The theme of the photographs in this report is based around the Manx Triskelion. This pictorially demonstrates diversity, history (clockwise and anti-clockwise) and the Manx nationality.
Mission statement

To protect the public interest by providing effective regulation and supervision within the Island’s financial services sector; to support a competitive environment in which quality products and services are promoted for the economic benefit of the Island, and to foster good working relationships within the business community.

25 YEARS

of the Financial Supervision Commission
The Commissioners

Top row:
Rosemary Penn (Chairman) MBE, John Aspden (Chief Executive)

Middle row:
John Cashen OBE, Tim Cullen, Bryan Stott

Bottom row:
Geoff Karran, Alan Smith
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I am delighted to present this Annual Report of the Financial Supervision Commission for the year 2007/08. It has been a busy and successful year for the Commission. This Report gives a full account of our work and I hope that you will find it interesting.

In July 2008 we reach a very important milestone. The Commission will celebrate its 25th Anniversary. To mark the occasion we have included a special chapter in the Report outlining the history of the Commission and some of the important events which have occurred in its lifetime so far. I would like to thank Jim Noakes who was the Commission’s first Chief Executive and who, with his Board colleagues, set the tone for the organisation which we now have today, for substantially contributing to this historical piece.

The fact that the Commission was established as a composite regulator so long ago, and well before many of the newer regulatory bodies since established in many larger jurisdictions, shows how far sighted the Island was in planning the oversight of the finance sector.

The second half of the period under review saw exceptional turbulence in global financial markets, especially in terms of illiquidity in the banking system and a lack of confidence arising from a shortage of credit. Turbulence of this nature has not been seen before in such severity and it has caused regulators world-wide to re-examine many of their priorities. The speed with which contagion moved cross-border certainly gave a new dimension to the concept of global markets.

The Island is for the most part a host regulator. It provides important services in particular to the London market, in terms of deposit funding, asset and fund management, and wealth management together with trust and corporate services. Life and captive insurance, which is regulated by the Insurance & Pensions Authority, is also an important activity. The international dimension to our finance sector can make us vulnerable to external shocks. It is important that we are prepared to manage them in conjunction with the parent regulators and authorities with whom we maintain close contact.

It is a fact that in the minds of regulators generally, liquidity adequacy has often taken second place to capital adequacy when it comes to formal regulatory guidance. Events have now caused us all to look carefully at our different stages of preparedness for changing market conditions, including contingency planning. They have also been a salutary reminder of how important it is to maintain quality standards in terms of market entry and financial soundness.

Against this background it is especially encouraging to see that customer deposits have continued to grow by 8.5%, as have funds under management and administration. A key strength of the Island is the broadly based nature of its finance sector, and in uncertain times such diversity becomes an important asset.
As a regulatory body the Commission assumes many different risks, which need to be properly identified, assessed and mitigated. The Board’s own Risk & Internal Control Committee has proved an effective resource for carrying out this work and an account of its work appears in the Report.

The legislative programme has been heavy during the year and I am especially grateful to industry practitioners who have provided much of their time and experience to ensure that the various regulatory initiatives being proposed are workable and can achieve the intended objectives. The Financial Services Bill has been a major project, but other legislation in the funds, companies and AML CFT arenas has been equally intensive.

Much time and work during the year was devoted to supporting the initiatives of the Funds Review Group, and the new fund products (and licensing regime) which the industry proposed for taking development of the funds sector to a more advanced level. From the Commission’s perspective, the fact that the new Specialist and Qualifying funds are aimed more towards institutional investors with appropriate safeguards takes away the uncertainty previously associated with Experienced Investor Funds. The latter have now been withdrawn as a new fund category.

The Island is committed to observing the principles of the FATF Recommendations on AML CFT. The Criminal Justice (Money Laundering) Code 2007 was an important revision, on which the Commission has subsequently elaborated in its Rulebook and Handbook. The Island has established a very clear position for itself in making sure that it only attracts business which meets appropriate standards of due diligence. Business which does not meet this threshold is declined.

An important part of the fight against crime is to ensure that there exist appropriate gateways for the authorities to co-operate with enquiries being made often overseas. The Commission, as a signatory to the IOSCO MMOU, is very aware of the need to provide full and timely assistance, and it demonstrated a strong record of co-operation during the period.

It is very pleasing to report that the Island’s corporate sector has continued to grow, with new incorporations of all Manx companies up 26% on the previous period. Incorporations of 2006 Act companies now comprise 50% of all new incorporations, with appropriate additional safeguards and disclosures built in where the companies are used in a regulated context.

The IMF will be returning to the Island later in 2008 to undertake a review of the Island’s financial sector regulation and supervision, with a major focus also on AML CFT measures.

At the time of the last assessment in 2003 the Island received a very favourable report. Undoubtedly this was a reflection not just of the regulatory framework but also of how the finance sector understands and accepts the need for a credible and workable regulatory regime. A number of international standards and methodologies have changed since the IMF’s last visit, so there will be new benchmarks against which we will be assessed. The IMF assessment process is constructive and provides an important measure of consistency in gauging the effectiveness of a regulatory system alongside its peers. It is also an important discipline for the Commission’s effectiveness to be reviewed independently, just as the Commission in turn undertakes reviews of its own licenceholders.

Two new Board members - Geoff Karran and Alan Smith - were appointed in July 2007, adding further to the expertise and commercial acumen of the Board in the professional and regulated sectors. An appreciation of the work undertaken by Tony Barber and John Webster, who decided to step down from the Board, appeared in my report for last year.

With a demanding agenda of work, it would not have been possible to meet our objectives without the advice and strong support of the Board. For this I am most grateful. Through its staff the Commission has aimed to improve delivery of its objectives and most staff, I believe, regard their work as both rewarding and very worthwhile. This ethos has encouraged them to reach new heights. Professionalism and helpfulness are two adjectives frequently used in licenceholder feedback returns submitted to me, and these speak for themselves. I would like to thank everyone for their contribution to the Commission’s work.

John R Aspden
Chief Executive and Commissioner
The Financial Supervision Commission was created by Tynwald in 1983. This was to establish a separate regulatory body to oversee a developing financial services sector and reinforce the Island’s reputation as a credible jurisdiction.

The Commission’s first task was to address those “banks” which were not financially sound or had adopted imprudent or incestuous practices. This required among other things the addition of winding up powers to the Banking Act 1975. At the same time a moratorium was imposed on the issue of new banking licences to enable the Commission to devise and implement a new licensing policy, together with licence conditions and reporting requirements.

To provide the maximum economic benefits to the Island and to ensure clear accountability the Commission chose a “real presence” policy. Hence no Representative Offices, brass plate operations, or so-called “cubicle banks” were permitted, though these restrictions were later relaxed to permit “third party fund administrators” and “managed bank” operations but only where clear responsibility and accountability could be demonstrated locally. The recent “sub-prime” crisis illustrates clearly what can happen when the link between risk and responsibility is weak or broken.

Rebuilding the Island’s reputation meant attracting financial institutions of established standing and repute; offering financial legislation which met their needs; establishing and maintaining the confidence of foreign regulatory authorities; and deterring abuse of the Island’s financial facilities by criminals.

One of the first things the Commission did was to set out to attract the largest UK building societies to the Island. Recognising the significance of the proposed liberalisation of UK building society legislation, five out of the top ten societies set up operations on the Island.

The most important event affecting the Island’s financial services industry was, of course, Big Bang in the UK and the far-reaching consequences arising from the Financial Services Act 1986. The first task was to provide appropriate legislation for the regulation of collective investment schemes so that some Isle of Man schemes could continue to be marketed in the UK. The result was the Financial Supervision Act 1988 and later that year the Island received “Designated Territory” status from the UK, which it has since maintained following reviews by HM Treasury. Over the years similar arrangements have been entered into by other financial centres.

The Financial Supervision Act provided the seed-bed for the development of schemes and other collective investment products to meet the needs of wealth managers and retail investment businesses, whereas investment business is regulated in the Isle of Man under the Investment Business Act 1991. This Act was specifically crafted by the Commission and its lawyers so that it was relevant to the needs and capacities of the Island’s investment business sector but at the same time fully compliant with international standards of regulation. It was subsequently copied in many other jurisdictions around the world.

Earning and maintaining the respect and confidence of other regulatory bodies has always been a high priority for the Commission, not only for the sake of the Island’s reputation with financial institutions and their customers - vital though that is - but also to preserve market access for the Island’s financial businesses and to reduce the risk of abuse by criminals, whether fraudsters or money launderers.

The Isle of Man was an early member of the Offshore Group of Banking Supervisors under the auspices of the Basel Committee. When IOSCO offered observer (1989) and then associate (1991) status, the Commission applied and was accepted, giving it access to investment business regulators worldwide. Closer to home the Commission over the years entered into Memoranda of Understanding and Mutual Assistance Arrangements with UK regulatory bodies and others, including the London Stock Exchange, the UK Law Society, and the Institute of Chartered Accountants in England & Wales.
Any review of the Commission’s work in the 1980s and 1990s cannot overlook the subject of Money Laundering. From its inception, the Commission had been concerned about the damage to the Island’s reputation which could arise from assisting criminals to launder the proceeds of crime and the vulnerability of the finance sector to abuse of this kind. Indeed, in 1985 the Commission issued a warning to the Island’s banks and coined the phrase “Know Your Customer”. By 1989, when the Financial Action Task Force was established by the G7 group of countries, the Island was ahead of the curve and was recognised by the FATF as a co-operative jurisdiction. A subsequent inspection by the FATF validated the Island’s status. At no time have Island financial businesses been hampered by concerns about the Island’s reputation in this area.

While the Commission’s early priorities were to lay the foundations for a sound and relevant system of regulation, to inaugurate appropriate legislation, and to establish relationships of trust with foreign regulators, it was always aware that protecting the Island’s reputation was also about the ability to enforce the Island’s legislation against those who would not co-operate or deliberately set out to abuse it. So in 1991 the Commission began to develop a small but effective enforcement capability, which actively implemented the enforcement provisions of the legislation against those who contravened them. Its work did much to raise the Commission’s profile among international regulators and increased the acceptance of the Isle of Man as a well-regulated jurisdiction to the benefit of Isle of Man financial businesses.

The closure of a local bank in 1982 (and the collapse of Barings in 1985) had major implications for the Island as well as for banking supervision. The failure of BCCI triggered the Island’s Deposit Compensation Scheme, which paid out £22 million in compensation in respect of eligible deposits, following levies collected from participating banks over a period of four years. The participating banks received back their original contributions (levies) following dividends received into the DCS arising from the liquidation of BCCI. For the Commission it meant a new Banking Bill to reflect the necessary changes as well as the start of a more pro-active approach to supervision. The Commission had always sought through its “standalone” policy of supervision to protect, as far as it was able, Island banks from cross-infection of problems arising elsewhere and this helped to shelter the Island from the worst effects of the crises in the 1990s.

As the 1990s drew to a close, more rigorous enforcement action was accompanied for the first time by active consumer information. The Commission began actively to use its powers to issue public warnings about investment business activities. Although the Commission is a regulatory body and not a consumer protection agency, it issued a booklet entitled “Protecting Yourself from Fraud and Mis-selling” as well as Regulatory Guides for the benefit of licenceholders and their advisers. The Commission’s successful track record had become widely recognised and the stage was set for a substantial expansion of its work and responsibilities.

At the beginning of 1998 began an era of increased scrutiny of financial regulation generally, when the Home Secretary of the UK Government commissioned a review of financial regulation in the Crown Dependencies. The ensuing report, published later that year, commented that the three islands had been very successful in recent decades in developing their international financial centres. The report also recognised that the islands had “developed reputations for stability, integrity, professionalism, competence and good regulation”. A number of recommendations for continued improvement were made.

In the same year there was a change of Chief Executive. Jim Noakes, who had held the position since the Commission was first established in 1983, retired and his place was taken by John Aspden.

Also in 1998 a new Anti-Money Laundering Code came into operation. This formed the platform for a substantially upgraded AML regime (later to include the countering of the financing of terrorism), which also involved the introduction of comprehensive guidance notes to assist the industry in compliance.

The Euro was introduced as the new European currency in 1999. This was a major event for currency markets, although it had little effect in the Island. At the time the Manx Government stated that it would consider introducing the Euro in the Island if and when the UK also converted the pound sterling. This has not yet occurred.

An FATF Mutual Evaluation was conducted of the Island’s defences against money-laundering. Its positive report concluded that the Island was a co-operative jurisdiction with measures in place which are close to full adherence with FATF recommendations. A later (2001), onsite review by the FATF also came to the same conclusion. These were important milestones as they confirmed the Island’s standing as a responsible
and co-operative jurisdiction in the fight against all forms of financial crime.

The Experienced Investor Fund was introduced as a new fund category in the same year. This was the first step in revitalising the Island’s funds sector and has since attracted significant new funds under management and administration.

At the end of 1999 financial markets were preoccupied with the new millennium. All businesses faced uncertainty as to how their computer systems would cope with the transition to the year 2000, and what impact this might have. A significant amount of preparation and contingency planning was conducted, and the occasion passed off smoothly.

Meanwhile the Financial Stability Forum considered the effect which offshore centres generally could have on global financial stability and in April 2000 issued the report of a working group on this subject. It canvassed opinion among major countries on the strength of regulatory practice in the different centres, and it was very pleasing to note that the Isle of Man was placed in the top group of centres reviewed. Shortly afterwards responsibility for assessing the compliance of centres such as the Island with international standards moved to the IMF.

In April 2000 the Commission formally assumed responsibility for Companies Registry. An immediate challenge was the fact that company records were all maintained as hard copies with no contingency backup in the event of loss. A major exercise then commenced to scan 40,000 company files which comprised over one million documents with nearly six million pages going back to the first company incorporated on the Island in 1865. The resulting database, which included all historical documents, became the backbone of the new public view system which was formally introduced when the Commission completed its move (with Companies Registry) to new premises in March 2002. The ability to search and download company documents electronically was widely welcomed by the industry and gave the Island a strong competitive advantage in the sector.

During this time much work was also being undertaken in preparing for a new regime to regulate corporate service providers. This was not an easy period as the corporate services sector had been operating for many years without regulation (other than in an anti-money laundering context), and it was naturally apprehensive as to what the new regime would mean. However, after extensive consultation the Corporate Services Act 2000 came into operation and 140 businesses applied for a licence. The regime, embracing on-site visits from the outset, has subsequently developed into an important means of maintaining standards in an activity which carries a potential for high reputational risk. At the same time the Commission began to make more use of the power under section 26 of the Companies Act 1992 to petition the High Court for the disqualification of directors.

A key part of the Commission’s requirement for licenceholders to be run and managed by persons who are deemed to be “fit and proper”, contains a test of competency. With this in mind, in 2001 the Commission issued a statement of Good Practice on Training and Development.

In 2001 the FATF issued eight special recommendations (later increased to nine) in connection with countering the financing of terrorism. At the same time the Basel Committee issued a paper on Customer Due Diligence for Banks, and both these initiatives resulted in revisions to the Commission’s anti-money laundering and countering the financing of terrorism guidance notes.

At this time the Commission was strengthening its resources. In addition to adding staff, the Commission seconded a senior manager to the FSA in London for a one year period of training and experience.

The Commission was conscious that more steps needed to be taken to strengthen communication with its stakeholders, and a new system was introduced for receiving feedback from licenceholders on the visits which it was making. Companies Registry also introduced an ongoing series of practice notes, to explain to the public the different requirements applying to the incorporation and administration of companies. Later on, the cost attached to making the Commission’s handbook publicly available was removed.

Following the introduction of the CSP (and later TSP) licensing regime, the Commission quickly commenced
on-site visits to corporate service providers. These were and still are most instructive, not only in providing an important means of reviewing AML CFT and other compliance but also in allowing the Commission better to understand and communicate with its newly regulated sector.

In 2002/03 the IMF conducted an assessment of the Island’s regulatory arrangements. The IMF’s Report confirmed that the Island "complies well" with international standards for the regulation and supervision of financial services. It concluded that the Isle of Man has a "high level of compliance" with international standards in such areas as banking, insurance, securities, anti-money laundering and combating the financing of terrorism. This again was a very important statement of the Island’s commitment to the principles of sound regulation.

In 2003 an internal reorganisation was conducted, mainly in Supervision, which aimed to merge expertise within existing sectoral teams to reflect the important development of consolidated supervision. As a result multi-disciplined teams now make visits to licenceholders.

In May of the same year and following a review, HM Treasury of the UK renewed the Island’s designated territory status which applies to the distribution of its authorised funds in the UK. Separately the Commission announced steps to ensure that new regulatory proposals were made subject to an appropriate cost/benefit review.

During 2004 trust service providers were preparing for the new regulatory regime applying to them. Supervision of banks further intensified, with a particular focus on market and credit risks. A survey of banks was undertaken in preparation for Basel II. An independent review of the Commission’s procedures for petitioning for the disqualification of directors led to changes in its enforcement procedures.

In August of the same year the Commission launched its new public view internet system in Companies Registry. This was a world-leading service, allowing members of the public to search the public records of Isle of Man companies and to purchase individually copy documents - all online through the Commission’s website. This has since become a vitally important service for many off-Island users of Isle of Man companies, and was commented upon very favourably in a customer satisfaction survey.

In 2005 the Commission received accreditation from Investors In People. It represented an important commitment by the Commission to its staff, especially in terms of sound management and communication practices. The Commission also commissioned an external review of its salary review process (and subsequently followed this up with a detailed market pricing assessment).

