission to spend time in ensuring that investors' interests are protected, and in particular that they are kept up-to-date with developments so they can make informed decisions.

One of the most significant aspects of the last revision of the FATF's Recommendations on AML/CFT was the introduction of a new, risk-based approach for the setting of an anti-money laundering agenda. Based on an analysis of a jurisdiction's vulnerabilities and threats, the framework provides for the setting of objectives and the implementation of measures to tackle the specific risks which have been identified. Overall compliance with the FATF Recommendations only comes when a jurisdiction is able to demonstrate, with evidence, that implementation is being carried out effectively.

The process and outcome of carrying out this work is known as the National Risk Assessment (for AML/CFT). It requires a thorough bottom-up approach across Government, law enforcement and regulatory stakeholders, with further input to come from industry. The Commission has devoted much time to this work which is being co-ordinated across-Island by the Government's Chief Secretary.

Another significant development in the Island's anti-money laundering regime is the preparation of new legislation for extending oversight to a range of non-financial businesses and professions, such as accountants, estate agents

and lawyers. In many cases some form of oversight is already in place but there is a need to demonstrate effectiveness and ensure that measures are in place consistently. The Commission has been discussing proposals for delegating part of the oversight to some existing professional bodies, while in other cases the oversight role will be assumed directly by the Commission.

During the period the UK Government pursued a policy on seeking greater transparency on the ultimate beneficial ownership of business relationships, and consulted on wide-ranging proposals for making this information available publicly.

The Island is well placed to address this initiative, having applied a full licensing and supervisory regime for all corporate and trust service providers since 2000 and 2005 respectively. These practitioners have had to ensure that they possess full details of those ultimately standing behind the structures for which they act, which in turn means that regulatory, tax and law enforcement authorities can retrieve the required information to co-operate fully when asked to assist international investigations. As yet it is unclear how the UK's proposals will eventually be finalised, but when they are the Island will need to consider whether or not any change to its present arrangements is needed.

Innovation is also having a significant impact. Crowd-funding, peer-to-peer lending and virtual currencies are examples of new developments where the Commission has been in



regular dialogue with the Department of Economic Development and Treasury on potential new initiatives. Sometimes these new activities do not fall easily or at all within existing legislation, even if there is a consumer interest potentially to be protected. The Commission does not immediately presume that everything should be fully regulated. Indeed the regime for registration under the proposals for designated non-financial businesses and professions provides a new option of oversight for activities where the principal risk is adequacy of AML/CFT measures.

With this in mind there has been increasing interest from Island businesses wishing to become involved in the market for virtual currencies. Recognising this trend, the Isle of Man Government has decided that certain activities relating to such business should be brought within the AML/CFT framework, while deferring the introduction of any prudential oversight until there is more of an international consensus on how it could be framed. In the meantime the Commission's view is that this can be a high risk area for participants who do not understand the risks involved, and they need to be aware that there is no Government protection in place for them.

The Commission responded to a series of questions from Tynwald's Economic Policy Review Committee, which are still being considered by that Committee. As part of its response the Commission suggested that it would welcome the opportunity to appear

in front of Tynwald on a more regular basis, as part of an important process of increasing accountability of the Commission. The Commission believes that this could be a useful opportunity to update Members of Tynwald on current developments and on any macro issues which may be causing concern.

As hopefully will be seen in a number of places in this Report, the Commission places a high priority on communicating with its stakeholders. Effective dialogue with the industry is vital if the Commission is to understand the impact which its proposals will have. The Commission is acutely conscious that there has been a steady flow of consultations, which are needed if the Island's regime is to stay modern and effective in the new environment. We are very grateful for the time which licenceholders have taken to respond and input into the process.

I am very fortunate that I work with a highly competent and motivated group of staff, most of whom come from the private sector with the commercial experience which that implies. I receive positive feedback especially from our visit work, and often with comments about the professionalism adopted. This is reflected throughout our organisation and I would like to thank everyone involved. I know that my colleagues would also like to join with me in thanking our Board for the support and guidance which it has continued to provide.

**John R Aspden**  
**Chief Executive**

# Economic Setting

In the second half of 2013 there was a global strengthening of economic momentum and by April 2014 the IMF reported that activity had broadly strengthened and is expected to improve further in 2014-15. Nevertheless, Mme. Lagarde's hopes that 2014 would be the start of "seven strong years" were tempered by acknowledgement that the global financial system was still in a challenging transition on its path to greater stability.

Not many years ago inflation was a major concern, but today the IMF sees deflation as the "ogre that must be fought decisively". None of the major economies are now experiencing double-digit inflation and just a few nations are experiencing slight deflation. Even Japan is soon likely to reach the +2.6% inflation now seen in both China and the UK, whilst inflation in both the USA and Eurozone currently averages 1.5% and in the Isle of Man it stands at 2.6% (RPI) and 1.6% (CPI).

The developing countries and emerging markets kept the economic wheels of growth turning during the worst of the crisis, but some are now slowing just as the more developed economies (including the USA and UK) start to pick up. The IMF is concerned at the uneven distribution of current growth

however, as the rich getting richer is not considered "a recipe for stability and sustainability". Global growth is expected to increase to about 3.6% in 2014 (3% in 2013) - just below the IMF's target of 4% - with advanced economies averaging 2.2% and emerging and developing countries still reaching 4.9%.

The Eurozone remains an area of concern, although it is now in a "weak recovery that remains uneven and fragile". The IMF expects the UK's economy to grow faster than other G7 nations' in 2014 (+2.9%). The Isle of Man meanwhile, is in its 29th year of economic growth and is the world's 8th wealthiest country in terms of GDP per capita. The Island's economy is in the top ten in terms of Gross National Income (GNI) per head - recently it overtook Guernsey's and Jersey's - and



it is rated “stable” at Aaa and Aa1 by Moody’s. However, Moody’s believes that pressures on offshore financial centres are unlikely to abate in the short term and “there are limits to the ability of a small jurisdiction such as the Isle of Man to mitigate these risks to its economic model”.

The increasing strength of the UK economy will undoubtedly benefit the Isle of Man, but if interest rates (still at the historic low of 0.5%) were to rise suddenly this could have a detrimental effect and an even stronger pound (currently US\$1.68, €1.22) may reduce exports. Unemployment in the Isle of Man rose slightly in 2013 to 2.6%, against a European average of 12.1% and 7.9% for all advanced economies. E-business and engineering are seen as two major growth areas in the Isle of Man, although the finance sector remains the largest wealth contributor in terms of jobs and GDP. In 2013 the Manx shipping register rose to 14th in the world and the Island now has the 9th largest business jet register.

The Isle of Man was the first to sign a FATCA (tax) agreement with the UK in October 2013, followed two months later by an agreement with the USA. In November the Isle of Man was also awarded the top “compliant” rating by the OECD Global Forum on tax transparency. Of the 50 countries reviewed, it was one of only 18 to receive the top rating - higher than that awarded to either the UK or the USA.

Average gross earnings in the Isle of Man equal those in the UK, but income

tax rates remain more favourable for Manx residents. The Island’s ‘tax cap’ of £120,000 brings economic benefits of nearly £16 million per year and its lack of corporation tax (for most companies) is also considered beneficial to the economy. Government income and expenditure are both likely to increase further in the next few years, but from 2015 the revenue budget is expected to balance.

The FTSE 100 moved up during the period, gaining 14.4% in 2013, and continues to fluctuate around the mid-6,000s. There have also been consistent gains in USA indices, but Far Eastern markets have fluctuated more. Most forecasters predict further gains during 2014.

# The Commission: Organisation and Corporate Governance

The Commission is an independent Statutory Board established under the Financial Supervision Commission Order 1983.

## Organisation of the Commission

The functions of the Commission are set out at Appendix A. The membership of the Board is set out at Appendix B.

Appointments to the Board of the Commission are approved by Tynwald, and Commissioners are appointed for a five-year term.

The Commission's regulatory objectives are set out in section 2 of the Financial Services Act 2008, and they are to:

- secure an appropriate degree of protection for the customers of persons carrying on a regulated activity
- reduce financial crime
- support the Island's economy and

its development as an international financial centre.

These regulatory objectives are supported by the following matters to which the Commission must have regard when discharging its functions:

- the need for the regulatory, supervisory and registration regimes to be effective, responsive to commercial developments and proportionate to the benefits which are expected to result from the imposition of any regulatory burden
- the need to use its resources in the most efficient and economic way
- the desirability of implementing and

applying recognised international standards

- the desirability of co-operating with governments, regulators and others outside the Island
- the need to safeguard the reputation of the Island
- the responsibilities of those who manage the affairs of permitted persons
- the international character of financial services and markets and the desirability of maintaining the competitive position of the Island
- the desirability of facilitating the development of the financial services industry
- the impact of its decisions on the stability of the financial system of the Island.

The last matter was added to this list for the first time during the period of this report, by virtue of the Financial Services (Miscellaneous Amendments) Act 2013.

The full Board of the Commission meets each month. In addition, the full Board or at least a quorum (comprising a minimum of three Commissioners) meets regularly to consider licensing matters. The following meetings were held during the period:

Meetings of the Financial Supervision Commission	12
Licence Application Meetings	7

There are three sub-committees of the Board: the Risk and Internal Control Committee, the Remuneration

Committee and the Complaints Committee (which provides a review body for complaints that may be made against the Commission and which are initially dealt with by the Chief Executive). The following meetings of these committees were held:

Meetings of the Risk and Internal Control Committee <sup>1</sup>	4
Meetings of the Remuneration Committee <sup>2</sup>	3

There were no meetings of the Complaints Committee during this period. A range of policy, risk, case and operational matters were discussed by the Board during its monthly meetings. Topics included (in no particular order):

- material issues concerning specific licenceholders
- current banking issues such as the impact of UK banking reform, recovery and resolution, and international standards such as Basel III
- the sales process for financial products
- the Commission's regime surrounding professional qualifications and ongoing professional development for financial advisers
- consumer information about financial advice
- the draft Designated Businesses (Registration and Oversight) Bill
- a joint initiative with the Isle of Man

<sup>1</sup>Tim Cullen, Sir David Lewis and Paul Wright

<sup>2</sup>John Aspden, Roger Butler, Alan Smith, and Bryan Stott

Office of Fair Trading regarding consumer awareness

- an enhanced civil penalty regime
- additions and updates to the Commission's secondary legislation including the latest version of the Financial Services Rule Book
- divisional periodic reports
- AML/CFT developments including the admission to MONEYVAL and the need for the Island to produce a National Risk Assessment
- regular reviews of progress with implementing recommendations following the latest assisted self-assessment in readiness for the next IMF review.

Under Schedule 1 to the Financial Services Act 2008 the Commission is required to submit a report to Treasury on its proceedings and activities for the previous year, together with its accounts audited under the Audit Act 2006. This Annual Report for 2013/14 is being submitted to Treasury in fulfilment of this obligation. The Financial Services Act 2008 also requires the Annual Report to be laid before Tynwald.

The Commission's Annual Report and Accounts for 2012/13 were laid before Tynwald in October 2013 in fulfilment of the requirement in the Financial Services Act 2008.

## Corporate governance and risk management

The Chief Executive of the Commission is responsible for ensuring that its business is conducted in accordance

with the law and proper standards, and for developing and operating internal controls to ensure that public money is safeguarded, properly accounted for, and used economically, efficiently and effectively.

In discharging his responsibility and reporting to the Board, the Chief Executive and senior officers of the Commission are required to put in place adequate arrangements for the governance of the Commission's affairs and the stewardship of resources at its disposal. This is also embraced within the Isle of Man Government's Corporate Governance Principles and Code of Conduct. The Commission is required to submit to Government an annual Statement of Internal Control covering implementation of these arrangements.

The Commission operates within a control environment which includes the Government's Financial Regulations, a framework of functions and responsibilities delegated to individual officers via job descriptions and monitored by a regular appraisal system, the staff handbook (including codes of conduct, etc.) and an internal reporting mechanism through the senior management team to the Chief Executive and to the Board.

The control environment sets the overall structure for internal control and the exercise of the responsibilities of the Commissioners, Chief Executive, Directors, and Officers in regard to all matters, including such areas as the:

- accomplishment of established goals and objectives

- appropriate exercise of powers and delegated authorities within the Commission
- compliance with policies, plans, procedures, law and other requirements
- management of conflicts of interests
- reliability and integrity of management information
- economical and efficient use of all resources
- safe-guarding of all assets.

Whilst responsibility and accountability for internal control is vested with the Chief Executive, the Treasury has a role in reviewing the adequacy of the Commission's internal controls through a programme of internal audit work.

The Commission's RICC has now completed its eighth full year of operation. The RICC has defined published terms of reference. Its purpose is to advise the Board on the quality of the Commission's financial management, corporate governance and the adequacy of its systems of internal control. The RICC also actively considers new and emerging risks, and a process is in place internally to alert both the RICC and the Board of Commissioners to these. Matters covered by the RICC at its meetings during the period included:

- A meeting with the Commission's external auditors to consider any issues arising from the audit of the Commission's Annual Report and Accounts for the period in advance of the Board's consideration of the Audited Accounts. The auditors raised

no issues in relation to the audit and the audit opinion was unqualified.

- The Commission's annual Statement of Internal Control. The auditors undertook a review of controls supporting this statement and no issues were raised.
- Delegations of authority from the Board to the Chief Executive and others within the Commission.
- Risk factors affecting the various divisions of the Commission including the way in which these are drawn to the attention of the RICC.
- A review of the types of risk that the RICC should consider.

## External communication

As a financial services regulator, the Commission's stakeholders are many in number and each category of stakeholder has its own imperatives. The imperatives of one stakeholder type can sometimes be the antithesis to those of another. Effective communication with all stakeholders remains of paramount importance to the Commission, which must on occasion determine the direction to follow and judge between competing views of the stakeholders - using the regulatory objectives and factors it must consider to guide it.

The Commission's main stakeholders are as follows:

The public - including local residents as well as the international community that use the services of the Commission's licenceholders

Tynwald

Licenceholders

Treasury

Other regulatory and law enforcement authorities within and outside of the Island

Gatekeepers - those persons and bodies that provide important services to licenceholders, such as lawyers and accountants  
Its own staff.

In view of the importance to the Commission of relations with all of its stakeholders, this subject is included as a standing item on each agenda for Board meetings.

Communication occurs regularly as part of the day-to-day supervision of licenceholders, but in addition to this other stakeholder communication takes place including:

- consultation on the Commission's proposals for regulatory or legislative change
- issuance of a regular Licenceholder News bulletin
- seminars, workshops and briefings for the industry
- issuance of relevant consumer information via 'Frequently Asked Questions' documents available on the Commission's website and via local Town Halls, Citizens Advice Service offices and the OFT
- meetings between Commissioners and industry members and professional bodies
- regular meetings with Treasury and

liaison with relevant Government Departments

- regular communication with other home/host regulators, including locally the Gambling Supervision Commission, Insurance and Pensions Authority and OFT
- responding to consultations from other bodies, including those emanating from the UK FCA and HM Treasury as well as the European Supervisory Authorities such as ESMA or standard-setting bodies such as IOSCO
- contact with the IMF and standard-setting bodies as appropriate
- active participation in Government working parties on particular topics
- briefings for Members of Tynwald
- participation in industry fora
- co-operation in responding to requests for assistance through established gateways
- liaison with the media.

Actions linked to the above are referred to throughout this Report.

On 29 October 2013 representatives of the Board of the Commission met Board members of the Guernsey and Jersey financial services regulators in London. These meetings are usually held annually and they provide a forum to exchange views on international and domestic issues, discuss commonalities of approach and learn from each other's supervisory experiences. At this meeting topics for discussion included the ICB report and UK banking reform and major international regulatory developments.



Consultation with industry is the main way in which the Commission discusses and seeks comments on regulatory proposals, and the Commission appreciates the time which respondents set aside to make sure this process works effectively.

In conducting its work and communicating with stakeholders the Commission met regularly (usually quarterly) with the following industry representatives and practitioners:

Accountancy bodies and representatives

Association of Corporate Service Providers

Financial Planners & Insurance Brokers Association

Isle of Man Bankers Association

Isle of Man Funds Association

In addition in July 2013 approximately 160 persons attended the Commission's annual Finance Sector briefing.

The Commission remains a strong supporter of the Small Countries Financial Management Programme which contributes to the growth and prosperity of small countries through capacity building in the government financial sector.

## **Complaints against the Commission**

Many of the decisions taken by the Commission in the course of exercising its regulatory functions are subject to review in accordance with the Tribunals Act 2006, if the affected person so

requests. This is an important safeguard for those who may be affected, and at the same time ensures that the Commission must be ready to justify its actions and that it is accountable for the procedures which it has followed.

Sometimes a person may wish to lodge a formal complaint about the Commission and how it has handled a matter. The Commission has published, on its website, its procedures for dealing with complaints made against it, providing for a review of the matter and response by the Chief Executive. If the complainant remains unsatisfied, then that person may seek a further review by the Board of the Commission.

No complaints were made against the Commission during the period of this report.

# Corporate Plan

The Commission prepares a medium-term corporate plan which is built around its regulatory objectives and reflects the key messages of international co-operation, risk mitigation and economic development.



## Corporate Plan 2013/14

The Commission's corporate plan for 2013/14 is set out below. The items listed beneath each objective are some of the measures that were scheduled to be undertaken over the period of this Report to meet these objectives.

The Target Date column provides an update on progress.

