

**A Consultative Paper on the
Review and Consolidation of the Financial
Services Regulatory Legislation**

6th March 2006



Financial Supervision Commission *Barrantee Oaseirys*

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SECTION 1

1. INTRODUCTION

The Financial Supervision Commission is currently undertaking a review of all the financial services regulatory legislation under which it operates with the aim of consolidating this into one Act and one “rule-book” that will apply to all the activities and financial products (Schemes) it is responsible for regulating.

A principal reason for the consolidation and review is that there is currently a plethora of Acts, Regulations, Regulatory Codes and Orders, which have developed piecemeal over the years as the Commission assumed responsibility for the regulation of different types of financial services. The various Acts remain based upon the foundation laid down over 25 years ago when banking business first became a regulated activity. The Commission believes that it is now time to modernise this regulatory framework to provide a good platform for commercial growth whilst ensuring that the legislation is suitable to meet today’s regulatory risks.

The first stage of this review is to consolidate and modernise the primary legislation. The Commission recognises that the needs of the industry are key to this process and to this end, the new Bill needs to be flexible enough to avoid the perception of unnecessary “red tape” but contain powers that are robust enough to enable the Commission to regulate effectively whilst, at the same time remaining accountable. The Commission is not seeking to increase its powers but rather to ensure that those powers are fit for the purpose.

The intention is that the Bill will make clear the Commission’s objectives, functions and the principles it applies in regulating licenceholders, and will formalise the mechanisms relating to the Commission’s accountability both to Government and to the industry. Many of the mechanisms for this accountability already exist on an informal basis but these should be set out in a formal structure so that the Commission’s performance can be measured against its objectives.

It is also envisaged that the consolidation will make changes that iron out inconsistencies across the different licensed sectors as well as streamline and update the legislation. The shape of the modernised consolidated Bill is outlined in Section 4 of this paper and, where there are proposed changes to the practical effect of existing provisions, these are detailed in Section 6.

The Commission’s impact assessment in Section 3 further examines the advantages and disadvantages of this legislative review and includes the proposed timetable for future consultation. On balance, the Commission believes that there are significantly greater benefits to industry than disadvantages in revising the legislation.

To ease the burden on the industry, we will be consulting on specific aspects of the consolidation in stages. In this first stage of the consultation, your views are particularly sought in respect of the structure and content of the new Bill, which not only has the longest lead-time but is also the key to the entire regulatory framework. Later in the process, we will be consulting further on issues relating to the subordinate legislation (Regulated Activities Order, Exemption Regulations, Regulatory Codes / “rule-book”).

In addition, as part of the consultation process, it is proposed that a Legislative Liaison Group is established with representation from the relevant industry bodies, advocates, accountants etc. The Legislative Liaison Group will meet on regular basis to discuss elements of the review, and then feedback and seek comments from the respective members of their industry bodies. Accordingly, we will be writing to the representative associations and professional bodies asking them to identify a representative for this working party.

It would assist us in our consideration of the industry's responses if you could relate your comments to the specific questions. However, we welcome your views on all related issues and so if you have any additional comments, please add them after your answers to the questions. The questions are summarised in Section 7 and it would assist us if you use the link to submit your answers and comments electronically via the link provided in Section 7.

It would be much appreciated if we could have your response as soon as possible and at the latest by **28th April 2006**.

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SECTION 2

2. EXECUTIVE SUMMARY

This document explains the Financial Supervision Commission's proposals for the forthcoming replacement of the Commission's primary legislation by one new law, known as the Financial Services Bill. Where practical, legislation will be consolidated for all industry sectors, in order to provide a simpler framework for diversified financial services businesses.

Our intention is:

- to reduce bureaucracy and
- to produce legislation that facilitates the development of quality business, both now and in the future.

The Financial Services Bill will specify:

- the remit
- the regulatory functions and
- the accountabilities of the Commission
- its enforcement powers
- its powers in relation to the exchange of regulatory information and
- its relations with other bodies in the Island and elsewhere.

The Bill will be supplemented by new secondary legislation defining:

- which activities are regulated
- what is required of operators in these industries, and
- how business should be conducted.

The single law will enable us to issue one licence per licenceholder. This licence will list the activities for which each entity is licensed.

In revoking and replacing the existing laws, the Commission's main aims are to make legislation:

- simpler
- clearer
- more user-friendly and
- up-to-date.

In designing the new framework, we are reviewing rules in the UK, Jersey, Guernsey and other jurisdictions, as well as our own current laws, to identify what appear to be the options best suited to the Isle of Man.

The new framework will take full account of relevant international issues and is designed to meet international expectations, in order to help our licenceholders to remain competitive and develop their business opportunities globally. The Commission is keen to facilitate the expansion of the Island's financial industry, whilst discouraging and preventing the abuse of the jurisdiction, in order to enhance the economy and reputation of the Isle of Man.

We plan to ensure that the Commission's powers are clear, logical and appropriate, but sufficiently robust to enable us to address risk and to investigate/terminate illegal or inappropriate business promptly. Our increased accountability will be evidenced by enhanced reporting and annual audits, as well as rights of appeal against the Commission.

Whilst we appreciate that any change initially presents a hurdle of familiarisation, we believe that the benefits of the simplicity and clarity of a consolidated framework based on one single law will be a distinct advantage over the current, sometimes out-dated, financial supervisory legislation.

To help ensure that the Financial Services Bill gives us the flexibility to monitor and control risk effectively in a changing financial services environment, we are convening a Legislative Liaison Group of representatives from industry and professional bodies, as well as seeking the views of all interested parties on these proposals. There will be ongoing opportunities for comment as the project progresses.

SECTION 3

3. WHY ARE WE DOING IT?

The Commission has considered the benefits of the proposed review and consolidation of the financial services regulatory framework and has tried to identify and address potential concerns that industry may have. The conclusions reached during this consideration are detailed below.

The Commission has published an impact methodology¹ to be applied prior to, and during the process leading up to the introduction of any new policy or change of policy. At this early stage, the Commission has undertaken an initial Benefit/Impact Analysis and, following this consultation and throughout the process, the Commission will continue to consider the impact of the proposals in conjunction with industry. This will ensure that the project is supported by a full and meaningful Impact Assessment process.

3.1 Stage 1 – Preliminary Consideration of the introduction of a consolidated financial services regulatory framework

The consolidation exercise will provide an opportunity to review and update existing legislation. The main benefits of a consolidated financial services regulatory framework would be to:-

- Streamline and update existing legislation;
- Reduce “red tape”;
- Meet both international standards and business needs; and
- Encourage and support innovation within the industry.

As part of its deliberations, the Commission has researched the legislative frameworks of other relevant jurisdictions and compared the various regimes against each other and against its own current framework as part of a process designed to identify the most appropriate way to enhance the Island's competitiveness. The Commission has concluded that, in line with many modern legislative frameworks, the preferred course of action is to have:-

- One Financial Services Act (working title), which would establish the broad regulatory framework for all of the existing regulated persons/products (banking, building societies, investment business, fiduciaries and collective investment schemes);
- A Regulated Activities Order, made under the Act, which would identify all the regulated activities and services and exclusions (where the Act does not apply). As subordinate legislation, this will be easier to amend thus enabling the Commission to keep up with new trends and developments in a timely fashion;
- Exemption Regulations which would specify exemptions (where the Act does apply but a licence is not required); and
- One Regulatory Code (or “rule-book”) to specify both the various general business requirements e.g. regulatory reporting, conduct of business and financial resource requirements as well as sector-specific requirements.

¹ [www.fsc.gov.im/Supervision & Policy / Policy Statements / “A Framework for Impact Analysis / Flow Chart / Aide Memoire”](http://www.fsc.gov.im/Supervision%20&%20Policy/Policy%20Statements/%20A%20Framework%20for%20Impact%20Analysis/Flow%20Chart/Aide%20Memoire)

The Commission has identified a number of areas where significant improvements could be made and discussions have been held with Treasury to gain general support for the Commission's proposals. It is concluded that a consolidation would be of substantial benefit both to licenceholders and potential new licenceholders as well as the Isle of Man generally. However, it is also acknowledged that, in the short term, the consultation process and "bedding in" of the new legislation may be a temporary burden to licenceholders. The Commission has tried to anticipate, and address in advance, concerns that may arise at various stages. However, input from practitioners working within the framework is crucial to ensure that it is as workable and flexible as possible.