In October of the same year the Commission became a full signatory of the IOSCO MMOU, representing an important milestone in its commitment to be a responsible and co-operative regulator. A number of ongoing requests for assistance are nowadays received under the MMOU.

In 2006 a new Manx corporate vehicle was introduced, following major input from the industry. Use of this vehicle has grown in popularity and currently comprises nearly half of all new incorporations of Manx companies. They are now also used in the listing of AIM companies in London, where the Island has established a leading position as a domicile of choice.
Market Developments

International financial markets and the global economy

Over the course of 2007 there was a shift from a situation of over confidence in the financial markets to one where confidence became very low. An extended period of abundant liquidity and low interest rates worldwide, combined with a favourable economic backdrop, had encouraged many investors to underestimate the risk of traditional high-risk investments and consequently to take on additional risk. However, this benign financial environment began to turn in early 2007.

The degree of risk was especially underestimated in the sub-prime US mortgage market; hence, many asset-backed securities became grossly overpriced. The first indication that financial conditions would tighten came during the first quarter of 2007. Concerns over the credit quality in the US sub-prime mortgage markets led to an increase in investor risk aversion and there was some correction in the market’s pricing of risk. Over the summer, markets began a more fundamental reassessment of the risks following the fallout from US sub-prime mortgages. Corrections to the overvaluation in this market spilled over into equity, currency, and bond markets worldwide creating interbank liquidity difficulties and financial turbulence. This encouraged a “flight to quality” to Government bonds and an increased demand for liquidity. These events resulted in unstable financial markets and funding problems for many firms, most notably for the UK problems encountered by Northern Rock.

Although economic growth in the US was sound in the second and third quarters of 2007, the US economy began to look increasingly fragile towards the end of 2007 due to weakening credit. As the economy deteriorated, the US dollar depreciated against most major currencies, reaching a record low against the Euro at $1.4278/€. Sterling appreciated by 2.7% against the dollar by November before further depreciating, but still ending up on the year at $1.9851/£.

In line with the financial turbulence, 2007 saw the US housing market fall significantly and Europe’s housing markets slow. The recent house price slowdown in Europe is mainly due to higher interest rates. The ECB raised its key interest rate eight times in 15 months. The repo rate was raised to its current level of 4% in June 2007 from its historic low of 2% in November 2006.

In response to growing concerns over inflation throughout 2006 and into early 2007, the Bank of England tightened monetary policy, raising interest rates by 25bp in January, May and July. After pausing at 5.75%, the Bank of England lowered rates in December reflecting concerns about the impact on UK output and tightening in the supply of credit to households and businesses.

As with other financial markets, volatility in the commodity markets also increased. There were record increases in crude oil prices during the second half of 2007, with the benchmark crudes hovering just below the $100 per barrel level and eventually pushing through this level in early 2008. Industrial metals saw record growth in the first half of 2007 but increasing uncertainty over the global financial market conditions and the sustainability of demand left prices down over the year. On the other hand, precious metals, particularly gold, benefited from the flight to quality and gold nominal prices hit all time highs at the end of 2007.

Isle of Man economy

The Isle of Man has enjoyed an enviable combination of high growth, stable prices and full employment over the last decade.

Now in its twenty-fifth consecutive year of economic growth, the period since the mid-90s has seen a particularly impressive performance with real growth averaging just under 8% p.a. over the last decade. Although the rate of growth has slowed over the last few years the economy is currently estimated to be expanding at around 8% p.a. in real terms. Per capita income is now 13% higher than that of the UK and 25% higher than the EU15 average. This differential is expected to widen as growth of 6% is anticipated over the next few years.

The key sectors in generating this performance over the last two decades have been financial, professional and scientific services as well as construction. Banking generates almost one-fifth of the Island’s gross domestic product and combined with the rest of the finance industry contributes a total of 36%. One of the Government’s key objectives is to diversify its economic
base so as not to become too dependent on the finance sector. As a result there are now greater contributions being recorded in areas such as film production, e-business and the space industry.

One consequence of the economy’s performance has been an ongoing strengthening of public finances. Even after the introduction of the zero/10% rate of income tax for business (10% for deposit-taking and property development) and a maximum tax liability of £100,000 per annum on personal incomes, the Government continues to have a healthy budget surplus. Over the last five years Treasury’s receipts have climbed from £466 million in 2001/02 to £606 million in 2006/07 whilst over the same period expenditure has risen from £360 million to £528 million.

A key element of the Island’s fiscal strength is the long established and self imposed legislative requirement that Government must budget for a surplus in respect of its annual revenue spending. Its success in achieving such surpluses has been critical in obtaining AAA credit ratings from both Moody and Standard & Poor’s.

The Island’s unemployment rate has been below 1.5% of the economically active population for over ten years. Despite a tight labour market the flexible work permit system has allowed employers to recruit from off-island if no suitably qualified Isle of Man workers can be found. Consequently, despite full employment, employment costs have generally increased at a modest and manageable rate. The latest figure from the 2007 Earnings Survey shows that wages have risen 2.8% over the last 12 months.

Rising energy prices put some pressure on local costs in the last few years. The Island’s inflation rate in January 2008 stood at 4.2% (compared to 4.1% in the United Kingdom).

Despite warnings over house price falls in the UK and a slump in the US, the property market in the Island has remained healthy. The average sale value of a residential house in 2007 was over 11% higher than the previous year. By the end of the year the average house price was over £260,000. The volume of transactions was also up slightly on the previous year. Tough credit conditions may put some pressure on house prices in 2008 but the strong economic conditions are expected to prevent any significant downturn.

International financial business

The market for international financial services has so far remained remarkably buoyant amidst the turbulence in the markets generally. However it is unlikely to remain immune from wider events. For many depositors considerations of financial soundness are now greater than headline rates of interest. Weakening property markets are a function of not just tighter credit conditions but also a lack of confidence. Capital market transactions are slowing and investors are cautious, although in some cases sovereign wealth funds have stepped in to provide significant sources of new capital where losses have had to be recognised.

Economically the Island is entering this more difficult climate in a strong position. As described on page 44, corporate activity has been high. The figures on page 16 demonstrate how the banking and funds sectors have been growing. Profitability of the financial sector has also increased.

At present the outlook remains uncertain because of weaker economic conditions in important markets such as the US, the UK and more recently in the eurozone. Undoubtedly this affects the ‘wealth factor’ and therefore the extent to which funds are available for new investment.

On a positive note the Isle of Man Government has taken a proactive stance to promote new business streams. Following publication of the report of the Funds Review Group, Isle of Man Finance and the industry last Autumn undertook a major promotion of new funds products (see page 41). This is now bearing fruit with new licencees and funds under management attracted to the Island. The Government also sponsored a major review of the banking sector to examine new areas for growth. A similar review initiative was also undertaken for the captive insurance sector (this activity is supervised by the Insurance & Pensions Authority).

In September 2007 the Policy and Resources Committee of the City of London published the GFCI. This provides an indicative rating of the competitiveness of each major financial centre in the world. It enables financial centres to be ranked against each other and identifies changing priorities and concerns of financial professionals. The Isle of Man was included for the first time and was ranked 21 out of 50 centres, and took the leading offshore centre position within the index.
Market statistics

Bank Deposits

The deposit base net of local inter-bank placings totalled £65.59bn as at 31 March 2008, consisting of £43.36bn sterling deposits and £22.23bn non-sterling deposits.

Of the £65.59bn, £13.23bn relates to deposits held with overseas branches of Isle of Man incorporated banks.

Distribution of locally incorporated banks by Risk Asset Ratio

The capital adequacy of Isle of Man incorporated banks is measured on a risk-weighted basis in accordance with international standards. The higher the ratio, the greater is the level of adequacy. The statutory minimum risk asset ratio is 8% although during the transition to Basel II no bank has been allowed to operate under a ratio of 10%.

Of the 26 locally incorporated banks eight had risk asset ratios between 10% and 15%, five had risk asset ratios between 15% and 20% and nine had risk asset ratios above 20%. As regards Tier 1 ratios, nine banks had ratios above 20% and the remaining 13 were all above 11.5%. A total of four banks did not take deposits. All figures are at the end of March 2008.

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

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<td>Europe (non EU)</td>
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<td>Middle and Far East</td>
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<td>North America</td>
<td>5%</td>
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<td>Other</td>
<td>10%</td>
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<th>Source of Non-Bank Deposits</th>
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<td>United Kingdom</td>
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<td>European Union (exc. UK)</td>
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<td>Middle and Far East</td>
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<td>North America</td>
<td>4%</td>
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<td>Other</td>
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<tr>
<th>At 31 March 2008</th>
<th>At 31 March 2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Subsidiaries Branches</td>
<td></td>
</tr>
<tr>
<td>United Kingdom</td>
<td>26</td>
</tr>
<tr>
<td>Ireland</td>
<td>5</td>
</tr>
<tr>
<td>South Africa</td>
<td>3</td>
</tr>
<tr>
<td>Spain</td>
<td>1</td>
</tr>
<tr>
<td>France</td>
<td>2</td>
</tr>
<tr>
<td>Switzerland</td>
<td>2</td>
</tr>
<tr>
<td>Cayman Islands</td>
<td>1</td>
</tr>
<tr>
<td>Iceland</td>
<td>1</td>
</tr>
<tr>
<td>USA</td>
<td>1</td>
</tr>
<tr>
<td><strong>Sub total</strong></td>
<td><strong>42</strong></td>
</tr>
<tr>
<td>Isle of Man</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>44</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Assets</th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Money market assets, due from banks and building societies</td>
<td>59.0</td>
<td>51.4</td>
</tr>
<tr>
<td>Loans, advances and assets leased</td>
<td>10.7</td>
<td>9.5</td>
</tr>
<tr>
<td>Investments</td>
<td>0.2</td>
<td>0.2</td>
</tr>
<tr>
<td>Other assets</td>
<td>1.0</td>
<td>0.8</td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td><strong>70.9</strong></td>
<td><strong>61.9</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deposits due to banks and building societies</td>
<td>11.2</td>
<td>7.4</td>
</tr>
<tr>
<td>Deposits due to customers</td>
<td>54.4</td>
<td>50.1</td>
</tr>
<tr>
<td>Other deposits (held as security and interest payable) including deposits due to public sector bodies</td>
<td>1.8</td>
<td>1.7</td>
</tr>
<tr>
<td>Other liabilities</td>
<td>1.0</td>
<td>0.8</td>
</tr>
<tr>
<td>Capital and reserves</td>
<td>2.5</td>
<td>1.9</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td><strong>70.9</strong></td>
<td><strong>61.9</strong></td>
</tr>
</tbody>
</table>
Collective investment schemes

During the year to 31 March 2008, there has been an increase in the net asset value of funds under management of 21.3% ($9.5bn), to $54bn. The total number of funds has increased from 452 schemes to 464.

Expansion in the local fund industry continues to be attributed to growth in the Closed-ended and Overseas Fund sectors. The total net asset value of Closed-ended Investment Companies has grown by $2.7bn. The total net asset of Overseas Funds has grown by $5.6bn.

Sectoral fund breakdown by value as at 31 March 2008

<table>
<thead>
<tr>
<th>Category</th>
<th>Total NAV Funds under management $million</th>
</tr>
</thead>
<tbody>
<tr>
<td>Authorised Schemes</td>
<td>1,288</td>
</tr>
<tr>
<td>International Schemes</td>
<td>4,746</td>
</tr>
<tr>
<td>Professional Investor Funds</td>
<td>686</td>
</tr>
<tr>
<td>Experienced Investor Funds</td>
<td>11,960</td>
</tr>
<tr>
<td>Exempt International Funds</td>
<td>3,288</td>
</tr>
<tr>
<td>Inward Outsourcing</td>
<td>148</td>
</tr>
<tr>
<td>Specialist Funds</td>
<td>167</td>
</tr>
<tr>
<td>Qualifying Funds</td>
<td>348</td>
</tr>
<tr>
<td>Legacy Experienced Investor Funds</td>
<td>417</td>
</tr>
<tr>
<td><strong>Sub total</strong></td>
<td>23,028</td>
</tr>
<tr>
<td>Overseas Funds</td>
<td>18,726</td>
</tr>
<tr>
<td>Closed-ended Investment Companies</td>
<td>12,016</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>53,770</td>
</tr>
</tbody>
</table>
25 YEARS
The Commission is an independent Statutory Board established under the Financial Supervision Commission Order 1983. The Commission has in its previous reports described how it operates: except as described in this report, this modus operandi remained broadly in place during the period.

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

Appointments to the Board of the Commission are approved by Tynwald. At the time of a national election all Commissioners, as members of a Statutory Board, retire. However existing Commissioners remain in position until such time as a new Board is approved by Tynwald.

Organisation of the Commission

Following the elections held in November 2006, the Board of the Commission remained in place until a new Board was approved by Tynwald. This occurred later than planned, in July 2007. Mrs Rosemary Penn MBE was reappointed Chairman, and John Cashen OBE was reappointed but on this occasion as Deputy Chairman. John Aspden, Tim Cullen and Bryan Stott were also reappointed as Commissioners, together with Geoff Karran and Alan Smith who were both appointed for the first time. Tony Barber and John Webster, who had served on the Board since 1998, did not seek reappointment. A note of appreciation for the work of Mr Barber and Mr Webster appeared in the Annual Report for 2006/07.

The Board is very aware that the key to having a successful jurisdiction to regulate, lies in achieving the right balance between effective regulation and demonstrating a commercial understanding of the activities being regulated. The composition of the Board with professionals from varied disciplines goes a long way to ensuring this.

For the future, the Board has proposed that Board appointments should be made more on a rotating basis so that not everyone retires (even if being reappointed) at the same time.

Appendix D describes how the Commission functions through a structured approach to its operations. This also includes an explanation of how conflicts of interest are managed at Board level.

The full Board meets monthly. In addition a quorum of the Board meets monthly to consider licensing matters. The following meetings were held during the period:

Meetings of the Financial Supervision Commission 12
Licence Application meetings 13

Individual members of the Board attended four meetings of the Risk and Internal Control Committee (Tim Cullen, Rosemary Penn and Alan Smith), five meetings of the sub-Committee on Remuneration (John Cashen, Geoff Karran and Bryan Stott) and other ad hoc meetings to discuss particular issues affecting the Commission. In addition, each Commissioner has been assigned to take a close interest in a particular area of a Division’s work. This is so that the Board collectively deepens its understanding of how the core functions of the Commission are exercised, and can have a more informed debate about issues arising at its regular meetings.

The Board also constituted a new Committee (currently comprising Tim Cullen, Rosemary Penn and Alan Smith) to address complaints. The Commission’s policy on handling complaints is set out on its website (and the handling of complaints in 2007/08 is discussed on page 21). In short the policy provides for a review of the Chief Executive’s handling of a complaint if this is requested by a complainant. The new Committee will conduct these reviews if and when the need arises.
A range of policy, case and operational matters were discussed by the Board during its monthly meetings. The following items were covered:

- Financial services legislation consolidation project
- Companies Amendment Bill 2007
- Collective Investment Schemes Bill 2007
- Development of a regulatory regime for E-money providers and Money Service Businesses
- Implementation of Funds Review Group initiatives resulting in the introduction of the Specialist and Qualifying Funds
- Market liquidity conditions
- Memorandum of Understanding with the Treasury
- External relations
- Review and upgrade of the Commission’s website
- Strategic review of the Commission’s IT strategy
- Supervision Division’s annual supervisory visit plan
- Independence of the Commission
- Anti-money laundering Code
- Pandemic flu contingency planning
- Annual business plan
- Licenceholder feedback
- Companies Registry fees
- Review of the Depositors’ Compensation Scheme
- External review of staff remuneration
- Specific institutional issues
- Divisional periodic reports.

An important part of the Board’s oversight has been a regular monitoring of the Commission’s compliance with international standards of supervision. In the Commission’s case these are primarily the Basel Core Principles of banking supervision, the IOSCO principles and the recommendations of the FATF. The Best Practice Statement for the Supervision of Trust and Company Service Providers issued by the OGBS is also a core document.

The recommendations of the IMF in 2003 were initially the platform for this, although more recently the Board commissioned an interim and external review of regulatory and supervisory arrangements as a check on progress being made. The results have been a very useful guide on where legislative and regulatory resources need to be directed. An ongoing action plan is reviewed by the Board on a quarterly basis.

No data subject access requests were received under the Data Protection Act 2002.

Corporate governance and risk management

The Risk and Internal Control Committee of the Board, whose role is to consider and report to the full Board on the adequacy of the control environment within the Commission, met on four occasions during the year. Its work has encompassed the following:

- Consideration of the Committee’s terms of reference, and its planned programme of work
- A meeting with the Commission’s External Auditors to consider any issues arising from the audit of the Commission’s annual report and accounts for the year ending 31 March 2007, in advance of the Board’s consideration of the Audited Accounts
- Approval of the approach and the work to assess the Commission’s internal control structure
- Meetings with Heads of Divisions to discuss the risks facing each Division and the Commission’s Risk Register
- Detailed consideration of:
  - The risks to the Commission posed by market turbulence
  - As a general concept, contingency planning for licenceholder failure
  - The Commission’s internal whistle blowing policy
  - The results of an Internal Audit review of the Commission’s payroll
  - The Commission’s Risk Register, which is prepared in line with Government Policy, was reviewed and updated.

The Committee also reviewed the delegated authority arrangements to reflect changes in legislation and practice.

The Commission’s business continuity procedures were subject to testing which will continue on an ongoing basis.

Compliance with international standards was reassessed by an external consultancy as part of the Commission’s preparations for the visit of the IMF in September 2008. Any areas of non-compliance were viewed as a potential risk for the Commission, quite apart from the wider consequences for the effectiveness of regulation generally.