### **Objective: Secure an appropriate degree of protection for customers of persons carrying on a regulated activity**

Initiative	Deliverables	Lead Division	Target Date
Domestic Systemically Important Financial Institutions	Develop an approach to identify and regulate Domestic (including IoM) Systemically Important Financial Institutions.	Supervision	2014 Ongoing
Implement retail distribution review	Establish a relevant level 4 qualification and enhanced CPD mandatory for all persons giving financial advice to retail investors. Enhance disclosure requirements to investors.	Supervision	Completed
Review of Commission's secondary legislation	Review of the Financial Services Rule Book, Exemption Regulations and Regulated Activities Order, issue for consultation, consider responses and take new documents through Tynwald.	Policy	Completed
Civil penalties	Expansion of the use of civil penalties to encourage good compliance - consider consultation responses, review policy, consult on revised policy and draft Regulations and bring into effect.	Policy	September 2014 Ongoing
Structured deposits and packaged products	Consider how structured deposits and packaged products are sold and marketed, including visits to banks.	Supervision	2014 Ongoing
Basel III implementation	In conjunction with other Crown Dependencies consider what changes in regulatory approach are appropriate, develop response and update industry.	Supervision	2013-2018 Ongoing
Bank Special Resolution Regime (including recovery and resolution)	Review Basel Core Principles and decide upon action in response.	Supervision	2014-2016 Ongoing
ICB report and UK banking legislation	Participate in Government working group where objectives and deliverables are set.	Supervision	2014-2015 Ongoing

**Objective: Reduce financial crime**

Initiative	Deliverables	Lead Division	Target Date
Desk-based MONEYVAL assessment	Complete desk-based questionnaire.	Enforcement	Completed
On-site MONEYVAL assessment	Prepare for a full on-site assessment by MONEYVAL.	Enforcement	Ongoing, now taking place 2016
National Risk Assessment	Formulate a National Risk Assessment in line with Recommendation 1 of the FATF methodology.	Enforcement	September 2014 for first phase (beneficial ownership action plan)  Full National Risk Assessment ongoing, expected 2015
DNFBPs - AML/CFT monitoring	Consult on draft Bill, oversee passage of Bill through Tynwald, implement regime.	Enforcement	Ongoing, expected March 2015

**Objective: Support the Island's economy and its development as an international financial centre**

Initiative	Deliverables	Lead Division	Target Date
AIFMD	Establish co-operation agreements with EU and EEA competent authorities as necessary to ensure Isle of Man alternative investment funds can be marketed into the EU from July 2013 onwards.	Policy	Completed
Assisted self-assessment review	Formulate action plan, consider response to recommendations and implement agreed changes.	Policy	Ongoing, now taking place 2016
Consideration of the funds offering (including review of closed-ended investment companies)	Consider options and consult with the industry.	Supervision	2014 Ongoing
SEPA	Progress application with EPC to become SEPA member.	Policy	EU dependent Ongoing

Initiative	Deliverables	Lead Division	Target Date
Financial Services (Miscellaneous Amendments) Act	Implement Act and internal procedures.	Supervision	December 2014 Ongoing - Act now in force but some CISA 08 elements are pending formalisation of civil penalty project
MIFID2/MIFIR	Monitor proposed items for effect on Isle of Man and its financial services sector.	Policy	EU dependent Ongoing

Although not a statutory objective, in order to maximise efficiency and ensure the most productive use of resources the following tasks were also identified:

Initiative	Deliverables	Lead Division	Target Date
Off-site storage	Review paper files held off-site in line with agreed retention policies.	Operations	Completed
Review of licence fees	Undertake a review of the Commission's policy on licence fees, consult with the industry, make changes to fees orders.	Policy	May 2013 Completed
Online reporting system for funds and funds database	Complete development of funds database for online submission of funds data and implement.	Operations	September 2013 Behind schedule - expected June 2014
Supervision database	Develop proposals to re-engineer existing system to provide for a flexible framework to submit static and annual compliance data online.	Operations	November 2013 Behind schedule - revised to 2015
SharePoint 2010	Migrate to SharePoint 2010, implement SharePoint within Supervision and Authorisations. Replace existing general intelligence system, establish physical and electronic records management across the Commission.	Operations	December 2014 Ongoing



Initiative	Deliverables	Lead Division	Target Date
Scope of Government	Participate in efficiency reviews as part of Scope of Government review.	Operations	To be advised by Government

## Corporate Plan 2014/15

The Commission's corporate plan for 2014/15 carries forward all ongoing matters from the 2013/14 plan set out above and also includes the additional items below. Some of these additional matters result from the suggestions for further actions made by the independent assessor who assisted the Commission to produce a self-assessment of the Island's adherence to relevant international standards in 2013:

Initiative	Deliverables	Lead Division	Target Date
Credit Unions	Liaise with DED and Treasury over the drafting instructions for changes to the Credit Unions law, and bringing Credit Unions into the remit of the FSA08 and the Regulated Activities Order.	Policy	2015
Self-assessment - IOSCO / CIS measures	Take forward necessary IOSCO/CIS changes via funds scope project. Following consultation any secondary legislative changes to be made by December 2015.	Policy	December 2015
Self-assessment - Treasury / Governance measures	Take forward request to Treasury on dealing with necessary points that require changes to FSC/Treasury relationship, seek Treasury's agreement to implement and assist Treasury to do so.	Chief Executive	December 2014
Self-assessment - Basel measures	Implement changes necessary (excluding those detailed separately above: D-SIBS, Basel III and Bank Special Resolution Regime).	Supervision	2014





# Regulatory and Supervisory Approach

The Commission's regulation and supervision are designed to protect consumers, reduce financial crime and meet the standards required of international standard setters. In so doing the Commission provides a framework for industry to adhere to and which thereby provides opportunities for compliant Isle of Man businesses.



**Michael Weldon**  
Director - Supervision

In both authorising and supervising licenceholders a risk-based approach is used. The Commission seeks to understand the risks and impact posed by the institutions it supervises, and how these may increase or decrease over time or how they may change due to external or internal issues impacting upon the licenceholder or its wider area of operation. However, the role of a regulator is not to prevent licenceholder failure, which instead is the responsibility of the boards and management of the licenceholders. Indeed, failure can occur if there are serious shortcomings in these responsibilities.

For any business conducting regulated activity, consideration of risks by the Commission commences when determining its licence application. In considering whether to licence any business there is a difficult balance to be struck. On one hand the Commission must consider consumer protection,

fitness and propriety and reputational issues, and on the other it must be cognisant of innovation and new products and services and ways of doing business. There is a natural tension in these considerations and dialogue with licenceholders, licence applicants and the wider business community remains important.

## Licenceholder survival

Over this period an analysis was undertaken of the financial services licences that have been issued by the Commission over the previous five years, and then to compare this figure against how many of those licences remain in issue. After removal of items from the population that could distort results (such as simple licence extensions), and acknowledging that the relatively small sample size may result in percentages that look more significant than they ought, the following data was returned:

Survival rate	1 year %	2 years %	3 years %	4 years %
2009	100.00	83.33	75.00	66.67
2010	92.31	53.85	46.15	46.15
2011	83.33	83.33	66.67	
2012	71.43	71.43		
2013	100.00			

Table showing survival rate in % for licences issued to start-up companies in each of the previous 5 years.

It is interesting to note that of licences issued in 2009 the failure rate has been 33.33%, or one of three licences issued, and for those issued in 2010 the failure rate was over 53% within three years. If this data is further broken down by sector, it illustrates large variations in the 'survival rates' between different regulated activities, with the fiduciary services sector strongly outperforming the others.



## Authorisations

The Commission's General Licensing Policy is published on its website and details the criteria applied by it when considering licence applications. The aim of the General Licensing Policy is to ensure firms meet and maintain the necessary standards, which in turn help to protect consumers and maintain the Island's reputation.

The General Licensing Policy makes sure that applicants are fully aware of the Commission's expectations, such as the requirement for a business to have a real presence on the Island and to be operated by key persons who are fit and proper with a demonstrable track record. It also provides details of the different categories of regulated activity. With regard to Class 3 regulated activity - the provision of services to collective investment schemes - there is a supplementary licensing policy. Having regard to the General Licensing Policy should ensure that applicants are able to frame their applications appropriately, which can ultimately save time and resources for both the applicant and the Commission.

The General Licensing Policy has been expanded over this period to provide clarification that in making a determination of a licence application, the Commission will consider the cumulative effect of matters before it, which taken together, could cause a licence to be refused.

A further addition to the Policy was in relation to the Commission's prohibition power, which was introduced following

the Financial Services (Miscellaneous Amendments) Act 2013 coming into force in July 2013.

In addition to consulting on the General Licensing Policy, the Commission urges potential licence applicants to contact the Commission's Authorisations Division to discuss their plans at an early stage. The Division has a positive, welcoming, open-for-business approach to new business proposals wherever they meet the Commission's criteria, and Commission staff can then talk applicants through the licensing procedure. This is an excellent opportunity to open up positive two-way dialogue and assist understanding from both sides.

During the year, the Division met with and handled enquiries from individuals interested in undertaking a wide range of financial services in the Isle of Man. During the latter part of the period, the majority of enquiries related to payment services, foreign exchange and virtual currencies. Not all enquiries involve regulated activities and many of them are early stage enquiries that do not progress to implementation.

Applications for financial services licences are prepared by the Authorisations Division. Following preparation, the applications are considered by an internal committee made up of staff from across the Commission including the Supervision Division. This internal committee conducts a preliminary review of the proposal.

In due course, following the

internal committee's review, a final recommendation is sent concurrently to the applicant and the Board of the Commission at least 14 days ahead of the licence hearing. The hearing will take place in front of at least a quorum of the Board. An applicant may attend the licence hearing to make any representation.

If an applicant is not satisfied with the decision of the Commission, an application for review can be made to the Financial Services Tribunal.

The following table shows the number of applications for licences that were issued over this period, compared to the

period of the previous Annual Report. The number of licence applications received during the year is lower than the number for the previous year. In addition a number of applicants had a change of heart and withdrew from the process prior to conclusion. The application withdrawals were for a variety of reasons, including a decision that the timing was not right for the launch of the proposed venture. The lower amount of applications and the decision not to pursue applications to a conclusion are both felt to reflect the challenging economic climate which persists for financial services enterprises.

<b>Regulated Activity</b>	<b>Issued 2013/14</b>	<b>Issued 2012/13</b>
<b>Class 1 - Deposit taking</b>	0	0
<b>Class 2 - Investment business</b>	2	1
<b>Class 3 - Services to collective investment schemes</b>	1	3
<b>Class 4 - Corporate services</b>	1	7
<b>Class 5 - Trust services</b>	1	3
<b>Class 7 - Management &amp; administration</b>	0	0
<b>Class 8 - Money transmission services</b>	0	0
<b>Total</b>	<b>5</b>	<b>14</b>

(Note: Where a licence covers more than one class of regulated activity, it has been recorded against the 'principal' regulated activity of the applicant.)

Where the necessary information required by the Commission is provided in a timely manner, applications should be processed within a three month period. This timescale can be shortened particularly if the persons involved are already undertaking regulated activity in the Isle of Man.

In last year's Report it was noted that the quality of a number of business plans, submitted in support of licence applications, was sub-standard. This has again been a feature of applications. As noted previously, it is important that all applicants can articulate the reasons why they believe their business venture will be a success. It is also important to document the assumptions underlying any financial projections and to demonstrate that suitable financial support is in place should income assumptions not be met.

The Commission has in place an arrangement whereby persons who make a licence application are invited after the exercise to comment on how

they feel the Commission performed. The feedback on licence applications received during this period was largely positive. One applicant felt additional clarity would be helpful on the financial resources information needed to support an application. As a result the Commission's business plan guidance has been updated with additional information being included in the section covering financial information.

The number of individuals vetted by the Commission during the period was 498. This is an increase of around 20% over the previous period. As the amount of licence applications is lower this year, the increased vetting represents a higher number of changes to senior appointments within existing licenceholders.

<b>Full</b>	278
<b>Update</b>	220
<b>Total</b>	498

## Supervision

### **The Supervision Division is responsible for the Commission's core task of monitoring and supervising licenceholders.**

The Division is split into four teams. Three teams have direct responsibility for the supervision of specific regulated activities which are:

- Banking (responsible for deposit takers and also money transmission services)

- Fiduciary services
- Funds and investment services.

The fourth team manages the Division's Risk and Compliance matters and also provides administrative support to the remainder of the Division. This team is responsible for undertaking ongoing compliance reviews of Supervision Division staff's adherence to the internal systems, controls and procedures, and highlighting, co-ordinating and addressing any risk or compliance matters.



The following table identifies permissions held by category - some licences contain more than one permission:

Regulated Activity	Number of licenceholders conducting the following regulated activities As at 31 March	
	2014	2013
Class 1 - Deposit taking	28	32
Class 2 - Investment business	54	56
Class 3 - Services to collective investment schemes	58	63
Class 4 - Corporate services	172	183
Class 5 - Trust services	126	131
Class 7 - Management & administration	9	9
Class 8 - Money transmission services	6	6

The figures record a decline in the number of licence permissions held year-on-year. This does not necessarily mean that the business conducted by those firms has been lost to the Island. Several licence surrenders are the result of retirements and consolidation but with the business remaining on the Island. The Class 1 deposit taking reduction is due to the withdrawal of the AIB banking group (2 licences) and reorganisations within 2 other banking groups, which resulted in the surrender of one deposit taking permission in each instance.

## Supervisory approach

The supervisory approach is contained in a published document available on the Commission's website that sets out the Commission's approach to the

supervision of the different elements of the financial services industry that it regulates.

The nature and frequency of on-site visits is related to the size, activity and risk profile of any licenceholder or its corporate group.

The supervision of licenceholders is multi-faceted and it includes a combination of the following:

- receipt and review of prudential returns, statistical information and notifications
- use of general and themed questionnaires
- on-site visits, with follow-up action plans



- formal and informal discussions with management
- provision of feedback and guidance to licenceholders.

The on-site oversight of licenceholders' adherence to AML/CFT requirements is a constant theme within the supervisory process. Another important theme that was specifically focused upon this year was the use of clients' money bank accounts and the associated record keeping and controls surrounding

them, including sample testing some of the transactions passing through such accounts. Themed visits on the operation, control and oversight of clients' money bank accounts and the use of such (including further transaction testing) will continue to be a feature of our supervisory on-site visits.

Commission staff keep abreast of current consumer issues. Regular meetings are held with the OFT to assist in determining which products and services are causing concern to clients

of the Isle of Man financial services industry.

In respect of banks and in addition to AML/CFT oversight, the Commission's focus continues to be on prudential risks (such as liquidity, capital adequacy, credit and large exposures), corporate governance and risk management, and conduct issues (such as complaint handling, sale of products and treatment of customers). There is also a developing area of focus covering bank resolution.

The supervisory approach continues to include Annual Desk Based Reviews. The ADBR is a review of each licenceholder's previous 12 months' regulatory history coupled with a consideration and review of each licenceholder's forward-looking risk assessment and risk mitigation programme to ensure that these are accurate and up-to-date. The ADBR encompasses an examination of a licenceholder's Annual Return pack and its audited financial statements, an assessment of the licenceholder's compliance with the Rule Book, any current issues or key events in the period, and the licenceholder's risk and impact ratings as well as its risk mitigation programme.

On and off-site supervision will often result in suggestions or requirements for licenceholder improvement, or observations relating to shortcomings and the required action necessary to ensure regulatory compliance. Where this is the case the Commission clearly details its requirements to the licenceholder along with agreed

timescales for completion of the action. Occasionally, there may be the need for follow-up visits to validate that any remediation work or other necessary actions have taken place.

As is the case for seeking feedback on the licence application process, the Commission also invites licenceholders that have received an on-site visit to comment on how they feel the Commission performed. Suggestions for the improvement of visits, including in relation to efficiency and effectiveness, are welcomed and encouraged. The feedback on visits during this period was very positive in the majority of cases. Approximately one licenceholder in every two provided feedback and we do issue reminders to licenceholders to complete the feedback form. The Chief Executive provides a periodic report to the Board on the feedback that has been provided by licenceholders.

Licenceholders, or their group companies, may also be subject to regulation by the IPA, and as a result the staff of Supervision Division regularly meet with the IPA to share supervisory information and conduct other ad hoc meetings as required.

## **Risk and compliance**

The Risk and Compliance team is involved with the maintenance of the Commission's 'compliance support' section of its website, including the provision of template registers for optional use by licenceholders in respect of various matters. The team also undertakes the analysis of licenceholders' annual and interim

financial returns, and ensures the Division's operational procedures and controls are up-to-date and effective.

The Risk and Compliance team is also responsible for handling complaints about non-bank licenceholders. Over the period of the report the total number of non-banking complaints reviewed was 26. The nature of these complaints included mis-selling of financial products, quality of service, fee disputes and corporate governance issues.

The Commission does not have a power to rule on complaints or make awards - this is the role of the Financial Services Ombudsman. However, it will usually discuss a complaint with a licenceholder, encouraging a resolution if possible and will take action if any regulatory breaches have occurred.

The Risk and Compliance team has recently taken on the function

of assessing how the Commission is performing against the internal standards that it measures itself against. These include standards for:

- issuing responses to correspondence received
- issuing visit reports following on-site visits
- review of Annual Compliance Returns and other submitted data
- review of financial returns
- complaint handling
- responding to international requests for assistance.

The Commission believes that it is important to monitor such areas in order to ensure it is dealing with matters in a timely manner.

The following table sets out the remedial and other licenceholder actions taken

	Year ended 31 March	
	2014	2013
<b>Directions</b>	66 - of which 14 were remedial	59 - of which 8 were remedial
<b>Civil penalties</b>	25	26
<b>Section 11 warning notices</b>	0	0
<b>Licences (or classes thereof) suspended or revoked</b>	0	0

The Remediation Unit (which was part of the Risk and Compliance team) has now transferred to the Enforcement Division of the Commission, as a separate Disciplinary Unit, with two members of Supervision Division seconded to assist in the staffing of the Unit. Further information regarding the Disciplinary Unit can be found in the Enforcement section of this Report.

## Banking and money transmission services

The following table outlines the number of visits to, and annual business meetings with, banking groups:

Visits to and meetings with banks				
Period	Annual business meeting	Compliance		Total
		Supervisory	Focus/Themed	
Actual for year ended 31 March 2014	20	0	16	36
Planned visits for year ended 31 March 2014	21	0	18	39
Actual for year ended 31 March 2013	20	0	17	37

### Banking business

Over the period of this Annual Report the Commission's supervisory work with banking groups gave priority to the following key areas:

#### *AML/CFT*

Following a themed visit programme in 2012/13 on this topic, feedback was issued in December 2013 to the banking sector highlighting the key findings from the reviews; the key findings are also published on the Commission's website.

#### *Structured deposits and other non-standard accounts*

A detailed questionnaire was issued in 2012 to discover more about the way in which structured deposits are designed, marketed and sold by banks. Interim

feedback based on the questionnaire responses was issued in November 2013 and on-site visit work was also conducted. The Commission will also be considering monitoring the position in respect of packaged bank accounts. Any changes required to the regulatory framework to address relevant matters will be considered during 2014/15.

#### *Visits in the period*

Our visit programme in 2013/14 was undertaken on an individual bank basis. Each visit was tailored to areas where we considered there may be risks to the Commission's objectives, where an area of activity had materially changed since our last review and to cover matters pertinent to other supervisory work (for example structured deposits).



Examples of topics covered included: management and monitoring of problem loans; large exposures management; treasury and liquidity management; governance and risk management; AML/CFT and prudential reporting.

### *Large exposures*

Previous changes made to the rules governing large exposures, including exposures to other group banks, are now embedded. Updated guidance was also issued in March 2014.

The Basel Committee on Banking Supervision issued a consultation in 2013 covering proposed revisions to the supervisory framework for measuring and controlling large exposures. A final set of revised standards was published in April 2014, for implementation by supervisors by 1 January 2019.

### *Complaints and conduct matters*

During the year, some complaints about banks were received by the Commission. There were no specific themes and complaints ranged from issues concerning service and delays, loan products and banks' approach to account closures.

The Commission also monitors and reviews how conduct/consumer issues that arise in the home jurisdictions of banks located in the Isle of Man (most notably the UK) could impact on customers of banks in the Island. Licenceholders are expected to take into account best practice expectations and treat customers appropriately. This can result in issues originating, say, in the UK having an impact locally with customer redress having to be considered.