3.2 Stage 2 – Initial Assessment of the advantages and disadvantages to the Industry, the Commission and the Isle of Man

The Commission considers that the advantages of reviewing and consolidating the financial services legislation far outweigh the disadvantages and the risks arising from not undertaking the consolidation at all. Consideration has also been given to the time it will take to complete the project, which is estimated to be approximately two years allowing for consultation and the legislative process.

The Commission has categorised the review and consolidation of financial services legislation to be a high priority as it is believed that the proposed new legislation will enhance the Island's reputation and provide an opportunity for the Commission to regulate its licenceholders more effectively and respond to industry's needs with more flexibility. In the longer term, it is envisaged that a consolidated financial services regulatory framework will reduce the cost of compliance without lowering the standards of compliance.

The Commission has also considered the importance of the updated consolidation to the industry, the Commission and the Island and, given the benefits to all parties, which are outlined below, this is also categorised as high.

3.2.1 Streamlining and Updating

The consolidation will give the Commission the opportunity to streamline and update the legislation underpinning its licensing and supervision roles in each area of regulated business, resulting in a dynamic and commercial framework which will facilitate competitive advantage.

It will also allow undesirable inconsistencies in content and style, which may confuse or have the potential for different interpretation to be addressed and provide the basis for a clear and consistent approach to authorisation and supervision, supporting the Commission's consolidated supervisory approach.

Apart from the initial costs of familiarisation and implementing the new framework, there will be a reduction in the regulatory burden especially for those entities undertaking more than one regulated activity facilitating expansion of existing businesses. New businesses will only have to familiarise themselves with one, modern piece of legislation, which may encourage new business to the Island.

3.2.2 Reduction of “red tape”

The Commission does already try to minimise “red tape” wherever this can be achieved without compromising regulatory standards or increasing risk. As part of the consolidation the Commission would particularly welcome any feedback from industry about areas where they perceive that there is unnecessary “red tape”.

The consolidation exercise will provide the Commission with an opportunity to simplify the authorisation process for new activities as well as reducing the regulatory burden which will result in a more attractive framework:-

- An integrated regulatory framework with clearer rules and increased transparency will result in a reduction in the regulatory burden and in the costs of compliance.
- It is envisaged that the new framework will be more attractive to both existing and new businesses to the Island.
- A consolidated framework will enable the Commission to issue a single licence for a number of regulated activities, instead of the current arrangement where some entities undertaking different activities require several licences.
- The “one licence approach” will simplify and expedite the process for undertaking new or amended activities as this would be an extension of an existing licence with a simplified process concentrating on the new activity rather than going through a full new licence application process. It is considered that this may encourage licenceholders to expand their activities on the Island.

Question A:

Are there any processes which you feel result in unnecessary “red tape” in the current regulatory framework?

3.2.3 Review of Powers

The consolidation is a catalyst for a review of the powers of the Commission. Such a review is important to ensure that the Commission's powers are clear, effective, proportionate and appropriate. For example, the current regulatory enforcement powers could be made clearer, more proportionate, logical and effective.

3.2.4 Assessing Regulatory Risk

The Island's financial sector has matured considerably since the inception of the Commission in 1983, resulting in more sophisticated licensed sectors and a higher degree of trust between the Commission and licenceholders. Consequently, it is appropriate that the Commission reviews the legislation, to favour a more flexible approach balanced against the level of regulatory risks rather than retaining a framework which may be seen to encourage a more restrictive and rigid style of regulation.

3.2.5 Compliance with international trends and standards

The Island's international reputation would be enhanced by, for example, new modern and up-to-date legislation, which would reflect well both on the Island as an international centre, and on those businesses operating on the Island.

The review would also provide an opportunity to ensure that the new legislation encapsulates all relevant international standards which it is deemed essential to adopt e.g. Basel II.

However, the review would also provide an opportunity to ensure that the regulatory framework fully implements and reflects the proposed overriding regulatory strategy in relation to the implementation of international standards as set out in Section 5.2.1 below.

As a preliminary to this exercise, in considering the revised framework, the Commission has researched the legislative frameworks of other relevant jurisdictions and compared the various regimes against each other to ensure that, as far as possible, there would be a level playing field with other jurisdictions, thus reducing the potential for regulatory arbitrage, whilst ensuring that it is not "ahead of the game" in the imposition of regulatory standards.

3.2.6 Opportunity for industry to input into revised framework

The review and consolidation will provide an opportunity to encourage and support innovation within the industry.

Industry is encouraged to contribute meaningfully to the proposed legislative changes to ensure that these meet their current and future needs.

The extensive consultation, which will be on a phased basis at appropriate times during the review, may be a temporary burden on the industry, professional advisers etc. However, it is considered that this is counter-balanced by the ability to contribute to the design of the regulatory framework. It is also the Commission's intention to facilitate the consultation process by consulting on focussed issues, on a staggered basis, as well as identifying areas of amendment by providing a "road map" to changes.

3.3 Stage 3 – Consultation

The purpose of this consultation is to inform you of the Commission's proposals with regard to the review and consolidation of financial services legislation, outline the proposed shape of the Bill, and to discuss with you our initial thoughts on how this will be progressed.

The Commission has completed a comparison and analysis of the provisions of the principal Acts which will be consolidated and revised, to identify areas where changes will have no material effect on the relevant licenceholders and those which will be subject to a more significant amendment. The matrices are attached as Appendix A and your comments are invited on the more significant amendments, which are explained in Sections 5 and 6. The questions in Section 5 and 6 are summarised in Section 7, including a link to enable you to answer electronically.

As mentioned earlier, in order to reduce the burden of this level of consultation, the Commission will be providing a "road-map" to assist in identifying those areas where material

amendments are proposed as opposed to pure consolidation where minor changes have been made.

In addition, as part of the consultation process, it is proposed that a Legislative Liaison Group is established specifically to assist with the review, with representation from the relevant industry bodies, advocates, accountants etc. The Legislative Liaison Group will meet regularly to discuss elements of the review, and then feedback and seek comments from the respective members of their industry bodies.

3.4 Stage 4 – Post Analysis, Implementation and Review

Following this initial consultation, it is proposed that the following additional consultation will occur at later stages of the process:-

Consultation Timetable	Timeframe
Initial consultative document on the Regulated Activities Order	Q 2 - 2006
Subject to the Legislative Draftsman, the draft Bill will be circulated for information purposes	Q 3 - 2006
Initial consultation document on Client Money/Client Asset/Custody elements of the Regulatory Code	Q 3 - 2006
Initial consultation document on Conduct of Business/Advertising elements of the Regulatory Code	Q 4 - 2006
Initial consultation document on Financial Resources/Liquidity/Capital Adequacy, Audit Requirements and general requirements elements of the Regulatory Code	Q 4 - 2006
Consultation on ancillary matters including fees and forms	2007

It is proposed that the consultation period at each stage will be at least 8 weeks.

SECTION 4

4. SHAPE OF THE BILL

As noted in the introduction and impact assessment (Sections 1 and 3 respectively), a consolidation of the relevant financial services legislation into one Financial Services Act provides the opportunity to modernise and adapt the existing provisions to provide the framework for a regime that can be flexible enough to avoid red-tape, whilst providing the platform for effective regulation that covers all relevant regulatory risks. These positive effects on licenceholders may become more apparent in the next stage when the Regulatory Codes are consolidated and revised, however, in order to achieve this, it will be necessary to make some changes to the primary legislative framework under which the Codes are made.

The Commission is not seeking any additional powers and therefore the regulatory framework in the existing Acts will remain substantially unaltered but, within that framework, the “furniture” may move around as the opportunity will be taken to modernise, make the legislation more accessible and easier to understand, and ensure consistency across all regulated sectors. There also needs to be some flexibility in the Bill so that regulation can be adapted to meet the needs of the Island’s fast developing finance sector. It is proposed that the Bill includes an appropriate level of formal accountability and the Commission will also be reviewing its disciplinary powers to ensure that they are proportionate, fair and appropriate.

4.1 Current legislation to be repealed or amended

The Acts that will be affected by the Bill are as follows.

Legislation relating to the constitution and responsibilities of the Commission

Financial Supervision Commission Act 1984

Statutory Boards Act 1987 and Statutory Boards (Amendment) Act 2001 (may be affected by amendments made to the above Act)

Financial Supervision Commission Order 1983 made under the Statutory Bodies (Transfer of Functions) Act 1969

Regulatory legislation

Building Societies Acts 1892 – 1986 (regulatory provisions only)

Financial Supervision Act 1988

Investment Business Acts 1991 – 1993

Banking Act 1998

Corporate Service Providers Act 2000 (as amended by the Fiduciary Services Act 2005)

To assist industry in finding what has happened to existing provisions, changes will be mapped for you when the Bill is finalised.