After each meeting the Committee reports on its findings to the full Board.
As a Statutory Board the Commission is also required to report annually on its compliance with the Government’s Code of Conduct, in the form of a Statement of Internal Control signed by the Chief Executive and submitted to the Chief Financial Officer. In preparation for this each Division of the Commission completes a corporate governance self assessment questionnaire which is discussed with the Committee. The Statement for the year to 31 March 2008 was submitted shortly after the end of the period on 30 April 2008.

External relations

The Commission regards its main external stakeholders as follows:

- Tynwald
- Licenceholders, and indirectly their clients and customers
- Government
- Other regulatory and law enforcement authorities, as well as relevant professional organisations.

Successful regulation depends on a co-operative relationship between supervisor and licenceholder. Through regular meetings with licenceholders, full consultation on legislative and other proposals (referred to mainly in Section 7, of this report), and a pragmatic approach towards the setting of supervisory requirements, the Commission has continued to put much effort into this area.

The Board meets regularly with industry. It also arranged seven lunch-time gatherings with practitioners to listen to concerns and issues which may affect regulatory strategy.

A Commissioner attends the various Treasury quarterly consultative meetings with the industry which are chaired by the Minister for the Treasury. The Board also received a presentation from the Head of Isle of Man Finance on how its future marketing plans were to be directed.

The feedback received from licenceholders from completed inspection feedback questionnaires indicates that many licenceholders feel that the supervisory process can be constructive and helpful.

Complaints against the Commission

The Commission’s policy in dealing with complaints made against the Commission is published on its website. (Complaints about individual licenceholders are referred to on page 34).

During the period two complaints were made against the Commission. One of these related to a business name, and the other related to remedial action previously undertaken by the Commission. Both complaints have been reviewed by the Board.
Corporate Business Plan

The Commission prepares a medium term corporate plan which is integrated within the wider plan of Government. The Government plan for 2008/09 was published earlier during the period.

Business Plan 2008/09

The aim of the Commission is to provide effective regulation which promotes the Island as a competitive and secure location from which to conduct financial business. The Commission’s mission statement is set out on the first page of this Report.

Below is the extract from the Government Business Plan for 2007/08 setting out the Commission’s aims, purposes, objectives and what it will seek to deliver. The Commission has set for itself the following objectives within the framework set down by Government. In developing its business plan an Away Day takes place where Board members and the Executive discuss and review current and future issues it may face.

Objective: Effective Regulation - To promote the Island as a competitive and well regulated economy.

The Commission will:

- Deliver an effective programme of on-site supervisory visits prioritised on a risk assessed basis and undertake effective desk-based supervision
- Consult and communicate with the industry on changes in international standards and develop, propose and implement changes to ensure proposals do not impact negatively on the Island’s competitive position
- Consider and make recommendations on licence applications from businesses wishing to conduct regulated business from the Island
- Streamline efficiency and effectiveness to ensure the regulatory process is as cost efficient as possible
- Continue to provide an effective service in relation to the incorporation of companies, the filing of company and related documents and the availability of a public searching facility.

Objective: Good Governance - To ensure the Commission complies with the principles of Corporate Governance.

The Commission will:

- Implement the Commission’s Governance framework enhancing accountability and transparency
- Develop the role and work of the Risk & Internal Control Committee
- In conjunction with Treasury, progress a framework through which there can be wider external input into regulatory strategy, also leading to greater accountability
- Participate in the corporate governance initiative of the Isle of Man Government and other relevant initiatives.
Objective: International reputation; Effective Regulation - To protect and enhance the Island’s international reputation.

The Commission will:
- Develop preventative strategies and techniques to deal with unlicensed activity
- Monitor the internet for frauds/intelligence and take appropriate action
- Take timely action to protect investors where activities are, or have been, conducted in breach of Commission related legislation.

Objective: International reputation - To further develop working relations with the United Kingdom and EU to ensure the Island’s interests are effectively promoted internationally.

The Commission will:
- Provide co-operation to overseas regulatory authorities through established gateways
- Promote and sustain our dialogue overseas to encourage a good understanding of the economic, legal and regulatory environment within which the Island operates.

Objective: External Relations - To develop constructive relations with the EU and international organisations to promote the Island’s interests and rights to trade.

The Commission will:
- Assist Government in developing and maintaining EU and international relations promoting the Island’s interests and rights to trade
- Ensure that the Island maintains international standards of regulation keeping under review previous IMF recommendations and prepare for the IMF inspection of the Island in September 2008.

Objective: External Marketing - To market the Island’s positive image.

The Commission will:
- Work with the industry promoting good regulation which can lead to economic growth
- Assist Government in promoting the Island as an international financial centre.

In order to assess its performance in meeting its aims and objectives, the Commission has set for itself a number of performance indicators.
Regulatory Approach

The guiding principles for the Commission’s regulatory approach continue to be those set internationally. If the Island is to continue to attract reputable institutions and enjoy market access overseas, then these are the standards against which it will be judged.

In order to conduct regulated activity businesses need to apply to the Commission for a licence. Licences are issued for banking, investment, funds and fiduciaries activities. Other categories of regulated activity such as money service businesses are being added.

Within the Commission the work of authorising or licensing businesses is carried out separately by the Authorisations function. Once licensed the holder of the licence then becomes the responsibility of the Supervision Division for ongoing regulation and oversight.

Authorisations

The Commission publishes its licensing policy. This is an important way of explaining to potential applicants the key considerations involved in deciding whether an application is to be recommended for approval. Wherever possible the Commission will guide applicants during the processing stage on any matters which need addressing before the formal hearing. The licensing policy was amended in May 2007:

- To allow companies registered under the Companies Act 2006 to be licensed as investment businesses or fiduciaries (see page 41 regarding collective investment schemes)
- To allow custodians of certain types of collective investment schemes to operate under a category 3 group (b) or a category 5 investment business licence
- To limit the licensing of sole trader and partnerships to a restricted category of fiduciary licence that is designed for natural persons only.

An applicant is sent a copy of the Executive’s recommendation on the application and is invited to attend the hearing. Typically there will be a number of matters to be finalised if a positive decision is reached, and in these cases applicants will be advised of the decision on a “subject to” basis. They will then have a maximum of six months to complete the outstanding points, while also confirming that there have been no material changes to the application during this period, before the licence is finally issued.

The Commission recognises that applications need to be processed promptly, as commercial decisions can depend on the outcome. In the Commission’s experience applicants can greatly assist the timetable by making sure that applications are properly completed and that requested information is fully provided at the outset.

For the first six months of the period Authorisations had a different reporting line (to the Head of Policy & Legal). However because of a reorganisation within the Commission, Authorisations now reports to the Head of Enforcement. A move of some of the relevant staff following completion of licensing of trust service providers was forewarned in the last Annual Report.

The following table provides an overall summary of the number of licence applications received, the number determined by the Board and the number of licences actually issued. The number of licences determined and issued exceeds the number received because of applications received but not determined during the preceding period. One application was refused, and a request for a review of the Commission’s decision has been lodged with the Financial Services Review Committee.

<table>
<thead>
<tr>
<th>Applications</th>
<th>Received</th>
<th>Determined</th>
<th>Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSP</td>
<td>14</td>
<td>15</td>
<td>14</td>
</tr>
<tr>
<td>TSP</td>
<td>8</td>
<td>28</td>
<td>31</td>
</tr>
<tr>
<td>Inv Business</td>
<td>9</td>
<td>9</td>
<td>11</td>
</tr>
<tr>
<td>Total</td>
<td>31</td>
<td>52</td>
<td>56</td>
</tr>
</tbody>
</table>

These applications and the movement of existing licenceholders’ key staff generated a need to conduct 642 individual vettings, including 312 new vettings and 330 updates of previous vettings. All directors, controllers (as defined) of a business, managers, persons with ‘four-eyes’ responsibility and other key staff are subject to the vetting process. The Commission believes the vetting procedure is an essential part of licensing as it requires applicants to give a full account of their career history. It forms a basis on which the Commission can then come to an informed decision on whether a person is suitable to fulfil a regulated role. There have been occasions where the vetting has revealed matters not properly disclosed and which are nevertheless material to the application.

The Commission undertakes a review of licence application and ongoing licence fees charged to licenceholders approximately every two years. A review of fees conducted during the previous period resulted in an increase in fees with effect from 1 April 2007.
Supervision

The Commission’s supervisory approach is risk-based and is published on the Commission’s website.

The areas that pose a risk to the Commission’s Core Objectives of Supervision in licenceholders are:

- Financial Failure
- Misconduct/Mismanagement and/or inappropriate conduct of business practices
- Fraud or dishonesty
- Money Laundering and/or Financing Terrorism.

The risk profile of each licenceholder is assessed taking into account business risks and control risks as well as the extent to which the control environment operating within the business mitigates the business risks. The resulting risk rating primarily determines the frequency of on-site visits to the group/licenceholder.

The impact rating determines the nature of the Commission’s relationship with the group/licenceholder and the type of on-site visit to be undertaken. The evaluation of the risk and impact ratings is translated into a comprehensive on-site visit programme for the year. The Commission will now be sharing with each group/licenceholder the overall impact and risk rating it has assigned to it. Where a risk rating of “Medium” or “Higher” has been assigned, the Commission will explain the reason(s) for the rating. The Commission risk rates groups/licenceholders in relation to the risks it believes the group/licenceholder poses to the Commission in relation to its Core Objectives of Supervision.

The principal risks attached to each activity sector on the Island may be summarised as follows:

<table>
<thead>
<tr>
<th>Financial Risk</th>
<th>Customer Protection Risk</th>
<th>AML/CFT Risks</th>
<th>Reputational</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking</td>
<td>Capital or liquidity inadequacy, impacting on solvency or ability to repay deposits. Loan quality in some cases. Potential systemic consequences. Inward cross-border infection. Intra-group exposures.</td>
<td>As for financial risk.</td>
<td>Non face-to-face business creates higher AML CFT risk.</td>
</tr>
<tr>
<td>Investment business</td>
<td>Financial soundness less of a risk as client assets held off-balance sheet.</td>
<td>Mis-selling or unsuitable advice.</td>
<td>AML CFT risk present, but less non face-to-face business.</td>
</tr>
<tr>
<td>Fund administration</td>
<td>Retail funds require a higher degree of regulation. Concern if retail investors subscribe to more professional funds.</td>
<td></td>
<td>Non face-to-face business creates higher AML CFT risk.</td>
</tr>
<tr>
<td>Fiduciaries</td>
<td>Financial soundness less of a risk as client assets held off-balance sheet.</td>
<td>Risk of directors and trustees not fulfilling their responsibilities for corporate governance.</td>
<td>Risk of layering through the use of trusts and companies. Risk of inadequate due diligence, and AML CFT risk present for non face-to-face business.</td>
</tr>
</tbody>
</table>

Michael Weldon
Head of Supervision

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</tr>
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</table>

<table>
<thead>
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</tr>
</tbody>
</table>
The role of the Commission is to seek to minimise these risks through regular supervision of the business and follow-up on shortcomings against prudential requirements. However the Commission does not manage or administer licenceholders, nor does it take management decisions on their behalf. Thus it is not the role of the Commission ultimately to prevent failure.

To underline a renewed emphasis on risk and compliance the Supervision Division made a new appointment during the period of a Senior Manager - Risk and Compliance. His responsibilities include ensuring that the Division is meeting the standards which it has set for itself in applying risk-based supervision. Global financial instability also has caused the Commission to review its contingency plans for handling a licenceholder failure.

In a further reorganisation the schemes and investment business teams were merged, which has consolidated expertise and given a much greater depth to the work in this area of Supervision.

The following table sets out the number of visits undertaken over the last three years, and the number of days required for each interaction:

<table>
<thead>
<tr>
<th>Type of Visit</th>
<th>Banking</th>
<th>FIS</th>
<th>Fiduciary</th>
<th>Total</th>
<th>Average days per visit</th>
<th>Total days</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual business meetings</td>
<td>28</td>
<td>14</td>
<td>13</td>
<td>55</td>
<td>2</td>
<td>110</td>
</tr>
<tr>
<td>Focus visits</td>
<td>31</td>
<td>4</td>
<td>66</td>
<td>101</td>
<td>9</td>
<td>909</td>
</tr>
<tr>
<td>Supervisory visits</td>
<td>0</td>
<td>29</td>
<td>21</td>
<td>50</td>
<td>12</td>
<td>600</td>
</tr>
<tr>
<td>Total</td>
<td>59</td>
<td>47</td>
<td>100</td>
<td>206</td>
<td></td>
<td>1,619</td>
</tr>
</tbody>
</table>

The Commission initially planned to conduct 184 visits during the year, so the overall final number was 22 ahead of target. This was partly achieved by creating a dedicated on-site visit team within the Fiduciary Services area to undertake focus visits to review progress made by licenceholders on agreed remediation plans. There were 55 visits of this nature and the overall findings are contained in the Fiduciary Services sub-section of this report (see page 32).

<table>
<thead>
<tr>
<th>Type of Visit</th>
<th>Number of visits undertaken</th>
<th>Average man-days per visit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual business meetings</td>
<td>19</td>
<td>51</td>
</tr>
<tr>
<td>Focus visits</td>
<td>35</td>
<td>27</td>
</tr>
<tr>
<td>Supervisory and on-site risk assessments</td>
<td>68</td>
<td>45</td>
</tr>
<tr>
<td>Total</td>
<td>122</td>
<td>123</td>
</tr>
</tbody>
</table>

* this line represents total, not average, man-days.
On page 40 of this report there is a description of the progress made with the Financial Services Bill. When enacted this Bill will have important consequences for licenceholders in terms of implementation of the new legislation, including secondary legislation, the new unitary licences to be issued, and other new provisions. The implementation timetable, which involves different stages for existing and new licenceholders, commences on enactment of the new Act and is expected to be completed by 1 January 2009. This was conveyed to licenceholders at a seminar in January 2008 and further industry briefing events will be held as necessary.

An important element of the implementation of the Financial Services Bill will be the Handbook, containing the Rules and associated Guidance.

In accordance with the relevant regulations (the Banking (Civil Penalties) Regulations 2006, the Building Societies (Civil Penalties) Regulations 2006, the Investment Business (Civil Penalties) Regulations 2006, and the Fiduciary Services (Civil Penalties) Regulations 2006) the Commission imposes financial penalties on licenceholders if they submit their returns late. The timely submission of prudential data is essential for the Commission’s offsite review work, and if information is late then the Commission cannot react quickly if any adverse trends are developing.

Civil penalties levied during the year totalled £7,900 arising from 52 events. A number of the penalties related to Annual Compliance Returns due to be submitted by 30 April 2007 (in relation to 31 December 2006 year-ends).

<table>
<thead>
<tr>
<th>Number of penalties levied</th>
<th>£100 Penalties</th>
<th>£1,000 Penalties</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banks &amp; Building Societies</td>
<td>12</td>
<td>0</td>
</tr>
<tr>
<td>Fiduciaries</td>
<td>14</td>
<td>2</td>
</tr>
<tr>
<td>Funds &amp; Investment Businesses</td>
<td>23</td>
<td>1</td>
</tr>
</tbody>
</table>

Last year’s report referred to the external review which the Board commissioned to examine the way in which Supervision Division records and evidences the work undertaken during on-site visits. The recommendations contained within that report have now been implemented. This has resulted in a new file structure and more formal recording and reviewing of evidence collected on visits, as well as a timely follow-up on points for action.

The main result for licenceholders is that following a focus or a supervisory visit, the Commission now issues a generally shorter form report concentrating on exceptions - in particular where the Commission’s Codes are not being applied appropriately.

The visit reports also seek to identify “Best Practice” issues, which licenceholders are invited to consider if they believe them appropriate to their business.

A vital element of the Division’s work is communicating with other regulators of licenceholders and their groups. This is so that each regulator understands and agrees to the division of regulatory responsibilities and accountabilities.

During the year, the Commission continued to share a copy of our on-site visit report with the home regulator where the licenceholder is a part of a larger regulated group.

The Commission sent 179 letters to other regulators for regulatory purposes. These included our standard annual letters to home and host regulators in relation to high impact licenceholders, requests for information and replies to other regulators’ requests for assistance, as well as sharing on-site visit reports. Approximately 75% of the correspondence was initiated by the Commission and 25% was the Commission responding to enquiries from other regulators.

The number of licences surrendered during the year were as follows. Some of these related to consolidation of existing licenceholder businesses:

<table>
<thead>
<tr>
<th>Type</th>
<th>Licences surrendered</th>
</tr>
</thead>
<tbody>
<tr>
<td>Banking</td>
<td>3</td>
</tr>
<tr>
<td>Services to Collective Investment Schemes</td>
<td>3</td>
</tr>
<tr>
<td>Investment Business</td>
<td>9</td>
</tr>
<tr>
<td>CSP</td>
<td>4</td>
</tr>
<tr>
<td>TSP</td>
<td>2</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>21</strong></td>
</tr>
</tbody>
</table>

The Commission’s officers undertook a number of visits to home regulators during the year including the UK Financial Services Authority and the Irish Financial Services Regulatory Authority.
The Criminal Justice (Money Laundering) Code 2007 requires licenceholders to vet those employees who may be engaged in activities that could be exposed to the risk of money laundering. The Division has identified a suitable benchmark to assist licenceholders in compliance, and is developing procedures internally to examine this during its supervisory visits.