Examples have included the sale of interest rate hedging products to small businesses and payment protection insurance.

### *Closure, integration and restructuring*

The closure, restructuring, integration and sale of some banking groups continued over 2013/14. Supervisory work linked to this activity involves ensuring that any change in controller is acceptable to the Commission, relevant notification requirements are adhered to, liaison takes place with relevant regulatory authorities, and customer communication is clear and dealt with in a timely manner.

Significant work in this period has included:

- monitoring the wind-down and ultimate surrender of the AIB Group's regulated business in the Island
- monitoring the wind-down of Bank of Ireland's regulated business in the Island, which is due to be completed in the summer of 2014
- monitoring the wind down of Britannia International's regulated business in the Island
- considering the restructure of the deposit-taking business of the Nationwide and Santander Groups in the Island, whereby deposits were transferred from Isle of Man subsidiaries into Isle of Man branches of UK entities.

### *Reporting to the Bank for International Settlements (BIS)*

The Isle of Man participates in the reporting of statistics on banking activity

in the Island to BIS. The Commission is the body in the Isle of Man which collects information from banks quarterly and aggregates this for reporting purposes. BIS compiles and publishes two sets of statistics on international banking activity: locational banking statistics and consolidated banking statistics. Only the locational banking statistics are relevant to the Island.

During the year the Commission and banks have undertaken considerable work to ensure the Island is able to comply with enhanced statistical reporting to BIS (known as Stage 2 enhancements). Reporting to BIS under Stage 2 commenced for data as at 31 December 2013. The data now being supplied by banks (for aggregation and reporting), is more granular and includes greater detail on breakdowns of assets and liabilities.

## **International developments and the Isle of Man banking sector**

### *Basel III*

The Commission started work with its counterparts in Guernsey and Jersey in 2012 (the tri-party group) to determine how Basel III may be implemented in the Crown Dependencies. Following the issuance in September 2012 of the first high-level tri-party group discussion paper, a decision was made to issue further detailed discussion papers covering specific proposals relating to the following core areas of Basel III: capital adequacy, liquidity and leverage ratio. Work on domestic systemically

important banks and recovery and resolution is covered below but also links to Basel III.

In December 2013 the tri-party group issued a discussion paper containing detailed proposals regarding capital adequacy; feedback was received from banks in March 2014. Further papers covering liquidity and leverage are expected to be published in 2014.

The aim, once all discussion papers have been issued, comments received and considered, will be to produce a final consultation on proposals to implement changes to the legislative framework.

### *UK's Independent Commission on Banking (ICB) Report (UK banking reform)*

As previously reported, the primary recommendation of the ICB Report was the proposed ring-fencing of certain retail operations of UK banks from their wholesale/investment activities. The rationale was to provide the ring-fenced banks with 'economic independence' and to assist financial stability and orderly resolution.

Following work undertaken in 2012/13 by the Commission, in conjunction with Guernsey and Jersey, in April 2013 the Isle of Man Government established a working group to address the challenges created by the proposals. It was identified that the proposals could have a fundamental effect on the structure of certain banks in all of the Crown Dependencies; impacting on areas such as permitted services, depositor protection, cross-border resolution

and insolvency legislation (including preference of creditors).

The working group, which includes a representative of the Commission, meets at least monthly and works in collaboration with Guernsey and Jersey on engagement with the UK authorities.

During this period the key events in relation to UK banking reform have been:

- Submission of papers to, and meetings with, HM Treasury ahead of the UK Government's draft secondary legislation covering banking reform.
- Publication by the UK Government in July 2013 of draft secondary legislation for banking reform. This included the proposal that UK ring-fenced banks should be allowed to maintain branches in the Crown Dependencies.
- Submission in October 2013 of an Isle of Man Government response to the draft secondary legislation (a summary of responses was published by the UK in December 2013).
- Further meetings with, and submissions to, HM Treasury, focused on depositor preference and deposit compensation arrangements.
- Provision of a paper in January 2014 to local banking groups that will be affected by the changes covering different scenarios (structures) and the key regulatory matters that need to be considered.

The working group expects further clarity to be provided during 2014 on how deposit preference and 'bail-in'

arrangements will operate within the UK and EU banking systems, and how third countries, such as the Isle of Man, will fit into these frameworks.

#### *Domestic systemically important banks and recovery and resolution*

In October 2012 the Basel Committee published a document on "a framework for dealing with domestic systemically important banks". This framework is focused on the impact a bank may have on the domestic economy if it fails. The framework is part of Basel III but specifically applies to subsidiaries and, at the discretion of the supervisory body, branches.

The framework has 12 key principles covering two aspects: assessment methodology (which defines what makes a bank a D-SIB) and requirements for D-SIBs to have higher loss absorbency (capital). It also recognises that other tools such as more intensive supervision and the development of a more appropriate framework for recovery and resolution play a part.

In considering recovery and resolution, the paper "Key Attributes of Effective Resolution Regimes for Financial Institutions" issued by the Financial Stability Board in October 2011 is considered to be guidance on best international practice. Similarly, the UK Special Resolution Regime and proposals connected with ICB and the EU proposals regarding the new Bank Recovery and Resolution Directive will be important reference points.

The Commission is working with the

tri-party group to determine how to approach the matter of D-SIBs and recovery and resolution in the Crown Dependencies. A tri-party discussion paper was issued in January 2014. Work will continue in 2014/15 in conjunction with Government where required, covering the following key areas:

- the development of a regime addressing the Basel framework for D-SIBs
- how Isle of Man branches and subsidiaries will fit into group-based recovery and resolution plans
- whether the Island needs to strengthen its powers and tools to facilitate recovery and resolution of banks
- the role of the depositors' compensation scheme
- how bail-in and deposit preference measures in other jurisdictions may impact on operations in the Island (for branches and subsidiaries which have large intra-group exposures)
- the scope and detail of the EU's proposed Bank Recovery and Resolution Directive, and how this is implemented in the UK.

### *FATCA*

FATCA is principally a taxation matter, not a regulatory one but it has an effect on the Island's banking (and other) sectors. Because of this, Commission staff took part in a cross-Government FATCA liaison group, which has now been disbanded following the signing

by the Isle of Man Government of two Intergovernmental Agreements - one with the UK and one with the USA.

To accompany the UK IGA, HMRC in the UK established a Disclosure Facility which licenceholders were required to notify relevant persons of by 31 December 2013, and they must do so again during the six months to 30 September 2016.

In January 2014, and again in April 2014, the Income Tax Division of the Isle of Man Treasury issued draft Guidance Notes on the IGAs to the industry for comment (in conjunction also with Guernsey and Jersey).

## **Looking ahead: 2014/15**

### *Planned visit themes for 2014/15*

Our visit programme in 2014/15 is being undertaken on an individual bank basis but with some core themes built into the approach. These themes are AML/CFT, operational risk and remuneration/incentive schemes. Each visit will also be tailored to areas where we consider there may be risks to the Commission's objectives, or where an area of activity has materially changed since our last review.

### *Lending data*

The Commission wishes to improve the regular information it receives in relation to banks' loan exposures. It is currently working on a draft reporting form and completion notes with a view to having a final agreed reporting form in place with effect from 1 December 2014.

### *International developments*

The core topics of Basel III, UK banking reform, D-SIBs and recovery and resolution will continue to be a primary focus of our work over the next year and beyond. Legislative changes will ultimately be required, and some banks may need or wish to restructure their operations in the Island.

### *Supervisory approach*

The approach to banking supervision will continue to change. This covers both prudential and conduct supervision. The Commission will be considering how it communicates its approach and continues to ensure that it is meeting the expectations of stakeholders.

## **Money transmission services**

In 2011/12 the banking team took over the responsibility of supervising MTS businesses. Currently, MTS businesses in the Island are split into two distinct sub-categories for supervisory purposes:

- Those that *only* conduct bureau de change, cheque cashing and provision of payment services as agent (e.g. for Moneygram or Western Union).
- Those that conduct the provisions of payment services directly.

A programme of on-site visits and discussions commenced from April 2012. All licenceholders have now been visited at least once, with some follow-up visits also held to ensure actions required by the Commission

have been implemented. By the end of the 2014/15 period all will have been visited at least twice within three years.

### *Bureau de change, cheque cashing and provision of payment services as agent (3 licenceholders)*

The core focus of the banking team's work since April 2012 has been on AML/CFT compliance. In 2012/13, four visits were planned and undertaken (including a visit to an exempt person which is not required to hold a licence but is subject to the provisions of the AML/CFT legislation in the Island). In 2013/14, three follow up visits were also planned and all have been undertaken.

Following the first set of visits, it was considered beneficial to provide more specific AML/CFT sector guidance for these businesses. This was completed and guidance issued in June 2013.

Although the banking team's prime focus will remain on AML/CFT, in order to supervise these entities it also implemented some additional rule requirements with effect from 1 February 2014. These cover certain notifiable events and also the provision of audited financial statements for Isle of Man incorporated entities.

### *Provision of payment services directly (3 licenceholders)*

The core focus of the banking team's work since April 2012 has been on understanding business models and risk assessing firms, AML/CFT compliance, and the operation of the segregated payment accounts to hold relevant funds. In 2012/13, one visit was planned and undertaken, and in 2013/14 a



further two visits were planned and held. Further updates (visits or annual meetings) are scheduled for 2014/15.

## Fiduciary services

The Isle of Man is one of few jurisdictions globally that licenses CSP and TSP activity, and its regulation of such enhances the Island's transparency as well as providing some protection for the consumers of these services.

The total number of companies and trusts under administration remained

broadly stable during 2013/14. Companies and foundations showed a similar increase to the previous year (3%) whilst trusts and private trust companies reduced by 0.6%.

The turnover of trust and corporate service providers increased by approximately 5% and profitability also increased.

The following table outlines the number of visits to, and annual business meetings with, fiduciary companies and professional officers:

Visits to and meetings with fiduciaries					
Period	Annual business meeting	Compliance			Total
		Supervisory	Focus/Themed	Professional Officers	
Actual for year ended 31 March 2014	35	34	18	5	92
Planned visits for year ended 31 March 2014	40	43	16	7	106
Actual for year ended 31 March 2013	50	24	18	1	93

The approach to on-site visits has moved away from the issuance of initial themed questionnaires and then selecting the necessary visits based on the responses. The team has returned to a programme based around on-site visits, using focus visits in particular to review the operation of client money accounts. This is reflected in a reduction in annual business meetings and an increase in supervisory visits. Most of the reduction in actual visits compared to the initial plan resulted from visits no longer being required, for example because a business had restructured.

The team has provided detailed feedback on its visit findings over this period through the ACSP and industry presentations given in February 2014.

*Looking ahead: 2014/15*

Themes in 2014/15 will include further checks on client money transactions and PLCs and companies with 50+ shareholders.

The fiduciary team will continue to emphasise the importance of corporate governance and a comprehensive approach to risk management. As the Commission has emphasised in previous years, aggressive tax planning and mitigation structures are not a prudent business strategy, as such business brings unacceptable risk to the licenceholder but also the Island's reputation. The team's emphasis on risk management will include reviewing that licenceholders' AML/CFT risk assessments, which must be used by licenceholders to address and mitigate the risks they have identified.

Supervisory visits will continue to address risks that can arise from cross-selling of services and from

client-client transactions. In particular, the Commission has written to TCSPs, drawing attention to the issues of conflict of interest and commercial risk that can arise where loans or investments are arranged by the TCSP between its customers. The Commission believes that some TCSPs have under-estimated these issues, and it is in the process of conducting an exercise to assess the extent to which such transactions have taken place. Discussions will continue to take place with those TCSPs that have been involved in such lending, and in due course the Commission will decide whether any regulatory intervention is necessary.

## Investment and funds services

The following table outlines the number of visits to, and annual business meetings with, investment and funds services businesses during the period:

<b>Visits to and meetings with investment and funds services businesses</b>				
<b>Period</b>	<b>Annual business meeting</b>	<b>Compliance</b>		<b>Total</b>
		<b>Supervisory</b>	<b>Focus/Themed</b>	
<b>Actual for year ended 31 March 2014</b>	53	12	40	105
<b>Planned for year ended 31 March 2014</b>	53	4	46	103
<b>Actual for year ended 31 March 2013</b>	54	0	47	101

## Investment businesses

### *Retail Distribution Review (RDR)*

As described in the previous Annual Report, the Commission has now progressed with its RDR plans, and changes to the Rule Book that took place on 1 February 2014 have increased the minimum qualification level of financial advisers and enhanced the disclosure of material matters to clients, including regarding remuneration. All financial advisers who advise the retail public are now required to demonstrate they meet the compliance Level 4 standard with a relevant professional body. This implementation increases the level of competency required of advisers and will further protect clients from mis-selling.

In addition the enhancements to the Rule Book require Statements of Professional Standing to be held by advisers from 1 January 2015.

### *Consumer guidance*

The Supervision and Policy Divisions have worked together over this period to develop high-level principles for investor guidance. This is an area of concern given that sustained low interest rates encourage investors to seek higher returns, often by taking increased risk without their necessarily obtaining an understanding of the types of financial products involved, or the true level of risk they are facing.

This initiative was undertaken jointly with the OFT, and resulted in the issuance of two consumer-focused leaflets concerning financial advice shortly after

the end of the period of this report. In order to bring these useful documents to the attention of consumers the Commission issued advertisements in the local press.

The aim of the leaflets is to disseminate important information to consumers about investing and the risks that they should consider when doing so. There is a short leaflet available through the OFT and certain civic amenities and a more detailed leaflet that can be provided by advisers to their clients.

### *Suitability of advice*

Over this period the Commission continued to focus upon the processes and controls adopted by licenceholders to ensure the suitability of advice provided to investors.

This work included consideration of whether advisers were following the Commission's guidance on a number of matters relating to the fair treatment of consumers and the provision of suitable advice. These documents included a pensions advice guidance note (October 2012), a guidance note on advertising, distribution and promotion of financial services (November 2012) and a public statement on the provision of advice, arrangement of a deal or exercise of discretion in relation to higher risk investments for retail investors (December 2012).

The Commission is aware that the Isle of Man Financial Services Ombudsman Scheme's Annual Report of 2012/13 included comment on a number of cases that it had considered which concerned allegations of mis-selling.

In these and other cases where there may be concerns about the suitability of advice given and consumer outcomes, the Commission has commenced investigations.

#### *Investment business visit programme*

- *Financial advisers* - During 2013/14 supervisory visits to financial advisers continued to consider the suitability of advice on investments together with AML/CFT issues. The funds and investment services team also carried out a number of visits focusing specifically on the suitability of pension advice.

Currently, with regard to financial advisers, suitability of advice continues to be the main focus for supervisory work. The Division has collected information from financial advisers regarding their product and risk assessments, sources of income and the breakdown between commissions and fees. This information will provide a more detailed picture of their business and assist the Commission to identify industry norms and outliers thereto. Over the forthcoming period we will visit all advisers who are due a visit on the ordinary cycle to assess suitability of advice.

In addition the funds and investment services team will undertake a short visit to all financial adviser licenceholders to discuss the findings of the financial advice questionnaire and the changes that they have made to procedures and processes required as a result of the most recent Rule

Book update.

- *Other investment businesses including investment managers, stockbrokers, fund investment advisers and asset managers* - During 2013/14 supervisory visits were bespoke according to the nature of business undertaken, but included a focus on compliance, corporate governance, risk management, outsourcing and trading protocols. This approach will continue in 2014/15.

## **Services to collective investment schemes**

The funds industry continues to face many challenges. This period saw the implementation of the AIFMD (July 2013) as well as changes to private placement regimes of EU Member States. The period also saw the UK move away from its previous regime whereby it granted designated territory status to certain fund regimes in designated jurisdictions. It has now moved to requiring the individual recognition of funds directed at the UK retail investor.

Where funds are in liquidation, the funds and investment business team continues to work with the liquidators of such schemes in order to keep updated on any issues arising which may impact on the fitness and propriety of key persons, including the governing bodies of such funds.

The Commission continues to promote the principles of good corporate governance for funds, including the timely issue of investor updates and

audited financial statements. A guidance note for the governing bodies of funds, planned for issue in 2013, will now be finalised and issued in 2014.

Following the granting of an Order by the High Court in 2012/13 in relation to Louis Group Structured Fund Plc, an experienced investor fund, and five other associated companies (Louis Group (IOM) Limited, the holder of a CSP/TSP licence, Louis Group Structured Capital Limited, LG SP Investments Limited, Louis Group International (Europe) Limited and Louis Group SLN Limited) and the appointment of a liquidator deemed Official Receiver under the control of the High Court, the Commission has provided support to and had regular liaison with the liquidator. The Commission has also sought and obtained from the liquidator such information as it has required for its own regulatory purposes. The liquidation continues and the Commission will continue to support and co-ordinate with the work of the liquidator.

During the period the Commission intervened in relation to four linked collective investment schemes - Guardian Alpha Limited, Guardian Analysis Limited, Guardian Beta Limited and Guardian Delta Limited ('the Guardian Schemes'). In July 2013 Mr Maurice Singer and Mr David Peter Craine were appointed to:

- a) advise the Guardian Schemes on the proper conduct of their affairs; and
- b) assume control of the affairs of the Guardian Schemes.

Investors in these schemes have

received an update about the schemes' position from the appointees.

On 1 February 2014 the Collective Investment Schemes (Authorised Schemes) (Trustee and Fiduciary Custodian) Order 2013 came into effect, which amended Schedule 1 to the Collective Investment Schemes Act 2008, to enable authorised collective investment schemes to have a trustee or fiduciary custodian that does not have a place of business in the Island if that trustee or fiduciary custodian meets other criteria. While not part of the Commission's licenceholder base, the Supervision Division has established a system to oversee the quality of work undertaken by non-Isle of Man fiduciary custodians and trustees of authorised schemes. This system may be extended to non-Isle of Man fiduciary custodians and trustees of full international schemes and regulated funds.

#### *Scheme functionaries - Visit programme*

During 2013/14 supervisory visits were bespoke according to the nature of business undertaken. Visits included a focus on compliance, corporate governance, risk management and scheme-based protocols. This approach will continue in 2014/15.

Looking forward, the Commission is working on the following areas in relation to funds:

- Completion of the guidance document on corporate governance for the governing bodies of funds.
- The implementation of the funds database which will enable electronic



notification of funds and changes to funds, annual compliance declarations and the supply of statistical information. The database will streamline the administration of funds information for the Commission and licenceholders, provide electronic reminders in advance of regular reporting dates and act as a source of reference to licenceholders for their submissions to the Commission in respect of funds.

- On the basis of the revised IOSCO Principles and Methodology - updating and simplifying Isle of Man's funds structure and related legislation and guidance, and considering whether or not some closed-ended investment companies should be placed within the definition of collective investment schemes in future.

## Depositors' and Investors' Compensation Schemes

The Isle of Man has both Depositors' and Investors' Compensation Schemes. Further information and details of the coverage which they provide are set out on the Commission's website.