4.2 How the new Bill will look

The Bill will bring together in one piece of legislation all the existing provisions that affect licence applicants and licenceholders across all regulated sectors. This is mainly a consolidation of the relevant “regulatory” Acts but, to enhance transparency and make the legislation more accessible, it is also proposed to include provisions relating to “How the Commission works”. It is envisaged that, subject to the drafting preferences of the Attorney General’s Chambers, the Financial Services Bill will be laid out as follows:-

Part 1 – The Commission

- Objectives
- Statement of functions
- Principles to be applied in carrying out the objectives and functions
- Accountability mechanisms

Part 2 – How the licensing regime operates

What is regulated

- Regulated activities (detail to be contained in a Regulated Activities Order)
- Exclusions from the application of the Bill
- Exemptions from the requirement to hold a licence (detail to be contained in Exemption Regulations)

Licensing

- Requirement to hold a licence in respect of regulated activities
- Power to issue, vary and revoke a licence or make a licence subject to conditions

How we regulate

- Power to make subordinate legislation (regulatory codes/ “rule-book”)
- Supervisory powers – powers to visit, require information, make directions etc.
- Sector-specific requirements in respect of banking and investment business including functionaries of Schemes (to protect investors and to protect financial markets)
- Obligation on auditors to report breaches of regulatory legislation

Powers of Intervention

- Appointment of a reporting accountant
- Application to Court to appoint a manager or receiver

Disciplinary and Enforcement Powers

- Investigations
- Not Fit and Proper Directions/Sanctions
- Other Disciplinary Sanctions
- Unlicensed business
- Offences/penalties

Part 3 – Collective investment schemes

Subject to a review of particular issues, this will largely reflect the current provisions relating to Schemes as set out in the Financial Supervision Act 1988.

Part 4 - Information, international obligations, compensation schemes, the Ombudsman etc.

A number of overarching matters would be gathered at Part 4 of the Bill. These would include:-

- Non-Public and Restricted Information
- Relations with other jurisdictions and bodies (gateways and international cooperation)
- Compensation schemes
- Financial Services Ombudsman Scheme
- Complaints
- Review of Decisions

SECTION 5

5. THE COMMISSION'S REMIT, FUNCTIONS AND ACCOUNTABILITY

The Commission is conscious that its remit, functions and accountability mechanisms are not clearly set out in one place, and in some cases, are not formalised. This is largely due to the way in which the Commission has evolved over the last 22 years and can lead to a lack of clarity for third parties who want to understand what the Commission is entrusted to do, how it achieves its aims and to whom it is accountable.

The Commission sees this project as the ideal opportunity to set out in statute a clear statement of its remit and functions as well as statutory requirements to ensure that the Commission is clearly accountable to its stakeholders². A clear and transparent statement of what the Commission is and how it operates will assist not only the Commission itself but also those who deal with it.

The following proposals should also be seen in the context of evidencing the development of the Commission's operational independence.

This section sets out proposals for the content of such a statement, including:

- the responsibilities (remit) of the Commission;
- how regulatory strategy is to be determined; and
- the operation of the interface between the Commission and its key stakeholders and the mechanisms that should be put in place to ensure that the Commission carries out its responsibilities in a transparent fashion and is accountable for its actions.

The Commission and Treasury have discussed the broad coverage outlined in this section and welcome comments.

5.1 Remit (Objectives, Functions & Guiding Principles)

The Commission's current statutory objective is set out in the Financial Supervision Commission Order 1983 as follows:

"6. (1) The Commission shall exercise the functions conferred on it by this Order and such other functions as may be conferred on it by any other statutory provision.

(2) The Commission shall take such steps as appear to it to be necessary or expedient for the effective supervision of the private financial and commercial sector in the Island, but with the exception of the insurance industry."

Whilst the scope of this remit is wide, it is not particularly clear and it has been supplemented by the Commission's published Mission Statement:

"To protect the public interest by providing effective regulation and supervision within the Island's financial services sector and to support a competitive environment in which quality products and

² The key stakeholders being (in no particular order) Government, Tynwald, the Judiciary, Licenceholders and Consumers/the General Public.

services are promoted for the economic benefit of the Island, and to foster good working relationships within the business community."

Since 1983 the Commission's remit and activities have extended and changed and it is therefore appropriate that they should be reviewed and updated at this time.

The International Monetary Fund ("IMF"), in its assessment report, suggested that the Commission should establish a clear, complete and authoritative statement of its responsibilities and noted that:

"There are a number of reasons why this statement of responsibilities should be readily available in an authoritative form. The FSC has extensive powers of regulation which touch upon the reputation of those who deal with it. They are entitled to have a statement in this form. The commissioners and staff need to be constantly aware of the nature of the FSC's responsibilities as well as the terms of the Mission Statement."

In order to address these points and to formalise the Commission's objectives, which will encompass all of its current responsibilities including responsibility for Companies Registry, it is proposed that these are enshrined within the Bill. The objectives will be underpinned by a statement of the Commission's regulatory functions and the guiding principles it applies in achieving its objectives and performing its functions.

The objectives should be sufficiently defined to show how the Commission relates to its licence applicants and licenceholders and to allow them to measure the Commission's performance of its functions against its objectives, functions and regulatory principles. However, the definition also needs to be flexible enough to adjust to developments in the finance sector. For example, Treasury has already identified e-money as an area that requires regulation and we are currently looking (with the support of that industry) at developing a regulatory regime for this sector. The newly restated remit of the Commission will have to be sufficiently flexible to allow additional new regimes to be developed if necessary.

The Commission is therefore, proposing that the following areas are included within the Objectives, Functions and Guiding Principles for the Commission under the Bill.

Objectives – The Commission would like to have clear stated objectives which cover:-

- The effective regulation and supervision of persons undertaking regulated activities;
- Specific powers in relation to the prevention of financial crime in the context of regulated activities;
- The Commission's role in relation to offences under the Companies Acts and the duties of company directors (e.g. petitioning the Court for Disqualification of Unfit Directors);
- The Commission's responsibilities for running an efficient and commercial Companies Registry;
- The Commission's role in relation to -
 - seeking to protect the interest of consumers; and
 - the development of the Island as an international financial centre (by having a commercial, flexible and effective regulatory regime).

Functions³ - It is proposed that the Commission's specific regulatory functions are clearly defined to encompass licensing and authorisation matters, supervision and enforcement. There should also be a clear statement of the Commission's general responsibilities for developing the regulatory regime, operation of Companies Registry, operation of compensation schemes and any other relevant roles it is considered appropriate that the Commission undertakes.

Guiding Principles⁴ - The Commission would like to introduce Guiding Principles, which would require the Commission to consider the following issues when undertaking all of its functions:

- The responsibilities of controllers of a licensed entity when conducting business;
- The proportionality of burden to expected benefits when considering proposals for change;
- The efficient and economic use of resources by the Commission;
- The importance of facilitating licenceholder innovation in the regime;
- The importance of maintaining the Island's competitive position by -
 - minimising the adverse effects on competition from regulation (and avoiding regulatory arbitrage); and
 - facilitating competition.

Question B:

Do you feel that the objectives, functions and guiding principles outlined above would assist you in understanding the broad boundaries under which the Commission should operate in the future? We would welcome any comments that you have on this proposal.

5.2 Determining Regulatory Strategy

It is not currently clear to everyone who has (or should have) responsibility for setting the broad principles that should govern and inform the creation of regulatory policy. As a result, concern can arise that the Commission is not subject to appropriate controls in setting its regulatory policy. This lack of clarity should be addressed as part of the review.

The Commission's existence and current institutional form as a Statutory Board depend on the will of Tynwald and it is recommended that this should continue to be the case. Furthermore, the Commission's powers to carry out its role are derived from legislation. Any changes to those powers, including any changes necessary to implement regulatory policy that it seeks to put in place, will require legislation to be passed. Tynwald approval is also necessary for this, as is the support of the Commission's sponsoring Department, Treasury. Thus, without a close relationship and the support of Treasury, the Commission cannot carry out regulatory policy, regardless of who sets it.

