

06/15***

Financial Services Authority

Reforming the Approved Persons regime

Including feedback
on CP05/10

August 2006



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This document contains two sets of proposals for consultation and a Feedback Statement. Each set of proposals has a different deadline for responses.

The Financial Services Authority invites comments on this Consultation Paper. Comments should reach us by:

- 9 November 2006 about our proposals in Chapter 3 section IV Markets in Financial Instruments Directive (MiFID) – impact and consultation.
- 23 November 2006 about our proposals in Chapter 3 section III Consultation on merging the customer functions.

The Feedback Statement reports on the feedback from respondents to our proposals in Consultation Paper 05/10 *Reviewing the FSA Handbook* (July 2005) to streamline the Approved Persons regime.

Please address any comments or queries to:

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Copies of this Consultation Paper are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

1 Overview

- 1.1 In July 2005 we published our Consultation Paper 05/10, Reviewing the FSA Handbook, (CP05/10) which set out our proposals to simplify the requirements we place on firms in respect of Money Laundering, Approved Persons and Training and Competence. We also outlined our plans to develop a new structure for our Conduct of Business (COB) rules. We were pleased by the number of responses received and would like to thank respondents for their contribution; a full list of non-confidential respondents can be found in Annex 1.
- 1.2 We published a Policy Statement (PS06/1)¹ in January 2006 about our proposals on Money Laundering and a Feedback Statement (FS06/1)² on Training and Competence in March 2006.
- 1.3 We are now able to issue our Feedback Statement on Approved Persons because the text of the Level 2 implementing measures (the implementing directive) of the Markets in Financial Instruments Directive³ (MiFID or the Directive) has been politically agreed.⁴ This gives us sufficient certainty to proceed with reforming the Approved Persons regime.

The Handbook Review programme

- 1.4 These proposals, together with our proposals in CP05/10, form part of our continuing plan to review our Handbook of Rules and Guidance (the Handbook) and are in line with our Guiding Principles (as set out in CP05/10) to make it as simple and accessible as possible, as well as to reduce the burden of regulation on all our stakeholders. We are aware of the cost of change for firms, so will focus future changes in areas where we can have real impact and where the benefits are clear.

1 www.fsa.gov.uk/pubs/policy/ps06_01.pdf.

2 www.fsa.gov.uk/pages/Library/Policy/CP/2006/fs06_01.shtml.

3 Directive 2004/39/EC of April 2004 amended by Directive 2006/31/EC of 5 April 2006.

4 Level 2 implementing measures were agreed by the European Parliament on 15 June 2006 and approved by the European Securities Commission on 26 June 2006. They have not yet been formally adopted.

- 1.5 We are mindful of the clear messages we received from CP05/10. So we will continue our work to make it easier to access and understand our regulatory requirements. And we will ensure firms continue to have an appropriate amount of guidance as we move towards a more principles-based approach to regulation.
- 1.6 We have also been very aware of the industry's concern that unnecessary, or untimely, changes would be made at a time when it is already facing major and unavoidable change to implement MiFID. So we have generally coordinated the timing for implementing our proposals in CP05/10 with MiFID. We will continue to take advantage of the opportunities to simplify our Handbook in the light of necessary changes to reflect directive implementation.
- 1.7 Our Handbook Review proposals are part of our wider programme on Better Regulation. Details of ongoing projects to simplify our Handbook and reduce the burden of regulation on firms are in our Better Regulation Action Plan, published on 2 December 2005⁵, and our Better Regulation Action Plan progress report, issued on 28 June 2006.⁶

Structure of this paper

- 1.8 This paper contains:
- feedback in relation to our proposals in Chapter 3 of CP05/10 on the Approved Persons regime;
 - further proposals for consultation on merging the customer functions into one generic customer function; and
 - consultation on the impact of MiFID on the Approved Persons regime.

The draft Handbook text

- 1.9 Appendix 1 sets out in full the Handbook text expected to be in place on 1 November 2007 for:
- the proposals we are taking forward from CP05/10;
 - the impact of MiFID; and
 - the proposal for merging the customer functions.

This will happen in two stages. In January 2007 we will make rules on implementing the proposals we are taking forward from CP05/10 and the impact of MiFID. In February 2007 we will make rules to merge the customer functions.

- 1.10 We believe it is easier to show all the changes in one document even though we have already consulted in CP05/10 on some of the draft Handbook text. While we are happy to accept further comments on the text already consulted on, please concentrate on the draft Handbook text relating to the proposals on which we are now consulting.

5 www.fsa.gov.uk/pubs/other/better_regulation.pdf.

6 www.fsa.gov.uk/pubs/other/2660_Action_plan.pdf.

Responding to the consultations in Chapter 3

- 1.11 Chapter 3 section III, ‘consultation on merging the customer functions’, is relevant to many authorised firms⁷. The consultation period for responses to this proposal is the standard 12 weeks and the deadline is 23 November 2006.
- 1.12 Chapter 3 section IV, ‘Markets in Financial Instruments Directive (MiFID) – impact and consultation’, is relevant to all firms within MiFID’s scope. MiFID has to be transposed by 31 January 2007 and, to ensure that responses are received in time to meet this deadline, the consultation period for MiFID is 10 weeks rather than the standard 12 weeks. The deadline for these responses is 9 November 2006.

Implementation

- 1.13 Our approach to implementation, with two exceptions⁸, is to bring in all the changes together – as endorsed by the feedback we received to CP05/10. The obvious date to choose is the MiFID implementation date of 1 November 2007.

Who should read this Consultation Paper?

- 1.14 This paper will be of particular interest to authorised firms and those applying for authorisation, as well as others involved in recruiting employees for controlled functions and in overseeing, developing and administering processes for complying with our Approved Persons regime.

Consumers

Except where we have a legal obligation under MiFID, the proposals in this paper will not reduce the scope of the Approved Persons regime, so there is no impact on our consumer protection objective.

Consumers may be interested in sections I, II, III and IV of Chapter 3, which outline our future approach to the Approved Persons regime.

7 We do not apply the customer functions to mortgage and general insurance firms.

8 See Chapter 3 section I on our approach to the annual reporting requirement for significant management functions and the sole trader function (CF7).

2 Key messages

Customer functions – feedback from CP05/10

- 2.1 We have assessed the feedback from CP05/10 and concluded that keeping customer functions for both the wholesale (or non-private) and retail markets is justified for the time being.
- 2.2 In response to industry feedback and in line with the Guiding Principles of our Handbook review, we are also consulting in Chapter 3 section III on merging the customer functions into one generic customer function, thereby simplifying the regime significantly.

Future scope of the customer functions

- 2.3 Our current approach to regulation is a combination of high-level principles and detailed rules and guidance. It will take time for us and the industry to deliver on our agenda for more principles-based regulation. We believe that principles-based regulation will provide greater flexibility for, and underline the responsibility of, firms and senior managers to determine how relevant regulatory outcomes can be achieved. As we and firms make progress on delivering this agenda we will look again at whether the customer functions continue to add value. This review will not be until 2009 at the earliest. If we decide there is no longer a case for customer functions, we will consult on this.

Future review of the Handbook provisions for approved persons

- 2.4 We shall be considering the messages about senior management responsibility in APER next year as part of a wider review of SYSC2. We will review the rest of the Handbook provisions when we review the customer functions.

The impact of MiFID

- 2.5 We propose to use the Approved Persons regime to implement certain MiFID provisions.

The recruitment and approvals process

- 2.6 Our requirements on firms when recruiting staff are set out in the Handbook⁹. We expect firms to perform their own due diligence before submitting an application to us to approve an individual.
- 2.7 Our vetting process is designed to complement firms' own recruitment practices and should not be viewed as a substitute by firms.
- 2.8 We expect senior management to assess, using a risk-based approach, which combination of checks including credit references, references from previous employees and criminal records checks are appropriate for a particular role. The industry should be aware that our standard vetting process on approved persons does not include criminal records checks, although we shall be arranging for such checks to be done in future on a sample basis. To underline the responsibility on firms and senior managers to carry out due diligence on prospective employees, and to highlight our policy on criminal records checks, we have amended SUP 10 Annex 1 Frequently Asked Questions G (see the amended text in Appendix 1).
- 2.9 We expect senior management to take responsibility for managing the risks in their firms properly and ensuring they have systems and controls to mitigate those risks. Failure to do so may result in disciplinary action against the individuals responsible as well as the firms.¹⁰

Cost savings

- 2.10 We estimate that implementing all the measures in this paper will provide annual savings of £3 million for the financial services industry.

9 SUP 10 Annex 1.

10 'Efficiency versus fairness', speech by Margaret Cole Director of FSA Enforcement, 16 June 2006.

3 Future scope of the Approved Persons regime

3.1 This chapter outlines our plans and proposals for the scope of the Approved Persons regime. It is divided into the following sections:

- **Section I** – Significant influence functions: the feedback from CP05/10, our response and planned approach.
- **Section II** – Customer functions: the feedback from CP05/10 and our response.
- **Section III** – Consultation on merging the customer functions.
- **Section IV** – Markets in Financial Instruments Directive (MiFID) – impact and consultation: how we plan to implement the Directive.
- **Section V** – Cost benefit analysis and compatibility statements

Consultation

3.2 We include proposals for consultation and we encourage you to respond about our proposals on

- merging the customer functions; and
- implementing MiFID.

3.3 Because CP05/10 was published back in July 2005, we summarise the proposals made at that time, together with our policy decisions and planned implementation dates. This is in Annex 2.

Section I – Significant influence functions¹¹

a) Introduction

- 3.4 In CP05/10 we proposed that the systems and controls functions (CF13 to CF15) and the significant management functions (CF16 to CF20) were each merged to create two new generic controlled functions and that the annual reporting requirement for significant management functions was deleted. We are now proceeding with the proposals to merge the functions and have already deleted the annual reporting requirement for significant management functions.
- 3.5 Our approach will not reduce the scope of the significant influence functions and the individual job roles will remain; for example we will still expect firms to apportion the internal audit role to an individual and then apply for them to be approved under the new generic systems and controls function. We expect firms to take responsibility for ensuring that individuals achieve the standards required to fulfil the specific nature of their role.
- 3.6 We also proposed deleting the sole trader function (CF7) and will be proceeding with this.

Summary of changes

Current requirement	CP05/10 proposal and our decision	Implementation date
Firms required to apply for separate systems and controls functions: <ul style="list-style-type: none"> • CF13 Finance • CF14 Risk assessment • CF15 Internal audit 	CP05/10 proposed we should merge these functions into one generic function. We will merge the systems and controls function into a new function: CF28 – Systems and controls	1 November 2007
Firms required to apply for separate significant management functions: <ul style="list-style-type: none"> • CF16 Designated investment business • CF17 Other business operations • CF18 Insurance underwriting • CF19 Financial resources • CF20 Settlements 	CP05/10 proposed we should merge these functions into one generic function. We will merge the significant management functions into a new function: CF29 – Significant management function	1 November 2007
Firms required to submit an annual significant management function report.	CP05/10 proposed we should delete the reporting requirement. We have already deleted this reporting requirement and the rules and associated guidance. ¹²	6 May 2006 to apply from 1 July 2006 when reports were due.
Relevant firms required to apply for sole trader function (CF7).	CP05/10 proposed we should delete this function. We will delete the sole trader function (CF7)	1 February 2007

11 The significant influence functions consist of all the controlled functions other than the customer functions. An individual performing a significant influence function is likely to have a significant influence on the affairs of their firm.

12 FSA Press release, FSA to delete the annual reporting requirement on senior managers, 3 May 2006.

b) The significant management functions and the systems and controls functions

We asked:

Q: Do you agree with our proposals to merge the significant management functions and the systems and controls functions?

- 3.7 A substantial number of respondents supported both these proposals. A small number of firms were concerned that merging the functions could lead to confusion over the division of responsibilities. And some argued against merging the systems and controls functions as they are fundamentally different.

Our response

- 3.8 Systems and control functions (CFs 13-15)
We will proceed with merging these functions into one generic systems and controls function.
- 3.9 Significant management functions (CFs 16-20)
We will proceed with merging these functions into one generic significant management function.
- 3.10 Even though the functions will be merged the scope of the regime will not alter and we expect firms to allocate roles according to our senior management arrangements and systems and controls requirements¹³. This will ensure the suitable division of responsibilities in firms.

c) The significant management functions annual reporting requirement

We asked:

Q: Do you agree with our proposal to delete the significant management functions annual reporting requirement?

- 3.11 There was unanimous support for this proposal.

Our response

- 3.12 We deleted this requirement with effect from 6 May 2006¹⁴ and the RealAssurance study¹⁵ estimates this will save firms approximately £2.2 million each year.

13 SYSC 3 for Non MiFID firms. SYSC 6 & 7 for common platform firms. Common platform firms are those subject to MiFID and the Capital Requirements Directive (CRD). See CP06/9:Organisational systems and controls (May 2006).

14 FSA Press release, FSA to delete the annual reporting requirement on senior managers, 3 May 2006.

15 'Estimation of FSA Administration Burdens' June 2006 (http://www.fsa.gov.uk/pubs/other/Admin_Burdens_Report_20060621.pdf). This report describes the results of work commissioned by the FSA in August 2005 to estimate the total cost of the administration burdens imposed on the UK financial services industry by the rules in the FSA Handbook.

d) The sole trader function

We asked:

Q: Do you agree with our proposal to delete the sole trader function (CF7)?

- 3.13 There was almost unanimous support for this proposal and only a small number of respondents were concerned this would create a perception that we regarded such firms as low risk.

Our response

- 3.14 We will delete the sole trader function. The management skills of sole traders and the control environment in which they operate will continue to be assessed as part of the corporate authorisation process. Sole traders who undertake designated investment business¹⁶ will continue to be approved under other parts of the Approved Persons regime.

e) Implementation

- 3.15 There will be three¹⁷ changes as a result of our approach to the significant influence functions.
- 3.16 The systems and control functions (CF13 to CF15) will merge and become the systems and controls function (CF28).
- 3.17 The significant management functions (CF16 to CF20) will merge and become the significant management function (CF29).
- 3.18 The sole trader function (CF7) will be deleted.
- 3.19 The two new functions (CF28 and CF29) will become effective on 1 November 2007 and individuals who currently hold controlled functions CF13 to CF15 and/or CF16 to CF20 will automatically become approved under the new merged functions CF28 and/or CF29 as our original grant of approval will remain valid.
- 3.20 Firms are reminded of the requirement¹⁸ to notify us if they become aware of any information which would be reasonably material to the continuing assessment of an approved persons fitness and propriety and, in particular, their competence to carry out an activity.
- 3.21 The transitional arrangements can be found in the draft Handbook text in Appendix 1.
- 3.22 We will update the FSA register to reflect the new merged function(s) for those individuals and the current controlled functions (CF13 through to CF20) will display an end date of 31 October 2007.