The Commission circulated an advice note to licenceholders on the importance of appropriate planning for an outbreak of pandemic flu. Research in the UK indicates that up to half the population could fall ill during the course of a pandemic, and that 15-20% of employees could be off work at the peak of a pandemic. Licenceholders have been advised to consider arrangements to maintain core operations and if necessary to suspend other activities. Smaller licenceholders have been encouraged to consider locum arrangements, and larger groups to consider options for temporary outsourcing.

Banking
Banks on the Isle of Man generally fall into one of three categories. Those which are part of very large international groups where their operations locally are part of significant offshore presences; more medium-sized banks where they are offering specialist services including private banking, wealth management and fiduciary opportunities to the group’s international client base; and a few other banks whose focus is mainly on the taking of deposits from international residents for lending to their parent groups.

In the case of the latter category it can mean that such banks may incur material exposures to group treasuries where the market risks - relating to interest rate, maturity and foreign exchange positions - are managed centrally. This is the principal reason why the Commission operates a policy of only licensing banks which are financially very sound and able to provide full support to their local operations at all times. However, in the light of the turbulence in financial markets during the period the Commission has been considering carefully its policy towards the cross-border dependencies which banks may have on their parent groups. The Commission has been considering carefully its policy towards the cross-border dependencies which banks may have on their parent groups.

In the light of the turbulence in financial markets during the period the Commission has been considering carefully its policy towards the cross-border dependencies which banks may have on their parent groups.
Basel II required the Commission to make some changes to the Banking (General Practice) Regulatory Code 2005. These changes were relatively minor and focused on capital, risk management, and reporting forms (which are specified in the schedule to the Code). These changes were completed in December 2007 and became effective from 1 January 2008.

In addition, the Commission is in the process of updating and reissuing its banking guidance notes, which are used to supplement the Code.

**Funds and investment business**

Authorised and full international schemes operate on the Island under appropriate regulations. Other international schemes, in particular those directed towards institutional and more expert categories of investors, rely in particular on the regulation and responsibilities of relevant functionaries, in addition to the adequate disclosure of information.

During the period the Commission moved to reinforce its supervision of funds in line with the following key principles and responsibilities:

**Governing body** - The Commission believes that the governing bodies of all funds have a primary responsibility for ensuring that a fund is managed and operated properly and in accordance with the offering documents. In particular this includes initial due diligence, fiduciary responsibility, the adequate disclosure of information to participants, the timely release of relevant information including audited accounts, compliance with a fund’s stated investment policy and objectives, the fair valuation of assets, and compliant and suitable promotion.

Shortly after the end of the period the Commission issued a policy statement drawing the attention of governing bodies and functionaries of alternative investment funds to the Offshore Alternative Fund Directors’ Guide – 2nd edition 2008 issued by AIMA. The Policy Statement represents best practice standards which will be used as a benchmark within the ongoing supervisory process.

**Due diligence** - It is the responsibility of the governing body of an Isle of Man fund to ensure that the investment objectives of a fund provide a viable basis for investment.

**Fiduciary responsibility** - Within a fund, functional responsibility for fiduciary care beneath the governing body will depend on the nature of the fund and degree of protection afforded relative to the intended category of investor. Fiduciary responsibility within Authorised and full International schemes is mandated, and is further made very clear in the case of managers of Qualifying Funds.

**Adequate and timely information** - Offering documentation must be complete and kept up-to-date. The Commission has adopted revised internal procedures to monitor the timelines within which audited accounts of funds are prepared. Where there are delays, this may or may not indicate a potential for future problems. The Commission is therefore alerted to the need for possible action.

**Fair valuation** - A fair, and wherever possible independent, valuation of assets provides the basis on which investors can subscribe to, or redeem their investments in, a fund. Sometimes certain assets may be illiquid or a market price unavailable. In these circumstances the basis on which a valuation is to be made should be clearly disclosed to investors. However it should be noted that accepted standards for valuing funds do not necessarily reflect the value which those assets will achieve in a liquidation.

In October the Commission issued a policy statement on hedge fund valuation, in particular drawing attention to the work of IOSCO, AIMA and the Isle of Man Fund Management Association in this area.

**Promotion** - The Commission believes that all funds should be properly distributed, and distributed only to those at whom the particular fund type is aimed. The suitability of advice given at the time of investment is also paramount.
The Commission has emphasised the responsibility of governing bodies in this area, to complement existing guidance for the promotion of funds. In addition it has introduced a new category of licensed promoter for Qualifying Funds, as referred to on page 41.

The principles set out above are embodied within the new arrangements for the Specialist and Qualifying Investor Funds.

As mentioned earlier in this report, the funds and investment business supervisory teams were merged during the year. This, together with the implementation of the recommendations of the Funds Review Group and some staff turnover, meant that it was a challenge always to meet core service level standards in the Schemes area. The on-site visit plan therefore had to be amended partly to accommodate visits that were considered a priority because of events occurring. Desk-based supervision in terms of up-to-date risk assessments also suffered during the year, but were back on schedule by the end of it.

Both the desk-based and on-site visit work in the investment business area (covering financial advisers and investment managers) went according to the plan approved by the Board at the start of the year.

During the year the Commission received and reviewed the responses from fund administrators and managers concerning its consultation on deferred sales charges. There were 28 Isle of Man funds identified as being administered in/from the Isle of Man and applying a deferred sales charge. Generally, administrators reported that the boards of individual fund companies believed that the disclosures already being made in scheme documentation and marketing material were adequate and that it was not necessary to make any additional disclosures to existing, or potential, investors.

The practice of a deferred sales charge (also called “deferred subscription charges”, “deferred initial charges”, “back end loading” or “marketing sales fee”) may cause inequalities for individual investors if that investor stays invested in the fund beyond the amortisation period, as after this date they will bear part of the amortisation of other investors who subscribed at a later date and this may be materially dependent on timings of cash flows into the fund. It was of concern to the Commission that this potential inequity between shareholders may not have been appropriately disclosed to investors. Accordingly, the Commission wished to be satisfied that adequate disclosure on this matter had been made in the relevant marketing material.

### Fiduciaries

Trust and company service providers – collectively known as fiduciaries - provide administration, trustee and director services respectively to both Isle of Man and overseas domiciled entities.

<table>
<thead>
<tr>
<th>Companies, Trusts &amp; Partnerships under administration by Fiduciary Services</th>
<th>Companies and Partnerships</th>
<th>Trusts</th>
</tr>
</thead>
<tbody>
<tr>
<td>IOM Companies</td>
<td>23,782*</td>
<td>19,006</td>
</tr>
<tr>
<td>Other Companies</td>
<td>19,240</td>
<td>Private Trust Companies</td>
</tr>
<tr>
<td>Partnerships</td>
<td>1,014</td>
<td>0</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>44,036</strong></td>
<td><strong>19,392</strong></td>
</tr>
</tbody>
</table>

*449 are 2006 Act Companies

A frequent question asked is to what bona fide use are trusts and companies put in a jurisdiction such as the Island.

In the course of carrying out its on-site work the Commission has noticed that trusts are most frequently used for tax and estate planning and to maintain continuity in inheritance. At the individual level companies will be used for a range of purposes, but especially for the holding of assets, aircraft and yacht management and for private business purposes.

The Commission believes that individuals have a right to plan their tax affairs efficiently in compliance with the law. However it does not regard very aggressive tax avoidance for clients as a prudent part of any licenceholder’s business strategy. Any suspicion of tax evasion would need to be reported as a suspicious transaction to the Financial Crime Unit.

Trading companies are fewer, although the Island is an important jurisdiction from where corporate groups manage their international operations. Further information on corporate activity is shown on page 44.

The core part of the Commission’s supervision of fiduciaries has been its risk-based programme of on-site visits to examine client files. Historically case experience suggests that trust and company service business is most vulnerable to corporate layering, where trusts and companies are used in a chain of transactions usually beginning and ending in other jurisdictions. Where used for nefarious purposes, the dangers are very evident.

However in recent years this risk has been significantly mitigated by the statutory requirement that all service providers must know the true identity of the various parties behind structures being administered.
This in turn is underpinned by the full regime of due diligence, ‘source of funds’, ‘source of wealth’, ‘nature of business’ and monitoring of transactions required by the anti-money laundering and prevention of terrorist financing regulations currently in place. Developments in this area are discussed further on page 35.

Findings from supervisory visits to fiduciaries

A total of 66 focused compliance visits were undertaken to fiduciaries during the year, together with 21 supervisory meetings - see page 28. Following on from this work it is instructive to provide a brief summary of the key points which emerged.

Whilst the Commission saw that licenceholders have made considerable efforts to ensure that they have appropriate procedures and hold appropriate documented information on their files, a number have been required to ensure that they update their documented policies and procedures to reflect changes in the legislative and regulatory requirements as well as to reflect operational changes that have occurred within their own businesses.

In relation to client identification licenceholders were reminded to make sure that, if they wish to make use of the eligible introducers’ regime, they have established that their introducers are eligible in accordance with the requirements of the Criminal Justice (Money Laundering) Code 2007 and with the Anti-Money Laundering Guidance Notes.

Generally, when dealing with direct clients, licenceholders held satisfactory documentary evidence of the identification and address of their clients. In some cases source of funds and source of wealth were less well documented and it was not always clear from the information available how licenceholders had verified the information that had been provided by their clients. This information is important in building up the customer profile and enabling the licenceholder to assess whether the activities of the client entity are in keeping with the known and anticipated activity and consistent with the client profile. It also provides an audit trail for compliance review.

Licenceholders have been asked to ensure that they are at all times familiar with the requirements of the Regulatory Codes and the Commission is always happy to discuss these should there be any queries with implementation.

Accounts do so in accordance with the requirements of the Code to ensure that at all times clients’ money is appropriately safeguarded.

Looking forward it will be very important with the implementation of the Financial Services Bill and the rulebooks, that licenceholders are aware of the changes which need to be made to their procedures and that these changes are implemented in a timely manner.

During the year the opportunity was taken to dedicate a manager within the team to deal with the more challenging cases, for example where through a lack of action a licenceholder demonstrated an inability to conduct their regulated business in a compliant manner. There are very few of these licenceholders but when they occur they absorb a disproportionate amount of time.

Depositors’ and Investors’ Compensation Schemes

The Depositors’ and Investors’ Compensation Schemes are separate from the Commission, although the Commission currently acts as Scheme Manager in the case of the DCS. The DCS produces its own report and accounts. No claim has ever been made against the Investors’ Compensation Scheme. Further details about the level of protection available are shown on the Commission’s website.

It is important to note that both schemes would need to be funded by relevant licenceholders in the event of any claims arising. The Schemes are not pre-funded and there is a limit on how much could be levied on participants in any one year. Neither do the schemes assume that any Government funds would, or indeed could, be made available in support of any failure.

In January 2008 the Treasury agreed terms of reference for a review by the Commission of the present...
terms of the DCS. In February the Commission circulated a questionnaire to banks to obtain additional information about the nature and mix of the Island’s deposit base. In March it issued a consultation paper setting out various options which might be pursued for altering the extent of coverage. Shortly after the end of the period the Commission submitted an interim report to Treasury, and this will be followed with a more substantive report with recommendations once the responses have been evaluated.

Complaints about licenceholders

The Commission does not have a role to arbitrate in relation to consumer complaints about its licenceholders. These may fall within the remit of the Financial Services Ombudsman Scheme, and full details of this may be obtained from the Office of Fair Trading as part of the Isle of Man Government.

The Commission is always interested to hear of customer complaints and in many cases is able to assist customers in successfully resolving problems. Such information also enables the Commission to assess if there may be any regulatory failings within a licenceholder.

However the Commission has no power to make any compensation award to a customer and any remedial action by the Commission against the licenceholder is likely to remain confidential between the two parties.

International relations

Most of the Island’s financial services activities are conducted by institutions which are part of regulated groups from other countries. It is therefore vital that strong links are established and maintained with authorities overseas, so that they can have confidence in the level of regulation being exercised locally. This helps to sustain the Island’s reputation as a well regulated and co-operative jurisdiction from which to do business.

The Island’s position as a signatory of the IOSCO MMOU also forms a key part of its regulatory standing.

Supervisory co-operation with other regulators is maintained through the sending of inspection reports to parent supervisors, to assist in their consolidated supervision of group entities. The Commission has signed Memoranda of Understanding with many overseas regulators to reinforce this relationship.

In response to the uncertainties in financial markets, the Commission has enhanced further its dialogue with the home regulators of banks that are represented in the Island.

The Board of the Commission met with the Board of the Jersey Financial Services Commission, and found this exchange of views most useful. The Commission also received a visit from the Lord Mayor of the City of London, among many other visitors.

The Commission was represented at the regular meetings of IOSCO and the OGBS. The Chief Executive and senior staff also spoke at international gatherings, and visited a number of international regulators.
The Prevention of Money Laundering and Countering the Financing of Terrorism and Enforcement Action

A strong enforcement function which ensures that AML CFT activity is kept up-to-date, and which can take prompt action to deal with unlicensed activity and pursue remedial action as required, is an essential part of an effective regulatory regime.

Prevention of money laundering and countering the financing of terrorism

As a responsible financial centre operating in international markets the Island is committed to full adherence to the principles of the FATF Recommendations on AML CFT.

Responsibility for AML CFT legislation lies with the Department of Home Affairs, as the Department also responsible for the Police and the Financial Crime Unit (which contains the Island’s Financial Intelligence Unit). Overall co-ordination of AML CFT activity, and consultation on new legislation and regulations, is conducted through JAMLAG. Membership of this group includes all regulated and key industry and professional sectors, as well as regulators, law enforcement authorities and relevant Government Departments. The group meets regularly, including through ad hoc working groups to assist in detailed drafting.

In implementing AML CFT measures particular focus has been given to the specific risks which the Island faces. These risks have been identified from a consideration of the relevant flows of business and experience in dealing with problem issues which have occurred. A large proportion of business is undertaken on a non face-to-face basis. The amount of domestic business is therefore relatively small.

The Island is also a significant service provider for companies and trusts. It is therefore more exposed to the risk of ‘layering’, than to the risk of cash movements which might be more prevalent in countries with more international transport links. As a result the Island finds itself needing to co-operate promptly with regulatory and other enquiries taking place elsewhere, where it has been used in a chain of transactions under investigation.

These risks require the Island to have in place measures which ensure that the true identity of everyone behind business relationships is established, along with measures to ensure that appropriate due diligence is carried out on the nature of that relationship including sources of funds. This is the cornerstone of the AML CFT policy administered by the FSC.

During the year the Commission participated extensively in the drafting of the Criminal Justice (Money Laundering) Code 2007. This redraft of the previous Code took important steps to put into legislation key requirements of the revised recommendations of the FATF. Most of these had previously been applied, but through guidance.

In parallel with this work the Enforcement Division drafted Chapter 9 of the Financial Services Rule Book 2008 concerning the prevention of money laundering and the financing of terrorism. This will come into operation after the end of the period when the Financial Services Act comes into operation. This statutory Rule Book further implements the recommendations of the FATF through enforceable means.

The Commission has also revised its comprehensive guidance to licenceholders to take account of the new Code and Rule Book, by drafting a new Anti-Money Laundering and Countering the Financing of Terrorism Handbook. The Handbook forms a very important part of the Commission’s assessment of institutions’ compliance with AML CFT measures, and enables the Commission to give guidance on how compliance can be achieved including with a risk-based approach. The Commission consulted with JAMLAG to assist with the drafting.
Non-financial businesses including estate agents, dealers in high value goods, car dealers and other persons accepting cash over €15,000 are covered by the Criminal Justice (Money Laundering) Code 2007. During the period the Commission assisted the Department of Home Affairs on a number of initiatives to raise public awareness of AML CFT measures, especially within the non-regulated sector. This included holding a seminar for those likely to be affected. Other initiatives used were newspaper flyers and advertisements, radio announcements and interviews, as well as posters being placed at the ferry terminal and airport.

The Commission has also provided assistance to the Chief Secretary’s Office regarding AML CFT issues with the European Union.

One of these issues was the implementation of FATF Special Recommendation VII on wire transfers. The UK has applied to the EU on the Island’s behalf to take advantage of a special EU derogation whereby a jurisdiction which is in monetary union with an EU member state can, for the purposes of Special Recommendation VII, treat the wire transfers between them as being “domestic”. These “domestic” wire transfers do not require originator details to be included with the wire transfer and consequently avoid prohibitive additional cost. To take advantage of the EU derogation several pieces of EU legislation have had to be copied into Manx law.

The second issue was over the inclusion of the Isle of Man on the EU’s list of equivalent jurisdictions. The Island’s inclusion on the list was regarded as important, as under the FATF Recommendations a financial business in one jurisdiction can only operate the eligible introducer system with another business which is regulated in a jurisdiction with equivalent AML CFT standards. Inclusion on the EU’s voluntary list of equivalent jurisdictions allows EU member states to include the Isle of Man on their own lists of equivalent jurisdictions. Much business between EU member states and Isle of Man businesses could then be conducted without repeatedly asking a customer to produce identification documents.

The Division received visits from law enforcement authorities in the Netherlands, Jersey and the UK as part of its mutual co-operation between jurisdictions. The Head of Division also assisted on two IMF technical assistance programmes during the period.

**Assistance with investigations and insider dealing**

The Island has in place important provisions to enable it to co-operate in cross border enquiries and investigations. Criminal matters are dealt with by the Attorney General while regulatory matters are dealt with by the Commission within its remit. Because of the importance which the Commission attaches to its responsibilities in this area, it has published a statement on its website describing the nature of co-operation provided and from whom assistance can be obtained in different circumstances.