The schemes only come into operation when a relevant default has been triggered, and no claim has ever been made against the Investors' Compensation Scheme, which covers only investors in authorised collective investment schemes.

The Depositors' Compensation Scheme and Investors' Compensation Scheme are separate from the Commission

and are administered under specific legislation. The DCS, which has previously been activated, produces its own report and audited financial statements.

It is important to note that neither scheme is pre-funded, both schemes are funded by participants (i.e. the relevant licenceholders), and in the case of the DCS also by Government, up to maximum levels set down in the relevant legislation. The Scheme Manager, which is the body responsible for managing the DCS, also has a power to borrow.

Broadly, the DCS compensates persons that have money in current and deposit accounts in the Isle of Man with 100% of their qualifying deposit subject to a maximum £50,000 of net deposits per individual depositor or £20,000 of net deposits for most other categories of depositor.

Because of the cap which the DCS legislation places on total contributions (paid by the Government and participating banks) to the DCS, and the fact that borrowing is discretionary and subject to availability, it is possible that there may be insufficient funds available to pay the full level of compensation to depositors at a particular time. This especially applies if a large bank fails and/or there is more than one failure within a short period of time.

Banks and financial advisers should take account of the DCS' limitations in any references they make to it. Depositors should also take into account the limitations of the DCS when deciding where to place their money. This is made clear in the consumer information

section of the Commission's website.

The DCS was previously activated (on 27 May 2009) in respect of the insolvency of KSFIOM and (on 16 January 1992) in respect of the failure of BCCI which had a branch in the Island. The DCS Regulations applying at these times differed in respect of the amount of compensation available to depositors.

The Commission, as Scheme Manager at the time of the KSFIOM and BCCI failures, has devoted considerable resources to ensure the effective operation of both schemes and publishes its own separate Annual Report and Accounts which refer to the events in greater detail.

In relation to KSFIOM, the Joint Liquidators are currently estimating a total dividend to all KSFIOM creditors of between 98.6p and 99.2p in the £, although this will take a few more years to complete. To date the dividends declared have reached 95.8p in the £ and a further dividend of at least 2p in the £ is expected to be made in 2014, which would take the total declared to date to at least 97.8p in the £.

In relation to BCCI, a final meeting of creditors was held on 17 May 2012, at which it was noted that the global liquidators of BCCI have resolved to pay a minimum final dividend of 3.5586% to ordinary admitted creditors which would give an aggregate dividend of just over 90%. The final dividend was paid in August 2012 and payments of surplus funds due to claimants of the DCS re BCCI were made. The Commission as Scheme Manager, has now made proposals to Treasury setting out what

steps should be put in place to enable the closure of the scheme that was created. Once these proposals have been fully considered details of the legislative changes that will need to be made will be published.

Compensation under the Investors' Compensation Scheme is payable as follows: 100% of the first £30,000, 90% of the next £20,000 with a maximum compensation of £48,000.

## Complaints about licenceholders

The Commission does not undertake dispute resolution or make awards in relation to complaints about licenceholders.

The Isle of Man has a Financial Services Ombudsman Scheme. The Ombudsman Scheme is a free, independent dispute resolution service for customers with unresolved complaints against some Isle of Man financial services firms such as banks, insurance companies and financial advisers. The Ombudsman Scheme does not cover complaints regarding corporate or trust services.

The role and powers of the Ombudsman Scheme are set down by law and the adjudicators are appointed by the Appointments Commission.

As an alternative, the Isle of Man Courts operate a small claims procedure which is available for claims up to £10,000.

If the Commission does receive a complaint about a licenceholder it will however review it in order to see whether any breaches of regulatory

requirements have occurred. Often the Commission finds that disputes tend to be of a commercial (rather than regulatory) nature, for example involving contractual issues.

## International relations

### *International co-operation*

The importance of co-operation agreements in relation to financial services continues to grow. In order to ensure that the local fund industry could continue to market Isle of Man alternative investment funds to professional investors in the EU and EEA, the Commission entered into 26 co-operation agreements with EU and EEA competent authorities over this period. The agreements bolster the Isle of Man's reputation as an excellent location from which to do business with the EU and the rest of the world.

In addition to specific agreements for particular topics, the Commission seeks to further extend its communication with home regulators. In many cases these relationships are underpinned by MOUs signed between the Commission and relevant authorities. While these are not formal legal agreements, they can assist mutual understanding by setting down how the various parties will interact and co-ordinate action. Over this period the Commission entered into a Statement of Co-operation with the China Banking Regulatory Commission and negotiated a further MOU with the China Securities Regulatory Commission.

The Commission is an ordinary member of IOSCO and a full signatory to the

IOSCO MMOU. An account is given in the 'Assistance with investigations and insider dealing' section of this Report of the assistance provided by the Commission in respect of requests made under the IOSCO MMOU.

The Island is a member of Group of International Finance Centre Supervisors and the Commission's Chief Executive is its Chairman.

A meeting of the Enlarged Contact Group of Collective Investment Fund Supervisors took place in Zurich in September 2013 during which a wide range of issues were discussed including:

- mutual co-operation arrangements between regulators
- complexity of funds and products and transparency of information
- risk management and on-site inspections
- management charges and quality of services - responsibilities of the governing body to ensure that these are reasonable
- implementation of the AIFMD
- retail versus non-retail schemes
- closed-ended investment companies and collective investment schemes.

### *International regulatory liaison*

Where a licenceholder is part of a cross-border group, the Commission's reports following its on-site visits are forwarded to that licenceholder's home regulator for their information and inclusion in the consolidated supervision of the group.

Over the period of this Report, the Commission sent 165 letters to other supervisors for regulatory purposes, and received 66. These included standard letters to home and host regulators in relation to high impact licenceholders, requests for information, the passing of information to inform other regulators (including the sharing of visit reports where there is a home supervisor) and replies to other regulators' requests for assistance.

The Commission participates in 'college' meetings and teleconferences arranged by home supervisors (primarily the PRA, the FCA and the Central Bank of Ireland). This enables the Commission to

better understand the financial position of the group and any supervisory issues being addressed by the parent supervisor, and provides an opportunity to discuss any local concerns it may have as host supervisor.

The Commission also writes to the home supervisors of licenceholders at least annually updating on any prudential concerns which are held by either party; it also meets face-to-face with home supervisors as necessary.

During the year, one overseas regulator came to the Island to undertake an on-site visit to part of a financial services group of which it is home regulator.

# Prevention of money laundering and countering the financing of terrorism, and enforcement action



The Commission's Enforcement Division is tasked with ensuring that the Commission's AML/CFT requirements are maintained in line with international expectations, and the Division is also empowered to deal with those who undertake regulated activities without the necessary licence and to pursue enforcement action with licenceholders as necessary. This has been an interesting and challenging period for Enforcement Division which has seen an expansion in terms of its responsibilities and staffing.





## **Prevention of money laundering and countering the financing of terrorism**

### **National Risk Assessment**

The international standard for AML/CFT requirements is the FATF 40 Recommendations. The revised FATF Recommendations and new Methodology are currently being reviewed with a view to amending the Money Laundering and Terrorist Financing Code 2013 so that it remains in line with international standards.

A consequence of the revised Recommendation 1 is that the Island must conduct an important formal assessment of the Island's AML/CFT risks - known as a National Risk Assessment - and should apply an approach based on that risk to ensure that measures to prevent or mitigate money laundering and terrorist financing are commensurate with the risks identified. The NRA will drive the Island's AML/CFT strategy and is expected to be a living document, regularly updated and which should form the basis of AML/CFT policy at the national level allowing a truly risk-based approach to be taken by Government and private sector to money laundering and terrorist financing.

As this is a new international requirement on which the Island will be evaluated in the next round of MONEYVAL evaluations, a high-level decision was made by the Isle of Man Government to commence the NRA process in 2013.

To this end, a NRA Strategic Group has been formed which is chaired by the Chief Secretary and met for the first time in September 2013. The Commission's Chief Executive, along with the Chief Constable, Acting Attorney General, Chief Financial Officer - Treasury, Chief Executive - IPA and Director of External Relations also sit on the Strategic Group. Staff of the Commission's AML/CFT Unit also take part in the NRA Working Group, which is chaired by the Director - Enforcement. The NRA Working Group will circulate risk assessment questionnaires to both public and private sectors in 2014.

The Commission's Chief Executive and Director - Enforcement attended a workshop on NRA in Liechtenstein in October 2013, and it is envisaged that, working together with colleagues from the other Crown Dependencies and the World Bank, a common approach to NRA will be developed. It is envisaged that the first NRA will be finalised in the first quarter of 2015.

The results of the NRA should provide useful information to financial institutions and DNFBPs to support the conduct of their own risk assessments.

## **MONEYVAL**

In December 2012 the Isle of Man was admitted into MONEYVAL which is the body that will undertake future assessments of the Island's AML/CFT regime. This means the Island is now able to participate in MONEYVAL evaluations and follow-up procedures.

In addition the Director - Enforcement underwent evaluator training in

November 2013 and is now a MONEYVAL-trained evaluator.

MONEYVAL is the European regional FATF-like body for Member States of the Council of Europe that are not members of FATF itself.

The Crown Dependencies of the Isle of Man, Guernsey and Jersey constitute one delegation to MONEYVAL and each jurisdiction may send one representative to the MONEYVAL plenary meetings which are held three times per year. This is a useful forum to attend as it allows the Island to keep up-to-date with AML/CFT developments in Europe, and also to be aware of other individual countries' progress and evaluations. During this period the Director - Enforcement, representing the Isle of Man attended three plenary meetings in Strasbourg together with a member of the AML/CFT Unit representing GIFCS.

In July 2013 the Island underwent a desk-based technical compliance assessment, co-ordinated by the AML/CFT Unit, against the specific requirements of the FATF Recommendations, covering how they have been implemented in the Island's legal and institutional framework and the powers and procedures of its competent authorities. The First 3rd Round Written Progress Report outlining the progress made by the Isle of Man to implement recommendations previously identified by the IMF, was presented and discussed at the MONEYVAL Plenary in September 2013 and published on MONEYVAL's website. The evaluation report confirmed the Island's continued improvement

in its compliance with the standards for countering money laundering and terrorist financing and concluded that the Isle of Man had made considerable progress in addressing issues identified in the IMF's assessment of the Island, including compliance with the FATF Recommendations on customer due diligence and identifying beneficial ownership.

The second part of the MONEYVAL review process will be an assessment of effectiveness which will involve a physical visit to the Island in 2016 to assess the adequacy of the implementation of the FATF Recommendations. This element involves 11 outcomes, and the extent to which a country achieves these outcomes will be assessed - in effect it considers the extent to which the legal and institutional framework is producing the expected results.

## Money laundering

During the period of this Report four convictions for money laundering were obtained by the Attorney General's Chambers under the Proceeds of Crime Act 2008 and further cases are known to be under review. The majority of convictions relate to localised cases of drug use and supplying, involving relatively low values. One conviction dating from 2011 was quashed on appeal to the Judicial Committee of the Privy Council.

The threat of money laundering and financial frauds changes according to current circumstances and international developments. During the period the

Commission was especially conscious of the following trends in fraudsters' methods:

*Cybercrime frauds* - Criminals have long been at the forefront of the development of new technology. The advent and global spread of personal computers and the increasing reach of the internet has opened opportunities for the criminal to reach victims, whilst remaining at 'arm's length'. Whether it be identity theft and the trawling of social network sites for personal data, or the more sophisticated service denial attacks on commercial entities, cybercrime continues to be an alarming growth area. The pace of development of new technology and platforms continues unchecked and the rapid uptake of it by the general public means that new opportunities for fraudulent activity are arising on a regular basis. The Enforcement Division has good access to information regarding developing frauds in this area and uses this knowledge to assist potential victims who have concerns.

*Green fraud* - Interest in eco-friendly projects continues to grow and 'green' issues have not escaped the notice of the criminal fraternity. In the past there have been some well documented frauds involving matters such as carbon trading. At present, an emerging trend, developing from land banking frauds in the recent past, involves the alleged purchase of land in remote places which it is claimed will be developed for green, eco-friendly profit. Fraudulent schemes have ranged from teak growing in Costa Rica to bio-fuel production in Indonesia.

### *Fraudulent investment opportunities* -

As noted over recent years the continuing general low rate of return on genuine investments makes it more challenging for potential victims of fraudulent approaches to assess their validity. The old maxim, that if something appears too good to be true then it probably is, becomes harder to apply when the difference can be mere percentage points. Notwithstanding that, contact from potential victims suggests that the level of awareness among the local population is generally high. Contact received over the past year has been focused more on making the Commission aware of potential fraudulent approaches and less on seeking to establish whether or not approaches are fraudulent. The number of cases where fraudulent emails or websites falsely claim an Isle of Man address has fallen dramatically over the past few years. This has resulted in the lowest number of Public Warnings being issued by the Commission since the early years of the millennium. This is likely to be a combination of increased public awareness of internet fraud, increased police activity worldwide and the effect of the Commission's Public Warning and disruption activity. It would be wrong, however, to become complacent. Such matters are cyclical, and we remain vigilant to the potential of false claims to an Isle of Man presence.

The implementation and monitoring of AML/CFT measures in the Island is not the sole responsibility of the Commission. The primary and secondary legislation is the responsibility

of the Department of Home Affairs. Other agencies are involved such as the law enforcement authorities, other regulators, and Government agencies.

The Chief Secretary chairs a cross-Government AML/CFT Strategic Group which meets regularly to consider the Island's commitment to the prevention of money laundering and the financing of terrorism and proliferation and also to review progress in meeting international AML/CFT standards. In this period four meetings of the Chief Secretary's Strategic Group were held. Decisions made by the Strategic Group and actions resulting are filtered to the Government's AML/CFT Technical Group. Members of the Enforcement Division also attend and chair these monthly meetings - ten of which have taken place over the period of this Report.

The Money Laundering and Terrorist Financing Code 2013 came into effect on 1 May 2013 which is, in effect, the merged Proceeds of Crime (Money Laundering) Code 2010 and the Prevention of Terrorism Code 2011. Following the coming into effect of the Code some minor drafting and typographical errors and potential ambiguities were identified. This necessitated a Money Laundering and Terrorist Financing (Amendment) Code 2013 which came into operation on 1 July 2013.

Industry co-ordination of AML/CFT matters takes place through the Joint Anti-money Laundering Advisory Group. JAMLAG is a key group



comprising industry representatives and most other AML/CFT stakeholders, and was established to advise and comment on proposed AML/CFT-related legislation and issues. The subjects covered at JAMLAG meetings included:

- modification and development of AML/CFT legislation so that it is consistent with the revised FATF Recommendations and new Methodology
- development of legislation to address the issue of DNFBPs
- progress against recommendations resulting from the Island's latest evaluation by MONEYVAL
- National Risk Assessment.

The Commission has issued an AML/CFT Handbook which is publicly available via its website. During the period three updates to that Handbook were issued.

In June 2013 the Enforcement Division ran an Anti-money Laundering and Financial Fraud conference for the benefit of 180 industry participants. Speakers included Mr John Baker from the MONEYVAL secretariat who spoke about MONEYVAL and the revised FATF Recommendations and new Methodology; Mr Elyot Godfrey from HMRC who spoke about HMRC's offshore tax disclosure facility, and Mrs Lindsey Birmingham from Cains Advocates who gave a talk entitled "Poyjiades and Baines: a case study in money laundering".

## Designated non-financial businesses and professions (DNFBPs)

As a result of the highlighting by the IMF of a deficiency during its last review - the lack of a suitable AML/CFT oversight regime for certain DNFBPs - the Council of Ministers approved the Commission's instructing on draft new primary legislation to rectify this. The aim of the draft legislation is to provide the Commission with the necessary powers to enable it to undertake AML/CFT oversight work in relation to DNFBPs.

Following liaison with the DHA and affected parties a draft Bill - the draft Designated Businesses (Registration and Oversight) Bill - was prepared and issued for consultation in April 2013.

The draft Bill does not seek to make persons affected by its provisions licenceholders of the Commission. The Commission's role in licensing and supervising financial services licenceholders is distinct and entirely separate from its future role under the draft Bill. The Commission's interest in designated businesses will be in monitoring and overseeing their adherence to the AML/CFT legislation which already applies to them. It is anticipated that the approach will be for affected persons to register for that purpose with the Commission, and for the Commission to oversee that person's adherence to the AML/CFT legislation by virtue of occasional on-site visits and the issuance of general guidance. It is envisaged that some of the compliance oversight will be

delegated to professional bodies, a number of which have expressed an interest in undertaking this work.

Following review of consultation responses and further constructive meetings and liaison with affected persons and their professional bodies, amendments were made to the draft Bill which was issued for further consultation in February 2014. Three briefings for those affected by this Bill have taken place.

To enable the Commission to commit the necessary resources to this new role, in addition to continuing with its

other AML/CFT activities, a separate AML/CFT Unit was established within the Enforcement Division which has grown to accommodate its increased responsibilities and now comprises four individuals. The Unit has been instrumental in liaising closely with accountancy and legal professional bodies and sectors on the Island to discuss how the registration and oversight in relation to certain DNFBPs will develop in practice when the Bill comes into force - which is now expected to be during the first quarter of 2015.



## AML/CFT Unit

As well as taking an active role in the construction of the draft Designated Businesses (Registration and Oversight) Bill, all DNFBP AML/CFT compliance oversight not delegated to professional bodies will be undertaken by members of the AML/CFT Unit.

The work of the AML/CFT Unit also involves working on the Island's AML/CFT policy to ensure that the Island's AML and Terrorist Financing legislation and the Commission's AML/CFT guidance is kept up-to-date, is consistent and complies with international standards.

In addition, members of the AML/CFT Unit are currently taking the lead on preparation of the Island's National Risk Assessment.

Members also represent the Island where necessary at local and international fora such as MONEYVAL and the AML/CFT Technical and Strategic Groups.

## Assistance with investigations and insider dealing

In order to be considered to have an internationally acceptable anti-money laundering and countering of the financing of terrorism regime, a jurisdiction must have effective co-operation and co-ordination of intelligence which can be shared with other regulators and law enforcement authorities globally.

The Island has in place important

provisions to enable it to co-operate in cross-border enquiries and investigations. Criminal matters are dealt with by the Attorney General's Chambers while the Commission is able to use its regulatory powers of inspection and investigation to obtain information on the Island on behalf of other signatories. Five requests were received during this period under the IOSCO MMOU from five different countries.

To assist other regulators, the Commission maintains a list of regulators and law enforcement agencies to which it can circulate public warnings, as well as publishing these warnings on its own and IOSCO's websites. On occasion the Commission becomes aware of instances where overseas persons falsely claim to have a presence on the Island in order to mislead the public. Where suspected instances come to light they are in the first instance investigated by the Enforcement Division in order to establish whether any criminal or regulatory proceedings are called for or possible. In many cases the Division is able to establish categorically that there is no genuine Isle of Man connection. In such cases the Division is limited in the action that it can take to stop the false claims however the Commission does have a power under the Financial Services Act 2008 to publish relevant information to protect the public. During the year a total of nine cases investigated resulted in the issue of public warnings on the Commission's website.