16 Designated investment business is any activity specified in Part II of the Regulated Activities Order.

17 The annual significant management function reporting requirement was already deleted on 1 May 2006.

18 SUP 10.13.16R.

- 3.23 The sole trader function (CF7) will cease from 1 February 2007 when the rules come into effect and the FSA register will show an end date of 31 January 2007. We want firms to benefit from administrative savings as soon as possible, and so have chosen an earlier implementation date.

Existing enforcement proceedings

- 3.24 If enforcement proceedings have commenced against an individual under the Approved Persons regime prior to 1 November 2007 and are still to be determined, the determination will be based on the rules at the time of the breach.

Section II - customer functions

a) Introduction

- 3.25 CP05/10 explored the scope for simplifying the customer functions. We consulted on disapplying the customer functions for individuals who deal with wholesale (or non-private) customers. And we outlined for discussion three options for the future application of the customer functions in the retail market.

Summary of changes proposed in CP05/10

Current requirement	New requirement proposed under CP05/10 and decision	Implementation date
Retail firms required to apply for customer functions.	CP05/10 discussed whether we should remove some or all of the customer functions that apply to the retail sector, simplify them or do nothing. See our proposal for merging the customer functions in Chapter 3 section III	N/A
Wholesale (or non-private) firms required to apply for customer functions.	CP05/10 proposed we should disapply the customer functions for the wholesale sector. We are not proceeding with this proposal but see our proposal for merging the customer functions in Chapter 3 section III	N/A
Relevant firms required to apply for the corporate finance function (CF23)	CP05/10 proposed we should delete this function. We are not proceeding with this proposal but see our proposal for merging the customer functions in Chapter 3 section III	N/A

b) The future of the customer functions

- 3.26 We know from the RealAssurance study that an application to perform a customer function ranks as the 23rd highest administrative burden which financial services regulation currently places on firms. Based on figures for the year ending 31 March 2006, removing customer functions would save firms nearly £5.5 million. However, we have listened to the feedback we received from CP05/10 and will retain the customer functions for the time being.

3.27 It will take time for us and the industry to deliver on our agenda for more principles-based regulation. We believe that principles-based regulation will provide greater flexibility for, and underline the responsibility of, firms and senior managers to determine how relevant regulatory outcomes can be achieved. As we and firms make progress on delivering this agenda we will look again at whether the customer functions continue to add value. This review will not be until 2009 at the earliest. If we decide there is no longer a case for customer functions we will consult on this.

c) Retail markets

3.28 In CP05/10 we discussed three options for the future of customer functions in the retail market. The options were: a) no change, b) remove some or all of the customer functions or c) simplify the customer functions.

Our approach at that time can be summarised as follows:

a) no change	b) remove some or all of the customer functions	c) simplifying the customer functions
We asked for information and opinions on the level of protection that our customer functions offer to consumers and the reliance that firms place on our regime in this area.	We considered whether it would be possible to scale back our regime in this area, without causing a significant increase in risk to our objectives, by using other regulatory tools to manage the risks involved. We highlighted our approach for the mortgage and general insurance regime where customer functions are not required and we rely on other regulatory tools. We asked for views on whether this option would require further change to work; for example, would we need to enhance the responsibility of senior managers through APER?	We asked if we could continue to use the customer functions as a successful tool for maintaining consumer protection and market confidence if the functions were less detailed. We asked for comments on whether firms could and would take responsibility for ensuring individuals achieved the standards needed to fulfil the specific nature of their roles in the absence of our more specific checks.

We asked:

Q: Do you think that we should pursue option a), b) or c) above?
Do you have any information on the practical implications, costs and benefits of each option?

Over 80% of respondents were in favour of our simplifying the customer functions.

3.29 Although some respondents proposed a partial merger of different categories of customer functions – for example, by separating investment advisers from those who manage investments, the most popular option was to merge all customer functions.

Our response

3.30 The responses indicated an appetite to simplify the customer functions: we consult in Chapter 3 section III on merging the existing customer functions into one generic customer function.

- 3.31 Merging the customer functions into one generic customer function will have no impact on our statutory objectives, relating to market confidence and consumer protection, as the scope of the customer functions will not reduce. We still expect firms to allocate roles as required by our rules (see Appendix 1 for the draft Handbook text for merging customer functions).
- 3.32 Our requirements on firms when recruiting staff are set out in the Handbook¹⁹; we expect firms to perform their own due diligence before submitting an application to us to approve an individual.
- 3.33 Our vetting process is designed to complement firms' own recruitment practices and should not be viewed as a substitute by firms.
- 3.34 We expect senior management to assess, using a risk-based approach, which combination of checks including credit references, references from previous employees and criminal records checks are appropriate for a particular role. The industry should be aware that our standard vetting process on approved persons does not include criminal records checks, although we shall be carrying out such checks in future on a sample basis. To underline the responsibility upon firms and senior managers to carry out due diligence on prospective employees, and to highlight our policy on criminal records checks, we have amended SUP 10 Annex 1 Frequently Asked Questions G (see the amended text in Appendix 1).

d) The wholesale market

We asked:

Q: Do you agree with our proposals to change the scope of the customer functions, so that they do not apply to individuals that do not deal with private customers?

- 3.35 Many respondents disagreed with our assertion that approved persons operating in wholesale markets pose less risk to our objectives of protecting consumers and maintaining market confidence. Some noted that scandals in the wholesale market had greatly affected retail customers. Others suggested that disapplying the Approved Persons regime would increase the risks to the wholesale market by giving the impression that we would not scrutinise this area as closely.
- 3.36 Several firms were concerned that they would incur additional costs in monitoring the perimeter between wholesale and retail business. Some suggested that it might impede the movement of staff between wholesale and retail markets and result in 'precautionary' approvals.²⁰

Our response

- 3.37 We are not pursuing our proposal to abolish the customer functions for the wholesale market at this time.

19 SUP 10 Annex 1.

20 Some responses referred to the use of criminal records checks and references. These issues have been dealt with separately in Chapter 4, The approval process and other practical issues.

e) Other proposals

We asked:

Q: Do you agree with our proposal to delete the corporate finance function (CF23)?

- 3.38 Responses were split three ways: some supported deleting it, others retaining it and a significant number were in favour of merging this function with the investment adviser function (CF 21). Respondents who opposed the deletion of the corporate finance function gave similar reasons to those used for arguing against disapplying the customer functions in the wholesale market.

Our response

- 3.39 We are not pursuing our proposal at this time. The function will remain an activity under the new merged customer function which we propose in Chapter 3 section III.

Section III – Consultation on merging the customer functions

a) Introduction

- 3.40 In this section, we seek your views on our proposal to merge all existing customer functions into one new generic customer function. It applies to all firms who fall within the scope of the Approved Persons regime, other than mortgage and general insurance firms who do not have customer functions. The deadline for comments on this is 23 November 2006.

b) Our proposals

- 3.41 There will be no reduction in the scope of activities that are covered by the Approved Persons regime, as the new generic customer function will incorporate each of the existing customer functions 21-27²¹.
- 3.42 This proposal will reduce the number of forms that firms have to submit per employee under the Approved Persons regime and, as a result, deliver administrative savings. Currently, we require a firm to submit a Form E (internal transfer request form) if an approved person wants to move between customer functions. Our proposal would result in approximately a 90%²² reduction in the number of these forms submitted by firms.
- 3.43 Firms are also required to submit a ‘short Form A’ when an approved person wants to add a controlled function to one already held. Our proposal will result in firms submitting at least 4,500 fewer ‘short Forms A’.
- 3.44 Our cost benefit analysis shows that our proposal will provide an annual administrative saving of between £800,000 and £975,000 to firms.

21 This includes the Lloyd’s Function (CF25) because, although we recognise it involves a different set of skills, only a small number of firms employ individuals with this function.

22 Approximately 10% of all Forms E received annually relate to movements between the significant influence functions

- 3.45 Our proposal is consistent with the requests from firms responding to CP05/10 for greater simplification of the current regime. It also emphasises the responsibility of firms and senior managers to ensure their approved persons only provide advice on the areas and activities for which they are competent.
- 3.46 We will not make a distinction between individuals operating in the retail and wholesale markets as this may cause complications for firms dealing with both types of customer.
- 3.47 Our ability to take enforcement action using the tools available to us through the Approved Persons regime will be unaffected as the scope of the customer functions remains the same.
- 3.48 To avoid confusion, we propose that the new generic customer function will be CF 30: Customer function. This function will cover all of the activities currently listed in each of customer functions CF 21- 27.
- 3.49 Our draft Handbook text provides a clear description of the activities that will be covered by the new generic customer function. This is set out in the draft Handbook text for SUP 10 in Appendix 1.
- Q1: Do you agree with our proposal to merge the customer functions?
- Q2: Do you support our decision not to create a distinction between those that deal with retail and wholesale customers?

c) Implementation

- 3.50 We will issue a Feedback Statement with made rules in early March 2007 in relation to our proposal. The rules will be effective from 1 November 2007. This coincides with the changes required by MiFID (see section IV). And the merger of the significant management and systems and control functions, at the same time, should minimise transitional costs for firms and us.
- 3.51 We believe this gives firms and us sufficient time to make the necessary adjustments to systems and processes.
- 3.52 The new function CF30 will become effective on 1 November 2007 and individuals who currently hold control function CF21 to CF27 will automatically become approved under the new merged function as our original grant of approval will remain valid.
- 3.53 Firms are reminded of the requirement²³ to notify us if they become aware of any information which would be reasonably material to the continuing assessment of an approved persons fitness and propriety and, in particular, their competence to carry out an activity.
- 3.54 The transitional arrangements can be found in the draft Handbook text in Appendix 1.

23 SUP 10.13.16R.

3.54 The changes we expect to occur as a result of this consultation are summarised below:

What we expect firms may need to do as a result of our proposal:	make changes to systems; update information held on approved persons; and communicate changes to staff where appropriate.
What we expect to do as a result of our proposal:	amend the forms relating to customer functions: Forms A, C, D and E; amend the corporate application pack; make changes to our systems and specifically our regulatory database, the public register and electronic application facilities; update the information held on approved persons; and ensure staff awareness.

Q3: Do you agree that you will have sufficient time to put the necessary changes in place for our planned implementation date of 1 November 2007?

d) Existing enforcement proceedings

3.55 If enforcement proceedings have commenced against an individual under the Approved Persons regime prior to 1 November 2007 and are still to be determined, the determination will be based on the rules at the time of the breach.

e) Implication for our fees regime

3.56 The number of approved persons with customer functions is the metric (or ‘tariff base’) we use to calculate FSA periodic fees and levies for the Financial Services Compensation Scheme (FSCS) and the Financial Ombudsman Service (FOS) in the following FSA fee-blocks:

- A.12 – advisory arrangers, dealers and brokers holding client money;
- A.13 – advisory arrangers, dealers and brokers not holding client money; and
- A.14 – corporate finance advisers.

3.57 Assuming we retain the tariff base of headcount (as opposed to another fee metric), there will be no impact on A.12 and A.13 fees. However, we will want to continue excluding from A.12 and A.13 fee calculations those individuals carrying out a corporate finance adviser²⁴ activity. However, such individuals will remain relevant for fees in the A.14 fee-block.

3.58 In addition, we will also want to exclude all individuals carrying out an investment management²⁵ role from fees calculations in the A.12, A.13 and A.14 fee-blocks, to preserve the status quo. As we will no longer hold information distinguishing the different activities that individuals carry on within the customer function, we will rely on firms notifying us of individuals only carrying out a corporate finance or investment management role, so they can be excluded from fees and levies calculations for A.12, A.13 and A.14 fees as appropriate.

²⁴ Currently CF23 controlled function.

²⁵ Currently CF27 controlled function.

- 3.59 Our proposal to merge the customer functions into one generic function will take effect from 1 November 2007. As we will have records of approved persons with CF 21 to CF26 on 31 December 2006, we will be able to calculate invoices on the existing headcount basis for the A.12, A.13 and A.14 fee-blocks for 2007/08 fees and levies, without firms needing to take any action.
- 3.60 The ongoing FSCS funding review is looking at alternative fee tariff metrics for its contribution groups from October 2007. The review of FSCS funding may result in changes to the FSA and FOS funding arrangements, including tariff bases for the 2008/09 FSA fees and the FOS levy. We will consult publicly before implementing any changes.

e) Our proposed Handbook text

- 3.61 We will need to amend our Handbook text to implement the changes to customer functions. The proposed amendments to the Handbook are in Appendix 1.

Q4: Do you have any comments on our proposed changes to the Handbook (Appendix 1) to implement our proposal?

Section IV – Markets in Financial Instruments Directive (MiFID) – impact and consultation

a) Introduction

- 3.62 This section sets out how we intend to implement the requirements of MiFID²⁶ as they relate to the Approved Persons regime.
- 3.63 The deadline for comments is **9 November 2006** and we will announce the outcome of this consultation in a Policy Statement with made text at the end of January 2007 in line with the timetable prescribed by MiFID.

b) The implementation and scope of MiFID

- 3.64 The Level 1 Directive (MiFID) of the European Parliament and Council was adopted in April 2004. In certain areas, MiFID provides for its requirements to be supplemented by ‘technical implementing measures’ adopted by the Committee. These are known as ‘Level 2’ legislation (the Implementing Directive) and were agreed by the European Parliament on 15 June 2006 and approved by the European Securities Commission on 26 June 2006. They have not yet been formally adopted.
- 3.65 Not all controlled functions will apply to all firms as a result of MiFID implementation; for more details see the table at Annex 3.