³ Regulatory functions are the mechanics which support the achievement of objectives. Currently the Commission's functions are not easily identifiable across the broad range of legislation and this can lead to inconsistency. The Commission would like its regulatory functions to be better defined to ensure clarity, transparency and accountability and to focus attention upon the Commission's performance in key areas.

⁴ Guiding principles are matters which would be considered by the Commission when meeting its objectives. The statement of these will have the benefit of setting out benchmarks against which actions can be judged and so underpin the Commission's accountability framework.

However, the questions remain as to who has responsibility for the initiation and implementation of regulatory policy; who is responsible for thinking up new ideas or setting new standards and who enforces the rules once made. It is recommended that these questions be addressed as part of the review and the responsibilities be clearly set down in the revised framework.

5.2.1 Overriding Government Regulatory Strategy

The Commission and Treasury put forward the following proposals for comment. The overriding Government strategy should be that regulation of the financial services industry on the Isle of Man should follow the principles of established international standards and embody the following broad principles:

- The Isle of Man is committed to promotion of a level playing field universally applicable to the regulation of financial services;
- The Isle of Man will adhere to principles of regulation which are widely accepted and applied in the leading international financial centres in both large and small countries;
- The Isle of Man will take cognisance of aspirational standards of regulation articulated by standard-setting bodies, even if such principles are not universally, or widely applied in other leading financial services centres. However, the implementation of such aspirational standards will be a discretionary decision, within domestic competence, determined by Treasury and will take into account competitive implications.

5.3 Setting Regulatory Policy

Treasury, the Commission or the industry may suggest changes to regulatory policy. It will typically be the Commission which will co-ordinate a consultation on resulting proposals involving all stakeholders and determine the detailed changes to legislation or guidance necessary to effect the policy.

Primary legislation is drafted by the Attorney General's Chambers on the instructions of the Commission with Treasury's concurrence. Secondary legislation and guidance is drafted by officers of the Commission under the guidance of the Attorney General's Chambers. All legislation (primary and secondary) is approved by Treasury, following consultation with the industry on the detailed changes proposed. Legislative changes will be submitted for Tynwald approval as necessary.

Treasury therefore already approves the regulatory policy as enshrined in legislation. The Commission is then responsible for implementing agreed policy within the terms of any guidance which may have been issued.

The roles in relation to setting and implementing regulatory policy can therefore be summarised as follows:

Role of Tynwald (the Legislature)

- Scrutiny and approval of the formal legislative framework to implement policy changes.

Role of Treasury (as the relevant Executive arm of Government)

- Decision on changes to the Overriding Government Regulatory Strategy (see 5.2.1) including any changes to Regulator's role and remit.
- Proposals for policy change.
- Consideration and approval of policy propositions in the light of the Island's strategic objectives, the overriding principles and the views of industry and the Commission.

Role of the Commission (the Regulator)

- Initiation and development of policy propositions in the light of market and international standards development, government strategy and industry consultation.
- Development of the detailed rules necessary to effect a policy change, in consultation with industry and subject to the approval of Treasury and Tynwald.
- Implementation of policy and legislation once adopted by Government and approved by Tynwald.

Role of Industry (as a stakeholder)

- Suggestions for policy change;
- Advising on potential policy propositions through various fora. It is proposed that an Industry Advisory Group could be formed to assist in this process (see 5.4.3 below);
- Comment upon policy propositions through formal consultation process;
- Contribute to the detailed assessment of impact for particular policy proposals under the Commission's published "Framework for Impact Analysis".

5.4 Accountability

The Commission believes that it is important that a regulator, like any other corporation or government agency, can demonstrate that it is transparent in its dealings and is accountable to its stakeholders. Accountability measures are important mechanisms for assessing whether the Commission is operating fairly, effectively and in accordance with appropriate standards of corporate governance in carrying out the functions summarised above.

The Commission is already subject to some formal statutory accountability requirements, and has informally adopted others to conform with best practice. Some of the current key accountability measures are set out below.

5.4.1 Accountability to its stakeholders (via Tynwald, the Island's parliament)

- The Commission's powers are established through Acts of Tynwald and as such are subject to full legislative scrutiny. The Commission must, at all times, operate in accordance with its statutory powers. If the Commission were to exceed these powers any such action would be open to challenge as invalid.
- The Commission publishes an Annual Report and audited Accounts each year. Whilst this is not currently a statutory requirement the Commission believes that it is important to be transparent about how it operates and is financed. The Commission would like to see the preparation and dissemination of an Annual Report and audited Accounts becoming a statutory requirement. As an adjunct to such a requirement, it may be appropriate for Treasury to have the ability to require the Commission to cover specific matters in the published Annual Report where necessary.

- The Commission, through Treasury, answers any questions raised in the parliamentary process and provides briefings on legislative proposals. The Commission is, however, conscious that in contrast to other jurisdictions there is no requirement for the Commission to provide briefings, or answer to, a specific Committee of Tynwald. Were Tynwald minded to set up such a committee, the establishment and remit of an appropriate Committee of Tynwald could be considered as part of this review. The Chairman and the Chief Executive could be called to answer questions of such a committee.
- As a further mechanism to evaluate the manner in which the Commission operates, the Commission would be willing, if Tynwald was so minded, to submit its budgets for “Value for Money” interrogation.

5.4.2 Accountability to Government (via Treasury, the relevant Executive arm)

- As the Commission’s sponsoring Department in Government, Treasury approves policy initiatives prior to the introduction of any legislative initiatives.
- The Commission is accountable to Treasury for its actions. As part of the accountability mechanisms it is proposed that the Commission should report annually to Treasury on performance against its statutory objectives. If such a system were to be established, it would be appropriate for Treasury to set out particular items that should be included in the report. This could include a report on the core corporate governance structure existing within the Commission.
- Such a report could include a statement from non-executive Board Members about the discharge of their functions, including a view about whether the Commission is using its resources in an efficient and economic way. The Treasury would retain an overall “Value for Money” responsibility.
- It is proposed that the Commission and Treasury enter into a Memorandum of Understanding setting out the manner in which each body will exercise its respective responsibilities and interact under the new framework (see 5.5 below).

5.4.3 Wider Stakeholder Accountability

- Published Annual Report and audited Accounts;
- The Commission believes that it is vital for the integrity of the regulatory system that there are appropriate mechanisms for the review of its decisions. The Commission used the opportunity of the Fiduciary Services Act 2005 to ensure that all significant decisions of the Commission in relation to licenceholders and the fitness and propriety of individuals are subject to right of appeal to the Council of Ministers’ Review Committee.
- As it is a public body, the actions of the Commission are subject to the general requirements of the law of “natural justice” and may be challenged in court under the Petition of Doleance procedures.
- The Commission believes that effective consultation with its stakeholders about new regulatory proposals is a key stage in developing relevant, effective and proportionate

regulation. The Commission will continue to consult upon its proposals and consider their impact on stakeholders through impact assessments. In addition, it is proposed that the desire of industry to have an influence on the strategic decision making of the Commission should be addressed, perhaps through a specifically appointed Industry Advisory Committee. These consultative processes might usefully be enshrined in the new legislation.

- The Commission has a published complaints procedure which sets out how complaints about the Commission are investigated. The requirement to have a complaints procedure and deal with complaints in an appropriate way could be made a statutory requirement.
- The Commission provides detailed information about its regulatory framework and how it operates, on its website and on enquiry. A new consolidated regime would be easier to understand and explain and as such, understanding of the Commission and the regulatory framework will be increased.

5.4.4 The Need for Operational Independence

Regulation within the established and approved regulatory framework sometimes requires tough decisions and these should not be affected by external factors and not be subject to political or other influence.

Furthermore, international standard setting bodies expect regulators to be independent of Government and/or political influence. In its 2002 assessment the IMF found that the Commission was not in theory operationally independent.

The Commission believes that in order to demonstrate that it is an effective, flexible and modern regulator, it is important to have, and be seen to have, operational independence from Government. That is to say, the Commission should be able to exercise its powers within the statutory framework without the potential for political intervention. As a result, the ability for Government to interfere in operational matters under the current legislation, although in practice never used, should therefore be reviewed.

It is accepted that, in practice, powers to direct the Commission in its decision-making have not been used, however their existence gives a false impression of the relationship between the Commission and Government. As can be seen from the list of accountability mechanisms, the Commission is not seeking to avoid consultation upon or scrutiny of its legislative framework or the manner in which it exercises its legislative powers.

As readers will be aware the Government is currently undertaking a Review on the Scope and Structure of Government. The Commission believes the factors set out above will be relevant to this review. Any move toward greater operational independence will also need to address the Commission's financing and Government revenues.

