



Statutory Document No.

**FINANCIAL SERVICES ACT 2008**

**FINANCIAL SERVICES RULE BOOK 2008**

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Statutory Document No.

## FINANCIAL SERVICES ACT 2008

### FINANCIAL SERVICES RULE BOOK 2008

<i>Laid before Tynwald</i>	2008
<i>Approved by Tynwald</i>	2008
<i>Coming into operation</i>	<i>1st August 2008</i>

In exercise of the powers conferred on the Financial Supervision Commission by section 18 of and Schedule 3 to the Financial Services Act 2008<sup>1</sup>, and of all other enabling powers, and after carrying out the consultations required by section 44(5) of that Act, the following Rule Book is hereby made:—

#### PART 1 — INTRODUCTORY

##### 1.1 Citation and commencement

This Rule Book may be cited as the Financial Services Rule Book 2008 and shall come into operation on 1st August 2008.

##### 1.2 Interpretation

(1) In this Rule Book —

"the Act" means the Financial Services Act 2008;

"the Order" means the Regulated Activities Order 2008<sup>2</sup>;

(2) References in these Regulations to —

(a) a class of regulated activities are to regulated activities of a class specified in Schedule 1 to the Order;

(b) a numbered class, or to a numbered paragraph of such a class, are to the class of regulated activities so numbered in Schedule 1 to the Order, or to the paragraph so numbered of that class, as the case may be.

(3) Other expressions in this Rule Book have the meanings given by Schedule 1.1.

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<sup>1</sup> 2008 c.

<sup>2</sup> SD /08

Price

(4) Any note in a Schedule to this Rule Book shall be construed as part of that Schedule.

### **1.3 Application**

(1) Part 9, and this Part so far as it relates to Part 9, apply to every licenceholder as from the coming into operation of this Rule Book.

(2) This Rule Book, except Part 9 and this Part so far as it relates to Part 9, applies to the holder of an existing licence as from 1st January 2009 in relation to the regulated activities which, by virtue of article 4 of the Financial Services Act 2008 (Appointed Day) Order 2008, the licence authorises the holder to carry on.

(3) Except as provided by paragraphs (1) and (2), this Rule Book applies to every licenceholder in relation to any regulated activities as from the date a licence is issued in respect of those activities.

(4) Where a provision of this Rule Book is stated to apply to a licenceholder licensed to carry on regulated activities of a specified description, that provision applies —

- (a) except where otherwise expressly provided,
- (b) only so far as applicable;
- (c) only in relation to regulated activities of that description; and
- (d) in the case of a licenceholder incorporated in a country or territory outside the Island, only in relation to regulated activities carried on in or from the Island.

### **1.4 Confirmation of oral notification**

Where a licenceholder –

- (a) is required by any provision of this Rule Book to notify the Commission of any matter, and
- (b) notifies the Commission orally of that matter,

that requirement shall not be taken to have been complied with unless the notification is confirmed in writing within 24 hours after it is given.

## PART 2 — FINANCIAL RESOURCES AND REPORTING

### *Chapter 1 — General requirements for all licenceholders*

#### **2.1 Application**

- (1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.
- (2) Subject to paragraph (1) rule 2.2 applies to all licenceholders.
- (3) Subject to paragraphs (1) and (2), this Chapter applies to all licenceholders other than those licensed to carry on only activities falling within either or both of —
  - (a) paragraph (6) of Class 4 (acting as officer of company), and
  - (b) paragraph (2) or (5) of Class 5 (acting as trustee or protector).

#### **2.2 Annual reporting date**

A licenceholder must notify the Commission of its annual reporting date.

#### **2.3 Notification of inability to comply**

A licenceholder must notify the Commission immediately where it has reason to believe that —

- (a) it will be unable to make a financial return; or
- (b) it will be unable to comply, or to demonstrate compliance, with any provision of this Part as a result of a failure in accounting systems.

#### **2.4 Reporting currency**

Any financial return made by a licenceholder must be expressed —

- (a) in such currency as the Commission, at the licenceholder's request, may approve; or
- (b) if no such currency is approved, in sterling.

#### **2.5 Responsibility for returns**

- (1) A licenceholder must by its responsible officers —
  - (a) designate one individual whose responsibility it is to make any financial return to the Commission,
  - (b) designate another individual to undertake that responsibility in the absence of the individual designated under sub-paragraph (a), and
  - (c) keep the Commission informed of the names of the individuals so designated.

(2) Any person who is an Isle of Man resident officer in relation to a licenceholder is responsible for the completeness and accuracy of any financial return made to the Commission by or in respect of the licenceholder.

## **2.6 Misleading financial returns**

A licenceholder must notify the Commission as soon as it has reason to believe that any financial return previously made by it to the Commission was or has become misleading in any material respect.

## **2.7 Electronic reporting**

- (1) A financial return must be made to the Commission –
  - (a) by such method of electronic communication as the Commission may reasonably require, or
  - (b) such other method of communication as the Commission may approve.
- (2) Paragraph (1) does not apply to —
  - (a) a licenceholder's annual financial return referred to in rule 2.9; or
  - (b) any annual accounts of a parent company, holding company, subsidiary or associated company referred to in rule 2.11 or 2.15.

(3) In paragraph (1) "electronic communication" has the same meaning as in the Electronic Transactions Act 2000.

## **2.8 Annual financial statements**

- (1) References in this Part to the annual financial statements of —
  - (a) a licenceholder,
  - (b) a company of which a licenceholder is a subsidiary, or
  - (c) a subsidiary or associated company of a licenceholder,

shall be construed in accordance with this rule.

(2) Subject to paragraph (3), the annual financial statements of a person referred to in paragraph (1) comprise one or more statements in monetary terms of the results of the transactions of —

- (a) that person, or
- (b) if the Commission so directs, that person and its subsidiaries,

over a year ending on its annual reporting date.

- (3) Those statements —
  - (a) must include —

- (i) a balance sheet as at that date, and
- (ii) a profit and loss account or income statement for that year; of that person, or that person and its subsidiaries, as the case may be;

- (b) may relate to a period other than a year where permitted by rule 2.9(3); and
- (c) must be prepared according to—
  - (i) the standards required by the law of the country or territory in which that person is incorporated, if that law requires them to comply with accounting standards;
  - (ii) otherwise, the standards referred to in rule 2.10.

## **2.9 Annual financial return**

(1) A licenceholder must provide to the Commission an annual financial return as soon as it is available, and in any case, within 4 months of the licenceholder's annual reporting date.

(2) The annual financial return must comprise —

- (a) the licenceholder's audited annual financial statements for the period to which the return relates, and
- (b) such other statements (if any) as are required by the following provisions of this Part.

(3) The period to which the annual financial return relates must be the year ending on the licenceholder's annual reporting date, unless —

- (a) it is the licenceholder's first annual financial return, in which case the period shall be the period (not being more than 18 months) beginning with the date the licenceholder began trading and ending on its annual reporting date; or
- (b) the licenceholder's annual reporting date has changed since the previous annual financial return, in which case the period shall be such period (not being more than 18 months) beginning on a previous annual reporting date and ending on the new annual reporting date.

(4) The annual financial statements provided under paragraph (2)(a) must be —

- (a) signed by the auditor, or
- (b) certified by a director of the licenceholder to be a true copy of a copy signed by the auditor.

## **2.10 Accounting standards**

Except where otherwise provided, any financial return which is required by this Rule Book to be submitted to the Commission must be prepared in accordance with either —

- (a) any applicable Financial Reporting Standards issued or adopted from time to time by the Accounting Standards Board in the United Kingdom; or
- (b) any International Financial Reporting Standards published from time to time by the International Accounting Standards Board.

## **2.11 Accounts of parent and holding companies**

(1) Where a licenceholder is a subsidiary of another company ("the parent company"), it must provide to the Commission a copy of the audited annual financial statements of —

- (a) the parent company, and
- (b) any company which is a holding company of the parent company,

as soon as they become available, and in any case, within 6 months of the licenceholder's annual reporting date.

(2) Those statements must be audited —

- (a) in accordance with the law of the country or territory in which the parent company or holding company (as the case may be) is incorporated, if they are required by that law to be audited;
- (b) otherwise, as if they were the annual financial statements of the licenceholder.

(3) The copy of the statements provided under paragraph (1) must be —

- (a) signed by the auditor, or
- (b) certified by a director of the licenceholder to be a true copy of a copy signed by the auditor.

## ***Chapter 2 — General requirements for all licenceholders incorporated in the Island***

### **2.12 Application**

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Chapter applies to all licenceholders which are incorporated in the Island.

### **2.13 Change of annual reporting date**

A licenceholder may not change its annual reporting date without the prior consent in writing of the Commission.

### **2.14 Accounting records**

(1) A licenceholder must keep such accounting records in the Island as are necessary accurately to show at any time —

- (a) the financial position of the licenceholder's business, and
- (b) whether the licenceholder complies with any applicable provisions of this Part relating to its financial resources.

(2) A licenceholder must preserve its accounting records for not less than 6 years beginning with the date on which they are made.



(3) Where a licence is surrendered or revoked, the licenceholder must preserve its accounting records for not less than 6 years beginning with the date of surrender or revocation.

(4) A licenceholder must keep the Commission informed of the method of storage and location of any records required by this rule to be preserved.

(5) The requirements of this rule are without prejudice to the requirements of any other statutory provision.

## **2.15 Accounts of subsidiary and associated companies**

(1) A licenceholder's audited annual financial return must include (in addition to the annual financial statements mentioned in rule 2.9(2)(a)) a copy of the latest audited annual financial statements of —

- (a) any subsidiary of the licenceholder, and
- (b) any associated company of the licenceholder,

except a company which the licenceholder's auditor confirms has not traded in the financial year in question.

(2) Those statements must be audited —

- (a) in accordance with the law of the country or territory in which the subsidiary or associated company (as the case may be) is incorporated, if they are required by that law to be audited;
- (b) otherwise, as if they were the annual financial return of the licenceholder.

(3) The copy of the statements provided under paragraph (1) must be —

- (a) signed by the auditor, or
- (b) certified by a director of the licenceholder to be a true copy of a copy signed by the auditor.

(4) In this rule —

"subsidiary" does not include a shelf company;

"shelf company" means a company which —

- (a) has been formed and maintained by a licenceholder in the course of regulated activities falling within Class 4 or Class 5 with the intention that it should at some time be transferred to a client, and
- (b) has not carried on any activity.

## ***Chapter 3— General requirements for all licenceholders incorporated outside the Island***

### **2.16 Application**

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Chapter applies to all licenceholders which are incorporated outside the Island.

### **2.17 Change of annual reporting date**

Without prejudice to rule 2.2, a licenceholder must notify the Commission before changing its annual reporting date.

### **2.18 Accounting records**

(1) A licenceholder must keep such accounting records in the Island as are necessary accurately to show its operations in or from the Island at any time.

(2) A licenceholder must preserve its accounting records for not less than 6 years beginning with the date on which they are made.

(3) Where a licence is surrendered or revoked, the licenceholder must preserve its accounting records for not less than 6 years beginning with the date of surrender or revocation.

(4) A licenceholder must keep the Commission informed of the method of storage and location of any records required by this rule to be preserved.

(5) The requirements of this rule are without prejudice to the requirements of any other statutory provision.

### **2.19 Contents of annual financial return**

A licenceholder's annual financial return must include (in addition to the annual financial statements mentioned in rule 2.9(2)(a)) a detailed profit and loss account in respect of its operations in or from the Island.

## ***Chapter 4 — Specific requirements for deposit takers incorporated in the Island***

### **2.20 Application**

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 1 which are incorporated in the Island.

### **2.21 Share capital**

The paid-up share capital of a licenceholder must not be less than £3,500,000 sterling or its equivalent in another currency.

### **2.22 Charges**

(1) A licenceholder must notify the Commission before —

- (a) creating any charge on any of its assets, or
- (b) entering into an agreement by virtue of which such a charge may be created.

(2) A notification under paragraph (1) must be made —

- (a) if practicable, not less than 20 business days before the charge is created or the agreement is entered into, as the case may be; or
- (b) otherwise, as soon as practicable.

### **2.23 Capital resources**

- (1) A licenceholder must by its directors —
  - (a) establish and maintain an internal capital adequacy assessment process (ICAAP) which is appropriate to the nature and scale of its business, and
  - (b) review that process annually.
- (2) A licenceholder must not at any time permit its risk-asset ratio to fall below the minimum risk-asset ratio.
- (3) A licenceholder must immediately notify the Commission if at any time it has reason to believe that its risk-asset ratio is or may fall below the minimum risk-asset ratio.

- (4) A licenceholder must by its directors —
  - (a) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the requirements of paragraph (3), and
  - (b) review those procedures annually.
- (5) A licenceholder must provide the Commission with details of —
  - (a) its internal capital adequacy assessment process,
  - (b) the procedures referred to in paragraph (4)(a), and
  - (c) any substantial amendment of it or them,

within 20 business days of the approval by the directors of the process, procedures or amendment.

- (6) In this rule, in relation to a licenceholder, "minimum risk-asset ratio" means —
  - (a) such risk-asset ratio as the Commission may direct in the case of that licenceholder;
  - (b) where no such direction is given, 8 per cent.

### **2.24 Deposit-taking returns**

- (1) The licenceholder must prepare the following deposit taking returns ("set of deposit taking returns") as at each quarter end —

Form SR-1A Balance Sheet Assets, Liabilities and Off Balance Sheet Items return

Form SR-1B Credit Risk return

Form SR-1C Operational Risk return

Form SR-2A Capital, Current Period's Profit and Loss, Provisions and Non-performing Assets return

- Form SR-2B Large Exposures Reporting return
- Form SR-2C Risk Asset Ratio and Memorandum Items return
- Form SR-3A Liquidity Risk return
- Form SR-3B Interest Rate Risk return
- Form SR-4 Market Risk (FX and gold, commodities) and Settlement Risk return.

(2) The licenceholder must prepare an additional set of deposit taking returns as at its annual accounting date if this does not fall on a quarter-end.

(3) The licenceholder must submit every set of deposit taking returns prepared under paragraph (1) or (2) to the Commission within one month of the date to which it relates.

(4) The deposit taking returns must contain the information specified in Schedule 2.1.

## 2.25 Contents of annual financial return

(1) A licenceholder's annual financial return must include (in addition to the annual financial statements mentioned in rule 2.9(2)(a)) —

- (a) a statement detailing the calculation of its large exposures capital base as at its annual reporting date;
- (b) a detailed profit and loss account relating to its own transactions (if not included in the annual financial statements); and
- (c) a statement providing a reconciliation of all material differences between —
  - (i) the set of deposit taking returns as at its annual reporting date, and
  - (ii) the balance sheet and profit and loss account.

(2) The balance sheet mentioned in rule 2.9(2)(a) must include or have annexed to it —

- (a) an analysis of assets and liabilities by maturity date in the following time bands, separately identifying deposit liabilities and placings with deposit takers —

From	less than
Sight	8 days
8 days	1 month
1 month	3 months
3 months	6 months
6 months	12 months
12 months	3 years
3 years	5 years

5 years —

- (b) the gross amount of all loans and advances due from intra-group companies;
  - (c) the gross amount of all loans and advances due from, and guarantee commitments entered into on behalf of:-
    - (i) shareholders; and
    - (ii) directors and managers;
  - (d) in respect of large exposures otherwise than to deposit takers, the number and total value of exposures which individually exceed 10% of the total of the large exposures capital base, loans to related parties being aggregated.
- (3) The profit and loss account mentioned in rule 2.9(2)(b) must include (or have annexed to it) statements of —
- (a) total income for the year;
  - (b) interest income and expenditure; and
  - (c) the effect on the profit and loss account of provisions for bad and doubtful debts, separately identifying amounts charged against the current year's income for amounts written off and provisions and any credit for releases of existing provisions, recoveries etc.

## **2.26 Publication of annual financial statements**

- (1) Within 4 months of its annual reporting date, a licenceholder must —
  - (a) make its audited annual financial statements available for public inspection in the Island;
  - (b) display a notice in its registered office and all other offices in the Island stating that —
    - (i) a copy of its latest audited balance sheet together with the last auditor's report (as it appears in the audited annual financial statements) may be inspected by any person on demand, and
    - (ii) copies are available to be taken away.
- (2) In addition to the annual financial statements referred to in paragraph (1), a licenceholder may make abridged financial statements available for inspection.
- (3) Any abridged statements made available under paragraph (2) must contain the following information as a minimum —
  - (a) a Balance Sheet identifying separately —

### **Liabilities**

Paid up element of issued share capital

Revenue reserves

Subordinated loans

Deposit liabilities

All other liabilities

Total liabilities

Assets

Money market assets, differentiating between intra-group and others

Loans

Investments

Intangible assets

Fixed assets

All other assets

Total assets

- (b) a note of any contingent liabilities;
- (c) the names of the directors and secretary;
- (d) the immediate and ultimate holding company of the licenceholder;
- (e) any subsidiaries of the licenceholder;
- (f) the registered office;
- (g) the auditor's report;
- (h) a note that a copy of the full audited financial statements is available upon request (specifying any fee that will be charged).

## ***Chapter 5 — Specific requirements for deposit-takers incorporated outside the Island***

### **2.27 Application**

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 1 which are incorporated outside the Island.

### **2.28 Deposit taking returns**

(1) The licenceholder must prepare the following deposit-taking returns (“set of deposit-taking returns”) as at each quarter end —

Form SR-1A Balance Sheet Assets, Liabilities and Off Balance Sheet Items return

Form SR-2A Capital, Current Period's Profit and Loss, Provisions and Non-performing Assets return (the licenceholder shall not complete the section on capital)

Form SR-2B Large Exposures Reporting return

Form SR-2C Risk Asset Ratio and Memorandum Items return (the licenceholder shall not complete the section on risk-asset ratio)

Form SR-3A Liquidity Risk return

(2) The licenceholder must prepare an additional set of deposit taking returns as at its annual accounting date if this does not fall on a quarter-end.

(3) The licenceholder must submit every set of deposit taking returns prepared under paragraph (1) or (2) to the Commission within one month of the date to which it relates.

(4) The deposit taking returns must contain the information specified in Schedule 2.1.

## **2.29 Publication of annual financial statements**

(1) Within 4 months of its annual reporting date, the licenceholder must —

(a) make its audited annual financial statements available for public inspection in the Island;

(b) display a notice in all its offices in the Island stating that —

(i) a copy of the latest audited balance sheet of the licenceholder together with the last auditor's report (as it appears in the audited annual financial statements) may be inspected by any person on demand, and

(ii) copies are available to be taken away.

(2) In addition to the financial statements referred to in paragraph (1), a licenceholder may make abridged financial statements available for public inspection.

(3) Paragraph (3) of rule 2.26 applies to abridged statements made available under paragraph (2).

## ***Chapter 6 — Specific requirements for investment businesses and CIS service, corporate service and trust service providers (except professional officers)***

### **2.30 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5 other than —

(a) those who are also licensed to carry on activities falling within Class 1, and

(b) individuals licensed to carry on only activities falling within either or both of —

(i) paragraph (6) of Class 4 (acting as officer of company), and

(ii) paragraph (2) or (5) of Class 5 (acting as trustee or protector).

### **2.31 Solvency**

A licenceholder must ensure that at all times it is able to meet its liabilities as they fall due.

### **2.32 Failure to comply with obligations**

(1) A licenceholder must notify the Commission as soon as it has reason to believe that it will be unable to make a payment to a creditor on the date that the payment is due.

(2) For the purpose of this rule —

(a) a payment under a contract is due on the date on which it is payable in accordance with the terms of the contract;

(b) a payment under a transaction subject to the rules of an exchange or clearing house is due on the date on which it is payable under those rules.

### **2.33 Financial commitments**

(1) A licenceholder must not give any guarantee, indemnity or other commitment (other than one entered into in the ordinary course of its business) without the consent of the Commission.

(2) A licenceholder must notify the Commission as soon as it becomes aware that any guarantee, indemnity or other commitment given by the licenceholder may result in a claim notifiable under rule 2.34.

(3) A licenceholder must notify the Commission as soon as it becomes aware of —

(a) any guarantee, indemnity or other commitment given in respect of the licenceholder by another member of the licenceholder's group in favour of an exchange;

(b) any contingent liability incurred by the licenceholder which might affect its ability to meet any of the requirements referred to in rule 2.37; and

(c) any change in information previously notified under paragraph (2) or this paragraph.

### **2.34 Claims**

A licenceholder must notify the Commission as soon as it becomes aware of any claim made in writing against the licenceholder where any amount claimed or disputed is likely to exceed the lower of —

(a) £10,000; or

(b) where applicable, 10% of the licenceholder's minimum net tangible asset requirement (specified in column 6 of Schedule 2.2)



### **2.35 Charges**

- (1) A licenceholder must not without the consent of the Commission —
  - (a) create any charge on any of its assets, or
  - (b) enter into an agreement by virtue of which such a charge may be created.
- (2) A licenceholder must —
  - (a) notify the Commission as soon as a charge (other than one created with the consent of the Commission) has been registered against the licenceholder; and
  - (b) at the same time state whether the charge has an adverse impact on its financial resources.
- (3) For the avoidance of doubt, references in this rule to assets of a licenceholder do not include property held by the licenceholder as trustee of an express trust.

### ***Chapter 7— Specific requirements for investment businesses and CIS service, corporate service and trust service providers incorporated in the Island***

### **2.36 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5 which are incorporated in the Island, other than those who are also licensed to carry on activities falling within Class 1.

### **2.37 Financial resources requirements**

- (1) A licenceholder licensed to carry on regulated activities falling within a class, and the paragraphs of a class, specified in columns 1 and 2 of Schedule 2.2 must at all times comply with the following requirements –
  - (a) its issued share capital (including any paid-up share premium) must not be less than the corresponding amount specified as its minimum share capital requirement in column 5 of Schedule 2.2;
  - (b) its net tangible assets (calculated in accordance with Part A of Schedule 2.3) must not be less than the corresponding amount specified as its minimum net tangible asset requirement in column 6 of Schedule 2.2;
  - (c) it must maintain liquid capital of an amount calculated in accordance with Part D of Schedule 2.3.
- (2) The requirements referred to in paragraph (1)(a) and (b) are subject to any qualification or exception specified in column 4 of Schedule 2.2.
- (3) Where the licenceholder carries on 2 or more regulated activities in respect of which different amounts are specified or calculated as mentioned in paragraph (1)(a), (b) or (c), the requirement in question shall be taken as relating to the highest amount so specified.

### **2.38 Procedures and controls**

A licenceholder must maintain appropriate procedures and controls for the purpose of monitoring its compliance with the requirements of rule 2.37.

### **2.39 Notification of actual or potential breach**

(1) A licenceholder must immediately notify the Commission if at any time it has reason to believe that its net tangible assets —

- (a) are or may fall below the amount referred to in rule 2.37(1)(b); or
- (b) without prejudice to sub-paragraph (a), are or may fall below 110% of that amount.

(2) A licenceholder must immediately notify the Commission if at any time it has reason to believe that its liquid capital —

- (a) is or may fall below the amount referred to in rule 2.37(1)(c); or
- (b) without prejudice to sub-paragraph (a), is or may fall below 110% of that amount.

(3) When giving a notification under paragraph (1) or (2) the licenceholder must also provide the Commission with —

- (a) a full explanation of the circumstances, and
- (b) details of the steps that the licenceholder is taking or has taken to prevent a breach of rule 2.37 occurring or to remedy the breach, as the case may be.

### **2.40 Contents of annual financial return**

(1) A licenceholder's annual financial return must include (in addition to the annual financial statements mentioned in rule 2.9(2)(a)) —

- (a) an audited financial resources statement; and
- (b) where the profit and loss account included in the annual financial statements is not sufficient to verify the calculations in the statement referred to in sub-paragraph (a), a detailed unconsolidated profit and loss account of the licenceholder;
- (c) where there are differences between the statements referred to in sub-paragraphs (a) and (b) and whichever of the following is applicable —
  - (i) the interim financial returns required by rule 2.42, or
  - (ii) the calculations referred to in rule 2.46(b),a reconciliation identifying those differences and the reasons for them.

(2) The statement referred to in paragraph (1)(a) must be prepared in accordance with Schedule 2.3.

**Chapter 8 — Specific requirements for investment businesses and CIS service providers incorporated in the Island (except financial advisers and promoters)**

**2.41 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2 and Class 3 which are incorporated in the Island, other than —

- (a) those who are also licensed to carry on activities falling within Class 1, and
- (b) those licensed to carry on only activities falling within either or both of —
  - (i) paragraphs (3) and (7) of Class 2 (advising on investments), and
  - (ii) paragraph (8) of Class 3 (acting as promoter of collective investment scheme).

**2.42 Interim financial returns**

(1) A licenceholder must prepare an unaudited interim financial return as at the end of the periods of —

- (a) 3 months,
- (b) 6 months, and
- (c) 9 months,

after each annual reporting date.

(2) In the case of a licenceholder licensed to carry on only activities falling within paragraphs (3) and (6) of Class 2 (investment adviser to retirement benefits schemes), paragraph (1) has effect with the substitution, for the words from "the periods" onwards, of "the period of 6 months after each annual reporting date".

(3) The licenceholder must provide an interim financial return prepared under paragraph (1) to the Commission as soon as it becomes available, and in any case, within one month after the end of the period to which it relates.

(4) An interim financial return must comprise a statement in monetary terms of the results of the licenceholder's transactions over the period to which it relates, including —

- (a) an unconsolidated balance sheet which shows the state of affairs of the licenceholder as at the end of the period to which it relates; and
- (b) an unconsolidated profit and loss account which shows the profit or loss (not cumulative) of the licenceholder for that period; and
- (c) a financial resources statement.

(5) The statement referred to in paragraph (4)(c) must be prepared in accordance with Schedule 2.3, with any necessary modifications.

(6) An interim financial return must be in sufficient detail to verify the calculations required by rule 2.37.

***Chapter 9 — Specific requirements for stockbrokers incorporated in the Island***

**2.43 Application**

This Chapter applies to all licenceholders licensed to carry on all the regulated activities falling within paragraphs (1) to (6) of Class 2 which are incorporated in the Island, other than those who are also licensed to carry on activities falling within Class 1.

**2.44 Counterparty risk requirement (CRR)**

The calculation (as part of the financial resources requirements) of the licenceholder's liquid capital referred to in rule 2.37(1)(c) must include an item representing the risk that counterparties to transactions to which it is party could default before final settlement, calculated in accordance with Schedule 2.4.

***Chapter 10 — Specific requirements for investment businesses, corporate service providers and trust service providers incorporated in the Island (except certain advisers and professional officers)***

**2.45 Application**

(1) This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2 which are incorporated in the Island, other than —

- (a) those who are also licensed to carry on activities falling within Class 1, and
- (b) those licensed to carry on only activities falling within —
  - (i) paragraphs (3) and (6) of Class 2 (investment adviser to retirement benefits schemes), or
  - (ii) paragraphs (3) and (7) of Class 2 (financial adviser).

(2) This Chapter also applies to all licenceholders licensed to carry on regulated activities falling within Class 4 or Class 5 which are incorporated in the Island, other than —

- (a) those who are also licensed to carry on activities falling within Class 1, and
- (b) individuals licensed to carry on only activities falling within paragraph (6) or (7) of Class 4 (acting as officer of company).

**2.46 Monitoring of financial resources requirements**

A licenceholder must —

- (a) monitor compliance with the requirements of rule 2.37 not less often than once in each quarter, and

- (b) if so required by the Commission, provide it with evidence of the calculations required for that purpose.

PART 3 — CLIENT MONEY AND TRUST MONEY

*Chapter 1 — Application and interpretation*

**3.1 Interpretation: general**

(1) In this Part —

"client" includes the trustee of a trust;

"client bank account", "designated client bank account", "general client bank account" and "separate client bank account" have the meanings given by rule 3.3;

"client money" has the meaning given by rule 3.2;

"money" means —

(a) legal tender in the Island or elsewhere, or

(b) anything which may be directly converted into legal tender,

and includes notes and coin, cheques, drafts and other bills of exchange, and funds held in electronic form;

"recognised bank" means an institution which is either —

(a) licensed to carry on an activity of Class 1; or

(b) carrying on business in a country or territory outside the Island the government of which has signified acceptance of the principles of the International Concordat on Banking Supervision issued by the Committee on Banking Regulation and Supervisory Practices, and authorised under the law of that country or territory to carry on activities corresponding to activities of Class 1;

except (in the case of an institution falling within (b) above) where the Commission has notified the licenceholder concerned that it has reason to believe that the principles referred to are not being applied; and any reference in this Part to a bank is to a recognised bank;

"relevant agreement" means any agreement the making or performance of which by either party constitutes a regulated activity to which this Part applies;

"regulated activity to which this Part applies" means a regulated activity falling within Class 2, Class 3, Class 4 or Class 5;

"trust money" has the meaning given by rule 3.2.

**3.2 Meaning of "client money" and "trust money"**

(1) In this Rule Book —

(a) "client money" means money which, for the purpose or in the course of a regulated activity to which this Part applies, a licenceholder —

(i) holds or receives on behalf of a client, or

(ii) owes to a client;

- (b) "trust money" means money, forming part or all of the assets of a trust, which, for the purpose or in the course of a regulated activity to which this Part applies, a licenceholder holds or receives as, or as agent or nominee of, the trustee of that trust.

(2) Where, for the purpose or in the course of a regulated activity to which this Part applies and which is carried on or to be carried on for a client, a licenceholder holds or receives (in the Island or elsewhere) money which is not immediately due and payable to the licenceholder for its own account, for the purpose of this rule it holds or receives that money on behalf of the client.

- (3) Without prejudice to paragraph (2), where —

- (a) a relevant agreement is in force between a licenceholder and a client, or
- (b) the licenceholder expects to enter into a relevant agreement with or for a client,

and the licenceholder, or an agent on its behalf, holds or receives (in the Island or elsewhere) any money —

- (i) which is not immediately due and payable on demand to the licenceholder for its own account; or
- (ii) which, although so due and payable, is held or received in respect of any obligation of the licenceholder under the agreement which has not yet been performed,

for the purpose of this rule the licenceholder holds or receives that money on behalf of the client.

(4) For the purpose of this rule a licenceholder owes money to a client where it is due and payable to the client by the licenceholder or an agent on its behalf, whether demanded or not.

- (5) Money ceases to be, or never becomes, client money if it is paid —
  - (a) to the client; or
  - (b) into a bank or other account in the name of the client (not being an account which is also in the name of the licenceholder); or
  - (c) otherwise at the direction of the client.

### **3.3 Meaning of "client bank account" and related expressions**

- (1) Subject to paragraph (2), in this Part —

"client bank account", in relation to a licenceholder, means an account held by the licenceholder at a recognised bank which is —

- (a) specially created by the licenceholder for the purpose of holding client money, and
- (b) segregated from any account holding money which is not client money;

"designated client bank account" means a client bank account which —

- (a) is held at a bank chosen by one or more clients;

- (b) holds client money of that client or those clients (and of no other client),
- (c) includes in its title the words "designated client bank account", and
- (d) in the event of the failure of a bank, other than the bank at which the designated client bank account is held, is not intended to be pooled with any other client bank account or type of client bank account;

"general client bank account" means a client bank account other than a separate client bank account or a designated client bank account;

"separate client bank account" means a client bank account which —

- (a) holds, and is intended to hold, client money of one particular client (and of no other client),
- (b) is segregated from any account holding money which is not client money of that client; and
- (c) includes in its title the name or designation of the client;

"trust bank account" means an account held by the trustee of a specified trust at a recognised bank which —

- (a) holds, and is intended to hold, trust money of that trust (and no other money), and
  - (b) is segregated from any account holding money which is not trust money of that trust.
- (2) An account is not a client bank account if —
- (a) in the event of a failure of the licenceholder, it may be combined with any other account; or
  - (b) there is any right of set-off or counterclaim against it in respect of any debt owed by the licenceholder.

### **3.4 General restriction on holding client money or trust money**

(1) A licenceholder must not hold or receive client money or trust money except in accordance with the following provisions of this Part.

(2) This rule applies to a branch of a licenceholder in a country or territory outside the Island except —

- (a) the United Kingdom, or
- (b) a country or territory which the Commission has notified to the licenceholder for the purpose of this rule as a country offering equivalent protection,

as it applies to an establishment of the licenceholder within the Island.



## **Chapter 2 — Client money**

### **3.5 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5 in relation to such activities carried on in or from the Island.