26 To find out if your firm is a MiFID firm see page 6 of ‘Planning for MiFID’ November 2005. www.fsa.gov.uk/pubs/international/planning_mifid.pdf.

c) Persons who effectively direct the business

- 3.66 MiFID²⁷ contains a variety of requirements pertaining to those persons that ‘effectively direct the business’ of a firm falling within its scope. These are:
- The persons directing the business should be of sufficiently good repute and experience to ensure the sound and prudent management of the firm;
 - The firm shall notify us of any changes to its management, along with all information needed to assess whether new staff meet the above conditions; and
 - We shall refuse authorisation of the firm if we are not satisfied that those persons meet the above conditions, or if there are objective and demonstrable grounds for believing that changes to the management of the firm pose a threat to its sound and prudent management.
- 3.67 The first two of these requirements will be delivered jointly through the Approved Persons regime and new provisions in SYSC 4²⁸. The SYSC 4 provisions implement the MiFID requirements regarding the sound and prudent management of the firm while the Approved Persons regime focuses on how we vet ‘good repute and experience’.²⁹
- 3.68 Under these requirements, MiFID requires us to vet the repute and experience of the persons who effectively direct the business of firms within its scope. Within the controlled functions, governing functions 1 to 5 seem the obvious way to implement this provision.
- 3.69 The second requirement will continue to be met by the Approved Persons regime, as firms are already required to inform us when there is a change to the individuals performing a governing function.
- 3.70 The third of these requirements is met through the provisions in the Financial Services and Markets Act (FSMA) and our requirements in the Threshold Conditions sourcebook (COND), relating to the Threshold Condition of suitability, and under our powers for withdrawing authorisation.

d) Implementing Article 9 for UK MiFID firms

- 3.71 As stated above, the governing functions 1 to 5 enable us to implement Article 9 of MiFID.
- 3.72 There are no explicit requirements under MiFID, other than those in Article 9, that require individuals in a MiFID firm to be approved by a competent authority. Recital 13 to the Implementing Directive makes clear that the organisational requirements of MiFID are without prejudice to systems established by national law for the registration of individuals working within investment firms.

27 MiFID Article 9.

28 CP06/9:Organisational systems and controls (May 2006).

29 CP06/14:Implementing MiFID for firms and markets (July 2006).

- 3.73 So, we intend to retain the Approved Persons regime and use it as a supervisory tool in relation to our obligations under MiFID and as a means to take enforcement action against approved individuals. However, we will amend the current scope of the regime in relation to incoming EEA firms (see section f below).

Energy market participants, oil market participants and service companies

- 3.74 Currently, these firms do not need to apply to us for the approval of persons performing governing functions on their behalf. However, the scope of MiFID captures firms which are presently energy market participants, oil market participants and service companies if their regulated activities include MiFID investment business, and they cannot rely on any of the exemptions in Article 2 of MiFID. The governing functions will then apply to those firms. We are currently working with these firms in relation to their MiFID obligations but, ultimately, it will be for the firms themselves to decide whether they fall within the scope of MiFID and, therefore, whether they are required to make applications in relation to the governing functions.

e) Scope of compliance function (CF10), risk assessment function (CF14) and the internal audit function (CF15)

- 3.75 We will continue to apply the above functions with reference to the responsibilities outlined in SYSC 3. However, MiFID places some additional responsibilities upon firms in relation to these functions. These extra responsibilities have been copied out for MiFID firms in the new SYSC 6 and 7³⁰ but, as stated above, MiFID does not require the vetting of individuals so these additional responsibilities currently fall outside of the Approved Persons regime.
- 3.76 We propose to amend SUP 10 to refer to SYSC 6 and 7 as well as the current requirements under SYSC 3. This will bring those additional MiFID responsibilities into the Approved Persons regime. It also avoids any artificial division as we believe the responsibilities are unlikely to be segregated within firms.
- 3.77 There is no restriction or specification under MiFID or the Implementing Directive about who should perform these functions, although the conditions relating to the outsourcing of activities in the Implementing Directive indicate that such oversight functions should be carried on by an employee of the firm rather than outsourced³¹.
- 3.78 We currently require that only those individuals who are senior managers or directors should undertake CF10, 14 and 15³² functions. We propose to amend SUP 10 so that any employee may undertake these functions. However, we will add guidance that we expect only individuals of appropriate seniority and experience to carry them out.

Q5: Do you agree that SUP 10 should be amended for CF10, CF14 & CF15 to incorporate the additional responsibilities under MiFID?

30 CP06/9: Organisational systems and controls (May 2006).

31 MiFID Implementing Directive Article 14(2)(e).

32 See chapter 3 section I confirming our decision to merge CF14 and CF15 into the new generic systems and controls function.

f) The impact on EEA incoming branches.

- 3.79 Currently, we do not apply the governing functions to a branch of an incoming EEA firm. This situation will continue under MiFID.
- 3.80 We currently apply other controlled functions to incoming EEA firms including CF9 (EEA business oversight) and CF10 (Compliance oversight). However, these functions need to be switched off in relation to the MiFID business of incoming EEA firms because they relate to matters falling within article 13 of MiFID, which are the exclusive responsibility of the home state. However, these controlled functions can be retained in relation to matters falling outside of the scope of the Directive for example, where the firm has a top-up permission.
- 3.81 In relation to the other controlled functions we currently apply to incoming EEA firms, the Implementing Directive³³ makes the assessment of an employees skills, knowledge and expertise a matter for the home state regulator. So we will no longer assess competence for individuals as part of our assessment of their fitness and propriety for approval to perform a controlled function. MiFID will not prevent us from continuing to approve the individual in respect of their probity and financial soundness. And we intend to approve individuals in an incoming EEA firm carrying on MiFID business in respect of these areas.
- 3.82 Although the fit and proper assessment will be different for individuals in incoming EEA firms, carrying on MiFID business, than for those in international or UK firms, the application process – and therefore the administrative burden – will be largely the same and therefore we do not anticipate any distortion in the market. The alternative would be not to approve individuals working in incoming EEA firms carrying on MiFID business.
- 3.83 However, if an incoming EEA firm passports in under a different directive – or wishes to top-up its existing MiFID permission to non-MiFID activities – then the assessment of competence will apply to those individuals who then undertake any activities as a result.

Q6: Do you agree we should continue to assess individuals only in relation to probity and financial soundness for controlled functions in incoming EEA MiFID firms?

g) CF8 - Apportionment and oversight function

- 3.84 Under the current provisions in SYSC 2³⁴ we require firms to allocate responsibility to one or more individual directors/senior managers for (1) the apportionment of functions and (2) the oversight of the establishment and maintenance of the systems and controls of the firm. SYSC 2 sets out who in the firm should undertake these responsibilities and these relate to our controlled function CF8³⁵.

33 MiFID Implementing Directive Article 5(1)(d).

34 SYSC 2.1.

35 SUP 10.7.1R.

- 3.85 The Implementing Directive requires a firm to allocate functions and responsibilities and further provides that, when allocating functions internally, it is the responsibility of the governing body to ensure that the firm complies with its responsibilities under MiFID. This allocation of functions and responsibility is a collective responsibility and is not delegated to an individual, as is currently the case under SYSC2.
- 3.86 A review of the current provisions under SYSC 2 in relation to the provisions in MiFID is underway with a consultation expected in 2007.

h) What do we expect firms to do?

- 3.87 The requirements and obligations under MiFID will come into force on 1 November 2007. Most of the changes will supersede current requirements rather than imposing new ones.

UK MiFID firms carrying on MiFID business

- 3.88 There are minimal changes for UK firms carrying on MiFID business as the Approved Persons regime will continue to apply. Firms will need to consider the additional responsibilities, in SYSC 6 and 7, for controlled functions CF10 (Compliance oversight), CF14 (risk assessment) and CF15 (internal audit). Our review of SYSC 2 may require some change with regard to the apportionment and oversight function (CF8).

EEA incoming MiFID firms

- 3.89 Firstly, firms will no longer need to apply for approval for those individuals performing an activity in relation to controlled functions CF9 (EEA business oversight) and CF10 (Compliance oversight) after 1 November 2007: those individuals who currently have approvals for these functions will show an end date of 31 October 2007 on our Register.
- 3.90 Secondly, firms will no longer need to confirm to us the competence of an individual applying for approved person status as this will be a matter for the home state regulator. We will amend our approval forms to indicate which section will no longer require completion.

EEA incoming firms with a different directive passport or with a top-up permission

- 3.91 Firstly, firms will need to continue to apply for controlled functions CF9 (EEA business oversight) and CF10 (Compliance oversight) for individuals undertaking these roles.
- 3.92 Secondly, firms will need to confirm to us the competence of an individual applying for approved person status. If firms are also undertaking MiFID business, they will need to think about what activities their employees will undertake and if they do or do not need to be assessed as competent for that role.
- 3.93 If an individual, who is already approved to undertake only MiFID business and not assessed for competence, is to begin non-MiFID business then their approval will need to be extended to include an assessment of his competence.

- 3.94 We are aware that we will need to provide with a way of informing us when this situation occurs. We are currently looking at options with a view to minimising bureaucracy.

i) Our proposed Handbook text

- 3.95 We will need to amend our Handbook text to implement MiFID. The proposed amendments to our Handbook are in Appendix 1.

Q7: Do you have any comments on our proposed changes to the Handbook (Appendix 1) to implement MiFID?

Section V - Cost benefit analysis and compatibility statements

- 3.96 We set out below a cost-benefit analysis on a) our proposal to merge customer functions into one generic customer function and b) the approach we are taking to implementing MiFID as it relates to the Approved Persons regime.

a) Merging customer functions

Benefits (one off and on-going)

- 3.97 In future, firms will, per employee, complete fewer Forms A and E which we estimate will annually save the financial services industry almost £1 million. This may be particularly important for large firms with regular changes to their population of approved persons.
- 3.98 Between 1 April 2005 and 31 March 2006 firms submitted approximately 8,200 Forms E (internal transfer). Merging customer functions would have delivered a 90%³⁶ reduction in the number of Forms E that firms would have completed and submitted during this period. On average, the administrative burden (including overheads) on a firm of completing and submitting a Form E is between £50 and £75 and therefore the total saving to industry would have been between £350,000 and £525,000.
- 3.99 There would also have been a 10% reduction (equivalent to 4,500 forms) in the number of short Forms A (approval to perform a controlled function) that firms would have completed and submitted during this period. On average, the administrative burden on a firm of completing and submitting 'short Form A' is, including overheads, £100. So the total saving to the industry would have been £450,000. In practice, the savings may be slightly higher because some firms submit a long Form A which takes more time to complete.
- 3.100 Firms will not have to wait for us to grant approval before the approved person changes roles within the firm. Although we cannot quantify this benefit precisely because the employee is likely to be engaged in other tasks while the new application is processed, this proposal will provide firms with added flexibility in responding to business needs.

36 Approximately 10% of all Forms E received annually relate to movements between the significant influence functions.

- 3.101 We will process fewer Forms A and E, which we estimate would deliver annual savings to us of approximately £70,000.

Costs (one off and on-going)

- 3.102 Firms will incur transitional costs, although we expect these would be of minimal significance. Firms will need to update their records and raise awareness of the changes among their population of approved persons and, where relevant, those overseeing the application process. However, this should only result in minimal cost.
- 3.103 Firms should not incur any new and significant costs in respect of monitoring or training their approved persons because there is already a requirement for firms to have competent employees. Furthermore, the investment adviser function (CF 21) encapsulates a wide range of activities, so firms already have to ensure that those approved for this controlled function advise only on products for which they are qualified and for which the firm has permission.
- 3.104 We will also incur transitional costs from, for example, amending our forms. Once again, we do not expect these costs to be significant.

b) Implementing MiFID

Benefits

- 3.105 There will be very minor ongoing savings for incoming EEA firms only carrying out MiFID activities, which should have no direct impact on competition. Although MiFID prevents us from applying the EEA investment business oversight (CF 9) and compliance oversight (CF 10) functions to individuals working in incoming EEA firms falling within its scope, the number of approved persons affected will be very small. For example, only 142 individuals in all EEA firms (MiFID scope and non-scope) are approved for CF9. We will also continue to apply both controlled functions to incoming EEA firms for their non-MiFID business (for example where they have a top-up permission).
- 3.106 Furthermore, our fit and proper assessment of individuals applying to undertake a controlled function will be different for incoming EEA firms falling within the scope of MiFID from the assessment for those in UK, international and non-MiFID scope incoming EEA firms because we are not allowed to assess their competence. However, the application process, and therefore the administrative burden, would be largely the same.

Costs

- 3.107 There will be no direct costs for UK firms. There will be a minor transitional cost to EEA firms in moving to the new arrangements and in monitoring the boundary between MiFID and non-MiFID business. However, these costs are a direct result of MiFID and, in practice, an incoming EEA firm with a permission wider than MiFID may want its employee to be vetted in relation to competence so they are approved for all parts of the firm's business and not just that related to MiFID. There should not be any impact on the competitive position of UK firms compared to other EEA firms.

Compatibility statement

- 3.108 In this section we set out how the approach, on which we are consulting, is compatible with our general duties under section 2 of FSMA and with the regulatory objectives set out in sections 3 - 6 of FSMA. We also outline how our proposals are consistent with the principles of good regulation to which we must have regard.

a) Our statutory objectives

Market confidence

- 3.109 We do not expect our approach to have any negative impact on market confidence and the CBA shows that our approach does not have any significant impact on competition. Furthermore, our approach does not diminish the requirement for firms to have fit and proper employees³⁷.

Consumer protection

- 3.110 Our proposals will not result in any reduction in scope of the customer functions. So individuals carrying out these functions will continue to be approved and consumers will still be able to access our Register to examine details of the approved person they are dealing with, such as their disciplinary history.

Financial crime

- 3.111 We do not expect there to be any material increase in the risk of financial crime as a result of our proposals and our approach to implementing MiFID means we will continue to apply the controlled function of a money laundering reporting officer (CF11) to all incoming EEA firms.

Public awareness

- 3.112 We do not believe there is any need to launch a specific campaign to promote public awareness of the proposals in our consultation. We are already a major source of impartial information on financial products and services through our factsheets and guides, our comparative tables, our online calculators and a host of other web-based materials.

b) Principles of good regulation

- 3.113 Section 2(3) of FSMA requires us to consider certain principles when discharging our general functions. We set out below how our approach supports these principles.

37 SUP Chapter 10 Annex 1.

The need to use our resources in the most efficient and economic way

- 3.114 We will process, per employee, fewer forms in respect of the Approved Persons regime which will deliver administrative and man-hour savings. Chapter 4, 'The approval process and other practical issues', also sets out ways in which we aim to make the process for applying for approval to perform a controlled function more efficient for firms.

The responsibilities of those who manage the affairs of authorised persons

- 3.115 Our approach maintains the emphasis we place on the senior managers of a firm for the approved persons they employ as they will need to ensure that the approved person does not provide advice in areas in which they are not competent.