Question C:

Do you feel that the accountability measures outlined above are sufficient to ensure that the Commission is publicly accountable in the exercise of its powers? We would welcome any comments that you have on these proposals.

5.5 Working arrangements - Treasury and the Commission

As stated above, Isle of Man Government has a responsibility to ensure that the Isle of Man's financial sector is effectively regulated and supervised. Treasury acts as the Commission's sponsor in Government. On finalisation of the new framework it is proposed that the Commission and Treasury enter into a Memorandum of Understanding, which would set out how the two bodies will work together in practice when exercising their respective responsibilities.

Such an agreement would typically set out:

- Each body's respective responsibilities under the regime including:
 - the Commission's responsibility for -
 - carrying out its remit in accordance with its Statutory Objectives and Guiding Principles;
 - initiating Regulatory Policy, as outlined at 5.2 above; and
 - implementing the agreed Regulatory Policy.
 - Government's responsibilities via Treasury for -
 - setting the Overriding Regulatory Strategy;
 - establishing the legal and institutional framework under which the Commission operates; and
 - appointing the executive and non-executive members of the Commission's Board.

- How accountability mechanisms would operate in practice including:
 - communication channels;
 - reporting and scrutiny mechanisms (both periodic and ad hoc); and
 - details to be included in formal reports.

- Provisions for the control of sensitive information.

SECTION 6

6. PROPOSED CHANGES TO EXISTING REGULATORY LEGISLATION AND POTENTIAL EFFECTS

The effect of the Bill will be to consolidate many of the existing provisions in the Acts listed in paragraph 4.1 above. However, a number of key changes are proposed and we are seeking views on each of the issues summarised below. Please respond to the specific questions and add any related comments after your response. (For quick reference and to allow you to respond electronically, the questions are repeated in Section 7 with an electronic link.)

The effect of the consolidation and review on the existing provisions in the Financial Supervision Act 1988, Investment Business Acts 1991 to 1993, Banking Act 1998 and Corporate Service Providers Act 2000 (as amended by the Fiduciary Services Act 2005) (“the principal Acts”) has been analysed and is attached as Appendices A1 - A4.

As you will see from the matrices relating to each of the principal Acts, the majority of the changes are pure consolidation or consolidation with some minor change, which are indicated by a tick in the first column (“No material effect on licenceholders”). If the consolidation of an existing provision to apply across all regulated sectors includes some small change, this is noted as a comment in that column. The second column (“More significant change proposed”) shows where an existing provision is being reviewed and the change that is proposed is summarised in the comment column. The purpose of this consultation is to explain the shape and content of the Bill and invite comment on the broad issues at this stage. There will be further detailed consultation with those affected on any substantive proposed changes (see 6.9 below re Schemes).

The proposed changes on which your comments are invited at this stage are explained in more detail below. It should be noted that it is proposed to move some items into subordinate legislation and they will be consulted on separately at a later date outside the consultation on the contents of the Financial Services Bill.

6.1 Regulated Activities

The modern trend is for primary legislation (the Financial Services Bill) to provide the legislative framework whilst complex and/or detailed requirements are contained in subordinate legislation (Orders, Regulatory Codes, Regulations etc). This provides more opportunity to achieve clarity and facilitates making adjustments to keep up with new trends and developments in financial markets and products. (Although both the Bill and Regulatory Codes will be subject to Tynwald approval, changing primary legislation can only be done by a new Act, which takes considerably longer to bring into operation than a new Code as a Bill must be considered at a number of separate sittings of Keys and Legislative Council, is then sent to the Department of Constitutional Affairs for comment before being signed by Tynwald and receiving Royal Assent.)

The requirement to hold a licence when undertaking any regulated activity, unless the person or activity is excluded or exempted (see 6.2 below), remains. However, it is proposed that all regulated activities will be described in detail in subordinate legislation made under the Financial Services Bill (a Regulated Activities Order).

Following the precedent set by the Investment Business Order 2004 made under the Investment Business Act 1991, the regulated activities in relation to banking, investment business, fiduciary services and functionaries of schemes will be defined in a single Regulated Activities Order. It should be noted that the Commission has also been asked to bring e-money into the regulatory framework.

It is envisaged that the definitions in the new Order will generally replicate current definitions of the regulated activities. However, these are being reviewed to take account of developments in the financial services industry and this review may result in a current definition being updated. Where any change is proposed, the industry will be fully consulted. In particular, it is expected that the definition of “banking business” will need to change to reflect the scope of and practices in modern day banking.

The Bill will include a statutory requirement for the Commission to consult those affected before making any change to the regulated activities.

Question D:

Do you agree that it is more appropriate to define the regulated activities in a Regulated Activities Order, which would allow for more detail and also facilitate the making of adjustments to keep up with developments in the finance sector?

6.2 Exclusions and exemptions

“Exclusions” refer to a person or a particular activity that is outside the scope of the regulatory regime because it was never intended to include such a person or activity.

“Exemptions” on the other hand apply to persons or the provision of services which fall within the scope of a regulated activity but which are specifically exempt from the requirement to hold a licence. The distinction is important because the Commission may, if necessary, exercise its powers under the Financial Services Bill in relation to an exempted person or activity but not in relation to an excluded one.

In recognition of the potential for regulatory risk, the opportunity will be taken to review whether it is more appropriate for an activity to be excluded or exempted and the extent to which a combination of individual exclusions and exemptions may be utilised by one entity.

As with the regulated activities, it is also proposed to move exemptions to subordinate legislation (Exemption Regulations). The Commission will seek guidance from the Legislative Draftsman as to whether it is more appropriate for exclusions to be contained in the Bill or in an Order.

As noted in relation to the regulated activities (see 6.1 above), this proposal follows the current trend in modern legislation to provide the framework in the primary and detailed descriptions in subordinate legislation. This provides more opportunity to achieve parity and facilitates adjustments where necessary to keep up with new trends and developments in financial markets and products. There will be a statutory requirement in the Bill for the Commission to consult those affected before making any change to the exclusions and exemptions.

It is envisaged that the definitions in the new Order will generally replicate current definitions but the opportunity will be taken to revise as appropriate. In particular, it is proposed that the exemption for “recognised persons” under s.4 of the investment Business Act 1991 be

removed. Such an exemption would only be viable if a “recognised person” was subject to regulation by another authority or body, which is equivalent to the Commission’s regulation of investment business licenceholders. This has not, in the Commission’s experience, been achievable and it is not therefore appropriate to allow anyone to operate outside the regulatory environment when they are providing the same service as those who are within the regime.

Question E:

- **Do you agree that it is more appropriate to define exemptions in Exemption Regulations, which would allow for more detail and also facilitate the making of adjustments to keep up with developments in the finance sector?**
- **If you do not agree that the exemption for “recognised persons” under s.4 of the Investment Business Act 1991 should be removed, please give your reasons.**

6.3 Directors, managers, controllers etc must be “fit and proper”

The fitness and propriety of a licence applicant/holder and key individuals who have significant powers and responsibilities in relation to that business, will remain central to the regulatory regime. However, in consolidating this requirement it is proposed to address the current differences in the appointments/roles specified in each of the principal Acts. To ensure consistency, it may be preferable to refer to particular functions relevant to a regulated sector rather than to appointment titles, which sometimes have different meanings in different businesses (for example “manager”).

The Bill should continue to reflect the Commission’s current practice in vetting the fitness and propriety of all key individuals within a regulated business and any change in the terminology used to describe such individuals does not therefore represent a change of policy.

The power for the Commission to declare an individual “not fit and proper” to act as a controller or in a key management role within a licenceholder’s business may, in some instances, be a sledgehammer to crack a nut. It may therefore be more proportionate, in the circumstances, for the Commission to have an intermediate disciplinary power (to issue a formal warning). (See 6.8.)

Question F:

Do you agree that, in respect of the individuals who are required to meet the Commission’s “fit and proper” test, it will enhance clarity if the Bill –

- **standardises the list of appointments/roles across all regulated sectors,**
- **extends to individuals who have significant powers or responsibilities in respect of the regulated activities undertaken by that business, and**
- **specifies those responsible for particular functions relevant to that regulated sector?**

6.4 Conduct of business and related matters (Regulatory Codes/Rule Book)

The current power for the Commission to make Regulatory Codes will remain but be reviewed in the consolidation for consistency and also to ensure clarity. It is proposed that, as with the Financial Services Bill, there will be just one Regulatory Code/“rule-book” that brings together the common standards and requirements that apply across all regulated sectors.

