

# ATEB consulting Newsletter 24 - April 2004

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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
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
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
Director/Partner		✓	✓	✓		✓				✓	✓	✓
Compliance / A&O Function		✓	✓	✓		✓	✓					✓
Sales Advisor												
T&C Supervisor												
Back Office												

\*Includes Mortgage arms of IFA and APF firms

## 1. Complaints Final Reminder - Deadline 30th April 2004

**Next Complaints Reporting Period:**

**ATEB view:**

None, for information only

**Action required by you:**

Make return within the deadline: For further information click on:  
[www.fsa.gov.uk/complaints\\_reporting/](http://www.fsa.gov.uk/complaints_reporting/)

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**2. Mortgage and General Insurance key deadlines for authorisation**

	<b>Mortgages</b>	<b>Mortgage &amp; General (Includes Variation of permission)</b>	<b>General Only</b>
<b>First deadline</b>			
<b>31 March 2004</b>	Apply by the 31 March 2004 to qualify for an early application fee discount	Apply by the 31 March 2004 to qualify for an early application fee discount	
<b>Second deadline</b>			
<b>30 April 2004</b>	This is the deadline for submitting applications if you want to be certain that the FSA will process it for 31 October 2004 start date*	This is the deadline for submitting applications if you want to be certain that the FSA will process it for 31 October 2004 start date*	
<b>First deadline</b>			
<b>31 May 2004</b>			Apply by the 31 May 2004 to qualify for an early application fee discount
<b>Second deadline</b>			
<b>13 July 2004</b>			This is the deadline for submitting applications if you want to be certain that the FSA will process it for 14 January 2005 start date*

\* Under the Financial Services and Markets Act 2000 the FSA has six months from the date the application is received to make a decision on a complete application (where no information is missing) and 12 months to decide on an incomplete application (where information is missing).

**ATEB view:**

Don't miss the deadlines

**Action required by you:**

Don't miss the deadlines!

### 3. Periodic (Authorisation) Fees Consultation

In the second quarter of this year the FSA will consult on, and set, fee rates for the newly regulated activities of mortgage business and general insurance broking, which will apply from the dates the FSA begin regulating these activities until 31 March 2005. There will be another consultation in January next year which will issue proposals for 2005/06 fees. The FSA will not invoice firms for fees until mid-2005. This will include both the 'stub' period (up to 31st March 2005) and full financial year (April 2005 to March 2006).

**ATEB view:**

None, for information only

**Action required by you:**

None, for information only

### 4. Supervision of 'Sole advising Firm Principals' assessed as competent

New proposals issued in April 2004 come into effect on 1st May 2004 and impact on certain IFAs and mortgage advisers (wef October 2004) who are subject to the T&C rules and guidance.

Currently, for IFA Firms where there is more than one proprietor or principal, the T&C rules require them to apply supervision requirements to one another. When the firm is a sole trader, or there is only one practitioner, director or partner engaged in the activity, the FSA now accept that, practically, it is difficult for that person to be 'supervised'.

Therefore, to provide clear guidance for firms and employees in this position the FSA have updated their T&C Sourcebook: The new guidance is shown in bold.

Quote: TC 2.7.4 G

Appropriate supervision will vary according to the competence of the employee and is likely to be less intense once competence has been attained. ***If the employee is, for example, a sole trader, or the only director or partner engaging in the activity, the firm should make whatever arrangements are appropriate in the circumstances, bearing in mind that it can become difficult to be objective about one's own performance.***

This guidance indicates that an employee, who is engaging in an activity with or for a private customer, may supervise himself if he is a sole trader or is the only director or partner of a firm who carries out an activity with or for private customers.

**ATEB view:**

Firms need to give some consideration as to what the FSA means by the term 'appropriate arrangements'. We presume they mean using external consultants / auditors.