Although the Island does not have a

stock exchange, regrettably there may be occasions when alleged insider dealing transactions are routed through the Island. Under the Insider Dealing Act 1998 the Commission may appoint inspectors to investigate such cases. Such inspectors are typically appointed from within the Commission.

## Enforcement action

### *Progression of escalating regulatory action*

The Commission has a range of regulatory powers to enable it to secure change and necessary improvement in the way in which regulated activities are managed and conducted.

The Commission's regulatory powers can be considered on a spectrum varying in severity, which are illustrated in the table below. In the table (F) reflects a power that is applicable to firms, whereas (I) reflects a power applicable to individuals:

<b>Remedial</b>	Administrative Fixed Penalties (F)
	Directions (F)
	Licence Conditions (F)
<b>Disciplinary</b>	Skilled Persons' Report (F)
	Public Notice (F)
	Discretionary Civil Penalties (F)
	Warning Notice (I)
	Lack of Fitness and Propriety (I)
	Prohibition (I)
<b>Enforcement</b>	Manager Appointments (F)
	Licence Suspension (F)
	Prosecution (F)
	Licence Withdrawal (F)
	Company Officers Disqualification Act 2009 (I)

In many cases matters towards the lower end of the spectrum - the Remedial matters - are dealt with by the Supervision teams, for example action plans following on-site visits and the issuance of directions or licence conditions to ensure these are dealt with. However when it becomes necessary for action to escalate, where supervisory powers need to be exercised in a more punitive manner, such matters are dealt with by the Disciplinary Unit.

## Disciplinary Unit

In previous Reports we provided some details about the Remediation Unit within the Risk and Compliance Area of the Supervision Division. In January 2014 a new team, the Disciplinary Unit, was established and reports to the Director of the Enforcement Division, although it still works closely with the Supervision Division. The Disciplinary Unit will consider regulatory failings or matters of fitness and propriety identified by Supervision staff, which may warrant disciplinary action against individuals or licenceholders. This was previously the responsibility of the Remediation Unit. This function being transferred to the Director of Enforcement's area was considered preferable as the skill set required for dealing with serious regulatory failings is similar to that needed for company officer disqualification or court proceedings. Also, some issues may escalate further, requiring formal Enforcement action such as the withdrawal of a licence or court action, and therefore handling all such cases within a single area is

believed to be more effective.

The relevant powers that this Unit considers include section 11 warnings and prohibitions. A warning under section 11 of the Financial Services Act 2008 can have effect for a period of up to three years, and is not a public matter. It is not a declaration of lack of fitness and propriety; it is instead notice to the relevant person that in the Commission's opinion, it has grounds to believe that person's activities (which must be specified in the notice) are prejudicial to their fitness and propriety. There are similar powers under the Collective Investment Schemes Act 2008.

The Commission's prohibition power was introduced following the Financial Services (Miscellaneous Amendments) Act 2013 coming into force in July 2013. The Commission may impose a prohibition if it appears that any individual is not a fit and proper person to perform one or more functions in relation to a regulated activity. The prohibition can apply to any role in relation to a regulated activity, and not only the roles of controller, director or key person.

A prohibition may prevent an individual from performing any function, a specified function, or a function of a specified class and can be in relation to a particular permitted person, a specified class of permitted person, or all permitted persons.

Furthermore, a prohibition may relate to:

- any regulated activity
- a regulated activity specified in the prohibition, or



- a regulated activity of a specified class.

In all of the above situations, reasons for the Commission's actions have to be clearly explained and the actions are subject to appeal. Since its formation, the Disciplinary Unit has enhanced the Commission's decision-making framework and is amending the detailed protocols and procedures to fit the new framework whilst also taking forward a number of cases.

The Enforcement Division is responsible for handling the most serious cases, and has various avenues for possible action. For example, under the Financial Services Act 2008, the Commission is empowered to petition the High Court for the appointment of managers over the affairs of a licenceholder. This power was successfully exercised in respect of one licenceholder during the year. The grounds for the appointment were the temporary disruption in the effective management of the company and the managers were appointed in order to ensure that the interests of the company and its clients were adequately protected during the period of disruption.

## Company law measures

By virtue of its remit over TCSPs, and in particular the client companies, foundations and trusts which they administer, the Commission's role can go beyond the immediate regulated sector.

On occasion the Commission will become aware that company officers (the definition of which includes

Council Members of an Isle of Man foundation) are not carrying out their legal duties and responsibilities. In such cases, the Commission considers any shortfalls in the context of the powers available to it, and if those shortfalls are sufficiently serious, and where it would be in the public interest to do so, it may consider action. In some cases, where a regulated activity is involved, such action may comprise the use of regulatory powers mentioned previously. In other cases the Commission has powers under the Company Officers Disqualification Act 2009 to petition the Court under section 3(1)(a) for the disqualification of the person.

Under CODA, the Commission also has the power to investigate a person it suspects of:

- being unfit to act as officer of a company, or
- acting in breach of a disqualification order or disqualification undertaking.

This includes the power to inspect and take possession of books, accounts and documents and to require information.

Upon successful application persons may be disqualified by the Court. Persons may also offer to enter into a 'disqualification undertaking', which is an agreement between the relevant person and the Commission whereby that person acknowledges their previous unfit conduct and agrees not to, amongst other responsibilities, be an officer of a company for a number of years. In this way the time and cost of going through the courts can be avoided.

During this period enquiries were undertaken in respect of a number of instances of suspected unfitness. High Court proceedings are not yet completed regarding one case in relation to two company officers. Meanwhile 12 persons remain subject to previous disqualifications which are still current.

In addition, over this period the Commission was requested to investigate whether to take action in connection with any of the individuals named in the Select Committee of Tynwald's Report on the Manx Electricity Authority; but after taking

into account all relevant factors, including consideration of any cogent evidence of relevant failings occurring subsequent to the matters contained in the Select Committee Final Report, the Commission decided that the public interest would not be best served by commencing any disqualification proceedings. CODA relates to those who act in an inappropriate manner in their capacity as directors or officers of companies. Statutory Boards of Tynwald do not fall within the definition of a company for the purposes of that Act.

The Commission also has power





under the Island's company legislation to petition the High Court of Justice for the winding-up of companies in the public interest. The Enforcement Division usually has responsibility for the conduct of such cases. This power is an important tool for the Commission in dealing with public interest concerns in respect of both regulated and unregulated companies.

The Commission has not wound up any companies in the year.

Another company legislation power is to petition the High Court of Justice for the appointment of inspectors to

investigate and report into the affairs of companies in the public interest. Over this period the Commission has made one successful application for the appointment of company inspectors and their inspection is ongoing.

This power was also used in the previous period in respect of Louis Group Structured Fund Plc. Further details of the Commission's actions and the current situation regarding Louis Group Structured Fund PLC and the other companies can be found above, and are also available on the Commission's website [www.fsc.gov.im](http://www.fsc.gov.im)



# Policy Development

The Commission's regulatory and legislative framework must be maintained so as to remain in line with developing international standards and best practice. This is the role of the Commission's Policy and Legal Division. This activity assists in maintaining the Island's position as an internationally recognised, well-regulated jurisdiction and enhances the development of appropriate business.



**Roxanne Oldham**  
Director - Policy and Legal

## International matters

The Island is part of a global financial community and it must play its part in the improvement of global standards, and the avoidance thereby, of further financial crises and instability. It is also incumbent on the Commission, as part of its regulatory objectives, to secure an appropriate degree of protection for the customers of licenceholders. Much of the international response to the financial crisis has resulted in measures to further protect the interests of customers.

The Policy and Legal Division maintains a close watch on international matters and continues to focus on matters such as EU Directives and Regulations and changing standards issued by the international standard setting bodies such as the Bank for International Settlements and IOSCO.

Over this period, in July 2013, the AIFMD Regulation and the national AIFMD implementing legislation of the various EU and EEA Member States took effect. Despite the Island not being part of the EU its business is affected by these matters because the provisions include detailed requirements concerning the marketing of non-EU alternative investment funds by non-EU alternative investment fund managers to professional investors in the EU. The Division was responsible for ensuring that the necessary co-operation agreements between the Commission and EU and EEA Member States were put in place, a precursor to the continued ability of Isle of Man alternative investment funds to continue to be marketed to professional investors

in the EU.

The Division has also maintained a watching brief over the draft MIFIDII/ MIFIR provisions. These measures will also affect the business that can be conducted by third country persons with clients in the EU. At the time of writing, after a protracted period of negotiations, the European Parliament, European Council and European Commission have come to agreement and the Level 1 texts have been issued.

Staff of the Policy and Legal Division took part in an Isle of Man Government Working Group that dealt with the Island's response to both the US and UK FATCA measures. The measures are not regulatory, however they rely on the regulated sector for effective implementation.

The Policy and Legal Division is responsible for monitoring and co-ordinating the Commission's progress with the recommendations made by the IMF in its last FSAP report and the recommendations made as a result of an independent self-assessment that took place in late 2012. The Division ensures that the Board of the Commission receives a report at least every six months on progress with the agreed action plan. Many recommendations from the IMF review were addressed by changes contained within the Financial Services (Miscellaneous Amendments) Act 2013 that took effect in July 2013.

Another matter flowing from the previous IMF review is the expansion of the use by the Commission of civil penalties to address serious



regulatory failings. The Commission recognises the potential impact that an expanded civil penalties framework may have upon licenceholders and the resulting importance of it having suitably robust internal procedures for the administration of the framework in an effective, proportionate and fair manner. Nevertheless, the ability to issue civil penalties can encourage good compliance and the envisaged framework will provide an efficient and cost-effective method for dealing with serious matters of non-compliance that could put licenceholders' clients greatly at risk.

Following the Commission's initial consultation in early 2013, and the subsequent review and consideration of the valuable responses received, a further detailed consultation was issued in January 2014. This second consultation included the detailed policy along with some draft Regulations and a draft Guidance Note. At the time of writing, consultation responses are being considered.

## Legislation and guidance

The Commission's regulatory framework is enshrined in different layers of provisions. The main regulatory legislation is the primary legislation enacted by Tynwald, which encompasses the Financial Services Act 2008 and the Collective Investment Schemes Act 2008.

Below this layer is the secondary legislation, which is enacted by Tynwald under specific sections of the relevant Acts. The secondary legislation contains

the detailed requirements that underpin the Commission's remit and the requirements it places on licenceholders. The main secondary legislation made under the Financial Services Act 2008 - being the Financial Services Rule Book, the Regulated Activities Order and the Financial Services (Exemption) Regulations was consulted on and updated over this period. The updated legislation came into effect from 1 February 2014.

Other secondary legislation which has been made over this period includes:

- the Transfer of Business including Deposit-Taking Regulations 2013 - which impose requirements that must be satisfied before the High Court can determine applications to transfer business including deposit-taking business from a licenceholder to another person
- the Collective Investment Schemes (Authorised Schemes) (Trustee or Fiduciary Custodian) Order 2013 - which enables authorised collective investment schemes to have a trustee or fiduciary custodian that does not have a place of business in the Island if that trustee or fiduciary custodian meets other criteria.

Additionally, the Division has been active in preparing various sets of drafting instructions for the draft DNFBP Bill, reviewing and commenting upon the drafts received from Attorney General's Chambers and preparing and issuing the two public consultations on the draft Bill. The most recent consultation was issued in February 2014.

In the coming period it is likely that consultation will start with regard to improving the Island's Credit Unions legislation, following the Council of Ministers agreeing that the Commission should take this matter forward.

As well as legislation, another layer of the regulatory framework is the guidance issued by the Commission. Guidance has been issued on various topics, and is a useful way of illustrating best practice, assisting licenceholders to comply with legislation and to provide examples or illustrations, etc. Guidance is not law in the way that primary and secondary legislation is, but following guidance is persuasive - where a licenceholder follows guidance this would tend to indicate compliance with the legislative provisions, and vice versa.

## Innovation

Innovation within the financial services industry continues apace, with new products and services of a financial nature being developed, as well as new methods for the distribution and sale of existing products.

The Policy and Legal Division maintains a close watch on such matters to determine whether some of the innovative activity could fall within the existing parameters of the Regulated Activities Order, or whether it arguably ought to do so. This activity is very interesting and challenging, and over this period the products and services under consideration have included shadow banking, binary options, crowdfunding, and virtual currencies. The latter is particularly topical, with much debate

taking place internationally as to whether virtual currencies are 'money' and therefore a means of exchange, whether they are a commodity, or neither of these things.

Crowdfunding, on the other hand, appears to be a term used to describe a method of intermediation and flow of funds to the person seeking them. Of regulatory interest is that the method may be new, using new technology as a conduit, however the underlying activity is not. For example, much crowdfunding activity falls into one of three broad categories - lending, investment or gifting. Some of the underlying activity, therefore, is already subject to regulation of some type, especially investment crowdfunding or lending crowdfunding. It is imperative that those undertaking these activities take specific legal advice on whether their activities amount to regulated activity and require a licence.

## Other activities

The Division is responsible for reviewing and commenting upon the relevant consultations of other bodies. Over this period staff were heavily involved in reviewing and responding to the Treasury's consultation on a draft Companies Bill to consolidate and update the Companies Acts 1931-2004. The draft Companies Bill is particularly relevant to the Commission in part due to its links to TCSP licenceholders and the fact that many company law provisions are relied on for compliance with some IOSCO principles. The Commission remains of the opinion that a thorough review of the Island's

company legislation should be further considered so that the Island remains competitive in this area.

In relation to IOSCO principles, a focus for 2014 will be on the simplification and clarification of the Island's collective investment schemes regime, as well as a review of the same to ensure it continues to meet the IOSCO principles as viewed under the latest IOSCO Methodology. The assisted self-assessment of 2012 raised some matters that warrant further work, and a joint project across Supervision and Policy Divisions is taking this work forward, consulting and liaising with industry in the process.

Policy staff deal with applications to be placed on, or continue on, the Register of Recognised Auditors. Additionally, they are responsible for liaison with competent authorities in Guernsey and Jersey, the UK's Financial Reporting Council, its Audit Inspection Unit and the ICAEW in relation to the EU 8th Directive on Statutory Audits. This period was successful in that the Island's auditor oversight regime as declared equivalent by EU authorities following a joint application of the three Crown Dependencies' Auditor Oversight systems.

The Division also handles requests from overseas auditors seeking to audit Isle of Man companies where those auditors do not meet the requirements of the Companies Act 1982. Section 14E of that Act provides the Commission with specific power to authorise such

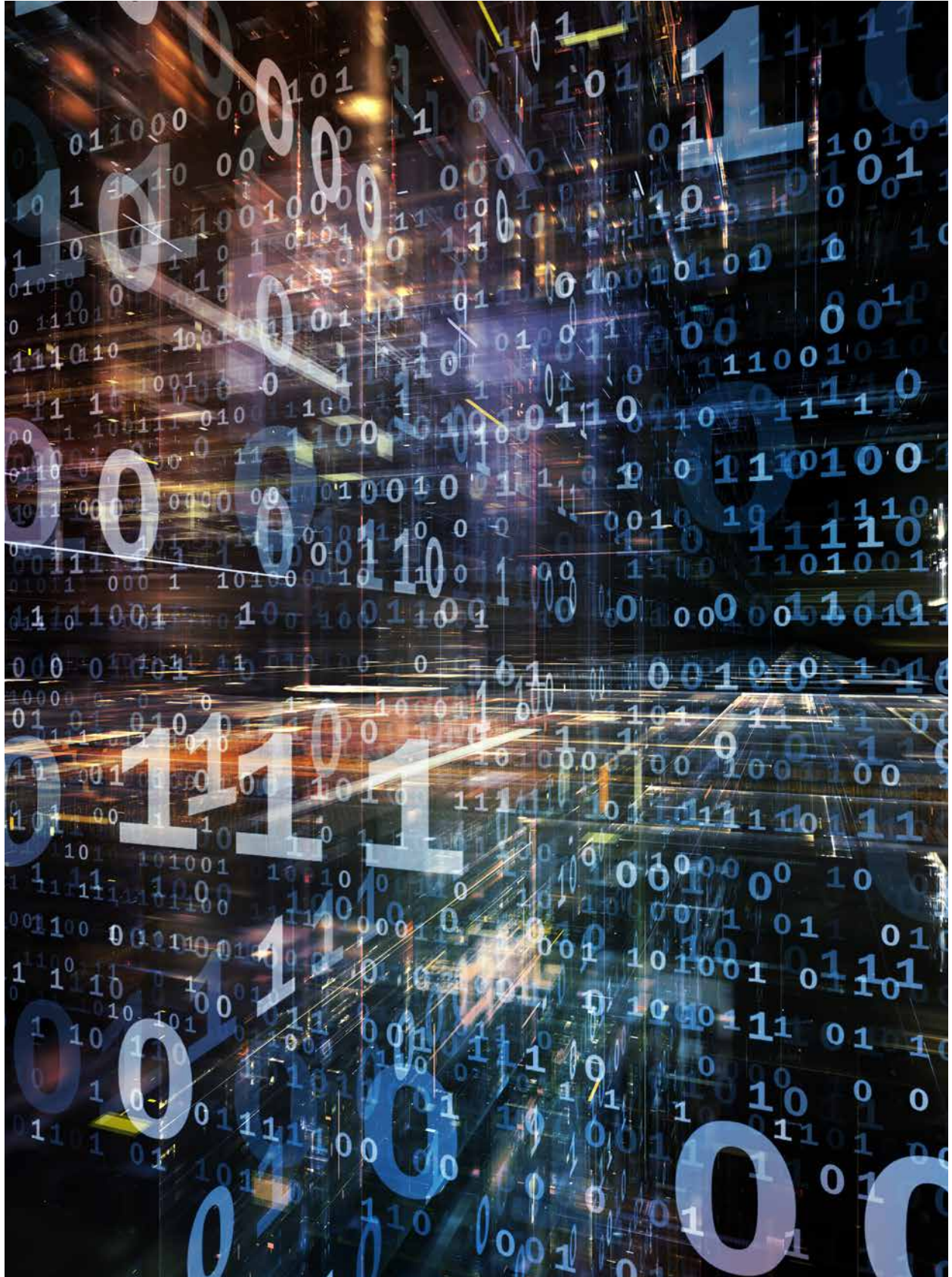
auditors, subject to their meeting certain criteria. Enhancements to this procedure, coupled with the possible introduction of a register and fees have been considered, and at the time of writing are subject to consultation.

In conjunction with the Attorney General's Chambers, the Department of Economic Development and a Working Group that includes Commission representatives and industry participants, work continues to prepare for the Island's banks to make applications to the European Payments Council for membership of SEPA. The Working Group is pleased with progress over this period and especially that the EPC has determined it does have responsibility to make such determinations, and that it has recently updated its third country entry criteria accordingly.