The restrictions we impose on the industry must be proportionate to the benefits that are expected to result from those restrictions

- 3.116 Our proposal to merge customer functions is designed to reduce the administrative burden we place on firms through the approved persons regime.

The desirability of facilitating innovation in connection with regulated activities

- 3.117 We do not consider that our proposals will restrict innovation.

The international character of financial services and markets and the desirability of maintaining the competitive position of the UK

- 3.118 We have not identified any significant international issues arising from our proposals. Our proposals are consistent with MiFID and all other requirements of EU legislation.

The need to minimise the adverse effects on competition that may arise from our activities and the desirability of facilitating competition between the firms we regulate

- 3.119 We do not expect the changes to the Approved Persons regime required by MiFID to have any significant effect on competition. Our proposal to merge customer functions will reduce administrative costs which may encourage new entrants to the market and provide consumers with greater choice.

4 The approval process and other practical issues

a) Introduction

- 4.1 Respondents took the opportunity of CP05/10 to feed back to us on a number of practical issues concerning employment and the approval process, including checks made at the employment stage, costs of implementing our proposals and further changes that firms would like to see.

b) Vetting

- 4.2 In responding to the proposal to delete customer functions for those dealing only with wholesale customers, many firms were concerned that we would no longer act as a 'long-stop' where we had information not readily accessible to the recruiting firm. Several also felt they would be unable to obtain informative references from other authorised firms without the support of our rules and guidance. Firms who use the Criminal Records Bureau as part of their recruitment procedure noted that they would not be entitled to receive standard disclosures for employees dealing with wholesale (non-private) customers³⁸. One suggestion was a different way of checking, with the individual's prior consent, any information that we held or, alternatively, that an industry body could maintain its own register of names on a consent basis.
- 4.3 We set out our requirements on firms when recruiting staff for controlled functions in the Handbook³⁹. We expect firms to perform their own due diligence before submitting an application to us for approval.
- 4.4 Our vetting process is designed to complement firms' own recruitment practices and should not be viewed as a substitute by firms.
- 4.5 We expect firms to assess, using a risk-based approach, which combination of checks including credit references, references from previous employees and criminal records checks they should use for a particular role.

38 This is because the Rehabilitation of Offenders Act 1974 Exceptions Order 1975 (as amended) currently refers specifically to approved persons.

39 SUP 10 Annex 1.

- 4.6 We expect senior management to take responsibility for managing the risks in their firms properly and ensuring they have systems and controls to mitigate those risks. Failure to do so may result in disciplinary action against the individuals responsible as well as firms.⁴⁰
- 4.7 Our new proposal to retain but merge all customer functions means that the current provisions relating to references⁴¹ and criminal records checks are unaffected. However, two key issues require clarification:

Criminal records checks

The industry should note that our standard vetting process on approved person applications does not currently include criminal records checks. We check criminal records only where there is reason to believe that information has not been disclosed about a criminal record. Firms who have been under a misapprehension on this point and who do not currently ask eligible staff to apply for Criminal Records Bureau disclosures should take a fresh look at their policy and processes.

We shall be arranging for criminal records checks to be done on a sample basis in future.

To underline the responsibility upon firms and senior managers to carry out due diligence on prospective employees, and to highlight our policy on criminal records checks, we have amended SUP 10 Annex 1 Frequently Asked Questions G (see the amended text in Appendix 1).

Obtaining references for customer function applications

We are aware that some firms have experienced difficulties in obtaining relevant information where a potential candidate is applying for a customer function. Our rules⁴² require firms to obtain references covering the last five years from previous employers who are FSA-authorized firms. Some firms claim not to hold the appropriate information. Firms should comply with the requirements to provide appropriate reference information when asked by future employers of their former staff.

c) Senior management responsibility

We asked:

Q: Do you agree with our approach to senior management responsibility for ensuring fitness and propriety?

- 4.8 There was widespread agreement that the senior management of a firm should take greater responsibility for ensuring the fitness and propriety of its approved persons under a simplified regime. However, there were differing views about how this should be achieved. Many respondents felt the firm should decide how this responsibility should be allocated, while others suggested that the apportionment and oversight function (CF8) already included this responsibility.

40 'Efficiency versus fairness', speech by Margaret Cole Director of FSA Enforcement, 16 June 2006.

41 SUP 10.13.12R.

42 SUP 10.13.12R.

Our response

- 4.9 Our proposal to lighten the administrative burden on firms by merging all customer functions will need to be matched by firms making sure they take on the responsibility for ensuring the competence of their approved persons holding customer functions.
- 4.10 We have discussed the implication of MiFID in relation to the apportionment and oversight function (CF8) in chapter 3 section IV.

d) Costs

We asked:

Q: Do you agree that firms should benefit from these changes and will not face costs of more than minimal significance as a result of them? Do you have any information on the likely costs and benefits involved?

- 4.11 Some firms claimed that their costs would increase if customer functions were disapplied for the wholesale sector and others noted the effect on periodic fees if this were to happen. In general, respondents felt the other proposed changes would not lead to significant additional costs for firms, although views about the scale of the benefits differed.

Our response

- 4.12 Based on the findings of the RealAssurance study, we estimate that implementing all the measures in this paper will provide annual savings of £3 million for the financial services industry.

e) Implementation

Q: Do you have any views on how we should implement any changes that we make to the controlled functions?

- 4.13 There was general support for any changes to the Approved Persons regime to take place on one specific date. Several respondents argued that no changes should take place until the implications of MiFID became clear. Others pointed to the need for sufficient lead-in time to allow firms to amend their computer systems and some were concerned about practical issues over removing wholesale customer functions from the regime.

Our response

- 4.14 We have set out the implementation timetable for the CP05/10 proposals in Annex 2. With the exception of two changes⁴³, where early implementation will give significant benefit to firms, we intend to implement these proposals, and the ones on which we are consulting now, on 1 November 2007.

43 See Chapter 3 section I on our approach to the annual reporting requirement for significant management functions and the sole trader function (CF7).

f) Future changes

We asked:

Q: Do you have any comments on further changes that could be made to the Approved Persons regime in the future?

- 4.15 Most suggestions centred on the use of technology and simplification of forms. Several respondents asked that further use be made of electronic forms for both applications and notifications and one encouraged us to introduce an electronic facility for the bulk submission of applications. Some asked us to shorten and simplify Form A (application to perform controlled functions), particularly for candidates who had previously been approved, while others encouraged us to improve Form D (notification of changes in personal information or application details).
- 4.16 Several respondents advocated greater transferability either between functions or between different companies within a group structure. A small number of respondents felt we were inconsistent in applying the Approved Persons regime to investment firms but not to mortgage and general insurance firms.

Our response

- 4.17 **Forms:** Firms are able to submit a shortened Form A (which omits sections 4 and 5 of the form) where an individual is moving to a new firm and not moving from a customer function to a significant influence function, provided there is no change to the answers given in the fitness and the propriety section of the original application form. There is further guidance attached to Form A: www.fsa.gov.uk/pubs/other/ivreg_forma.pdf
- Now we have assessed the implications of MiFID, we will be reviewing all of the Approved Persons forms. We encourage firms to provide us with specific suggestions for improvements to both these forms.
- 4.18 **Technology:** Firms can already submit an application electronically using the Firms Online system. However, we are aware of the need for improvements to this system and we have a programme in place to develop and improve our technology.
- 4.19 **Transferability within functions or group structure:** If we were to allow individuals to transfer within group structures without the need to apply for re-approval, a firm may then need to submit a list of approved persons annually. We do not want to add notification burdens of this kind.
- 4.20 **Mortgage and general insurance (M&GI) firms:** We recently established our M&GI regime and have no plans to make changes as we believe the current approach reflects the lower risk that M&GI firms pose to our statutory objectives.

5 Other changes to the Handbook

a) Introduction

- 5.1 CP05/10 proposed changes to SUP 10 text, in line with our Handbook simplification agenda, which included removing duplicate guidance and how the Approved Persons regime applies in particular situations.

b) Changes proposed in CP05/10

We asked:

Q: Do you have any comments on our proposed changes to the Handbook (in Annex 3 of CP 05/10) to implement our proposals?

- 5.2 Many respondents supported our proposal to reduce the amount of duplicative guidance in our Handbook. However, several felt it would be unhelpful to remove guidance from the Supervision manual, specifically SUP10, while others asked us to ensure that relocated materials were clearly signposted.
- 5.3 There were also critical comments about the drafting of new provision APER 4.7.9A E in the proposed Handbook text. Respondents also suggested we should have one sourcebook for approved persons to avoid having to refer to different areas of our Handbook.

Our response

- 5.4 We note the comments about the drafting of the new APER 4.7.9A E provision. This was proposed to ensure the proper segregation of duties if customer functions were to be disappplied for the wholesale sector. As we are not pursuing this proposal, the provision is no longer relevant.
- 5.5 To help firms, we provided a facility in April 2006 which draws together all the current requirements for approved persons with the training and competence requirements. This is on our website at <http://fsaHandbook.info/FSA/select-Handbook/focus-on>
- 5.6 We will also be developing an additional feature which we aim to have available as early as possible next year. This web-based tool will build on the existing facility and include further key material.

- 5.7 We note that several respondents felt it would be unhelpful to remove guidance from SUP 10. While we think it is still appropriate to remove the guidance proposed from the Handbook, we will relocate any guidance that remains beneficial to firms to a clearly indicated section of our website. Removal of guidance from the Handbook does not indicate a change in our Policy approach, just our commitment to simplify the Handbook.

c) Other changes

- 5.8 To underline the responsibility upon firms and senior managers to carry out due diligence on prospective employees, and to highlight our policy on criminal records checks, we have amended SUP 10 Annex 1 Frequently Asked Questions G (see the amended text in Appendix 1).

List of non-confidential responses to CP05/10

Abbey

ABN Amro

Adam Samuel

Advanced Insurance Centres Ltd

Aegon Asset Management UK

Alexander Forbes Risk Services

Alliance & Leicester

Amlin Underwriting Limited

Andrew Sheppard

Aon

Apax Partners

Association of Private Client Investment Managers and Stockbrokers

Artemis

Association of British Credit Unions Limited

Association of Electricity Producers

Association of Foreign Banks

Association of Friendly Societies

Association of Independent Financial Advisers

Association of Solicitors and Investment Managers

AVIVA

AXA

B & CE

Baillie Gifford & Co

Bank of Ireland Asset Management (UK) Ltd

Bank of New York

Banque AIG

Barclays
Barclays Capital
Bonnier Business Information
BP Oil International Ltd
BPP Professional Education
Brewin Dolphin Securities Ltd
Bridgepoint Capital Limited
Brit Insurance Ltd
Britannia
British Bankers' Association
British Nuclear Group
British Venture Capital Association
Building Societies Association
Cambridge Fund Managers
Cattellyst Consultancy, The
Charles Flint QC
Chartered Insurance Institute
Children's Mutual, The
CIFAS
City of London Police
City Personnel Group
CJ Russell Insurance Services
CMS Cameron McKenna
Council of Mortgage Lenders
David O'Sullivan
Deloitte
Duncan Lawrie Ltd
Ernst & Young
ET Capital Limited
Europa Capital
F & C Asset Management
Financial Services Consumer Panel
Financial Services Skills Council
Fraud Advisory Panel
Friends Provident
Friends Provident Life and Pensions Ltd
Global Home Loans

Goy Harris Cartwright & Co Ltd
Groves Financial Planning
Hermes
HSBC
Huntswood Consulting
Investment Management Association
ING Wholesale Banking
Institute of Chartered Accountants
International Financial Data Services
International Financial Services, London
Investment and Life Assurance Group
Investment Property Forum
International Underwriting Association
Killik & Co
King & Shaxson Ltd
KPMG
Law Society, The
LCF Rothschild Group
Legal and General
Lincoln Financial Group
Lloyd's Market Association
London Financial Academy
London Investment Banking Association
London Stock Exchange
M&G Investment Management Ltd
Misys General Insurance
Morecambe Bay Credit Union Ltd
Munro Partnership Ltd, The
National Australia Group
Nationwide Building Society
NFU Mutual
Nomura
Nord LB
Openwork
Paycare
PEP & ISA Managers Association
Price Waterhouse Coopers

Progressive Asset Management
Provincial Hospital Services Association
Prudential Assurance Co Ltd
Regulatory Alliance of Mortgage Packagers
Royal Bank of Scotland
Royal London
Royal Sun Alliance
RWE Trading Services Ltd
Schroders
Scottish Investments Operations
Scottish Widows
Securities and Investment Institute Compliance Forum
Securities and Investment Institute
Seymour Pierce Ltd
Skandia Group
Skipton Building Society
Smaller Businesses Practitioner Panel
Society of Pension Consultants, The
Standard Life Assurance Company
Standard Life Investments
Surrenda-link Ltd
The Association of Investment Trust Companies
The Futures and Options Association
Thinking about Crime Ltd
Thornhill Investment Management Ltd
Tolson Messenger Ltd
UBS
UK Society of Investment Professionals
Unum Provident
Universities Superannuation Scheme Ltd
Watson Wyatt
Wesleyan Assurance Society
WestLB
Which?