Where there are different sector-specific requirements, these will be specified separately. The Commission will, of course, continue to issue guidance to industry where this is appropriate.

Currently each of the principal Acts lists all potential matters that can be covered by regulatory codes. This is unduly restrictive and the Commission's current code-making powers do not allow a flexible approach to regulation, which can accommodate changes in business practices and thus provide effective regulation that is sensitive to commercial concerns. It is proposed that subject to the advice of the Attorney General's Chambers, the Commission's code-making powers are as flexible as possible to enable it to react and adapt the regulatory regime as appropriate to accommodate changes in the marketplace and/or address regulatory risk.

A statutory requirement for the Commission to consult with all those affected will be included in the Financial Services Bill. In addition any new code will, as currently, require Tynwald approval. It should be noted that the proposal to state the Commission's objectives and functions clearly in the Bill together with it being a statutory requirement for the Commission to consult with those affected before making any new Code and that Tynwald's approval is required, should provide sufficient safeguard to balance an increase in the proposed flexibility in the code-making powers.

Question G:

Would you prefer –

- **a more flexible regulatory framework, which can only be achieved if the Commission has more flexible code-making powers; or**
- **a more prescriptive regulatory framework, which provides greater certainty?**

6.5 Investigative powers/exchange of information

The Island's ability to attract the highest quality of business is closely linked to the Island's reputation as a safe, secure, well run and respectable jurisdiction. It is not in the interests of the regulated sectors or the Island as a whole for a perception to exist that the Island acts as a haven for dubious business. The ability of the Island to protect its reputation without prejudicing legitimate business interests is, therefore, of paramount importance.

In support of this, the Commission (like any other well run and respected regulatory body) must have adequate powers to obtain and exchange information in appropriate circumstances to assist another regulator in carrying out their functions.

The ability to assist other jurisdictions in preventing the use of financial services for criminal purposes and for the maintenance of orderly financial markets is therefore of both local and international importance in the prevention of terrorism, fraud or money laundering. Any significant weakness in a regulator's powers could, therefore, lead not only to criticism of the jurisdiction but also potentially to market access issues.

International regulatory cooperation is only possible if there are formal mechanisms in place for releasing relevant information. It is also important that there are adequate checks and balances in place to ensure requests are properly assessed and only appropriate information released.

In some circumstances the information needed to support a regulatory investigation in another jurisdiction could be related to a licenceholder's customer. For example, if a bank's customer was suspected of being a fraudulent broker committing securities offences in another jurisdiction, the regulator in that jurisdiction may seek evidence from the records of a bank based in the Island to show that the transactions did relate to securities breaches. It is important that the Island can assist in such cases. The Commission's current powers under section 17 of Investment Business Act 1991 would allow the Commission to assist in such a case but the same does not apply where the suspected transgression in the other jurisdiction does not relate to Investment Business and Securities. It is therefore proposed to extend the section 17 power to other areas of regulated activity.

This would enable the Commission to obtain information, including where necessary customer information, to assist trusted regulatory counterparts in investigating wrongdoing. In such cases, existing safeguards will be retained and any customer information obtained would only be released if it complied with the requirements of section 24 (6A) – (6C) of the Financial Supervision Act 1988. These provisions state that customer information will only be released where:

- the disclosure must be in the public interest; and
- the other regulator is required to observe rules of confidentiality and standards of information security; and
- the other regulator has undertaken to observe any conditions imposed on the release of the information to third parties; and
- the other regulator may only use the information for the purpose of assisting that body in the exercise of functions conferred on it by or under statute; and
- the disclosure is (either itself or when taken with other material) likely to be of substantial value to the body to which it is made.

Furthermore, in considering release the following factors are taken into account:

- the seriousness of the circumstances of the case;
- whether the information could be obtained by other means;
- whether the disclosure is proportionate; and
- whether reciprocal assistance would be given.

These safeguards should ensure that legitimate customer confidentiality will not be abused and may allow for an easier and less cumbersome avenue for the pursuit of investigations than at present thus enhancing the Island's reputation as a trusted and transparent jurisdiction in which to do business. The avenues for cooperation in serious criminal matters etc would continue to be controlled through the auspices of the Attorney General.

Question H:

Do you have any comments to make about whether the Commission should have the ability to assist other regulators in investigating wrong-doing in their jurisdiction?

6.6 Failure of a licenceholder and/or revocation of a licence

There is a lack of consistency in the principal Acts in relation to the Commission's power to apply to the Court to appoint a "receiver liquidator" to wind-up a licenceholder's business in an orderly manner.

This also applies in respect of the Commission's power to appoint a reporting accountant (or some other person) to report on the affairs or any particular aspect of the affairs of a licenceholder, where the Commission has concerns or requires a report by an expert.

It is proposed to extend these provisions to cover all regulated sectors and at the same time to review the adequacy and appropriateness of powers to intervene to protect the customers of a licenceholder where this becomes necessary. (See 6.7 below.)

Question I:

Do you agree that the Commission should have the same powers across all sectors in respect of being able to require a report on the affairs of a licenceholder (reporting accountant or other person) and to apply to the Court for the appointment of a "receiver liquidator"?

6.7 *Interim measures to protect customers*

The appointment of a receiver liquidator generally results in the business being wound up and may not therefore, in all cases, be the most appropriate measure to protect the interests of a licenceholder's customers. An interim measure may be for the Commission to apply to the Court in particular specified circumstances (set out in Regulations) to appoint a "receiver manager" who may manage and take control of the business through its difficulties (without winding it up) so that the interests of the licenceholder's customers can be protected.

This may apply in circumstances where issues of competence or integrity arise, for example, where there are insufficient qualified and experienced individuals to handle the affairs of customers. We are aware that the Jersey FSC has found it necessary and expedient to appoint such a receiver manager on more than one occasion to protect the interests of its customers.

At this stage we are seeking views on whether you think it appropriate to include in the Financial Services Bill an interim measure between a reporting accountant investigating and reporting back to the Commission on some aspect of a licenceholder's business, and the appointment of a receiver liquidator to wind up that business. The interim measure would be the option for the Commission to put a receiver manager in place to oversee the business in cases where the business might otherwise lose its licence or fail.

The circumstances in which the Commission may apply for the appointment of a receiver manager would be prescribed (i.e. set out in subordinate legislation).

Question J:

Do you think the Commission should investigate further the possible inclusion of the Commission having discretion (i.e. "may" not "shall") to appoint a "receiver manager", if the circumstances require, in relation to a licenceholder's business?

6.8 *Enforcement action: Offences/penalties*

The current definition of "enforcement action" is circular and potentially confusing. Consideration will be given to indicating the level of enforcement action that will apply in particular circumstances. For example, it may be more appropriate to state the next level of enforcement action following the issue of a recommendation as issuing a direction and failure to comply with a direction may in turn incur a civil penalty (fine).

Other disciplinary powers require refinement, for example, the power for the Commission to declare an individual “not fit and proper” to act as a controller or in a key management role within a licenceholder’s business may, in some instances, be a sledgehammer to crack a nut. It may be more proportionate, in the circumstances, to have an additional power to issue a formal warning.

This will involve a revision to the definition but no change of policy. The revised drafting will be subject to consultation when the Bill is circulated in due course.

The principal Acts are not consistent in respect of the circumstances in which non-compliance with an equivalent provision results in enforcement action or is an offence which attracts a penalty fixed by the Court. Furthermore, the prescribed penalties are not the same across all regulated sectors. The differences may, however, be justifiable.

The Attorney General’s Chambers advises on the appropriate level of penalties and the Bill will provide the opportunity to review the proportionality, fairness and consistency of the penalties relevant to each regulated sector.

Question K:

- **Do you agree that the definition of “enforcement action” could be improved, on the basis that this is not a change of policy and you will have the opportunity to comment on the re-wording when the draft Bill is circulated?**
- **Should the Commission have discretion to issue a formal warning as a preliminary to declaring an individual to be “not fit and proper”?**

Sector-specific amendments

6.9 Collective Investment Schemes

The following issues relating to collective investment schemes will concurrently with this consultation be discussed in detail with the Fund Management Association, which is already aware of the need for review:

- (a) The adequacy of the regulation-making powers in respect of schemes (Section 6 of the Financial Supervision Act 1988).
- (b) Review of section 11 of the Act with particular reference to exemptions.
- (c) The proportionality of current penalties and sanctions in respect of contraventions of individual regulations.
- (d) The appropriateness of interpretation and definitions under sections 30 and 31 of the Act in a modern context.