### **3.6 Duty to hold client money separately**

- (1) Subject to paragraph (2), a licenceholder must pay all client money into either —
  - (a) a client bank account, or
  - (b) a bank account in the name of the client.
- (2) If a licenceholder is requested by a client to do so, it must pay client money of that client into a separate client bank account.
- (3) Client money must be held on trust for the client entitled to it.
- (4) Paragraphs (1) to (3) do not apply where —
  - (a) the licenceholder pays client money to, or by the written direction of, the client entitled to it; or
  - (b) client money is held or received in respect of a relevant agreement which is governed by a law other than the law of the Island, in which case the licenceholder must warn the client in writing that his money may not be protected as effectively as it would be if those paragraphs applied.

### **3.7 Designated accounts**

A licenceholder may, with the specific written consent of the client concerned, pay client money into a designated client bank account.

### **3.8 Notification of receipt of client money in certain cases**

- (1) A licenceholder who receives client money in circumstances in which it is not authorised by the terms of its licence to receive such money must immediately pay the money into a client bank account in accordance with rule 3.5.
- (2) The licenceholder must also, on the date of receipt or the next working day, notify the Commission of the facts, including —
  - (a) the reason for the receipt of the money,
  - (b) the action taken, and
  - (c) the arrangements for paying the client money out of the client bank account.

### **3.9 Account to be specified in cheques etc.**

- (1) This rule applies where money —

- (a) is or is to be paid to a licenceholder, and
  - (b) on receipt by the licenceholder is or will be client money.
- (2) The licenceholder must advise any person by whom the money is or is to be paid to make the relevant cheque or other instrument payable to either —
- (a) the client entitled to the money, or
  - (b) a payee designated as follows —
    - (i) "[licenceholder] – client account";
    - (ii) "[licenceholder] – designated client account"; or
    - (iii) "[licenceholder] – client account re [client]",as the case may be;
  - (c) in the case of an account in a country or territory outside the Island, a payee designated by such description in an official language of that country or territory as is equivalent to the appropriate wording in subparagraph (b).

### **3.10 Operation of client bank account**

- (1) A licenceholder must comply with the following requirements of this rule in relation to a client bank account.
- (2) The title of the client bank account must include —
- (a) the words "client account" or "designated client account" (as the case may be), or
  - (b) in the case of an account in a country or territory outside the Island, such description in an official language of that country or territory as is equivalent to those words.
- (3) Subject to paragraph (4), the bank at which the account is held must acknowledge to the licenceholder in writing that —
- (a) it understands that all money standing to the credit of all client bank accounts maintained by the licenceholder is held by it as trustee and that the bank is not entitled to combine the account with any other account or to exercise any right of set-off or counterclaim against money in that account in respect of any debt owed to it by the licenceholder;
  - (b) interest earned on each such account will be credited to the account or to an account of the same type;
  - (c) the title of each such account —
    - (i) is in the form requested by the licenceholder, and
    - (ii) sufficiently distinguishes the account from any other account containing money belonging to the licenceholder;

and the licenceholder must supply the Commission with a copy of the acknowledgement.

(4) In the case of an account in a country or territory outside the Island, the licenceholder must either —

- (a) ensure that the account is protected by segregation under trust or otherwise by statutory or other regulation, as effectively as it would be if held in a client bank account in the Island, or
- (b) warn the client in writing that his money may not be protected as effectively as it would be if it were so held.

(5) Except in the case of an account referred to in rule 3.16, the licenceholder must not allow a client bank account to become overdrawn.

(6) Subject to rule 3.26, the licenceholder must not pay money which is not client money, or permit such money to be paid, into a client bank account unless it is required —

- (a) to open or maintain the account; or
- (b) to restore an amount withdrawn in error from the account.

(7) If money paid to the licenceholder contains both client money and money which is not client money, the licenceholder must —

- (a) pay the money into a client bank account, and
- (b) as soon as the funds are cleared and the amount which is not client money is ascertained, withdraw that amount from the account.

(8) The licenceholder must not withdraw money from a client bank account unless —

- (a) it is not client money;
- (b) it is properly required for payment to or on behalf of a client; or
- (c) it is properly transferred to another client bank account or into a bank account in the client's own name.

(9) The licenceholder must not withdraw for its own account any interest earned on a client bank account which is due to a client under rule 3.14.

(10) The licenceholder must not withdraw money for or towards payment of its own fees or commission unless —

- (a) the withdrawal is in accordance with the terms of a relevant agreement; or
- (b) the amount is agreed by the client or finally determined by a court or arbitrator.

### **3.11 Records to be kept by licenceholder**

(1) The licenceholder must keep proper records of client money received, paid or held by it.

(2) The records must in particular contain —

- (a) a record of all receipts and payments, explaining their nature;
- (b) entries from day to day of all receipts and payments, including interest if applicable;

- (c) an up-to-date record of the balances on —
  - (i) all client bank accounts,
  - (ii) all accounts of the licenceholder with brokers and other persons (other than recognised banks) in which money is held which, if it were held by the licenceholder, would be client money; and
  - (iii) the licenceholder's ledger accounts relating to client money received, paid or held by it; and
- (d) such further details as are reasonably necessary to demonstrate compliance with the requirements of this Part.
- (3) The records must identify the client on behalf of whom any client money is received, paid or held.
- (4) Where appropriate, the records must also —
  - (a) disclose with reasonable accuracy, at any time, the details of transactions in respect of which client money is received, paid or held; and
  - (b) permit the tracing of money in and out of accounts referred to in paragraph (2)(c)(i) and (ii).
- (5) A licenceholder must preserve any records referred to in this rule for not less than 6 years.

### **3.12 Accounting for and use of client money**

- (1) A licenceholder must account properly and promptly for client money.
- (2) In particular, the licenceholder must ensure that —
  - (a) client money and other money do not become intermingled (except in accordance with rule 3.10(6) and (7));
  - (b) it can at all times be sure how much client money stands to the credit of each client; and
  - (c) money belonging to one client is not used for another (except in the case of an account maintained under rule 3.15(2)).

### **3.13 Reconciliation**

- (1) A licenceholder must, at least once a month —
  - (a) reconcile the balance on each client bank account, as recorded by the licenceholder, with the balance on that account as set out in the statement issued by the bank at which the account is held; and
  - (b) as at the same date used under sub-paragraph (a), reconcile the total of the balances on all client bank accounts (as recorded by the licenceholder) with the total of the corresponding credit balances in respect of each of its clients (as recorded by the licenceholder).
- (2) All client bank accounts must be reconciled to the same date.

(3) A reconciliation under paragraph (1) must be checked by an individual other than the person by whom it was carried out.

(4) The licenceholder must keep a record of every reconciliation under paragraph (1) and every check under paragraph (3).

(5) The licenceholder must correct immediately any discrepancies discovered on a reconciliation under paragraph (1) unless, in the case of paragraph (1)(a), they arise solely as a result of normal timing differences.

(6) The licenceholder must immediately notify the Commission, with details, where it has not carried out or is not able to carry out the reconciliation required by paragraph (1).

(7) The licenceholder must notify the Commission, with details, within 5 business days where it has completed the reconciliation required by paragraph (1) but —

- (a) it is not able to correct a discrepancy; or
- (b) more than 3 months after completion, a discrepancy has not been corrected.

### **3.14 Interest on client money**

(1) This rule does not apply in relation to regulated activities falling within Class 3.

(2) Where rule 6.38 (client agreement or terms of business) applies —

- (a) a licenceholder must pay interest on client money in accordance with the terms set out in the client agreement or terms of business referred to in that rule;
- (b) if no interest on client money is to be paid to the client, this must be clearly set out in the client agreement or terms of business.

(3) Where rule 6.38 does not apply, a licenceholder must disclose to a client how interest earned on client money is to be treated.

### **3.15 Accounts for margined transactions**

(1) This rule applies only to licenceholders licensed to carry on regulated activities falling within Class 2; and the foregoing provisions of this Part are subject to the provisions of this rule.

(2) Where margined transactions are undertaken, a licenceholder must maintain a client bank account or accounts —

- (a) specially created for the purpose of holding margined client money, and
- (b) segregated from any account holding any other client money.

(3) Subject to paragraph (4), a licenceholder must hold any margined client money in a client bank account referred to in paragraph (2), and no other money may be held in such an account.

(4) When a licenceholder undertakes margined transactions with or for a client under the rules of an exchange and in the types of contracts traded on that exchange, the licenceholder may, instead of paying margined client money into a client bank account, pay it to the exchange or an intermediate broker to be credited to the licenceholder's client account with the exchange and to be dealt with in accordance with its rules and regulations.

(5) The licenceholder may withdraw money from a client bank account referred to in paragraph (2) where it is properly payable to an exchange, an intermediate broker or the licenceholder's client account with an exchange.

(6) A licenceholder must hold in such an account initial margins calculated in accordance with paragraph (7) on each client's positions (not on the overall net position across all clients).

(7) For the purpose of paragraph (6) the initial margin to be held for any client at any time is the total amount which, under the rules of the relevant exchange, the licenceholder or intermediate broker would be required to deposit in cash or approved collateral as a fidelity deposit in respect of all that client's open positions in margined transactions at that time, irrespective of any unrealised profit or loss on such positions.

(8) Where —

- (a) margins required by an exchange or intermediate broker in respect of any one client have not been received from the client, and
- (b) the licenceholder does not pay the required amount direct to the exchange or broker,

the licenceholder must itself pay the required amount into the relevant client bank account.

(9) A licenceholder must ensure that, on each business day, A is not less than B where —

A = the total, as at the close of business on the immediately preceding business day, of —

- (a) the aggregate of the balances on all the licenceholder's client bank accounts referred to in paragraph (2);
- (b) the net aggregate of the licenceholder's equity balances with exchanges and with intermediate brokers; and
- (c) the value of approved collateral deposited with the licenceholder, whether held by it or by an intermediate broker;

B = the aggregate of the required contributions of all the licenceholder's clients as at the close of business on the immediately preceding business day.

(10) In this rule —

a client's "equity balance" with a licenceholder at any time is the amount which —

- (a) the licenceholder would be liable to pay to the client, or
- (b) the client would be liable to pay to the licenceholder,

in respect of his margined transactions if each of his open positions were liquidated at the closing or settlement prices, and a licenceholder's "equity balance" with an exchange or with an intermediate broker has a corresponding meaning;

"margined client money" means client money held or received for the purpose or in the course of a margined transaction;

"margined transaction" means a transaction effected by a licenceholder with or for a client relating to an option, future or contract for differences under the terms of which the client will or may be liable to make deposits in cash or collateral to secure the performance of obligations which he may have to perform when the transaction falls to be completed or upon the earlier closing out of his position;

"option", "future" and "contract for differences" mean investments falling within paragraphs (g), (h) and (i) respectively of the definition of "investment" in Schedule 2 to the Regulated Activities Order 2008;

a client's "required contribution" is the greater of —

- (a) the amount of the client's initial margin at that time, calculated in accordance with paragraph (7); and
- (b) the aggregate of the client's equity balance at that time and the amount of the value of the approved collateral which the client has provided to the licenceholder.

### **3.16 Accounts for client settlement money**

(1) This rule applies only to licenceholders licensed to carry on regulated activities falling within Class 2.

(2) A licenceholder may not operate a separate bank account in which is held at any time the net balance required for the settlement of transactions ("clients' settlement money") —

- (a) without the consent of the Commission, or
- (b) otherwise than in accordance with such conditions as the Commission may impose.

### **3.17 Subscription and redemption accounts**

(1) This rule applies only to licenceholders licensed to carry on regulated activities falling within Class 3.

(2) Where a licenceholder holds money in respect of the sale or redemption of units in a collective investment scheme, the money must be held in a subscription account or a redemption account, as the case may be.

(3) In this rule "subscription account" and "redemption account" mean a client bank account which is segregated from any account holding money which is not held in respect of the sale or redemption, as the case may be, of units in —

- (a) the scheme in question, or
- (b) another scheme managed or administered by the same person.

### **Chapter 3 — Purposes for which client money is held**

#### **3.18 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2 or Class 3 in relation to such activities carried on in or from the Island.

#### **3.19 Trusts of client money**

Client money held by a licenceholder is held on trust —

- (a) on the terms and for the purposes set out in this Part and, subject thereto, *pari passu* for the respective clients for whom it is received or held;
- (b) subject to sub-paragraph (a), *pari passu* in meeting any shortfall in valid claims by clients to client money (disregarding rules 3.20 to 3.22 for this purpose); and
- (c) after all valid claims under sub-paragraphs (a) and (b) have been met, for the licenceholder itself.

#### **3.20 Pooling**

(1) For the purpose of rule 3.18(a), in determining the entitlement of clients to client money, all client money, even though held in more than one client bank account, shall be treated as pooled except as provided in rules 3.21 and 3.22.

(2) Where, at the time at which a default occurs, cheque or other payable order has been paid into a client bank account but has not been cleared, the amount of the order shall, when it is cleared, be pooled in accordance with this Chapter.

(3) For the purpose of this rule and rules 3.21 to 3.23 a licenceholder or bank is in default where —

- (a) a liquidator, receiver, administrator or trustee in bankruptcy has been appointed in respect of it;
- (b) any equivalent procedure has occurred in respect of it in a country or territory outside the Island and the United Kingdom; or
- (c) the Commission has directed that it shall be treated as in default for the purpose of this Chapter (in the case of a bank, either generally or in relation to the licenceholder in question).

#### **3.21 Default of bank — designated client bank accounts**

(1) This rule applies where client money held by a licenceholder is insufficient to pay the claims of all clients because a bank in which client money is held is in default.

(2) Where client money is held in a designated client bank account at the bank in default —



- (a) that money shall not be pooled with client money held in any other client bank account; and
- (b) a client or clients to whose credit any amount stands in that account —
  - (i) shall be entitled to claim (*pari passu* if more than one) against the money in that account in respect of that amount; but
  - (ii) shall not be entitled to claim against any other client bank account (at that or any other bank) in respect of that amount.
- (3) Where client money is held in a designated client bank account at a bank other than the bank in default, that money shall not be pooled with client money held in any other client bank account (at that or any other bank).

### **3.22 Money held in overseas bank**

(1) Where client money held by a licenceholder is insufficient to pay the claims of all clients because a bank outside the Island and the United Kingdom in which client money is held does not recognise that money in the account is held in accordance with this Part —

- (a) all client money held in the licenceholder's client bank accounts with that bank shall be pooled and made available to satisfy the claims of clients whose money was held or which should have been held in a client bank account with that bank; and
- (b) that client money shall not be treated as pooled with client money held in the licenceholder's client bank account or accounts with any other bank.

(2) Where client money held by a licenceholder is insufficient to pay the claims of all clients because a bank outside the Island and the United Kingdom in which client money is held is in default —

- (a) all client money held in the licenceholder's client bank accounts outside the Island and the United Kingdom with that bank shall be pooled and made available to satisfy the claims of clients whose money was held or which should have been held in a client bank account outside the Island and the United Kingdom with that bank; and
- (b) that client money shall not be treated as pooled with clients' money held in other client bank accounts of the licenceholder.

### **3.23 No withdrawal in case of default**

- (1) In the case of default by —
  - (a) a licenceholder, or
  - (b) a bank at which a client bank account of the licenceholder is held,

no money may be withdrawn from any client bank account of the licenceholder without the consent of the Commission.

(2) In the case of default by a bank, paragraph (1) does not apply to withdrawal from —

- (a) a designated client bank account at another bank;

- (b) a client bank account (other than a designated client bank account), where no such account is held at the bank which is in default.

(3) Paragraph (1) does not apply to any step taken by the licenceholder in good faith which he reasonably believes will preserve or enhance the fund of client money available despite the default.

### **3.24 Displacement of general law**

The duties of a licenceholder under this Part in relation to client money shall take the place of the corresponding duties which would be owed by it as a trustee under the general law, but without prejudice to the remedies available to clients.

## ***Chapter 4 — Trust money***

### **3.25 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 5 in relation to such activities carried on in or from the Island.

### **3.26 Duty to hold trust money separately**

A licenceholder must pay trust money into either —

- (a) a trust bank account, or
- (b) if, and only if, circumstances make it impractical to set up a separate account for the trust in question, a client bank account.

### **3.27 Operation of trust bank account**

The title of a trust bank account must clearly —

- (a) show that it is held by the trustee in his capacity as trustee, and
- (b) identify the trust to which it relates.

### **3.28 Accounting for and use of trust money**

- (1) A licenceholder must account properly and promptly for trust money.
- (2) In particular, the licenceholder must ensure that —
  - (a) trust money and other money do not become intermingled (except in accordance with rule 3.26(b)); and
  - (b) it can at all times be sure how much trust money stands to the credit of each trust.
- (3) Rules 3.10 to 3.14 apply to trust money paid into a client account in accordance with rule 3.26(b) as they apply to client money with the substitution, for references to a client, of references to the trust concerned or to the trustees of that trust, as the case may require.

### **3.29 Reconciliation**

(1) A licenceholder must, at least once a month, or at such other intervals as the trustee may direct, reconcile the balance on each trust bank account, as recorded by the licenceholder, with the balance on that account as set out in the statement issued by the bank at which the account is held.

(2) A reconciliation under paragraph (1) must be checked by an individual other than the person by whom it was carried out.

(3) The licenceholder must keep a record of every reconciliation under paragraph (1) and every check under paragraph (2).

(4) The licenceholder must correct immediately any discrepancies discovered on a reconciliation under paragraph (1) unless they arise solely as a result of normal timing differences.

(5) The licenceholder must immediately notify the Commission, with details, where —

- (a) it has not carried out or is not able to carry out the reconciliation required by paragraph (1), or
- (b) it has completed the reconciliation but —
  - (i) is not able to correct any discrepancy, or
  - (ii) more than 3 months after completion, a discrepancy has not been corrected.

## PART 4 — CLIENTS' INVESTMENTS

### *Chapter 1 — General*

#### **4.1 Application to investment businesses**

This Part applies to all licenceholders licensed to carry on regulated activities falling within Class 2 in relation to such activities carried on in or from the Island.

#### **4.2 Application to CIS service providers**

This Part applies to a licenceholder licensed to carry on an activity falling within paragraph (1), (2), (3), (4), (5), (11) or (12) of Class 3 in relation to such activities carried on in or from the Island as it applies to a licenceholder referred to in rule 4.1, with any necessary modifications, as if —

- (a) references to a client were references to a collective investment scheme, or to a participant in such a scheme, as the case may require (but so that each such scheme shall be treated as a separate client);
- (b) references to a client's investments were to investments which are assets of such a scheme;
- (c) references to safe-custody services were to those activities, so far as they relate to the custody of assets of such a scheme; and
- (d) references to an eligible custodian were to a licenceholder licensed to carry on an activity falling within paragraph (3), (4) or (5) of Class 3.

#### **4.3 Interpretation**

- (1) In this Part —

"eligible custodian" means (subject to rule 4.2(d)) —

- (a) a licenceholder licensed to carry on safe-custody services;
- (b) the licenceholder's own custodian; or
- (c) a person carrying on business in a country or territory outside the Island —
  - (i) whose business includes the provision of services which, if carried on in the Island, would be safe-custody services, and
  - (ii) who the licenceholder reasonably believes is subject to regulation and supervision in relation to those services by a regulatory body or agency of government in that country;

"investment" means any of the following (as defined in the Order) —

- (a) a share;
- (b) a debenture;
- (c) a government security;
- (d) a warrant;

- (e) a certificate representing securities;
- (f) a unit in a collective investment scheme, including a share in, or security of, an open-ended investment company;

"registrable investment" means an investment the title to which is entered in a register;

"safe-custody services" means (subject to rule 4.2(c)) services consisting of regulated activities falling within paragraph (5) of Class 2 (safeguarding and administering investments under a contractual relationship);

"title document" means —

- (a) a share certificate or stock certificate; and
- (b) any other document which is evidence of title to an investment.

(2) In this Part references to documents in the possession or under the control of a licenceholder include documents which —

- (a) are in the possession or under the control of the licenceholder's own custodian, or
- (b) at the request of the licenceholder are in the possession or under the control of any other eligible custodian.

(3) In this Part a reference to a licenceholder's own custodian is to a wholly-owned subsidiary of the licenceholder which —

- (a) carries on no other business than providing safe-custody services, and
- (b) acts only in accordance with the directions or instructions of the licenceholder.

#### **4.4 Records of transactions**

(1) A licenceholder must maintain records containing entries of all purchases and sales of, and other transactions relating to, an investment which the licenceholder undertakes on behalf of a client, including —

- (a) the nature and amount of the investment;
- (b) the identity of the client;
- (c) the nature of the transaction;
- (d) the time and date of the transaction; and
- (e) the identity of any intermediary who handled the transaction.

(2) The records referred to in paragraph (1) must enable investments to which they relate to be traced into and out of brokerage accounts.

(3) A licenceholder must preserve any records referred to in this rule for not less than 6 years.

## Chapter 2 — Safe-custody services

### 4.5 Records of safe-custody investments

- (1) A licenceholder must maintain such records as are necessary to identify —
  - (a) every investment in relation to which it provides safe-custody services,
  - (b) the client to whom that investment belongs; and
  - (c) where the title to the investment is in documentary form, the location of every title document relating to the investment;
  - (d) where the title to the investment is in electronic form, the form and location of any record of the title;
  - (e) where the investment is a registrable investment, the registrar and the person in whose name it is registered.
- (2) Where an investment referred to in paragraph (1)(a), or a title document relating to such an investment, is held for the licenceholder by an eligible custodian, the licenceholder must —
  - (a) maintain such records as are necessary to enable it to ascertain which custodian is holding the investment or document, and
  - (b) ensure that the custodian maintains the records referred to in paragraph (1) in relation to the investment or document.
- (3) A licenceholder must preserve any records referred to in this rule for not less than 6 years.

### 4.6 Use of custodians

- (1) A licenceholder must not —
  - (a) recommend to a client that a person other than the licenceholder undertake safe-custody services for the client, or
  - (b) procure the client's agreement to such a person so acting;unless that person is an eligible custodian.
- (2) Where a licenceholder arranges for any safe-custody services to be provided by the licenceholder's own custodian, the licenceholder must ensure that the custodian complies with rules 4.7 to 4.14.
- (3) Where a licenceholder arranges for any safe-custody services to be provided by an eligible custodian other than the licenceholder's own custodian, the licenceholder must comply with paragraphs (4) and (5).
  - (4) The licenceholder must —
    - (a) exercise reasonable skill, care and diligence in the selection of the custodian, and
    - (b) must, so long as the arrangement is in force, satisfy itself that the custodian continues to be suitable (including obtaining confirmation that it continues to be an eligible custodian).

- (5) The licenceholder must also ensure that the custodian has acknowledged in writing to the licenceholder that —
- (a) it will not have or claim any right to sell or pledge the client's investment or any lien or right of retention over any title document relating to it;
  - (b) it will not part with possession of any such title document otherwise than to the licenceholder or on the licenceholder's instructions;
  - (c) it will hold any such document so that it is readily apparent that the investment to which it relates does not belong to the custodian, the licenceholder or an associate of the licenceholder or custodian; and
  - (d) it will, not less than once every 6 months and at other times on the request of the licenceholder, prepare and deliver to the licenceholder a statement, made up as at a date specified by the licenceholder (being a date not earlier than 4 weeks before the statement is delivered), specifying in relation to each description of investment —
    - (i) the investments held by the custodian for the licenceholder;
    - (ii) the title documents relating to those investments which are held by the custodian; and
    - (iii) in the case of registrable investments, the amount so held in each different name or designation;
  - (e) it will not arrange for any safe-custody services to be provided on its behalf by any person other than an eligible custodian.

#### **4.7 Registrable investments**

- (1) Where a licenceholder provides safe-custody services relating to a registrable investment of a client, it must arrange that the investment is registered —
- (a) in the name of the client, or
  - (b) with the consent of the client, in the name of an eligible custodian.
- (2) Where the licenceholder's own investment and a client's investment are registered in the same name, the licenceholder must —
- (a) secure that the client's investment is registered in a designated account different from the account in which the licenceholder's investment is registered; and
  - (b) where appropriate, hold separate certificates evidencing the title to the licenceholder's own investment and the title to the client's investment.

#### **4.8 Reconciliation of investments and title documents**

- (1) A licenceholder which provides safe-custody services in relation to a client's investments must —
- (a) reconcile its books and records at 2 dates during every year, not more than 8 months nor less than 4 months apart; and
  - (b) promptly correct any discrepancies which are revealed.

- (2) The reconciliation referred to in paragraph (1) must comprise the following steps in respect of the client's investments —
- (a) the physical counting and inspection of all title documents relating to the investments which are in the possession or under the control of the licenceholder, or a check of the electronic records referred to in rule 4.5(1)(d) and relating to the investments, as the case may require; and
  - (b) a check of all records maintained by the licenceholder under rule 4.5 against those title documents or electronic records;
  - (c) obtaining a written statement (in the form specified in rule 4.6(5)(d)) from any custodian other than the licenceholder's own custodian of the investments held by it on behalf of the licenceholder.
- (3) A licenceholder must carry out the reconciliation required by paragraph (1) not later than the end of 3 months from the date at which the count or check referred to in paragraph (2)(a) was carried out.
- (4) In carrying out the reconciliation the licenceholder must —
- (a) in every case, reconcile the results with its own records in respect of each client;
  - (b) in the case of a registrable investment, reconcile any discrepancy revealed by (a) above with the records of the registrar of the investment; and
  - (c) in the case of documents held by a custodian other than the licenceholder's own custodian, reconcile the statement received with the licenceholder's own records in respect of each client.
- (5) The licenceholder must —
- (a) ensure that the counting and reconciliation of title documents required by this rule are —
    - (i) carried out, or observed and reviewed, by persons who are not responsible for the origination or maintenance of the licenceholder's records, and
    - (ii) supervised by a responsible officer; and
  - (b) retain for not less than 6 years all working papers which have been created to assist in the reconciliation.
- (6) The reconciliation may be undertaken by either —
- (a) the total check method (see paragraph (7)), or
  - (b) with the consent of the Commission, the rolling stock check method (see paragraph (8)).
- (7) The total check method requires the steps referred to in paragraph (2) to be taken in respect of all the client's investments.
- (8) The rolling stock check method requires the steps referred to in paragraph (2) to be taken in respect of the client's investments of a particular description, so that those steps are taken in respect of all the client's investments on a rolling basis within every period of 6 months.



(9) The Commission shall not consent to the use of the rolling stock check method unless it is satisfied, on the basis of a report from the licenceholder's auditors, that the licenceholder has in place a system of internal control which is adequate to ensure as far as reasonably practicable that an up-to-date record is maintained of all clients' investments in respect of which the licenceholder provides safe-custody services.

(10) The licenceholder must immediately notify the Commission, with details, where —

- (a) it has not carried out or is not able to carry out the reconciliation required by paragraph (1), or
- (b) it has completed the reconciliation but —
  - (i) is not able to correct any discrepancy, or
  - (ii) more than 6 months after completion, a discrepancy has not been corrected.

#### **4.9 Periodical statements**

(1) Unless expressly instructed to the contrary in writing by the client, a licenceholder must, every 6 months or, if the client's holding is unchanged, every year, provide to each client for whom it provides safe-custody services a statement of the investments to which those services relate.

- (2) A statement under paragraph (1) must —
  - (a) be provided to the client within 6 weeks of the date as at which it is made; and
  - (b) distinguish between investments held —
    - (i) by the licenceholder;
    - (ii) by the licenceholder's own custodian; and
    - (iii) by an eligible custodian other than the licenceholder or the licenceholder's own custodian.

(3) Where the licenceholder provides safe-custody services in respect of that client's investments and also manages that client's investments, the statement must also distinguish between —

- (a) investments in respect of which it provides safe-custody services and which it manages, and
- (b) investments in respect of which it provides safe-custody services but which it does not manage.

(4) The references in paragraph (3) to managing investments are to carrying on an activity falling within paragraph (4) of Class 2 in relation to those investments.

(5) The licenceholder must immediately notify the Commission, with details, where it has not provided or is not able to provide a statement to a client within the time required by paragraph (2)(a).

#### 4.10 Borrowing from a client

A licenceholder must not borrow, or permit any director or employee or a relative or associate of a director or employee of the licenceholder to borrow, any investment from a client.

#### 4.11 Loans of investments

(1) A licenceholder must not lend a client's investment, or any title document relating to a client's investment, to any person unless —

- (a) the Commission has given its prior written consent to the lending of clients' investments by the licenceholder;
- (b) the client —
  - (i) has been made aware of any effect of the transaction on his interests,
  - (ii) has been recommended to seek advice on his rights in relation to the investment and his tax position, and
  - (iii) has expressly agreed in writing to the loan;
- (c) the terms of the loan are set out in —
  - (i) a written agreement between the licenceholder and the client; and
  - (ii) a written agreement between the licenceholder and the borrower; and
- (d) the loan is authorised in writing by a key person approved for the purpose by the directors of the licenceholder.

(2) Where a licenceholder lends such an investment or document to any person, it must maintain a record stating —

- (a) a description (including the amount and value) of the investment;
- (b) the nature of the transaction or other purpose for which the loan is made;
- (c) the remuneration (if any) payable to the licenceholder in respect of the transaction;
- (d) the remuneration payable to the client in respect of the transaction;
- (e) the identity of the borrower;
- (f) the nature and value of any security provided by the borrower; and
- (g) in the case of a title document —
  - (i) a description of the document;
  - (ii) the date when the document left the possession or control of the licenceholder;
  - (iii) whether the borrower confirmed receipt of the document; and

- (iv) the date when it came back into the possession or control of the licenceholder.
- (3) While any loan is outstanding, the licenceholder must keep under review —
  - (a) the level of exposure of the parties to the transaction,
  - (b) the risk of default by the borrower,
  - (c) the value of any security referred to in paragraph (2)(f), and
  - (d) any effect of the transaction on the interests of the client (in particular the matters referred to in paragraph (1)(b)(i)).

#### **4.12 Investments etc. held as collateral**

(1) For the purpose of this rule a licenceholder holds a client's investment, or a title document relating to a client's investment, as collateral if with the written consent of the client he holds it as security for money which is due or may become due to the licenceholder from the client or any other person.

(2) Where a licenceholder holds a client's investments, or title documents relating to a client's investments, some (but not all) of which are held as collateral, the investments or documents which are held as collateral must be identified in the licenceholder's records as so held and distinguished from those which are not so held.

(3) The licenceholder must not, without the prior written consent of the client, return to the client an investment or title document other than the original investment or title document held as collateral; but this paragraph does not preclude the licenceholder returning the collateral in the form of cash where the investment matures.

(4) The licenceholder must not, without the prior written consent of the client, use an investment or title document held as collateral for the purpose of security for —

- (a) the licenceholder's own obligations; or
- (b) the obligations of another customer or person.

### ***Chapter 3 — Safekeeping of title documents***

#### **4.13 Safekeeping of clients' title documents**

- (1) Where a title document relating to a client's investment is in the possession or under the control of a licenceholder, it must —
- (a) maintain a record of the location of the document;
  - (b) take all proper steps to preserve the document, taking no less care of it than it ought to take if the document related to its own investment; and
  - (c) continue to comply with sub-paragraphs (a) and (b) until the document is delivered to the client or, on the instruction of the client, to another person (other than the licenceholder's own custodian).
- (2) In particular —

- (a) the licenceholder must not part with possession of the document to any person other than the client except —
  - (i) on the client's instructions,
  - (ii) in accordance with the terms of any written agreement with the client; or
  - (iii) pursuant to a requirement of a court of competent jurisdiction or other lawful demand;
- (b) the document shall be held so that it is readily apparent that the investment to which it relates does not belong to the licenceholder or to an associate of the licenceholder;
- (c) the document must be segregated from title documents relating to investments of persons other than that client;
- (d) a bearer document must be kept in locked custody with 2 or more keys or combination locks (or both) required to enter any particular stronghold, each key or combination to be held or controlled by a separate individual; and
- (e) the licenceholder must maintain a system of internal control over access to the document.

#### **4.14 Safekeeping by other persons**

(1) A licenceholder may not, without the consent in writing of the client, arrange for a title document relating to a client's investment to be kept by a person other than the licenceholder.

(2) Where a licenceholder arranges for a title document relating to a client's investment to be kept by a person other than the licenceholder, the licenceholder must ensure that that person complies with the requirements of rule 4.13 as though —

- (a) those rules applied to that person; and
- (b) the references to the licenceholder were references to that person.