The Island is a signatory to the IOSCO Multilateral Memorandum of Understanding. In order to become a signatory an IOSCO member (which includes the Island) has to demonstrate that it has the necessary laws and information gateways to enable it to co-operate with bona-fide requests for assistance from other regulators. This MMOU has become the international standard of co-operation for securities regulators globally.

During the period the Commission responded to eight requests for information under the MMOU from five different countries. Some of these were part of major international investigations. The Commission is very aware that prompt assistance is needed and will respond as speedily as possible, within one month or sooner. The Commission did not make any requests itself for information from other regulators under the MMOU.

Although the Island does not have a stock exchange, sometimes alleged insider dealing transactions are routed through financial institutions and companies based in the Island. In these cases Treasury may receive a request from an investigating authority in another jurisdiction for certain information to assist in their enquiries.

If appropriate Treasury will appoint inspectors locally to investigate the matter and obtain the requested information for passing to the overseas regulator.
Treasury typically appoints officers from the Commission under Schedule 3, paragraph 1(1) of the Insider Dealing Act 1998 to carry out this work. During the period Treasury appointed Commission employees as inspectors on two occasions, and in all cases the requested information was provided to the overseas regulator.

**Remedial action**

Company law sets down directors’ duties and responsibilities. There is no concept of a nominee director on the Island and directors of all companies (whether licensed or not) have a duty to exercise their own judgement as company officers. The High Court in the Island takes a poor view of directors who act in a cavalier, errant or reckless manner or fail to discharge their statutory responsibilities.

During the period the Commission successfully petitioned under section 26 of the Companies Act 1992 for the disqualification of one person from acting as a director of a company. Further information is shown on the Commission’s website, along with the details of 13 other persons whose previous disqualifications are still current.

**Public warnings**

Very often the Commission finds that persons attempting to undertake potentially fraudulent, mis-selling or other activities which could result in investor or counterparty loss, will seek to establish and market their schemes in different jurisdictions. This can cloud transparency and hamper detection.

As one tool in helping to stamp out such nefarious activities the Commission previously set up a system of publishing public warnings on its website about bogus names, companies, individuals and scams. To assist other regulators the Commission maintains a list of over 100 regulators and law enforcement authorities world-wide to whom it “pushes” warnings as soon as they are made. A total of 43 public warnings were made during the period. There is clear evidence that this has become an effective mechanism of saving people from loss, protecting the Island’s reputation and raising awareness of consumers, businesses and regulators in other jurisdictions of such scams.

**Other work**

During the year the Commission staged AML CFT training seminars for industry, the public and its staff. This included holding events at licenceholders own premises on occasions. The Commission has also researched and evaluated various computerised AML CFT training/testing packages and selected one which will be installed in 2008. The system will be used to highlight the current AML CFT training needs of staff and, if appropriate, be used as part of the selection process in recruiting new staff.
Policy Development

The role of the Commission’s Policy function is to ensure that its regulatory framework keeps up-to-date with evolving international standards and best practice, and to identify areas where the regulations need to be changed to enhance the Island’s competitive position and reflect business development.

The last twelve months has been a very busy period for the Policy and Legal Division, with a heavy programme of primary and secondary legislation progressing through the legislature.

The Commission is conscious that the different consultations conducted with the industry and professional bodies are time consuming and require much time and effort on the part of respondents. Although everyone is working towards a common benefit, the Commission is nonetheless most appreciative of the time taken. Some professional firms in particular have given their time pro bono publico.

Changes in policy generally either flow from suggestions made by industry or by the Commission in terms of what is needed to sustain an effective regulatory regime. Major policy proposals often require changes to legislation, which in the first instance necessitates support by Treasury before recommendations are prepared and put forward.

The Financial Services Bill is a core piece of legislation for the Commission. Its main purpose is to consolidate and bring up-to-date much of the Commission’s existing legislation covering banking, fiduciaries and investment business (collective investment schemes are being covered by a separate Collective Investment Schemes Bill - see below). The Financial Services Bill also clarifies the Commission’s remit and contains important new provisions to enhance its transparency and accountability including to Tynwald. Following the previous issue of a consultation paper on the Bill in December 2006, the Commission released its response to the comments received in May 2007.

On present progress the Commission is expecting the Bill to be enacted during the Summer of 2008, subject to Royal Assent.

In the meantime draft subordinate legislation under this Bill has been prepared to allow for the transition from the current regulatory regime to the new regime.

A briefing was held for the industry on the implementation of the prospective new legislation in January 2008.

As part of the arrangements under the new legislation, it is planned that the Commission will operate under a Memorandum of Understanding which has been agreed with Treasury and which will formally be signed when the Financial Services Bill receives Royal Assent.

The Collective Investment Schemes Bill, which also consolidates and brings up-to-date existing schemes legislation, is making similar progress to the Financial Services Bill.

Presentations were made by the Commission to members of the ACSP, the ICAEW and the Securities and Investment Institute, to assist their understanding of the scope and timetable of the Consolidation and Review of Legislation project.

During the year the Commission participated in the work of the Funds Review Group, which was an industry-led initiative sponsored by Treasury to develop some new funds products for the Island and broaden the appeal of the jurisdiction to attract incremental funds management business.

In March 2007 the Funds Review Group published a report which looked at the future opportunities for the Island’s funds industry. Amongst its recommendations, the group advocated the introduction of two new fund types, one targeted at the institutional funds market and another aimed at non-retail investors.

The Commission consulted with the industry on appropriate legislation. Tynwald subsequently approved
The Financial Supervision (Specialist Fund) (Exemption) Order 2007 and The Financial Supervision (Qualifying Fund) (Exemption) Order 2007. With effect from 1 November these respectively introduced the Specialist Fund and the Qualifying Fund. The Specialist Fund is targeted at the institutional market (with a minimum investment of not less than US$100,000) and the Qualifying Fund is aimed at non-retail investors.

There were also implications for existing Experienced Investor Funds, which were withdrawn as a fund category for new funds. A number of existing such schemes have since converted into the new fund types.

Meanwhile on 21 September the Commission consulted with the industry on new licensing arrangements for managers and asset managers, to complement the new regime. These are known as Associated Asset Managers, Specialist Asset Managers, and Managers of Qualifying Funds who are managed by Category 3(b) or 4 Investment Business Licenceholders. A new category of licence for promoters of Qualifying Funds was also introduced.

Subordinate legislation, in the form of the Investment Business Amendment Order 2007 and the Financial Supervision Commission (Financial Resources and Compliance Reporting) (Amendment) Regulatory Code 2007, covering these arrangements was introduced in November, and the Commission’s licensing policy was appropriately amended.

In November guidance was issued on the regulatory requirements applying where a company incorporated under the Companies Act 2006 is used as a vehicle for a collective investment scheme. In December 2007 the Financial Supervision Act 1988 (Definition of Collective Investment Schemes) (Amendment) Order 2007 and the Listed Limited Partnerships Regulations 2007 came into operation which allowed Isle of Man Limited Partnerships that are admitted to the Official List of the UK Listing Authority to fall outside of the definition of a collective investment scheme as set out in the Financial Supervision Act 1988.

Meanwhile a Companies Amendment Bill was prepared on which a consultation with interested parties commenced in January. The Bill proposed important changes to the Companies Acts 1931 – 2004, as well as to the Companies Act 2006 and related legislation.

Proposed amendments related to the preparation and audit of financial statements, the audit qualification requirements, a power to make regulations for the oversight of audits of Isle of Man companies with securities admitted to trade on a regulated market in the EU Member States (this is to ensure Third Country equivalence to comply with the EU Directive on Statutory Audits), and the accounting records provisions for 2006 Act companies.

The Commission subsequently commenced a dialogue with respondents on their comments prior to progressing the Bill through the legislature.

In October the Commission issued a consultation paper on a draft Company Officers Disqualification Bill 2007. Its primary aim was to address recommendations made in a previous independent review of the Commission’s approach to pursuing cases under section 26 of the Companies Act 1992, and to update relevant legislation in the light of general case experience.

This Bill also draws together into a single, stand-alone and more accessible body of law, all the current grounds for disqualification from holding certain offices in, or being involved in the promotion, formation or management of, companies.

Following the responses received the Commission worked on finalising the Bill for submission to the legislature.

Extended guidance was issued in December to the industry on directors’ duties and responsibilities, especially in relation to corporate directors of companies incorporated under the Companies Act 2006.

In May the Commission issued a consultation document on how money services businesses and electronic money providers could be brought under some form of, initially, limited regulation. This was considered necessary to give effect to the anti-money laundering and prevention of the financing of terrorism legislation which includes activities of money services businesses and electronic money providers within its scope.

The main proposals set out to introduce a licensing requirement, including the demonstration of fitness and propriety, compliance with the AML/CFT Code and relevant rules and handbook provisions to be supported.
by an on-site inspection programme, enforcement powers, and a licence fee.

In December a further consultation paper was released in the light of earlier comments with details of the regime to be applied. The Financial Services Bill and the relevant secondary legislation will introduce this regime in the second half of 2008. It is expected that applications for licences will be sought during a period of approximately eight weeks following the date on which the Financial Services Act comes into effect.

In January Tynwald approved a motion to ask Her Majesty by Order in Council to extend the relevant provisions in the UK’s Companies Act 2006 relating to the statutory powers of the Takeover Panel and to certain protections for the shareholders of companies involved in takeovers and mergers, to the Isle of Man. Liaison with the Takeover Panel and the Business Enterprise and Regulatory Reform Department on necessary modifications to UK law was conducted.

In conjunction with Jersey and Guernsey, discussions were also held with the Professional Oversight Board and ICAEW regarding the provision of audit oversight of companies whose securities are admitted to trade on EU Member States regulated markets. This initiative was made to enable the Crown Dependencies to achieve Third Country equivalence for the purpose of compliance with the EU Directive on Statutory Audits. These discussions are progressing well and the legislative provisions in relation to this matter will be taken forward within the Companies Amendment Bill.

In August the Companies Act 2006 (Appointed Day) (No.2) Order 2007 brought into operation the provision in the Companies Act 2006 which repealed the whole of the Prevention of Fraud (Investments) Act 1968. The 1968 Act was repealed because it had become obsolete and the protection provisions under that Act were now being achieved by other more recent legislation and other means.

The Policy and Legal Division review on a quarterly basis the progress made against the recommendations of the IMF contained in their assessment of the Island’s regulatory regime in 2003. This review also includes progress made against the independent follow-up assessment made of the Island’s standing against the standards and methodologies which have changed since 2003. The quarterly reviews were submitted for discussion by the Board.

The Commission organised a seminar for the industry in May on the effects and implications of MiFID on investment businesses. Angela Knight, CBE, Chief Executive of the British Bankers’ Association, together with a colleague spoke at the occasion. Although the EU Directive does not directly apply to the Island as the Island is not a member of the EU, many licenceholders are members of groups which are covered and therefore could be indirectly affected. It is also useful to consider what opportunities there might be for licenceholders from being outside of MiFID.

The Commission participates in an IOSCO Screening Group which reviews applications made by IOSCO members wishing to be considered as full signatories of the IOSCO MMOU. Members of the Policy and Legal Division undertake this work and attended meetings of the Screening Group during the year.

The Policy and Legal Division also commenced the review of the Depositors’ Compensation Scheme which is discussed on page 33.
Companies Registry and Corporate Activity

Companies Registry maintains the register and records of all companies incorporated in the Isle of Man, and provides a facility for the public to view documents which have been filed by these companies.

Companies Registry exists for its customers – be they companies, directors or people who search for company information. It aims to excel as a registration authority and as a source of public information for the benefit of the Island’s economy. To achieve this it actively looks for ways to continue to improve its performance and to raise standards in everything which it does.

Its functions include:

- Incorporating, re-registering and striking off companies
- Registering documents required to be filed under companies and related legislation
- Providing companies and related information to the public
- Enforcing compliance with statutory filing requirements.

The Commission has published on its website comprehensive service standards for the Companies Registry. Details of its actual performance since September 2005 are also displayed. Despite the introduction of the 2006 Act company in November 2006 and the replacement of the corporate charge with a new annual return fee (which is levied on companies, including foreign incorporated companies, with a place of business in the Isle of Man) in April 2007, Companies Registry consistently met all of its performance targets during the period.

The Commission has ambitious plans for the development of its online services for users of Isle of Man companies, and these are described further on page 51 of the report.

Corporate activity

During 2007 2,830 new companies were incorporated under the Companies Act 1931. Although this figure was lower than in 2006, 1,852 new companies were also incorporated under the Companies Act 2006. The combined total of 4,682 new companies incorporated on the Manx register was therefore 26% higher than in 2006 (3,719 companies). Since the end of 2007 the relative increase in the use of 2006 companies has continued.

The registration of limited partnerships, business names and LLCs also increased.

The total number of charges registered has also increased, mainly in respect of 2006 companies.

The following table summarises Companies Registry’s activity over the last six calendar years:

<table>
<thead>
<tr>
<th>Year</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incorporations 1931 Act</td>
<td>2,958</td>
<td>2,805</td>
<td>2,470</td>
<td>2,593</td>
<td>2,677</td>
<td>3,465</td>
<td>2,830</td>
</tr>
<tr>
<td>Total 1931 Act Cos</td>
<td>37,912</td>
<td>36,074</td>
<td>33,351</td>
<td>32,726</td>
<td>30,847</td>
<td>30,870</td>
<td>30,380</td>
</tr>
<tr>
<td>Dissolutions</td>
<td>1,726</td>
<td>2,028</td>
<td>2,056</td>
<td>2,401</td>
<td>2,105</td>
<td>2,003</td>
<td>2,290</td>
</tr>
<tr>
<td>Struck off</td>
<td>4,973</td>
<td>2,457</td>
<td>2,788</td>
<td>0</td>
<td>2,027</td>
<td>1,013</td>
<td>0</td>
</tr>
<tr>
<td>Charges – 1931 Act</td>
<td>1,810</td>
<td>1,715</td>
<td>2,181</td>
<td>2,350</td>
<td>2,751</td>
<td>3,270</td>
<td>3,269</td>
</tr>
<tr>
<td>Incorporations 2006 Act</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Charges – 2006 Act</td>
<td>254</td>
<td>1,852</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Business Names</td>
<td>666</td>
<td>698</td>
<td>738</td>
<td>722</td>
<td>673</td>
<td>689</td>
<td>676</td>
</tr>
<tr>
<td>Limited Partnerships</td>
<td>11</td>
<td>5</td>
<td>22</td>
<td>24</td>
<td>31</td>
<td>43</td>
<td>120</td>
</tr>
<tr>
<td>LLC</td>
<td>82</td>
<td>58</td>
<td>72</td>
<td>51</td>
<td>51</td>
<td>39</td>
<td>58</td>
</tr>
</tbody>
</table>

The number of documents received increased by 8% on the previous year.

<table>
<thead>
<tr>
<th>Year</th>
<th>2004</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of documents received</td>
<td>103,573</td>
<td>91,077</td>
<td>88,562</td>
<td>95,755</td>
</tr>
<tr>
<td>Total 1931 Act Cos</td>
<td>-3</td>
<td>-12</td>
<td>-3</td>
<td>-8</td>
</tr>
</tbody>
</table>

During the period 692 1931 Act companies converted to 2006 Act companies. The reasons were varied but in many cases reflected the greater flexibility offered by the new company. Companies which changed their domicile into the Island came from the BVI, Cayman Islands, Gibraltar and Luxembourg, among others.

In the past Companies Registry has warned persons administering companies that companies should not be left unattended in non-compliance with the law. It is therefore notable that more companies are now being properly dissolved than being left to be struck off which the Commission regards as punitive action.

To assist company officers and administrators in the discharge of relevant responsibilities, Companies
Companies Registry consistently met all of its performance targets during the period.

Companies Registry has issued a series of Practice Notes. During the period the following Practice Notes were issued:

PN4/2007 - Submission of Company Documents and the Calculation of Filing Fees. This practice note sets out the prescribed filing periods and how the Commission determines if a document is submitted on time.

PN5/2007 - Companies Registry Fees, which contains details of the fees payable in the Companies Registry as a result of changes introduced in the February 2007 budget.

PN6/2007 - The Responsibilities and Duties of Directors under the laws of the Isle of Man, outlining for non-licenceholders the responsibilities and duties of directors under the laws of the Isle of Man.

NMVPN1/2007 - The Companies Act 2006 - Fees, which contains details of the fees payable in the Companies Registry as a result of changes introduced in the February 2007 budget.

Companies fees

The statutory fees charged by Companies Registry for the incorporation of companies, filing of documents and other activities are reviewed approximately every two years. A comprehensive review was conducted during the period and recommendations submitted to Treasury. As a result some new statutory fees will be introduced with effect from April 2008, and others will increase by approximately 7% which represents the rate of inflation since the last change in August 2005.

The basic incorporation fee for a 1931 Act company was increased to £190 from £180 with effect from 6 April 2008. The incorporation fee was last increased in August 2003.

The annual return fee is not being increased and will remain at £320. This was amended in April 2007 when a corporate charge, introduced by Treasury, of £250 was added to the existing annual return fee of £70. However there was no increase in overall cost to affected companies because the corporate charge replaced previous income tax arrangements for exempt and non-resident companies.

Charities and property management companies continue to be exempted from payment of the annual return fee. However, in future dormant companies will be expected to pay the equivalent of the previous annual return fee, which is being increased from £70 to £75.

Details of the relevant legislation covering companies fees are set out in Appendix G.

AIM listed companies

As reported in last year’s Report, the Island is an important jurisdiction of incorporation for AIM listed companies. It has created a strong competitive position for itself largely because of the professional skills on hand to prepare companies for listing and the cost effectiveness of the work undertaken.

