

# ATEB consulting Newsletter 18 - October 2003

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## Ladies & Gentlemen

Please find enclosed the latest compliance and industry news.

As usual, site back and enjoy!

Kind Regards

## ATEB Consultants

### Which article applies to me?

Please use the following table to decide which article applies to you, if any:

<b>Investment (IFA)</b>	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Directors/Partners	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Compliance / A&O Function	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Money Laundering Officer			✓	✓										
Advisers & Trainees					✓	✓			✓		✓			✓
T&C Supervisor			✓	✓	✓	✓		✓	✓		✓		✓	✓
Pensions Transfer Specialist					✓			✓						
Back Office		✓												
<b>*Mortgage (inc. IFAs)</b>	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Director/Partner												✓		
Compliance / A&O Function												✓		
Sales Advisor														
T&C Supervisor														
Back Office														
<b>General Insurance</b>	1	2	3	4	5	6	7	8	9	10	11	12	13	14
Director/Partner												✓		
Compliance / A&O Function												✓		
Sales Advisor														
T&C Supervisor														
Back Office														

\*Includes Mortgage arms of IFA and APF firms

## 1. Implementation of the insurance mediation directive (IMD) for long-term insurance business – CP201

Proposals in CP201 affect general and mortgage intermediaries, IFAs, appointed representatives, introducers and authorised professional firms. Key proposals relate to the requirements that before any contract is concluded, all customers must be given:

- Specified information about a firm's status and services; and
- A statement of the customer's 'demands and needs' including, in the case of advised sales, the reasons for any advice given.

**The Insurance Mediation Directive (IMD)** sets minimum standards across the European Union for the sale and administration of both general insurance and life insurance and Member States are required to regulate persons carrying on this business. The standards apply to business done with any "customer" and cover matters such as: fitness and propriety; training and competence; prudential requirements; complaints handling; and **the provision of certain minimum pre-sale information.**

The IMD requires an insurance intermediary to give the following information to all customers (both private and non-private customers) **before any contract is concluded** (and, if necessary, on amendment or renewal of the contract):

1. Its name, address, and how customers can check that it is registered with a "competent authority" (the FSA in the case of the UK);
2. Any holdings it has in the provider firm (the insurer) to which the business is being directed and any holdings that provider has in the intermediary;
3. Whether it advises on or arranges contracts from the whole of the market, a limited number of providers or a single provider; and
4. How to complain to the firm.

### 'Initial Disclosure Document' (IDD)

If the FSA rules are amended as proposed in CP166, both insurers and intermediaries will give private customers an 'Initial Disclosure Document' (IDD) which will include the information required by the IMD. The FSA propose that for non-advised sales with private customers i.e. direct offer and execution only, intermediaries must use the IDD.

The FSA aim to publish final rules in Spring 2004. This will give firms a reasonable period of time to make the necessary changes to their systems and procedures before the rules implementing the IMD come into force on 14 January 2005.

#### **ATEB view:**

The proposals have the following key implications:

- The upshot here is that we are likely to see the end of post sale suitability letters, as advice needs to be confirmed prior to contract conclusion.
- Potentially greater requirements on introducer disclosure.
- Use of the IDD with non-advised sales such as direct offer and execution only.

#### **Action required by you:**

We have tried to keep this article as brief as possible, consequentially there are issues in CP201 which we have not covered, in particular issues where firms are dealing with non private customers. We suggest that if you want further information please go to <http://www.fsa.gov.uk/pubs/cp/201/> ATEB firms will be supported fully throughout the transition and the necessary changes to the compliance procedures manual will be explained as part of our regular monthly visits with you.

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## 2. Complaints Reporting

Don't forget that you need to send your reports (Including nil returns) to FSA by 30th October 2003. See article 1 in September newsletter for guidance and ATEB e-bulletin issued Monday 6th October.

#### **ATEB view:**

If you are late you will attract two things: A financial penalty and some unwanted attention.

#### **Action required by you:**

Ensure that you do not miss the deadline.