## PART 5 — AUDIT

### *Chapter 1 — General requirements for licenceholders incorporated in the Island*

#### **5.1 Application**

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Chapter applies to all licenceholders incorporated in the Island.

#### **5.2 Appointment of auditors**

(1) A licenceholder must have at all times an auditor who is qualified, and is not ineligible, to act as such.

(2) For the purpose of this rule, a person is qualified to act as an auditor of a licenceholder if, and only if, he —

- (a) is a member of, and holds a current practising certificate issued by, one or more of the following bodies —
  - (i) the Institute of Chartered Accountants in England and Wales;
  - (ii) the Institute of Chartered Accountants of Scotland;
  - (iii) the Institute of Chartered Accountants in Ireland; or
  - (iv) the Association of Chartered Certified Accountants; and
- (b) has a permanent place of business on the Island;
- (c) is covered by an appropriate level of professional indemnity insurance suitable to the licenceholder being audited; and
- (d) in the case of a licenceholder which is a company, he is not disqualified for appointment as auditor of the licenceholder by section 14 of the Companies Act 1982.

(3) For the purpose of this rule, a person is ineligible to act as an auditor of a licenceholder if —

- (a) in the case of an individual, he is —
  - (i) a director, partner, controller, officer, tied agent or employee of the licenceholder;
  - (ii) a partner of, or in the employment of, any person falling within (i) above; or
  - (iii) a close relative of any person falling within (i) above;
  - (iv) not treated as independent of the licenceholder under any code of ethics issued from time to time by the body of accountants of which he is a member; or

- (v) declared by the Commission to be ineligible to act as an auditor of the licenceholder, of any description of licenceholders which includes the licenceholder or of licenceholders generally;
- (b) in the case of a firm —
  - (i) it is declared by the Commission to be ineligible to act as an auditor of the licenceholder, of any description of licenceholders which includes the licenceholder or of licenceholders generally; or
  - (ii) the principal directly responsible in the firm for the audit of the licenceholder falls within sub-paragraph (a)(i), (ii), (iii), (iv) or (v).
- (4) For the purpose of paragraph (3) —
  - (a) an individual is not to be treated as an officer or employee of a licenceholder by reason only of being auditor of that licenceholder;
  - (b) "close relative", in relation to an individual, means a spouse, parent, step-parent, brother, sister, half-brother, half-sister, child or step-child, or a person, whether or not of the opposite sex, living with the individual in a relationship similar to that of husband and wife.

### **5.3 Suitability of auditor**

- (1) Before appointing a person as its auditor, a licenceholder must ensure that that person is qualified, and is not ineligible, to act as such.
- (2) A licenceholder must on request provide the Commission with evidence of the resources, knowledge, experience and competence of —
  - (a) its auditor, or
  - (b) any person whom it intends to appoint as its auditor.
- (3) If the Commission reasonably believes that a person —
  - (a) does not have sufficient resources, knowledge, experience and competence to perform the duties of the auditor of the licenceholder under this Part, or
  - (b) is otherwise incapable of performing those duties, or
  - (c) is otherwise unsuitable to be the auditor of the licenceholder,

the Commission may declare that that person is ineligible to act as auditor of the licenceholder.

### **5.4 Requirements for auditors**

- (1) Where the same firm carries out the internal and external audits of a licenceholder, different partners or directors must be responsible for these audits.
- (2) In this rule —

"external audit" means any audit of the licenceholder for the purpose of this Part, Part I of the Companies Act 1982 or any other statutory provision;

"internal audit" means any audit of the licenceholder carried out by it or at its request, except an external audit.

## **5.5 Engagement letter**

- (1) Before the commencement of the appointment of an auditor, a licenceholder must obtain from the auditor an engagement letter —
  - (a) containing an undertaking by the auditor to provide the licenceholder and the Commission with the reports and letters required by this Part;
  - (b) defining clearly the extent of the rights and duties of the auditor; and
  - (c) signed and accepted in writing by or on behalf of both the licenceholder and the auditor.
- (2) For the purpose of this Part a licenceholder is not to be treated as having an auditor unless an engagement letter complying with paragraph (1) has been obtained and is still in force.
- (3) A licenceholder must provide a copy of the engagement letter to the Commission on request.

## **5.6 Audit of annual financial statements**

- (1) A licenceholder must require that its annual financial statements are audited by its auditor in accordance with —
  - (a) the International Standards on Auditing issued from time to time by the International Auditing Practices Committee, or
  - (b) the International Standards on Auditing (UK and Ireland) issued from time to time by the Auditing Standards Board in the United Kingdom.
- (2) The licenceholder must submit its audited annual financial statements to the Commission not later than 4 months after its annual reporting date.

## **5.7 Notification**

- (1) A licenceholder must notify the Commission immediately on —
  - (a) the appointment of an auditor, and
  - (b) the removal or resignation of an auditor, and the reasons for it.
- (2) Where an auditor resigns or is removed by the licenceholder or is not reappointed at the end of his term in office, the licenceholder must provide the Commission with a statement signed by the auditor stating either —
  - (a) that there are no circumstances connected with his ceasing to hold office which the auditor considers should be brought to the attention of the Commission; or
  - (b) the circumstances connected with his ceasing to hold office which are required to be reported to the Commission under section 17 of the Act.
- (3) A licenceholder must notify the Commission immediately where —

- (a) its auditor has qualified his report on the annual financial statements of the licenceholder, or
- (b) it has reason to believe that its auditor is likely to qualify that report.

### **5.8 Management letter**

- (1) A licenceholder must —
  - (a) provide the Commission with a copy of any management letter which —
    - (i) the licenceholder receives from its auditor in respect of the audit of its annual financial statement, and
    - (ii) contains any recommendations to the licenceholder to remedy any weakness in its systems and internal controls of the licenceholder; and
  - (b) inform the Commission whether the licenceholder has implemented or is implementing those recommendations, and if not, its reasons for not doing so.
- (2) Where the licenceholder receives no such management letter from its auditor, it must provide the Commission with a copy of the auditor's letter confirming that no such management letter has been or will be issued.
- (3) A licenceholder must provide the Commission with a copy of the report made by its auditor pursuant to International Standard on Auditing (ISA) 260.
- (4) The licenceholder must comply with the requirements of paragraph (1) not later than 4 months after its annual reporting date.

### **5.9 Rights of auditor**

- (1) A licenceholder must afford its auditor —
  - (a) the right of access at all times to its accounting and any other records relevant to the auditor's duties, and
  - (b) the right to obtain from the officers, controllers and managers of the licenceholder such information and explanations as the auditor may consider necessary in the performance of his duties.
- (2) A licenceholder must permit and require his auditor to provide to the Commission such information and opinions as the Commission requests, being information or opinions relevant to the functions of the Commission.

### **5.10 Contents of audit reports**

- (1) The auditor's report on the annual financial statements of a licenceholder must state whether, to the best of the auditor's knowledge and belief —
  - (a) the statements have been properly prepared in accordance with Part 2;
  - (b) the balance sheet and profit and loss account are in agreement with the licenceholder's accounting records; and



- (c) proper accounting records appropriate to the licenceholder's business have been maintained throughout the financial year to which the statements relate.
- (2) Where the licenceholder is part of a group subject to a group audit, the auditor's report must be signed by the Isle of Man office of the auditor.

### **5.11 Meaning of 'auditor' for purposes of section 17 of Act**

The auditor of a permitted person for the purpose of section 17 of the Act (reports to Commission) is —

- (a) in the case of a licenceholder, any person appointed as its auditor in accordance with Chapter 1 of Part 5;
- (b) in any other case, any person by whom the accounts of or relating to the permitted person are audited (whether for the purposes of the Companies Act 1982 or otherwise); and
- (c) in any case, any accountant (not being an employee of the permitted person) who is in any way concerned in the keeping of the accounting records, or the preparation or audit of the accounts, of or relating to the permitted person.

## **Chapter 2— General requirements for licenceholders incorporated outside the Island**

### **5.12 Application**

- (1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.
- (2) Subject to paragraph (1), this Chapter to all licenceholders which are incorporated outside the Island.

### **5.13 Appointment of auditors**

- (1) A licenceholder must have at all times an auditor who is qualified, and is not ineligible, to act as such.
- (2) For the purpose of this rule, a person is qualified, and is not ineligible, to act as an auditor of a licenceholder if, and only if, he complies with whichever of the following conditions is applicable —
  - (a) where the licenceholder is required to have an auditor by the law of the country or territory in which it is incorporated, he is qualified under that law to act as an auditor of the licenceholder; or
  - (b) where the licenceholder is not required to have an auditor by that law, he is qualified, and is not ineligible, under rule 5.2 (except paragraph (2)(c)) to act as an auditor of a licenceholder incorporated in the Island.
- (3) A licenceholder must notify the Commission forthwith of —
  - (a) the appointment of an auditor, and
  - (b) the removal or resignation of an auditor, and the reasons for it.

(4) Where the licenceholder is not required to have an auditor by the law of the country or territory in which it is incorporated, rules 5.4, 5.5, 5.7 5.9 and 5.10 apply as if the licenceholder were incorporated in the Island.

#### **5.14 Management letter**

- (1) A licenceholder must —
- (a) provide the Commission with a copy of any management letter which, in respect of operations in the Isle of Man —
- (i) the licenceholder receives from its auditor in respect of the audit of any of its annual financial statements, and
- (ii) contains any recommendations to the licenceholder to remedy any weakness in its systems and internal controls of the licenceholder; and
- (b) inform the Commission whether the licenceholder has implemented or is implementing those recommendations, and if not, its reasons for not doing so; or
- (c) where the auditor states that is not issuing a management letter in respect of operations in the Isle of Man, provide the Commission with a copy of the auditor's letter confirming this fact.
- (2) The licenceholder must comply with the requirements of paragraph (1) not later than 4 months after its annual reporting date.

### ***Chapter 3 — Specific requirements for all deposit takers***

#### **5.15 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 1.

#### **5.16 Auditor's report on returns**

- (1) In connection with the audit of a licenceholder's annual financial statements, the licenceholder must secure that the auditor —
- (a) verifies one quarter's set of deposit-taking returns, as submitted to the Commission during that period in accordance with rule 2.24 or 2.28, against the licenceholder's accounting records, and
- (b) reports his findings in writing to the licenceholder.
- (2) The set of returns selected for the purpose of paragraph (1) must not be for a quarter the end of which coincides with the licenceholder's annual reporting date.
- (3) The licenceholder must provide the Commission with a copy of the auditor's report under paragraph (1)(b).
- (4) Where the auditor's report under paragraph (1)(b) identifies exceptions, the licenceholder must provide the Commission with its written comments on them when it submits the auditor's report to the Commission.

- (5) The licenceholder must comply with the requirements of paragraphs (3) and (4) not later than 4 months after its annual reporting date.

***Chapter 4 — Specific requirements for deposit takers incorporated in the Island***

**5.17 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 1 which are incorporated in the Island.

**5.18 Contents of audit reports**

(1) In connection with the audit of a licenceholder's annual financial statements for any accounting period, the licenceholder must provide the Commission with a letter from its auditor confirming that to the best of the auditor's knowledge and belief it has in that period complied with —

- (a) rule 2.14 (retention of accounting records),
- (b) rule 2.22 (charges on assets), and
- (c) rule 2.23 (capital resources).

(2) The licenceholder must comply with the requirements of paragraph (1) not later than 4 months after the end of the period in question.

***Chapter 5 — Specific requirements for investment businesses and CIS service, corporate service and trust service providers (except professional officers)***

**5.19 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5, other than individuals licensed to carry on only activities falling within either or both of —

- (a) paragraph (6) of Class 4 (acting as officer of company), and
- (b) paragraph (2) or (5) of Class 5 (acting as trustee or protector).

**5.20 Contents of audit report**

The auditor of a licenceholder must make a report on its annual financial statements which must —

- (a) be addressed to the Commission, and
- (b) state whether in the auditor's opinion —
  - (i) any general or specific requirements of Part 2 applicable to the statements are complied with;
  - (ii) the reconciliation required by rule 2.40(1)(c) has been prepared compiled in accordance with that rule;
  - (iii) the licenceholder's financial resources have been properly calculated in accordance with Part 2;

- (iv) the licenceholder has maintained throughout the period to which the statements relate systems adequate to enable it to comply with Parts 3 and 4 and complied with those Parts at the balance sheet date; and
- (v) reconciliations of clients' money and clients' investments have been performed in accordance with Parts 3 and 4.

## PART 6 — CONDUCT OF BUSINESS

### *Chapter 1 — General requirements for all licenceholders*

#### **6.1 Application**

- (1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.
- (2) Subject to paragraph (1), this Chapter applies to all licenceholders.

#### **6.2 Skill, care and diligence**

A licenceholder must act with due skill, care and diligence in carrying on regulated activities.

#### **6.3 Responsible behaviour in dealings by officers etc.**

A licenceholder must have procedures for ensuring that, where any regulated activity is carried on by any of its officers or employees, the officer or employee —

- (a) does so openly and fairly,
- (b) complies with any applicable law or regulations relating to that activity in the country or territory in which it is carried on,
- (c) so far as possible, avoids any conflict of interest;
- (d) so far as any conflict of interest cannot be avoided, discloses the conflict to the licenceholder and any client concerned; and
- (e) discloses to the licenceholder and any client concerned any private benefit to the officer or employee.

#### **6.4 Responsible behaviour**

- (1) A licenceholder must have procedures for requiring those seeking to obtain business on its behalf —
  - (a) to do so in a way which is clear, fair and not misleading;
  - (b) to avoid any undue pressure, and
  - (c) to make clear the purpose or purposes of the contact at the initial point of communication, and to identify themselves and the licenceholder whom they represent to clients and potential clients.
- (2) The licenceholder must give any recipient with whom he arranges an appointment a contact point.
- (3) The licenceholder must not communicate with a person at an unsocial hour, unless the person has previously agreed to such a communication.
- (4) For the purpose of paragraph (3), "unsocial hour" means —
  - (a) any time on a Sunday, Good Friday or Christmas Day;
  - (b) before 9.00 am or after 9.00 pm on any other day;

- (c) any other day or any other time —
  - (i) where the licenceholder knows that the person concerned does not wish to be called on that day or at that time, or
  - (ii) where the licenceholder has reason to believe that the person concerned would not wish to be called on that day or at that time (for example, because of religious observance or working patterns).

### **6.5 Introductions to overseas branches etc.**

- (1) A licenceholder who introduces a client to an overseas financial business must —
  - (a) disclose to the client that the business will not be regulated under the Act, and
  - (b) inform the client of the system of regulation of financial services applying to the business in the country or territory where it is located.
- (2) In this rule “overseas financial business” means a person carrying on, in a country or territory outside the Island, an activity which would be a regulated activity if it were carried on in the Island.

### **6.6 Action likely to bring Island into disrepute**

A licenceholder must not carry on business of such a kind or in such a way as may be likely to bring the Island into disrepute or damage its standing as a financial centre.

### **6.7 Integrity and fair dealing**

- (1) A licenceholder must —
  - (a) observe high standards of integrity and fair dealing in carrying on regulated activities, and
  - (b) comply with any applicable code or standard which is imposed or endorsed by —
    - (i) any professional body of which the licenceholder is a member, or
    - (ii) any investment exchange on which the licenceholder does business.
- (2) Rules 6.8 to 6.12 are without prejudice to the generality of paragraph (1).

### **6.8 Informed decisions**

- A licenceholder must —
- (a) take all reasonable steps to enable its clients to take informed decisions relating to their business with the licenceholder, and
  - (b) avoid misleading or deceptive representations or practices.

## **6.9 Independence**

- (1) A licenceholder —
  - (a) must not claim that it is independent or impartial if it is not, and
  - (b) must ensure that any claim it makes as to its independence or impartiality adequately includes any limitation which there may be on either.
- (2) Without prejudice to paragraph (1), a licenceholder must not represent itself as acting independently if it has any relationship or arrangement with any other person which —
  - (a) brings any distortion into the way in which it conducts its business with a client; or
  - (b) results in an advantage to the licenceholder, or a disadvantage to the client, in any business done with that person.

## **6.10 Gifts and other benefits**

A licenceholder must not —

- (a) offer or receive, or
- (b) permit any employee or agent to offer or receive,

any gift or other direct or indirect benefit, if to do so might adversely influence the giving of advice by, or the exercise of discretion on the part of, the licenceholder.

## **6.11 Remuneration**

A licenceholder's remuneration must be related to —

- (a) the disclosed relationship between the licenceholder and the client, and
- (b) the services provided by the licenceholder to the client.

## **6.12 Conflicts of interest — general**

- (1) Where a conflict of interest arises —
  - (a) between the licenceholder or any relevant person and its clients, or
  - (b) between one client and another,

in the course of carrying on any regulated activities, the licenceholder must promptly notify each of the clients concerned of that fact.

(2) For the avoidance of doubt, any borrowing by the licenceholder or a relevant person from a client amounts to a conflict of interest.

- (3) This rule is without prejudice to rules 8.7 and 8.8.

## **6.13 Advertisements — general**

A licenceholder must not publish or cause or permit to be published —

- (a) any advertisement for a product or service which does not contain a fair and accurate indication of the product or service;
- (b) any advertisement which hides, diminishes or obscures important statements or warnings;
- (c) any advertisement which might damage the reputation of the Island; or
- (d) any advertisement which makes a prediction or forecast of future income which —
  - (i) is not based on and consistent with present conditions, or
  - (ii) does not include a warning that past performance is not an indicator of future performance.

#### **6.14 Reference to licensing**

(1) A licenceholder must not publish or cause or permit to be published any advertisement (other than an advertisement which does not mention or relate to a regulated activity) which does not —

- (a) state in a prominent position —
  - (i) that the licenceholder is licensed by the Commission, and
  - (ii) the type or types of activity which it is licensed to carry on; and
- (b) state the business name of the licenceholder and its principal business address in the Island.

(2) A licenceholder must in all correspondence and other documents issued or published by it (including business cards, emails, websites, terms of business and client agreements) state in a prominent position —

- (a) that it is licensed by the Commission; and
- (b) the type or types of regulated activity which it is licensed to carry on.

(3) Subject to paragraph (4), the statement under paragraph (1)(a) or (2) must be in the following form —

"Licensed by the Financial Supervision Commission of the Isle of Man to [take deposits] [carry on investment business][provide [collective investment scheme][corporate][trust] services]"

as the case may be.

(4) The statement may use the term “Isle of Man Financial Supervision Commission” instead of “Financial Supervision Commission of the Isle of Man”.

- (5) This rule does not apply to —
  - (a) cheques, cheque books or paying in books,
  - (b) bank statements, deposit confirmations or foreign exchange confirmations, or
  - (c) cheque guarantee, charge, debit or credit cards or cards of a similar nature.



### **6.15 Display of licence**

- (1) A licenceholder must prominently display the first page, or a copy of the first page, of its licence in its principal place of business in the Island.
- (2) A licenceholder must provide to any client on request —
  - (a) information regarding the conditions attached to its licence, and
  - (b) details of any exception or modification of any rule applicable to it.

#### *Chapter 2— General requirements for deposit takers*

### **6.16 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 1.

### **6.17 Reference to compensation scheme in advertisements**

- (1) A licenceholder must not publish or cause or permit to be published any advertisement which states or implies that any deposits or interest will be guaranteed, secured, insured or the subject of any form of protection (other than that provided by regulations under section 25 of the Act) unless it states —
  - (a) the form of the protection;
  - (b) the extent of the protection; and
  - (c) the full name of the person who will be liable to meet any claim by the depositor by virtue of the arrangements conferring the protection.
- (2) A licenceholder which is not a participant in a scheme established by regulations under section 25 of the Act must not publish or cause or permit to be published any advertisement which refers to its deposit taking business or contains an invitation to make deposits unless it states in a prominent position that the licenceholder is not a participant in that scheme.

#### *Chapter 3 — General requirements for all investment businesses*

### **6.18 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 2.

### **6.19 Recommendations which may benefit licenceholder**

- (1) A licenceholder must not recommend to a retail investor a transaction if the recommendation is motivated largely by a benefit which it may bring to the licenceholder, unless the transaction is demonstrably to the client's advantage.
- (2) In this rule "benefit" includes a volume override (that is, an extra commission for generating additional trades).

## **6.20 Churning**

A licenceholder must not effect transactions with unnecessary frequency or in excessive size with or for a client for whom the licenceholder exercises discretion as to the management of the client's investments.

## **6.21 Valuation of investments which are not marketable**

(1) This rule applies where a licenceholder manages investments on behalf of a client and the amount of any remuneration of the licenceholder is dependent upon the value of any such investments.

(2) The valuation of any investment which is not readily marketable, or for which information for determining their current value may not be available, must be on the basis of an arm's length valuation which has been —

- (a) prepared by or confirmed as an arm's length valuation by an independent and competent person; or
- (b) agreed expressly with the client at the time that the management agreement is signed.

## **6.22 Front running**

A licenceholder must not enter, or permit any person associated with the licenceholder to enter, into an investment transaction ahead of a client, if that client ought to have priority.

## **6.23 Fairness in allocation**

Where, on an allocation of stock or other investments, there is not enough to go round, the licenceholder must always —

- (a) allocate what it has fairly and uniformly, and
- (b) put itself last unless its participation in the transaction enabled every participant to get a better deal.

## **6.24 Distribution of transactions among clients**

A licenceholder must not allocate or transfer to any client any deal (or part of a deal) in an investment which it entered into as principal unless —

- (a) the allocation or transfer was unconditionally decided upon in principle before the deal was done, or
- (b) the investment has improved in value since the deal, the licenceholder is satisfied that the investment is suitable for the client and the client obtains the benefit of best execution and of the improvement in value.

## **6.25 Skill, care and diligence**

Rules 6.26 to 6.32 are without prejudice to rule 6.2.

## **6.26 Prompt and timely execution**

(1) A licenceholder must act promptly in accordance with its instructions, unless —

- (a) it has been given a discretion as to timing, and
- (b) it uses that discretion in an alert and sensible way.

(2) Instructions and decisions to buy or sell must be recorded as soon as taken, with the date and, whenever possible, the time.

## **6.27 Best execution**

(1) Subject to paragraph (2), a licenceholder must not transact business for a client on worse terms than it would expect to obtain for itself, allowing for the size of the transaction.

(2) Where a licenceholder effects a transaction through —

- (a) another licenceholder, or
- (b) a person authorised and regulated by the Financial Services Authority in the United Kingdom,

it may rely upon that person to obtain best execution provided that the client has accepted those arrangements in writing.

## **6.28 Fairness with research or analysis**

A licenceholder must not —

- (a) deal for itself or any person associated with it ahead of the distribution of its own or an associate's research or analysis and with advance knowledge of anything that might possibly be price sensitive in it; or
- (b) distribute research or analysis containing recommendations from which a licenceholder expects to benefit (including by way of past or future principal transactions, or because of a material interest) unless the anticipated source of benefit is disclosed; or
- (c) otherwise behave unfairly in the way in which it acts upon its own or an associate's research or analysis.

## **6.29 Knowledge of client**

(1) A licenceholder must find out enough about a retail investor's personal and financial circumstances to enable it to act properly for him in investment matters.

(2) This rule does not apply in relation to a transaction where the licenceholder knows or reasonably believes that the client is not relying on the advice or judgment of the licenceholder on the merits or suitability of the transaction.

## **6.30 Suitability**

A licenceholder must ensure, as far as it can, —

- (a) in making recommendations to a client,

- (b) in exercising discretion, and
- (c) in advising about the client's instructions,

having taken reasonable steps to inform itself of what is available on the market, —

- (i) that any transaction is not unsuitable for the client, and
- (ii) if he is a retail investor, that it is positively suitable for him.

### **6.31 Life policies and collective investment schemes**

- (1) This rule applies to the following investments —
  - (a) a life policy;
  - (b) units in a collective investment scheme.
- (2) A licenceholder must not —
  - (a) recommend to any client, or
  - (b) effect on behalf of a client,

the acquisition of an investment to which this rule applies unless it is satisfied —

- (i) that it will be suitable for the client, and
  - (ii) that it does not compare unfavourably with competing products.
- (3) A licenceholder must not —
    - (a) recommend to any client, or
    - (b) effect on behalf of a client,

a switch of investments to which this rule applies unless it —

- (i) reasonably believes that the switch will be to the client's advantage, and
- (ii) can demonstrate to the Commission, if required, the basis of that belief.

(4) Instructions and decisions to acquire or switch an investment to which this rule applies must be recorded as soon as taken, with the date and, whenever possible, the time.

### **6.32 Restriction on authority conferred by product companies**

A licenceholder must prohibit by the terms of employment or contract its employees and tied agents who are authorised to canvass for business from canvassing for or advising about life policies or collective investment schemes other than its own.

### **6.33 Dealings by employees on own account**

- (1) This rule applies where —
  - (a) an employee of a licenceholder is permitted to deal on his own account, and

- (b) a conflict of interest may arise in relation to such dealings.
- (2) The licenceholder must ensure that –
  - (a) the employee is given a written notice (a “personal account notice”) complying with Schedule 6.1; and
  - (b) the employee gives the licenceholder a written undertaking to observe the requirements of the notice.
- (3) The licenceholder must establish and maintain compliance procedures and appropriate arrangements to mitigate the potential for conflicts of interest in relation to such dealings.

#### **6.34 Disclosure and information**

A licenceholder must take all reasonable steps to ensure that a retail investor is given sufficient information which he is able to understand to enable him to make balanced and informed investment decisions.

#### **6.35 Understanding of risk**

- (1) This rule applies where a client is a retail investor.
- (2) A licenceholder must not —
  - (a) recommend a transaction to the client, or
  - (b) exercise discretion for the client in the management of investments, unless it has taken reasonable steps —
    - (i) to ascertain the nature and level of the risk which the client is willing to accept, and
    - (ii) to enable him to understand the nature and level of the risks involved.
- (3) Without prejudice to the generality of paragraph (2), a licenceholder must not —
  - (a) advise the client to deal, or deal with or for him, in unregulated collective investment schemes, futures, options, contracts for differences or warrants, unless it has arranged for the client to receive, and the client has by returning a signed copy shown that he has understood, a risk disclosure statement in the form specified in —
    - (i) Part 1 of Schedule 6.2, in the case of dealings in unregulated collective investment schemes;
    - (ii) Part 2 of Schedule 6.2, in the case of dealings in futures, options or contracts for differences; or
    - (iii) Part 3 of Schedule 6.2, in the case of dealings in warrants; or
  - (b) advise him to buy or effect in the exercise of discretion any purchase of an illiquid investment, unless it has —

- (i) informed the client of the nature and extent of the risks involved in such investments, including any difficulties in determining their value, and
- (ii) obtained his written consent.

### **6.36 Disclosure of product particulars**

(1) A licenceholder must ensure that, before or immediately after a recommendation is made by it or on its behalf to acquire an investment to which rule 6.31 applies, and before a commitment is made to acquire the investment, a retail investor is given or sent a statement, prepared by the licenceholder or the product company, which informs him of —

- (a) details of the investment,
- (b) premiums or other amounts payable then and in the future,
- (c) the factors relevant to the ultimate value of the investment or benefits payable under it,
- (d) the consequences of not keeping up the payments, and
- (e) any surrender or transfer value.

(2) This rule does not apply where the licenceholder is acting under the terms of a discretionary management agreement.

### **6.37 Disclosure of conflicts of interest**

(1) Any borrowing from a client must be disclosed to the client.

(2) Without prejudice to paragraph (1), where the conflicts of interest policy referred to in rule 8.7 is not sufficient to ensure, with reasonable confidence, that risks of damage to the interests of its clients will be prevented, a licenceholder must clearly disclose the general nature or sources, or both, of conflicts of interest to the client before carrying on any activity on its behalf.

(3) The disclosure required by paragraph (1) or (2) must —

- (a) be in writing, and
- (b) include sufficient detail, taking into account the nature of the client, to enable him to take an informed decision with respect to the activity in the context of which the conflict of interest arises.

### **6.38 General need for client agreement or terms of business**

(1) Subject to paragraph (2), a licenceholder must not carry on any regulated activity for a client unless either —

- (a) it has entered into a written agreement (a "client agreement") with the client, signed by the client, relating to the services it provides, or
- (b) in the case of an activity falling within paragraph (3) or (7) of Class 2, it has notified the client in writing of its terms of business relating to those services.

(2) No client agreement or terms of business are required for —

- (a) the issue of any tipsheet, broker's circular or similar publication;
  - (b) transactions not involving undue risk which are made while negotiations leading to a client agreement are taking place; and
  - (c) transactions made solely to complete outstanding obligations after an agreement has expired or been brought to an end.
- (3) A client agreement or terms of business must —
- (a) set out the basis on which the licenceholder is to provide its services;
  - (b) be easy to understand and not likely to be misunderstood; and
  - (c) not deprive the client of any rights which he would have had if the agreement or terms had not existed.
- (4) A licenceholder must retain —
- (a) a copy of the client agreement, signed by the client, or
  - (b) evidence of a notification under paragraph (1)(b).
- (5) In rules 6.39 to 6.45 references to a client agreement include, where applicable, references to terms of business notified under paragraph (1)(b).

#### **6.39 Retail and other investors**

- (1) A licenceholder shall treat a client who is an individual as a retail investor unless —
- (a) the licenceholder has undertaken an adequate assessment of the client's expertise, experience and knowledge which gives a reasonable assurance that the client is capable of understanding the risks involved in making his own investment decisions,
  - (b) the licenceholder has informed him in writing that the level of protection afforded to him is lower than that offered to a retail investor, and
  - (c) the client agreement with the client states that he is not a retail investor.
- (2) A licenceholder shall treat a client who is not an individual as a retail investor if —
- (a) the client has requested the licenceholder in writing to treat it as a retail investor, or
  - (b) the client agreement with the client states that it is a retail investor.

#### **6.40 Contents of client agreement — general**

Every client agreement must —

- (a) provide information on all relevant facts relating to the licenceholder's remuneration (including the remuneration of any intermediary which is payable by the client) attributable to the services provided;
- (b) state that the client may request details of the amount of remuneration being received by the licenceholder;

- (c) state that the client has the right to request details of any relevant educational and professional qualifications, and the experience and track record, of —
  - (i) the licenceholder; and
  - (ii) any employee of the licenceholder directly engaged in providing services to the client;
- (d) state that the licenceholder will not advise a client to use the services of another person who is an associate of the licenceholder without disclosing that relationship;
- (e) where the licenceholder is a tied agent of the institution by which a financial product recommended to the client is marketed, disclose that relationship; and
- (f) where applicable, state how interest received on client money is to be dealt with, in accordance with rule 3.14, and the arrangements for crediting interest to the client bank account..

#### **6.41 Contents of client agreement with retail investor**

- (1) A client agreement with a retail investor must include terms relating to the following matters, so far as applicable —
  - (a) the nature of the services to be provided by the licenceholder under it, including, where appropriate, the client's investment objectives and any restrictions on investments or markets in which funds may be invested;
  - (b) in respect of any fees payable by the client to the licenceholder —
    - (i) the basis of calculation;
    - (ii) the notice required for any increase of fees;
    - (iii) the method of payment (e.g. deduction or billing);
    - (iv) the frequency of payment; and
    - (v) whether or not any fees payable are to supplement or be abated by any remuneration receivable by the licenceholder in connection with transactions effected by the licenceholder with or for the client;
  - (c) the fact that the licenceholder is regulated by the Commission in the conduct of regulated activities;
  - (d) the manner in which the instructions may be given by the client for any transaction;
  - (e) the arrangements for handling and accounting for client money, specifying how the money is at all times separated from the licenceholder's money;
  - (f) the arrangements for registration and identification of ownership and safe custody of documents of title and the name of any nominee company used;



- (g) the client's right to inspect copies of contract notes, vouchers and entries in books or electronic recording media relating to the clients' transactions, together with a statement that such records will be maintained for 6 years from the date of the transaction;
  - (h) arrangements for bringing the agreement to an end, which must include the right for the client to terminate the agreement on immediate written notice; and
  - (i) a statement that a summary of the licenceholder's conflicts of interest policy under rule 8.7 will be made available on request.
- (2) Where a licenceholder is effecting margined transactions on behalf of a retail investor, the agreement must include —
- (a) a warning that the licenceholder in certain circumstances may be required to obtain additional money from the client by way of margin;
  - (b) where the licenceholder intends to effect contracts which are not traded on and under a recognised exchange or designated exchange, the specific authority of the client to do so;
  - (c) a statement of when a deposit or margin (including the initial and variation margin) may be required and the licenceholder's rights on failure to pay;
  - (d) a warning that failure to meet margin calls may lead to closing out without reference;
  - (e) a statement of the circumstances in which it might be possible for a licenceholder to close out without reference to the client.
- (3) The terms of the client agreement relating to fees must not —
- (a) provide for notice of less than one month for an increase in fees;
  - (b) provide for deduction of fees from income or capital belonging to a client without prior notification to the client, in accordance with a procedure specified in the agreement.
- (4) This paragraph is without prejudice to rule 6.40.