This position continued during the period. As at 14 March 2008 the Island remained in the leading position for non-UK AIM 100 companies by country of registration. AIM listings can be sought by both 1931 and 2006 Act companies.

Number of non-UK AIM 100 companies by country of registration *

<table>
<thead>
<tr>
<th>Position</th>
<th>Country</th>
<th>No. of companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Isle of Man</td>
<td>12</td>
</tr>
<tr>
<td>2</td>
<td>Bermuda</td>
<td>8</td>
</tr>
<tr>
<td>3</td>
<td>Canada</td>
<td>6</td>
</tr>
<tr>
<td>4</td>
<td>Australia</td>
<td>5</td>
</tr>
<tr>
<td>4</td>
<td>British Virgin Islands</td>
<td>5</td>
</tr>
<tr>
<td>4</td>
<td>Guernsey</td>
<td>5</td>
</tr>
<tr>
<td>4</td>
<td>Jersey</td>
<td>5</td>
</tr>
<tr>
<td>8</td>
<td>Netherlands</td>
<td>4</td>
</tr>
<tr>
<td>9</td>
<td>Cyprus</td>
<td>3</td>
</tr>
<tr>
<td>9</td>
<td>Ireland</td>
<td>3</td>
</tr>
<tr>
<td>11</td>
<td>Cayman Islands</td>
<td>1</td>
</tr>
<tr>
<td>11</td>
<td>Denmark</td>
<td>1</td>
</tr>
<tr>
<td>11</td>
<td>Malaysia</td>
<td>1</td>
</tr>
<tr>
<td>11</td>
<td>South Africa</td>
<td>1</td>
</tr>
<tr>
<td>11</td>
<td>United States</td>
<td>1</td>
</tr>
</tbody>
</table>

The market capitalisation of non-UK AIM 100 companies by country of registration as at 14 March 2008 was also greatest in the Isle of Man.

**Market Capitalisation of non-UK AIM 100 companies by country of registration***

<table>
<thead>
<tr>
<th>Position</th>
<th>Country</th>
<th>MCAP of companies (£m)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Isle of Man</td>
<td>4586.92</td>
</tr>
<tr>
<td>2</td>
<td>Canada</td>
<td>2678.24</td>
</tr>
<tr>
<td>3</td>
<td>British Virgin Islands</td>
<td>2422.43</td>
</tr>
<tr>
<td>4</td>
<td>Bermuda</td>
<td>2031.72</td>
</tr>
<tr>
<td>5</td>
<td>Jersey</td>
<td>1764.47</td>
</tr>
<tr>
<td>6</td>
<td>Australia</td>
<td>1647.33</td>
</tr>
<tr>
<td>7</td>
<td>Cyprus</td>
<td>1273.29</td>
</tr>
<tr>
<td>8</td>
<td>Guernsey</td>
<td>1128.20</td>
</tr>
<tr>
<td>9</td>
<td>Netherlands</td>
<td>974.44</td>
</tr>
<tr>
<td>10</td>
<td>Ireland</td>
<td>924.24</td>
</tr>
<tr>
<td>11</td>
<td>Malaysia</td>
<td>330.60</td>
</tr>
<tr>
<td>12</td>
<td>South Africa</td>
<td>328.27</td>
</tr>
<tr>
<td>13</td>
<td>United States</td>
<td>237.39</td>
</tr>
<tr>
<td>14</td>
<td>Cayman Islands</td>
<td>146.27</td>
</tr>
<tr>
<td>15</td>
<td>Denmark</td>
<td>90.31</td>
</tr>
</tbody>
</table>


**Other**

The Commission is a member of the European Commerce Registrars Forum. Every registration authority in Europe is a member. The Commission attended the annual conference which keeps it in touch with developments in Europe, and allows it to benchmark our performance and service standards with other registration authorities.

The Commission also attended a conference in the UK of registration authorities in the British Isles and in Gibraltar.
Operations

The Operations Division is responsible for the day-to-day administration and running of the Commission. Its activities fall under three main headings - finance, human resources including training, and information technology. It also provides a Secretariat function for the Board.

Finance and administration

The Commission’s Statement of Income and Expenditure for the year ended 31 March 2008 and the Report of the Auditors are set out in Appendix F.

The Commission is an independent statutory body with its own Board of Commissioners and management. It is also part of the centralised Government accounting system. The Commission’s income and expenditure account is part of the Government’s general revenue account and as such all fees are received by Government. Expenditure is drawn against a budget agreed annually with Treasury. Accordingly, any surplus forms part of general revenue and is not retained by the Commission.

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

Compared to the financial year 2006/07 income has increased by over £5.3 million which relates to the collection by the Commission of the Corporate Charge referred to on page 45. There was an overall shortfall in budgeted income of just over £1,000,000. This related to a reduction in receipts within Companies Registry.

The Commission has remained within its expenditure budget for the year 2007/08 with additional costs being incurred in advertising and postage. There is also an outstanding rent review on the Commission’s office accommodation which is being negotiated by the Department of Local Government & the Environment.

The Chief Executive’s Committee, which meets weekly (see Appendix D), reviews monthly financial reports prepared by the Operations Division on the Commission’s current financial performance against budget together with the forecast of the year end position.

The system which supports administration of the Commission’s finances is a newly implemented central Government accounting system, AXAPTA. This system is being further developed to provide management information reports to enhance financial oversight.

The Commission has leased outside storage space to store its documents, in particular companies’ files from Companies Registry. A review has commenced of Commission’s policy on document retention, archiving and destruction and risks to assist to plan for its requirements going forward.

The Commission’s social and recreational committee arranged an active programme of events. These are important occasions to foster a strong team spirit among staff, and families are invited to a number of the gatherings.

One of the ways in which the Commission supports the local community is through the raising of money for charity. During the year the Commission’s staff participated in a number of fund raising initiatives, both within and outside the Commission, which raised a total of £5,663.10. This was a record amount for the Commission and the money was distributed to three main charities chosen by the staff.

Human resources

The total headcount of the Commission at the end of the period (including unfilled vacancies) was 63.5 full time employees but this excludes contract headcount permitted outside the Government approved headcount establishment. This figure is unchanged on the previous period. The Commission’s headcount is controlled centrally by Government and has been increased to 66.5 full time employees with effect from 1 April in addition to contract headcount.

During the period the Commission encountered a higher than usual turnover of staff at 20.4%, mainly in the middle management grades. However this should be seen in the context of considerable stability in the previous recent years.
The Commission is keen to attract, develop and retain good staff. However it also has to accept that younger people who join the Commission to gain regulatory experience often in conjunction with a professional qualification, may wish to go on to develop their careers in the wider market place. It is interesting to note that these same staff sometimes later apply to rejoin the Commission.

The higher turnover of staff prompted the Board to conduct an independent review of salaries, to see how they compared to the market price of equivalent roles in the private sector. The Commission mainly recruits from (and loses staff to) the private sector, and therefore a market comparison is an important benchmark to help retain personnel.

An important part of the review was to take into account the total value of the Commission’s remuneration package against comparable positions externally. While the Commission cannot offer an extensive benefits package as sometimes found in industry, it does provide generous pension arrangements as well as a degree of job security. These are important benefits to factor into any comparison.

As a result of this exercise some salaries were adjusted to bring them more into line with market levels. However this was done without changing the basic framework which the Commission had previously agreed as a basis for rewarding performance.

During the period the average sickness absence per employee was 5.3 days (3.3 days in the previous year).

Within the executive of the Commission there is a Personnel Committee which meets quarterly or on an as-needed basis. Initiatives pursued by the Committee during the period included:

- Changes to employment contracts and HR policies, to comply with new employment legislation which was effective from 1 October 2007
- Changes to superannuation arrangements for new FSC appointees following changes to the Civil Service Pension scheme to which the Commission’s scheme is analogous
- A review of the performance management annual appraisal process
- An analysis of exit interviews conducted when people leave the Commission
- Long service awards
- Whistleblowing policy
- The creation of a self contained training room
- A continued review of the pandemic flu contingency plan, with associated preparations.

The Commission conducted an annual review and upgrade of its health and safety risk register. This involved reviewing the current risks and whether there were changes to these and also identifying any new risks that may have arisen.

The Commission participated in the Isle of Man Careers Convention. As part of its recruitment strategy the Commission aims to hire persons who have recently qualified at degree level. Being able to put on display the opportunities which it offers is an important part of promoting career options at an early stage.

Learning and development

The Commission places a high priority on the learning and development opportunities which it offers its staff. These comprise financial and study leave support for professional qualifications, internal training and soft-skill development, and external and off-island attendance at seminars and courses.

A review of the Commission’s learning and development strategy took place in 2007 and some refinements were made to this. The overall benchmark for attendance on training days per employee per annum remains at the current level of ten days and during the year we met 91% of the target. Meanwhile the average training spend per employee during the period was £1,184 (£1,050 in the previous year).

The Commission conducted an extensive programme of internal training sessions, which included the following topics:

- The Commission’s business continuity plan
- Changes to the general licensing policy
- Corporate Governance within the Commission and the role of Risk and Internal Control Committee
- Data protection
- Prevention of money laundering and countering the financing of terrorism.
An evaluation of the previous year’s learning and development programme was undertaken, especially in the light of the key management competencies perceived to be critical for improving the Commission’s management capability.

As a result a new learning and development programme has been agreed which is provided by external training providers and includes the following subjects:

- Negotiation skills
- Communication
- Dealing with conflict situations
- Problem solving
- Expert witness
- Report writing
- Advanced management and leadership skills.

The Commission supported eight staff in their study towards professional qualifications during the year. These qualifications include:

- Securities & Investment Institute Diploma
- International Diploma in Anti-Money Laundering
- International Diploma in Compliance
- STEP International Diploma in Trustee Investment & Financial Appraisal
- CIPD Professional Assessment Programme
- International Diploma in Financial Administration.

The following table summarises the qualifications and experience now held by the Commission’s managers and above including Commissioners:

<table>
<thead>
<tr>
<th>Qualifications</th>
<th>Staff</th>
<th>Commissioners</th>
</tr>
</thead>
<tbody>
<tr>
<td>Masters Degree</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>Undergraduate Degree</td>
<td>19</td>
<td>2</td>
</tr>
<tr>
<td>Professional Qualification:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>ICSA</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>STEP</td>
<td>-</td>
<td>1</td>
</tr>
<tr>
<td>Legal</td>
<td>3</td>
<td>2</td>
</tr>
<tr>
<td>Accountancy</td>
<td>2</td>
<td>1</td>
</tr>
<tr>
<td>ACIB</td>
<td>3</td>
<td>1</td>
</tr>
<tr>
<td>FPC</td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td>-</td>
<td></td>
</tr>
</tbody>
</table>

No. of years of business, professional & financial services experience: 716 228

The Commission has continuing recognition from Investors In People, underlining its commitment to the IIP principles. As part of this commitment the Commission conducted staff surveys on communication, on learning and development and on team building. Improvement plans were implemented as a result. In addition self-assessments were conducted as part of an ongoing self-discipline to examine how each Division rated itself on meeting the IIP principles.

The Commission will be assessed against the IIP Profile model in June 2008.

Information technology

The Commission has embraced technology at all levels of its operations, and has a high dependency in this area. Companies Registry, in particular, is wholly dependent on its database and web-based access to company records and its users for on-line document purchasing.

The Board of the Commission commissioned a major review of IT strategy. A number of factors contributed to the need for this review:

- The risks which the dependency on IT is creating for the Commission’s operations, and a need to evaluate how they are being mitigated
- The need to push ahead with an ambitious development programme to ensure that the Commission’s services (especially in Companies Registry) remain internationally competitive
The difficulties arising for the Commission from being part of the Government’s centralised computer operations, and the lack of control which the Commission has over its computer systems including in relation to licenceholder data

• A wish to undertake a cost benefit analysis of different strategic options going forward

• A need to segregate the Commission’s statistical and prudential database from the rest of Government to ensure that its security is maintained at all times.

An independent report was commissioned to assist the Board in deciding on its options, which include a measure of securing much greater independence from the Government’s system. The report was considered by the Board in March 2008 and a more detailed consideration of the risks further occurred after the end of the period.

One consequence of the difficulties encountered by the Commission with the development of its technology was that it had to delay the testing and release of further phases for its 2006 companies database. Only recently has the Commission been able to acquire the necessary new hardware and establish an appropriate test environment for new software releases developed by external suppliers.

The new strategy will also open the way for a new online document filing system and the online incorporation of companies. Migration of the existing public viewing system to the public internet viewing system will be facilitated which will reduce maintenance costs. A number of efficiencies are planned for the back office, notably the introduction of a new records management system.

The Commission surveyed users about their view of the Commission’s website. Apart from providing extensive information on the supervision of licensed entities together with relevant legislation and regulations, the website is the central portal through which the public can search company files and purchase documents which companies have filed.

The results of the survey helped the Commission to undertake a major upgrade of its website. The user-experience has been enhanced from the suggestions received, and information can be more easily accessed. Positive feedback has been received.

The Commission had 843,680 visits to its web-site an increase of 21% on the previous year: 37% of the visits are from Europe and 21% from North America.

The Commission has prepared a comprehensive business continuity plan which covers all aspects of the Commission’s operations. A key part of that plan relates to information technology.

The Commission has acquired the use of offsite accommodation to be used in the event of a disaster. Testing of systems in this accommodation was carried out as part of a six monthly check on preparedness.

As reported on page 20, the Commission has drawn up a comprehensive register of the risks which it incurs in carrying out its various functions. A number of the risks relate to information technology, and these were reviewed on a quarterly basis. Within the Risk and Impact Register, areas where risk reduction measures have been taken are identified. These measures included resilient system solutions, established service level agreements and support contracts with software and hardware providers and alternative processing arrangements. However, as the Commission is connected to the Government infrastructure system impact that arises from the Government network is outside the Commission’s control and therefore there are limitations on the extent of risk reduction measures that can be implemented.

Statistical and prudential data is submitted to the Commission by licenceholders through the Commission’s on-line financial reporting system. Institutions can log into a specially provided and secure network to upload the relevant data and information. The Commission maintained a regular dialogue with users of the system during the period, as a result of which a number of common issues were addressed.

An “IT Committee” of the executive met quarterly during the period. Proposals considered included:

• Further development of the 2006 companies database including automated workflow

• Software replacement for document imaging and retention in Companies Registry and for the operation of the till

• Upgrading of scanners

• Further development of the Supervision database

• Use of mobile working

• Amendments to the information security policy

• Mainframe migration

• Automation of the vetting process.

There was a notable increase in the users of the public view internet system with an increase of 20% in documents purchased (93,271) over the previous year. Most popular documents relate to change in director/secretary and annual returns.

The Commission has prepared a comprehensive business continuity plan which covers all aspects of the Commission’s operations. A key part of that plan relates to information technology.

The Commission has acquired the use of offsite accommodation to be used in the event of a disaster. Testing of systems in this accommodation was carried out as part of a six monthly check on preparedness.

As reported on page 20, the Commission has drawn up a comprehensive register of the risks which it incurs in carrying out its various functions. A number of the risks relate to information technology, and these were reviewed on a quarterly basis. Within the Risk and Impact Register, areas where risk reduction measures have been taken are identified. These measures included resilient system solutions, established service level agreements and support contracts with software and hardware providers and alternative processing arrangements. However, as the Commission is connected to the Government infrastructure system impact that arises from the Government network is outside the Commission’s control and therefore there are limitations on the extent of risk reduction measures that can be implemented.

Statistical and prudential data is submitted to the Commission by licenceholders through the Commission’s on-line financial reporting system. Institutions can log into a specially provided and secure network to upload the relevant data and information. The Commission maintained a regular dialogue with users of the system during the period, as a result of which a number of common issues were addressed.

An “IT Committee” of the executive met quarterly during the period. Proposals considered included:

• Further development of the 2006 companies database including automated workflow

• Software replacement for document imaging and retention in Companies Registry and for the operation of the till

• Upgrading of scanners

• Further development of the Supervision database

• Use of mobile working

• Amendments to the information security policy

• Mainframe migration

• Automation of the vetting process.

The Order provides for the establishment and constitution of a statutory body under the name of the “Financial Supervision Commission” whose functions include taking steps leading to the effective supervision of the financial sector of the Isle of Man.

The Order came into operation on 12 July 1983, when it was approved by Resolution of Tynwald.

The main functions of the Commission include:

(i) The licensing and supervision of banks under the Banking Act 1998

(ii) The licensing and supervision of investment businesses under the Investment Business Acts 1991 to 1993

(iii) The authorisation and regulation of collective investment schemes under the Financial Supervision Act 1988

(iv) The authorisation and supervision of building societies pursuant to Sections 2 and 4(A) of the Building Societies Act 1986

(v) The licensing and supervision of fiduciaries under the Fiduciary Services Acts 2000 and 2005, and

(vi) The registration of companies and the registration of documents required to be filed under the Companies Acts 1931 - 1993 and related legislation.