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### 3. Money Laundering FSA Training CD ROM – Very Important

Please read in connection with our September Newsletter article 11. The FSA have just issued an ML Training CD ROM to (Ex PIA) IFA firms (Please note that currently this does not include authorised professional firms). The last two lines within the covering memo which accompanies the CD ROM seem to imply that the FSA will come out and visit IFA firms to confirm compliance in this area. **We strongly advise that firms implement the CD ROM with relevant staff, sooner rather than later.** The CD ROM has 6 key areas as follows:

Key Areas on the CD ROM	Quick Synopsis
What is Money laundering?	Covers basic understanding of ML, legal and regulatory requirements.
Assessing the situation	Gives hints on how to spot early signs.
Reporting Your Suspicions	Help with when and how to report
Scenarios	Interactive case studies
Assessment	80% pass mark
Links Resources and FAQ	Key hyperlinks to other useful websites.

As ever, the FSA points out that the CD ROM does not guarantee compliance with anti money laundering training requirements, but in our view it definitely will help. Looking on the positive side, the CD ROM contains a video message from Carole Sergeant (Managing Director of Regulatory Processes & Risk Directorate), so you get to hear things direct from the top and the horses' mouth, so to speak!

#### ATEB view:

ATEB has been predicting themed visits in this area for the last 2 years, if it happens it will be no surprise. **We further believe as an absolute minimum the FSA will expect that all relevant staff will have completed this training material.**

#### Action required by you:

- Ensure that the MLRO deals personally or delegates to a suitable person.
- Select a workstation and load the CD ROM
- MLRO to conduct training first so they are familiar with contents.
- Produce a schedule or timetable with 1½ hour time slots
- Send a memo to all staff asking them to respond to available slots.
- Oversee and ensure that all staff receive training, pass confirmation and certificate.

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### 4. Proposed updates to the ML Sourcebook to take effect on 1st January 2004

The FSA is updating the ML sourcebook in line with new legislation such as Proceeds of Crime Act 2000 and the Money Laundering Regulations 2003 (previously 2001 and 1993). You should also expect a change in the glossary to the definition of what constitutes Money Laundering. There are other proposed rule changes which ATEB will introduce subtly into your working procedures (Part of the Compliance Procedures Manual – 'CPM'). The FSA is currently inviting comments on these proposed changes as part of CP199. Further information is available at: [www.fsa.gov.uk/pubs/cp/cp199](http://www.fsa.gov.uk/pubs/cp/cp199)

#### Objective test of 'reasonable grounds for knowledge or suspicion'

The main area to be reminded of is the greater powers that exist when prosecuting someone for failing to report a suspicion. An objective test of 'reasonable grounds for knowledge or

suspicion' in relation to money laundering offences was introduced in the Proceeds of Crime Act 2002. This has meant that a person working in the regulated sector who failed to report his knowledge or suspicion of handling criminal funds could not simply claim that he neither knew nor suspected any criminal connection. In essence, he would have committed an offence if it could be proved, in court, that a reasonable man, faced with the same facts, would have been suspicious and would have made a report to the appropriate authorities.

**ATEB view:**

We are not lawyers and would therefore not wish to speculate on the intricacies, which exist in the law, but the only likely defense that someone can use today for failing to report is that they **'were not trained properly'**.

**Action required by you:**

The implications here are that it highlights further the need for firm principals and MLROs to have up to date training and assessment documented for all relevant staff. If you don't, then firms could be faced with a double assault from regulatory and legal stances. ***Don't forget that failure to comply with the training requirements in the Money Laundering regulations can result in up to 2 years imprisonment!***

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## 5. Recent FSA Consumer Fact Sheets

The following consumer fact sheets have been published recently:

- FSA Fact sheet - With-profits bonds: this sets out how these products work and what you get for your investment; and
- FSA Fact sheet - Contracting out of the State Second Pension: for those thinking about contracting out.

PDF versions of these publications can be found at:

[www.fsa.gov.uk/pubs/public/w\\_profits\\_bonds.pdf](http://www.fsa.gov.uk/pubs/public/w_profits_bonds.pdf)

[www.fsa.gov.uk/pubs/public/contracting\\_out.pdf](http://www.fsa.gov.uk/pubs/public/contracting_out.pdf)

**ATEB view:**

It's always good to have an idea of what the regulator thinks about a particular area, you never know it might just influence our view!

**Action required by you:**

We suggest that you are aware of the content of these publications.