The Commission is an ordinary member of IOSCO and a full signatory to the IOSCO MMOU. The Director - Policy and Legal continued to take an active part in the IOSCO MMOU Screening Group meetings during the period of this report as well as being involved in one of the Vetting Teams reviewing the applications for signatory status of certain jurisdictions.

The Division handles data protection issues for the Commission, as well as the administration of any complaints made about the Commission.





# Operations

The Operations Division's activities fall under the principal headings of: finance, human resources and technology. The Division has responsibility for the regular administration and running of the Commission. It also provides a Secretariat function for the Board.



**Anne Dorling**  
Director - Operations

## Finance and administration

The Commission's statement of Income and Expenditure for the year ended 31 March 2014 and the Report of the Auditors are set out in Appendix F. The Commission is part of the centralised Government accounting system, and its income and expenditure is part of the Government's general revenue account and as such all fees are received by Government. Expenditure is drawn against a budget approved by Tynwald.

In line with Government the Commission is audited under the Audit Act 2006 which sets out the requirements for accounting and reporting under the Act.

Licence fee income increased during 2013/14 as a result of the biennial review and subsequent increase in fees. The overspend in professional fees relates to one or two specific enforcement cases; the costs have been met from savings from within the Commission's overall budget.

The Commission manages its budget



closely to ensure that it receives value for money, and, where possible, reductions in expenditure are made. This has been of particular importance over the last few years where the Commission has seen no increase in its budget.

## Human resources

The Commission has a full time staff establishment of 50.5. A number of staff gained industry experience before joining the Commission, with some of our longer-serving members of staff having joined the Commission and progressed their careers within it. This year Michael Weldon - Director - Supervision reached the milestone of 30 years of service, having joined the Commission in 1984. The Commission very much appreciates his loyal service over this period.

Staff turnover was 4% in the year to March 2014.

The Commission has redeployed a number of staff internally in order to ensure that resources are targeted in those areas that meet the Commission's business priorities and to reflect levels of risk.

Within the Commission's approved headcount a new position within the anti-money laundering team was created to support the implementation of the Designated Businesses (Registration and Oversight) Bill 2014. This post was funded through savings made in the Commission's budget.

Average sickness absence per employee fell to 2.4 days - at a total average cost per annum of £27,731.

## Investors In People (IIP)

The Commission's Business Improvement Group continued its work to:

- review the Commission against the IIP framework
- identify areas where organisational improvements could be made within the Commission in relation to maintaining or enhancing its position against the IIP framework and make recommendations to the Chief Executive's Committee in relation to these
- communicate with all staff and obtain feedback on initiatives being undertaken by the Group, encouraging forward thinking to enhance the Commission as a vibrant place to work
- be ambassadors for improving and enhancing the Commission's performance and productivity
- champion IIP by sharing and promoting good business and people practice both internally and externally.

A number of initiatives were undertaken during the year including progressing development points arising from the Commission's staff satisfaction survey, undertaking a communication survey and implementing changes arising from this and progressing work within the programme of continuous review.

The Personnel Committee of the Executive met on three occasions during the period of the Annual Report. Key items discussed were:

- participation in the National Learning at Work Day
- drugs and alcohol in the work place
- talent management
- HR statistics
- team building
- The Commission's learning and development policy
- pay progression
- performance reviews
- use of social media.

The Commission participated in the Government's Employment Skills event in November 2013.

The Commission hosted two work placement students from the Island's secondary schools. This provided a good opportunity for them to gain some valuable work experience. A member of the Commission's staff has been seconded to a major Island accountancy firm for a period of three months to gain industry experience.

## Learning and development

The internal target of 40 hours training per employee per annum is included in the Commission's learning and development strategy which was reviewed during the year. The average actual training spend per employee in 2013/14 was £618.

The Commission has an extensive programme of internal training sessions. These are given by staff and have

included subjects such as:

- changes to licence fees
- anti-money laundering
- Financial Services (Miscellaneous Amendments) Act 2013
- Data Protection
- MLRO responsibilities and reporting
- the Commission's information management security policy
- international developments on shadow banking.

The Commission is currently supporting six staff studying towards the following qualifications:

- ACCA
- CAT
- Investment Compliance Diploma
- Compliance Diploma
- STEP Diploma

Staff have also attended a number of management and technical development programmes. These included attendance at the FCA's International Regulators programme and other programmes whose subjects included directors' duties, the role of the company secretary, formal interview techniques and professional indemnity insurance.

To ensure that the Commission's staff has full knowledge of the Island's anti-money laundering requirements, Supervision Division staff are required to undertake an online e-test to review their

level of knowledge and identify specific training gaps.

## Information technology

Initiatives in the information technology area continue to have an overarching focus of maximising efficiency in the use of the Commission resources.

Work on extending the Commission's existing online system to collective investment schemes has been completed and industry implementation is being planned during the coming months.

The Commission's systems are located within Government's Information Systems Division. During this year the Commission established an independent SharePoint platform which has enabled it to implement specific customisation and a records management facility. Implementation of a system to manage physical files and replacement of the existing general intelligence system, which is an unsupported legacy system,

is being planned, together with the roll-out of SharePoint to the Supervision and Authorisations Divisions.

The Commission's IT Committee met on three occasions during the period and considered papers on:

- SharePoint upgrade, changes to platform and customisation
- records management
- mobile working
- funds database
- national risk assessment
- implementation of the DNFBP Bill
- ongoing IT support.

The Commission's business continuity plan and risk register is reviewed on a quarterly basis. Testing at the Commission's off-site business continuity location takes place biannually.

The IT team within the Operations Division handled 318 internal user calls

# Financial Supervision Commission and its Functions

The Financial Services Act 2008 sets out the Commission's regulatory objectives which are as follows:

- securing an appropriate degree of protection for the customers of persons carrying on a regulated activity
- the reduction of financial crime, and
- supporting the Island's economy and its development as an international financial centre.

These regulatory objectives are supported by the following which the Commission must have regard to when discharging its functions:

- the need for the regulatory, supervisory and registration regimes to be effective, responsive to commercial developments and proportionate to the benefits which are expected to result from the imposition of any regulatory burden
- the need to use its resources in the most efficient and economic way
- the desirability of implementing and applying recognised international standards
- the desirability of co-operating with governments, regulators and others outside the Island
- the need to safeguard the reputation of the Island
- the responsibilities of those who manage the affairs of permitted persons
- the international character of financial services and markets and the desirability of maintaining the competitive position of the Island
- the desirability of facilitating the development of the financial services industry
- the impact of its decisions on the stability of the financial system of the Island.

The Commission's functions are set out in the Financial Services Act 2008 as follows:

- the regulation and supervision of persons undertaking regulated activities
- the maintenance and development of the regulatory regime for regulated activities
- the oversight of directors and persons responsible for the management, administration or affairs of commercial entities
- participation in consultative bodies, working groups and other arrangements
- the functions conferred on it under the Financial Services Act 2008
- the regulation and supervision of collective investment schemes within the meaning of the Collective Investment Schemes Act 2008
- the functions conferred on it under:
  - the Building Societies Act 1986
  - the Collective Investment Schemes Act 2008
  - the Industrial and Building Societies Act 1892
  - the Companies Acts 1931-2006
  - the Company Officers (Disqualification) Act 2009
  - the Companies (Transfer of Domicile) Act 1998
  - the Credit Unions Act 1993
  - the Income Tax Act 1970
  - the Incorporated Cell Companies Act 2010
  - the Insurance Act 1986
  - the Insider Dealing Act 1998
  - the International Business Act 1994
  - the Limited Liability Companies Act 1996
  - the Online Gambling Regulation Act 2001
  - the Terrorism (Finance) Act 2009
- the functions conferred on it under any other statutory provision.



# Membership of the Financial Supervision Commission

## **Geoff Karran MBE (Chairman)**

Appointed in July 2007 and became Chairman on 1 April 2012. Admitted to the Manx Bar in 1969 and during his time as an Advocate became Senior Partner in Dickinson Cruickshank and served for three years as President of the IOM Law Society. Retired from practising Law in February 2007. Appointed Deputy Police Complaints Commissioner in March 2008 and Police Complaints Commissioner in March 2009. Awarded the MBE in the New Year's Honours List 2009 and made a Freeman of the Borough of Douglas in 2012.

## **Bryan Stott (Deputy Chairman)**

Appointed in June 2001. Initially his career focussed mainly on the Island's property business. In 1973 he was appointed to the Board of the Isle of Man Bank Limited and became Chairman in 1980. Has 28 years' banking experience with the Isle of Man Bank and subsequently NatWest Offshore Limited. Retired as Chairman of NatWest Offshore Limited in 2000. Mr Stott has extensive experience in the investment and insurance field. He was also involved in the development of the space and satellite business for the Island and is now focussing on running the family office.

## **John Aspden (Chief Executive)**

Appointed as Chief Executive of the Commission in August 1998. Commenced his career for 15 years with the Bank of England including three years on secondment to the Council for the Securities Industry. Then became adviser to the Commissioner of Banking in Hong Kong. Subsequently moved to become Deputy General Manager at International Bank of Asia Limited, and then Managing Director of Matheson InvestNet Limited, both also in Hong Kong. John was appointed Chairman of the Group of International Finance Centre Supervisors in November 2011.

## **Roger Butler**

Appointed April 2012. Since 1998 Roger Butler has been chairman and non-executive director of, and consultant to, several companies in varied industries. Between 1996 and 1998, he was Chief Executive of Newton Investment Management, a major UK fund management company, until its sale to Mellon Bank. Previously, he was a Senior Advisor to Morgan Stanley, where he was involved in advising both the firm and its investment banking clients on corporate structuring and taxation matters. Prior to this, Roger was with Arthur Young (now Ernst & Young) where he was latterly Regional Managing Partner in London and Chairman of the global tax practice,

having previously been UK National Director of Taxation.

### **Tim Cullen MBE**

Appointed June 2001. Spent 21 years with the World Bank, where he served inter alia as Chief Spokesman of the Bank and, latterly, as Senior Advisor for External and United Nations Affairs. He is Executive Director of the Small Countries Financial Management Centre and an Associate Fellow of the Saïd Business School at the University of Oxford, where he directs the Oxford Programme on Negotiation. He is a trustee of WaterLinks, a Manila-based charity that facilitates better provision of water and sanitation by Asian water utility operators. He also heads a small international consulting firm that focuses on issues of governance, integrity and negotiation and teaches negotiation at Oxford University and throughout the world.

### **Sir David Lewis**

Appointed April 2012. Practised as a corporate and financial services solicitor in London and the Far East with the international law firm Norton Rose since 1969. Served as Senior Partner and Chairman, now a consultant. President of the City of London Law Society 2009-10. Served as Sheriff of London and then Lord Mayor of London 2007-8. Knighted in 2009.

### **Alan Smith**

Appointed July 2007. Initial career with Lloyds Bank Trust Division and then spent seven years as Manager

of Bank of Bermuda's Cayman operations. Moved to the Isle of Man in 1987 and was appointed Managing Director of Bank of Bermuda in 1994. Appointed to the Global Board of the Bank's Fund Services Division in 2001 as Global Head of Marketing and Strategy and subsequently of HSBC's Alternative Fund Services Division up to his retirement in 2005. He has over 40 years' experience in Trust Administration, Corporate Services, Banking, Custody and Fund Administration.

### **Paul Wright**

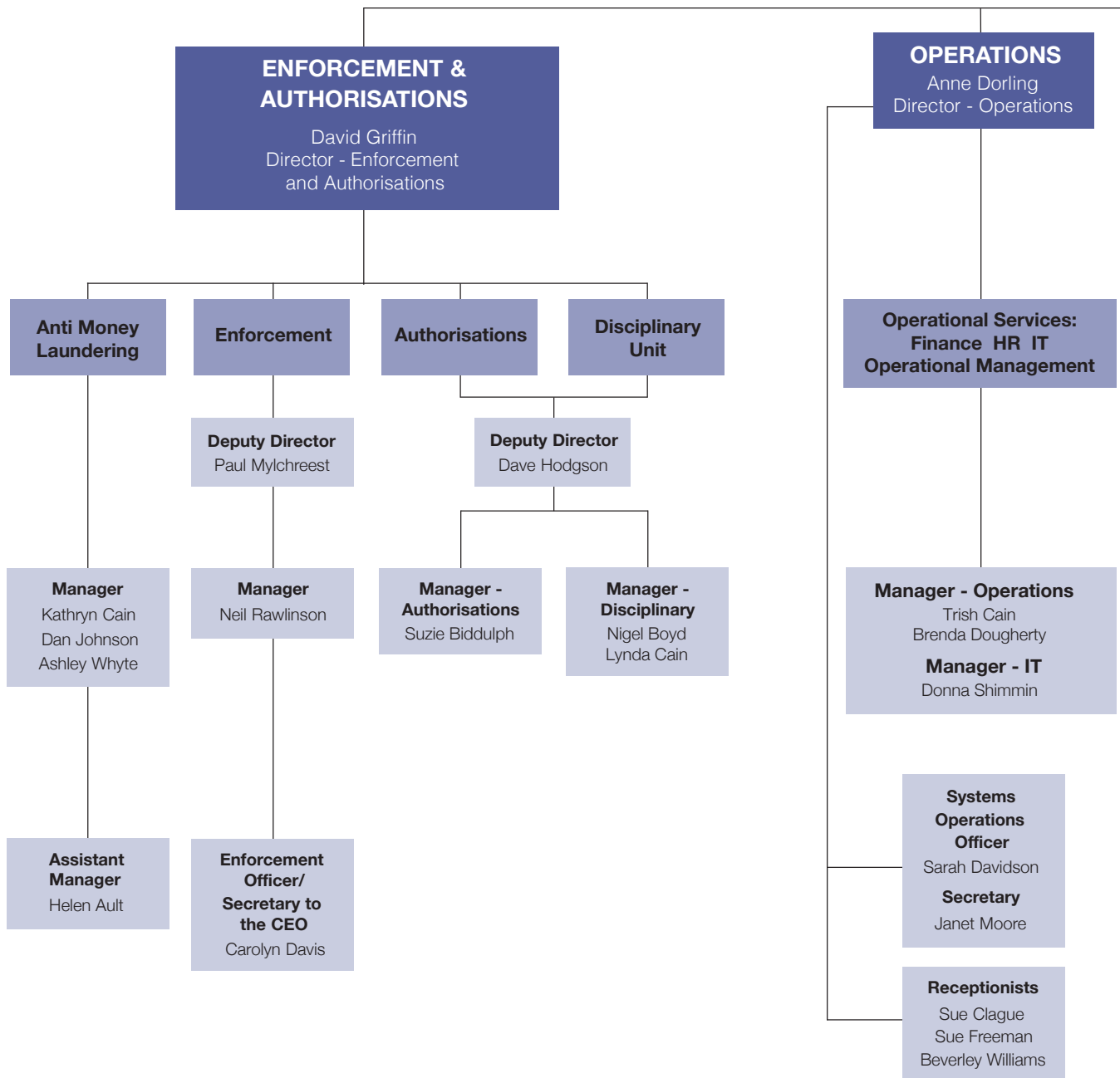
Appointed in May 2012. Spent much of his career with the Bank of England in a variety of economics, international and supervisory roles and was UK Alternate Director at the IMF 1990 to 1992. Joined the UK FSA at its formation and was responsible for the major overseas financial institutions in the UK and subsequently for EU and global policy. From 2009 to 2012 he was Senior Director at the Institute of International Finance in Washington DC. Paul is the CSFI/Swiss Re Fellow in Global Insurance Issues, a Visiting Fellow at Lancaster University Management School and a member of the Advisory Board of the Toronto Centre for Financial Leadership.

# Organisation Chart

## Board of Commissioners

Geoff Karran MBE (Chairman) - John Aspden - Roger Butler - Tim Cullen MBE  
 Sir David Lewis - Bryan Stott - Alan Smith - Paul Wright

## Chief Executive



**Secretary to the Board**  
Anne Dorling

John Aspden

**POLICY & LEGAL**  
Roxanne Oldham  
Director - Policy & Legal

**SUPERVISION**  
Michael Weldon  
Director - Supervision

**Deputy Director**  
Shirley Corlett

**Deputy Director**  
Paul de Weerd

**Deputy Director**  
Andrew Kermode

**Deputy Director**  
Claire Whitelegg  
Hazel Gawne

**Deputy Director**  
Hazel Gawne

**Policy Adviser**  
Susan Woolard

**Manager**  
Pat Brogan  
Jean Dick  
Sue Ferrario  
Mark Long  
Kieran Tomlinson

**Manager**  
David Clucas  
Elaine McCormack

**Manager**  
John Corlett  
Bobby Keig  
Victoria Liddle  
Julie Thomas

**Manager (Analyst)**  
Nicola Quinn

**Assistant Policy Adviser**  
Andrew Kniveton

**Supervision Officer**  
Samantha Chappell  
Joyce Jackson  
Laura Muscutt

**Assistant Manager**  
Ruth Baxendale

**Assistant Manager**  
Emma Cuddy  
Nicola Igoea  
Nick Platten

**Compliance Officer**  
Graham Connor

**Financial and Information Officer**  
Carolyn Williams

**Supervision Officer**  
Elaine Craine

**Fiduciary Services**

**Banking and Money Transmission Services**

**Funds and Investment Services**

**Risk and Compliance**

# How the Commission operates

The purpose of this Appendix is to describe how the Commission operates through a structured approach to its operations.

## Statutory Board

The Commission is an independent Statutory Board established under the Financial Supervision Commission Order 1983. As a Statutory Board the Commission operates under the Statutory Boards Act 1987, as amended.

## The Commission's Regulatory Objectives are:

- securing an appropriate degree of protection for the customers of persons carrying on a regulated activity
- the reduction of financial crime; and
- supporting the Island's economy and its development as an international financial centre.

The Commission's regulatory and supervisory role extends to the banking, investment, funds and fiduciary sectors.

## Members of the Commission

Appointments to the Board of Commissioners are made by Treasury and are subject to the approval of Tynwald.

Commissioners are appointed for a five year term. Government issues a

public invitation for persons to apply to be appointed as Members of Statutory Boards including the Commission.

The remuneration paid to Members of Statutory Boards is set down by Order.

The Board of Commissioners currently comprises a Chairman, a Deputy Chairman, the Chief Executive and a further five Non-Executive Commissioners. The quorum of the Board is a minimum of three persons. Further background details of Members of the Board as at 31 March 2014 are set out in Appendix B.

The Board has established Sub-Committees on Remuneration, Risk and Internal Control, and Complaints.

## Conflicts of interest

The Board of Commissioners benefits from having members who have broad, up-to-date commercial and compliance experience. Inevitably this means that from time-to-time conflicts of interest may arise in dealing with particular issues. A Code of Conduct has been drawn up to cover these situations. The Code provides for the prior disclosure of interests and sets down how they should be handled. Commissioners are required to absent themselves from decisions where they may be conflicted.