**Action required by you:**

None, for information only

### 5. Fee Tariffs

So that the FSA treat all advisory firms consistently, they are aiming to apply a tariff base of **income** to certain fee-blocks. Currently for advisory firms this is calculated on the number of approved persons dealing with private customers. The FSA are looking to change the tariff base in the A.12 (Advisory arrangers, dealers, or brokers (holding or controlling client money or assets, or both)) and A.13 (Advisory arrangers, dealers, or brokers (not holding or controlling client money or assets, or both)) fee-blocks in particular.

The fee tariff issue has become of greater significance given that the FSA will charge mortgage and general insurance intermediaries periodic fees based on the **income** they receive from their mediation activity.

**ATEB view:**

This is likely to result in some firms paying more and other paying less than currently.

**Action required by you:**

None, for information only

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## 6. FOS and FSCS funding – CP04/4

The FSA has published proposals in CP04/4 [www.fsa.gov.uk/pubs/cp04\\_04](http://www.fsa.gov.uk/pubs/cp04_04) for the future funding of the Financial Ombudsman Service (FOS) and the Financial Services Compensation Scheme (FSCS) for mortgage firms and general insurance intermediaries.

### Proposals for Funding Arrangements for FOS

1. The FOS's costs are funded by a combination of a **general levy** on all firms and a **case fee** charged on individual firm complaints handled by the FOS. The case fee covers the costs of processing complaints whilst the remaining operating costs are met through the general levy.
2. Two new industry funding blocks will be created: one for mortgage broking and one for general insurance broking. In line with the existing FSA fees regime, firms must pay the general levy in each funding block to which they belong. Each funding block has a tariff base which is the measure used to calculate a firm's share of the general levy. For mortgage firms and general insurance intermediaries, the tariff base will be the same 'annual income' measure that will be used for FSA fees.
4. For the financial year 2004/2005, the FOS will not be charging a general levy for mortgage firms and general insurance intermediaries. Firms will, however, pay a special case fee of £550 per case. **The first two cases will not be subject to a fee.**
5. The FSA will consult on the FOS general levy for the financial year 2005/06, as part of its annual fees consultation at the end of this year. This will cover the tariff rates for the new industry blocks and also their minimum levy amounts.

### Proposals for Funding Arrangements for FSCS

**6. It is proposed that there will be two separate sub-schemes, with one for mortgage arranging and advice and the other for general insurance brokers. Firms will have to contribute to each sub-scheme, as appropriate, through the contribution group for that scheme.**

7. The FSCS makes two types of levy on participant firms - one for **management expenses** and one for **compensation costs**. The management expenses levy covers operating costs and has two components - base operating costs and the specific costs of processing claims. Where a contribution group has no claims against it, firms in that group will not be levied for specific costs - they will only be levied for base costs.
8. When firms go into default the FSCS raises a compensation levy. This is done on a 'pay as you go' basis. Each contribution group has a tariff base which is used to calculate each firm's share of the compensation levy.
9. For mortgage firms and general insurance intermediaries, the tariff base will be the same annual income measure that will be used for FSA fees.
10. The management expenses levy will not be collected until the 2005/06 financial year. Invoices for 2005/06 will cover that year and the 'stub' period (of regulation to 31 March 2005). The FSA will consult on the management expenses levy limit - the maximum the FSCS can raise in total from the industry - at the end of this year in its annual consultation on fees.

**ATEB view:**

None, for information only

**Action required by you:**

None, for information only

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## 7. Mortgage Exams and Grand fathering (Policy Statement (04/10))

Very soon, the FSA will no longer prescribe (Specifications currently within the T&C

Sourcebook) what exams an individual will have to take. Amongst other things, Policy Statement (04/10) clarifies the move to 'appropriate exams'.

For mortgage advisers new to the industry from 1st November 2004, it will be broadly up to employers to decide what is right for their employees. A list of 'appropriate exams' will be accessible electronically from the \* FSSC's website and will be available to all, free of charge. Draft syllabi have been passed to the FSSC who will take on responsibility for securing the appropriate examinations as part of the ongoing examination review. The work of the FSSC will focus on those who will be new to the role of mortgage adviser.