To fulfil its Mission, the Commission will:

(i) Set and publish standards designed to:
   a) Protect investors’, depositors’ and fiduciary clients’ interests
   b) Promote the financial stability of financial institutions
   c) Promote the highest standards of competence and professional qualification
   d) Protect the integrity of the financial community.
   e) Protect the reputation of the Isle of Man

(ii) Monitor compliance with the standards, taking prompt action where necessary

(iii) Take steps to investigate and where appropriate prosecute those engaged in unlicensed investment, banking or fiduciary business

(iv) Co-operate with other regulators and play an integral role in the development of international regulatory standards

(v) Provide consistent delivery of a high level of service within the Companies Registry

(vi) Assist Government in reviewing and promoting legislation relevant to the financial services industry, and

(vii) Seek the participation and support of the industry in achieving its objectives.
Membership of the Financial Supervision Commission

The Financial Supervision Commission Order 1983, as amended, states that “the Commission shall consist of not less than three persons appointed by the Treasury, subject to the approval of Tynwald”. The Treasury have appointed the following persons to be members of the Commission:

Rosemary Penn MBE (Chairman)

John Cashen OBE (Deputy Chairman)

John Aspden
Appointed as Chief Executive of the Commission in August 1998. Commenced his career for 15 years with the Bank of England including three years on secondment to the Council for the Securities Industry. Then became adviser to the Commissioner of Banking in Hong Kong. Subsequently held a senior position at International Bank of Asia Limited and was then Managing Director of Matheson InvestNet Limited, both also in Hong Kong.

Tim Cullen
Appointed June 2001. Spent 21 years with the World Bank, where he served inter alia as Chief Spokesman of the Bank and, latterly, as Senior Advisor for External and United Nations Affairs. He is an Associate Fellow of the Said Business School at the University of Oxford, where he directs the Oxford Programme on Negotiation. He also heads an international consulting firm in Oxford that focuses on issues of governance, integrity and the environment. In 2007 he was appointed a trustee of the Institute of Business Ethics.

Geoff Karran
Appointed in July 2007. Admitted to the Manx Bar in 1969 and during his time as an Advocate he became Senior Partner in Dickinson Cruickshank and served for three years as President of the IOM Law Society. Retired from practising Law in February 2007. He continues as Chairman of the DHSS Social Security Appeals Tribunal and the Disability Appeals Tribunal. Appointed Deputy Police Complaints Commissioner in March 2008.

Alan Smith
Appointed July 2007. Initial career with Lloyds Bank Trust Division and then spent seven years as Manager of Bank of Bermuda’s Cayman operations. Moved to Isle of Man in 1987 and was appointed Managing Director of Bank of Bermuda in 1994. Appointed to the Global Board of the Bank’s Fund Services Division in 2001 as Global Head of Marketing and Strategy and subsequently of HSBC’s Alternative Fund Services Division up to his retirement in 2005. He has over 36 years’ experience in Trust Administration, Corporate Services, Banking, Custody and Fund Administration.

Bryan Stott
Appointed in June 2001. Initially his career focussed mainly on the Island’s property business. In 1973 he was appointed to the Board of the Isle of Man Bank Limited and became Chairman in 1980. Has 28 years’ banking experience with the Isle of Man Bank and subsequently NatWest Offshore Limited. Retired as Chairman of NatWest Offshore Limited in 2000. Mr Stott also has extensive experience in the investment and insurance field.
The purpose of this Appendix is to describe how the Commission operates through a structured approach to its operations.

Statutory Board

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

The Commission’s Mission Statement

“To protect the public interest by providing effective regulation and supervision within the Island’s financial services sector; to support a competitive environment in which quality products and services are promoted for the economic benefit of the Island, and to foster good working relationships within the business community.”

The Commission’s regulatory and supervisory role extends to the banking, investment, funds and fiduciary sectors. In addition Companies Registry forms part of the Commission, and the Commission has delegated powers under the Companies Acts.

Members of the Commission

Appointments to the Board of Commissioners are approved by Tynwald.

At the time of a national election all Commissioners, as Members of a Statutory Board, automatically retire. New Commissioners, which may include those previously appointed, are then chosen. On the last occasion and following a new procedure, the Government issued a public invitation for persons to apply to be appointed as Members of Statutory Boards including the Commission. The remuneration paid to Members of Statutory Boards is set down by Order.

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

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

Conflicts of interest

The Board of Commissioners benefits from having members who have broad, up-to-date commercial and compliance experience. Inevitably this means that from time-to-time conflicts of interest may arise in dealing with particular issues. A Code of Conduct has been drawn up to cover these situations. The Code provides for the prior disclosure of interests and sets down how they should be handled. Commissioners are required to absent themselves from decisions where they may be conflicted. Staff also have to disclose their conflicts of interests. The code is published on the Commission’s website together with a list of current directorships.

Meetings of the Board

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

During the period the Board met for -
12 routine monthly meetings
13 licensing meetings (quorum)
A significant number of other ad hoc meetings.

Delegated authorities

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

- Changes in licence conditions attached to a licence
- Extensions to licences to include new schemes etc.
- Surrender of lapsed licences
- Restructure of organisations/sale or merger of licenceholders
- Approving recognition of schemes under Section 13 of the Financial Supervision Act.

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

The Executive

The Executive management team is structured as follows:

- The Chief Executive, also a Commissioner
- Heads of Division
- Senior Managers
- Managers

There are five Divisions within the Commission comprising Authorisations and Enforcement, Operations, Policy, Supervision and Companies Registry. An organisation chart is set out in Appendix C.
Accountability and scrutiny

The Commission is accountable and subject to scrutiny in the following areas:

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

In addition the Commission’s regulatory and supervisory approach is subject to ongoing review by standard-setting organisations including the International Monetary Fund and the FATF. The Island’s designated territory status (which effectively permits the distribution of Isle of Man authorised funds within the UK) is also subject to ongoing review by HM Treasury in the UK.

Appeals against decisions of the Commission

The key decisions of the Commission, including in relation to licensing, are subject to review by a committee established by the Council of Ministers. Tynwald has approved the Financial Services Review Regulations 2001 governing this committee and a panel of persons has been nominated by the Council of Ministers from which it may select individuals to hear a particular case.

Finance

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

As at 31 March 2008, the number of institutions licensed or authorised by the Financial Supervision Commission were as follows:

(i) Banking licences issued under Section 6 of the Banking Act 1998, as amended  \( \text{41} \)

(ii) Building Society authorisations issued under Sections 2 and 4(A) of the Building Societies Act 1986 \( \text{3} \)

(iii) Fiduciary Service Providers

(a) Corporate Service Providers
   - Category 1 \( \text{174} \)
   - Category 2 \( \text{11} \)

(b) Trust Service Providers
   - Trust Corporations \( \text{13} \)
   - Category 1 \( \text{103} \)
   - Category 2 \( \text{4} \)

(iv) Investment Business licences issued under Section 3 of the Investment Business Act 1991 \( \text{87} \)

In total 436 authorisations under categories (i) to (iv) were current, and these had been granted to 312 licensed entities.

(v) Collective Investment Schemes

a) Authorised under Section 3 of the Financial Supervision Act 1988 \( \text{8} \)
b) International within the meaning of Section 11 of the Financial Supervision Act 1988 \( \text{20} \)
c) Professional investor funds \( \text{9} \)
d) Experienced investor funds \( \text{133} \)
e) Recognised under Section 12 of the Financial Supervision Act 1988 \( \text{24} \)
f) Recognised under Section 13 of the Financial Supervision Act 1988 \( \text{8} \)
g) Overseas Funds notified under the Financial Supervision (Overseas Funds) (Exemption) Order 2003 \( \text{140} \)
Statement of responsibilities in respect of the Chief Executive’s report and the accounts

The Chief Executive is responsible for preparing the Chief Executive’s Report and the accounts in accordance with applicable law and regulations.

The Audit Act 2006 requires the Commission to prepare accounts for each financial year, which meet the requirements of the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006. The regulations require the Commission to prepare the accounts in accordance with UK Accounting Standards, as modified by the Audit Directions 2008.

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

In preparing these accounts, the Commission is required to:

- select suitable accounting policies and then apply them consistently
- make judgements and estimates that are reasonable and prudent
- state whether applicable UK Accounting Standards have been followed, as modified by the Audit Directions 2008, subject to any material departures disclosed and explained in the accounts, and
- prepare the accounts on the going concern basis unless it is inappropriate to presume that the Commission will continue in operation.

The Commission is responsible for keeping proper accounting records that disclose with reasonable accuracy at any time the financial affairs of the Commission and to enable them to ensure that the accounts comply with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Commission and to prevent and detect fraud and other irregularities.
Report of the Independent Auditors, KPMG Audit LLC, to the Isle of Man Financial Supervision Commission

We have audited the accounts of the Isle of Man Financial Supervision Commission for the year ended 31 March 2008 which comprise the Income and Expenditure Account and the related notes. These accounts have been prepared under the accounting policies set out therein.

This report is made solely to the Commission, as a body, in accordance with section 6 of the Audit Act 2006. Our audit work has been undertaken so that we might state to the Commission those matters we are required to state to them in an auditor’s report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Commission, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Commission and Auditors

The Commission’s responsibilities for preparing the accounts in accordance with applicable laws and regulations and UK Accounting Standards (UK Generally Accepted Accounting Practice), as modified by the Audit Directions 2008, are set out in the Statement of Responsibilities on page 59.

The Audit Directions 2008 modify UK Generally Accepted Accounting Practice by:

- allowing fixed assets to be expensed in the year incurred, except for advances made from the Consolidated Loans Fund, and amending the application of Financial Reporting Standards 10 (Goodwill and Intangible Assets), 11 (Impairment of Fixed Assets and Goodwill) and 15 (Tangible Fixed Assets) and Statements of Standard Accounting Practice 19 (Accounting for Investment Properties) and 21 (Accounting for Leases and Hire Purchase Contracts);
- defining all matters relating to superannuation schemes as defined contribution schemes for the purposes of FRS 17 (Retirement Benefits) and SSAP 24 (Accounting for Pension Costs);
- defining who is a related party, which transactions require disclosure and which transactions are exempt from disclosure requirements, and removing the requirement to comply with FRS 8 (Related Party Disclosures).

Our responsibility is to audit the accounts in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the accounts give a true and fair view and are properly prepared in accordance with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006.

In addition we report to you if, in our opinion, the Commission has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding related party transactions with the Commission is not disclosed.

We read the Chief Executive’s Report and any other information accompanying the accounts and consider the implications for our report if we become aware of any apparent misstatements or inconsistencies within it. Our responsibilities do no extend to any other information.

We review whether the Statement of Internal Control prepared by the Commission reflects compliance with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006. We report if the statement is misleading or inconsistent with other information we are aware of from our audit of the accounts. We are not required to consider, nor have we considered, whether the Statement on Internal Controls covers all risks and controls.

Basis of opinion

We conducted our audit in accordance with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006 and International Standards on Auditing (UK and Ireland) issued by the UK Auditing Practices Board. An audit includes examination, on a test basis, of evidence
relevant to the amounts and disclosures in the accounts. It also includes an assessment of the significant estimates and judgments made by the Commission in the preparation of the accounts, and of whether the accounting policies are appropriate to the Commission’s circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the accounts are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the accounts.

Opinion

In our opinion:

• the accounts give a true and fair view, in accordance with UK Generally Accepted Accounting Practice as modified by the Audit Directions 2008, of the Commission’s income and expenditure for the year ended 31 March 2008

• the accounts have been properly prepared in accordance with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006, and

• the information given in the Chief Executive’s Report is consistent with the accounts.

KPMG Audit LLC
Chartered Accountants
## Income and Expenditure Account for the year ending 31 March 2008

<table>
<thead>
<tr>
<th>Income</th>
<th>Notes</th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>£</td>
<td>£</td>
</tr>
<tr>
<td>Licence &amp; Scheme Fees</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Banking</td>
<td>681,667</td>
<td>722,300</td>
<td></td>
</tr>
<tr>
<td>Investment Business</td>
<td>186,965</td>
<td>176,783</td>
<td></td>
</tr>
<tr>
<td>Fund Managers</td>
<td>156,017</td>
<td>138,832</td>
<td></td>
</tr>
<tr>
<td>Collective Investment Schemes</td>
<td>99,988</td>
<td>76,350</td>
<td></td>
</tr>
<tr>
<td>Fiduciary Service Providers</td>
<td>463,990</td>
<td>385,358</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>1,588,627</td>
<td>1,499,623</td>
</tr>
<tr>
<td>Companies Registry</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Resident Company</td>
<td>298,428</td>
<td>1,537,810</td>
<td></td>
</tr>
<tr>
<td>Companies Registration Fees</td>
<td>10,038,310</td>
<td>3,372,715</td>
<td></td>
</tr>
<tr>
<td>Companies Capital Fees</td>
<td>552,395</td>
<td>812,262</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>10,889,133</td>
<td>5,722,787</td>
</tr>
<tr>
<td>Other</td>
<td></td>
<td>131,596</td>
<td>77,891</td>
</tr>
<tr>
<td>Total Income</td>
<td>1(b)</td>
<td>12,609,356</td>
<td>7,300,301</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Expenditure</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>£</td>
<td>£</td>
</tr>
<tr>
<td>Salaries</td>
<td>3</td>
<td>2,495,067</td>
<td>2,408,287</td>
</tr>
<tr>
<td>Commissioners’ Remuneration</td>
<td></td>
<td>85,998</td>
<td>88,631</td>
</tr>
<tr>
<td>Premises</td>
<td></td>
<td>459,789</td>
<td>449,419</td>
</tr>
<tr>
<td>Training</td>
<td></td>
<td>71,417</td>
<td>60,493</td>
</tr>
<tr>
<td>Travel</td>
<td></td>
<td>59,459</td>
<td>51,823</td>
</tr>
<tr>
<td>Professional Fees</td>
<td></td>
<td>178,973</td>
<td>77,056</td>
</tr>
<tr>
<td>Operating expenses</td>
<td></td>
<td>166,093</td>
<td>141,075</td>
</tr>
<tr>
<td>Information technology</td>
<td></td>
<td>360,140</td>
<td>657,569</td>
</tr>
<tr>
<td>Secondments</td>
<td></td>
<td>19,544</td>
<td>(20,362)</td>
</tr>
<tr>
<td>Other</td>
<td></td>
<td>1,076</td>
<td>109</td>
</tr>
<tr>
<td>Total Expenditure</td>
<td>1(c), 2</td>
<td>(3,897,556)</td>
<td>(3,914,100)</td>
</tr>
<tr>
<td>Surplus for the year</td>
<td>1(a)</td>
<td>8,711,800</td>
<td>3,386,201</td>
</tr>
</tbody>
</table>

The notes on pages 63 to 65 form part of these accounts.
The income and expenditure account was approved by the Financial Supervision Commission on the 6 June 2008 and signed on its behalf by: Mrs R V Penn (Chairman) and Mr J R Aspden (Chief Executive and Commissioner).
Notes to the accounts for the year ended 31 March 2008

1. Accounting policies

a) Basis of accounting

The Isle of Man Financial Supervision Commission is constituted under the Financial Supervision Commission Order 1983 as a Statutory Board of Tynwald. The income and expenditure account is part of the general revenue account of the Isle of Man Government. Accordingly, any surplus for the year forms part of general revenue and is not retained by the Commission.

These are the first accounts which have been prepared in accordance with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006. They are also the first accounts which have been prepared in accordance with accounting principles generally accepted in the United Kingdom (“UK GAAP”), as modified by the Audit Directions 2008, and in accordance with the Isle of Man Statement of Recommended Practice 2007 on accounting for entities subject to the Audit Act 2006 (“the SORP”), to the extent applicable to the Commission.