Summary of proposed changes under CP05/10

Current requirement	New requirement proposed under CP05/10 and decision	Implementation date
Firms required to apply for separate systems and controls functions: <ul style="list-style-type: none"> • CF13 Finance • CF14 Risk assessment • CF15 internal audit 	CP05/10 proposed we should merge these functions into one generic function. We will merge the systems and controls function into a new function: CF28 – systems and controls	1 November 2007
Firms required to apply for separate significant management functions: <ul style="list-style-type: none"> • CF16 Designated investment business • CF17 Other business operations • CF18 Insurance underwriting • CF19 Financial resources • CF20 Settlements 	CP05/10 proposed we should merge these functions into one generic function. We will merge the significant management functions into a new function: CF29 – significant management	1 November 2007
Firms required to submit an annual significant management function report.	CP05/10 proposed we should delete the reporting requirement We have already deleted this reporting requirement and the rules and associated guidance were removed. ⁴⁴	6 May 2006 to apply as from 1 July 2006 when reports were due
Relevant firms required to apply for sole trader function (CF7).	CP05/10 proposed we should delete this function. We will delete the sole trader function (CF7)	1 February 2007
Retail firms required to apply for customer functions.	CP05/10 discussed whether we should remove some or all of, the customer functions that apply to the retail sector, simplify them or do nothing with them. See our proposals for merging the customer functions in Chapter 3 section (iii)	N/A
Wholesale (non-private) firms required to apply for customer functions.	CP05/10 proposed we should disapply the customer functions for the wholesale sector. We are not proceeding with this proposal but see our proposals for merging the customer functions in Chapter 3 section (iii)	N/A
Relevant firms required to apply for the corporate finance function (CF23)	CP05/10 proposed we should delete this function. We are not proceeding with this proposal but see our proposals for merging the customer functions in Chapter 3 section (iii)	N/A

44 FSA press release, 'FSA to delete the annual reporting requirement on senior managers', 3 May 2006.

The application of controlled functions after 1 November 2007

		UK firms (MiFID and non-MiFID)	Incoming EEA firms (MiFID passport only)	Incoming EEA firms (Other directive passports or top-up permission)	Third country branches
Competence assessment required?		Yes	No	Yes	Yes
Controlled function	Controlled function description				
CF1	Director	Yes	No	No	No
CF2	Non-executive Director	Yes	No	No	No
CF3	Chief executive	Yes	No	No	Yes
CF4	Partner	Yes	No	No	No
CF5	Director of unincorporated association	Yes	No	No	No
CF6	Small friendly society	Yes	No	No	No
CF8*	Apportionment and oversight	Yes	No	No	Yes
CF9	EEA investment business oversight	No	No	Yes	No
CF10	Compliance oversight	Yes	No	Yes	Yes
CF11	Money laundering reporting officer	Yes	Yes	Yes	Yes
CF12	Actuarial	Yes	No	Yes**	Yes
CF12A	With-profits actuary	Yes	No	Yes**	No
CF12B	Lloyd's actuary	Yes	No	Yes**	Yes
CF28	Systems and controls	Yes	No	No	No
CF29	Significant management function	Yes	Yes***	Yes***	Yes
CF30	Customer function	Yes	Yes (not Lloyd's)	Yes (Lloyd's only applies for top-up permission)	Yes

* Our proposed review of the regulation of senior management responsibility may result in changes to CF8 (see Chapter 3 IV section g)

** These controlled functions will only apply where there has been a top-up permission

*** Not all the underlying activities under the scope of the generic significant management function will apply, firms will need to check our requirements to ensure relevant approval status

List of questions in this Consultation Paper

Chapter 3 section III – Consultation for merging the customer functions

- Q1: Do you agree with our proposal to merge the existing customer functions?
- Q2: Do you support our decision not to create a distinction in the customer functions between those that deal with retail and wholesale customers?
- Q3: Do you agree that you will have sufficient time to put the necessary changes in place for our planned implementation date of 1 November 2007?
- Q4: Do you have any comments on our proposed changes to the Handbook (Appendix 1) to implement our proposal?

Chapter 3 section IV – Markets in Financial Instruments Directive (MiFID) – impact and consultation

- Q5: Do you agree that SUP10 should be amended for CF10, CF14 & CF15 to incorporate the additional responsibilities under MiFID?
- Q6: Do you agree that we should continue to assess individuals only in relation to probity and financial soundness for controlled functions in incoming EEA MiFID firms?
- Q7: Do you have any comments on our proposed changes to the Handbook (Appendix 1) to implement MiFID

Draft Handbook text

APPROVED PERSONS REGIME (SIMPLIFICATION AND MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE) INSTRUMENT 2007¹

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 ("the Act"):
- (1) section 59 (Approval of particular arrangements);
 - (2) section 64 (Conduct: statements and codes);
 - (3) section 138 (General rule-making power);
 - (4) section 149 (Evidential provisions);
 - (4) section 156 (General supplementary powers); and
 - (6) section 157(1) (Guidance).
- B. The rule-making powers listed above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force as follows:
- (1) the provisions relating to the deletion of the sole trader function in MIPRU 2.2.3G (3), SUP10.4.5R, SUP 10.6.1A G and SUP 10.6.30R to SUP 10.6.32G, SUP 12.2.14G (2) and TP 8C in Annex H and the deletion of sole trader function from the Glossary in Annex A come into force on 1 February 2007;
 - (2) the remainder of the instrument comes into force on 1 November 2007.

Amendments to the Handbook

- D. The modules of the FSA's Handbook of rules and guidance listed in column (1) below are amended in accordance with the Annexes to this instrument listed in column (2).

(1)	(2)
Glossary	Annex A
Senior Management Arrangements, Systems and Controls Sourcebook	Annex B
Statements of Principle and Code of Conduct for Approved Persons	Annex C
The Fit and Proper test for Approved Persons Sourcebook	Annex D
Fees Manual	Annex E
Integrated Prudential Sourcebook	Annex F
Mortgage Firms and Insurance Intermediaries Prudential Sourcebook ²	Annex G

¹ For the purposes of this consultation paper we have shown all the changes as one instrument. However, as noted in the text of the consultation page these changes will be brought into force through two separate instruments.

² This sourcebook is the new sourcebook as consulted on in the Consultation Paper Strengthening Capital Standards – Restructuring the Handbook CP 06/10.

Training and Competence Sourcebook	Annex H
Supervision Manual	Annex I
Credit Unions Sourcebook	Annex J

Citation

- E. This instrument may be cited as the Approved Person's Regime (Simplification and Markets in Financial Instruments Directive) Instrument 2006.

By order of the Board
25 January 2007³

³ The changes relating to the merged customer function will be made under a separate instrument following a feedback statement in February 2007

Annex A

Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

<i>adviser on syndicate participation at Lloyd's function</i>	controlled function CF25 in the table of controlled functions, described more fully in SUP 10.10.15R.
<i>corporate finance adviser function</i>	controlled function CF23 in the table of controlled functions, described more fully in SUP 10.10.13R.
<i>customer function</i>	any of the controlled functions 21 to 27 in the table of controlled functions <u>the controlled function 30 in the table of controlled functions,</u> described more fully in SUP 10.10.7R.
<i>customer trading function</i>	controlled function CF26 in the table of controlled functions, described more fully in SUP 10.10.16R.
<i>finance function</i>	controlled function CF13 in the table of controlled functions, described more fully in SUP 10.8.1R.
<i>governing function</i>	any of the <i>controlled functions 1 to 7</i> <u>6</u> in the table of controlled functions.
<i>internal audit function</i>	controlled function CF15 in the table of controlled functions, described more fully in SUP 10.8.6R.
<i>investment adviser (trainee) function</i>	controlled function CF22 in the table of controlled functions, described more fully in SUP 10.10.11R
<i>investment adviser function</i>	controlled function CF21 in the table of controlled functions, described more fully in SUP 10.10.7R.
<i>investment management function</i>	controlled function CF27 in the table of controlled functions, described more fully in SUP 10.10.20R.
<i>Lloyd's actuary</i>	<u>controlled function CF12B in the table of controlled functions, described more fully in SUP 10.7.22R.</u>

function

MiFID
business

investment services and activities and ancillary services carried on by a
MiFID investment firm.

MiFID
investment
firm

an [~~investment firm~~] that has a registered office (or, if it has no registered
office, its head office) in an EEA State:

(a) ~~excluding a person to whom MiFID does not apply as a result of
Articles 2 or 3 of MiFID; but~~

(b) ~~including, subject to (a), a BCD credit institution when providing
one or more investment services and/or carrying on performing
investment activities.~~

(in summary) a firm to which MiFID applies including, for some purposes
only, a credit institution and UCITS investment firm.

(in full) a firm which is:

(1) an investment firm with its head office in the EEA (or, if it has a
registered office, that office);

(2) a BCD credit institution (only when providing an investment service
or activity in relation to the rules implementing the Articles referred
to in Article 1(2) of MiFID);

(3) a UCITS investment firm (only when providing the services referred
to in Article 5(3) of the UCITS Directive in relation to the rules
implementing the articles of MiFID referred to in Article 5(4) of that
Directive);

unless, and to the extent that, MiFID does not apply to it as a result of
Article 2 (Exemptions) or Article 3 (Optional exemptions) of MiFID.

Note for consultation: the text underlined and struck through is the text
contained in CP_06/9 “Organisational systems and controls - Common
platform for firms”.

<i>pension transfer specialist function</i>	controlled function CF24 in the table of controlled functions, described more fully in SUP 10.10.14R.
<i>risk assessment function</i>	controlled function CF14 in the table of controlled functions, described more fully in SUP 10.8.3R.
<i>significant influence function</i>	any of the <i>controlled functions</i> 1 to 20 <u>29</u> in the <i>table of controlled functions</i> .
<i>significant management (designated investment business) function</i>	controlled function CF16 in the table of controlled functions, described more fully in SUP 10.9.10R.
<i>significant management (financial resources) function</i>	controlled function CF19 in the table of controlled functions, described more fully in SUP 10.9.16R.
<i>significant management (insurance underwriting) function</i>	controlled function CF18 in the table of controlled functions, described more fully in SUP 10.9.14R.
<i>significant management (other business operations) function</i>	controlled function CF17 in the table of controlled functions, described more fully in SUP 10.9.12R.
<i>significant management (settlements) function</i>	controlled function CF20 in the table of controlled functions, described more fully in SUP 10.9.18R.
<i>significant management function</i>	any of the <i>controlled functions</i> 16 to 20 <u>CF29</u> in the <i>table of controlled functions</i> , described more fully in <u>SUP 10.9.10R</u> .
<i>sole trader function</i>	controlled function CF7 in the table of controlled functions, described more fully in SUP 10.6.30R.

*systems and
controls
function*

~~any of controlled functions 13 to 15~~ CF28 in the *table of controlled functions*, described more fully in *SUP 10.8.1R*.

Annex B

Amendments to the Senior Management Arrangements, Systems and Controls Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 3.2.10 G (1) ...
- (3) The term 'risk assessment function' refers to the generally understood concept of risk assessment within a *firm*, that is, the function of setting and controlling risk exposure. The risk assessment function is not a *controlled function* itself, but is part of the *systems and controls function* (CF28).

...

- 3.2.15 G Depending on the nature, scale and complexity of its business, it may be appropriate for a *firm* to form an audit committee. An audit committee could typically examine management's process for ensuring the appropriateness and effectiveness of systems and controls, examine the arrangements made by management to ensure compliance with requirements and standards under the *regulatory system*, oversee the functioning of the internal audit function (if applicable – see SYSC 3.2.16G) and provide an interface between management and the external auditors...

- 3.2.16 G (1) Depending on the nature, scale and complexity of its business, it may be appropriate for a *firm* to delegate much of the task of monitoring the appropriateness and effectiveness of its systems and controls to an ~~*internal audit function*~~ internal audit function. An ~~*internal audit function*~~ internal audit function should have clear responsibilities and reporting lines to an audit committee or appropriate *senior manager*, be adequately resourced and staffed by competent individuals, be independent of the day-to-day activities of the *firm* and have appropriate access to a *firm's* records.
- (2) The term 'internal audit function' refers to the generally understood concept of internal audit within a *firm*, that is, the function of assessing adherence to and the effectiveness of internal systems and controls, procedures and policies. The internal audit function is not a *controlled function* itself, but is part of the *systems and controls function* (CF28).

...

...

The following amendments are based on the text consulted on in the Consultation Paper Organisation Systems and Controls – Common Platform for firms CP 06/9

- 14.1.33 G Where a *firm* outsources a *controlled function*, such as ~~*internal audit*~~ internal audit it should...
- ...
- 14.1.39 G (1) In accordance with SYSC 3.2.10G a *firm* should consider whether it needs to set up a separate ~~*risk assessment function*~~ risk assessment function (or functions) that is responsible for assessing the risks that the *firm* faces and advising its *governing body* and *senior managers* on them.
- (2) The term 'risk assessment function' refers to the generally understood concept of risk assessment within a *firm*, that is, the function of setting and controlling risk exposure. The risk assessment function is not a *controlled function* itself, but is part of the *systems and controls function* (CF28).
- 14.1.40 G Where a *firm* does decide that it needs a separate ~~*risk assessment function*~~ risk assessment function (see SYSC 14.1.39G), the *employees* or contractors that carry out this function should not normally be involved in risk taking activities such as business line management (see SYSC 14.4.30G to SYSC 14.4.43G on the segregation of duties).
- 14.1.41 G A summary of the results of the analysis undertaken by a *firm's* ~~*risk assessment function*~~ risk assessment function in accordance with SYSC 14.4.39G (including, where necessary, an explanation of any assumptions that were adopted) should normally be reported to relevant *senior managers* as well as to the *firm's governing body*.
- ...
- 14.1.43 G (1) In accordance with SYSC 3.2.15G and SYSC 3.2.16G, a *firm* should consider whether it needs to set up a dedicated ~~*internal audit function*~~ internal audit function.
- (2) The term 'internal audit function' refers to the generally understood concept of internal audit within a *firm*, that is, the function of assessing adherence to and the effectiveness of internal systems and controls, procedures and policies. The internal audit function is not a *controlled function* itself, but is part of the *systems and controls function* (CF28).
- 14.1.44 G Where a *firm* decides to set up an ~~*internal audit function*~~ internal audit function (see SYSC 14.1.43G), this function should provide independent assurance to its *governing body*, audit committee or an appropriate *senior manager* of the integrity and effectiveness of its systems and controls.

14.1.45 G In forming its judgements, the *person* performing the ~~*internal-audit function*~~ internal audit function (see SYSC 14.1.43G) should test the practical operation of a *firm's* systems and controls as well as its accounting and risk policies. This should include examining the adequacy of supporting records.

...

14.1.48 G A *firm* should consider what information needs to be made available to its *governing body* and *senior managers*. Some possible examples include:

- (1) ...
- (3) reports from a *firm's* ~~*internal-audit and risk-assessment functions*~~ internal audit and risk assessment functions (see SYSC 14.1.43G and SYSC 14.1.39G), if applicable, including exception reports, where risk limits and policies have been breached or systems circumvented;
- (4) ...

...

Annex C

Amendments to the Statements of Principle and Code of Practice for Approved Persons

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.1 Application

Who?

1.1.1 G *APER applies to approved persons.*

1.1.2 G The Statements of Principle apply only to the extent that a person is performing a controlled function for which approval has been sought and granted.

1.1.3 G Section 64(11) of the Act states that the power to issue Statements of Principle and codes of practice includes power to make different provisions in relation to persons, cases or circumstances of different descriptions. Statements of Principle 1, 2, 3 and 4 apply to all approved persons, and Statements of Principle 5, 6 and 7 apply to those approved to perform significant influence functions.

