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Financial Services Authority

The Conduct of Business Sourcebook

February 2000



The Conduct of Business Sourcebook

- 1 The following is the Executive Summary taken from the FSA's consultation paper 45. This is being sent to all firms.
- 2 Firms or other interested parties can access the full consultation paper and draft rules on the FSA website: www.fsa.gov.uk.
- 3 Alternatively, you can request a printed copy of the consultation paper by calling 0845 675 6775 quoting reference 45aDR. There is normally no additional charge for this service.

The FSA would welcome comments on consultation paper 45. Comments must be received by 19 May 2000*. You can send your response by electronic submission using the form on the FSA's website (at www.fsa.gov.uk/cp-question/cp45q.pdf), in writing or by e-mail to the following:

Brenda Gibson
Investment Business Policy Department
The Financial Services Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

Telephone: 020 7676 5648
Fax: 020 7676 5649
E-mail: conduct.business@fsa.gov.uk

It is the FSA's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise.

*** The consultation period for CP45, 'The Conduct of Business Sourcebook', has been extended. The period for consultation responses now closes on 30 June 2000.**

Executive summary

- 1.1 This paper sets out for comment the FSA's draft Conduct of Business Sourcebook (COBS), the part of the FSA Handbook of rules and guidance containing the detailed conduct of business requirements for firms regulated by the FSA.
- 1.2 COBS contains the rules and guidance which will apply principally to firms' dealings with private and intermediate customers (CP43, published on 10 February, sets out the FSA's proposed approach to the classification of customers). In some cases, as with client money and custody, for example, the rules and guidance will apply to a firm's dealings with all its clients. The Market Conduct and Infrastructure Sourcebook will contain the new inter-professional code aimed principally at dealings between market counterparties. The FSA will consult separately on this.
- 1.3 The content of COBS relates mainly to the business of investment firms (that is, firms conducting 'investment business' as currently defined in the Financial Services Act 1986). However, it also contains rules and guidance of relevance to deposit takers, general insurers and certain participants in the Lloyd's market. Most of these latter provisions are designed to give effect to the new requirements in the Financial Services and Markets Bill ('the Bill') relating to financial promotions. These new requirements replace existing provisions in the Insurance Companies Act 1982, the Banking Act 1987, the Building Societies Act 1986 and the Financial Services Act 1986.
- 1.4 Investment firms will find that COBS has a wider scope than the equivalent conduct of business requirements which they have to meet at present. For example, the separate rules relating to client money and custody have been brought within COBS.
- 1.5 When enacted the Bill will give the FSA power to make rules which apply to the regulated and non-regulated activities of authorised persons. It will also have the power to make rules about financial promotions and the holding of

client money. The FSA proposes to use these powers to make the conduct of business rules set out in this paper. These rules will support pursuit of our consumer protection objective. They will also have a bearing on our achievement of our other statutory objectives.

- 1.6 The FSA's aim has been to produce a consolidated set of rules which is fit for purpose from N2 (the date on which the FSA assumes its full powers and which we are assuming to be in October 2000). Our approach, therefore, has generally been to replace and integrate the existing standards, which are principally contained in the rulebooks of the self-regulating organisations (SROs) and the recognised professional bodies (RPBs). We have reviewed those existing standards from first principles to satisfy ourselves that they will fulfil what is expected of the FSA, particularly as regards the principles of good regulation as set out in the Bill. In framing the new rules we have also sought to harmonise the existing, and usually small, differences among rulebooks which cannot now be justified on policy grounds. In some instances, however, we have upheld differences where they are appropriate and there appears good reason to do so. Firms will therefore find much which is familiar to them in both the scope and content of these requirements. There are, however, some new features in COBS, particularly the section on 'financial promotion', which stem from the new approach to this subject in the Bill.
- 1.7 We envisage that over time the rules in COBS will be reviewed because of shifting consumer needs and market developments. Another stimulus to review of the COBS rules will be the FSA's strategic review of its regulatory approach, details of which were set out in 'A New Regulator for the New Millennium' published in January 2000. There are also some other specific developments already identifiable as possible influences on COBS after N2. They are:
- the outcome of consideration of the polarisation regime, following the OFT report, on which the FSA has recently announced a research study;
 - the FSA's programme of consumer research which will look at aspects of consumers' understanding and use of the information which firms must disclose;
 - a project on 'Comparative Information' details of which we gave in CP28 published in October 1999;
 - a review of the FSA's policy post-N2 on 'best execution' requirements on firms dealing for customers;
 - the Government's planned introduction from April 2001 of Stakeholder Pensions subject to minimum standards.

1.8 The FSA has recently published two other consultation papers which are complementary to this one:

- *Customer Classification* (CP43) – which sets out our proposals for how customers should be classified and is relevant in deciding which of the COBS requirements apply to which customers; and
- *Protecting Client Money on the failure of an authorised firm* (CP38) – exposes the issues which can arise when a firm handling client money is in default.

Responses on these subjects (on which the FSA will shortly be publishing draft rules as a Supplement to this paper) will be taken into account along with those to the present paper in finalising COBS. The Supplement will also cover draft rules on certain other matters which it has not been possible to cover in this paper. Details of these matters are given in the main text of this paper.

1.9 The FSA seeks comment on this CP by 19 May. We will publish the final version of COBS to be available to any newly-authorized firm ahead of N2. There will, however, be some transitional arrangements for existing firms. Our aim will be to provide a sufficient period to ensure a smooth and orderly transition to the new regime.

1.10 Within the text of the CP, we have highlighted specific issues on which we would welcome comment but, more generally, we are seeking comment on all of the draft rules and guidance covered by this paper. We have conducted some preliminary consultation with practitioners on some key sections of COBS. However, we need to know in particular that in consolidating a number of different rulebooks we have not inadvertently created any technical or practical difficulties. We also need to be confident the rules will deliver an adequate standard of protection for consumers.

The Financial Services Authority
25 The North Colonnade Canary Wharf London E14 5HS
Telephone: +44 (0)20 7676 1000 Fax: +44 (0)20 7676 1099
Website: <http://www.fsa.gov.uk>

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