Consequently, prior year comparatives shown in the income and expenditure account have been restated to comply with the Accounts and Audit Regulations 2007 to 2008 and the Audit Directions 2008, made under the Audit Act 2006, UK GAAP as modified by the Audit Directions 2006, and the SORP. The effect of the restatement is shown in note 11.

b) Income

Income is accounted for on an accruals basis. Amounts due to the Commission at year end but not yet received are included within income, less any provision for non-recoverable amounts. Provisions for non-recoverable amounts include an estimate of specific fees unlikely to be received and a general provision of 25% of other debtors.

c) Expenditure

Expenditure is accounted for on an accruals basis. Amounts properly incurred during the year but not yet paid are included within expenditure. Pursuant to the Audit Directions 2008 the Commission has elected to include within expenditure the cost of fixed assets, not being made from the Consolidated Loans Fund of the Isle of Man Government. Consequently the following Financial Reporting Standards do not apply:

- FRS 10 – Goodwill and Intangible Assets
- FRS 11 – Impairment of Fixed Assets and Goodwill
- FRS 15 – Tangible Fixed Assets
- SSAP19 – Accounting for Investment Properties
- SSAP21 – Accounting for Leases and Hire Purchase Contracts

d) Pensions

The Commission’s employees are members of the Financial Supervision Commission Superannuation Scheme 1983 which is analogous to the Principal Civil Service Scheme, which is funded from central Treasury and Isle of Man Government reserves. No payments have been made to the Scheme by the Commission.

e) Related parties

The requirements of FRS 8 – Related Party Disclosures have been replaced by the requirements of the Audit Directions 2008, which define who are related parties and the transactions which require disclosure in the accounts.

f) Balance sheet

The Commission is a statutory board of the Isle of Man Government and does not hold any assets or liabilities in its own name. Accordingly, an independent Balance Sheet does not form part of the Accounts. A statement of current assets and liabilities attributable to the normal operations of the Commission is included in the notes to the Accounts.
2. Auditors’ remuneration

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

3. Salaries

Remuneration of members, officers and employees of the Commission are payable within the following bands:

4. Debtors

The following have been adjusted for within the income and expenditure account:

5. Prepayments

The following have been adjusted for within the income and expenditure account:

6. Accruals

The following accruals have been included within expenditure:

<table>
<thead>
<tr>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>£</td>
<td></td>
</tr>
<tr>
<td>Accrued expenditure</td>
<td>63,601</td>
</tr>
</tbody>
</table>

7. Operating lease commitments

The Commission has the following rental lease commitments expiring:

<table>
<thead>
<tr>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td>£</td>
<td></td>
</tr>
<tr>
<td>Within 12 months</td>
<td>372,440</td>
</tr>
<tr>
<td>Between 1 and 5 years</td>
<td>1,794,878</td>
</tr>
<tr>
<td>After 5 years</td>
<td>3,117,420</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>5,284,738</strong></td>
</tr>
</tbody>
</table>

8. Segmental reporting

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

9. Related party disclosures

There were no related party transactions requiring disclosure in the accounts.
10. Commitments and contingencies

The Commission had committed to or planned to make the following expenditures at year end:

<table>
<thead>
<tr>
<th></th>
<th>2008</th>
<th>2007</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£</td>
<td>£</td>
</tr>
<tr>
<td>Premises</td>
<td>2,026</td>
<td>19,869</td>
</tr>
<tr>
<td>Training</td>
<td>3,775</td>
<td>-</td>
</tr>
<tr>
<td>Travel</td>
<td>4,319</td>
<td>-</td>
</tr>
<tr>
<td>Professional fees</td>
<td>82,905</td>
<td>100,000</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>10,004</td>
<td>6,360</td>
</tr>
<tr>
<td>Information technology</td>
<td>622,801</td>
<td>488,175</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>725,830</td>
<td>614,404</td>
</tr>
</tbody>
</table>

11. Restatement of comparatives

<table>
<thead>
<tr>
<th></th>
<th>As per 2007 signed accounts</th>
<th>Adjustment</th>
<th>Restated balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>£</td>
<td>£</td>
<td>£</td>
</tr>
<tr>
<td>Income</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Licence &amp; Scheme Fees</td>
<td>1,499,623</td>
<td>-</td>
<td>1,499,623</td>
</tr>
<tr>
<td>Companies Registry</td>
<td>5,670,255</td>
<td>52,532</td>
<td>5,722,787</td>
</tr>
<tr>
<td>Other</td>
<td>77,891</td>
<td>-</td>
<td>77,891</td>
</tr>
<tr>
<td>Total Income</td>
<td>7,247,769</td>
<td>52,532</td>
<td>7,300,301</td>
</tr>
<tr>
<td>Expenditure</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Salaries</td>
<td>2,366,287</td>
<td>42,000</td>
<td>2,408,287</td>
</tr>
<tr>
<td>Commissioners’ Remuneration</td>
<td>88,631</td>
<td>-</td>
<td>88,631</td>
</tr>
<tr>
<td>Premises</td>
<td>463,795</td>
<td>(14,376)</td>
<td>449,419</td>
</tr>
<tr>
<td>Training</td>
<td>36,293</td>
<td>24,200</td>
<td>60,493</td>
</tr>
<tr>
<td>Travel</td>
<td>51,823</td>
<td>-</td>
<td>51,823</td>
</tr>
<tr>
<td>Professional Fees</td>
<td>34,191</td>
<td>42,865</td>
<td>77,056</td>
</tr>
<tr>
<td>Operating expenses</td>
<td>146,152</td>
<td>(5,077)</td>
<td>141,075</td>
</tr>
<tr>
<td>Information technology</td>
<td>492,448</td>
<td>165,121</td>
<td>657,569</td>
</tr>
<tr>
<td>Secondments</td>
<td>(21,562)</td>
<td>1,200</td>
<td>(20,362)</td>
</tr>
<tr>
<td>Other</td>
<td>109</td>
<td>-</td>
<td>109</td>
</tr>
<tr>
<td>Total Expenditure</td>
<td>3,658,167</td>
<td>255,933</td>
<td>3,914,100</td>
</tr>
<tr>
<td>Surplus for the year</td>
<td>3,589,602</td>
<td>(203,401)</td>
<td>3,386,201</td>
</tr>
</tbody>
</table>

The adjustments relate to the recording of income on an accruals basis, the removing of prepaid expenditure and the removing of expenditure accruals which had been approved but not yet incurred and which were previously recognised as expenditure when the expenditure was planned.
Legislation introduced from 1 April 2007 - 31 March 2008

Primary Legislation

Financial Services Bill 2007
Consolidates into a single Act the regulatory legislation relating to investment business, banking, and corporate and trust service providers. It also updates and replaces the legislative provisions relating to the Financial Supervision Commission’s functions and powers. The Bill was introduced into the Branches of Tynwald on 26.06.07 and it is anticipated that it will complete its progress through Tynwald and receive Royal Assent by the second half of 2008.

Collective Investment Schemes Bill 2008
Repeals and replaces with modifications the provisions of the Financial Supervision Act 1988 which relate to collective investment schemes and which will be the only remaining operative provisions of the 1988 Act following the enactment and commencement of the Financial Services Bill 2007. The primary aim of this Bill is to ensure that the legislative framework for schemes is transparent and appropriate to the different types of schemes that are established, promoted, managed or administered in or from the Island. The Bill was introduced into the Branches of Tynwald on 22.01.08 and it is anticipated that it will complete its progress through Tynwald and receive Royal Assent by the second half of 2008.

Order in Council
This is an Order made by the UK Government to extend its relevant legislation to the Isle of Man so that the UK’s Takeover Panel can continue to supervise takeovers and mergers involving relevant Isle of Man companies under the powers contained in the UK’s Companies Act 2006. Tynwald approved the making of this Order on 15.01.08. The Commission and the Attorney General’s Chambers are working with the UK’s Department for Business Enterprise and Regulatory Reform in respect of the necessary modifications to the UK’s legislation. When the Order is made, it will be laid before Tynwald. The making of this Order is outside the control of the Island and it is therefore not possible to estimate when it will be in operation.

Secondary Legislation

SD No 110/07 in operation 01.04.07. Banking (Fees) Regulations 2007. These Regulations prescribe an annual licence fee for banks. The Regulations also prescribe the fee that shall accompany applications for a banking licence, except where the application relates to group reorganisations. The Regulations also provide that banks carrying on investment business shall pay an additional fee dependent on the category of investment business undertaken.

SD No 111/07 in operation 01.04.07. Building Societies (Authorisation) (Fees) Regulations 2007. These Regulations specify the fees to be paid by a building society when it is first granted authorisation and for the continuation of its authorisation.

SD No 112/07 in operation 01.04.07. Collective Investment Scheme (Fees) Regulations 2007. These Regulations specify the fees payable in respect of the following collective investment schemes:
(a) schemes authorised under section 3 of the Financial Supervision Act 1988
(b) schemes recognised under sections 12 and 13 of the Financial Supervision Act 1988
(c) schemes which are international collective investment schemes within the meaning of section 11 of the Financial Supervision Act.

The Regulations do not require those international collective investment schemes which are professional investor funds or experienced investor funds to pay fees.

SD No 113/07 in operation 01.04.07. Fiduciary Services (Fees) Regulations 2007. These Regulations prescribe the annual licence fees payable by holders of the different classes (corporate service provider or trust service provider) and categories (Trust Corporation, Category 1 CSP, Category 1 TSP, Category 2 CSP or Category 2 TSP) of Fiduciary Services licences. The Regulations also prescribe the fees that shall accompany applications for the specified types of fiduciary services licences.

SD No 114/07 in operation 01.04.07. Investment Business (Fees) Regulations 2007. These Regulations prescribe the annual licence fees payable by certain holders of investment business licences. The Regulations also prescribe the fees that shall accompany applications for specified types of investment business licences.
SD No 155/07 in operation 06.04.07. Companies (Fees and Duties) (Amendment) Order 2007. This Order increased the annual return fee for a 1931 Act Company following the repeal of the Corporate Charge by Treasury. It also introduced an annual return filing fee for a foreign company registered under Part XI of the 1931 Companies Act.

SD No 156/07 in operation 06.04.07. Companies (Fees, Duties and Penalties) (Amendment) Regulations 2007. This Order increased the annual return fee for a 2006 Act Company following the repeal of the Corporate Charge by Treasury.

SD No 175/07 in operation 06.04.07. Companies (Annual Return) Regulations 2007. This Order amended the annual return form prescribed under the Companies Act 2006 to allow a company to claim relief from payment of the annual return fee.

SD No 176/07 in operation 06.04.07. Companies (Forms) Regulations 2007. This Order amended the annual return form prescribed under the Companies Act 1931 to remove reference to the non-resident company as this regime was repealed. It also amended the form to allow a company to claim relief from payment of the annual return fee and prescribed the form of the new annual declaration for a foreign company.

SD No 713/07 in operation 29.08.07. The Companies Act 2006 (Appointed Day) (No.2) Order 2007. This Order brought into operation the provision in the Companies Act 2006 which repealed the whole of the Prevention of Fraud (Investments) Act 1988.

SD No 806/07 in operation 01.11.07. Financial Supervision (Experienced Investor Fund) (Exemption) (Amendment) Order 2007. This Order amends the Financial Supervision (Experienced Investor Fund) (Exemption) Order 1999. The effect of the Order is that from 1 November 2007 no new Experienced Investor Funds can be established. Existing EIFs have 18 months to become legacy EIFs, Qualifying Type EIFs or to close to new business.

SD No 807/07 in operation 01.11.07. Financial Supervision (Specialist Fund) (Exemption) Order 2007. This Order introduces the Specialist Fund: a fund with a minimum investment level of US$100,000 which is aimed at institutional and specialist investors.

SD No 808/07 in operation 01.11.07. Financial Supervision (Qualifying Fund) (Exemption) Order 2007. This Order introduces the Qualifying Fund: which is aimed at non retail qualifying investors.

SD No 848/07 in operation 23.11.07. Banking Business (Compensation of Depositors) (Amendment) Regulations 2007. These Regulations amend the schedule of names of institutions that are not participants in the scheme of compensation to protect depositors with banks licensed in the Isle of Man.

SD No 927/07 in operation 01.01.08. Banking (General Practice) Regulatory (Amendment) Code 2007. This Code amends the Banking (General Practice) Regulatory Code 2005 in respect of capital requirements, operational risk management policies and prudential reporting requirements for banks, to ensure effective implementation of the revised international capital adequacy standards commonly known as Basel II.

SD No 933/07 in operation 19.11.07. Investment Business Amendment Order 2007. This Order updates the Investment Business Order 2004 by clarifying the existing position for promoters of schemes which do not require a regulated promoter.


SD No 982/07 in operation 5.12.07. Financial Supervision Act 1988 (Definition of Collective Investment Schemes) (Amendment) Order 2007. This Order inserts subsections (6A) and (6B) into section 30 of the Financial Supervision Act 1988. Subsection (6A) specifies that limited partnerships formed under the law of the Island will not constitute a collective investment scheme if its interests are admitted to the Official List of the UK Listing Authority. Subsection (6B) defines “interests” for the purposes of subsection (6A) only.

SD No 983/07 in operation 5.12.07. Listed Limited Partnerships Regulations 2007. These Regulations have the effect of permitting limited partnerships to consist of more than 20 persons in cases where a limited partnership is formed under the law of the Island and its interests are admitted to the Official List of the UK Listing Authority.
Consultative Documents issued during 1 April 2007 - 31 March 2008

The following consultation documents were released under the proposed Financial Services Act.

<table>
<thead>
<tr>
<th>Title of Consultation</th>
<th>Date Consultation Published</th>
<th>Date Consultation Closed</th>
</tr>
</thead>
<tbody>
<tr>
<td>CAROL 4 – Consultation on the Financial Resources and Audit Requirements Chapters of the Rule Book</td>
<td>16 April 2007</td>
<td>22 June 2007</td>
</tr>
<tr>
<td>Regulation of Money Service Businesses</td>
<td>4 May 2007</td>
<td>17 June 2007</td>
</tr>
<tr>
<td>Further Consultation on the Financial Services Rule Book</td>
<td>4 December 2007</td>
<td>31 January 2008</td>
</tr>
<tr>
<td>Consultation on the regulation of Money Service Businesses including e-money providers</td>
<td>17 December 2007</td>
<td>8 February 2008</td>
</tr>
<tr>
<td>Further Consultation on the Regulated Activities Order and Exemption Regulations</td>
<td>17 January 2008</td>
<td>15 February 2008</td>
</tr>
</tbody>
</table>
Other Information

The Commission’s website www.fsc.gov.im contains useful information including an outline of the regulatory requirements covering all areas of its responsibility.

Online Handbooks are available through the website for:

Banks
Investment Services
Funds
Fiduciary Services

Each provides up-to-date searchable text explaining the Commission’s regulatory requirements and downloadable PDFs of the various legislation and regulations.

The following publications are available from the Isle of Man Government, Isle of Man Finance, Illiam Dhone House, Circular Road, Douglas, Isle of Man:

Isle of Man International Finance Centre
Isle of Man Financial Review (Quarterly Newsletter)
Flourish - Exclusive Lifestyles in the Isle of Man
Isle of Man Companies Act 2006
Space Business
Because you can - A world class opportunity for funds in the Isle of Man
Isle of Man Captives - the domicile of choice

Some of these publications can be downloaded from the Division’s website www.isleofmanfinance.gov.im.

The Isle of Man Government Insurance and Pensions Authority has published the following online Handbooks which may be accessed free of charge from their website www.gov.im/ipa:

Regulation of Insurance Business
Anti Money Laundering Standards for Insurance Businesses
Isle of Man International Centre for Insurance (Guidance Notes)
Regulation of Insurance Intermediaries (general business)
Retirement Benefits Schemes Act 2000

Telephone calls made to or from the Commission may be recorded or monitored.
<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
</tr>
</thead>
<tbody>
<tr>
<td>ACIB</td>
<td>The Association of Chartered Institute of Bankers</td>
</tr>
<tr>
<td>ACSP</td>
<td>Association of Corporate Service Providers</td>
</tr>
<tr>
<td>AIM</td>
<td>Alternative Investment Market</td>
</tr>
<tr>
<td>AIMA</td>
<td>Alternative Investment Management Association</td>
</tr>
<tr>
<td>BCCI</td>
<td>Bank of Credit &amp; Commerce International</td>
</tr>
<tr>
<td>BVI</td>
<td>British Virgin Islands</td>
</tr>
<tr>
<td>AML</td>
<td>Anti-Money Laundering</td>
</tr>
<tr>
<td>CAROL</td>
<td>Consolidation and Review of legislation</td>
</tr>
<tr>
<td>CFT</td>
<td>Countering the Financing of Terrorism</td>
</tr>
<tr>
<td>CIPD</td>
<td>Chartered Institute of Personnel &amp; Development</td>
</tr>
<tr>
<td>Commission</td>
<td>The Financial Supervision Commission</td>
</tr>
<tr>
<td>CSPs</td>
<td>Corporate Service Providers</td>
</tr>
<tr>
<td>DCS</td>
<td>Depositors' Compensation Scheme</td>
</tr>
<tr>
<td>ECB</td>
<td>European Central Bank</td>
</tr>
<tr>
<td>EIF</td>
<td>Experienced Investor Fund</td>
</tr>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
<tr>
<td>EU15</td>
<td>15 countries in the European Union before the expansion on 1 May 2004</td>
</tr>
<tr>
<td>FATF</td>
<td>Financial Action Task Force</td>
</tr>
<tr>
<td>FIS</td>
<td>Funds and Investments Services</td>
</tr>
<tr>
<td>FPC</td>
<td>Financial Planning Certificate</td>
</tr>
<tr>
<td>FSA</td>
<td>Financial Services Authority</td>
</tr>
<tr>
<td>FSC</td>
<td>Financial Supervision Commission</td>
</tr>
<tr>
<td>G7</td>
<td>Group of seven industrialised nations of the world formed in 1976</td>
</tr>
<tr>
<td>GFCI</td>
<td>Global Financial Centres Index</td>
</tr>
<tr>
<td>ICAAP</td>
<td>Individual Capital Adequacy Assessment Process</td>
</tr>
<tr>
<td>ICAEW</td>
<td>The Institute of Chartered Accountants in England and Wales</td>
</tr>
<tr>
<td>ICSA</td>
<td>Institute of Chartered Secretaries and Administrators</td>
</tr>
<tr>
<td>IIP</td>
<td>Investors in People</td>
</tr>
<tr>
<td>IMF</td>
<td>International Monetary Fund</td>
</tr>
<tr>
<td>IOSCO</td>
<td>International Organisation of Securities Commissions</td>
</tr>
<tr>
<td>Island</td>
<td>Isle of Man</td>
</tr>
<tr>
<td>JAMLAG</td>
<td>Joint Anti-Money Laundering Advisory Group</td>
</tr>
<tr>
<td>LLC</td>
<td>Limited Liability Company</td>
</tr>
<tr>
<td>NAV</td>
<td>Net Asset Value</td>
</tr>
<tr>
<td>MiFID</td>
<td>The Markets in Financial Instruments Directive</td>
</tr>
<tr>
<td>MMOU</td>
<td>Mutual Memorandum of Understanding</td>
</tr>
<tr>
<td>OGBS</td>
<td>Offshore Group of Banking Supervisors</td>
</tr>
<tr>
<td>STEP</td>
<td>The Society of Trust &amp; Estate Practitioners</td>
</tr>
<tr>
<td>TSPs</td>
<td>Trust Service Providers</td>
</tr>
<tr>
<td>UK</td>
<td>United Kingdom</td>
</tr>
<tr>
<td>US</td>
<td>United States</td>
</tr>
</tbody>
</table>
The theme of the photographs in this report is based around the Manx Triskelion. This pictorially demonstrates diversity, history (clockwise and anti-clockwise) and the Manx nationality.