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## 6. Regulation of long-term care insurance (LTCI) – CP200

CP200 sets out FSA draft policy proposals, rules and guidance for regulating the sale of LTCI 'pure protection' products (The term 'pure protection' includes some term assurance, critical illness, LTCI and income protection; generally these products are currently classed as 'non regulated'). In some areas, the FSA propose new requirements for all LTCI products, including those already subject to regulation.

As you are probably already aware, some LTCI products (i.e. LTCI investment bonds and 'immediate care' annuities) are already defined as 'designated investments' under FSA rules and subject to full conduct of business (COB) regulation as 'packaged products (this includes life policies, pensions, collective investment schemes and investment trust savings schemes) But LTCI 'pure protection' contracts currently fall outside the FSA regulatory remit. Of these pure protection contracts, it is the sale and marketing of the LTCI products that will become subject to full conduct of business regulation for the first time from 31 October 2004.

***LTCI pure protection policies will, therefore be subject to the COB sourcebook for investment business and the proposals in Consultation Paper 200.***

Other pure protection policies (such as some term policies, critical illness and income protection) will be subject to ICOB (Insurance Conduct of Business (ICOB) sourcebook) rules on which the FSA are currently consulting in CP187. FSA aim to make the final rules in April 2004 to give firms a reasonable period before the new requirements come into force on 31 October 2004.

**ATEB view:**

We are not surprised by the proposals as they link in with the FSAs statutory objectives.

**Action required by you:**

If you are involved in this market and are not doing so already we suggest that you treat all LTIC as regulated with immediate effect and stay alert to changes in the lead up to October 2004. Go to <http://www.fsa.gov.uk/pubs/cp/200> for further information.

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## 7. Introduction of the Client Assets Sourcebook (CASS).

Generally, this will only be relevant to General Insurance Brokers and or / IFAs who hold or control client money.

FSA are proposing to introduce another new sourcebook – the Client Assets sourcebook

(CASS). This will bring together in one sourcebook the existing client assets rules from the Conduct of Business sourcebook (COB chapter 9), and the proposed client money rules from the Insurance and Mortgage Conduct of Business sourcebooks (ICOB and MCOB). CASS will stand alongside COB, MCOB and ICOB as a distinct sourcebook within the Business Standards section of the Handbook.

**ATEB view:**

None, for information only

**Action required by you:**

The FSA is currently inviting comments on these proposed changes as part of CP199. Further information is available at: [www.fsa.gov.uk/pubs/cp/cp199](http://www.fsa.gov.uk/pubs/cp/cp199)

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## 8. Change to the "pension transfer" definition

FSA proposes to bring this change into force with **effect from 1 January 2004.**

The FSA proposes to change the "pension transfer" definition as currently defined in the *Glossary*. They now accept the current definition does not specify that transfers to pension buy-out contracts are included. This was contrary to their policy intention. Here is an advance copy of the amended definition:

*Pension transfer a transaction resulting from a decision made, with or without advice from a firm, by a customer who is an individual, to transfer deferred benefits from:*

*(a) an occupational pension scheme; or*

*(b) an individual pension contract providing fixed or guaranteed benefits that replaced similar benefits under a defined benefits pension scheme; or*

*(c) (in COB 6.7 (Cancellation and withdrawal)) a stakeholder pension scheme or a personal pension scheme)*

***to a stakeholder pension scheme or to a personal pension scheme (including a self-invested personal pension scheme), or to any deferred annuity policy (including a pension buy-out contract) for a customer who is an individual where the eventual benefits depend in whole or in part on investment performance in the period up to the intended retirement date.***

**ATEB view:**

Most firms undertaking pension transfer business will in fact have interpreted the old definition as including pension buy-out contracts (and will therefore have applied the same detailed transfer value analysis requirements and checking procedures to these contracts). IFAs can ignore Definition (C) as it applies generally to Product Providers and Fund Managers.

**Action required by you:**

Firms must always ensure that all pension buy-out contracts are included in firms' quarterly and half yearly returns (COB 5.3.26R). ATEB will update the CPM section 21 automatically as part of our regular visit.