Staff also have to disclose their conflicts of interests. The code is published on the Commission's website together with a list of current directorships.

### Meetings of the Board

Routine meetings of the Board are held monthly, generally on the last Thursday of a calendar month. In addition a quorum of the Board meets monthly as necessary to hear licence applications. The Board additionally meets on an ad hoc basis as required.

During the period the Board met for:

12 routine monthly meetings

7 licensing meetings (quorum)

A number of other ad hoc meetings including with industry and other regulators.

Attendance at board meetings is set out below:

G Karran	10
B Stott	10
J Aspden	12
R Butler	12
T Cullen	9
D Lewis	11
A Smith	12
P Wright	11

### Delegated authorities

The Board has delegated certain powers to the Chief Executive. These include:

- changes in licence conditions attached to a licence
- extensions to licences to include new schemes etc.
- surrender of lapsed licences
- restructure of organisations/sale or

merger of licenceholders

- approving recognition of schemes under Section 13 of the Financial Supervision Act.

The Chief Executive in turn delegates certain matters within the Executive.

### The Executive

The Executive Management Team is structured as follows:

The Chief Executive, also a Commissioner

Directors

Deputy Directors

Managers

There are four Divisions within the Commission comprising Authorisations, Enforcement, Operations, Policy and Legal, and Supervision.

An organisation chart is set out in Appendix C.

### Accountability and scrutiny

A Memorandum of Understanding between the Commission and Treasury sets out the arrangements which have been established to ensure that the Commission is accountable to Treasury for its actions and clarifies the circumstances in which sensitive information might flow. The division of responsibilities is based on four guiding principles:

- Clear accountability: each authority must be accountable for its actions, so each must have unambiguous and well-defined responsibilities.
- Transparency: Tynwald, the financial services industry and the public must know who is responsible for what.

- Avoidance of duplication: each authority must have a clearly defined role, to avoid second guessing, inefficiency and the unnecessary duplication of effort. This will help ensure proper accountability.
- Regular information exchange: this helps each authority to discharge its responsibilities as efficiently and effectively as possible.

The MOU is available from the Commission's website.

The Commission is subject to scrutiny in the following areas:

- Tynwald: appointment of Commissioners, Corporate Plan, new legislation
- Government and Treasury: strategic objectives, legislative policy and proposals, budgeting and funding, establishment headcount
- Industry: consultation on regulatory and supervisory proposals
- Home regulators of licensed institutions.

In addition the Commission's regulatory and supervisory approach is subject to ongoing review by standard-setting organisations including the International Monetary Fund, and Moneyval.

### **Appeals against decisions of the Commission**

The key decisions of the Commission, including in relation to licensing, are subject to review by a committee established by the Council of Ministers. Tynwald has approved the Financial Services Review Regulations 2001 governing this committee and a panel

of persons has been nominated by the Council of Ministers from which it may select individuals to hear a particular case.

### **Finance**

The Commission operates within a budget agreed with Treasury, and within a headcount restriction set down centrally within Government. The Commission's revenue and expenditure is audited annually by the Government's external auditors, and the Commission is subject to review by the Government's internal audit department. Further details of the Commission's financial position are set out in Appendix F.

# Industry Statistics

## Licenceholders

### Number of licences

As at 31 March 2014, a total of 253 institutions held a licence issued by the Financial Supervision Commission under section 7 of the Financial Services Act 2008. The Classes of regulated activity which these institutions were permitted to conduct were as follows:

Deposit Taking (Class 1) (excluding Kaupthing Singer & Friedlander (Isle of Man) Limited, in liquidation)	27
Investment Business (Class 2)	54
Services to Collective Investment Schemes (Class 3)	58
Corporate Services (Class 4)	172
Trust Services (Class 5)	126
Money Transmission Services (Class 8)	6

Some licenceholders are permitted to conduct more than one Class of regulated activity; hence the total of the above (443) exceeds the number of licenceholders.

## The Banking industry

### Profit and loss data - deposit takers

The data below is taken from the year-end (unaudited) prudential returns for all year-ends up to and including 31 March 2014 (current year) and 31 March 2013 (prior year). The data includes figures relating to overseas branches of Isle of Man incorporated banks.

	<b>Current Year</b> (year-ends between 1 April 2013 and 31 March 2014)		<b>Prior Year</b> (year-ends between 1 April 2012 and 31 March 2013)	
	<b>£'m</b>	<b>£'m</b>	<b>£'m</b>	<b>£'m</b>
<b>Income</b>				
Net interest income	433		393	
Other banking income (including FX income, fees, commissions and charges)	113		124	
<b>Total banking income</b>		<b>546</b>		<b>517</b>
<b>Total non-banking income</b>		<b>49</b>		<b>50</b>
<b>Total income</b>		<b>595</b>		<b>567</b>
<b>Expenses</b>				
Total operating expenses	261		242	
Total other expenses	4		2	
<b>Total expenses</b>		<b>(265)</b>		<b>(244)</b>
<b>Profit before tax and impairment (bad debts)</b>		<b>330</b>		<b>323</b>
Impairment (bad debt) charge		(31)		(52)
<b>Profit before tax</b>		<b>299</b>		<b>271</b>

## Assets and liabilities of licensed banks

Assets	As at 31 March		Liabilities	As at 31 March	
	2014 £'bn	2013 £'bn		2014 £'bn	2013 £'bn
Money market assets, due from banks and building societies	45.8	53.9	Deposits due to banks and building societies**	8.7	12.8
Loans, advances and assets leased*	8.6	9.3	Deposits due to customers	43.7	47.8
Investments	0.1	0.3	Other deposits (held as security and interest payable) including deposits due to public sector bodies	0.3	0.3
Other assets	0.6	0.7	Other liabilities	0.4	0.6
			Capital and reserves	2.0	2.7
<b>Total assets</b>	<b>55.1</b>	<b>64.2</b>	<b>Total liabilities</b>	<b>55.1</b>	<b>64.2</b>

\* At 31 March 2014, 68.0% of loans, advances and assets leased were classified as being secured on residential property (31 March 2013: 64.4%). The above figures relating to loans and advances are net of impairment charges.

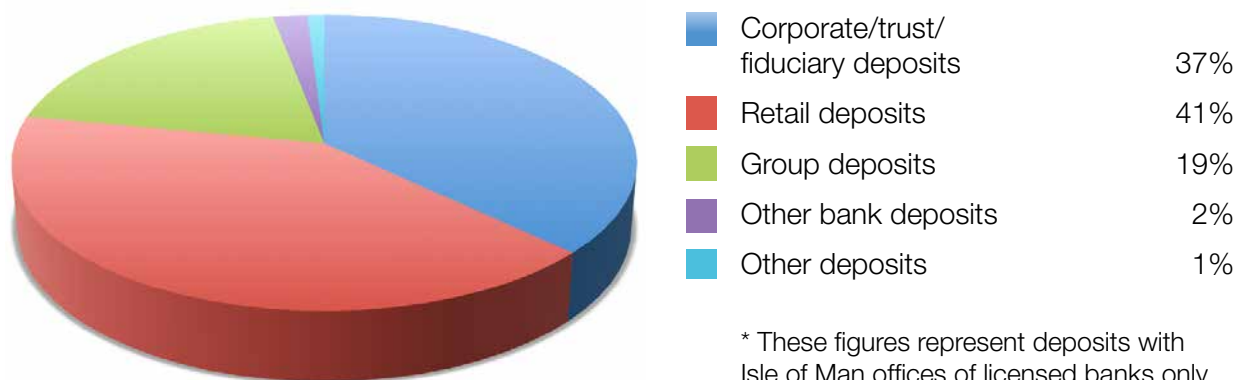
\*\* Includes deposits/loans received from other Isle of Man banks of £1.33bn (2013: £1.08bn).



## Geographical source of non-bank deposits

Country	31 March 2014	31 March 2013	31 March 2012
Isle of Man	28%	29%	29%
United Kingdom	36%	36%	35%
European Union (excluding UK)	6%	6%	7%
Europe (non-EU)	7%	7%	7%
Middle and Far East	6%	5%	5%
North America	4%	5%	5%
Other	13%	12%	12%

## Sector analysis of deposits\* including inter-Isle of Man banks as at 31 March 2014



### Ultimate country of origin of banking and building society groups\* operating in the Isle of Man

The ultimate country of origin is that used for definitions of reporting information to the Bank of International Settlements and relates to the country of incorporation of the ultimate parent / controlling party.

As at March 2014			
	Total	Subsidiaries	Branches
United Kingdom	14	6	8
Ireland	2	2	0
Spain	1	0	1
South Africa	3	2	1
Switzerland	2	2	0
France	1	0	1
Belgium	1	1	0
Cayman Islands	1	1	0
USA	1	0	1
<b>Sub total</b>	<b>26</b>	<b>14</b>	<b>12</b>
Isle of Man	1		
	<b>27</b>		

\* excluding Kaupthing Singer & Friedlander (Isle of Man) Limited, in liquidation

### Distribution of locally incorporated banks by risk asset ratio

The capital adequacy of Isle of Man incorporated banks is measured on a risk-weighted basis in accordance with Basel II international standards. The higher the ratio, the greater is the level of capital adequacy relative to risk rated assets. The statutory minimum risk asset ratio is 8% and the Commission can agree a higher minimum ratio on an individual bank basis. All Isle of Man incorporated banks are required to notify the Commission if their actual risk asset ratio falls, or is expected to fall, within at least 1% of their minimum ratio. All banks have a notification level of 10% or above.

At the end of March 2014 all Isle of Man incorporated banks held more than the minimum risk asset ratio.

The actual risk asset ratios are in the following ranges:

	Number of locally incorporated banks		Number of locally incorporated banks
<b>Minimum prescribed risk asset ratio:</b>		<b>Actual risk asset ratio:</b>	
Less than 10%	5	Less than 10%	0
From 10% to less than 15%	9	From 10% to less than 15%	4
From 15% to less than 20%	1	From 15% to less than 20%	5
20% and over	0	20% and over	6
<b>Total</b>	<b>15</b>	<b>Total</b>	<b>15</b>

## Collective Investment Schemes and services to schemes

### Types of scheme and asset values

Category of collective investment scheme	Number of schemes	Net asset value of funds under management/administration US\$m	Gross asset value of funds under management/administration US\$m
Authorised Schemes	7	891	891
Full International Schemes	6	1,791	1,791
Regulated Funds	3	83	84
Professional Investor Funds	2	3	3
Specialist Funds	16	646	658
Qualifying Funds	16	525	591
Experienced Investor Funds			
• Qualifying EIF	8	715	718
• Legacy EIF	12	692	1,267
• Closed EIF	12	192	210
Exempt Schemes	171	6,137	7,450
Overseas Funds	57	4,137	4,445
Closed-Ended Investment Companies*	41	4,837	6,044
Inward Outsourcing	14	1,194	1,205
<b>Total all schemes: 31/03/14</b>	<b>365</b>	<b>21,843</b>	<b>25,357</b>
<b>Total all schemes: 31/03/13</b>	<b>387</b>	<b>21,680</b>	<b>26,939</b>
<b>% change: 2013-2014</b>	<b>-5.4</b>	<b>0.8</b>	<b>-5.9</b>

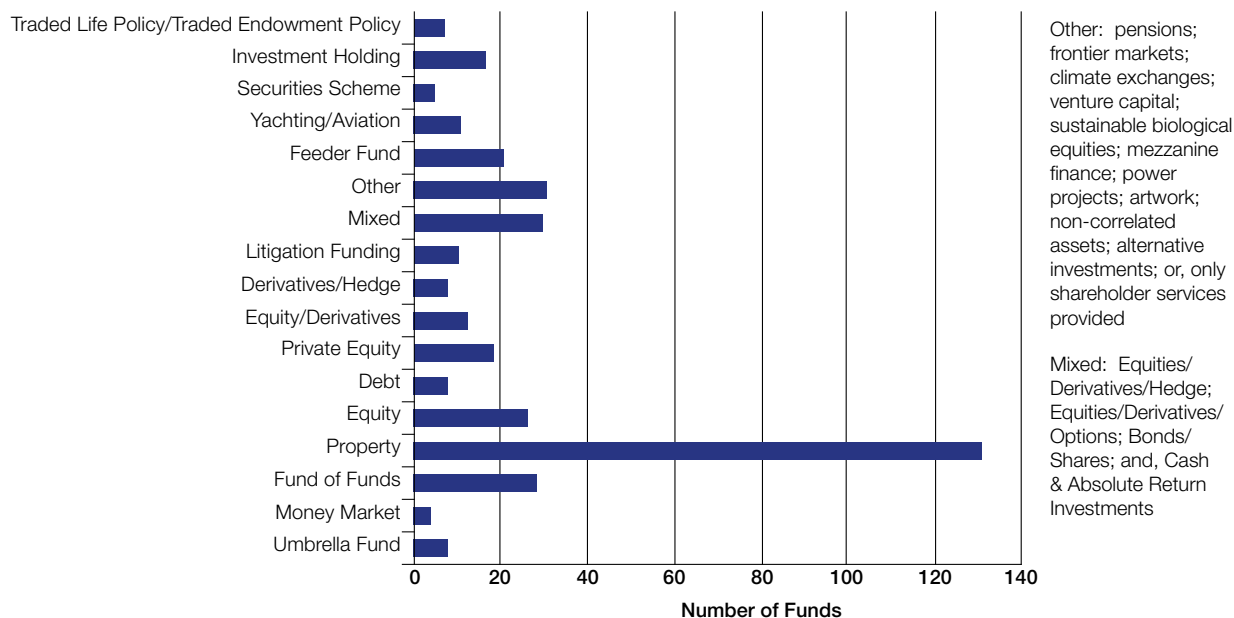
As at 31 March 2014 the Commission also had 24 Recognised Schemes from a designated territory under Schedule 4 paragraph 1 to the Collective Investment Schemes Act 2008 and two Individually Recognised Schemes under Schedule 4 paragraph 2 to that Act.

\* Statistics are only collected in relation to services provided to Closed-Ended Investment Companies that are listed vehicles or with a minimum NAV of USD\$50 million

## Types of Isle of Man schemes (percentage breakdown by NAV)

	As at 31 March 2014
Authorised Schemes	4.08%
Full International Schemes	8.20%
Regulated Funds	0.38%
Professional Investor Funds	0.02%
Specialist Funds	2.96%
Qualifying Funds	2.40%
Qualifying EIF	3.27%
Legacy EIF	3.17%
Closed EIF	0.88%
Exempt Schemes	28.10%
Overseas	18.94%
Closed-Ended Investment Companies	22.14%
Inward Outsourcing Arrangements	5.47%

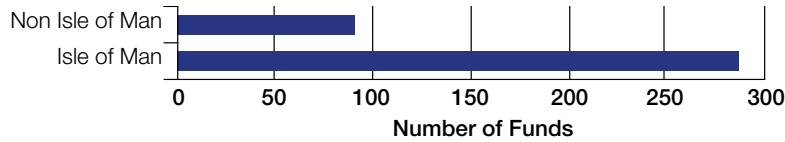
## Asset classes of schemes





## Geographical origin of schemes

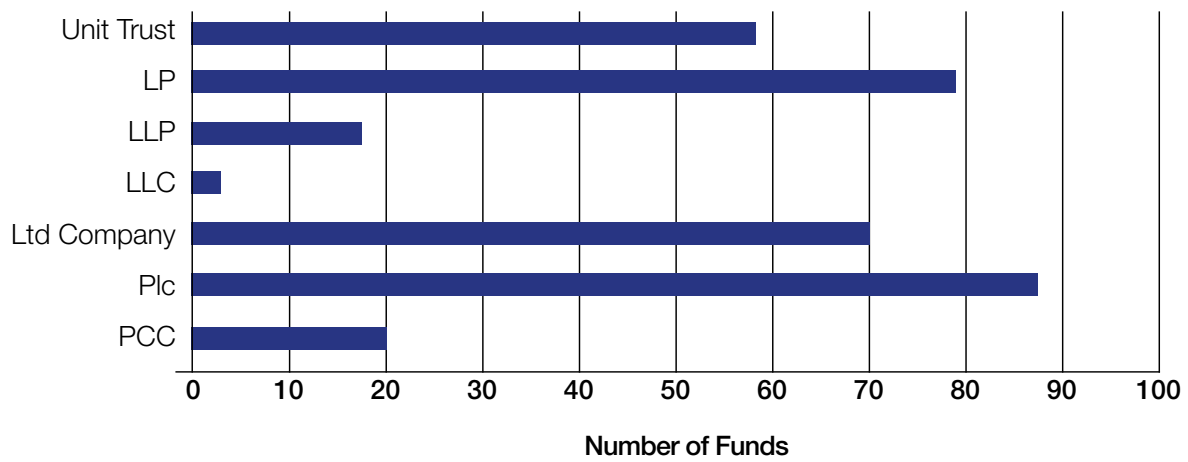
Domicile of collective investment schemes administered in the Island



### Origin of non-Isle of Man schemes:

Cayman	51	Bermuda	1
BVI	16	Guernsey	1
Luxembourg	6	Delaware	1
Jersey	3	Mauritius	1
UK	2	Ireland	1

## Legal constitution of schemes administered in the Isle of Man



## Corporate and Trust Services

### Companies, trusts, partnerships and foundations under administration

Companies, partnerships and foundations	2013/14	2012/13	Movement
1931 Act Companies	11,080	12,174	-9%
2006 Act Companies	6,915	5,952	+16%
Isle of Man public limited companies	150	152	-1%
Public companies incorporated elsewhere	14	14	0
Non-public limited companies with more than 50 shareholders	19	25	-24%
Overseas companies not registered under Part XI of the Companies Act 1931	15,145	14,341	+6%
Overseas companies registered under Part XI of the Companies Act 1931 (a.k.a. 'F-Registered')	738	695	+6%
Limited Liability Companies	465	481	-3%
Partnerships	533	529	+1%
Foundations	66	76	-13%

Trusts	2013/14	2012/13	Movement
Trusts	19,089	19,569	-2%
Private Trust Companies	645	292	+121%

# Statement of reponsibilities in respect of the Chief Executive's Report and the Accounts

The Isle of Man Financial Supervision Commission ("the Commission") is responsible for preparing the Accounts in accordance with applicable law and regulations.

The Audit Act 2006 requires the Commission to prepare accounts for each financial year, which meet the requirements of the Accounts and Audit Regulations 2013 made under the Audit Act 2006. In addition, the Commission has elected to prepare the accounts in accordance with UK Accounting Standards.

The accounts are required by law to give a true and fair view of the state of affairs of the Commission and of the profit or loss of the Commission for that period.

In preparing these accounts, the Commission is required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with UK Accounting Standards; and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the Commission will continue in operation.

The Commission is responsible for keeping proper accounting records that are sufficient to show and explain the Commission's transactions and disclose with reasonable accuracy at any time the financial position of the Commission and to enable them to ensure that the accounts comply with the Accounts and Audit Regulations 2013 made under the Audit Act 2006. The Commission has general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Commission and to prevent and detect fraud and other irregularities.