#### **6.42 Discretionary management agreement**

- (1) Where a licenceholder is to exercise discretion for a retail investor in the management of investments, the client agreement must include statements as to —
- (a) whether or not there is any restriction on —
    - (i) the categories of investment in which the fund may be invested, or
    - (ii) the amount or the proportion of the fund which may be invested in any category of investment or in any one investment;and, if so, what the restriction is;
  - (b) the frequency with which the client is to be supplied with a statement of the money and investments held and a valuation of them, and what the basis of valuation is to be;

- (c) if the agreement is to include a measure of portfolio performance, the basis on which that performance is to be measured;
- (d) whether hedging or borrowing powers are to be used, the nature of such powers and limits upon their use;
- (e) whether the licenceholder may lend investments to or borrow investments from third parties or charge investments to secure borrowings, how such powers are to be exercised and the limits placed upon them;

(2) The licenceholder must, at the time that the client agreement is signed or as soon as practicable thereafter, provide the client with a statement showing the initial composition of the investments and their initial value (so far as it can be ascertained).

(3) Where investment is contemplated in areas involving higher risk investments on behalf of a retail investor, including —

- (a) writing of options and doing business in futures and contracts for differences;
- (b) other margined transactions;
- (c) illiquid investments; and
- (d) participation in underwriting securities,

the agreement must specifically state whether such transactions are permitted and any limits on the category of investment or on the financial commitment involved.

### **6.43 Compliance with client agreement**

A licenceholder must comply with the terms of the client agreement in all dealings with or on behalf of a client.

### **6.44 Periodical information**

(1) Subject to paragraph (2), a licenceholder which is managing investments for a client must normally account to him at least once in every 6 months as to the investment performance of the portfolio, stating —

- (a) the current valuations,
- (b) a suitable comparison with the movement of the market, and
- (c) any changes in the composition of the investments.

(2) A client may expressly waive the requirement for a biannual report in favour of an annual report, but before he does so the licenceholder must make the client aware that he is entitled to receive information every 6 months.

### **6.45 Penalty on termination**

Where the client is a retail investor, the client agreement may provide for an additional payment to be made to the licenceholder upon the termination of the agreement, but this must be clearly disclosed in the client agreement.

Futures, options and contracts for differences

#### **6.46 Risk warning**

(1) A licenceholder must secure, before it enters into any transaction in futures, options and contracts for differences with or for a retail investor, that the investor receives, signs and returns to the licenceholder a risk disclosure statement in the form set out in Schedule 6.2.

(2) This rule does not apply where the licenceholder is acting under the terms of a discretionary management agreement.

#### **6.47 Contracts to be on-exchange**

(1) A licenceholder must not undertake a margined transaction on behalf of a client through another person unless that person is either —

- (a) another licenceholder licensed to carry on that activity; or
- (b) an overseas person authorised in the country or territory in which it carries on business to undertake such transactions who is required to hold clients' money received in relation to such transactions in a segregated bank account for that purpose and in his books to credit the client accordingly.

(2) The licenceholder must take steps to ensure that the client's money is treated as client money by the person referred to in paragraph (1)(a) or (b).

(3) A licenceholder must not, without the express permission of the client, undertake a margined transaction for a retail investor in a contract which is not traded on a recognised exchange or designated exchange.

#### **6.48 Liability in respect of margins**

(1) In relation to margined transactions a licenceholder must —

- (a) keep daily track of the amount of margin or other requirements which must be paid for each client;
- (b) ensure that any margin payable is required to be deposited in advance in cash or approved collateral,
- (c) ensure that any deposit on a limited liability transaction is deposited promptly and in cash,
- (d) ensure that margin, whenever properly required to be paid, is deposited in cash or approved collateral;
- (e) make the client aware of the consequences of not paying a margin.

(2) Where a licenceholder is effecting margined transactions as a discretionary portfolio manager or stockbroker, it must ascertain from —

- (a) the person referred to in rule 6.47(1)(a) or (b), or
- (b) the exchange on which the contract is traded,

whether or not the licenceholder is responsible for the fulfilment of its clients' obligations.

(3) If there is a shortfall on a margined transaction, the licenceholder must make up the difference until it obtains more cash or collateral from its client.

(4) Where a licenceholder lends money to a client to make up such a shortfall, it must properly record the loan in its accounts.

(5) In this rule "limited liability transaction" means a margined transaction effected by a licenceholder with a client, the terms of which provide that the maximum liability of the client in respect of the transaction shall be limited to an amount determined before the transaction is effected

#### **6.49 Contract note etc**

(1) After a transaction has been carried out for a client, a licenceholder must send or cause to be sent to the client or to his order promptly a statement of the transaction.

(2) Paragraph (1) does not apply where —

- (a) the licenceholder reasonably believes that another licenceholder or the product company will send such a note to the client;
- (b) the transaction is effected with a market counterparty (unless otherwise required by contract or custom);
- (c) the transaction relates to a life policy; or
- (d) the client has made a specific request in writing, separate from any other agreement, that statements must not be sent to him and has not revoked the request.

(3) Paragraph (1) does not apply where the transaction is part of a series of linked transactions, but the licenceholder must send or cause to be sent to the client or to his order a statement of the transactions —

- (a) on completion of the series, or
- (b) at appropriate intervals not more than 3 months apart;

(4) Paragraph (1) does not apply where —

- (a) the transaction involves a third party who has failed to provide information required of him; or
- (b) a transaction involves the conversion of one currency into another and that conversion has not been made;

in which case the licenceholder must send or cause to be sent to the client or to his order a statement of the essential features of the transaction as soon as practicable.

(5) A statement required by paragraph (1), (3) or (4) must specify the essential features of the transaction including —

- (a) the name and address of the licenceholder;
- (b) the client's designation and account number;
- (c) the date of the transaction;
- (d) a description of the investment and size of transaction;

- (e) the nature of the transaction and unit price (and whether forward or historic price);
  - (f) the total cost;
  - (g) the amount of remuneration of the licenceholder;
  - (h) the amount of fees, taxes or duties;
  - (i) the settlement date;
  - (j) if the transaction involves converting one currency into another, the exchange rate.
- (6) Where —
- (a) the transaction relates to units in a collective investment scheme, and
  - (b) deductions for charges and expenses are not made uniformly throughout the life of an investment but are loaded disproportionately on the early years,

the amount of any deductions must be expressed either in cash terms or as a percentage of the unit price.

- (7) Upon exercise of an option, the following items must be included in the statement required by paragraph (1), (3) or (4) —
- (a) the profit or loss to the client arising out of the exercise of the option; and
  - (b) the fees, commissions and expenses payable by the client, if any, in connection with the transaction.

#### *Chapter 4 — Specific requirements for CIS service providers*

### **6.50 Application and interpretation**

(1) This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 3.

(2) In this Chapter "relevant scheme" means a collective investment scheme for which a licenceholder provides services which are regulated activities falling within Class 3.

### **6.51 Interests of scheme to be paramount**

(1) Where a licenceholder carries on any activity relating to a relevant scheme, the interests of the scheme must be the licenceholder's paramount consideration.

- (2) A licenceholder must —
- (a) where practicable, avoid any conflict of interest arising in relation to a relevant scheme; and
  - (b) where a conflict arises, address that conflict through internal rules of confidentiality by —
    - (i) declining to act,

- (ii) disclosing the nature of the conflict to the governing body of the scheme, or
- (iii) where appropriate, seeking that body's written confirmation that the licenceholder may continue to provide services to the scheme.

(3) When entering into financial, banking or other transactions on behalf of a relevant scheme, the licenceholder must —

- (a) act in the best interests of the scheme; and
- (b) not effect such transactions with unnecessary frequency or in excessive size.

(4) Where the licenceholder provides services in respect of more than one scheme, the licenceholder should ensure that all schemes are dealt with fairly and no scheme is given unfair advantage.

### **6.52 Observance of terms of scheme particulars**

In relation to a relevant scheme, a licenceholder must take all reasonable steps to comply with every statement in the most recently published prospectus, explanatory memorandum or other documentation describing how he will —

- (a) operate the scheme, and
- (b) comply with the duties imposed on him by or under the Act.

### **6.53 Valuation of investments which are not marketable**

(1) This rule —

- (a) applies where the licenceholder has responsibility for the calculation of net asset valuations of a relevant scheme; but
- (b) does not apply in relation to activities falling within paragraph (11) or (12) of Class 3.

(2) The valuation of any investment which is not readily marketable, or for which information for determining their current value may not be available, must be either —

- (a) calculated in line with the licenceholder's documented policies and procedures in relation to the valuation of schemes, or
- (b) prepared by or confirmed as an arm's length valuation by an independent and competent person.

(3) The licenceholder must ensure that the method of valuation under paragraph (2)(a) or (b) is appropriate.

### **6.54 Participants to be treated fairly**

(1) In carrying on its activities a licenceholder must ensure that —

- (a) all participants in a relevant scheme are treated fairly in accordance with the terms of the scheme, and

(b) no participant is given unfair advantage or priority.

(2) Where a licenceholder is in possession of information that may be material to the prospects of a relevant scheme, it must, subject to any legal requirements and any duty of confidentiality, ensure that all participants are treated fairly when communicating such information.

(3) A licenceholder must not give itself, or permit any person associated with it to be given, an unfair advantage or priority.

#### **6.55 Material interests**

Subject to any legal requirements and any duty of confidentiality, the licenceholder should, within a reasonable time, notify the governing body of a relevant scheme of any matter —

(a) of which it becomes aware, and

(b) the disclosure of which might reasonably be expected to be in the material interests of the scheme.

#### **6.56 Forecasts of future income**

(1) This rule does not apply in relation to activities falling within paragraph (11) or (12) of Class 3.

(2) Where a licenceholder makes or publishes a prediction or forecast of future income from a relevant scheme, it must be based on and consistent with present conditions.

(3) The licenceholder must be able to justify the prediction or forecast to the Commission if required to do so.

#### **6.57 Information to be supplied by tied agents**

A licenceholder must ensure that its tied agents, when communicating with a retail investor, adequately inform the investor about the licenceholder and the agent's relationship with it.

#### **6.58 Provision of statistical information about schemes**

A licenceholder must provide to the Commission on a quarterly basis such statistical information about the schemes for which it carries on regulated activities as the Commission may require.

#### **6.59 Services for overseas schemes**

A licenceholder must notify the Commission within 10 business days after entering into an agreement to provide services which are regulated activities falling within paragraphs (1) and (2) of Class 3 to a collective investment scheme established in a country or territory outside the Island.

## **6.60 Contract note etc**

(1) After a transaction has been carried out for a client, a licenceholder must send or cause to be sent to the client or to his order promptly a statement of the transaction.

(2) Paragraph (1) does not apply where the transaction is part of a series of linked transactions, but the licenceholder must send or cause to be sent to the client or to his order a statement of the transactions —

- (a) on completion of the series; or
- (b) at appropriate intervals not more than 3 months apart.

(3) A statement required by paragraph (1) or (2) must specify the essential features of the transaction including —

- (a) the name and address of the licenceholder;
  - (b) the client's designation and account number;
  - (c) the date of the transaction;
  - (d) a description of the investment and size of transaction;
  - (e) the nature of the transaction and unit price (and whether forward or historic price);
  - (f) the total cost;
  - (g) the amount of remuneration of the licenceholder;
  - (h) the amount of fees, taxes or duties;
  - (i) the settlement date;
  - (j) if the transaction involves converting one currency into another, the exchange rate.
- (4) Where —
- (a) the transaction relates to units in a collective investment scheme; and
  - (b) deductions for charges and expenses are not made uniformly throughout the life of an investment but are loaded disproportionately on the early years,

the amount of any deductions must be expressed either in cash terms or as a percentage of the unit price.

## **6.61 Requirement for written functionary agreement**

A licenceholder must not carry on any regulated activity falling within Class 3 for any person (other than a participant) except in accordance with an agreement in writing which sets out the terms on which its services are to be provided.



**Chapter 5—General requirements for all corporate service and trust service providers**

**6.62 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 4 or Class 5.

**6.63 Client agreement or terms of business**

(1) A licenceholder must not carry on any regulated activity for a client unless either —

- (a) it has entered into a written agreement (a "client agreement") with the client relating to the services it provides, or
- (b) it has notified the client in writing of its terms of business relating to those services.

(2) A client agreement or terms of business must set out —

- (a) the fees to be charged or the basis of calculation of the fees to be charged, or both
- (b) the method by which such fees are to be collected,
- (c) the method by which increases in fees are notified to the client;
- (d) the conditions for the termination of services by the licenceholder, including, if applicable, the provisions for the refund of any fees due to the client as a result of the termination of services; and
- (e) how interest received on client money is to be dealt with, in accordance with rule 3.14.

(3) A licenceholder must retain —

- (a) a copy of the client agreement referred, signed by the client, or
- (b) evidence of a notification under paragraph (1)(b).

**Chapter 6 — Specific requirements for corporate service providers**

**6.64 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 4.

**6.65 Nominee shareholders**

Where a licenceholder acts or arranges for another person to act as a nominee shareholder or nominee member of a company, the licenceholder must —

- (a) ensure that in all such cases a written nominee agreement or such other trust instrument as may be appropriate exists; and
- (b) retain a copy of the agreement or instrument in its records.

### **6.66 Resignation of licenceholder**

(1) If a licenceholder intends, without the consent of a client, to cease carrying on relevant activities for or on behalf of that client, it must notify in writing —

- (a) the client, and
- (b) where the client is a company, the directors, the shareholders and, if different, the beneficial owner of the client.

(2) Where a licenceholder ceases to carry on relevant activities for or on behalf of a client company for any reason, it must —

- (a) preserve the company's records in a readily realisable format until they are handed over to the company, another licenceholder or another person who is to provide those or similar services, and
- (b) co-operate with the company, licenceholder or other person to ensure a smooth transition.

(3) Where —

- (a) a licenceholder ceases to carry on relevant activities for or on behalf of a client company, and
- (b) the company is struck off the register under section 273 or 319A of the Companies Act 1931,

the licenceholder must, unless it hands over the company's records as mentioned in paragraph (2)(a), retain those records for not less than 13 years after the date on which the company is struck off the register.

(4) In this rule "relevant activities" means regulated activities falling within Class 4.

### **6.67 Compliance by clients**

A licenceholder must take reasonable steps to ensure that any company or partnership for which it carries on any regulated activity complies with such statutory obligations as are applicable to that activity.

#### *Chapter 7 — Specific requirements for trust service providers*

### **6.68 Application**

This Chapter applies to all licenceholders licensed to carry on regulated activities falling within Class 5.

### **6.69 Resignation of licenceholder**

If a licenceholder ceases to carry on regulated activities in relation to a trust, it must take whatever steps are appropriate and necessary —

- (a) to facilitate the transfer of that business to another licenceholder or another person who is to provide those or similar services, and

- (b) to secure the appointment of a replacement trustee, protector or enforcer, as the case may be, and

and co-operate with the new trustee, protector or enforcer to ensure a smooth transition.

## PART 7 — ADMINISTRATION

### 7.1 Application

(1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.

(2) Subject to paragraph (1), this Part applies to all licenceholders.

### 7.2 Change of name or address

A licenceholder must notify the Commission, not less than 20 business days in advance, of a change in —

- (a) its name,
- (b) any business name under which it trades in the Island;
- (c) its principal place of business;
- (d) any permanent place of its business, normally open to the public, in the Island;
- (e) its registered office.

### 7.3 Changes in capital structure

(1) A licenceholder which is incorporated in the Island must not, without the consent of the Commission, take any step towards reducing, increasing or changing the nature of —

- (a) its issued share capital, or
- (b) its loan capital.

(2) A licenceholder must notify the Commission not less than 20 business days before taking any step towards altering the rights or obligations of its shareholders or debenture holders.

### 7.4 Changes in ownership

(1) A licenceholder must notify the Commission of —

- (a) any transfer of 5% or more of its voting shares; or
- (b) any other transfer of its voting shares which has a material effect on the immediate or ultimate control of the licenceholder.

(2) A notification under paragraph (1) must be made —

- (a) where the shares are quoted on a recognised stock exchange, within 5 business days after the licenceholder becomes aware of the transfer;
- (b) in all other cases, 20 business days before the transfer is registered.

(3) A licenceholder must notify the Commission of —

- (a) any change in the ownership structure between it and its ultimate parent company; or

- (b) any material change in its ultimate ownership.
- (4) A notification under paragraph (3) must be made —
  - (a) if practicable, not less than 20 business days before the change takes place; or
  - (b) otherwise, as soon as practicable.

#### **7.5 Acquisition etc. of business**

- (1) This rule applies to the following transactions —
  - (a) a merger of the licenceholder's business with another;
  - (b) a takeover or acquisition by the licenceholder of another business;
  - (c) a purchase by the licenceholder of the assets or liabilities of another business;
  - (d) the acquisition of a controlling interest, or any change in an existing controlling interest, in the licenceholder's business.
- (2) A licenceholder which is licensed to carry on activities falling within Class 1 must not enter into a transaction to which this rule applies without the consent of the Commission.
- (3) A licenceholder, other than one mentioned in paragraph (2), must notify the Commission of any transaction to which this rule applies —
  - (a) if practicable, not less than 20 business days before the transaction takes place; or
  - (b) otherwise, as soon as practicable.

#### **7.6 Sale or disposal of business**

A licenceholder must notify the Commission of the sale or disposal of, or an agreement to sell or dispose of, the whole or any part of the licenceholder's business —

- (a) if practicable, not less than 20 business days before the transaction takes place; or
- (b) otherwise, as soon as practicable.

#### **7.7 Acquisition of shares of company**

- (1) A licenceholder must notify the Commission before subscribing for or acquiring, or entering into a contract to subscribe for or acquire, 10% or more of the issued share capital of a company.
- (2) Paragraph (1) does not apply to a subscription for shares, undertaken in the course of regulated activities falling within Class 4 or Class 5, by a licenceholder licensed to carry on those activities or an officer or employee of such a licenceholder.
- (3) A notification under paragraph (1) must be given —
  - (a) if practicable, not less than 20 business days before the event; or

- (b) otherwise, as soon as practicable.

## **7.8 Subsidiaries etc.**

A licenceholder incorporated in the Island must not, without the consent of the Commission, acquire or establish a trading subsidiary, branch or representative office in the Island or elsewhere.

## **7.9 New appointments and departures from office**

(1) In relation to any licenceholder, this rule applies to the following offices and positions —

- (a) Isle of Man resident officer;
- (b) key person;
- (c) compliance officer;
- (d) money laundering reporting officer; and
- (e) deputy money laundering reporting officer.

(2) In relation to a licenceholder incorporated in the Island, this rule also applies to the following offices and positions —

- (a) controller;
- (b) director; and
- (c) secretary.

(3) A licenceholder must notify the Commission at least 20 business days in advance of —

- (a) an appointment or intended appointment to any office or position to which this rule applies; and
- (b) the title and responsibilities of the office or position.

(4) A licenceholder must notify the Commission of any departure or intended departure from an office or position to which this rule applies, giving reason for departure, within 10 business days of the giving of notice or other event giving rise to the departure.

(5) For the avoidance of doubt, references in this rule to an appointment include an appointment of an existing officer or employee of a licenceholder.

## **7.10 Staff disciplinary action**

(1) A licenceholder must notify the Commission within 10 business days of the discovery of an event which may lead to a final warning being given to, or other serious disciplinary action being taken against, any of its employees.

(2) A notification under paragraph (1) must specify the event but, except in the case of a key person, need not disclose the name of the employee.

(3) A licenceholder must notify the Commission within 5 business days after it gives any final warning to, or takes any other serious disciplinary action

against, any of its key persons, supplying full details of the action including copies of any notices or written warnings given by the licenceholder to the key person.

(4) The licenceholder must provide the key person concerned with a copy of a notification under paragraph (3).

(5) The requirements of paragraphs (1) to (3) have effect notwithstanding any agreement imposing an obligation of confidentiality.

(6) For the purpose of this rule "serious disciplinary action" is to be interpreted in accordance with the licenceholder's internal human resources policy.

#### **7.11 Disqualification as a director etc.**

A licenceholder must notify the Commission as soon as it becomes aware of any disqualification or any application for disqualification relating to the licenceholder or any of its key persons under —

- (a) section 208 or 259 of the Companies Act 1931,
- (b) section 31 of the Companies Act 1982,
- (c) section 26 of the Companies Act 1992, or
- (d) any equivalent provision having effect in a country or territory outside the Island.

#### **7.12 Service of notice etc.**

(1) A licenceholder must notify the Commission as soon as it becomes aware of any action specified in paragraph (2) against —

- (a) the licenceholder,
- (b) an associated company of the licenceholder; or
- (c) any person for or on behalf of whom the licenceholder carries on any regulated activity.

(2) The actions referred to in paragraph (1) are —

- (a) the service of any notice under section 24 of the Criminal Justice Act 1990;
- (b) the service of any summons or issue of any warrant under section 21 or section 22 of the Criminal Justice Act 1991;
- (c) the making of any order or the issue of any warrant under section 52 or section 53 of the Drug Trafficking Act 1996; or
- (d) the making of any order or the issue of any warrant under Schedule 5 to the Anti-Terrorism and Crime Act 2003.

#### **7.13 Criminal proceedings and convictions**

(1) A licenceholder must notify the Commission as soon as it becomes aware of the bringing of any criminal proceedings against, or the conviction of, —

- (a) the licenceholder or any associated company, or

- (b) any officer or employee of the licenceholder or any associated company,

for an offence to which this rule applies.

- (2) This rule applies to —
  - (a) an offence which is or, if committed in the Island, would be triable on information;
  - (b) an offence relating to a regulated activity or an activity which, if carried on in the Island, would be a regulated activity;
  - (c) an offence under the Companies Acts 1931 to 2004 or the Companies Act 2006, or any legislation having similar effect in any country or territory outside the Island;
  - (d) an offence relating to the formation, management or administration of companies in any country or territory;
  - (e) an offence under the Purpose Trusts Act 1996 or any legislation having similar effect in any country or territory outside the Isle of Man;
  - (f) an offence relating to trusts in any country or territory;
  - (g) an offence relating to insolvency; or
  - (h) an offence involving fraud or dishonesty.

(3) Nothing in this rule requires a licenceholder to disclose any matter subject to legal professional privilege.

#### **7.14 Surrender of licence**

(1) Where a licenceholder intends voluntarily to surrender its licence, it must notify the Commission of —

- (a) its intention to do so, and
- (b) the arrangements it proposes to make to dispose of its business.

(2) A notification under paragraph (1) must be given not less than 20 business days before the surrender of the licence.

#### **7.15 Cessation of regulated activities**

(1) Where a licenceholder intends voluntarily to cease carrying on a regulated activity of any description, it must notify the Commission of —

- (a) its intention to do so, and
- (b) the arrangements it proposes to make to for the safeguarding of its clients' deposits or other assets.

(2) A notification under paragraph (1) must be given —

- (a) if practicable, not less than 20 business days before the event; or
- (b) otherwise, as soon as practicable.



### **7.16 Bankruptcy, winding up, etc.**

A licenceholder must notify the Commission as soon as it becomes aware of any of the following (whether occurring in the Island or elsewhere) —

- (a) the commencement of proceedings for the winding up of the licenceholder;
- (b) the appointment of a receiver, liquidator, provisional liquidator, administrator or trustee in bankruptcy of the licenceholder;
- (c) the making of any composition or arrangement with creditors of the licenceholder;
- (d) where the licenceholder is a partnership or unincorporated association —
  - (i) an application to dissolve the partnership or association, or
  - (ii) the commencement of proceedings for the bankruptcy of a partner;
- (e) where the licenceholder is an individual, the commencement of proceedings for the bankruptcy of the licenceholder;
- (f) the appointment of an inspector by a statutory or other regulatory authority to investigate the affairs of the licenceholder.

### **7.17 Voluntary winding up**

(1) This rule applies to a licenceholder incorporated in the Island.

(2) A licenceholder must notify the Commission of the intention of its directors to make a declaration of solvency in accordance with section 218 of the Companies Act 1931 not less than 5 business days before the declaration is signed.

### **7.18 Legal proceedings — deposit takers**

(1) This rule applies to licenceholders licensed to carry on regulated activities falling within Class 1.

(2) A licenceholder must notify the Commission as soon as it becomes aware of any actual or intended legal proceedings taken by or against it where the amount claimed or disputed is likely to exceed —

- (a) £500,000 sterling or its equivalent in another currency, or
- (b) in the case of a licenceholder incorporated in the Island, 5% of the licenceholder's large exposures capital base,

whichever is the lower.

(3) Nothing in this rule requires a licenceholder to disclose any matter subject to legal professional privilege.

**7.19 Legal proceedings — investment businesses and CIS, company and trust service providers**

(1) This rule applies to licenceholders licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5 (except licenceholders to which rule 7.18 applies).

(2) A licenceholder must notify the Commission as soon as it becomes aware of any actual or intended legal proceedings taken or to be taken by or against it where the amount claimed or disputed is likely to exceed —

- (a) £100,000 sterling or its equivalent in another currency; or
- (b) in the case of a licenceholder incorporated in the Island, 10% of the licenceholder's minimum net tangible asset requirement,

whichever is the lower.

(3) Nothing in this rule requires a licenceholder to disclose any matter subject to legal professional privilege.

**7.20 Criminal proceedings against client — corporate and trust service providers**

(1) This rule applies to licenceholders licensed to carry on regulated activities falling within Class 4 or Class 5.

(2) A licenceholder must notify the Commission and, where possible, provide a brief summary of the case, as soon as it becomes aware of the bringing of any criminal proceedings against a client for, or the conviction of a client of, an offence which is or, if committed in the Island, would be triable on information.

- (3) In this rule "client" means —
  - (a) in the case of a licenceholder licensed to carry on regulated activities falling within Class 4 —
    - (i) a company which is a client of the licenceholder,
    - (ii) any officer of such a company, or
    - (iii) the beneficial owner of such a company;
  - (b) in the case of a licenceholder licensed to carry on regulated activities falling within Class 5, the trustee or settlor of any trust for which it provides services.

**7.21 Notification of default — deposit takers**

(1) This rule applies to licenceholders authorised to carry on regulated activities falling within Class 1.

(2) The licenceholder must notify the Commission immediately if an event occurs which would give rise to a claim under a scheme established by regulations under section 25 of the Act (compensation schemes).

PART 8 — RISK MANAGEMENT AND INTERNAL CONTROL

*Chapter 1 — General requirements*

**8.1 Application**

- (1) This Chapter does not apply to any licenceholder in relation to activities falling within Class 6.
- (2) Subject to paragraph (1), this Chapter applies to all licenceholders.

**8.2 Interpretation**

In this Chapter, in relation to any licenceholder, "the regulatory requirements" means the requirements of —

- (a) the conditions of the licenceholder's licence,
- (b) any direction issued to the licenceholder under section 14 of the Act;  
and
- (c) the following, so far as applicable to the licenceholder —
  - (i) any provision of the Act;
  - (ii) this Rule Book,
  - (iii) any other Rule Book under section 18 of the Act,
  - (iv) the Criminal Justice (Money Laundering) Code 2007;
  - (v) any other relevant code of practice under section 17F (money-laundering codes) of the Criminal Justice Act 1991,
  - (vi) any other provision having effect under or by virtue of the Act;  
and
  - (vii) any statutory provision referred to in section 43 of the Act.

**8.3 Corporate governance**

- (1) The responsible officers of a licenceholder are responsible for the good governance of the licenceholder and compliance with the regulatory requirements.
- (2) A licenceholder must have in place arrangements for effective corporate governance which are appropriate to its size and the nature of its business.

**8.4 Management controls**

- (1) A licenceholder must —
  - (a) organise and control its internal affairs in a responsible manner, and
  - (b) promote high ethical standards in the conduct of its regulated activities.
- (2) The responsible officers of a licenceholder must establish and maintain appropriate internal and operational controls, systems, policies and procedures relating to all aspects of its business to ensure –

- (a) effective communication between the licenceholder and its clients; and
  - (b) appropriate segregation of key duties and functions; and
  - (c) the fair treatment of clients; and
  - (d) effective maintenance of accounting and other records and the reliability of this information; and
  - (e) appropriate safeguards to prevent and detect any abuse of the licenceholder's services for money laundering, financial crime or the financing of terrorism; and
  - (f) appropriate safeguards to prevent and detect market manipulation or market abuse.
- (3) A licenceholder must review the controls required by this rule annually, or more frequently if appropriate.
- (4) Where the licenceholder employs staff or is responsible for regulated activities conducted by others, it must make adequate arrangements to ensure that they are suitable, adequately trained and properly supervised.
- (5) A licenceholder must secure that the persons to whom this paragraph applies carry out their duties in a diligent and proper manner in accordance with the systems, controls, policies and procedures referred to in paragraph (2).
- (6) Paragraph (5) applies to —
    - (a) the licenceholder's key persons; and
    - (b) any other individual, whether or not employed by the licenceholder, who performs any regulated activity in the course of his employment, or under any contract, with the licenceholder.

## **8.5 Compliance with non-statutory obligations**

A licenceholder must have regard to any code or set of standards promulgated by any authority or body other than the Commission having responsibility in the public interest for the supervision or regulation of the licenceholder's activities, except to the extent that it is inconsistent with the regulatory requirements.

## **8.6 Risk management**

- (1) A licenceholder must by its responsible officers —
  - (a) establish and maintain comprehensive policies, appropriate to the nature and scale of its business and, where appropriate, its position in the group, for managing the risks specified in paragraph (2); and
  - (b) review those policies annually.
- (2) The risks referred to in paragraph (1)(a) are —
  - (a) all material risks associated with the licenceholder, including financial, legal, regulatory and other risks posed by a group company, which may affect the licenceholder;
  - (b) all operational risks associated with the licenceholder's activities;

- (c) in the case of a licenceholder conducting regulated activities falling within Class 4 or Class 5, material regulatory and other risks to the licenceholder associated with the activities of its clients;
  - (d) any other risks which the Commission has, by notice in writing to the licenceholder, specified as additional risks for the purpose of this rule.
- (3) A notice under paragraph (2)(d) —
- (a) shall remain in force until it is withdrawn by the Commission by a further notice in writing to the licenceholder; and
  - (b) may specify actions to be taken for the purpose of measuring, monitoring and controlling the additional risks;

and the licenceholder must take such action as is specified under sub-paragraph (b).

- (4) The policies referred to in paragraph (1)(a) must include —
- (a) clear arrangements for —
    - (i) delegating (where delegation is appropriate) and separating functions which involve committing the licenceholder, paying away its funds, and accounting for its assets and liabilities;
    - (ii) reconciliation of those processes;
    - (iii) safeguarding its assets; and
    - (iv) appropriate independent internal audit and compliance procedures to test adherence to the regulatory requirements;
  - (b) appropriate procedures and controls for the purpose of identifying, measuring, monitoring and controlling the risks specified in paragraph (2);
  - (c) arrangements for regular consideration of those risks by the responsible officers.
- (5) The licenceholder must —
- (a) ensure that the policies referred to in paragraph (1)(a) are complied with;
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with those policies; and
  - (c) monitor the risks specified in paragraph (2) on a frequent and timely basis.

### **8.7 Conflicts of interest policy**

- (1) A licenceholder must establish, implement and maintain an effective conflicts of interest policy which must be —
- (a) in writing; and
  - (b) appropriate to its size and organisation and the nature, scale and complexity of its business.
- (2) Where the licenceholder is a member of a group, the policy must also take into account any circumstances of which it is or should be aware and which may

give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

(3) Where the licenceholder's functions have been delegated (whether or not to a member of the same group) the policy must also take into account any circumstances of which it is or should be aware and which may give rise to a conflict of interest arising as a result of the delegation.