1.1.4 G The relevance of MiFID to the Statements of Principle will depend on the extent to which the corresponding requirement imposed on firms under MiFID is reserved to a Home State regulator or has been disapplied under MiFID (see [SIGNPOST – NEWCOB provisions disaplying Art 19, 21 and 22 duties]).

Where?

1.1.4 G The territorial scope of the approved persons regime and its application to incoming EEA firms is set out in SUP 10.1 (see SUP 10.1.13R and 10.1.14R).

1.2	Purpose	
1.2.1	...	
1.2.4	G	Section 64(11) of the Act states that the power to issue Statements of Principle and codes of practice includes power to make different provisions in relation to persons, cases or circumstances of different descriptions. Statements of Principle 1, 2, 3 and 4 apply to all approved persons, and Statements of Principle 5, 6 and 7 apply to those approved to perform significant influence functions.
...		
2.1	The Statements of Principle	
2.1.1	G	...

<u>2.1.1A</u>	P	<u>An approved person will not be subject to a <i>Statements of Principle</i> to the extent that it would be contrary to the <i>UK's</i> obligations under a <i>Single Market Directive</i>.</u>
...		

Annex D

Amendments to The Fit and Proper test for Approved Persons Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.2	Introduction	
...		
1.2.4A	G	<u>Under Article 5(1)(d) of the <i>MiFID Implementing Directive</i> and Article 31 and 32 of <i>MiFID</i>, the requirement to employ personnel with the knowledge, skills and expertise necessary for the discharge of the responsibilities allocated to them is reserved to the <i>firm's Home State</i>. Therefore, in assessing the fitness and propriety of a <i>person</i> to perform a <i>controlled function</i> solely in relation to the <i>MiFID business</i> of an <i>incoming EEA firm</i>, the <i>FSA</i> will not have regard to that <i>person's</i> competence and capability.</u>

Annex E

Amendments to the Fees manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

FEES 4 Annex 1R Activity groups, tariff bases and valuation dates applicable

R Part 1 ...

...

Part 2

...

Activity group	Tariff-base
...	.
A.12	<p>APPROVED PERSONS</p> <p>The number of <i>persons</i> approved to undertake one, or more, of the following customer functions: <u>(CF 30)</u>, but excluding those <i>persons</i> <u>solely acting in the capacity of an investment manager or solely advising clients in connection with corporate finance business or carrying out functions related to these.</u></p> <p>CF21Investment adviser function; CF22Investment adviser (trainee) function; CF24Pension transfer specialist function; CF25Adviser on syndicate participation at Lloyd's function; or CF26Customer trading function.</p>
A.13	<p>APPROVED PERSONS</p> <p>The number of <i>persons</i> approved to undertake one, or more, of the following customer functions <u>(CF 30)</u>, but excluding those <i>persons</i> <u>solely acting in the capacity of an investment manager or solely advising clients in connection with corporate finance business or carrying out functions related to these.</u></p> <p>CF21Investment adviser function; CF22Investment adviser (trainee) function; CF24Pension transfer specialist function; CF25Adviser on syndicate participation at Lloyd's function; or CF26Customer trading function.</p>

A.14	<p>APPROVED PERSONS</p> <p>The number of <i>persons solely</i> approved to undertake the <i>customer function (CF 30)</i> who advise <i>clients in connection with corporate finance business</i> or perform related <i>functions, following (controlled function: CF23Corporate finance adviser function.</i></p>
...	

Annex F

Amendments to the Integrated Prudential Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

- 5.1.75 G In addition to the regular review and evaluation described in *PRU 5.1.74G*, a firm's ~~*internal audit function*~~ internal audit function (see *SYSC 3.2.16G*) should periodically review the liquidity risk management process in order to identify any weaknesses or problems. Any weaknesses should be addressed by management in a timely and effective manner.

...

Annex G

Amendments to Mortgage and Insurance Prudential Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text. The amendments are based on text consulted on in the Consultation Paper Strengthening Capital Standards – Restructuring the Handbook CP 06/10.

...

- 2.2.2 R The *firm* may allocate the responsibility for its *insurance mediation activity* under *MIPRU 2.2.1R* to an *approved person* (or *persons*) performing:
- (1) a *governing function* (other than the *non-executive director function*);
or
 - (2) the *apportionment and oversight function*; or
 - (3) the *significant management* (~~*other business operations*~~) *function* in so far as it relates to *dealing in investments as principal*, disregarding article 15 of the *Regulated Activities Order* (Absence of holding out etc)(or *agreeing to do so*) or an activity which is not *designated investment business*.
- 2.2.3 G ...
- (3) In the case of a *sole trader*, the *sole trader* will be responsible for the *firm's insurance mediation activity*; ~~whether or not he is himself a *person* approved to perform the *sole trader function*.~~

Annex H

Amendments to the Training and Competence Manual

In this Annex, underlining indicates new text and striking through indicates deleted text.

TC 2.5 Appropriate examinations

...

2.5.5 R Time limits

- (1) ...
- (2) ...
- (3) Paragraphs (1)(b) and (c) do not apply for an *employee* who would be performing the functions in SUP 10.10.7R (1), (2) and (6) under the customer function
 - a) ~~the investment adviser function; or~~
 - b) ~~the corporate finance adviser function; or~~
 - c) ~~the investment management function;~~but for the 30-day rule, unless the individual is advising *private customers* retail client on packaged products or is a *broker fund adviser*.
- (4) In (3), the '30-day rule' means the provisions of: SUP 10.10.7AR.
 - a) ~~SUP 10.10.7 R (3); or~~
 - b) ~~SUP 10.10.13 R (2); or~~
 - c) ~~SUP 10.10.20 R (2);~~as appropriate.

Annex I

Amended text to be inserted in the Supervision Manual

In this annex, underlining indicates new text and striking through indicates deleted text. Where an entire section of the text is being deleted, the place where the change will be made is indicated and the text is not struck through.

...

- 4.6.1 G The *Society* must:
- (1) appoint an *actuary* to perform the *Lloyd's actuary* ~~function~~ function;

...

...

- 4.6.8 R An *actuary* who has been appointed to perform the *Lloyd's actuary* ~~function~~ function must:

...

- 10.1.1 R This chapter applies to a every firm that is required under section 59 of the Act to take reasonable care to ensure that one or more persons is approved to perform a controlled function.

...

- 10.1.3 G The *rules* in this chapter specify the descriptions of controlled functions functions under section 59 of the *Act* (Approval for particular arrangements). ~~The effect of these rules, and the provisions of Part V of the Act (Performance of Regulated Activities), is that every firm, except an overseas firm to which SUP 10.1.6R applies, must apply for the approval of one or more persons to perform a controlled function on its behalf.~~

...

- 10.1.5 G [Deleted]

...

- 10.1.7 R Only the following *controlled functions* apply to an *overseas firm* which maintains an establishment in the *United Kingdom* from which *regulated activities* are carried on:
- (1) ...
- (3) the significant management (designated investment business) function;
in so far as the function relates to:

- (a) designated investment business other than dealing in investments as principal, disregarding article 15 of the Regulated Activities Order; or
 - (b) processing confirmations, payments, settlements, insurance claims, client money and similar matters in so far as this relates to designated investment business; and
- (4) [Deleted]
- (5) the *customer functions*:-
- 10.1.8 G [Deleted]
- Incoming EEA firms, incoming Treaty firms and UCITS qualifiers
- ...
- 10.1.13 R Only the following *controlled functions* apply to an *incoming EEA firm* with respect to its *passported activities* carried on from a *branch* in the *United Kingdom*:
- (1) the *EEA investment business oversight function*;
 - (2) the *compliance oversight function*;
 - (3) the *money laundering reporting function*;
 - (4) the *significant management (designated investment business) function* in so far as the function relates to:
 - (a) designated investment business other than dealing in investments as principal, disregarding article 15 of the Regulated Activities Order; or
 - (b) processing confirmations, payments, settlements, insurance claims, client money and similar matters in so far as this relates to designated investment business; and
 - (5) [Deleted]
 - (6) the *customer functions* other than where this relates to the function in SUP 10.10.7R (4) the adviser on syndicate participation at Lloyd's function
- 10.1.13A R If the only investment business carried on by an incoming EEA firm in the United Kingdom is MiFID business, only SUP 10.1.13R (3), (4) and (6) apply to that firm.
- Incoming EEA firms etc with top-up permission activities from a UK branch
- 10.1.14 R In relation to the activities of a *firm* for which it has a *top-up permission*,

only the following *controlled functions* apply:

- (1) the *required functions*, other than the *apportionment and oversight function*;
- (2) the *significant management (designated investment business) function*; in so far as it relates to:
 - (a) designated investment business other than dealing in investments as principal, disregarding article 15 of the Regulated Activities Order; or
 - (b) processing confirmations, payments, settlements, insurance claims, client money and similar matters in so far as this relates to designated investment business; and
- (3) [Deleted]
- (4) the *customer functions*.

10.1.15 G [Deleted]

Appointed representatives

10.1.16 R The descriptions of the following *controlled functions* functions apply to an appointed representative of a firm, except an *introducer appointed representative*, as they apply to a firm:

- (1) the *governing functions*, subject to SUP 10.1.16A R; and
- (2) the *customer functions* other than in relation to acting in the capacity of an investment manager (see SUP 10.10.7R (6)) in the investment management function.

...

10.1.17 G [Deleted]

Members of a profession

10.1.18 R ...

10.1.19 G [Deleted]

10.1.20 G [Deleted]

10.1.21 R The descriptions of *significant influence functions*, other than the *required functions*, and if the firm is a MiFID investment firm, the *governing functions*, do not extend to activities carried on by a firm whose principal purpose is to carry on activities other than *regulated activities* and which is:

....

Committees of the Society of Lloyd's

10.1.24 G [Deleted]

10.1.25 G [Deleted]

...

10.2 Purpose

10.2.1 G The immediate purpose of *SUP* 10.3 to *SUP* 10.10 is to specify, under section 59 of the *Act*, descriptions of the ~~27~~ 16 *controlled functions* which are listed in *SUP* 10.4.5 R. The underlying purpose is to establish, and mark the boundaries of, the "approved persons regime". ~~An *approved person* is a *person*, generally an individual, who is approved to perform a *controlled function*.~~

10.2.2 G [Deleted]

10.2.3 G [Deleted]

10.2.4 G [Deleted]

10.4 Specification of functions

10.4.1 R ...

10.4.2 G [Deleted]

...

10.4.4 G [Deleted]

10.4.5 R Controlled functions

Type	CF	Description of controlled function
<i>Governing functions*</i>	1	<i>Director function</i>
	2	<i>Non-executive director function</i>
	3	<i>Chief executive function</i>
	4	<i>Partner function</i>
	5	<i>Director of unincorporated association function</i>

	6	<i>Small friendly society function</i>
	7	<i>Sole trader function</i> [Deleted]
<i>Required functions*</i>	8	<i>Apportionment and oversight function</i>
	9	<i>EEA investment business oversight function</i>
	10	<i>Compliance oversight function</i>
	11	<i>Money laundering reporting function</i>
	12	<i>Actuarial function</i>
	12A	<i>With-profits actuary function</i>
	12B	<i>Lloyd's actuary function</i>
<i>Systems and controls functions*</i>	13 28	<i>Finance function</i> <i>Systems and controls function</i>
	14	<i>Risk assessment function</i> [Deleted]
	15	<i>Internal audit function</i> [Deleted]
<i>Significant management functions*</i>	16 29	<i>Significant management (designated investment business) function</i>
	17	<i>Significant management (other business operations) function</i> [Deleted]
	18	<i>Significant management (insurance underwriting) function</i> [Deleted]
	19	<i>Significant management (financial resources) function</i> [Deleted]
	20	<i>Significant management (settlements) function</i> [Deleted]
<i>Customer functions</i>	30	<i>Customer function</i>
	21	<i>Investment adviser function</i>
	22	<i>Investment adviser (trainee) function</i>
	23	<i>Corporate finance adviser function</i>

	24	<i>Pension transfer specialist function</i>
	25	<i>Adviser on syndicate participation at Lloyd's function</i>
	26	<i>Customer trading function</i>
	27	<i>Investment management function</i>
<i>*significant influence functions</i>		

10.5 Significant influence functions

10.5.1 G The *significant influence functions*, which are specified in SUP 10.4.1R, comprise the *governing functions* (see SUP 10.6), the *required functions* (see SUP 10.7), the *systems and controls functions* (see SUP 10.8) and the *significant management functions* (see SUP 10.9). SUP 10.5 applies to each of the *significant influence functions*.

...

10.5.4 G Whether a ~~function~~ *controlled function* is likely to result in the *person* responsible for its performance exercising significant influence on the conduct of the *firm's* affairs is a question of fact in each case. The *FSA* has identified the *significant influence functions* as satisfying this condition. ~~What amounts to exercising significant influence in any particular case will depend on the circumstances. The *person* performing one of these functions is likely to play a part in ensuring that effective governance structures, systems and controls are developed and operated. In relation to a *firm* as a whole, this is expected to include setting the business strategy, regulatory climate and ethical standards of the *firm*. In relation to a *branch*, this will include ensuring that the *firm's* strategy (as it affects the *branch*) is appropriate in the context of the *UK regulatory system*, and setting the regulatory climate and ethical standards of the *branch* in the United Kingdom.~~

...

10.6 Governing functions

Introduction

...

10.6.1A G *A sole trader will not fall within the description of the governing functions.*

What the governing functions include

- 10.6.2 R Each of the *governing functions* (other than the *non-executive director function*) includes where apportioned under SYSC 2.1.1 R:
- (1) the systems and controls functions; and
 - (2) the significant management functions.
- 10.6.3 G The effect of SUP 10.6.2 R is that a *person* who is *approved* to perform a *governing function* (other than the *non-executive function*) will not have to be specifically approved to perform ~~any of the systems and controls functions or the significant management functions~~. ~~However, a firm may apply for the systems and control functions or significant management functions to be explicitly added for such persons, if it wishes.~~ A *person* who is *approved* to perform a *governing function* will have to be additionally approved before he can perform any of the *required functions* or the customer functions.
- 10.6.3A G ~~PRU 9.1.3R~~ MIPRU 2.2.1R provides that an *insurance intermediary*, other than a *sole trader*, must allocate to a *director* or *senior manager* the responsibility for the *firm's insurance mediation activity*. ~~PRU 9.1.4R(1)~~ MIPRU 2.2.2R (1) provides that the *firm* may allocate this responsibility to one or more of the *persons* performing a *governing function* (other than the *non-executive director function*).
- 10.6.3B G Where a *person* performing a *governing function* is also responsible for the *firm's insurance mediation activity*, the words "(insurance mediation)" will be inserted after the relevant *controlled function* (see ~~PRU 9.1.7G~~ MIPRU 2.2.5 G).
- Director function (CF1)
- ...
- 10.6.5 G [Deleted]
- 10.6.6 G [Deleted]
- ...
- Non-executive director function (CF2)
- ...
- 10.6.9 G [Deleted]
- 10.6.10 G [Deleted]
- Chief executive function (CF3)
- ...