# Report of the independent auditors, KPMG Audit LLC, to the Isle of Man Financial Supervision Commission



KPMG Audit LLC  
Chartered Accountants  
Heritage Court  
41 Athol Street  
Douglas  
Isle of Man IM99 1HN

We have audited the accompanying Income and Expenditure Account (“the financial statement”) of the Isle of Man Financial Supervision Commission (“the Commission”) for the year ended 31 March 2014 and notes, comprising a summary of significant Accounting policies and other explanatory information (together “the Accounts”). The Accounts have been prepared for the purpose of the Commission’s obligations in accordance with the Audit Act 2006.

This report is made solely to the Commission, as a body, in accordance with Section 4 of the Audit Act 2006. Our audit work has been undertaken so

that we might state to the Commission those matters we are required to state to them in an auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Commission for our audit work, for this report, or for the opinions we have formed.

## **Commission’s Responsibility for the Accounts**

The Commission is responsible for the preparation and fair presentation of the Accounts in accordance with the requirements of United Kingdom Accounting Standards and the Accounts and Audit Regulations 2013 made

under the Audit Act 2006, to the extent relevant to preparing an Income and Expenditure Account, and for such internal control as management determines is necessary to enable the preparation of the Accounts that are free from material misstatement, whether due to fraud or error.

### **Auditor's Responsibility**

Our responsibility is to express an opinion on the financial statement based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statement is free from material misstatement.

An audit involved performing procedures to obtain audit evidence about the amounts and disclosures in the Accounts. The procedures selected depend on our judgement, including the assessment of the risk of material misstatement of the Accounts, whether due to fraud or error. In making those risk assessments, we consider the internal controls relevant to the entity's preparation and fair presentation of the Accounts in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, if any, made by the Commission, as well as evaluating the overall presentation of the accounts.

### **Opinion on the accounts**

In our opinion the accounts:

- give a true and fair view of the Commission's income and expenditure for the year ended 31 March 2014 in accordance with UK Accounting Standards; and
- have been properly prepared in accordance with the provisions of the Accounts and Audit Regulations 2013 made under the Audit Act 2006, to the extent that is relevant to preparing an Income and Expenditure Account.

### **Matters on which we are required to report by exception**

We review whether the Statement of Internal Control prepared by the Commission reflects compliance with the Accounts and Audit Regulations 2013 made under the Audit Act 2006. We report if the statement is misleading or inconsistent with other information we are aware of from our audit of the accounts. We are not required to consider, nor have we considered, whether the Statement of Internal Controls covers all risk and controls.

We have nothing to report in this regard in respect of the Statement of Internal Control.



## Income and Expenditure Account for the year ending 31 March 2014

Income	Note	2014		2013	
		£	£	£	£
<b>Licence &amp; Scheme Fees</b>					
Fees Income	2		<b>1,847,335</b>		1,641,113
Government Grant	10		<b>1,601,193</b>		
Other income			<b>15,485</b>		14,192
<b>Total Income</b>	1(b)		<b>3,464,013</b>		1,655,305
<b>Expenditure</b>					
Salaries	4	<b>2,478,838</b>		2,424,317	
Commissioners' Remuneration		<b>143,681</b>		141,617	
Premises		<b>293,088</b>		321,355	
Training		<b>43,099</b>		42,369	
Travel		<b>45,046</b>		42,348	
Professional Fees		<b>291,214</b>		372,442	
Operating Expenses		<b>43,051</b>		39,681	
Information Technology		<b>119,420</b>		108,250	
Other expenses		<b>6,576</b>		23,320	
<b>Total Expenditure</b>	1(c), 3		<b>3,464,013</b>		(3,515,699)
<b>Surplus/(deficit) for the year</b>					(1,860,394)

The notes on pages 93 to 95 form part of these accounts.

The income and expenditure account was approved by the Financial Supervision Commission on 29 May 2014 and signed on its behalf by Mr Geoff Karran MBE (Chairman) and Mr John Aspden (Chief Executive).

## Notes

### to the accounts for the year ended 31 March 2014

#### 1 Accounting policies

##### *a) Basis of accounting*

The Isle of Man Financial Supervision Commission (“the Commission”) is constituted under the Financial Supervision Commission Order 1983 as a Statutory Board of Tynwald. The income and expenditure account is part of the general revenue account of the Isle of Man Government. Accordingly, any deficit or surplus for the year forms part of general revenue and any surplus is not retained by the Commission. The Isle of Man Government is committed to funding any shortfall of the Commission on an on-going basis, in accordance with section 52(1) of the Financial Services Act 2008.

The accounts are prepared in accordance with the Accounts and Audit Regulations 2013, made under the Audit Act 2006 to the extent that is relevant to an Income and Expenditure Account. They are also prepared in accordance with UK Accounting Standards, and in accordance with the Isle of Man Statement of Recommended Practice 2007 on accounting for entities subject to the Audit Act 2006 (“the SORP”), to the extent applicable to the Commission.

The accounts have been prepared on a going concern basis. As noted in note 1(e), the Commission does not hold any assets or liabilities in its own name and therefore will always have a nil net asset / liability position. Any deficit incurred by the Commission during the financial year is met by the

Isle of Man Government. Details of financial arrangements held with the Isle of Man Government are included in the note 10.

##### *b) Income*

Income is accounted for on an accruals basis.

##### *c) Expenditure*

Expenditure is accounted for on an accruals basis. Amounts properly incurred during the year but not yet paid are included within expenditure.

The Commission has elected to include within expenditure, rather than capitalising, the cost of fixed assets not being made from the Consolidated Loans Fund of the Isle of Man Government. The Commission, as a Statutory Board, does not hold assets in its own name. Any assets purchased are of immaterial value with limited useful lives therefore a policy of non-capitalisation is adopted.

##### *d) Pensions*

The Commission’s employees, with the exception of the Chief Executive, are members of the Isle of Man Government Unified Pension Scheme which is administered by the Public Service Pensions Authority. Employees contribute to the scheme with employer’s contributions being funded from central Treasury and Government reserves.

##### *e) Balance sheet*

The Commission is a statutory board of the Isle of Man Government and does not hold any assets or

## Notes (continued)

### to the accounts for the year ended 31 March 2014

liabilities in its own name other than accruals and prepayments which may occur at period ends due to timing of receipts and payments. Accordingly, an independent Balance Sheet does not form part of the Accounts. A statement of accruals and prepayments attributable to the normal operations of the Commission is included in the notes to the Accounts (note 5).

#### 2 Licence and scheme fees income

Licence and scheme fee income comprises licence fee income due in relation to Deposit Taking, Investment Business, Services to Collective Investment Schemes, Corporate Services, Trust Services, E-money and Money Transmission Services and fee income due in relation to Collective Investment Schemes.

#### 3 Auditors' remuneration

Auditors' remuneration is paid by the Isle of Man Government and is therefore not included within the expenditure of the Commission.

#### 4 Salaries

Remuneration of members, officers and employees of the Commission, earning more than £50,000 per annum, are payable within the following bands:

	2014 Number	2013 Number
£50,000 - £74,999	5	5
£75,000 - £99,999	3	3
£100,000 - £124,999	1	1
£125,000 - £149,999	-	-
£150,000 - £174,999	-	-
£175,000 - £199,999	-	-
£200,000 - £224,999	-	-
£225,000 - £250,000	-	-
£250,000 +	1	1

Included within salaries are pension contributions of £nil (2013: £nil).

#### 5 Debtors and Accruals

There were no significant accruals or prepayments in both the current and previous year.

#### 6 Operating lease commitments

The Commission has the following rental lease commitments expiring:

	2014 £	2013 £
Within 12 months		243,020
Between 1 and 5 years		972,080
After 5 years		1,002,069
		2,217,169

The operating lease for the current year has been reduced to nil (2013: £2,217,169 total outstanding commitment). During the year ended 31 March 2014, Isle of Man Government purchased the building in which the Financial Supervision Commission operate due to the rising cost of the commitment.

As a result of this purchase, all previous obligations by the FSC to the building's previous owners have been nullified. The FSC now pay an annual fee to Isle of Man Government for the use of the building on a non-lease basis. This fee is equivalent to the annual sum paid under the operating lease (£243,020 per annum).

For these reasons, no operating lease commitment has been recognised in the current year, nor will any obligation be recognised going forward.

## 7 Segmental reporting

No segmental analysis has been provided as the Commission has only one business activity and operates in only one geographical area, being the regulation of relevant entities in the Isle of Man.

## 8 Related party disclosures

There were no related party transactions requiring disclosure in the accounts with the exception of transactions with the Isle of Man Government as detailed in notes 6 and 10.

During the year ended 31 March 2014 fees of £113,709 were paid to Norton Rose Fulbright LLP ("NRF") in respect

of professional services provided to the Commission. Sir David Lewis acted as a consultant to NRF until 30 April 2013. The services rendered by NRF were done so on an arm's length basis and were provided subsequent to Sir David Lewis ceasing to act as consultant to NRF.

## 9 Commitments and contingencies

The Commission has committed to expenditure of £76,961 in relation to Information and Communications Technology improvements held in the Government ICT Fund (2013: £44,311).

## 9 Government Grant

As per note 1(a), any deficit or surplus generated by the Commission during the financial year forms part of general revenue and any surplus is not retained by the Commission. The Isle of Man Government is committed to funding any shortfall of the Commission on an on-going basis, in accordance with section 52(1) of the Financial Services Act 2008.

In the current year, in contrast to previous years, this arrangement has been secured through the authorisation of a budgetary grant in advance of the current financial year. This grant was approved by Tynwald in their February 2013 sitting, and published in the same month within the Isle of Man Government's "Budget Report and Estimates 2013-14". This grant secured the provision of up to £1,867,000 to cover the Commission's deficit for 2013-14. During the year ended 31 March 2014, the Commission utilised £1,601,193 of the total allocated grant.

# Legislation coming into operation between 1 April 2013 and 31 March 2014

All recent Isle of Man legislation is accessible via:  
<http://www.gov.im/infocentre/acts/>

## Secondary legislation

**SD no 113/2013 effective 24/05/13 - Collective Investment Schemes (Fees) Order 2013.** This Order revised the fees charged in respect of collective investment schemes.

**SD no 114/2013 effective 24/05/13 - Financial Services (Fees) Order 2013.** This Order revised the fees charged to the Commission's licenceholders.

**SD no 122/2013 effective 01/06/13 - Financial Services (Miscellaneous Amendments) Act 2013 (Appointed Day) Order 2013.** This Order brought the Financial Services (Miscellaneous Amendments) Act 2013 into operation.

**SD no 307/2013 effective 01/11/13 - Recognised Auditors (Miscellaneous Amendments) Regulations 2013.** These Regulations amended the Accounting (Recognised Auditors) Regulations 2010, the Register of Recognised Auditors Regulations 2010 and the Public Oversight of Recognised Auditors Regulations 2010, all of which relate to the oversight of auditors of EU-listed 'market traded companies'.

**SD no 372/2013 effective 01/02/14 - Financial Services Rule Book 2013.** This Rule Book revoked and replaced the Financial Services Rule Book 2011 and provides the regulatory rules for licenceholders.

**SD no 373/2013 effective 01/02/14 - Regulated Activities (Amendment) Order 2013.** This Order made minor changes to the Regulated Activities Order 2011 which specifies activities that are subject to regulation and licensing.

**SD no 374/2013 effective 01/02/14 - Financial Services (Exemptions) (Amendment) Regulations 2013.** These Regulations made minor changes to the



Financial Services (Exemptions) Regulations 2011 which specify exemptions from the requirement to hold a licence.

**SD no 412/2013 effective 01/02/14 - Collective Investment Schemes (Authorised Schemes) (Trustee and Fiduciary Custodian) Order 2013.** This order amended the Collective Investment Schemes Act 2008 in respect of certain functionaries of authorised collective investment schemes.

**SD no 413/2013 effective 01/02/14 - Transfer of Business Including Deposit-Taking Regulations 2013.** These Regulations introduced a mechanism for the transfer of deposit-taking and associated business to another bank.

# Consultative documents issued between 1 April 2013 and 31 March 2014

Title of consultation	Date consultation published	Date consultation closed
Draft Designated Businesses (Registration and Oversight) Bill 2014 - 1st consultation	26 June 2013	26 July 2013
Draft revisions to the Financial Services Rule Book, Regulated Activities Order and Financial Services (Exemption) Regulations	27 June 2013	31 August 2013
Draft Transfer of Business Including Deposit-Taking Regulations	6 August 2013	18 September 2013
Draft Collective Investment Schemes (Authorised Schemes) (Trustee and Fiduciary Custodian) Order	30 August 2013	4 October 2013
Banks / Deposit Takers: Basel III - capital adequacy (Discussion Paper)	17 December 2013	17 March 2014
Banks / Deposit Takers: Domestic Systemically Important Banks (including recovery and resolution)	17 January 2014	17 April 2014
Civil penalties - expansion of use - 2nd consultation	24 January 2014	21 March 2014
Draft Designated Businesses (Registration and Oversight) Bill 2014 - 2nd consultation	20 February 2014	2 April 2014

## Other Information

The Commission's website [www.fsc.gov.im](http://www.fsc.gov.im) contains useful information including an outline of the regulatory requirements covering all areas of its responsibility.

The website provides legislation and guidance for licenceholders together with downloadable PDFs of the various legislation and Regulations.

Further publications relating to Fiduciaries, Funds, Insurance and Pensions, Tax, and Business Relocation are available from the Department of Economic Development, St George's Court, Upper Church Street, Douglas, Isle of Man, IM1 1EX or can be downloaded from <http://www.whereyoucan.im/resources>

The Isle of Man Insurance and Pensions Authority also provides copies of legislation on its website [www.gov.im/ipa](http://www.gov.im/ipa), including:

- The Insurance Act 2008 and attendant regulations and guidance
- The Retirement Benefits Schemes Act 2000 and attendant regulations
- The Insurance (Anti-Money Laundering) Regulations 2008 and associated guidance notes.

Telephone calls made to or from the Commission may be recorded or monitored.

<b>ACCA</b>	The Association of Chartered Certified Accountants	<b>IGA</b>	Inter-Governmental Agreement
<b>ACSP</b>	Association of Corporate Service Providers	<b>IIP</b>	Investors in People
<b>ADBR</b>	Annual Desk Based Review	<b>IMF</b>	International Monetary Fund
<b>AIFMD</b>	Alternative Investment Fund Managers Directive	<b>IOM</b>	Isle of Man
<b>AML</b>	Anti-money Laundering	<b>IOMBA</b>	Isle of Man Bankers Association
<b>BCCI</b>	Bank of Credit and Commerce International S.A.	<b>IOMFA</b>	Isle of Man Funds Association
<b>BIS</b>	Bank for International Settlements	<b>IOSCO</b>	International Organisation of Securities Commissions
<b>BRICS</b>	Brazil, Russia, India, China and South Africa	<b>IPA</b>	Insurance and Pensions Authority
<b>BVI</b>	British Virgin Islands	<b>ISD</b>	Isle of Man Government's Information Systems Division
<b>CAT</b>	Certified Accounting Technician	<b>Island</b>	Isle of Man
<b>CFT</b>	Countering the Financing of Terrorism	<b>IT</b>	Information Technology
<b>CIS</b>	Collective Investment Scheme	<b>JAMLAG</b>	Joint Anti-money Laundering Advisory Group
<b>CISA08</b>	Collective Investment Schemes Act 2008	<b>KSFIOM</b>	Kaupthing Singer & Friedlander (Isle of Man) Limited
<b>CISI</b>	Chartered Institute for Securities & Investment	<b>MIFID2</b>	Draft Markets in Financial Instruments Directive
<b>Commission</b>	The Financial Supervision Commission	<b>MIFIR</b>	Draft Markets in Financial Instruments Regulation
<b>CODA</b>	Company Officers Disqualification Act 2009	<b>MLRO</b>	Money Laundering Reporting Officer
<b>CPD</b>	Continuing Professional Development	<b>MMOU</b>	Multilateral Memorandum of Understanding
<b>CPI</b>	Consumer Price Index	<b>MONEYVAL</b>	Committee of Experts on the Evaluation of Anti-money Laundering Measures
<b>CSP</b>	Corporate Service Provider	<b>MOU</b>	Memorandum of Understanding
<b>DCS</b>	Depositors' Compensation Scheme	<b>MTS</b>	Money Transmission Services
<b>DED</b>	Department of Economic Development	<b>NAV</b>	Net Asset Value
<b>DHA</b>	Department of Home Affairs	<b>NRA</b>	National Risk Assessment
<b>D-SIBs</b>	Domestic Systemically Important Banks	<b>OECD</b>	Organisation for Economic Co-operation and Development
<b>DNFBPs</b>	Designated Non-Financial Businesses and Professions	<b>OFT</b>	Office of Fair Trading
<b>ECB</b>	European Central Bank	<b>OSCE</b>	Organisation for Security and Co-operation in Europe
<b>EEA</b>	European Economic Area	<b>PDF</b>	Portable Document Format
<b>EIF</b>	Experienced Investor Fund	<b>PEP</b>	Politically Exposed Persons
<b>EPC</b>	European Payments Council	<b>PLC</b>	Public Limited Company
<b>ESMA</b>	European Securities and Markets Authority	<b>PRA</b>	UK Prudential Regulatory Authority
<b>EU</b>	European Union	<b>RDR</b>	Retail Distribution Review
<b>FATCA</b>	Foreign Account Tax Compliance Act	<b>RICC</b>	Risk and Internal Control Committee
<b>FATF</b>	Financial Action Task Force	<b>RPI</b>	Retail Price Index
<b>FCA</b>	UK Financial Conduct Authority	<b>Rule Book</b>	Financial Services Rule Book
<b>FSAP</b>	Financial Sector Assessment Programme	<b>S&amp;P</b>	Standard and Poor's
<b>FSA08</b>	Financial Services Act 2008	<b>SEPA</b>	Single Euro Payments Area
<b>GDP</b>	Gross Domestic Product	<b>STEP</b>	Society of Trust and Estate Practitioners
<b>GIFCS</b>	Group of International Finance Centre Supervisors	<b>TCSPs</b>	Trust and Corporate Service Providers
<b>GNI</b>	Gross National Income	<b>TSP</b>	Trust Service Provider
<b>GSC</b>	Gambling Supervision Commission	<b>UK</b>	United Kingdom
<b>HMT</b>	Her Majesty's Treasury	<b>UN</b>	United Nations
<b>HMRC</b>	HM Revenue and Customs	<b>USA</b>	United States of America
<b>ICA</b>	International Compliance Association	<b>VAT</b>	Value Added Tax
<b>ICB</b>	Independent Commission on Banking		
<b>ICAEW</b>	The Institute of Chartered Accountants in England and Wales		
<b>ICSA</b>	Institute of Chartered Secretaries and Administrators		





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