- (4) The policy must —
  - (a) identify, with reference to the specific activities of the licenceholder, the circumstances which constitute or may give rise to a conflict of interest entailing a material risk of damage to the interests of one or more of its clients;
  - (b) specify procedures to be followed and measures to be adopted in order to manage such conflicts.
- (5) The procedures and measures referred to in paragraph (4)(b) must —
  - (a) ensure that any relevant persons engaged in activities involving a conflict of interest of the kind specified in paragraph (4)(a) carry on those activities at a level of independence appropriate to —
    - (i) the size and activities of the licenceholder and (where appropriate) of the group to which it belongs, and
    - (ii) the materiality of the risk of damage to the interests of clients; and
  - (b) include such of the following as are necessary and appropriate for the licenceholder to ensure the requisite degree of independence —
    - (i) effective procedures to prevent or control the exchange of information between relevant persons who are engaged in activities involving a risk of a conflict of interest, where the exchange of that information may harm the interests of one or more clients;
    - (ii) the separate supervision of relevant persons whose principal functions involve carrying out activities on behalf of, or providing services to, clients whose interests may conflict, or who otherwise represent different interests that may conflict, including those of the licenceholder;
    - (iii) the removal of any direct link between the remuneration of relevant persons principally engaged in one activity and the remuneration of, or revenues generated by, different relevant persons principally engaged in another activity, where a conflict of interest may arise in relation to those activities;
    - (iv) measures to prevent or limit any person from exercising inappropriate influence over the way in which a relevant person carries on regulated activities;
    - (v) measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate activities where

such involvement may impair the proper management of conflicts of interest.

## **8.8 Conflicts of interest register**

- (1) A licenceholder must maintain a register of conflicts of interest.
- (2) The register referred to in paragraph (1) —
  - (a) may be in summary form, provided that a full record of each conflict of interest and the measures adopted to manage it is kept elsewhere;
  - (b) must contain the following information relating to each conflict of interest —
    - (i) a description of the regulated activity in relation to which the conflict arises;
    - (ii) the name of the client, or the description of clients, whose interests are at a material risk of damage by reason of the conflict;
    - (iii) the nature of the conflict;
    - (iv) if the conflict arises by reason of the involvement of an officer, employee or tied agent of the licenceholder or of a person employed by them (in the latter case, the name of the person concerned);
    - (v) the measures adopted to manage the conflict;
    - (vi) the date when the conflict was first identified; and
    - (vii) if the conflict has ceased, the date when it ceased and the grounds for considering that it has ceased.
- (3) The information relating to a conflict of interest must be kept on the register until at least 6 years after the date mentioned in paragraph (2)(b)(vii).

## **8.9 Business plan**

- (1) A licenceholder must operate in accordance with its business plan.
  - (2) Where —
    - (a) any matter to be notified by a licenceholder to the Commission under rule 8.10 involves a material change in its activities as set out in its business plan, or
    - (b) the licenceholder ceases to carry on any description of regulated activity,
- the licenceholder must, before or as soon as practicable after the change takes place —
- (i) draw up a fresh business plan incorporating any necessary amendments to take account of that change; and
  - (ii) provide the Commission with a copy of the plan.

(3) In this rule “business plan” means a statement describing the licenceholder’s business or projected business, containing such details and projections as the Commission may reasonably require; and references to a licenceholder’s business plan are to —

- (a) the statement most recently provided under paragraph (2)(ii); or
- (b) if none has been so provided, the statement submitted to the Commission with the licenceholder’s application for a licence.

#### **8.10 Changes to activities, services or products**

A licenceholder must notify the Commission, not less than 20 business days in advance, of any addition or material change to —

- (a) any regulated activities which it carries on, or
- (b) any of the services or products which it offers, whether or not their provision constitutes a regulated activity.

#### **8.11 Business resumption and contingency arrangements**

A licenceholder must —

- (a) establish and maintain business resumption and contingency arrangements which are appropriate to the nature and scale of its business; and
- (b) test those arrangements at appropriate intervals.

#### **8.12 Business continuity**

A licenceholder must —

- (a) establish and maintain arrangements for safeguarding the interests of its clients, appropriate to the size and organisation and the nature, scale and complexity of its business, in the event of —
  - (i) the death, incapacity or sickness; and
  - (ii) holidays and other periods of absence,of the individuals responsible for controlling or carrying on its activities;
- (b) cover the arrangements referred to in subparagraph (a) with either a disaster recovery plan or a locum;
- (c) provide the Commission with details of those arrangements on request; and
- (d) notify the Commission of any substantial changes to those arrangements.

#### **8.13 Delegation of function, outsourcing or inward-outsourcing**

(1) A licenceholder may not, without the consent in writing of the Commission —



- (a) delegate any material management or business function to another person (whether or not that person is another company within the same group as the licenceholder);
- (b) make any material change to any such delegation.
- (2) Any such delegation must be evidenced by a written agreement between the parties setting out clearly —
  - (a) their respective responsibilities and duties, including the monitoring of the delegated function by the licenceholder, and
  - (b) the provisions for terminating the delegation.
- (3) Any such delegation shall not affect the ultimate responsibility of the licenceholder for the delegated functions.
- (4) The licenceholder must ensure that —
  - (a) the Commission has access to all records relating to the delegated functions;
  - (b) in the event of a breakdown in the delegation, the licenceholder is able to carry out or assume control of the delegated functions.

#### **8.14 Breaches of regulatory requirements**

- (1) A licenceholder must notify the Commission as soon as it becomes aware of a breach by the licenceholder of any of the regulatory requirements.
- (2) Where a licenceholder gives a notification under paragraph (1), it must also inform the Commission of the steps which it proposes to take to remedy the situation.
- (3) A licenceholder must maintain a register of all breaches referred to in paragraph (1).

#### **8.15 Fraud or dishonesty**

- (1) A licenceholder must notify the Commission as soon as —
  - (a) it has reason to believe that a controller, director or employee of the licenceholder has been engaged in activities involving fraud or other dishonesty; or
  - (b) it becomes aware of any event which may amount to fraud or serious mismanagement in the conduct of its business.
- (2) A notification under this rule, except in the case of a controller, director or key person, need not disclose the name of the individual concerned.

#### **8.16 Investigation of member's conduct by professional body**

A licenceholder must notify the Commission as soon as it becomes aware of any action of the following kinds taken against a controller, director or key person by a professional body of which that person is a member —

- (a) an inquiry into that person's professional conduct;

- (b) the termination of that person's membership;
- (c) any disciplinary action against him;
- (d) any censure of his conduct.

### **8.17 Matters to be notified — general**

(1) Without prejudice to the specific requirements of any other rule, a licenceholder must notify the Commission of any relevant material change affecting its business, systems, controllers, responsible officers and key persons.

(2) A licenceholder must notify the Commission as soon as it becomes aware that any of the following has occurred, whether within or outside the Island —

- (a) the breakdown of administrative or control procedures relevant to any of the licenceholder's business (including breakdowns of computer systems or other accounting problems resulting, or likely to result in, failure to maintain proper records);
- (b) any event which makes it impracticable for a licenceholder to comply with any of the regulatory requirements;
- (c) the appointment of inspectors by a statutory or other regulatory authority to investigate the affairs of the licenceholder or any associated company;
- (d) the imposition of disciplinary measures or sanctions on the licenceholder or any associated company, in relation to its business, by any statutory or other regulatory authority;
- (e) any event which may constitute market manipulation or market abuse by the licenceholder or any controller, director, key person or employee;
- (f) an application by the licenceholder or its immediate parent or subsidiary for authorisation to carry on an activity in any country or territory outside the Island which, if carried on in the Island, would be a regulated activity;
- (g) the refusal of any application mentioned in sub-paragraph (f); or
- (h) the revocation of any such authorisation of the licenceholder or an associated company as is mentioned in sub-paragraph (f).

(3) Where a licenceholder gives a notification under paragraph (2)(a) or (b), it must also inform the Commission of the steps which it proposes to take to remedy the situation.

#### Officers of licenceholders

### **8.18 Compliance officer and money laundering reporting officer**

- (1) A licenceholder must appoint the following officers —
  - (a) a compliance officer with responsibility for overseeing the licenceholder's compliance with the regulatory requirements, including those relating to money laundering and combating the financing of terrorism;

- (b) a money laundering reporting officer as required by the Criminal Justice (Money Laundering) Code 2007; and
- (c) a deputy money laundering reporting officer to cover for any absence of the money laundering reporting officer.
- (2) The same individual may be appointed as compliance officer and as money laundering reporting officer or deputy money laundering officer.
- (3) A compliance officer must have —
  - (a) appropriate independence and direct access to the licenceholder's responsible officers;
  - (b) unfettered access to all business lines and support departments;
  - (c) appropriate status within the licenceholder to ensure that the directors and senior management react appropriately to recommendations; and
  - (d) sufficient time and resources to discharge properly the responsibilities of the position.
- (4) This rule does not apply to a licenceholder who is licensed to carry on only activities falling within either or both of —
  - (a) paragraph (6) of Class 4 (acting as officer of company), and
  - (b) paragraph (2) or (5) of Class 5 (acting as trustee or protector).

#### **8.19 Functions of compliance officer**

A compliance officer is responsible, in relation to the requirements referred to in rule 8.18(1)(a), for ensuring that –

- (a) the licenceholder has robust and documented arrangements appropriate to the nature and size of the business for compliance with those requirements;
- (b) the operational performance of those arrangements is suitably monitored;
- (c) prompt action is taken to remedy any deficiencies in arrangements; and
- (d) the registers required by rules 8.8, 8.14 and 8.29 are maintained.

#### **8.20 Isle of Man resident directors**

- (1) This rule applies to a licenceholder which is incorporated in the Isle of Man.
- (2) Not less than two of the licenceholder's directors must be resident in the Isle of Man.

#### **8.21 Isle of Man resident officers**

- (1) A licenceholder must —
  - (a) secure that its business is effectively controlled on a day-to-day basis by at least 2 nominated individuals —

- (i) who are directors or key persons; and
  - (ii) who are resident in the Island; and
  - (iii) who have joint responsibility for overseeing the licenceholder's proper conduct; and
  - (iv) whose functions are separated, where appropriate.
- (b) establish and maintain internal procedures to ensure that sub-paragraph (a) is complied with.
- (2) A nominated individual referred to in paragraph (1) is in this Rule Book referred to as an Isle of Man resident officer.

### **8.22 Absence of Isle of Man resident officers**

A licenceholder must have appropriate arrangements, approved by the Commission, in place so that, if it is at any time unable to comply with rule 8.21, either temporarily or otherwise, a fit and proper person exercises the functions of the Isle of Man resident officer so that the licenceholder's regulated activities can continue without interruption.

### **8.23 Company secretary**

The secretary of a licenceholder incorporated under the Companies Act 1931 to which section 19(4) of the Companies Act 1982 does not apply must be an individual who is —

- (a) qualified in accordance with that section; or
- (b) in the case of a licenceholder licensed to carry on activities of Class 1, an associate of the Chartered Institute of Bankers or an associate of the ifs School of Finance; or
- (c) approved by the Commission as suitable, by virtue of his knowledge and experience, to be secretary of the licenceholder.

### **8.24 Systems and controls for record keeping**

(1) A licenceholder must establish and maintain procedures to ensure that sufficient information is recorded and retained about the conduct of its business and its compliance with the regulatory requirements.

(2) A licenceholder must establish and maintain adequate systems and controls over its general records, having regard to its size and the nature and complexity of its activities.

- (3) The systems and controls referred to in paragraph (2) must be —
  - (a) such as to enable the licenceholder to comply with the regulatory requirements; and
  - (b) adequately and correctly documented.
- (4) A licenceholder must —
  - (a) maintain records relating to its business transactions, financial position, internal organisation and risk management systems such as to

demonstrate to the Commission that it complies with the regulatory requirements; and

- (b) keep those records for at least 6 years after it ceases to hold a licence.

### **8.25 Clients' records**

(1) A licenceholder must keep and maintain proper records to show and explain transactions effected by it on behalf of its clients.

(2) Those records must —

- (a) be kept in English;
- (b) be kept up to date;
- (c) be in such a form as to demonstrate compliance with the regulatory requirements.

### **8.26 Records kept by third parties**

For the purpose of rules 8.24 and 8.25 a licenceholder may accept and rely on records supplied by a third party so long as those records are capable of being, and are, reconciled with records created by the licenceholder.

### **8.27 Relations with regulators**

A licenceholder must —

- (a) co-operate in an open and honest manner with the Commission and any other regulatory body to which it is accountable, and
- (b) keep them promptly informed of anything relevant to the exercise of their regulatory functions.

### **8.28 Compliance returns**

(1) A licenceholder must make a return (an "annual compliance return") to the Commission within 4 months of the licenceholder's annual reporting date.

(2) The return must —

- (a) state the position as at the annual reporting date, and
- (b) be in the form, contain the information and be accompanied by the documents specified in Schedule 8.1.

## **Complaints**

### **8.29 Complaints**

(1) A licenceholder must ensure, in relation to any written complaint received relating to its regulated activities, that —

- (a) the complaint is recorded in a complaints register;
- (b) where appropriate, further details in writing, with supporting evidence, are requested from the complainant;

- (c) the complaint is brought to the attention of an officer or employee of the licenceholder with appropriate authority to deal with complaints;
  - (d) the complaint is investigated promptly and thoroughly within 12 weeks of receipt;
  - (e) appropriate action is taken and recorded; and
  - (f) the complainant is notified of the outcome of the investigation and of any action taken.
- (2) A licenceholder must —
    - (a) have documented procedures for dealing with complaints from clients;
    - (b) make those procedures readily accessible on request; and
    - (c) ensure that any remedial action needed is taken promptly (including, where appropriate, correcting any failures or weaknesses in its systems and procedures and carrying out training of its staff).
  - (3) Any procedures referred to in paragraph (2)(a) must —
    - (a) comply with paragraph (1); and
    - (b) include reference to the Financial Services Ombudsman Scheme where appropriate.
  - (4) The register referred to in paragraph (1)(a) —
    - (a) may be in summary form, provided that a full record of the complaint and action taken in relation to the complaint is kept elsewhere;
    - (b) must contain the following information relating to each complaint —
      - (i) the name and address of the complainant;
      - (ii) the date when the complaint was received;
      - (iii) the date when the complaint was reported to the person with authority to deal with complaints;
      - (iv) the nature of the complaint;
      - (v) whether the complaint involves a breach of the regulatory requirements;
      - (vi) how and when the complaint was investigated;
      - (viii) the action taken to resolve the complaint;
      - (ix) the date the complaint is considered closed; and
      - (x) whether the licenceholder's professional indemnity insurers were informed, if applicable.

## ***Chapter 2— Specific requirements for all deposit takers***

### **8.30 Application**

This Chapter applies to all licenceholders which are licensed to carry on regulated activities falling within Class 1.

### **8.31 Risk management policies**

(1) A licenceholder must provide the Commission with a copy of the policies referred to in rule 8.6(1)(a), and any substantial amendment of those policies, within 20 business days of the approval by the responsible officers of the policies or amendment.

(2) A licenceholder must notify the Commission, within 4 months after the end of its financial year, that at their last full meeting the responsible officers reviewed and approved the policies referred to in rule 8.6(1)(a) and were satisfied that they were up to date and appropriate.

## ***Chapter 3— Specific requirements for deposit takers incorporated in the Island***

### **8.32 Application**

(1) This Chapter applies to all licenceholders which are licensed to carry on regulated activities falling within Class 1 and are incorporated in the Island.

(2) This Chapter is without prejudice to the generality of rule 8.6.

### **8.33 Corporate governance**

(1) The directors of a licenceholder must ensure that its regulated activities are managed and controlled from the Island.

(2) At least one director of a licenceholder must be of non-executive status.

### **8.34 Credit risk policy**

(1) A licenceholder must by its directors —

- (a) establish and maintain a credit risk policy which is appropriate to the nature and scale of its business; and
- (b) review that policy annually.

(2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by its directors of the policy or amendment.

(3) The policy must include —

- (a) limits on different types of lending (including geographical, economic and individual sectors),
- (b) provisions in respect of connected and related party lending,
- (c) provisions in respect of sanctioning limits and authorisation procedures,
- (d) provisions as to permissible forms of security;
- (e) monitoring and control procedures, and
- (f) arrears and provisioning procedures.

(4) A licenceholder must —

- (a) secure that the policy is complied with, and
- (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

### **8.35 Large exposures policy**

- (1) A licenceholder must by its directors —
  - (a) establish and maintain a large exposures policy which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by the directors of the policy or amendment.
- (3) The policy must include —
  - (a) exposure limits for customers, counterparties, countries and economic sectors,
  - (b) sanctioning limits and authorisation procedures,
  - (c) permissible forms of security or collateral,
  - (d) procedures where exposures are to a guarantor,
  - (e) monitoring and control procedures, and
  - (f) a regulatory reporting policy.
- (4) A licenceholder must —
  - (a) secure that the policy is complied with, and
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

### **8.36 Large exposure management**

- (1) A licenceholder must —
  - (a) not incur an exposure which (including accrued interest) exceeds 25% of its large exposures capital base (“LECB”), unless the exposure is an exempt exposure; or
  - (b) not incur large exposures, excluding exempt exposures, exceeding in the aggregate 800% of its LECB.
- (2) A licenceholder must maintain appropriate procedures and controls for the purpose of monitoring its large exposures on a daily basis.
- (3) A licenceholder must —
  - (a) notify the Commission before entering into an exempt exposure, except —
    - (i) an exposure falling within rule 8.38(a); or



- (ii) where the Commission has directed that the exposure need not be notified;
  - (b) notify the Commission immediately when the total of its large exposures, excluding exempt exposures, exceeds or is likely to exceed 300% of its LECB;
  - (c) notify the Commission immediately of any breach of —
    - (i) the limit in paragraph (1)(a) or (b), or
    - (ii) any other counterparty limit agreed with the Commission for the purpose of this sub-paragraph;
  - (d) notify the Commission immediately if its adjusted capital base falls below its current LECB.
- (4) A licenceholder must report to the Commission as at each quarter-end, within 20 business days of the quarter-end, all exposures (including exempt exposures) which have equalled or exceeded 10% of its LECB during that quarter; and for this purpose no account shall be taken of —
- (a) accrued interest; or
  - (b) any provision for bad and doubtful debts.

### **8.37 Calculation of exposures**

- (1) A licenceholder must calculate any exposure as the gross amount at risk from —
- (a) claims, including —
    - (i) actual and potential claims which would arise from the drawing down in full of undrawn advised facilities (revocable or irrevocable, conditional or unconditional) which the licenceholder has committed itself to provide, and
    - (ii) claims which the licenceholder has committed itself to purchase or underwrite;
  - (b) contingent liabilities, including —
    - (i) those which arise in the normal course of business, and
    - (ii) those which would arise from the drawing down in full of undrawn advised facilities (whether revocable or irrevocable, conditional or unconditional) which the licenceholder has committed itself to provide; and
  - (c) assets, including those which the licenceholder has committed itself to purchase or underwrite —
    - (i) whose value depends wholly or mainly on a counterparty performing its obligations, or
    - (ii) whose value otherwise depends on a counterparty's financial soundness but which do not represent a claim on the counterparty.

(2) Except as provided in rule 8.36(4), in calculating an exposure a specific provision made against a loan should be set off against the gross amount of the exposure.

(3) If a third party has provided an express unconditional and irrevocable guarantee in respect of an exposure, a licenceholder may report the exposure as being to the guarantor.

(4) A licenceholder must not net its claims and obligations in calculating its exposure to a counterparty unless —

- (a) there is a legally enforceable contract allowing the licenceholder to set off any claim against the counterparty; and
- (b) it notified the Commission before it entered into the contract.

### **8.38 Exempt exposures**

The following exposures are exempt exposures —

- (a) exposures of one year or less to banks in Zone A countries (excluding multilateral development banks) not related to a licenceholder, provided that —
  - (i) the placing is not subject to any form of charge or pledge, and
  - (ii) the exposure is part of a licenceholder's normal treasury operations;
- (b) exposures to or guaranteed by central governments and central banks of Zone A countries;
- (c) exposures to central governments of Zone B countries if they are denominated in local currency and funded by liabilities in the same currency;
- (d) exposures secured by either cash (including certificates of deposit issued by the lending bank) held by the lender, a guarantee by the central government of a Zone A country, or central bank securities, provided that —
  - (i) the legal title of the lender is fully protected;
  - (ii) only the portion of an exposure which is fully secured by cash or securities and over which a licenceholder has a full right of set-off is exempt for this purpose;
  - (iii) if the security is in a different currency from the exposure or is in the form of securities, the amount of the collateral includes a margin to cover possible fluctuations in value;
- (e) exposures to other group companies which are credit institutions in Zone A countries;
- (f) exposures with parental guarantees.

### **8.39 Arrears and provisions policy for bad and doubtful debts**

- (1) A licenceholder must by its directors —

- (a) establish and maintain a policy on arrears and provisions for bad and doubtful debts which is appropriate to the nature and scale of its business; and
- (b) review that policy annually.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by the directors of the policy or amendment.
- (3) A licenceholder must —
  - (a) secure that the policy is complied with, and
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.
- (4) A licenceholder must —
  - (a) hold an adequate level of provisions for specific bad and doubtful debts; and
  - (b) report to the Commission its arrears and provisions for bad and doubtful debts —
    - (i) as at each quarter-end, within 20 business days of the quarter-end, or
    - (ii) at such other intervals as may be required by the Commission, within 20 business days of the reporting date.

#### **8.40 Liquidity policy**

- (1) A licenceholder must by its directors —
  - (a) establish and maintain a prudent liquidity policy (including specific limits for liquidity) which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by the directors of the policy or amendment.
- (3) A licenceholder must —
  - (a) secure that the policy is complied with, and
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.
- (4) A licenceholder must —
  - (a) establish and maintain an appropriate liquidity contingency plan, and
  - (b) provide the Commission with a copy of the plan.

#### **8.41 Liquidity management**

- (1) A licenceholder must —

- (a) maintain liquidity at the minimum level specified in paragraph (2); and
- (b) measure and monitor liquidity, as frequently as is appropriate, by calculation of mismatch positions.
- (2) The level of liquidity referred to in paragraph (1)(a) is within —
  - (a) such mismatch limits as the Commission may direct, or
  - (b) if no such direction is given, the following mismatch limits —

sight to 8 days	0%
sight to 1 month	-5%
- (3) A licenceholder must —
  - (a) notify the Commission immediately of any breach of paragraph (1)(a);
  - (b) remedy any such breach and take action to prevent future breaches as soon as possible; and
  - (c) report its liquidity positions to the Commission as at each quarter-end, within 20 business days of the quarter-end.

#### **8.42 Foreign exchange risk**

- (1) A licenceholder must by its directors —
  - (a) establish and maintain a prudent foreign exchange risk management policy (including specific limits of risk) which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually, or more frequently if appropriate.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by the directors of the policy or amendment.
- (3) A licenceholder must —
  - (a) secure that the policy is complied with, and
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.
- (4) A licenceholder must maintain appropriate procedures and controls for the purpose of measuring and monitoring its foreign exchange risks on a frequent and timely basis.
- (5) A licenceholder must report its foreign exchange risk positions to the Commission as at each quarter-end, within 20 business days of the quarter-end.

#### **8.43 Interest rate risk**

- (1) A licenceholder must by its directors —
  - (a) establish and maintain a prudent interest rate risk management policy (including specific limits of risk) which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually, or more frequently if appropriate.

(2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the approval by the directors of the policy or amendment.

(3) A licenceholder must —

- (a) ensure that the policy is complied with, and
- (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

(3) A licenceholder must maintain appropriate procedures and controls for the purpose of measuring and monitoring its interest rate risks on a frequent and timely basis.

(4) A licenceholder must report its interest rate risk positions to the Commission as at each quarter-end, within 20 business days of the quarter-end.

#### **8.44 Annual review of certain policies**

A licenceholder must notify the Commission, within 4 months after the end of its financial year, that at their last full meeting the directors reviewed and approved each of the following and were satisfied that they were up to date and appropriate —

- (a) its credit risk policy under rule 8.34;
- (b) its large exposures policy under rule 8.35;
- (c) its policy on arrears and provisions for bad and doubtful debts under rule 8.39;
- (d) its liquidity policy under rule 8.40;
- (e) its foreign exchange risk management policy under rule 8.42; and
- (f) its interest rate risk management policy under rule 8.43.

#### **8.45 Capital charge for operational risk**

(1) A licenceholder must notify the Commission of its capital charge for operational risk, calculated in accordance with Form SR-1C in Schedule 2.1, as at each quarter-end.

(2) A notification under paragraph (1) must be given within 20 business days of the quarter-end.

### ***Chapter 4 — Specific requirements for deposit takers incorporated outside the Island***

#### **8.46 Application**

(1) This Chapter applies to all licenceholders which are licensed to carry on regulated activities falling within Class 1 and are incorporated in a country or territory outside the Island.

(2) This Chapter is without prejudice to the generality of rule 8.6.

#### **8.47 Credit risk policy**

- (1) A licenceholder must —
  - (a) establish and maintain a credit risk policy which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the adoption of the policy or amendment.
- (3) The policy must include —
  - (a) limits on different types of lending (including geographical, economic and individual sectors),
  - (b) limits on connected and related party lending,
  - (c) provisions in respect of sanctioning limits and authorisation procedures,
  - (d) provisions as to permissible forms of security or collateral;
  - (e) monitoring and control procedures, and
  - (f) arrears and provisioning procedures.
- (4) A licenceholder must —
  - (a) secure that the policy is complied with, and
  - (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

#### **8.48 Large exposures**

- (1) A licenceholder must report to the Commission as at each quarter-end, within 20 business days of the quarter-end —
  - (a) the 10 largest exposures to banks and other credit institutions, and
  - (b) the 10 largest exposures other than those within sub-paragraph (a), which relate to its operations in or from the Island.
- (2) A licenceholder must have and comply with documented controls and procedures in accordance with the large exposures policy of its head office or parent company.

#### **8.49 Arrears and provisions policy for bad and doubtful debts**

- (1) A licenceholder must —
  - (a) establish and maintain a policy on arrears and provisions for bad and doubtful debts which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually.

(2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the adoption of the policy or amendment.

(3) A licenceholder must —

- (a) secure that the policy is complied with, and
- (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

(4) A licenceholder must —

- (a) hold an adequate level of provisions for specific bad and doubtful debts; and
- (b) report to the Commission its arrears and provisions for bad and doubtful debts as at each quarter-end, within 20 business days of the quarter-end.

### **8.50 Liquidity policy**

(1) A licenceholder must —

- (a) establish and maintain a prudent liquidity policy (including specific limits for liquidity) which is appropriate to the nature and scale of its business; and
- (b) review that policy annually or more frequently if appropriate.

(2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the adoption of the policy or amendment.

(3) A licenceholder must —

- (a) secure that the policy is complied with, and
- (b) maintain appropriate procedures and controls for the purpose of monitoring its compliance with the policy.

(4) A licenceholder must —

- (a) establish and maintain an appropriate liquidity contingency plan, and
- (b) provide the Commission with a copy of the plan.

### **8.51 Liquidity management**

(1) A licenceholder must measure and monitor its liquidity, as frequently as appropriate, by calculation of mismatch positions.

(2) A licenceholder must report its liquidity positions to the Commission as at each quarter-end, within 20 business days of the quarter-end.

### **8.52 Foreign exchange risk**

(1) A licenceholder must —

- (a) establish and maintain a prudent foreign exchange risk management policy (including specific limits of risk) which is appropriate to the nature and scale of its business; and
- (b) review that policy annually, or more frequently if appropriate.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the adoption of the policy or amendment.
- (3) A licenceholder must maintain appropriate procedures and controls for the purpose of measuring and monitoring its foreign exchange risks on a frequent and timely basis.

### **8.53 Interest rate risk**

- (1) A licenceholder must —
  - (a) establish and maintain a prudent interest rate risk management policy (including specific limits of risk) which is appropriate to the nature and scale of its business; and
  - (b) review that policy annually, or more frequently if appropriate.
- (2) A licenceholder must provide the Commission with a copy of the policy, and any substantial amendment of that policy, within 20 business days of the adoption of the policy or amendment.
- (3) A licenceholder must maintain appropriate procedures and controls for the purpose of measuring and monitoring its interest rate risks on a frequent and timely basis.

## ***Chapter 5— Specific requirements for investment businesses and CIS service, corporate service and trust service providers***

### **8.54 Professional indemnity insurance**

- (1) This rule applies to all licenceholders which are licensed to carry on regulated activities falling within Class 2, Class 3, Class 4 or Class 5, but does not apply to any such licenceholder which is also licensed to carry on regulated activities falling within Class 1.
- (2) Subject to paragraphs (4) to (6), unless the Commission otherwise directs, a licenceholder must maintain professional indemnity insurance which —
  - (a) is appropriate to the nature and size of its business, and
  - (b) in any event provides the minimum cover specified in paragraph (3).
- (3) The cover required by paragraph (2)(b) is, in the case of a licenceholder licensed to carry on regulated activities falling within a class, and the paragraphs of a class, specified in columns 1 and 2 of Schedule 8.2 —
  - (a) the amount specified in column 4 of that Schedule, or
  - (b) 3 times its annual turnover in the previous year ending on the licenceholder's annual reporting date,



whichever is the greater.

(4) Where the licenceholder carries on 2 or more regulated activities in respect of which different amounts are specified as mentioned in paragraph (3)(a), paragraph (2) shall be taken as requiring cover of the higher amount so specified.

(5) A licenceholder is not required to maintain cover exceeding £10,000,000 in aggregate.

(6) No account shall be taken of insurance provided by —

(a) an insurer which has been notified by the Commission to the licenceholder as being unsatisfactory for the purpose of this rule; or

(b) an insurer located in a country or territory, other than the Island or the United Kingdom, which has been notified by the Commission to the licenceholder as being unsatisfactory for the purpose of this rule (having regard to the system of regulation of insurers in force there).

(7) A licenceholder must notify the Commission as soon as practicable of —

(a) any claim exceeding £10,000 on its insurance; and

(b) any change in the insurance previously notified to the Commission.

#### **8.55 Retention of client records**

(1) This rule applies to all licenceholders which are licensed to carry on regulated activities falling within Class 2.

(2) Subject to paragraphs (4) and (5), a licenceholder must keep —

(a) the records which it is required by this Part to make;

(b) copies of the statements which it is required by rule 6.49 (contract note etc.) to provide; and

(c) any working papers which are created to assist in the preparation of the financial returns required to be prepared under Part 2;

for not less than 6 years after the date on which they are made or provided.

(3) The documents referred to in paragraph (2) must be kept either —

(a) at a place where the licenceholder carries on business, or

(b) in such a manner that they can be produced at such a place within 24 hours of demand.

(4) In the case of a transaction which relates to long-term business within the meaning of the Insurance Act 1986, a licenceholder must keep the records referred to in paragraph (2) for the duration of the contract in question.

(5) In the case of pension transfers, pension opt-outs or free-standing additional voluntary contributions a licenceholder must keep the records referred to in paragraph (2) indefinitely.

### **8.56 Inspection of records**

(1) This rule applies to all licenceholders licensed to carry on regulated activities falling within Class 2.

(2) Subject to paragraph (3), a licenceholder must allow each of its clients during business hours to inspect, either personally or by his agent, any entry in a record kept by it of matters relating to the client —

- (a) as soon as practicable, and
- (b) in any event, not more than 10 business days after it receives a request to carry out such an inspection.

(3) Paragraph (2) applies to records which do not relate exclusively to the client subject to any prohibition or limitation imposed by or under the Data Protection Act 2002.

### **8.57 Pricing errors**

(1) This rule applies to all licenceholder licensed to carry on regulated activities falling within Class 3.

(2) A licenceholder must notify the Commission as soon as it becomes aware of a pricing error in relation to a collective investment scheme.

(3) Where a licenceholder makes a notification under paragraph (1), it must also inform the Commission of the steps which it proposes to take to remedy the error and prevent a repetition of the error.

(4) A licenceholder must maintain a register of all errors referred to in paragraph (1).

### **8.58 Provision of officers**

(1) This rule applies to all licenceholders which are licensed to carry on regulated activities falling within Class 4.

(2) Where a licenceholder carries on a regulated activity falling within paragraph (8) of Class 4 (providing officer of company) it must take reasonable steps to ensure that the person concerned —

- (a) is a suitable and competent person to undertake the office in question, and
- (b) understands the duties and responsibilities of the office.