10.6.12 G [Deleted]

...

10.6.14 G For a *branch* in the *United Kingdom* of an *overseas firm*, the *FSA* would not normally expect the overseas *chief executive* of the *firm* as a whole to be approved for this function where there is a *senior manager* under him with specific responsibility for those activities of the *branch* which are subject to the *UK regulatory system*. In some circumstances, the *person* within the *firm* responsible for *UK* operations may, if the function is likely to enable him to exercise significant influence over the *branch*, also perform the *chief executive function* (see *SUP 10.7.4 G*). ~~The *senior manager* may be called a *Managing Director*, *UK Regional Head*, *Branch Manager*, *UK Country Head*; or, in the case of a non-*EEA insurer* with a *branch* in the *United Kingdom*, *UK chief executive*.~~

...

Partner function (CF4)

...

10.6.18 G [Deleted]

...

10.6.22 G [Deleted]

...

Director of unincorporated association function (CF5)

...

10.6.25 G [Deleted]

Small friendly society function (CF6)

...

10.6.27 G [Deleted]

...

~~Sole trader function (CF7)~~

10.6.30 R [Deleted]

10.6.31 G [Deleted]

10.6.32 G [Deleted]

- 10.7 Required functions
- Apportionment and oversight function (CF8)
- ...
- 10.7.2 G [Deleted]
- ...
- 10.7.4 G Generally, in relation to a *UK* establishment of an *overseas firm* or a *firm* which is part of an *overseas group*, where an overseas manager's responsibilities in relation to the *United Kingdom* are strategic only, he will not need to be an *approved person*. However, where, in accordance with *SYSC 3* or *SYSC 4* to *SYSC10*, he is responsible for implementing that strategy in the *United Kingdom*, and has not delegated that responsibility to a *senior manager* in the *United Kingdom*, he is likely to be performing a *controlled function*, such as, for example, the *chief executive function*. This is subject to SUP 10.1.13AR, which applies where the firm is a MiFID investment firm and the only investment business carried out by it in the United Kingdom is MiFID business.
- 10.7.4A G ~~PRU 9.1.3R~~ MIPRU 2.2.1R provides that an *insurance intermediary*, other than a *sole trader*, must allocate to a *director* or *senior manager* the responsibility for the *firm's insurance mediation activity*. ~~PRU 9.1.4R (2)~~ MIPRU 2.2.2R (2) provides that the *firm* may allocate this responsibility to the *person* performing the *apportionment and oversight function*.
- 10.7.4B G Where the *person* performing the *apportionment and oversight function* is also responsible for the *firm's insurance mediation activity*, the words "(insurance mediation)" will be inserted after this *controlled function* (see ~~PRU 9.1.7G~~ MIPRU 2.2.5G).
- 10.7.5 G [Deleted]
- ...
- Compliance oversight function (CF10)
- 10.7.8 R The *compliance oversight function* is the function of acting in the capacity of a *director* or *senior manager* who is allocated the function set out in *SYSC 3.2.8 R* or *SYSC 6.1.4R (2)*.
- 10.7.9 G [Deleted]
- 10.7.10 G [Deleted]
- 10.7.11 G [Deleted]
- 10.7.12 G [Deleted]

Money laundering reporting function (CF11)

...

- 10.7.14 G A firm's obligations in respect of its money laundering reporting officer are set out in SYSC 3.2.61R and SYSC 6.

Actuarial function (CF 12) and *with-profits actuary function* (CF12A)

...

- 10.7.18 G [Deleted]

- 10.7.19 G [Deleted]

- 10.7.20 G [Deleted]

- 10.7.21 G [Deleted]

Lloyd's actuary function (CF12B)

- 10.7.22 R ~~The Lloyd's actuary function~~ function is the function of acting in the capacity of the *actuary* appointed under SUP 4.6.1R to perform the duties set out in SUP 4.6.7R.

- 10.7.23 G [Deleted]

10.8 Systems and control functions

~~Finance~~ Systems and controls function (CF13 28)

- 10.8.1 R ~~The finance function is the function of acting in the capacity of a senior manager with responsibility for reporting to the governing body of a firm in relation to its financial affairs.~~ The systems and controls function is the function performed by an employee of the firm with responsibility for reporting to the governing body of a firm, or the audit committee (or its equivalent) in relation to:

- (1) its financial affairs;
- (2) setting and controlling its risk exposure (see SYSC 3.2.10G and SYSC 7.1.6R);⁴
- (3) adherence to internal systems and controls, procedures and policies (see SYSC 3.2.16G and SYSC 6.2⁵).

⁴ SYSC 7.1.6R is the subject of consultation in the Consultation Paper Organisation Systems and Controls – Common Platform for firms CP 06/9 see p. 26 of Annex 4.

- 10.8.2 G [Deleted]
- 10.8.2A G Where an *employee* performs the *systems and controls function* the *FSA* would expect the firm to ensure that the *employee* had sufficient expertise and authority to perform that function effectively. A *direction* or *senior manager* would meet this expectation.

~~Risk assessment function (CF14)~~

10.8.3 R [Deleted]

10.8.4 G [Deleted]

10.8.5 G [Deleted]

~~Internal audit function (CF15)~~

10.8.6 R [Deleted]

10.8.7 G [Deleted]

10.8.8 G [Deleted]

10.9 Significant management functions

Application

10.9.1 R *SUP* 10.9 applies only to a *firm* which, under *SYSC* 2.1.1 R, apportions a significant responsibility, within the description of a the significant management function, to a *senior manager* of a significant business unit.

10.9.2 G The *FSA* anticipates that there will be only a few *firms* needing to seek approval for an individual to perform a ~~the significant management function~~. In most *firms*, those approved for the *governing functions*, *required functions* and, where appropriate, the *systems and controls functions*, are likely to exercise all the significant influence at senior management level.

10.9.3 G However, the scale, nature and complexity of the *firm's* business may be such that a *firm* apportions under *SYSC* 2.1.1 R a significant responsibility to an individual who is not approved to perform the *governing functions*, *required functions* or, where appropriate, the *systems and controls functions*. If so, the *firm* should consider whether the functions of that individual fall within a the significant management function. For the purposes of the description of the *significant management function*, the following additional factors about the *firm* should be considered:

		...
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⁵ *SYSC* 6.2 is the subject of consultation in the Consultation Paper Organisation Systems and Controls – Common Platform for firms CP 06/9 see p. 23 of Annex 4.

10.9.5 G The question may arise whether a manager who is based overseas will be performing a *controlled function* (such as the *significant management (designated investment business) function*) and should therefore be an *approved person*. This is especially true where the *firm* operates matrix management. The fact there is a *person* performing the *apportionment and oversight function*, and who has responsibility for activities subject to regulation by the *FSA*, may have a bearing on this. It is a factor to take into account when assessing the likely influence of the overseas manager.

...

...

10.9.7 G See also *SUP* 10.7.3G to *SUP* 10.7.4B 5G in relation to matrix management.

...

Significant management (designated investment business) function (CF16 29)

10.9.10 R (1) ~~The *significant management (designated investment business) function* is the function of acting as a *senior manager* with significant responsibility for a significant business unit which carries on *designated investment business* other than *dealing in investments as principal*, disregarding article 15 of the *Regulated Activities Order* (Absence of holding out etc), (and agreeing to do so). The *significant management function* is the function of acting as a *senior manager* with significant responsibility for a significant business unit that:~~

(a) carries on *designated investment business* or other activities not falling with (b) – (d);

(b) *effects contracts of insurance* (other than *contractually based investments*);

(c) makes material decisions on the commitment of a *firm's* financial resources, its financial commitments, its assets acquisitions, its liability management and its overall cash and capital planning;

(d) processes confirmations, payments, settlements, insurance claims, *client money* and similar matters.

(2) This ~~function~~ *controlled function* does not include any of the activities described in any other *controlled function*.

10.9.10A G A *senior manager* with significant responsibility for a significant business unit that carries on activities other than *designated investment business* for the purposes of *SUP* 10.9.10R (1)(a) could, for example, be the head of a unit carrying on the activities of: retail banking, personal lending, corporate lending, salvage or loan recovery, or proprietary trading; or a member of a committee (that is, a *person* who, together with others, has authority to

commit the *firm*) making decisions in these functions. The *senior manager* could also be a proprietary trader whose trading limits are such that he may put, or potentially put, his *firm* at significant risk. This function would not extend to every proprietary trader.

10.9.11 G [Deleted]

~~Significant management (other business operations) function (CF17)~~

10.9.12 R [Deleted]

10.9.13 G [Deleted]

10.9.13A G ~~PRU 9.1.3R MIPRU 2.2.1R~~ provides that an *insurance intermediary*, other than a *sole trader*, must allocate to a *director* or *senior manager* the responsibility for the *firm's insurance mediation activity*. ~~PRU 9.1.4R(3) MIPRU 2.2.2R (3)~~ provides that the *firm* may allocate this responsibility to the *person* performing the *significant management (other business operations) function*.

10.9.13B G Where the *person* performing the *significant management (other business operations) function* is also responsible for the *firm's insurance mediation activity*, the words "(insurance mediation)" will be inserted after this *controlled function* (see ~~PRU 9.1.7G MIPRU 2.2.5 G~~).

~~Significant management (insurance underwriting) function (CF18)~~

10.9.14 R [Deleted]

10.9.15 G [Deleted]

~~Significant management (financial resources) function (CF19)~~

10.9.16 R [Deleted]

10.9.17 G [Deleted]

~~Significant management (settlements) function (CF20)~~

10.9.18 R [Deleted]

10.9.19 G [Deleted]

10.9.20 G [Deleted]

10.10 Customer functions

10.10.1 R *SUP 10.10 (Customer functions)* applies with respect to activities carried on from an establishment maintained by the *firm* (or by its *appointed*

representative) in the *United Kingdom*.

10.10.2 G Without *SUP* 10.10.1 R the descriptions of the *customer functions* would extend to this functions wherever it was ~~they are~~ performed. The effect of *SUP* 10.10.1 R is that the descriptions ~~are~~ is limited, in relation to *regulated activities* with an overseas element, in a manner which is broadly consistent with the scope of conduct of business regulation.

10.10.3 G The *customer functions* ~~have~~ has to do with giving advice on, *dealing* and arranging deals in and *managing investments*; ~~they have~~ it has no application to banking business such as deposit taking and lending, nor to *general insurance business*.

...

The customer conditions (the second and third conditions)

10.10.4 R ~~Each~~ The *customer function* is one which will involve the *person* performing it in dealing with *clients* ~~customers~~, (and for the corporate finance adviser function, *clients*), or dealing with property of *clients* ~~customers~~, of a *firm* in a manner substantially connected with the carrying on of a *regulated activity* of the *firm*.

10.10.5 G *SUP* 10.10.4 R gives effect to sub-sections (6) and (7) of section 59 of the *Act* (referred to in that section as the second and third conditions). *Customer* is given the meaning in the *Glossary* (which is not the same as the definition given in section 59 (11) of the *Act*).

...

~~Investment adviser function (CF21)~~ Customer function (CF 30)

10.10.7 R (1) ~~The investment adviser function is the function of:~~
The customer function is the function of:

(a) ~~advising on investments other than a non-investment insurance contract; and~~

(b) ~~performing functions within the customer trading function in connection with advising on investments other than non-investment insurance contracts.~~

- (2) This function does not include:
- (a) ~~the investment adviser (trainee) function;~~
 - (b) ~~the pension transfer specialist function;~~ and
 - (c) ~~advising on investments in the course of carrying on the activity of providing basic advice on a stakeholder product.~~
- (3) This function does not extend to an individual who is based overseas and who, in a 12 month period, spends no more than 30 days in the United Kingdom to the extent that he is appropriately supervised by a person approved for this function.
- (1) advising on investments other than a non-investment insurance contract (but not where this is advising on investments in the course of carrying on the activity of providing basic advice on a stakeholder product) and performing other functions related to this such as dealing and arranging;
 - (2) giving advice to clients solely in connection with corporate finance business and performing other functions related to this;
 - (3) giving advice or performing related activities in connection with pension transfers or opt-outs for retail clients;
 - (4) giving advice to a person to become, or continue or cease to be, a member of a particular Lloyd's syndicate;
 - (5) dealing, as principal or as agent, and arranging (bringing about) deals in investments other than a non-investment insurance contract with or for, or in connection with customers where the dealing or arranging deals is governed by COB 7 (Dealing and managing);
 - (6) acting in the capacity of an investment manager and carrying on functions connected to this.

10.10.7A R The customer function does not extend to an individual who is performing the functions in SUP 10.10.7R (1) - (2) or SUP 10.10.7R (5) – (6) and who is based overseas and who, in a 12 month period, spends no more than 30 days in the United Kingdom to the extent that he is appropriately supervised by a person approved for this function.