## 9. New rules for investment companies

FSA has recently finalised new rules for investment companies, including Split Capital Investment Trusts, which will **increase the information and protection available to investors in such companies**. The changes will ensure clearer warnings for investors about the nature of these products and associated key risks and will also place limits on the investment practices that accelerated the collapse of some splits. The key safeguards being introduced into the Listing Rules are:

- Limit on cross-holdings
- Risk factors in all listing documents
- Increased portfolio disclosure in other listed investment companies
- New Conduct of Business risk warnings
- Increased board independence
- Changes to investment policy requiring prior shareholder approval
- Extending the Listing Rules' Model Code for Directors Dealings

### ATEB view:

None, for information only

### Action required by you:

None for information only. The Feedback Statement can be found at [www.fsa.gov.uk/pubs/policy/ps164](http://www.fsa.gov.uk/pubs/policy/ps164)

## 10. Anyone considering a change of legal status?

From	To	New Part IV required? (FSA Authorisation)
Sole Trader	<ul style="list-style-type: none"><li>• Partnership</li><li>• Limited Liability Partnership</li><li>• Limited Company</li></ul>	<b>Yes</b>
Partnership	<ul style="list-style-type: none"><li>• Limited Liability Partnership</li><li>• Limited Company</li></ul>	<b>Yes</b>

Anyone who has had the pleasure of going through a new FSA Part IV application will know that it involves a great deal of work and cost (Base application is over 400 pages). Just to start with, the FSA charge £2000 with every completed application. Before this you need to decide how much time it will take to compile the application and whether it may be more cost effective to outsource this to someone like ATEB.

We are aware of a sole trader who has recently considered changing to a partnership. The change involved 100% retained equity control with the current sole trader and the addition of a couple of salaried partners. **The interesting point is that there is nothing in the FSA Handbook that gives guidance on this specific situation.**

ATEB were aware that changing from a sole trader to a partnership is a significant change of legal entity and the Financial Services and Markets Act requires the completion of a new application for FSA authorisation. This is fortunate from the point it has prevented the firm from trading without the correct authorisation, but it has created a bitter taste over the costs of reauthorisation.

### ATEB view:

We think this is terribly unfair and it hits firms in the pocket forcing them through a massively bureaucratic process for what are non-practical 'legal reasons'. However, we accept that for firms looking to change legal status the costs of reauthorisation will not simply go away.

### Action required by you:

ATEB have completed and submitted many Part IV applications, if you need help and

guidance you are more than welcome to ask. Don't forget, however, that failure to cancel your current permission once your new firm is authorised could result in two annual invoices being issued!

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## 11. Compliance Consultants Communication Strategy Conference

On the 9th October, Steve and Huw attended the FSA's first conference designed specifically for compliance consultants. We were addressed by, among others, David Kenmir and Lesley Titcomb, Director and Head of Department respectively of the Investment Firms Division.

It was an interesting day and while there wasn't anything of great surprise, you'll be pleased to hear that what ATEB is advocating for its clients, is most definitely in line with FSA thinking. For example, our stance and viewpoint on Suitability Letters/Reports is virtually exactly the same as that of the FSA's. Many issues were raised, however, and we will be coming back over the coming months to address these issues in more detail. For now and to give you a taster (excited?) here is a snapshot of issues raised and comments made by the FSA speakers.

Click on: [Compliance Conference Key Issues](#)

### ATEB view:

None, for information only

### Action required by you:

None, for information only

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## 12. Fees for mortgage firms and insurance intermediaries - PS180

**This Policy Statement (PS) sets out the application fees that mortgage firms and insurance intermediaries will need to pay. Here are a few bullets:**

- Firms who apply early and/or electronically will receive a discount on their fees.
- Many smaller firms will pay less than the fees originally proposed in CP180 because FSA have introduced additional fee bands, as a result of feedback during consultation. The first year's **periodic (annual authorisation) fees** are not fixed yet and will be subject to consultation at a later date.
- FSA currently expects the minimum periodic fee for each of the A.18 and A.19 fee-blocks for a full year to be about £750. The minimum periodic fee will apply up to a certain level of income, which will be much less than the level of the lowest application fee band (£1 million).
- If a firm's application causes it to fall into more than one fee-block (e.g. A.2 and A.18), only one fee - the highest applicable - is payable.
- Variation of permission (firms already authorised) fees will be 50% of the applicable standard application fee amount. ***The FSA hope to inform currently authorised firms of the variation process in November this year.***

### ATEB view:

None, for information only

### Action required by you:

Firms not currently authorised by the FSA will be able to **register to receive an application pack from early November** this year, and the FSA will accept applications from firms to carry out the newly regulated activities from mid-January 2004. To qualify for the early application discount, the FSA must receive applications from firms doing:

1. Mortgage lending and administration or advising and arranging on mortgages by **31 March 2004**.
2. General insurance intermediaries, the early application deadline is **31 May 2004**.
3. Firms applying to be authorised for advising and arranging on both mortgages and general insurance, the FSA must have received the firm's application **by 31 March 2004** for it to get the early discount.