#### ***Employees not assessed as competent prior to 31st October 2004***

**(Policy Statement (04/10) also confirmed that a firm must ensure that individuals pass the relevant appropriate examinations within the time limits imposed by its previous regulator (i.e. MCCB). Here is an extract from the MCCB rules.**

Extract from MCCB rules 3.8

A Trainee Adviser will have **two years** from the date on which he is first entered on any registered firm's list of Trainee Advisers in which to complete his training and professional qualifications.

For the purposes of calculating the period of two years a registered firm must:

(1) Aggregate periods of time spent by the Trainee Adviser with different registered firms as a Trainee Adviser;

Note: A registered firm must ensure that an individual who does not pass the professional qualifications within the specified time **ceases all activity associated with the provision of mortgage advice** (under section 3.1(a) of the Mortgage Code) and does not resume such activity without first passing the professional qualifications.

#### ***New Employees from 31st October 2004***

Following the introduction of mortgage regulation on 31 October 2004, an employee training to advise on standard mortgages (other than business lending) will have two years from the start of the activity to complete the appropriate exam.

#### ***Employees assessed as competent prior to 31st October 2004***

Employees who have already been assessed as competent by a firm in line with the rules of the Mortgage Code Compliance Board will be 'grandfathered' for the purposes of Training and Competence.

##### **ATEB view:**

Little change in that the same exams are likely to be available in the short term as appropriate i.e. CeMap and MAQ, FPC

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

Employers should make every effort to ensure that the majority of their staff are fully qualified as soon as possible. This will not only improve the standards within the firm, but also prevent a 'pressure' situation where individuals are left without the ability to advise. Perfect timing to plug ATEB CeMap training which we will be advertising shortly.

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## **8. Pensions - switching into income drawdown**

In a recent speech John Tiner, FSA Chief Executive, said:

***"We are alive to the fact that the associated proposal to raise from 50 to 55 the earliest age at which pension benefits can be drawn might lead advisers to encourage pension scheme members of a certain age to bring forward their retirement, possibly to their disadvantage".***

He also said:

***"And some people may be persuaded to take action to avoid tax penalties on surplus pension funds in excess of any lifetime limit. For example, people may be tempted to retire prematurely, perhaps switching into income drawdown contracts immediately***

**before the proposed tax rules take effect. Firms will need to be sure that their advice in this area is of a high standard”.**

He also made reference to "unlocking pensions", the dangers and the poor advice given. Sadly, those who need to do this in order to release cash are probably already in financial difficulty. So, such action, bringing a smaller pension to last over a longer time, will probably bring greater problems in due course.

**ATEB view:**

Clearly, this is a warning to us to be careful what we advise and ensure that our client files contain sufficient detail and more!

Suitability Letters and Reports should be specific and detailed (Remember **a repeat** of what is in the technical detail and Key features documents is not important. What is important is **explaining 'why'** and not 'what' you have recommended. We will always leave ourselves open if we do not cover the downsides clearly.

**Action required by you:**

Make use of the ATEB checklists including the detailed income draw down checklist together with other systems and controls and ensure all advisers follow the same detailed process, don't leave anything to chance or you may end up paying for it later.

The FSA has issued a leaflet: "Unlocking your pensions making sure that you understand the risks" [http://www.fsa.gov.uk/pubs/public/unlock\\_pension.pdf](http://www.fsa.gov.uk/pubs/public/unlock_pension.pdf)

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## **9. Requirement to know your customer, restricted advice & focused advice.**

We had a query on this subject so we felt it was worth letting others know the outcome.

Consider the following two rules in the Conduct of Business Sourcebook (COB).

COB 5.2.5 R Before a firm gives a personal recommendation concerning a designated investment to a private customer, or acts as an investment manager for a private customer, it must take reasonable steps to ensure that it is in possession of sufficient personal and financial information about that customer relevant to the services that the firm has agreed to provide.