(3) Where the person concerned is a body corporate, the licenceholder's obligation under paragraph (2) relates to the directors of the body corporate.

(4) Where the person concerned is an officer of or employed by, or a professional associate of, the licenceholder, the licenceholder must take reasonable steps to ensure that the person concerned undertakes the office in a diligent and proper manner.

## PART 9 — MONEY-LAUNDERING AND FINANCING OF TERRORISM

### 9.1 Application

This Part applies to all licenceholders.

### 9.2 Interpretation

(1) In this Part —

"beneficial owner" means the natural person who ultimately owns or controls an applicant for business or on whose behalf a transaction or activity is being conducted; and in relation to a legal person or legal arrangement, includes (but is not restricted to) —

- (a) in the case of a legal person other than a company whose securities are listed on a recognised stock exchange, a natural person who ultimately owns or controls (whether through direct or indirect ownership or control, including through bearer share holdings) more than 25% of the shares or voting rights in the legal person; or
- (b) in the case of any legal person, a natural person who otherwise exercises control over the management of the legal person;
- (c) in the case of a legal arrangement —
  - (i) the trustees or other persons controlling the applicant; and
  - (ii) the settlor or other person by whom the arrangement is made,

"the Code" means the Criminal Justice (Money Laundering) Code 2007;

"correspondent banking services" means banking services provided by a financial institution in one country or territory ("the correspondent bank") to a financial institution in another country or territory ("the respondent bank");

"customer due diligence" (except in the expression "enhanced customer due diligence") means the measures specified in paragraphs 5 to 8 of the Code;

"legal arrangement" means —

- (a) an express trust, or
- (b) any other arrangement which has a similar legal effect (such as a *fiducie*, *Treuhand* or *fideicomiso*);

"legal person" includes any body corporate or unincorporate which is capable of establishing a permanent customer relationship with a financial institution or of owning property;

"money laundering reporting officer" means an individual appointed under paragraph 14(1) of the Code;

"payable-through account" means an account maintained by a correspondent bank which may be operated directly by a customer of the respondent bank;

"politically exposed person" means any of the following resident in a country or territory outside the Island —

- (a) a natural person who is or has been entrusted with prominent public functions, including —
  - (i) a head of state, head of government, minister or deputy or assistant minister;
  - (ii) a senior government official;
  - (iii) a member of parliament;
  - (iv) a senior politician;
  - (v) an important political party official;
  - (vi) a senior judicial official;
  - (vii) a member of a court of auditors or the board of a central bank;
  - (viii) an ambassador, chargé d'affaires or other high-ranking officer in a diplomatic service;
  - (ix) a high-ranking officer in an armed force;
  - (x) a senior member of an administrative, management or supervisory body of a State-owned enterprise; and
  - (xi) a senior official of an international entity or organisation;
- (b) any of the following family members of a person mentioned in sub-paragraph (a) —
  - (i) a spouse;
  - (ii) a partner considered by national law as equivalent to a spouse;
  - (iii) a child or the spouse or partner of a child;
  - (iv) a brother or sister (including a half-brother or half-sister);
  - (v) a parent;
  - (vi) a parent-in-law;
  - (vii) a grandparent; and
  - (viii) a grandchild;
- (c) any close associate of a person mentioned in sub-paragraph (a), including —
  - (i) any natural person who is known to have joint beneficial ownership of a legal entity or legal arrangement, or any other close business relations, with such a person;
  - (ii) any natural person who has sole beneficial ownership of a legal entity or legal arrangement which is known to have been set up for the benefit of such a person;
  - (iii) any natural person who is known to be beneficiary of a legal arrangement of which such a person is a beneficial owner or beneficiary;
  - (iii) any natural person who is in a position to conduct substantial financial transactions on behalf of such a person.

"risk" means a risk of money laundering or the financing of terrorism, or both;

- (2) In this Part "shell bank" means a bank which is —
  - (a) incorporated in a country or territory in which it has no physical presence, and
  - (b) not affiliated with a financial services group which is subject to effective consolidated supervision;

and for this purpose —

"consolidated supervision", in relation to a financial services group, means supervision of the group by a regulatory body on the basis of the totality of its business, wherever conducted;

"financial services group" means a group of companies whose activities include to a significant extent activities which are, or if carried on in the Island would be, regulated activities.

(3) In this Part the following expressions have the same meanings as in the Code —

"applicant for business"

"business relationship"

"FATF Recommendations"

"one-off transaction"

### **9.3 Anonymous accounts etc.**

- (1) A licenceholder must not maintain —
  - (a) an anonymous account, or
  - (b) an account in a fictitious name.
- (2) If a licenceholder maintains a numbered account it must —
  - (a) identify, and verify the identity of, the customer, and
  - (b) maintain the account in such a way as to comply fully with the requirements of the Code and this Part.

### **9.4 Business risk assessment**

(1) For the purpose of determining the measures to be taken when carrying out customer due diligence, a licenceholder must carry out a risk assessment in accordance with this rule.

(2) The assessment must estimate the risk of money laundering and terrorist financing on the part of the licenceholder's customers, having regard to —

- (a) the nature, scale and complexity of its activities;
  - (b) the products and services provided by it, and
  - (c) the persons to whom, and the manner in which, they are provided.
- (3) The assessment must be —

- (a) undertaken as soon as reasonably practicable —
  - (i) after this Part comes into force, in the case of an existing business;
  - (ii) after the licenceholder commences business, in any other case; and
- (b) regularly reviewed and, where appropriate, amended so as to keep it up to date.

## **9.5 Customer due diligence — general**

When carrying out customer due diligence, whether in relation to an applicant for business, an existing business relationship or a one-off transaction, a licenceholder must do so —

- (a) on the basis of materiality and risk, and
- (b) in accordance with its current risk assessment under rule 9.4.

## **9.6 Customer due diligence procedures**

(1) This rule applies where a licenceholder is operating the procedures required by paragraphs 5 to 8 of the Code, except where paragraph 5(4) or 7(4) of the Code applies.

- (2) The licenceholder must, in the case of any applicant for business, —
  - (a) determine who is the beneficial owner of the applicant;
  - (b) take reasonable steps to verify the identity of those persons, using relevant information or data obtained from a reliable source; and
  - (c) determine whether the applicant is acting on behalf of another person and, if so, take reasonable steps to identify that other person, and to verify his identity using relevant information or data obtained from a reliable source.

(3) Without prejudice to paragraph (2), the licenceholder must, in the case of an applicant for business which is a legal person or legal arrangement —

- (a) verify that any person purporting to act on behalf of the applicant is authorised to do so;
- (b) identify and verify the identity of that person using reliable and independent source documents, data or information;
- (c) in the case of a legal arrangement, identify any known beneficiaries;
- (d) verify the legal status of the applicant using relevant information or data obtained from a reliable source;
- (e) obtain information concerning the names and addresses of the applicant and any natural persons having power to direct its activities;
- (f) obtain information concerning the person by whom, and the method by which, binding obligations may be imposed on the applicant;

(g) take reasonable steps to understand the ownership and control structure of the applicant.

(4) Where the licenceholder deals with an applicant for business otherwise than face-to-face, it must, in taking any steps under this rule, take adequate measures to compensate for any risk arising as a result.

(5) The licenceholder must not proceed with the business relationship or transaction in question unless the requirements of paragraph (2) and (where appropriate) paragraphs (3) and (4) have been complied with.

(6) In this rule "applicant for business", in relation to a continuing business relationship, means the person who, in relation to the formation of the business relationship, was the applicant for business.

### **9.7 Source of funds**

(1) This rule applies where —

- (a) a licenceholder enters into a new business relationship with a customer,
- (b) in the course of a continuing business relationship between the licenceholder and a customer, any of the events referred to in paragraph 6(2) of the Code occurs, or
- (c) the licenceholder enters into a one-off transaction with or on behalf of a customer.

(2) The licenceholder must take all reasonable steps to establish the source of the customer's funds with which the relationship or transaction is concerned.

### **9.8 Payments to beneficiaries**

A licenceholder must not make a payment of income or capital under a legal arrangement to a beneficiary of the arrangement unless it has —

- (a) identified the beneficiary, and
- (b) verified his identity using relevant information or data obtained from a reliable source.

### **9.9 Enhanced customer due diligence**

(1) Where in accordance with the risk assessment an applicant for business, business relationship or one-off transaction poses a higher risk, the licenceholder must carry out enhanced customer due diligence.

(2) For the purpose of this rule matters which pose a higher risk include but are not restricted to —

- (a) a business relationship or one-off transaction with —
  - (i) a politically exposed person; or
  - (ii) a person or legal arrangement resident or located in a country which the licenceholder has reason to believe does not apply, or

insufficiently applies, the FATF Recommendations in respect of the business or transaction in question;

- (b) a person or legal arrangement which is the subject of a warning issued by the Commission for the purpose of this rule; and
- (c) a company which has shares in bearer form.

(3) In this rule "enhanced customer due diligence" means steps, additional to the measures specified in paragraphs 5 to 8 of the Code, for the purpose of identifying customers and other persons, namely —

- (a) considering whether additional identification data needs to be obtained;
- (b) considering whether additional aspects of the customer's identity need to be verified;
- (c) taking reasonable measures to establish the source of the wealth of the customer and any beneficial owner; and
- (d) considering what ongoing monitoring should be carried on in accordance with rule 9.15.

#### **9.10 Introduced business**

(1) This rule applies where a licenceholder enters into a business relationship with a person ("the customer") who is introduced by a third party ("the introducer").

(2) The written terms of business between the licenceholder and the introducer which are required by sub-paragraph (6) of paragraph 8 of the Code must, in addition to the requirements specified in that sub-paragraph, include that mentioned in paragraph (3).

(3) The requirement referred to in paragraph (2) is that, if the introducer at any time is no longer able to comply with those requirements, whether —

- (i) because of a change in the law applicable to the introducer, or in the terms of business between the introducer and the customer;
- (ii) because the introducer has ceased to do business with the customer, or has ceased trading; or
- (iii) for any other reason;

the introducer must —

- (a) notify the licenceholder that he is no longer able to comply, and
- (b) provide the licenceholder with the records, or copies of the records, which the introducer maintains pursuant to that sub-paragraph.

#### **9.11 Politically exposed persons**

(1) A licenceholder must maintain appropriate procedures and controls for the purpose of determining whether any of the following is a politically exposed person —

- (a) an applicant for business;



- (b) a customer;
  - (c) any natural person having power to direct the activities of a person mentioned in sub-paragraph (a) or (b);
  - (d) the beneficial owner of a person mentioned in sub-paragraph (a) or (b);
  - (e) a known beneficiary of a legal arrangement mentioned in sub-paragraph (a) or (b).
- (2) A licenceholder must maintain appropriate procedures and controls for requiring the approval of its senior management —
- (a) before any business relationship is established with a politically exposed person; or
  - (b) where it is discovered that an existing business relationship is with a politically exposed person, to the continuance of that relationship.

### **9.12 Correspondent banking services**

(1) This rule applies to a business relationship or one-off transaction, as the case may be, which involves correspondent banking services or similar arrangements.

(2) A licenceholder must not enter into or continue a relationship to which this rule applies with a shell bank.

(3) A licenceholder must not enter into or continue a relationship to which this rule applies with a financial institution in a country or territory outside the Island unless it is satisfied that the respondent bank does not permit its accounts to be used by shell banks.

(4) Before entering into a relationship or transaction to which this rule applies, a licenceholder must take the following additional steps —

- (a) obtain sufficient information about the respondent bank to understand fully the nature of its business;
- (b) determine from publicly available information —
  - (i) the reputation of the respondent bank,
  - (ii) the quality of the supervision to which it is subject, and
  - (iii) whether it has been subject to investigation or regulatory action with respect to money laundering or the financing of terrorism;
- (c) assess the procedures and controls maintained by the respondent bank for preventing money laundering or the financing of terrorism, and ascertain that they are adequate and effective;
- (d) ensure that the approval of the licenceholder's senior management is obtained;
- (e) document the respective responsibilities of the licenceholder and the respondent bank with respect to measures to prevent money laundering and the financing of terrorism.

(5) Where a relationship or transaction to which this rule applies involves a payable-through account, a licenceholder must be satisfied that the respondent bank —

- (a) has taken steps complying with the requirements of Recommendation 5 (customer due diligence and record keeping) of the FATF Recommendations with respect to every customer having direct access to the account; and
- (b) will provide the licenceholder on request with relevant evidence of the identity of the customer.

### **9.13 Technological developments**

A licenceholder must maintain appropriate procedures and controls for the purpose of preventing the misuse of technological developments for the purpose of money laundering or the financing of terrorism.

### **9.14 Foreign branches and subsidiaries**

(1) A licenceholder must ensure that any branch or subsidiary in a country or territory outside the Island takes measures consistent with the Code, this Rule Book and guidance issued by the Commission for preventing money laundering and the financing of terrorism, to the extent permitted by the laws and regulations of that country or territory.

(2) Where the minimum measures for preventing money laundering and the financing of terrorism in such a country or territory differ from those required by the law of the Island, the licenceholder must ensure that any branch or subsidiary in that country or territory applies the higher standard, to the extent permitted by the laws and regulations of that country or territory.

(3) The licenceholder must inform the Commission when a branch or subsidiary is unable to take any of the measures referred to in paragraph (1) or (2) because it is prohibited by the laws and regulations of the country or territory concerned.

(4) In this rule "subsidiary", in relation to a licenceholder, means a legal person more than half of whose equity share capital is owned by the licenceholder.

### **9.15 Ongoing monitoring**

(1) A licenceholder must perform ongoing and effective monitoring of any existing business relationship, including —

- (a) review of information held for the purpose of customer due diligence to ensure that it is up to date and appropriate (in particular where the relationship poses a higher risk for the purpose of rule 9.9);
- (b) appropriate scrutiny of transactions and other activities, paying particular attention to transactions which are —
  - (i) complex,
  - (ii) both large and unusual, or
  - (iii) of an unusual pattern of transactions,

and which have no apparent economic or lawful purpose; and

- (c) appropriate scrutiny of transactions to ensure that they are consistent with the licenceholder's knowledge of the customer, its business and risk profile and, where necessary, the source of funds.

(2) The extent and frequency of any monitoring under this rule must be determined —

- (a) on the basis of materiality and risk,
- (b) in accordance with the licenceholder's current risk assessment under rule 9.4, and
- (c) having regard to whether the business relationship poses a higher risk for the purpose of rule 9.9.

(3) Where the licenceholder deals with a customer otherwise than face-to-face, it must, in carrying out any monitoring under this rule, take adequate measures to compensate for any risk arising as a result.

#### **9.16 Retention etc. of records**

- (1) Where a licenceholder takes any steps under this Part for —
  - (a) identifying, or verifying the identity of, or obtaining any information concerning, any person, or
  - (b) ascertaining the source of any funds,

it must retain a record of those steps and copies of any documents produced for that purpose.

(2) The licenceholder must make the record and copies available if required to —

- (a) the licenceholder's money laundering reporting officer,
- (b) any other appropriate staff of the licenceholder;
- (c) any constable, and
- (d) the Commission.

(3) The licenceholder must keep the record and copies for at least 5 years

- (a) in the case of activities relating to a one-off transaction or a series of linked transactions, from the date when the activities were completed;
- (b) in the case of activities under a business relationship —
  - (i) from the date when the relationship was formally ended; or
  - (ii) if the relationship was not formally ended, from the date when all activities relating to the transaction in question were completed.

(4) Without prejudice to paragraph (3), where —

- (a) a report has been made to a constable in pursuance of paragraph 14(2)(f) of the Code, or

- (b) the licenceholder knows or believes that a matter is under investigation,

the licenceholder must retain all relevant records for as long as required by a constable.

Rule 1.2

**Schedule 1.1 — Interpretation**

accommodation address facilities	has the same meaning as in the Order;
accounting records	means the records kept in accordance with rule 2.14 or 2.18;
the Act	means the Financial Services Act 2008;
adjusted capital base (“ACB”)	in relation to a licenceholder, means a measurement of its capital available to cover its risk weighted assets, calculated in accordance with Form SR-2A in Schedule 2.1;
administrator	has the same meaning as in the CIS Act;
advocate	includes a person who is registered under the Legal Practitioners Registration Act 1986;
agent	includes an attorney and a nominee;
annual compliance return	means a return made in accordance with rule 8.28;
annual financial return	means a return made in accordance with rule 2.9;
annual financial statements	has the meaning given by rule 2.8;
annual reporting date	in relation to any person, means the end of that person's financial year;
asset manager	has the same meaning as in the CIS Act;
associated company	means — (a) any company in which the licenceholder holds more than 20% of the equity shares; or (b) a company, other than a subsidiary, over which the licenceholder is able to exercise a significant influence, and in which the licenceholder's interest is either — (i) effectively that of a partner in a joint venture or consortium; or (ii) both long-term and substantial;
attorney	means the donee of a power of attorney acting under that power;
bureau de change	means a licenceholder who carries on activities falling within paragraph (1) of Class 6;
business day	means a day other than — (a) a Saturday or Sunday, or (b) a day which is a bank holiday under the Bank Holidays Act 1989;

business plan	means a statement in writing provided by a licenceholder to the Commission setting out the licenceholder's proposed activities for a future period of not less than 2 years, including a budget for that period;
certificates representing securities	has the same meaning as in the Order;
charge	means a charge referred to in section 79 of the Companies Act 1931 or section 138 of the Companies Act 2006, and includes, in the case of a company incorporated in a country or territory outside the Island, a charge required to be registered under any equivalent provision having effect in that country or territory;
the CIS Act	means the Collective Investment Schemes Act 2008;
client	includes a customer (and vice versa);
client agreement	means an agreement referred to in rule 6.38;
client company (in relation to a corporate service provider)	means a company for which the corporate service provider carries on any regulated activity falling within Class 4;
client money	has the meaning given by rule 3.2;
collateral	means any form of real security;
collective investment scheme	has the same meaning as in the CIS Act;
the Commission	means the Financial Supervision Commission;
company	includes any body corporate, whether constituted under the law of the Island or elsewhere;
contract note	means a note of the essential features of a transaction carried out for a client;
corporate service provider ("CSP")	means a person who carries on regulated activities falling within Class 4;
counterparty	means another party to a transaction to which the licenceholder is a party;
custodian	(a) in relation to regulated activities falling within Class 2, means a person carrying on regulated activities falling within paragraph (5) of that class; (b) in relation to regulated activities falling within Class 3, has the meaning given in section 26 of the CIS Act;
dealing	has the same meaning as in the Order;
debenture warrant	has the same meaning as in the Order;
debentures	has the same meaning as in the Order;
deposit	has the same meaning as in the Order;

deposit taker	means a person carrying on regulated activities falling within Class 1;
deposit taking return	means a return required by rule 2.24 or 2.28;
Depositors Compensation Scheme	means the scheme for the time being having effect under section 25 of the Act;
designated exchange	means an investment exchange (not being a recognised exchange) for the time being notified by the Commission in writing to licenceholders as being a designated exchange;
discretionary management agreement	means a client agreement which includes additional statements required by rule 6.42 (exercise of discretion in management of investments);
discretionary portfolio manager	means a person carrying on regulated activities falling within paragraphs (2), (3), (4), (5) and (6) only of Class 2;
disposal	has the same meaning as in the Order;
electronic money	has the same meaning as in the Order;
enforcer	has the same meaning as in section 1(1)(d) of the Purpose Trusts Act 1996;
equity balance	has the meaning given by rule 3.15(10);
exchange	means — (a) a recognised exchange, (b) a designated exchange, or (c) a recognised clearing house;
exempt exposure	means an exposure referred to in rule 8.38;
exempt scheme	has the same meaning as in the CIS Act;
existing licence	means a licence or authorisation under an enactment repealed by the Act which, by virtue of paragraph 2 of Schedule 8 to the Act, has effect as a licence under the Act;
exposure	means a claim on an individual counterparty or group of closely related counterparties;
express trust	has the same meaning as in the Order
fiduciary	means a licenceholder who carries on activities falling within Class 4 or Class 5;
fiduciary custodian	has the same meaning as in the CIS Act;
financial adviser	means a licenceholder who carries on activities falling within paragraphs (3) and (7) of Class 2;
financial return	means any return, statement or account required to be made, provided or submitted to the Commission by Part 2;
Financial Services Ombudsman Scheme	means Schedule 4 to the Act;
governing body	has the same meaning as in the CIS Act;

government security	has the same meaning as in the Order;
group company	in relation to a licenceholder, means a company which is a member of the same group as the licenceholder;
group of closely related counterparties	means individual counterparties which are related in such a way that the financial soundness of any one of them may affect the financial soundness of the others and as such they constitute a single risk;
illiquid investment	means an investment which, either generally or under certain market conditions, may be difficult or impossible to realise;
instrument	has the same meaning as in the Order;
interim financial return	means a statement prepared in accordance with rule 2.42;
intermediate broker	in relation to a margined transaction, means any person through whom the licenceholder undertakes that transaction;
internal capital adequacy assessment process ("ICAAP")	in relation to a licenceholder, means procedures for assessing the adequacy of its capital and financial resources;
international collective investment scheme	has the meaning given in the section 26 of the CIS Act;
investment	has the same meaning as in the Order;
investment adviser to retirement benefit schemes	means a licenceholder licensed to carry on activities falling within paragraphs (3) and (6) of Class 2;
Isle of Man resident director	in relation to a licenceholder, means a director who is resident in the Island;
Isle of Man resident officer	in relation to a licenceholder, means an individual nominated in accordance with rule 8.21;
items subject to legal privilege	has the meaning given by section 13 of the Police Powers and Procedures Act 1998;
joint enterprise	has the same meaning as in the Order;
large exposure	in relation to a licenceholder, means any exposure which is 10% or more of the licenceholder's large exposures capital base;
large exposures capital base ("LECB")	in relation to a licenceholder, means the adjusted capital base calculated annually on the licenceholder's latest audited financial statements;
large exposures policy statement	means a statement of a bank's policy on treatment of large exposures;
licenceholder	includes the holder of an existing licence;
liquidity	means the risk of non-availability of liquid assets;



management letter	means a letter from a licenceholder's auditor highlighting possible weaknesses in the licenceholder's systems and internal controls, and making recommendations to remedy the weaknesses;
margined transaction	has the meaning given in rule 3.15(10);
minimum net tangible asset requirement	in relation to a licenceholder, means the amount specified in column 6 of Schedule 2.2;
mismatch	in relation to liquidity, means the difference between the cumulative totals of assets and liabilities in specified time-bands, expressed as a percentage of total deposit liabilities;
Net tangible assets	in relation to a licenceholder, means the amount calculated in accordance with Part A of Schedule 2.3;
open-ended investment company	has the same meaning as in the CIS Act;
The Order	means the Regulated Activities Order 2008;
overseas person	has the same meaning as in the Order
participant	in relation to a collective investment scheme, has the same meaning as in the CIS Act;
professional officer	means an individual licensed to carry on activities falling within either or both of - (a) paragraph (6) of Class 4 (acting as officer of company), and (b) paragraph (2) or (5) of Class 5 (acting as trustee or protector).
promoter	has the same meaning as in the CIS Act;
property	has the same meaning as in the Order;
protector	means a person other than a trustee who, as the holder of an office created by or under the terms of an express trust, is authorised or required to participate in the administration of the trust;
quarter	means a period ending on a quarter-end
quarter-end	means 31st March, 30th June, 30th September or 31st December;
recognised clearing house	means a body for the time being declared to be a recognised clearing house by an order of the Financial Services Authority under section 290 of the Financial Services and Markets Act 2000 (an Act of Parliament);
recognised collective investment scheme	has the same meaning as in the CIS Act;

recognised exchange	means a body for the time being declared to be a recognised investment exchange by an order of the Financial Services Authority under section 290 of the Financial Services and Markets Act 2000 (an Act of Parliament);
regulated activity	has the same meaning as in the Order;
regulatory authority	has the same meaning as in the Order;
responsible officers	in relation to a licenceholder, means — (a) in the case of a licenceholder incorporated in the Island, its directors; (b) in any other case, its senior management.
retail investor	in relation to a licenceholder carrying on an activity of Class 2, means a client who is required by rule 6.39 to be treated as a retail investor;
relevant person	in relation to a licenceholder, means any of its officers, employees and tied agents and persons employed by them
risk-asset ratio ("RAR")	means a ratio of adjusted capital base to risk-weighted assets;
risk-weighted assets	means assets weighted by risk (calculated in accordance with the requirements applicable to Form SR-2C referred to in rule 2.24 or 2.28);
scheme	means a collective investment scheme;
securities	has the same meaning as in the Order;
senior management	means, in relation to a licenceholder — (a) its chief executive in the Island, (b) its Isle of Man resident directors; and (c) its Isle of Man resident officers;
set of deposit-taking returns	means a set of returns required by rule 2.24 or 2.28;
share	has the same meaning as in the Order;
share warrant	has the same meaning as in the Order
stockbroker	means a person carrying on regulated activities falling within all of paragraphs (1) to (6) of Class 2;
tied agent	means an agent or intermediary who is permitted by his terms of employment or agency to recommend only products marketed by one or more specified companies;
trust	has the same meaning as in the Order;
trust bank account	has the same meaning as in the Order;
trust corporation	has the meaning given in section 65A(b) of the Trustee Act 1961;
trust money	has the meaning given by rule 3.2;

trust service provider (“TSP”)	means a licenceholder licensed to carry on regulated activities falling within Class 5;
unit trust scheme	has the same meaning as in the CIS Act;
units	in relation to a collective investment scheme, has the same meaning as in the CIS Act;
warrant	has the same meaning as in the Order;
Zone A country	means — (a) a country which is a full member of the Organisation for Economic Co-operation and Development; (b) a country which has concluded special lending arrangements with the International Monetary Fund associated with the Fund's general arrangements to borrow; (c) the Island; (d) the Bailiwick of Jersey; (e) the Bailiwick of Guernsey; (f) Gibraltar; or (g) Bermuda;
Zone B country	means any country which is not a Zone A country.

Rules 2.24 and 2.28

### *Schedule 2.1 — Deposit Taking Returns*

#### **Form SR-1A - Balance Sheet Assets, Liabilities and Off Balance Sheet Items**

All sterling and other currency denominated balances must be reported. All monetary balances must be reported in sterling (including those of currency denominated balances) to the nearest round thousand without decimal points.

##### Balance Sheet Assets

###### Cash

- Notes and coins
- Cash items in the course of collection
- Gold

###### Loans to Banks

- Loans to parent
- Loans to fellow banking subsidiaries
- Loans to other banks - 1 year or less to maturity
- Loans to other banks - greater than 1 year to maturity

###### Marketable Assets

- Zone A Government debt
- Zone A PSE debt
- CDs, CP and FRNs of less than 1 year to maturity, split as:
  - Parent issued
  - Other group bank issued
  - Other banks
  - Other marketable CP
- Other Marketable Bank Debt, split as:
  - Parent issued
  - Other group bank issued
  - Other banks
- Other Marketable Assets, split as:
  - Other marketable debt - group non-banking entities
  - Other marketable debt - corporate
  - Other marketable debt - securitisation exposures - non equity
  - Other marketable debt - sovereign
  - Other marketable PSE debt
  - Marketable bank equity holdings
  - Marketable corporate equity holdings
  - Marketable securitisation exposures - equity tranche holdings

###### Loans and Advances

- Group non-banking entities
- Sovereigns
- PSEs
- Corporate lending
- Retail lending
- Residential mortgages
- Capital connected lending

Investments

- Non marketable Sovereign Debt
- Non marketable PSE Debt
- Non marketable debt - parental
- Non marketable debt - other group bank
- Non marketable debt - other bank issued
- Non marketable debt - group non-banking entities
- Non marketable debt - corporate
- Non marketable securitisation exposures - non capital
- Investments requiring deduction
- Capital investments in subsidiaries and other associated companies
- Capital investments in other banks
- Equity - corporate
- Securitisation exposures - equity tranches

Other Financial

- Items in suspense
- Settlement balances
- Debtors and prepayments
- Operating leases
- All past due assets

Other

- Premises owned and occupied by the licenceholder
- Other land and property owned by the licenceholder
- Plant, equipment, leasehold premises, and motor vehicles
- Intangible assets, including goodwill

Balance Sheet Liabilities

Deposits due to:

- Parent / Holding Company or Group
- Associated Banking Companies
- Fellow Subsidiaries
- Other Deposit Takers . Retail Customers
- Corporate / Trust / Fiduciary
- All Other

CDs and Other Debt

- Certificates of deposit issued
- Promissory notes, bills and other short term paper issued
- Non-capital term debt issued

Creditors, accruals and provisions

- Interest payable
- Creditors and accruals
- Current taxation
- Other taxation
- Settlement balances
- Items in suspense
- Provisions
- Dividends payable
- Other liabilities

Capital (for licenceholders incorporated in the Isle of Man only)

- Tier 1 capital items, before deductions
- Tier 2 capital items, before deductions
- Capital items falling outside of regulatory capital

Capital (for licenceholders which are incorporated outside the Isle of Man only - i.e. branches)

- Retained profits
- General/collective provisions
- Capital issued by the branch
- Capital items - other working capital

#### Off Balance Sheet Items

##### Off balance sheet commitments

- Direct credit substitutes
- Transaction related contingencies
- Trade related contingencies
- Asset sales with recourse
- Forward asset purchases
- Partly paid up shares and securities
- Forward deposits placed
- Note issuance and revolving underwriting facilities
- Other commitments with original maturity of less than 1 year
- Other commitments with original maturity of 1 year and over
- Commitments that are unconditionally cancellable without prior notice

##### OTC contracts

- Interest rate contracts
- Foreign exchange and gold contracts
- Equity contracts
- Other precious metal contracts
- Other commodity contracts

##### Netted exposures

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#### **Form SR-1B - Credit risk**

(does not apply to licenceholders incorporated outside the Isle of Man)

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

The following information must be reported for amounts before and after credit risk mitigation as appropriate.

The licenceholder must report using either the standardised approach or the simplified standardised approach to credit risk (indicating which approach has been used).

##### On balance sheet items

- Claims on Sovereigns, split as:
  - Claims on Isle of Man
  - Claims on other Sovereigns (risk weighted at 0%, 20%, 50%, 100% and 150%)
  - Claims on Multilateral Development Banks and other relevant international organisations

- Claims on Public Sector Entities (PSEs), split as:
  - Claims on Isle of Man PSEs
  - Claims on other PSEs (risk weighted at 0%, 20%, 50%, 100% and 150%)
- Claims on Corporates (risk weighted at 20%, 50%, 100% and 150%)
- Claims on Banks - except guarantees, split as:
  - Maturity more than 3 Months (risk weighted at 20%, 50%, 100% and 150%)
  - Maturity less than 3 Months (risk weighted at 20%, 50%, 100% and 150%)
- Claims on Banks - secured by guarantees from banks, split as:
  - Maturity more than 3 Months (risk weighted at 20%, 50%, 100% and 150%)
  - Maturity less than 3 Months (risk weighted at 20%, 50%, 100% and 150%)
- Securitisations (risk weighted at 20%, 50%, 100% and 350%)
- Cash, split as:
  - Notes and coins
  - Cash items in the course of collection
  - Gold
  - Claims collateralised by Cash deposits
- Retail Exposures, split as:
  - Claims in regulatory retail portfolio
  - Claims falling outside the regulatory retail portfolio
- Residential Mortgages (risk weighted at 35%, 50%, 75% and 100%)
- Past Due Exposures, split as:
  - Secured (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%)
  - Unsecured (risk weighted at 50%, 100% and 150%)
- Capital Deductions, split as:
  - Investments in Subsidiaries
  - Capital connected lending
  - Holdings of Financial Service Business' Capital Instruments
  - Goodwill
  - Securitisations - Equity Tranches
  - Other
- Other Balance Sheet Exposures, split as:
  - Tangible Assets
  - Equity
  - High Risk Assets
  - Other, including Prepayments and Debtors (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%)

#### Off Balance Sheet

- Direct credit substitutes (risk weighted at 0%, 20%, 35%, 50%, 75%, 100%, 150%, other at average weight, or items requiring capital deduction)
- Transaction related contingencies (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Trade-related contingencies (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Asset sales with recourse (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Forward asset purchases (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Partly paid up shares and securities (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Forward deposits placed (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Note issuance and revolving underwriting facilities (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)

- Other commitments with original maturity of less than 1 year (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Other commitments with original maturity of 1 year and over (risk weighted at 0%, 20%, 35%, 50%, 75%, 100% and 150%, or items requiring capital deduction)
- Commitments that are unconditionally cancellable without prior notice

#### Off Balance Sheet - Over the Counter (OTC) Derivatives

The nominal amount underlying the contract and any positive mark to market value of OTC derivative contracts are recorded on a maturity ladder as follows:

- Less than 1 year
- Over 1 year, less than 5 years
- 5 years and over

Returns are required in respect of:

- Interest rate contracts
- Foreign exchange and gold contracts
- Equity contracts
- Other precious metal contracts
- Other commodity contracts
- Netted Exposures (no maturity analysis)

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#### Form SR-1C - Operational risk

(does not apply to licenceholders incorporated outside the Isle of Man)

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

The licenceholder must report using only one of the approaches shown below (indicating which approach has been used).