Further information is available at: <http://www.fsa.gov.uk/pubs/policy/ps180/>

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## 13. Lloyds TSB fined – What can we learn?

The Financial Services Authority (FSA) recently fined Lloyds TSB Bank plc (LTSB) £1.9 million for a number of unsuitable sales of a high-income equity-linked bond through the LTSB branch network. LTSB will pay compensation of approximately £98 million in respect of 22,500 sales.

#### ATEB view:

We feel there are two key issues here

- When dealing with any product, particularly medium to high risk, IFAs must first document through a rigorous process that the **product fits in with the clients risk profile**. This means, for example, that if the client has a relatively secure portfolio of investments and has no prior experience of this type of product, then arguably this may be the wrong product. Some of you reading this article may disagree with this, but, whatever your stance, clear documentation and justification is crucial.
- The second point is that once you have decided that the product is suitable for the client you need to ensure that **the client understands the risks**. Firms should consider how they could explain and document the risks without putting the client off. Bearing in mind no client will ever invest money knowing that they are likely to lose out.

#### Action required by you:

Only by following these points very carefully will firms avoid the problems that are now faced by LTSB. As we have said on so many occasions, getting points 1 and 2 right depends on the firm's systems and controls, in particular:

- Detailed fact find which focuses on specific and personalised risk
- Suitability letter, which contains a personalised explanation.
- Consistent training across all advisers and relevant staff.
- Supervisors and Principals checking that the above are actioned.

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## 14. Supervisor Skills Workshop

**Reminder:** If you employ investment advisers (anyone giving advice on insurance company products to members of the public) then you must have an allocated firm supervisor (or supervisors). For fuller information on whether supervisor training applies to you please refer to ATEB practice bulletin 15 on supervision and our February newsletter article 6. ***The need to have supervisor training is a relevant and up to date issue having been remarked upon during a recent FSA visit and the FSA compliance conference see article 11.***

#### Overview:

##### Day 1- overview (9.30am until 4.30 pm)

- Setting field sales process standards
- Consistent and accurate assessment skills
- Using an objective observation aid
- T&C Knowledge

##### Day 2 - overview (9.30am until 4.30 pm)

- Theory of coaching and training
- SMARTA development plans
- Giving consistent feedback
- Structuring one to ones
- Monitoring performance and training needs analysis

#### Who should attend?

- Qualified supervisors wishing to top up existing supervisor knowledge
- Newly appointed supervisors
- Supervisors who had previously been classified as 'self supervising' (under PIA)

#### Do I need to attend both days?

- You may wish to attend only a single day at present; there will be other days later in the year.

#### Course details:

**Dates:** Day 1 – **Wednesday 19th November** and Day 2 – **Thursday 20th November**

**Location:** Newcastle Upon Tyne

**Cost:** £150 plus vat per day per person

**ATEB view:**

Where relevant and suitable training has not been undertaken within firms, it will result in a serious breach of the regulations and the consequences may be significant. It is more than possible that the FSA will suspend the firm from trading until this requirement is met. Although we often quote the regulatory requirements, let's not forget that quality supervisor training will almost certainly have a positive impact on your business.

**Action required by you:**

Please let us know if you would be interested in attending by email or telephone or by completing the online booking form: <http://www.atebconsulting.co.uk/bookings/November-03.htm>

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**Important Note:**

*The ATEB Newsletter is intended to provide general guidance on areas of compliance and T&C; however it is not a replacement for the main Rules and Guidance contained within the FSA Handbook.*

*We welcome all feedback. If you have any feedback or questions relating to any articles then please direct them to your local ATEB consultant or the newsletter editor Steve Bailey email [steve@atebconsulting.co.uk](mailto:steve@atebconsulting.co.uk)*

*Unless you have consulted specifically (as part of a regular visit) with ATEB on a particular issue then ATEB Consulting accept no liability for any actions taken based on the information contained solely within the newsletter.*

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