6.10 Powers of the Office of Fair Trading in relation to the Ombudsman Scheme

Conciliation in disputes over financial services, investigation and adjudication over financial services and supplemental services (the Ombudsman Scheme etc) is within the power of the Office of Fair Trading and in the light of their experience, they will be asked if these issues require any amendment.

SECTION 7

7. SUMMARY OF QUESTIONS

To assist the Commission in developing the regime we are seeking your views on the following questions. We would welcome any further details that you wish to provide in support of your answers wherever relevant. (Please click [here](#) for an electronic submission of this questionnaire.)

Question A – Section 3.2.2

Are there any processes which you feel result in unnecessary “red tape” in the current regulatory framework?

Question B – Section 5.1

Do you feel that the objectives, functions and guiding principles outlined would assist you in understanding the broad boundaries under which the Commission should operate in the future? We would welcome any comments that you have on this proposal.

Question C – Section 5.4

Do you feel that the accountability measures outlined are sufficient to ensure that the Commission is publicly accountable in the exercise of its powers? We would welcome any comments that you have on these proposals.

Question D – Section 6.1

Do you agree that it is more appropriate to define the regulated activities in a Regulated Activities Order, which would allow for more detail and also facilitate the making of adjustments to keep up with developments in the finance sector?

Question E – Section 6.2

- **Do you agree that it is more appropriate to define exemptions in Exemption Regulations, which would allow for more detail and also facilitate the making of adjustments to keep up with developments in the finance sector?**
- **If you do not agree that the exemption for “recognised persons” under s.4 of the Investment Business Act 1991 should be removed, please give your reasons.**

Question F – Section 6.3

Do you agree that, in respect of the individuals who are required to meet the Commission’s “fit and proper” test, it will enhance clarity if the Bill –

- **standardises the list of appointments/roles across all regulated sectors,**
- **extends to individuals who have significant powers or responsibilities in respect of the regulated activities undertaken by that business, and**
- **specifies those responsible for particular functions relevant to that regulated sector?**

Question G – Section 6.4

Would you prefer –

- a more flexible regulatory framework which can only be achieved if the Commission has more flexible code-making powers; or
- a more prescriptive regulatory framework, which provides greater certainty?

Question H – Section 6.5

Do you have any comments to make about whether the Commission should have the ability to assist other regulators in investigating wrong-doing in their jurisdiction?

Question I – Section 6.6

Do you agree that the Commission should have the same powers across all sectors in respect of being able to require a report on the affairs of a licenceholder (reporting accountant or other person) and to apply to the Court for the appointment of a “receiver liquidator”?

Question J – Section 6.7

Do you think the Commission should investigate further the possible inclusion of the Commission having discretion (i.e. “may” not “shall”) to appoint a “receiver manager”, if the circumstances require, in relation to a licenceholder’s business?

Question K – Section 6.8

- Do you agree that the definition of “enforcement action” could be improved, on the basis that this is not a change of policy and you will have the opportunity to comment on the re-wording when the draft Bill is circulated?
- Should the Commission have discretion to issue a formal warning as a preliminary to declaring an individual to be “not fit and proper”?

Question L

Please provide any other comments that you may have in relation to the proposals for the Review and the Consolidation of the Commission’s financial services regulatory legislation.

MATRICES OF PRINCIPAL "REGULATORY" ACTS

- A1 Financial Supervision Act 1988**
- A2 Investment Business Act 1991**
- A3 Banking Act 1998**
- A4 Corporate Service Providers Act 2000**

Appendix A1

PROPOSED CHANGES TO THE FINANCIAL SUPERVISION ACT 1988			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
Part 1	Collective Investment Schemes		
	<i>Promotion of Schemes</i>		
1	Restrictions on promotion	✓	
	<i>Authorised Schemes</i>		
2	Applications for authorisation	✓	
3	Authorisation orders	✓	
4	Revocation of authorisation	✓	
5	Representation against revocation	✓	
5A	Review of Commission decisions	✓	
6	Constitution and management		The adequacy of the regulation making powers to be reviewed
7	Alteration of schemes and changes of manager or trustee	✓	
8	Restrictions on activities	✓	
9	Avoidance of exclusion clauses	✓	
10	Publication of scheme particulars	✓	
	<i>Other schemes connected with Island</i>		
11	International Schemes		A review of the operation of s.11 will be undertaken in conjunction with the Fund Management Association
	<i>Overseas Schemes</i>		
12	Schemes authorised in designated countries	✓	
13	Other overseas schemes	✓	
14	Revocation of recognition	✓	
15	Facilities and information in the Island	✓	
	<i>Powers of intervention in relation to schemes</i>		
16	Directions	To be considered in line with s.11 review	

Appendix A1

PROPOSED CHANGES TO THE FINANCIAL SUPERVISION ACT 1988			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
17	Notice of directions	To be considered in line with s.11 review	
18	Application to the court	To be considered in line with s.11 review	
19	Investigations	To be considered in line with s.11 review	
20	Contraventions		Full review to ensure that offences are proportionate to the contravention.
Part 2	Miscellaneous and Supplementary		
21	Compensation schemes	✓	
21A	Conciliation in disputes over financial services	Refer to the OFT to see if amendment is sought.	
21B	Investigation and adjudication in disputes over financial services	Refer to the OFT to see if amendment is sought.	
21C	Investigation and adjudication: supplemental service	Refer to the OFT to see if amendment is sought.	
	<i>Information etc</i>		
22	Publication of information and advice	✓	
23	Restrictions on disclosure of information	✓	
24	Exceptions from restrictions on disclosure	✓	
24A	Public registers	✓	
	<i>Offences</i>		
25	False and misleading statements	✓	
26	Offences	✓	
	<i>Public Documents</i>		
27	Regulations and orders		The adequacy of the regulation making powers to be reviewed
	<i>Banking and investment businesses</i>		
28	Amendments		
	<i>Supplementary</i>		
29	Financial provisions	✓	

Appendix A1

PROPOSED CHANGES TO THE FINANCIAL SUPERVISION ACT 1988			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
30	Collective investment schemes: interpretation		Appropriateness of definitions in modern context to be reviewed with Industry.
31	Interpretation		Appropriateness of definitions in modern context to be reviewed with Industry.
32	Miscellaneous and consequential amendments		
33	Repeals		
34	Short title, commencement and transitional		
33	Repeals		
34	Short title, commencement and transitional		

Appendix A2

PROPOSED CHANGES TO THE INVESTMENT BUSINESS ACT 1991			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
	<i>Investment Business</i>		
1	Meaning of investment business	Investment business to be defined in Regulated Activities Order (replacing Investment Business Order with some minor changes to current definitions).	
	<i>Recognised and Permitted Persons</i>		
2	Offence to carry on investment business without a licence	✓	
3	Application for, and grant of, an investment business licence	✓	
	<i>Recognised and permitted persons</i>		
4	Recognised persons	"recognised persons" exemption to be removed.	
5	Register of permitted persons	✓	
	<i>Regulation of Investment Business</i>		
6	Regulatory codes	Code-making powers to be less prescriptive to allow for a more flexible regulatory approach. Also, definition of "enforcement action" to be clarified.	
6A	Civil penalties	✓	
7	Client money	✓	
8	Inspection and investigation	See proposed changes in paragraph 5.2.5 of consultative paper.	
8A	Power of Commission to require information	✓	
	<i>Supervisory powers and remedies</i>		
9	Recommendations and directions to permitted persons	✓	
9A	Requests for information	See proposed changes in paragraph 5.2.5 of consultative paper.	