COB 5.2.7 G If a private customer declines to provide relevant personal and financial information, a firm should not proceed to provide the services described in COB 5.2.5 R without promptly advising that customer that the lack of such information may affect adversely the quality of the services, which it can provide. The firm should consider sending written confirmation of that advice.

The upshot here is that where your client declines to provide full information it is your responsibility to explain to the client in, for example, your suitability letter that any advice will be **restricted** by this fact.

There is no FSA rule requiring advisers to give "all-encompassing" advice across the whole range of financial needs, you may wish to conduct **focused** advice (for example involving a group stakeholder plan). It is important that clients should be made aware, both verbally and in writing, of the limits to your advice being given and that needs which may be of a higher priority are not being addressed.

Note: The term 'restricted' and 'focused' are terms which ATEB use to describe situations. These terms (and any equivalent terms) are not defined in the FSA Glossary.

**ATEB view:**

If you do not confirm this to the client then we believe you are potentially placing the firm at a disadvantage.

**Action required by you:**

Ensure that you have the right 'Systems and Controls' (checklists, fact find & letter templates) in place.

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## **10. Client Trust Accounts**

This article applies to General Insurance Brokers.

Many general insurance brokers currently run their client account and firm account combined. To date, that has seemed a sensible method under which to operate. Firms have generally allowed surpluses to build up so that in the event of any problem such as insolvency of the client or late premiums, then a reserve is at hand. The new FSA rules, as outlined in CASS, will mean many General Insurance Brokers having to change the way in which they run their bank accounts.

Any client money a firm receives should be held in a bank account designated a statutory trust account or in a bank account designated a non-statutory trust account. The main difference between the two types of trust is that, unlike the statutory trust, the firm acting as trustee may use the non-statutory trust to make advances of credit, to enable a client's premium obligation to be met **before** the firm receives the premium from the client. Similarly, firms can pay claims and premium refunds to a client from a non-statutory trust before they receive those monies from the insurance company. **Neither is permitted under the statutory trust.**

The other problem that is faced by firms is that where they receive mixed remittances e.g. client premium which includes an element of commission, the firm will need to remove any commission from the statutory trust as soon as practical and, at latest, within 25 days of receipt. (Note: the commission payment receipt terms will normally be set out in the product providers terms of business with the firm)

CASS (Client Assets Sourcebook) contains detailed rules relating to how and when client money should be paid in and out of client accounts, how trusts should be established and how and when client accounts should be reconciled.

**ATEB view:**

It is envisaged that smaller firms will opt for the statutory trust because it is simpler, more relevant and cost effective and will result in a lower financial resource requirement.

**Action required by you:**

Firms should consider the most cost effective way of dealing with the changes and this may involve changing their software or back office system. It certainly highlights the need for robust account reconciliation systems and procedures

This is an important area for firms and if they are unsure as to the requirements we suggest that they take individual guidance from the FSA or speak with ATEB.

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## 11. Risk Transfer – Acting as Agent

This article applies to General Insurance Brokers.

When a firm acts as agent for an insurance company (to receive and handle premiums, claims money or premium refunds) the insurance company bears the risk for any losses which may arise from the failure of the firm to make a transfer of these funds. Such failure could occur, for example, because the money is misappropriated by the firm (or by a third party to whom the firm passed the money) or it is lost through either party's insolvency. When the insurance company bears the risk of such losses, the industry often refers to this as **risk transfer**. Money held as agent for an insurance company is not client money under FSA rules, so the firm must not hold it in a segregated client money bank account, however .....

The firm might hold some of its customers' funds as agent for an insurance company, while in its dealings with other customers it might not act as agent for an insurance company. In these circumstances it would have to hold money received from the second group of customers as client money in a segregated bank account. The FSA are aware that this is changed practice for most firms.

When your firm is holding money as agent of an insurance company, the insurance company may specify in the terms of the agency agreement the required banking arrangements.