##### Basic Indicator Approach ("BIA")

- BIA as agreed approach
- Income, split as:
  - Net Interest Income (for last year, 1 year prior and 2 years prior)
  - Net Non-Interest Income (for last year, 1 year prior and 2 years prior)
- BIA Calculation, showing:
  - Average income, where positive
  - Alpha (set at 15%)
- BIA Requirement - Capital Charge and RWA Equivalent

##### Standardised Approach to Operational Risk ("SAO")

- SAO as agreed approach
- Income, split as:
  - Corporate Finance (for last year, 1 year prior and 2 years prior)
  - Trading and sales (for last year, 1 year prior and 2 years prior)
  - Retail banking (for last year, 1 year prior and 2 years prior)
  - Commercial banking (for last year, 1 year prior and 2 years prior)
  - Payment and settlement (for last year, 1 year prior and 2 years prior)
  - Agency services (for last year, 1 year prior and 2 years prior)
  - Asset management (for last year, 1 year prior and 2 years prior)
  - Retail brokerage (for last year, 1 year prior and 2 years prior)
- Capital Charge, split as:
  - Corporate Finance (for last year, 1 year prior and 2 years prior)



- Trading and sales (for last year, 1 year prior and 2 years prior)
- Retail banking (for last year, 1 year prior and 2 years prior)
- Commercial banking (for last year, 1 year prior and 2 years prior)
- Payment and settlement (for last year, 1 year prior and 2 years prior)
- Agency services (for last year, 1 year prior and 2 years prior)
- Asset management (for last year, 1 year prior and 2 years prior)
- Retail brokerage (for last year, 1 year prior and 2 years prior)
- SAO Requirement - Capital Charge and RWA Equivalent

Alternative Standardised Approach ("ASA")

- ASA as agreed approach
- Retail / Commercial Lending - Volume (for last year, 1 year prior and 2 years prior)
- Income, split as:
  - Retail / Commercial Lending (for last year, 1 year prior and 2 years prior)
  - All other income (for last year, 1 year prior and 2 years prior) .
- Capital Charge, split as:
  - Retail / Commercial Lending (for last year, 1 year prior and 2 years prior)
  - All other income (for last year, 1 year prior and 2 years prior)
- ASA Requirement - Capital Charge and RWA Equivalent

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**Form SR-2A - Capital, Current Period's Profit and Loss, Provisions and Non-performing Assets**

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

**Capital**

(does not apply to licenceholders incorporated outside the Isle of Man)

Tier 1 Capital

- Ordinary shares / Common stock
- Perpetual non-cumulative preferred stock
- Reserves - share premium account
- Reserves - disclosed prior year reserves
- Reserves - FX translation differences
- Reserves - Current period's profit verified by external audit
- Current period's losses (if appropriate)
- Minority interests in tier 1 capital

Less deductions:-

- Goodwill and other intangible assets
- Securitisations - gains on sale

Tier 2 Capital

- Fixed asset revaluation reserve
- Reserves / fair value gains of securities not held for trading
- General / collective provisions
- Hybrid debt/equity instruments
- Subordinated term debt
- Minority interests in tier 2 capital

Less deductions:-

- Excess general / collective provisions
- Amortisation on tier 2 subordinated debt

- Excess tier 2 subordinated debt .
- Excess tier 2

Deductions from capital

- Investments in subsidiaries
- Capital connected lending
- Holdings of licenceholder's capital instruments
- Securitisations - equity tranches
- Off balance sheet items of a capital nature
- IRB deductions, including deduction for excess expected losses
- Other

Capital after deductions

- Tier 1 capital
- Deductions pro rata
- Net tier 1 capital
- Tier 2 capital
- Deductions pro rata
- Net tier 2 capital
- Adjusted Capital Base

Current period's profit and loss

The profit and loss account should cover the period from the end of the previous financial year end to the date of the return.

Income

- Banking Income, split as:
  - Interest income
  - Interest expense
  - Profit / loss on foreign exchange dealing and currency positions
  - Profit / loss on investments held for dealing
  - Net income from banking fees, charges and commissions
  - Increase / decrease in book value of investments .
- Non-Banking Income (related to customers / clients), split as:
  - Investment management fees
  - Trust and company administration fees
  - Trustee / Custodian fees
  - Fund management fees
  - Investment dealing profits and commissions
  - Other
- Dividends and Other Income, split as:
  - Dividends / share of profits (or losses) from subsidiaries and associated companies
  - Other income

Expenses

- Operating expenses, split as:
  - Staff costs
  - Occupancy
  - Audit and Legal fees
  - Directors Remuneration
  - Group management / administration charge
  - Other
- Other expenses, split as:

- Interest paid and payable on subordinated debt
- Net charge / credit for specific/individual and general/collective bad debt provisions
- Other expenses

Profit or Loss

- Profit / loss before taxation, extraordinary items and dividends
- Extraordinary items
- Taxation
- Profit after extraordinary items and taxation
- Dividends
- Retained profit

Provisions and non-performing assets

Provisions against bad and doubtful debts

- Gross value of loans against which specific/individual provisions made
- Amounts written off in the period - specific/individual provisions only
- Recoveries of amounts previously written off - specific/individual provisions only

Non-performing assets and loans

- Loans and other assets - 60 days past due date
- Loans and other assets - 90 days past due date

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**Form SR2-B - Large Exposures Reporting**

Exposures to be reported are split between exposures to non-credit institutions and exposures to credit institutions.

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

Exposures to non-credit institutions

- Licenceholders incorporated in the Isle of Man must report all such exposures of 10% or above of their LECB.
- Licenceholders incorporated outside the Isle of Man must report their ten largest such exposures.

For each exposure, or group of closely related exposures, the following information is required:

- The name of the customer / counterparty
- Whether the customer / counterparty is connected to the licenceholder
- The value of the exposure at the reporting date (whether drawn down or otherwise) gross of specific / individual provisions
- Specific / individual bad debt provisions
- Maturity date(s)
- Currency denomination
- Where the exposure is reported on Form SR-1A
- The facility limit
- The maximum exposure in the quarter
- The nature of the security
- The date a large exposure card was submitted to the Commission (does not apply to licenceholders incorporated outside the Isle of Man)

Exposures to credit institutions

- Licenceholders incorporated in the Isle of Man must report all such exposures of 10% or above of their LECB.
- Licenceholders incorporated outside the Isle of Man must report their ten largest such exposures.

For each exposure, or group of closely related exposures, the following information is required:

- The name of the credit institution
- Where the exposure is reported on Form SR-1A
- Maturity date(s)
- The limit (maximum amount that can be put at risk)
- The current amount at risk

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### **Form SR-2C - Risk Asset Ratio and Memorandum Items**

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

#### **Risk Asset Ratio**

(does not apply to licenceholders incorporated outside the Isle of Man)

- Credit risk - Risk Weighted Asset ("RWA") Equivalent, split as appropriate between:
  - Simplified standardised approach ("SSA")
  - Standardised approach ("SAC")
  - Foundation International Ratings Based Approach ("FIRB")
  - Advanced Internal Ratings Based Approach ("AIRB")
- Operational risk - RWA Equivalent, split as appropriate between:
  - Basic Indicator Approach ("BIA")
  - Standardised Approach ("SAO")
  - Alternative Standardised Approach ("ASA")
  - Advanced Modelling Approach ("AMA")
- Market risk - RWA Equivalent - FX and Gold
- Market risk - RWA Equivalent - Commodities
- Settlement risk - RWA Equivalent
- Adjusted Capital Base (total eligible capital)
- Total Risk Weighted Assets (Pillar 1)
- Actual Risk Asset Ratio
- Agreed Minimum Risk Asset Ratio
- Eligible Capital required to support Pillar 1 risks
- Eligible Capital required to support Pillar 2 risks
- Surplus Eligible Capital

#### **Memorandum Items**

- Amounts due to parties connected to the licenceholder, showing where reported under Form SR-1A, the amount drawn and the facility limits, split between:
  - Other group companies - credit institutions
  - Other group companies - others
  - Directors, controllers and their associates
  - Non-group companies, trusts and other bodies with which directors and controllers are associated
- Amounts due from parties connected to the licenceholder, showing where reported under Form SR-1A, the amount drawn and the facility limits, split between:
  - Other group companies - credit institutions
  - Other group companies - others

- Directors, controllers and their associates
  - Non-group companies, trusts and other bodies with which directors and controllers are associated
  - Quoted investments: Market Valuation (split between sterling and other currencies)
  - Unquoted investments: Directors' valuation (split between sterling and other currencies)
  - Encumbered Assets (split between sterling and other currencies)
  - Fiduciary Deposits (split between sterling and other currencies)
  - Number of staff employed - full time versus part time
  - Number of accounts at the reporting date (sterling and other currency denominated)
  - Deposits/loans received from other Isle of Man credit institutions (split between sterling and other currencies)
- 

### **Form SR-3A - Liquidity Risk**

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

The licenceholder must report the following information as at the end of each calendar quarter:-

Assets and liabilities, including off balance sheet items, by maturity date as follows:

- Sight less than 8 days
- 8 days less than 1 month
- 1 month less than 3 months
- 3 months less than 6 months
- 6 months less than 12 months
- 1 year less than 3 years
- 3 years less than 5 years
- Over 5 years

The following information is required in relation to assets and liabilities:

#### Assets

- Deposits with, and CDs issued by, group credit institutions
- Deposits with credit institutions
- Deposits with credit institutions incorporating embedded options (including group)
- CDs, FRNs and bills of exchange purchased
- Bonds and other instruments purchased incorporating embedded options (including group)
- Bonds issued by Zone A governments
- Bonds issued by Zone B governments
- Other investments
- Loans and overdrafts
- Residential mortgages
- All other assets
- Foreign exchange cash inflows
- Undrawn committed standby facilities
- Other known future cash inflows
- Behavioural Adjustments

#### Liabilities

- Demand and notice accounts - Retail
- Demand and notice accounts - Other
- Fixed term deposits - Retail

- Fixed term deposits - Other
- Structured deposits, deposits and deposit bonds issued that incorporate embedded options
- Total capital and reserves
- All other liabilities
- Foreign exchange cash outflows
- Undrawn commitments
- Other known future cash outflows
- Behavioural Adjustments

#### Mismatches

From the assets and liabilities reported, figures for:

- Net adjusted mismatch position
- Cumulative mismatch position
- Cumulative mismatch position as a percentage of total deposit liabilities

Analysis of the ten largest depositors (including credit institutions)

Information is to be reported by:

- Customer / Counterparty name
- Amount
- Maturity Date(s)
- Currency

Analysis of non-credit institution depositors

Information is to be reported on a geographical basis by:

- Isle of Man - individuals
  - Isle of Man - other
  - United Kingdom
  - Republic of Ireland
  - Other EU countries
  - European non EU countries
  - Middle East
  - Far East (including Japan)
  - North America (including Canada) . Other
- 

#### **Form SR-3B - Interest Rate Risk**

(does not apply to licenceholders incorporated outside the Isle of Man)

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

The licenceholder must report the following information as at the end of each calendar quarter, for sterling denominated balances and any other currency that represents in excess of 25% of the licenceholder's deposit liabilities. Other currencies should be calculated individually and aggregated. Currencies that constitute less than 5% of total deposit liabilities may be ignored:-

Assets and liabilities, including off balance sheet items, by maturity date / interest re-determination date as follows:

- Non-interest bearing
- Sight less than 1 month
- 1 month less than 3 months

- 3 months less than 6 months
- 6 months less than 12 months
- 1 year less than 2 years
- 2 years less than 4 years
- 4 years less than 10 years
- Over 10 years

The following information is required in relation to assets and liabilities:

Assets

- Deposits with credit institutions
- Deposits with credit institutions incorporating embedded options (including group)
- CDs, FRNs and bills of exchange purchased
- Bonds and other instruments purchased incorporating embedded options (including group)
- Other investments
- Loans and overdrafts
- Residential mortgages - floating and variable rate
- Residential mortgages - fixed rate
- All other assets
- Forward foreign exchange purchases
- Other interest rate related contracts
- Other off balance sheet assets

Liabilities

- Demand and notice accounts
- Fixed term deposits
- Deposit bonds issued
- Structured deposits, deposits and deposit bonds issued incorporating embedded options
- All other liabilities
- Forward foreign exchange sales
- Other interest rate related contracts
- Other off balance sheet liabilities

Amount at Risk

From the assets and liabilities reported, figures for:

- Net Position
- Weighted Position
- Amount at Risk

Interest Rate Risk - Summary of All Currencies

Carried forward "Amounts at Risk" are required for:

- Sterling currency
  - All specified currencies
  - All other currencies combined
  - Total Amount at Risk
- 

**Form SR-4 - Market Risk (FX and gold, commodities) and Settlement Risk**

(does not apply to licenceholders incorporated outside the Isle of Man)

All monetary balances must be reported in sterling to the nearest round thousand without decimal points.

The licenceholder must report the following information as at the end of each calendar quarter:-

#### FX and Gold

The following information is required in relation to a licenceholder's foreign currency and gold exposure:

- Spot balance sheet assets
- Spot balance sheet liabilities
- Forward gross purchases
- Forward gross sales

Returns are required in respect of:

- Sterling (if the licenceholder's accounting currency is non-sterling)
- US Dollars
- Euro
- Swiss Francs
- Japanese Yen
- Other currencies - long
- Other currencies - short
- Gold

#### Commodities

The following information is required in relation to a licenceholder's commodity positions:

- Gross long position
- Gross short position

Returns are required in respect of:

- Precious metals (excluding gold)
- Base metals
- Energy contracts
- Other contracts

#### Settlement Risk

##### Delivery versus Payment (DvP)

The following information is required in relation to failed DvP transactions across a range of working days after settlement date of 5-15, 16-30, 31-45 and 46 or more:

- Number of trades
- Nominal of trades
- Loss if trade fails

##### Free Delivery

The following information is required in relation to free delivery transactions for 4 days or less since delivery, split between counterparty risk weightings of 0%, 20%, 50%, 100% and 150%:

- Number of trades
- Mark to market receivable

The following information is required in relation to free delivery transactions for over 4 days since delivery:



- Number of trades
- Mark to market receivable

## Rule 2.37

*Schedule 2.2 — Minimum Share Capital Requirement etc.*

Description of activity				Minimum Share Capital Requirement	Minimum Net Tangible Assets Requirement
Class	Paragraph(s)	Description	Qualification or exception		
		<b>Investment business</b>			
2	(3) and (6) only	Investment adviser to retirement benefits schemes		£15,000	£15,000
2	(3) and (7) only	Financial adviser		£10,000	£10,000
2	(2) to (6) only	Discretionary portfolio manager		£25,000	£75,000
2	All	Stockbroker		£25,000	£175,000
2	(2) and (5) only	Custodian		£25,000	£175,000
2	Any (except as specified above)	Other		£25,000	£75,000
		<b>Services to collective investment schemes</b>			
3	(1) or (2) (or both) only	Manager or administrator	except where schemes are exempt schemes or exempt-type schemes (or both)	£25,000	£75,000
3	(3), (4) or (5) only	Trustee, fiduciary custodian or custodian	except where scheme is an authorised scheme or full international scheme	£25,000	£175,000
3	(3) or (4) only	Trustee or fiduciary custodian	where scheme is an authorised scheme or full international scheme	£3.5 million	£3.5 million
3	(6)	Asset manager		£25,000	£75,000
3	(7)	Investment adviser		£25,000	£50,000
3	(8)	Promoter (where regulated promoter is required)		£10,000	£10,000
3	(9)	Provider of management or administration services to another manager or administrator		£25,000	£175,000
3	(10)	Provider of administration services to overseas manager or administrator		£25,000	£50,000

3	(11)	Manager, administrator, trustee, fiduciary custodian or custodian of more than one exempt scheme or an exempt-type scheme		£25,000	£25,000
3	(12)	Provider of administration services to exempt manager etc. of certain schemes		£25,000	£25,000
		<b>Corporate services</b>			
4	Any	Corporate service provider	except where only activities within paragraph (6) (officers) are licensed	£10,000	£10,000
		<b>Trust services</b>			
5	Any	Trust service provider	except where (a) licenceholder is an individual and (b) only activities within paragraphs (1) and (4) (trustee or protector) are licensed	£25,000	£25,000

Rule 2.37

**Schedule 2.3 — Financial Resources Statement**

**Part A - Calculation of Net Tangible Assets**

<b>Net Tangible Assets Calculation</b>	<b>£</b>	<b>£</b>
Capital and Reserves (see Note 1)		<b>X</b>
Less:		
Goodwill and other intangible assets (see Note 2)	X	
Any accumulated losses of subsidiaries or associated companies (see Note 3)	X	
		<b>X</b>
<b>Add:</b>		
Qualifying subordinated loans (see Note 4)		<b>X</b>
<b>NET TANGIBLE ASSETS</b>		<b>X</b>

Note 1	<p>Capital and Reserves. Capital and reserves are to be based on audited balance sheets prepared so as to give a true and fair view in accordance with accounting standards generally accepted in the UK or International Financial Reporting Standards, or other internationally accepted accounting standards.</p> <p>A licenceholder may include freehold and leasehold land and buildings at a valuation taken as its open market value on an existing use basis, if it has been valued by a qualified surveyor or valuer within the preceding 18 months, or in other cases its net book value. The Commission may require evidence of the valuation or request that a valuation be carried out at the licenceholder's expense.</p>
Note 2	<b>Goodwill and other intangible assets. Disallowed.</b>
Note 3	<p><b>Shortfall in attributable net assets of a subsidiary or associated company compared with the book value of the investment in that subsidiary or associated company.</b></p> <p>The shortfall should be calculated as the accumulated losses of the subsidiary or associated company not the net liability figure. Provision should be made for this deficiency or (in the case of an associated company) the portion attributable to the licenceholder as well as deducting the full book value of the investment as a fixed asset investment.</p> <p>Where an adjustment has been made to the book value of an investment in a subsidiary or associated company in calculating the net tangible assets only the adjusted amount should be deducted to avoid double counting, but where there is a deficiency of net tangible assets in a subsidiary or associated companies, this must not be added back.</p>
Note 4	<p>Qualifying subordinated loans. A loan to a licenceholder may be treated as a qualifying subordinated loan for the purposes of this Rule provided that it is in the same form as the model issued by the Commission and it is signed by authorised signatories of all of the parties.</p> <p>A licenceholder must obtain the prior written approval of the Commission before the repayment, prepayment or termination of a subordinated loan.</p>

**Part B - Calculation of Liquid Capital**

<b>Liquid Capital Calculation</b>	<b>£</b>	<b>£</b>
Net Tangible Assets		<b>X</b>
<b>Less:</b>		
Tangible fixed assets	X	
Fixed asset investments	X	
Stock/Inventories (excluding stocks of investments)	X	
Disallowed Debtors Adjustment (see Table I below and Note 5)	X	
Market Value Adjustments (see Table II below and Note 6)	X	
Amounts given as guarantees or charges over assets (see Note 7)	X	
Counterparty Risk Requirement (if applicable : see rule [3.41])	X	
		<b>X</b>
<b>Add:</b>		
Qualifying secured liabilities (see Note 8)	X	
Non refundable deferred income (see Note 9)	X	
		<b>X</b>
<b>Liquid Capital</b>		<b>X</b>

<b>Table I - Disallowed Debtors Adjustment</b>	<b>£</b>	<b>£</b>
Loans owing to licenceholder (including related party and group loans)		X
Total debtors, WIP, accrued income and prepayments		X
		<b>X</b>
<b>Less:</b>		
Debtors or WIP o/s less than 3 months	X	
Prepaid expenses for 3 months or less	X	
Amounts due from related parties that have a fixed repayment term of 3 months or less or arise in the normal course of business and are settled at least every 60 days (unless proven to the FSC that the counterparty has liquid funds that will enable it to repay within 3 months if necessary)	X	
		X
<b>Total disallowed debtors and loans</b>		<b>X</b>

<b>Table II - Market Value Adjustments</b>	<b>Market Value</b>	<b>MV Adj %</b>	<b>Market Value Adj</b>	<b>MV less MV Adj</b>	<b>Book Value</b>	<b>MV &lt; BV</b>
Certificates of Deposit	X	0%	(X)	X	X	(X)
UK Treasury Bills	X	5%	(X)	X	X	(X)
Quoted fixed rate securities	X	10%	(X)	X	X	(X)
Quoted floating rate and index-linked securities	X	15%	(X)	X	X	(X)
Units in CIS authorised or recognised in IOM or UK	X	15%	(X)	X	X	(X)
Designated stocks	X	20%	(X)	X	X	(X)
Inv on recognised exchange not covered above and ICIS units (Not EIFs/PIFs,	X	30%	(X)	X	X	(X)

SFs/QFs, Exempt ICIS)						
Other current asset investments	X	100%	(X)	X	X	(X)
<b>Total market value adjustment</b>						(X)
<b>Settlement adjustments</b>					£	£
Valuation adjustment for creditors outstanding for >30 days after settlement date - Excess of MV over Creditor amount					X	
Valuation adjustment for amount paid in advance where delivery has been outstanding for more than 5 days					X	
<b>Total settlement adjustments</b>						(X)
<b>Total Investment adjustment</b>						(X)

Note 5	<p><b>Disallowed Debtors Adjustment</b> Debtors and Work in Progress are disallowed unless they due and receivable within 3 months and prepayments for 3 months or less. Amounts due from related parties are disallowed unless:</p> <ul style="list-style-type: none"> <li>• they have a fixed repayment term of 3 months or less;</li> <li>• they arise in the normal course of business and are settled every 60 days, or the licenceholder can provide audited financial statements of the related party, made up the same year end as the licenceholder's own financial statements, which demonstrate that the related party has liquid funds that would enable it to repay the loan within 3 months if necessary.</li> </ul>
Note 6	<p><b>Market Value adjustments</b> The percentages in Section 4 shall be applied to calculate the amount by which the market value less the investments adjustment is lower than the book value of current asset investments. This calculation is to be provided to the Commission and any exceptions to the above percentages must be agreed in writing by the Commission.</p> <p><b>Settlement adjustments</b> Unless calculating a CRR requirement (See below), a valuation adjustment must be calculated for the following:</p> <ul style="list-style-type: none"> <li>• Debtors arising from sales of investments outstanding for 30 days or more from contractual settlement date, in which case each debtor shall be included at the lower of its book value and the market value of the underlying investments, but only if the licenceholder retains control of the relevant documents of title.</li> <li>• Creditors arising from purchases of investments outstanding for more than thirty days from contractual settlement date, the extent (if any) to which the market value of the underlying investments exceeds the amount of each creditor.</li> </ul>
Note 7	<p><b>Amounts given as guarantees or charges over assets. Where a licensed entity has obtained approval from the Commission to enter into a guarantee arrangement or give a charge over its assets, the amount of existing loans drawn down over which a guarantee is in force should be deducted from the Liquid Capital.</b></p>
Note 8	<p>Qualifying secured liabilities. A liability secured against freehold or leasehold land and buildings, where the property is the sole security for the liability, may be treated as a qualifying secured liability to the extent of the lower of:</p> <p>A – the total of the secured liability due more than one year after the balance sheet date; or B – 80% of the value of the property on which the liability is secured.</p> <p>For the purposes of the above, the value of the property shall be taken as its open market value on an existing use basis, if it has been valued by a qualified surveyor or valuer within the</p>

	preceding 18 months, or in other cases its net book value. The Commission may require evidence of the valuation or request that a valuation be carried out at the licenceholder's expense.
Note 9	<b>Non refundable deferred income. Where the licenceholder has received income (e.g. in the form of annual fees billed in advance) which is non-refundable under the terms of the contract this amount should be added back.</b>

### Part C - Calculation of Annual Audited Expenditure

Calculation of Annual Audited Expenditure ("AAE") and Expenditure Based Requirement ("EBR") (See Note 10)			
		£	£
Operating expenses (see Note 11)		X	
Interest payable (see Note 12)		X	
Tax expense		X	
Other expenses (see Note 13)		X	
Total Audited Expenditure			X
<b>Audited expenditure</b>			<b>X</b>
Adjustments to Expenditure			
Discretionary bonuses/profit share (see Note 14)		X	
Depreciation / Amortisation		X	
Bad debt expense (see Note 15)		X	
Exceptional costs (see Note 16)		X	
Total Adjustment to Expenditure			X
<b>Annual Audited Expenditure (AAE)</b>			<b>X</b>
<b>Expenditure Based Requirement = AAE x 1/4</b>			<b>X</b>

Note 10	<b>Calculation of Annual Audited Expenditure ("AAE") and Expenditure Based Requirement ("EBR")</b>	<p>Where the relevant audited financial statements are for a period other than a year, the annual audited expenditure shall be calculated on a proportional basis in accordance with the following calculation -</p> <p><math display="block">\frac{\text{(annual audited expenditure)} \times 12}{\text{length of period of financial statements in months}}</math></p> <p>The Commission may require a licenceholder to adjust its relevant annual expenditure where:</p> <ul style="list-style-type: none"> <li>(a) there has been a significant change in the circumstances or activities of the licenceholder; or</li> <li>(b) the licenceholder has a material proportion of its expenditure incurred on its behalf by third parties and such expenditure is not fully recharged to the licenceholder; or</li> <li>(c) it is a licenceholder's first period of account.</li> </ul> <p><b>The Expenditure Based Requirement shall be determined by reference to the Annual Audited Expenditure.</b></p>
Note 11	Operating expenses	Per audited financial statements.
Note 12	Interest payable	'Netting off' is not permitted under any circumstances, for example, interest payable must not be "netted off" against interest receivable. Interest payable must be treated as an expense.

Note 13	Other expenses	As agreed in advance with the Commission.
Note 14	Discretionary bonuses etc	Any form of discretionary (i.e. not contractual) profit related bonus payable to employees, Directors, Partners or Proprietors made can be deducted from operating expenses for the purposes of the expenditure based requirement.
Note 15	Bad debt expense	Where a bad debt provision relates to a debtor that has been disallowed in the calculation of liquid capital, the related expense may be included as an adjustment when arriving at the Annual Audited Expenditure.
Note 16	Exceptional costs	Exceptional items either as defined in UK FRS 3, or IAS 1. Examples given in IAS1 include asset write downs, restructuring costs, profit or loss on disposal of assets, discontinuing operations and reversal of provision. Litigation settlements would not be acceptable as deductions unless the litigation concluded during the relevant financial year and there are no ongoing costs.

### Part D - Calculation of Liquid Capital Requirement

<b>Liquid Capital Requirement</b>			
Expenditure Based Requirement (AAE x ¼) (from Part C)		<b>X</b>	
Excess on PII Insurance (if applicable) (see Note 17)		<b>X</b>	
Other (see Note 18)		<b>X</b>	
<b>Total Liquid Capital Requirement</b>			<b>X</b>

Note 17	Excess on PI insurance x 1	The licenceholder should maintain liquid capital to be able to fund the excess on one potential claim on the PI insurance policy, except where a letter of support is in place from a group company.
Note 18	Other	As determined by the Commission (e.g. a deduction for contingent liabilities if required).



**Part E - Calculation of Financial Resources**

<b>Minimum Share Capital Requirement</b>	
Paid up Share Capital /Share Premium	<b>X</b>
Less Minimum Share Capital/Share Premium Requirement (see Schedule I)	<b>X</b>
<b>Surplus/Deficit</b>	<b>X</b>

<b>Minimum Net Tangible Asset Requirement</b>	
Net Tangible Assets (from Part A)	<b>X</b>
Less Minimum Net Tangible Asset Requirement (see Schedule I)	<b>X</b>
<b>Surplus/Deficit</b>	<b>X</b>

<b>Liquid Capital Requirement</b>	
Liquid Capital (from Part B)	<b>X</b>
Liquid Capital Requirement (from Part D)	<b>X</b>
<b>Excess/Shortfall of Liquid Capital</b>	<b>X/(X)</b>
<b>110% of Total Liquid Capital Requirement</b>	<b>X</b>
<b>Notification Level Reached</b>	<b>Yes/No</b>

Rule 2.44

***Schedule 2.4 — Calculation of Counterparty Risk Requirement***

**Frequency of calculation.**

1. A licenceholder must calculate its counterparty risk requirement ("CRR") at least once each business day; for the purposes of the relevant calculations the licenceholder may use prices of investments and physical commodities as at the close of business on the previous day.

**Negative amounts.**

2. A licenceholder must not include any CRR if it is a negative amount.

**Instruments for which no CRR has been specified.**

3. Where a licenceholder is in doubt as to the classification of an item for the purposes of CRR, it must promptly seek advice from the Commission and until the Commission informs the licenceholder of the correct treatment in the CRR calculation, the licenceholder must add to its CRR the whole of the exposure on the item concerned.

**Provisions.**

4. A licenceholder may reduce the exposure on which its CRR is calculated to the extent that it makes provision for a specific counterparty balance.

**Associated companies and subsidiaries.**

5. For the avoidance of doubt, a licenceholder must calculate a CRR as appropriate on exposures to or from associated companies and subsidiaries.

**Basis of valuation.**

6. For the purposes of valuing instruments and physical commodities at market value in the calculation of CRR, a licenceholder must be consistent in the basis it chooses and may use either mid market value or bid and offer prices (as appropriate).

**Acceptable collateral.**

7. A licenceholder may reduce the exposure to a counterparty on which its CRR is calculated to the extent that it holds acceptable collateral from that counterparty.

**Nil weighted counterparty exposures.**

8. A licenceholder may disregard any counterparty exposure calculated in accordance with paragraphs 2 to 9, if the counterparty is or the contract is guaranteed by or is subject to the full faith and credit of a sovereign government or province or state thereof (or a corporation over 75% owned by such government, province or state), which is a member of the OECD and the government, province, state or corporation has not defaulted, or entered into any rescheduling or similar arrangement, or announced the intention of so doing, in respect of itself or its agency's debt within the last five years.

**Cash against documents transactions**

9. (1) A licenceholder which enters into a transaction on a cash against documents basis must calculate the market risk for transactions still unsettled 16 calendar days after settlement date as set out in (2) below and must then multiply this by the appropriate

percentage set out in Table A below to calculate a CRR for each separate unsettled transaction.

Table A  
Percentage to be applied to the market risk

Calendar days after settlement day	Percentage
0 – 15	Nil
16 – 30	25%
31 – 45	50%
46 – 60	75%
Over 60	100%

- (2) Market risk calculation:
- (a) Where a licenceholder has neither delivered securities nor received payment when purchasing securities for, or selling securities to, a counterparty, the market risk is the excess of the contract value over the market value of the securities.
- (b) Where a licenceholder has neither received securities nor made payment when selling securities for, or purchasing securities from, a counterparty, the market risk is the excess of the market value over the contract value of the securities.

(3) The sum of the amounts calculated in accordance with (1) and (2) above is the licenceholder's total CRR for cash against documents transactions.

**Free deliveries of securities**

10. (1) When a licenceholder makes delivery to a counterparty of securities without receiving payment or pays for securities without receiving the certificates of good title, the licenceholder must calculate the free delivery value for each transaction.

(2) A licenceholder must calculate the free delivery value for each transaction as set out below and multiply this value by the appropriate percentage in Table B below for free deliveries of securities as follows –

- (a) if the licenceholder has delivered securities to a counterparty and has not received payment, the free delivery amount is the full amount due to the licenceholder (i.e. the contract value);
- (b) if the licenceholder has made payment to a counterparty for securities and not received the certificates of good title, the free delivery amount is the market value of the securities.

(3) The sum of the amounts calculated in accordance with (1) and (2) above is the licenceholder's total CRR for free deliveries of securities.