Appendix A2

PROPOSED CHANGES TO THE INVESTMENT BUSINESS ACT 1991			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
10	Directors, controllers etc	<p>This requires that individuals whose particular role in relation to a licenceholder are fit and proper. Although the appointments specified and acting as a controller (see s.10) may cover individuals who are "key persons", specifying particular appointments may have limitations. It is therefore proposed to extend the named roles / functions to anyone who has significant powers or responsibilities in relation to the regulated activities (as in the Corporate Service Providers Act 2000).</p> <p>Introduce a new intermediate power to formally warn a person who is required to be fit and proper but whose actions are questionable. This would be appropriate in cases where there is insufficient evidence to make a "not fit and proper direction" but a formal sanction is warranted.</p>	
11	Vesting of assets in trustees	See below re "receiver manager".	
12	Public statements	✓	
13	Injunctions and restitution orders	✓	
14	Actions for damages	✓	
15	Review of Commission decisions	✓	
15A	Indemnity for designated bodies	✓	
15B	Matters to be communicated to the Commission by auditors	✓	
16	Indemnity for auditors	✓	
17	Mutual assistance agreements	✓	
17A	Misleading statements	✓	
17B	Misleading practices	✓	
18	Fees and expenses	✓	
19	Offences	Attorney General's Chambers to advise on proportionality of penalties and standardisation, if appropriate, across all regulated sectors.	
20	Power of the Commission to make regulations	✓	

Appendix A2

PROPOSED CHANGES TO THE INVESTMENT BUSINESS ACT 1991			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
21	Tynwald procedure: orders and regulations	✓	
22	Interpretation	✓	
22A	Gaming contracts	✓	
23	Amendments to Banking Act 1975		
24	Minor and consequential amendments and repeals		
25	Short title and commencement		
Add	Reporting accountants	Extend FSC's power to appoint a reporting accountant to investment business licenceholders to mirror s.21 Banking Act 1998 and s.25 Corporate Service Providers Act 2000.	
Add	Power to appoint a "receiver liquidator"	Extend FSC's power to petition Court appoint a receiver to investment business licenceholders to mirror s.16 Corporate Service Providers Act 2000. (See paragraph 5.2.6 of the consultative paper.)	
Add	Power to appoint a "receiver manager"	See paragraph 5.2.7 of the consultative paper.	

Appendix A3

PROPOSED CHANGES TO THE BANKING ACT 1998			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
	<i>Banking business</i>		
1	Banking business	Definition of banking to be moved to subordinate legislation (Regulated Activities Order).	Definition of banking to be updated to cover full range of banking activities now undertaken by Banks.
	<i>Restrictions on unlicensed banking business</i>		
2	Offence to carry on banking business without a banking licence	✓	
3	Managers of bank businesses	✓	
	<i>Banking business licences</i>		
4	Application for and other matters relating to a banking licence	✓	
5	Criteria for grant of banking licences	✓	
6	Grant and refusal of licences	✓	
7	Revocation and alteration of banking licences	✓	
8	Register of licences	✓	
	<i>Banking names</i>		
9	Restriction on the use of the word "bank"	✓	
	<i>Regulation of banking business</i>		
10	Regulatory codes	Code-making powers to be less prescriptive to allow for a more flexible regulatory approach. Also, definition of "enforcement action" to be clarified.	
	<i>Supervisory powers etc</i>		
11	Recommendations and directions to banking institutions	Definition of "enforcement action" to be clarified.	
12	Requests for information	In respect of removing restrictions on exchange of customer information with other regulators, see proposed changes in paragraph 5.2.5 of consultative paper.	
13	Inspection and investigation	Same comment as re section 12 applies here also.	
14	Power of Commission to require information	✓	
15	Deemster's search warrant	✓	

PROPOSED CHANGES TO THE BANKING ACT 1998			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
16	Directors, controllers etc	<p>This requires that individuals whose particular role in relation to a licenceholder are fit and proper. Although the appointments specified and acting as a controller (see s.16) may cover individuals who are "key persons", specifying particular appointments may have limitations. It is therefore proposed to extend the named roles / functions to anyone who has significant powers or responsibilities in relation to the regulated activities (as in the Corporate Service Providers Act 2000).</p> <p>Introduce a new intermediate power to formally warn a person who is required to be fit and proper but whose actions are questionable. This would be appropriate in cases where there is insufficient evidence to make a "not fit and proper direction" but a formal sanction is warranted.</p>	
17	Public statements	✓	
18	Unauthorised acceptance of deposits	✓	
19	Injunctions	✓	
19A	Civil penalties	✓	
	<i>Auditors and reporting accountants</i>		
20	Matters to be communicated to the Commission by Auditors and reporting accountants	✓	
21	Reporting accountants	✓	
22	Indemnity for auditors and reporting accountants	✓	
	<i>Compensation</i>		
23	Compensation schemes	✓	
	<i>Rights to reviews</i>		
24	Review of Commission decisions	✓	
	<i>Offences</i>		
25	Fraudulent inducement to make a deposit	✓	
26	Prejudicing investigations	✓	
27	False statement, etc	✓	
28	Offences by body corporate	✓	

Appendix A3

PROPOSED CHANGES TO THE BANKING ACT 1998			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
29	Penalties etc	Attorney General's Chambers to advise on proportionality of penalties and standardisation, if appropriate, across all regulated sectors.	
	<i>Miscellaneous and general</i>		
30	Treasury directions	Although power for Treasury to direct FSC has not and is unlikely to be used, IMF Review recommended its removal to ensure FSC can operate independent of political influence. Statutory accountability measures to be introduced to balance independence. (See paragraph 5.1.2 of the consultative paper.)	
31	Public documents	✓	
32	Definition of "related company"	✓	
33	Interpretation: general	✓	
34	Repeal of s.12 of 1995 c.10		
35	Amendments and repeals		
36	Short title and commencement Statutory indemnity is in IBA see s.15A(2) definition of "specified enactment".		
Add	Power to appoint a "receiver manager"	See paragraph 5.2.7 of the consultative paper.	

Appendix A4

PROPOSED CHANGES TO THE CORPORATE SERVICE PROVIDERS ACT 2000			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
Part 1	Fiduciaries		
1	Fiduciaries and regulated activities	Regulated activities (Sch 1) to be moved to subordinate legislation (Regulated Activities Order)	
Part 2	Licensing of fiduciaries		
2	Offence to act, etc as a fiduciary without licence	Exemptions (Sch 2) to be moved to subordinate legislation (Exemption Regulations)	
2A	Restriction on the use of the word "trust", "trustee", etc	✓	
3	Application for, and issue of, a fiduciary licence	✓	
4	Revocation and suspension of licence	✓	
5	Register of fiduciaries	✓	
Part 3	Regulation of fiduciaries		
6	Regulatory codes	Code-making powers to be less prescriptive to allow for a more flexible regulatory approach.	
7	Recommendations and directions to fiduciaries	Definition of "enforcement action" to be clarified.	
8	Civil penalties	✓	
9	Directors, controllers, etc	Introduce a new intermediate power to formally warn a person who is required to be fit and proper but whose actions are questionable. This would be appropriate in cases where there is insufficient evidence to make a "not fit and proper direction" but a formal sanction is warranted.	
10	Inspection and investigation	In respect of removing restrictions on exchange of customer information with other regulators, see proposed changes in paragraph 5.2.5 of consultative paper.	
11	Requests for information	Ditto - re customer information. In addition, definition of "enforcement action" to be clarified.	
12	Power of Commission to require information	✓	
13	Deemster's search warrant	✓	
14	Public statements	✓	
15	Injunctions	✓	
16	Appointment of receiver and manager	✓	
Part 4	General and supplementary		

Appendix A4

PROPOSED CHANGES TO THE CORPORATE SERVICE PROVIDERS ACT 2000			
EXISTING ACT		PROPOSAL	
Section	Description	No material effect on licenceholders	More significant change proposed
	<i>Miscellaneous</i>		
17	Application in doubtful cases	Specific to fiduciary regulated activities and exemptions. May need to move to Exemption Regulations together with definition of relevant exemption.	
18	Review of Commission decisions	✓	
19	Statutory indemnity	✓	
	<i>Offences</i>		
20	False statements, etc	✓	
21	Offences	Attorney General's Chambers to advise on proportionality of penalties and standardisation across all licensed sector, if appropriate.	
	<i>Public Documents</i>		
22	Regulations	✓	
23	Tynwald procedure: regulations	✓	
	<i>Supplementary</i>		
24	Obligation for auditors to report to Commission	Duty to report breaches of the Act, a regulatory code or licence condition or failure to comply with a direction to be qualified as "material breaches". This follows precedent set by Banking Act 1998 and Investment Business Act 1991.	
25	Appointment of reporting accountants	✓	
26	Fees	✓	
27	Interpretation	✓	
28	Amendment of enactments		
29	Short title and commencement		
Sch 1	Activities which are regulated activities	To be moved to Regulated Activities Order	
Sch 2	Exemptions from Section 2(1) and (2)	To be moved to Exemption Regulations	
Sch 3	Amendment of enactments		
Add	Power to appoint a "receiver manager"	See paragraph 5.2.7 of the consultative paper.	