However, **provided the insurance company does not specify banking arrangements to the contrary**, until 14 January 2006, the FSA will temporarily allow firms to hold money received as agent of an insurance company in the segregated client money bank account (i.e. the statutory trust account).

### FSA application process - Problem

There is a problem with the application process in that the relevant question does not allow you

to answer [Statutory Trust or non Statutory Trust] and Risk Transfer. If you intend to operate, both risk transfer and [statutory trust or non statutory trust] the FSA have suggested that you input a combination of Non Statutory trust, Statutory Trust and Risk Transfer (i.e. Option e). This (they say) should be selected even if you will not use either of the non-statutory trust or statutory trust.

#### **ATEB view:**

ATEB are currently clarifying whether this is indeed the correct option and that (if selected) it will not result in additional requirements being placed on smaller firms which intend operating a statutory trust. Providing someone in the retail firms division is kind enough to respond to our emails we will report back, although don't hold your breath, as we are more likely to see the return of Lord Lucan first!

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

If your firm is in any doubt as to whether it is holding money as agent it should consult the terms of its written agreements or terms of business with insurance companies and, if necessary, seek clarification with the relevant insurance companies. This is an important area for firms and if they are unsure as to the requirements we suggest that they take individual guidance from the FSA or speak with ATEB.

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## **12. Scanning System – Document management made easy**

It's a fact that many Firms are reluctant to get involved in scanning, probably because they believe it to involve additional cost and maybe because, psychologically, they feel more comfortable with hard copies. Over recent years, scanning systems have developed to become more cost effective and simpler to use. So, what is the FSA's view? Lets look at what the FSA say in their 'handbook'.

### **Systems and Controls Sourcebook (SYSC)**

(SYSC) 3.2.20 Records

(1) A firm must take reasonable care to make and retain adequate records of matters and dealings (including accounting records)

(SYSC) 3.2.20 expands to explain that the records ..."must be capable of being reproduced in the English language on paper"

(SYSC) 3.2.21 A firm should have appropriate systems and controls in place to fulfil the firm's regulatory and statutory obligations with respect to adequacy, access, periods of retention and security of records. The general principle is that records should be retained for as long as is relevant for the purposes for which they are made.

### **Conduct of Business Sourcebook (COB)**

Form of records – relating specifically to 'Financial Promotions'

(COB) 3.7.5 a firm may arrange for records to be kept in such form as it chooses, such as hard copy, disk or tape. If the financial promotion is not in a written form, the record should represent the actual financial promotion as accurately as possible. A record would be "readily accessible" if it were available for inspection within 48 hours of the request being made. \_ SYSC 3.2.20 R (2) (Records to be capable of reproduction on paper) does not apply to records of non-real time financial promotions.

### **Introducing Office Warehouse Document Management System**

Office Warehouse is a flexible and easy to use Document Management system. It is particularly suitable for Independent Financial Advisors desperately trying to comply with regulations without being forced to use all their office space to store paper documents (which subsequently can't be found).

The Office Warehouse software runs on a single PC, or in a network environment for the larger users, and is able to store and manage any file regardless of type. Paper documents, pictures, even signatures are scanned, and indexed by client and stored ready for instant retrieval along with word-processor files. Every time a new document is added or a change is made, the automatic audit trail records the transaction. Very analogous to a filing cabinet (or a storage box!), except that once the images are securely stored, 99% of the original paper can be safely discarded.

A universal comment by users of Office WareHouse is how easy the system is to use.

The phrase 'user-friendly interface' is an often overused term, but in this case, one that describes how the system fits into a working practise without being an IT imposition on day-to-day users.

**ATEB view:**

Scanning systems cater for all the above and, arguably, they are more accessible and secure than paper based systems. If we apply the general principles that records should be available within 48 hours, the scanning system will cater for this and more. If you would like more information or testimonials, please contact us.

**Action required by you:**

You are under no obligation – why not call us for a free demonstration and price estimate.

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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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