Table B

Percentage to be applied to free deliveries relating to securities

Nature of counterparty to whom free delivery is made		Business days since delivery		
		0- 3	4 - 15	over 15
1	A counterparty to whom securities have been delivered or to whom payment for securities has been made	Nil	100% of contract or market value	100% of contract or market value

2	A regulated financial institution or regulated banking institution to whom securities have been delivered or payment made with the expectation that market practice will result in a settlement day longer than three days from delivery date	15% of contract or market value	100% of contract or market value
2A	A counterparty to whom securities have been delivered which settle through the Crest or to whom payment for such securities has been made.	15% of contract or market value	100% of contract or market value
3	A Manager, underwriter, sub-underwriter or member of a selling syndicate or issuer to whom payment for securities has been made; or a manager of a regulated collective investment scheme to whom units of the scheme have been delivered or payment for units of the scheme has been made.	Nil	100% of contract or market value or, if the issue is a country approved by the Commission, 15% of contract or market value.

**Options purchased for a counterparty**

**11. (1) Single premium options. Where a licenceholder has purchased a single premium option on behalf of a counterparty and the counterparty has not paid the full option premium cost within three business days after trade date, a licenceholder must calculate a CRR as the amount by which the option premium owed to the licenceholder exceeds the market value of the option or acceptable collateral.**

**(2) Traditional options. Where a licenceholder has purchased a traditional option for its own account or a counterparty and paid the option premium, it must calculate a CRR equal to the value of the option premium.**

(3) The sum of the amounts calculated in accordance with (1) and (2) above is the licenceholder's CRR in respect of purchased options.

Rule 6.33

***Schedule 6.1 — Personal account notice***

1. **A licenceholder must ensure that the personal account notice identifies the compliance officer or a specifically designated employee of the licenceholder to be responsible for receiving reports and granting permissions in respect of activities undertaken by its employees in accordance with the personal account notice.**
2. The personal account notice must require that an employee —
  - (a) does not deal for his own account in investments in which the licenceholder carries on investment business to any material extent, or in any related investments, without the permission of the licenceholder (such permission may be general or specific);
  - (b) does not deal in investments for his own account with any of the licenceholder's customers without the prior consent of the licenceholder;
  - (c) reports promptly to the licenceholder in writing any transaction for his own account for which permission is required under (a) above which he enters into otherwise than through the licenceholder unless he has arranged for the licenceholder to receive promptly a copy of the contract or similar note issued in respect of the transaction;
  - (d) does not deal for his own account in an investment in circumstances where he knows or should know that the licenceholder intends to publish a written recommendation, or a piece of research or analysis, in respect of that investment or any related investment which could be reasonably expected to affect the price of that investment;
  - (e) does not deal for his own account at a time or in a manner which he knows or should know is likely to have a direct adverse effect on the particular interests of any customer of the licenceholder; and
  - (f) does not accept any gift or inducement from any person which is likely to conflict with his duties to any customer of the licenceholder.
3. The personal account notice must specify that the references to an employee dealing for his own account include an employee —
  - (a) dealing in his capacity as a personal representative of an estate or as a trustee of a trust, in which estate or under which trust there is a significant interest held by the employee, or any associate of the employee, or any company or partnership controlled by him or by any associate of the employee;
  - (b) otherwise dealing in his capacity as a personal representative or a trustee, unless he is relying entirely on the advice of another person from whom it is appropriate to seek advice in the circumstances; or
  - (c) dealing for the account of another person unless he does so in the course of his employment with the licenceholder.
4. The personal account notice must further state that, if an employee is precluded from entering into a transaction for his own account, he must not (except in the proper course of his employment):—
  - (a) procure any other person to enter into such a transaction; or
  - (b) communicate any information or opinion to any other person if he knows, or has reason to believe, that the person will, as a result, enter into such a transaction, or counsel or procure some other person to do so.

5. Paragraphs 2 and 3 do not apply to —
  - (a) any transaction by an employee for his own account in a packaged product;  
and
  - (b) any discretionary transaction entered into for, and without prior communication with the employee, provided that the discretion is not exercised by the licenceholder.

Rule 6.35

**Schedule 6.2 — Risk disclosure statement**

**Part 1 — Unregulated collective investment schemes**

- I. This notice is provided to you as a retail investor in compliance with the Rule Book issued by the Financial Supervision Commission of the Isle of Man. Retail investors are afforded greater protection under those Rules than those classed as professional investors, and you should ensure that the licenceholder with whom you are dealing tells you what this protection is.
- II. This notice does not disclose all of the risks relating to unregulated collective investment schemes. Nor does it attempt to define all the relevant terms used, and you should ensure that any terms which you do not understand are fully explained to you before completing this risk disclosure statement. You should not deal in unregulated collective investment schemes unless you understand the extent of your exposure to risk. You should also be satisfied that such investments are suitable for you in the light of your circumstances and financial position.
- III. Retail investors, investing in unregulated collective investment schemes should understand the features and risks attendant to investing in an unauthorised and unapproved scheme and should have read and fully understood the offering document, including in particular the information on the risks associated with the fund, before deciding to invest in the fund.
- IV. Retail investors must personally accept all the risks associated with investment in unregulated collective investment schemes, in particular that the investment involves risks that could result in a loss of a significant proportion or the entire sum invested.
- V. Where appropriate, retail investors should take independent advice on the suitability of investment in unregulated collective investment schemes.

[Name of licenceholder]

[on duplicate for signature by client]

I / we have read and understood the risk disclosure statement set out above.

Date \_\_\_\_\_

Signature \_\_\_\_\_

Signature \_\_\_\_\_  
(joint account holders)

[Notes to licenceholders -

- 1) This statement may be incorporated as part of a two-way customer agreement, except that the customer must sign separately that he has read and understood the risk warnings.
- 2) Licenceholders may also include further descriptions of the types of investments covered by this statement, provided such descriptions do not lessen the effect of the risk warnings provided.

## ***Part 2 — Derivatives***

- I. This notice is provided to you as a retail investor in compliance with the Rule Book issued by the Financial Supervision Commission. Retail investors are afforded greater protection under those Rules than those classed as professional investors, and you should ensure that your Licenceholder tells you what this protection is.

This notice does not disclose all of the risks and other significant aspects of derivatives products such as futures, options and contracts for differences. Nor does it attempt to define all the relevant terms used, and you should ensure that any terms which you do not understand are fully explained to you before completing this risk disclosure statement. You should not deal in derivatives unless you understand the nature of any such contracts that you may be entering into or which may be entered into on your behalf, and the extent of your exposure to risk. You should also be satisfied that such contracts are suitable for you in the light of your circumstances and financial position.

- II. Whilst derivatives can in certain circumstances be used for the management of investment risk, some such investments are unsuitable for many investors. Further, strategies intended to reduce risk may be impossible to complete in some market conditions, and so the intended level of protection will not be obtained. You should establish whether this will be a possibility. Your Investment Management Agreement should make it clear whether your Licenceholder may use derivatives on your behalf for speculative purposes, or whether they may only be used to effect an investment strategy of reducing risk.
- III. Certain strategies using a combination of instruments, such as those described as “spreads” or “straddles”, may be as risky as - or more risky than - simple “long” or “short” positions. Investors may not only lose their entire capital, but be liable to pay much more. Different instruments involve different levels of exposure to risk, and in deciding whether to trade such instruments you should be aware of the following points:—

### **Futures**

Transactions in futures involve the obligation to make, or to take, delivery of the underlying asset of the contract at a future date, or in some cases to settle a position with cash. They carry a high degree of risk. The “gearing” or “leverage” often obtainable in futures trading means that a small deposit or down-payment can lead to large losses as well as gains. It also means that a relatively small market movement can lead to a proportionately much larger movement in the value of an investment, and this can work against you as well as for you. Futures transactions carry a contingent liability, and you should be aware of the implications of this, in particular the margining requirements which are set out in paragraph f) below.

### **Options**

There are many different types of options, with different characteristics and subject to different conditions. You should ensure that these characteristics are appropriate to your circumstances; you should also be aware of the relevant expiry dates, after which the rights attached to your options can no longer be exercised.

**Buying options:** Buying options involves less risk than writing options, because you can simply allow your option to lapse if the price of the underlying asset moves against you. The maximum loss is limited to the cost of the option (the “premium”) you have paid, plus any



commission or other transaction charges. However, if you buy a call option on a futures contract, and you later exercise the option, you will acquire the future. This will expose you to the risks described under “Futures” and “Contingent Liability Transactions”.

**Writing Options: If you write an option, the risk involved is considerably greater than that involved in buying options. By writing an option, you accept a legal obligation to purchase or sell the underlying asset if the option is exercised against you, however far the market price has moved away from the exercise price. You may be liable for margin to maintain your position, and a loss may be sustained well in excess of any premium received. If you already own the underlying asset which you have contracted to sell (this is known as dealing in “covered call options”) the risk is reduced. If you do not own the underlying asset (i.e. you are dealing in “uncovered call options”) the risk can be unlimited. Such transactions are not generally suitable for retail investors and so only experienced persons should contemplate writing uncovered options, and then only after securing full details of the applicable conditions and potential risk exposure.**

Traded options are options which are traded on an exchange. There is therefore a market in them and this can be helpful in valuing or liquidating (“closing out”) positions.

Traditional Options: A further type of option known as a “traditional option” is written by certain London Stock Exchange firms under special exchange rules. These may involve greater risk than other options (eg Traded Options above). Two way prices are not usually quoted in them, and there is no exchange market on which to close out an open position or to effect an equal and opposite transaction to reverse an open position. It may be difficult to assess the option’s value, or for the seller of such an option to manage his exposure to risk. Certain options markets operate on a margined basis, under which buyers do not pay the full premium on their option at the time they purchase it. In this situation you may subsequently be called upon to pay margin on the option up to the level of your premium. If you fail to do so as required, your position may be closed or liquidated in the same way as a futures position.

#### Contracts for Differences

Futures and options contracts can also be referred to as “Contracts for Differences”. These can include options and futures on the FTSE100 index or any other index, as well as currency and interest rate swaps. However, unlike other futures and options, these contracts can only be settled in cash. Investing in a contract for differences carries the same risk as investing in a future or an option and you should be aware of these as set out in paragraphs A and B respectively. Transactions in contracts for differences may also have a contingent liability and you should be aware of the implications of this as set out in paragraph F below.

#### Off-exchange Transactions in Derivatives

It may not always be apparent whether or not a particular derivative is effected on or off-exchange. Your Licenceholder must make it clear to you if you are entering into an off-exchange derivative transaction, and may only enter into off-exchange transactions which have a contingent liability (see paragraph (6)) with your express permission.

While some off-exchange markets are highly liquid, transactions in off-exchange or “non-transferable” derivatives may involve greater risk than investing in on-exchange derivatives because there is no exchange market on which to close out an open position. It may not be possible to liquidate an existing position, to assess the value of the position arising from an off-exchange transaction or to assess the exposure to risk. Bid and offer prices need not be quoted, and, even where they are, they will be established by dealers in these instruments and consequently it may be difficult to establish what is a fair price.

## Foreign Markets

Foreign markets will involve different risks from UK markets. In some cases the risks will be greater, and moreover timely and accurate information may be harder to obtain. On request, your Licenceholder must provide an explanation of the relevant risks and protections (if any) which will operate in any relevant foreign markets, including the extent to which he will accept liability for any default of a foreign broker through whom he deals. The potential for profit or loss from transactions on foreign markets or in foreign currency denominated contracts will be affected by fluctuations in exchange rates, which may more than wipe out any profits made through the underlying investment.

## Contingent Liability Transactions

Contingent liability transactions which are “margined” require you to make a series of payments against the purchase price, instead of paying the whole purchase price immediately.

If you trade in futures, contracts for differences or options, you may sustain a total loss of any margin your Licenceholder has deposited on your behalf to establish or maintain a position. If the market moves against you, you may be called upon to pay substantial additional margin at short notice to maintain the position. If you fail to do so within the time required, your position may be liquidated at a loss and you will be liable for any resulting deficit. You should ascertain from your Licenceholder whether he will be liable for any such deficit in the event that he fails to make such payments on your behalf; otherwise, you yourself will be liable.

Even if a transaction is not margined, it may still carry an obligation to make further payments in certain circumstances over and above any amount paid when you entered the contract.

Except in specific circumstances, your Licenceholder may only carry out margined or other contingent liability transactions with or for you if they are traded on or under the rules of a Recognised or Designated Investment Exchange. Contingent liability transactions which are not traded on or under the rules of a Recognised or Designated Investment Exchange may expose you to substantially greater risks.

## Collateral

If you deposit collateral as security, the way in which it will be treated will vary according to the type of transaction involved and where it is traded. There could be significant differences in the treatment of your collateral depending on whether you are trading on a Recognised or Designated Investment Exchange, with the rules of that exchange (and associated clearing house) applying, or traded off-exchange. Deposited collateral may lose its identity as your property once dealings on your behalf are undertaken. Even if your dealings should ultimately prove profitable, you may not get back the same assets that you deposited and you may have to accept payment in cash instead. You should ascertain from your Licenceholder how your collateral will be dealt with.

## Commissions

Before you begin to trade, your Licenceholder should explain to you in writing details of all commissions and other charges for which you will be liable. If any charges are not expressed in money terms (but, for example, as a percentage of the contract value), this should include a clear written explanation, including appropriate examples, to establish what such charges are likely to mean in specific money terms. In the case of futures, when commission is charged as

a percentage, it will normally be as a percentage of the total contract value and not simply as a percentage of your initial payment.

#### Suspensions of Trading

Under certain trading conditions it may be difficult or impossible to liquidate a position. This may occur, for example, at times of rapid price movement if the price rises or falls in one trading session to such an extent that under the rules of the relevant exchange, trading is suspended or restricted. Placing a “stop-loss” order will not necessarily limit your losses to the intended amounts, because market conditions may make it impossible to execute such an order at the stipulated price.

#### Clearing House Protections

On many exchanges, the performance of a transaction by your Licenceholder (or the third party with whom he is dealing on your behalf) is “guaranteed” by the exchange or its clearing house. However, this guarantee is unlikely in most circumstances to cover you, the retail investor, and may not protect you if the Licenceholder or another party defaults on its obligations to you. On request, your Licenceholder must explain any protection provided to you under the clearing agreement applicable to any on-exchange derivatives in which you are dealing. There is no clearing house for traditional options, nor normally for off-exchange instruments which are not traded on or under the rules of a Recognised or Designated Investment Exchange.

#### Insolvency

The Rule Book provides for the segregation of Client Money and Clients Investments from the “own funds” of a Licenceholder acting on behalf of clients. Nonetheless, your Licenceholder’s insolvency or default, or that of any broker involved with your transaction, may lead to positions being liquidated or closed out without your consent. In certain circumstances, you may not get back the actual assets which you lodged as collateral and you may have to accept any available payment in cash (which may not cover the sum in full). On request, your Licenceholder must provide an explanation of the extent to which he will accept liability for any insolvency of, or default by, any brokers involved with your transactions.

[Name of licenceholder]

[on duplicate for signature by client]

I / we have read and understood the risk disclosure statement set out above.

Date \_\_\_\_\_

Signature \_\_\_\_\_

Signature \_\_\_\_\_  
(joint account holders)

[Notes to licenceholders -

- 1) This statement may be incorporated as part of a two-way customer agreement, except that the customer must sign separately that he has read and understood the risk warnings.
- 2) Licenceholders may also include further descriptions of the types of investments covered by this statement, provided such descriptions do not lessen the effect of the risk warnings provided.

- 3) Paragraphs A to G may be deleted, as appropriate, where they relate to business which will not be carried out with or for the investor. Paragraphs 1 to 4 and H to K are mandatory and may not be deleted.]

### ***Part 3 — Warrants***

This notice is provided to you as a retail investor in compliance with the Rule Book issued by the Financial Supervision Commission. Retail investors are afforded greater protection under those Rules than those classed as professional investors, and you should ensure that your Licenceholder tells you what this protection is.

This notice does not disclose all of the risks and other significant aspects of warrants; nor does it attempt to define all the relevant terms used, and you should ensure that any terms which you do not understand are fully explained to you before completing this Risk Disclosure Statement. You should not deal in warrants unless you understand the nature of any transaction that you may enter, or which may be entered into on your behalf, and the extent of your exposure to potential loss.

You should also consider carefully whether warrants are suitable for you in the light of your circumstances and financial position. In deciding whether or not to trade, you should be aware of the following matters : -

#### **Warrants**

A warrant is a right to subscribe for shares, debentures, loan stock or government securities, and is exercisable against the original issuer of the securities. Warrants often involve a high degree of gearing, so that a relatively small movement in the price of the underlying security results in a disproportionately large movement in the price of the warrant. The prices of warrants can therefore be very volatile. You also need to take into account the fact that warrants have expiry dates, after which the rights attached to them can no longer be exercised.

You should not buy warrants unless you are prepared to sustain a total loss of the money you have invested plus any commission or other transaction charges.

Some other instruments are also called warrants, but are actually options; for example, a right to acquire securities which is exercisable against someone other than the original issuer of the securities (often called a “covered warrant”).

#### **Off-exchange Transactions**

Transactions in off-exchange warrants may involve greater risk than those in exchange-traded warrants because there is no exchange market on which to liquidate your position, to assess the value of the warrant or to assess the exposure to risk. Bid and offer prices need not be quoted, and, even where they are, they will be established by dealers in these instruments and consequently it may be difficult to establish what is a fair price.

Your Licenceholder must make it clear to you if you are entering into an off-exchange transaction and advise you of any risks involved.

#### **Foreign Markets**

Foreign markets will involve different risks from UK markets. In some cases the risks will be greater and further, timely and accurate information may be harder to obtain. On request, your Licenceholder must provide an explanation of the relevant risks and protections (if any) which will operate in any relevant foreign markets, including the extent to which he will accept liability for any default of a foreign broker through whom he deals. The potential for

profit or loss from transactions on foreign markets or in foreign currency denominated contracts will be affected by fluctuations in exchange rates, which may more than wipe out any profits made through the underlying investment.

#### Commissions

Before you begin to trade, your Licenceholder should explain to you in writing details of all commissions and other charges for which you will be liable. If any charges are not expressed in money terms (but, for example, as a percentage of the transaction value), this should include a clear written explanation, including appropriate examples, to establish what such charges are likely to mean in specific money terms.

[Name of licenceholder]

[on duplicate for signature by client]

I / we have read and understood the risk disclosure statement set out above.

Date \_\_\_\_\_

Signature \_\_\_\_\_

Signature \_\_\_\_\_  
(joint account holders)

[Notes to licenceholders -

- 1) This notice may be incorporated as part of a two-way customer agreement, except that the customer must sign separately to confirm that he has read and understood the risk warnings.
- 2) Licenceholders may also include further descriptions of the types of investments covered by this statement, provided such descriptions do not lessen the effect of the risk warnings provided.]

Rule 8.28

*Schedule 8.1 — Annual compliance return*

*Part I – To be completed by all licenceholders*

**1. DETAILS OF LICENCEHOLDER**

Name of Licenceholder:	
Due date of return:	
Registered office address:	
Principal business address in the Isle of Man (if different from above):	
Telephone numbers:	
Fax numbers:	
Website:	
E-mail addresses:	

## 2. CONTROLLERS, DIRECTORS AND KEY PERSONS

Please complete the table below with core information about the directors, controllers and key persons of the licenceholder.

For an example of how the completed table might look, see

<http://www.gov.im/lib/docs/fsc//samplettable.pdf>

Name	No of Shares	Date Appointed Director	Date Appointed Secretary	Isle of Man resident officer – “X”	Date Appointed Manager	MLRO – “X”	Deputy MLRO – “X”	Compliance Officer – “X”	For Class 4 and 5 licenceholders only				
									No of Client Company Directorships	No of Client Company Secretaryships	No of Trusteeships	No of Protectors	No of Enforcers

Has the licenceholder carried out anti-money-laundering training for all relevant staff as required by the Criminal Justice (Money Laundering) Code 2007?	
Has the licenceholder carried out other training as required by rule 8.4(5)?	
Please state the number of disciplinary actions taken against staff during the year notifiable under rule 7.10 and confirm that all have been notified to the Commission.	
Total number of staff directly employed by the licenceholder	
Total number of staff not directly employed by the licenceholder but contracted through a service agreement etc	



**3. COMPLIANCE**

Can the licenceholder demonstrate that it carried out regular and adequate monitoring of its arrangements for compliance with the regulatory requirements as specified in rule 8.19?	
Have the responsible officers been made aware of compliance monitoring findings and/or of any issues of a compliance nature on a regular basis?	
Has adequate action been taken to correct any deficiencies found?	

**4. COMPLAINTS**

<b>To be completed by Class 1, 2 and 3 licenceholders only</b> Please state how many complaints have been referred under the Financial Services Ombudsman Scheme during the year.	
<b>To be completed by Class 4 and 5 licenceholders only</b> Please state how many complaints have been recorded in on the complaints register during the year in compliance with rule 8.29.	
Have any material changes to procedures, systems or staff training been identified as a consequence of any complaints and if so have they been implemented? If the answer is yes please give details on a separate sheet.	
Is the licenceholder satisfied that the complaints register is complete and accurate and complies with rule 8.29? If the answer is no please give details on a separate sheet.	

**5. BREACHES AND PRICING ERRORS**

Have breaches during the year been recorded in the breaches register in accordance with rule 8.14(3) ?	
Have details of pricing errors during the year been recorded in the pricing errors register in accordance with rule 8.57(4) ?	
Have any of the breaches or pricing errors been repeated? If the answer is yes please give details on a separate sheet.	
Have any material changes to procedures, systems or staff training been identified as a consequence of any breaches or pricing errors and if so have they been implemented? If the answer is yes please give details on a separate sheet.	

**6. CONFLICTS OF INTEREST**

Have all conflicts of interest been logged during the year in compliance with rule 8.8?	
Is the licenceholder satisfied that any conflicts of interest have been disclosed and handled appropriately?	

**7. BUSINESS RESUMPTION PLAN**

Have the licenceholder's maintain business resumption and contingency arrangements been reviewed during the year and assessed as being appropriate in compliance with rule 8.11?	
Were the business resumption and contingency arrangements tested during the year? If yes, state whether fully or partially tested and the date(s), and whether there were any problems. If there were problems, give details on a separate sheet, including whether they are now resolved.	
Were the business resumption and contingency arrangements activated or partially activated during the year? If yes, give details on a separate sheet, including the circumstances of the implementation, and state whether the arrangements were satisfactory.	

**8. OTHER REGULATORY ACTION**

To the best of its knowledge, has the licenceholder, or its immediate or ultimate parent company (if any), been the subject of any disciplinary action or had its affairs investigated by any other regulatory body as set out in rule 8.17? If yes, give brief details on a separate sheet.	
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**9. LEGAL ACTION**

To the best of its knowledge, has there been any legal action within the limits imposed by rule 7.18 or 7.19 taken against the licenceholder during the year, or is there any pending? If yes, give brief details on a separate sheet.	
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**10. RISK MANAGEMENT**

Has the licenceholder maintained risk management policies in accordance with rule 8.6?	
<b>To be completed by Class 1 Licenceholders incorporated in the Island only</b> Has the licenceholder maintained risk management policies in accordance with rules 8.33, 8.35, 8.39, 8.40 and 8.43?	
<b>To be completed by Class 1 Licenceholders incorporated in the Island only</b> Has the licenceholder maintained its internal capital adequacy assessment process (ICAAP) in accordance with rule 2.23?	
<b>To be completed by Class 1 Licenceholders incorporated outside the Island only</b> Has the licenceholder maintained risk management policies in accordance with rules 8.47, 8.49, 8.50, 8.52 and 8.53?	

**Part 2 – To be completed by licenceholders authorised to conduct regulated activities of Class 2, Class 3, Class 4 or Class 5**

**11. NOMINEE COMPANIES**

List below any companies which are subsidiaries of the licenceholder and which are taking advantage of the nominee company or nominee services exemptions contained in the Financial Services (Exemption) Regulations 2008. (Note: Any change during the year following the date				
<b>Name</b>	<b>Place of Incorporation</b>	<b>Names of Directors</b>	<b>Activity</b>	<b>No. of Appointments (Class 4 and 5 licenceholders only)</b>

**12. CLIENTS' MONEY AND INVESTMENTS**

Has the licenceholder complied with the requirements of Part 3 (client money) of the Rule Book? Please answer yes/no/not applicable. If no, please detail on a separate sheet.	
Has the licenceholder complied with the requirements of Part 4 (clients' investments) of the Rule Book? Please answer yes/no/not applicable. If no, please detail on a separate sheet.	
Has the licenceholder carried out the reconciliations required by rules 3.13, 3.29 and 4.8, as appropriate, and corrected any discrepancies arising within the periods specified in those rules? Please answer yes/no/not applicable. If no, please give brief details on a separate sheet.  Licenceholders which have been granted consent to adopt the rolling stock check method of reconciliation of clients' investments under rule 4.8 should indicate whether the system of internal control has ensured as far as reasonably practicable that an up-to-date record is maintained.	

**13. CLAIMS ON PROFESSIONAL INDEMNITY "(PI)" INSURANCE**

How many matters has the licenceholder referred to its PI insurers during the year?	
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How many claims have been made on the PI Insurance during the year? If claims have been made please provide details (including amounts) on a separate sheet.	
Have any claims been settled by the PI insurers during the year? If yes, please detail on a separate sheet.	
How many claims are outstanding? (please provide details of amounts)	
Have you identified any implications for your internal controls or procedures as a result of any of the claims?	
Have your PI Insurers refused cover in respect of any claims or prospective claims during the year?	

**Part 3 – To be completed by licenceholders authorised to conduct regulated activities of Class 2**

**14. BUSINESS PROFILE**

State the maximum indemnity commission liability of the licenceholder, based on the assumption that all policies sold on an indemnity basis lapsed on the accounting reference date.	
State the average persistency rate (lapsed or cancelled policies) over the period.	

**Part 4 – To be completed by licenceholders authorised to conduct regulated activities of Class 4 or Class 5**

**15. COMPANIES AND TRUSTS**

<b>In relation to Class 4 activities:</b>	
As at the date of this return, state the number of companies etc. in respect of which the licenceholder carries on regulated activities:	
(1) Isle of Man incorporated companies	
(2) overseas companies not registered under Part XI of the Companies Act 1931	
(3) overseas companies registered under Part XI of the Companies Act 1931 (commonly referred to as the “F Register”).	
(4) partnerships	
(5) limited liability companies	

(6) foundations (including Stiftungen, Anstalten and similar entities)	
<b>To be completed by Class 4 Professional Officers<sup>1</sup> only</b>  State the number of companies of which the licenceholder is a director.	
<b>In relation to Class 5 activities:</b>  State the number of trusts in respect of which the licenceholder carries on regulated activities.	
<b>To be completed by Class 5 Professional Officers<sup>2</sup> only</b>  State the number of trusts of which the licenceholder is a trustee, enforcer or protector.	

<b>In relation to Class 5 activities:</b> State the number of, and list below, the companies which are taking advantage of exemption 5.6 (private trust companies) in Schedule 1 to the Financial Services (Exemption) Regulations 2008, which are operated by the licenceholder (the list may be appended if preferred).			
Name	Place of Incorporation	Names of Directors	Number of trusts for which company acts

<b>In relation to Class 5 activities:</b>  List below the companies which have taken advantage of exemption 5.6 (private trust companies) in Schedule 1 to the Financial Services (Exemption) Regulations 2008, but which have ceased to be operated by the licenceholder since the last Annual Compliance Return, stating whether the company has been transferred to another licenceholder for administration or has been dissolved (the list may be appended if preferred).
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<sup>1</sup> ie. licensed to carry on only activities falling within paragraph (6) or (7) of Class 4

<sup>2</sup> ie. licensed to carry on only activities falling within paragraph (1), (2) or (5) of Class 5

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Name	If transferred, name of new licenceholder	If dissolved, tick here

**Part 5 – To be completed by all licenceholders****16. DECLARATION OF COMPLIANCE**

	Yes	No	N/A
<p>1. During the period covered by this return the business of the licenceholder has been conducted in accordance with:-</p> <ul style="list-style-type: none"> <li>✦ the Financial Services Act 2008 (“FSA”);</li> <li>✦ all relevant Parts of the Rule Book issued under the FSA;</li> <li>✦ any licence conditions imposed by the Commission;</li> <li>✦ any directions issued by the Commission;</li> <li>✦ the Collective Investment Schemes Act 2008 (“CISA”); and</li> <li>✦ any orders or regulations made under the CISA</li> </ul>			
<p>2. In so far as the business of the licenceholder has not been conducted in accordance with 1. above, all material breaches of the Rule Book and any breaches of the other items above have been notified to the Commission in writing. If the answer to this question is “no”, details should be attached to this return.</p>			
<p>3. The Commission has been notified in writing of all matters which may influence the continuance of the licence. If the answer to this question is “no”, details should be attached to this return.</p>			
<p>We confirm that the information provided in this return is complete and correct to the best of our knowledge and belief.</p>			
Signed:			
Full Name:			
Isle of Man Director / Isle of Man Resident Officer delete as appropriate			
Date:			
Signed:			
Full Name:			
Isle of Man Director / Isle of Man Resident Officer delete as appropriate			
Date:			
<p><b>Under section 40 of the Financial Services Act 2008 a person commits an offence if he knowingly or recklessly gives any information to the Commission which is false or misleading in a material particular, and is liable:-</b></p> <p>(a) <b>on summary conviction, to a fine not exceeding £5,000 or to a term of custody not exceeding 6 months, or to both;</b></p> <p>(b) <b>on conviction on information, to a fine or to a term of custody not exceeding 2 years, or to both.</b></p>			

**OTHER DOCUMENTATION WHICH FORMS PART OF THIS RETURN**

The following documents must accompany this return, where appropriate:

Structure Chart: A group structure chart showing the name and jurisdiction of all subsidiaries and where the licenceholder appears in the group. A condensed version may be accepted for large groups, subject to the agreement of the Commission.

Management and Staff Structure: A copy of the management and staff structure of the licenceholder in the Isle of Man and of its subsidiaries and, in the case of a licenceholder incorporated in the Isle of Man, any overseas branches. The structure must show “Key Persons” and their responsibilities and the date at which they commenced in the post.

Professional Indemnity Insurance Policy: Details of the most recent Professional Indemnity Insurance policy taken out by the licenceholder in compliance with rule 8.54, if applicable

Where a letter of comfort is in place to support professional indemnity insurance, please submit a copy of the latest audited financial statements of the entity providing the letter.

A signed Declaration of Compliance: The declaration forms part of this return and should be signed by two persons, each of whom must be an Isle of Man director or an Isle of Man resident officer of the licenceholder.

Document Attached



Rule 8.54

**Schedule 8.2 — Professional indemnity insurance**

<b>Class</b>	<b>Paragraph(s)</b>	<b>Description</b>	<b>Minimum cover</b>
		<b>Investment business</b>	
2	(3) and (7) only	Financial adviser	£250,000
2	Any (except as specified above)	Other	£500,000
		<b>Services to collective investment schemes</b>	
3	(8)	Promoter (where regulated promoter is required)	£250,000
3	(11)	Manager, administrator, trustee, fiduciary custodian or custodian of more than one exempt scheme or an exempt-type scheme	£250,000
3	(12)	Provider of administration services to exempt manager etc. of certain schemes	£250,000
3	Any (except as specified above)	Other	£500,000
		<b>Corporate services</b>	
4	Any	Corporate service provider	£250,000
		<b>Trust services</b>	
5	Any	Trust service provider	£500,000

MADE

2008

Chairman

Chief Executive

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#### EXPLANATORY NOTE

(This note is not part of the Rule Book.)

This Rule Book contains detailed rules to be complied with by the holders of licences under the Financial Services Act 2008 in carrying on regulated activities. It replaces the regulatory codes issued under the Acts repealed by that Act.

Part 1 is introductory. Part 2 imposes requirements with respect to financial resources and reporting. Part 3 requires client money and trust money to be kept separate from a licenceholder's money. Part 4 deals with the safeguarding and safekeeping of clients' investments. Part 5 provides for the audit of licenceholders' accounts. Part 6 lays down standards for the conduct of business by licenceholders. Part 7 imposes requirements with regard to their administration, and Part 8 with risk management and internal control. Part 9 contains new requirements to prevent money-laundering and the financing of terrorism, to supplement the Criminal Justice (Money Laundering) Code 2007.

Apart from Part 9, which comes into force on 1st August 2008, the Rule Book applies to new licenceholders as from the issue of their licence, and to existing licenceholders as from 1st January 2009.