- 10.10.7B G The FSA would expect an individual from overseas to be accompanied on a visit to a customer. TC 2.5.5R (1) provides that the firm will have to be satisfied that the individual has at least three years' up-to-date relevant experience obtained outside the United Kingdom. However, the remaining provisions of TC 2.5.5R (1) are disapplied in these circumstances (except for an individual who gives advice to retail clients on packaged products or is a broker fund adviser). The effect of this is that such individuals need not pass the relevant regulatory module of an appropriate examination (see TC 2.5.5R (3) and TC 2.5.5R (4)).
- 10.10.7C G The customer function in SUP 10.10.7R (5) does not extend to the individual who, on the instructions of the customer, simply inputs the customer's instructions into an automatic execution system where no discretion is or may be exercised by the individual carrying out the activity. Nor does it extend to merely introducing a customer to a firm or distributing advertisements.
- 10.10.7D G An individual may advise on investments if they have not yet been assessed as competent in accordance with the rules in the Training and Competence sourcebook (TC).
- 10.10.8 G [Deleted]
- 10.10.9 G [Deleted]
- 10.10.10 G [Deleted]
- 10.10.11 R [Deleted]
- 10.10.12 G [Deleted]
- 10.10.13 R [Deleted]
- 10.10.13A G [Deleted]
- 10.10.14 R [Deleted]
- 10.10.15 R [Deleted]

- 10.10.16 R [Deleted]
- 10.10.17 G [Deleted]
- 10.10.18 G [Deleted]
- 10.10.19 G [Deleted]
- 10.10.20 R [Deleted]
- 10.10.21 G [Deleted]
- 10.10.22 G [Deleted]

		Frequently asked questions	
		G	
10 Ann 1 10 Ann 1G:		Question	Answer
		Requirements of the regime	
	1	...	
	2	What are the procedures for 'emergency situations'?	Individuals may perform <u>the significant influence functions</u> for up to 12 weeks in any consecutive 12 month period without requiring approval. When it becomes clear that a <i>person</i> will be performing the function on a permanent basis, then an application for approval should be made. However, there is no provision for individuals to perform the <i>customer functions</i> on a continuing basis without approval. See SUP 10.5.5 R.
		...	
	6	Can a <i>significant influence function</i> be outsourced?	It is a question of fact in each case who is performing a <u>the significant influence function</u> . <u>Thise</u> functions <u>are</u> mostly

		described at a high level of responsibility, that is, for example, the <i>director</i> of a <i>company</i> or a <i>partner</i> in a <i>partnership</i> . The <i>persons</i> or <i>persons</i> performing <u>these</u> functions cannot avoid their ultimate responsibility and therefore the need for approval. However, some of the <i>significant influence functions</i> may be performed by a <i>person</i> who is specifically brought in to do the job, for example the <i>chief executive function</i> (where it is to be performed by a <i>body corporate</i>) and the <i>actuarial</i> and <i>with-profits actuarial functions</i> .
	...	
11	What checks must <u>should</u> a <i>firm</i> make on a <i>candidate</i> before submitting an application for approval from the <i>FSA</i> ?	The <i>FSA</i> expects <i>firms</i> to perform due and diligent enquiries about their <i>candidates</i> <u>before they submit an application to us for approval</u> . Our approval process is not a substitute for the checks that a <i>firm</i> should be carrying out on its prospective recruits. It is for the <i>firm</i> to determine what checks are appropriate but in making its decision, a <i>firm</i> should have regard to the <i>controlled function</i> to which the application relates. Note also the provisions of <i>ENF</i> 8.12.2 G (Publication) and <i>TC</i> 2.2.1R (Recruitment).
11A	Should these checks include a check of criminal records?	It is for senior management to decide what checks should be made. <u>In deciding if it is necessary to carry out a check of criminal records</u> , the <i>firm</i> should consider that the <i>FSA</i> does not routinely carry out these checks during the approval process. By virtue of the Rehabilitation of Offenders Act 1974 (Exceptions) Order 1975 (see Articles 3 and 4 of the Order), the <i>FSA</i> and the industry also have a right to ask about spent, as well as unspent, criminal convictions for employment purposes about <i>candidates</i> for <i>approved person</i> status (see Question 5.01a of Form A (Application to perform controlled functions under the approved persons regime)). Note also the provisions of <i>ENF</i> 8.12.2 G (Publication) and <i>TC</i> 2.2.1 R (Recruitment).

Activity	Paragraph 1 of the table in TC 2.1.4R	Controlled Function	SUP
Advising and dealing	(a) – (c)	<i>investment adviser function</i> (CF21) <i>investment adviser (trainee) function</i> (CF22)	10.10.7R 10.10.11R
Managing	(d) and (e)	<i>investment management function</i> (CF27)	10.10.20R
Advising (without dealing)	(f) – (h)	<i>investment adviser function</i> (CF21) <i>investment adviser (trainee) function</i> (CF22)	10.10.7R 10.10.11R
	(i)	<i>corporate finance adviser function</i> (CF23)	10.10.13R
	(j) – (m)	<i>investment adviser function</i> (CF21)	10.10.7R
		<i>investment adviser (trainee) function</i> (CF22)	10.10.11R
	(n)	<i>adviser on syndicate participation at Lloyd's function</i> (CF25)	10.10.15R
	(o)	<i>pension transfer specialist function</i> (CF24)	10.10.14R
Advising and dealing, Managing, Advising (without dealing)	(a) – (c), (d) and (e), (f) – (o)	<i>customer function</i> (CF 30)	10.10.4R

12.2.14 G (1) ...

- (2) If a firm appoints an appointed representative who is an individual in (1), that appointed representative will also be a representative. The individual may need to be approved to perform the *investment adviser function* or the *customer trading function* or both and possibly also the *sole trader function* *customer function*, (see SUP 12.6.8 G and SUP 12.6.9 G). In these circumstances, in addition to complying with the requirements of SUP 12 and other regulatory requirements, the firm should ensure that the rules for representatives in COB 5 (Advising and selling) are complied with.

...

Obligations of firms under the approved persons regime

- 12.6.8 G (1) Some of the *controlled functions*, as set out in SUP 10.4.1 R, apply to an *appointed representative* of a *firm*, other than an *introducer appointed representative*, just as they apply to a *firm* (see SUP 10.1.16 R). These are the *governing functions* and the *customer functions* (other than the *investment management function*) such as, for example, CF 21, the *investment adviser function*. As explained in SUP 10.1.16A R, ~~SUP 10.1.17G (3)~~ and SUP 10.3.2 G respectively:
- (a) ...
 - (b) although the *customer functions* (other than the *investment manager function*) ~~apply~~ applies to an appointed representative, the descriptions of the functions themselves do not extend to ~~mortgage mediation activity~~ mortgage mediation activity or *insurance mediation activity*; and
 - (c) ...
- (2) The *approved persons* regime applies differently to an *appointed representative* whose scope of appointment includes *insurance mediation activity* in relation to *non-investment insurance contracts* but no other *regulated activity* and whose principal purpose is to carry on activities other than *regulated activities*. These *appointed representatives* need only one *person* performing one of the *governing functions*. This means that only one *director* (or equivalent) of these *appointed representatives* must be approved under section 59 of the *Act* for the performance of the *director function*, the *chief executive function*, the *partner function* or the *director of unincorporated association function*, whichever is the most appropriate (see SUP 10.1.16AR and ~~SUP 10.1.17G (3)~~).

Part 1:

Transitional provisions applying to the Supervision manual only

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provision coming into force
...					
<u>8A</u>	<u>SUP 10.4.1R</u>	<u>R</u>	<u>(1) An application made under section 60 of the Act received before 31</u>	<u>From 1 November 2007</u>	<u>From 1 November 2007</u>

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
			<p><u>October 2007 will be taken to relate to the <i>controlled function</i> existing at the date of determination.</u></p> <p><u>(2) The <i>controlled functions</i> CF 13 (<i>finance function</i>), CF 14 (<i>risk assessment function</i>) and CF 15 (<i>internal audit function</i>) are subsumed in the new <i>controlled function</i> CF 28 (<i>systems and controls function</i>) to the extent that they fall within the description of the <i>systems and controls function</i>.</u></p> <p><u>(3) The <i>controlled functions</i> CF 16 (<i>significant management (designated investment business) function</i>), CF 17 (<i>significant management (other business operations) function</i>), CF 18 (<i>significant management (insurance underwriting) function</i>), CF 19 (<i>significant management (financial resources) function</i>) and CF 20 (<i>significant management (settlements) function</i>) are subsumed in the new <i>controlled function</i> CF 29 (<i>significant management function</i>).</u></p>	<p><u>On 1 November 2007</u></p> <p><u>On 1 November 2007</u></p>	<p><u>On 1 November 2007</u></p> <p><u>On 1 November 2007</u></p>

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
			<p><u>to the extent that they fall within the description of the <i>Significant management function</i>.</u></p> <p><u>(4) The <i>controlled functions</i> CF 21 (<i>investment adviser function</i>), CF 22 (<i>investment adviser (trainee) function</i>), CF 23 (<i>corporate finance adviser function</i>), CF 24 (<i>pension transfer specialist function</i>), CF 25 (<i>adviser on syndicate participation at Lloyd's function</i>), CF 26 (<i>customer trading function</i>) and CF 27 (<i>investment management function</i>) are subsumed in the new <i>controlled function</i> CF 30 (<i>customer function</i>) to the extent that they fall within the description of the <i>customer function</i>.</u></p>	<p><u>On 1 November 2007</u></p>	<p><u>On 1 November 2007</u></p>
8B		G	<p><u>(1) The effect of TP 8AR is that if immediately prior to 1 November 2007 a <i>person</i> was an <i>approved person</i> in relation to any of the <i>controlled functions</i> to be subsumed into the <i>Systems and controls function</i> the original grant of approval by the</u></p>		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
			<p><u>FSA will remain valid in relation to the <i>Systems and controls function</i> and no new approval to perform that <i>controlled function</i> will be required.</u></p> <p><u>(2) The effect of TP 8AR is that if immediately prior to 1 November 2007 a <i>person</i> was an <i>approved person</i> in relation to any of the <i>controlled functions</i> to be subsumed into the <i>Significant management function</i> the original grant of approval by the <i>FSA</i> will remain valid in relation to the <i>Significant management function</i> and no new approval to perform that <i>controlled function</i> will be required.</u></p> <p><u>(3) The effect of TP 8AR is that if immediately prior to 1 November 2007 a <i>person</i> was an <i>approved person</i> in relation to any of the <i>controlled functions</i> to be subsumed into the <i>Customer function</i> the original grant of approval by the <i>FSA</i> will remain valid in relation to the <i>Customer function</i> and no new</u></p>		

(1)	(2) Material to which the transitional provision applies	(3)	(4) Transitional provision	(5) Transitional provision: dates in force	(6) Handbook provision coming into force
			<u>approval to perform controlled function will be required.</u>		
		<u>G</u>	<u>Firms are reminded of their obligation under SUP 10.13.16R to notify FSA if the firm becomes aware of information which would be reasonably material to the continuing assessment of an approved person's fitness and propriety and in particular their competence to carry on an activity.</u>		
<u>8D</u>	<u>SUP 10.13.6R (Ceasing to perform a controlled function) and SUP 10.13.3D (Moving within a firm)</u>	<u>R</u>	<u>The obligation to submit Form C or Form E does not apply in relation to a person who:</u> <u>(a) ceases to perform a controlled function because that controlled function ceases to exist on 1 February 2007; or</u> <u>(b) performs a function which falls within the description of a different controlled function after 1 November 2007 as a result of TP 8AR..</u>	<u>From 1 February 2007 in relation to the sole trader function and 1 November 2007 in all other cases.</u>	<u>From 1 February 2007 in relation to the sole trader function and 1 November 2007 in all other cases.</u>

Annex J

Amendments to the Credit Unions Sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

2.4.4 G ...For example, *CRED* 4.3.11E indicates that a failure of a *credit union* to have an ~~*internal audit function*~~ internal audit function would “tend to establish contravention” of the *rule* (described earlier in *CRED* 4.3.1G) that all *firms* should take reasonable care to establish and maintain such systems and controls as are appropriate to their business.

...

4.3.11 E (1) A *credit union* should have an ~~*internal audit function*~~ internal audit function (this may be either in house or outsourced to a third party).

...

4.3.12 G The term 'internal audit function' in *CRED* 4.3.11E refers to the generally understood concept of internal audit within a *firm*, that is, the function of assessing adherence to and the effectiveness of internal systems and controls, procedures and policies. The internal audit function is not a *controlled function* itself, but is part of the *systems and controls function* (CF28). Guidance on internal audit is given in *CRED* 4.3.50G - *CRED* 4.3.60G.

...

4.3.50 G *CRED* 4.3.11E states that ~~an *internal audit function* should oversee the internal audit process~~ a *credit union* should have an internal audit function (see also *CRED* 4.3.12G).

...

4.3.54 G The ~~*internal audit function*~~ internal audit function (see *CRED* 4.3.12G) should develop an audit plan, covering all aspects of the *credit union's* business....

...

4.3.56 G The key elements of a satisfactory system of internal audit include the following:

- (1) Terms of reference. These should be specified with precision and include, amongst other things, scope and objectives of the audit committee and the *internal audit function* internal audit function (see *CRED 4.3.12G*), access to records, powers to obtain information and explanations for *officers*, and reporting requirements. These should be approved by the committee of management.

...

4.3.57 G The *internal audit function* internal audit function (see *CRED 4.3.12G*) should be independent of all of the functions it inspects.

...

4.3.59 G The qualifications, experience and training of individuals performing the *internal audit function* internal audit function (see *CRED 4.3.12G*) should be adequate in relation to its objectives.

4.3.60 G The committee of management should be satisfied that the *internal audit function* internal audit function (see *CRED 4.3.12G*) is being properly carried out. In order to review the overall effectiveness of the *internal audit function* internal audit function it should consider the following:

...

- (5) a review of the overall effectiveness of the *internal audit function* internal audit function.

...

6.3.9 G *SUP 10.8*: the systems and controls functions:

- (1) *SUP 10.8.1R* the *finance function*

The function of acting in the capacity of a *senior manager* with responsibility for reporting to the committee of management in relation to its financial affairs.

- (2) *SUP 10.8.3R*: the *risk assessment function*

The function of acting in the capacity of a *senior manager* with responsibility for reporting to the committee of management on the setting and controlling of its risk exposure.

- (3) *SUP 10.8.6R*: the *internal audit function*

The function of acting in the capacity of a *senior manager* with responsibility for reporting to the committee of management in relation to its adherence to internal systems and controls, procedures and policies.

The function of acting as an *employee* with responsibility for reporting to the committee of management in relation to:

- (1) its financial affairs;
- (2) setting and controlling its risk exposure; or
- (3) adherence to internal systems and controls, procedures and policies.

6.3.9A G Where an *employee* performs the *systems and controls function* FSA would expect the firm to ensure that the *employee* had sufficient expertise and authority to perform that function effectively, for example be a *director* or *senior manager*.

6.3.10 G *SUP* 10.9: the significant management functions: ~~These~~
This controlled functions will only apply to the credit union if the functions ~~are~~ is not being performed by a member of the committee of management and the credit union has followed the guidance in *SUP* 10.9.3G.

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