

**POSITION PAPER
NO. 1 2013**

On the Review of Financial Advice

ISSUED 13 JUNE 2013

POSITION PAPER

If you require any assistance or clarification, wish to discuss any aspect of this Position Paper or have any observations please contact the Jersey Financial Services Commission (the “**Commission**”).

Responses to this Position Paper are not requested but any general questions or comments as to the policy outlined here should be sent to the following contact at the Commission. Any specific queries from registered persons as to the application to their businesses of the policies set out here should be directed to their usual contact at the Commission.

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Glossary of Terms

APCIMS	means the Association of Private Client Investment Managers and Stockbrokers.
the Commission	means the Jersey Financial Services Commission.
the Commission Law	means the Financial Services Commission (Jersey) Law 1998, as amended.
CPD	means Continuing Professional Development.
Feedback Paper	means the Commission's Feedback on Position Paper 1 on the RFA issued in November 2012.
the FCA	means the United Kingdom's Financial Conduct Authority.
the FSA	means the United Kingdom's Financial Services Authority.
the FS(J)L	means the Financial Services (Jersey) Law 1998, as amended.
the IB Codes	means the Codes of Practice for Investment Business.
Investment Employee	means an individual that meets the definition of an investment employee as provided in the Investment Business Fees Notice published on the Commission Website: http://www.jerseyfsc.org/the_commission/fees_notices/index.asp
JFA	means the Jersey Funds Association.
JCOA	means the Jersey Compliance Officers Association.
MiFID	means the Markets in Financial Instruments Directive.
Position Paper 1	means the Commission's Position Paper No. 1 2011 on the RFA issued in August 2011.
Position Paper 2	means this Position Paper on the RFA (No. 1 2013 issued in June 2013).
Professional Client	means a client within the definition set out in paragraph 4.7.4 to 4.7.8 of Position Paper 2.
QCF	means Qualifications and Credit Framework.
RDR	means the FSA's Retail Distribution Review.
RFA	means the Commission's Review of Financial Advice.
SPS	means a Statement of Professional Standing.

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1 Executive Summary

1.1 Overview

- 1.1.1 The Commission issued [Position Paper No. 1 2011](#) (“**Position Paper 1**”) as its first step in relation to its work on the Review of Financial Advice (“**RFA**”). Position Paper No. 1 2013 (“**Position Paper 2**”) now sets out (without reasons) the position reached by the Commission as the result of this process. The reasons for reaching the conclusions reflected here were set out in its [Feedback Paper on Position Paper 1](#) issued in November 2012 (the “**Feedback Paper**”).
- 1.1.2 RFA is the Commission’s response to the Retail Distribution Review (“**RDR**”), which was initiated by the UK’s Financial Services Authority (the “**FSA**”). The RDR is now being progressed by the UK’s Financial Conduct Authority (the “**FCA**”), the successor organisation to the FSA.
- 1.1.3 The RDR is a key part of the FCA’s consumer protection strategy. The aim of the RDR is to improve clarity for people who are looking to invest, raise the professional standards of advisers, and reduce the conflicts of interest which are found in commission-based remuneration for adviser services.
- 1.1.4 The intention was and remains that the RDR will result in a modernisation of the industry to address a market that the FSA felt was not working, in that it did not work well for consumers, advisers or the firms which provide these products and services.
- 1.1.5 Some of the concerns identified by the FSA also exist in Jersey. The Commission has addressed these in its RFA.
- 1.1.6 The Commission’s final position is set out in Section 4 of Position Paper 2. This is the position which will apply from 1 January 2014 to registered persons carrying on Class C or D Investment Business in or from within Jersey and it is hoped that it will be of assistance to registered persons in reviewing their operations and making any changes to ensure that they will comply with the new requirements from 1 January 2014.

1.2 Review of the Reasons for RFA

- 1.2.1 The two key proposals of the RDR are:
 - 1.2.1.1 to increase professional standards of all retail investment advisers; and
 - 1.2.1.2 to address the potential for adviser remuneration (initial and trail commissions) to result in biased advice.
- 1.2.2 The Commission considers, and the feedback received to Position Paper 1 largely supports the view, that increasing professional standards together with new adviser charging requirements will contribute significantly to the

reduction of risk to the public of financial loss due to incompetence, dishonesty or malpractice of persons carrying on the business of financial services in or from within Jersey. Further, these measures will protect and enhance the reputation of Jersey in commercial and financial matters. This is in line with the Commission's guiding principles described in more detail in section 2.3 below.

1.3 Who will be affected?

- 1.3.1 All persons registered to undertake Class C¹ and D² investment business; and
- 1.3.2 Investment Employees at those firms, existing clients of such firms and members of the public who seek investment advice.

1.4 Next steps

- 1.4.1 Position Paper 2 is one of the last steps in the implementation of RFA.
- 1.4.2 The Commission intends to consult publicly, in due course, on amendments to the Codes of Practice for Investment Business (the "**IB Codes**") to give effect to the policy outlined here. The Commission also intends to update and re-issue the Guidance Note: "Professional Qualifications: Investment Business". It is also possible that the Commission will issue further guidance in relation to the implementation of the RFA changes.

1.5 Timetable

- 1.5.1 The amendments to the regulatory framework as a result of the RFA will, as consistently stated, take effect from 1 January 2014.

¹ Giving investment advice when **not prevented** from holding client assets by virtue of a condition of registration.

² Giving investment advice when **prevented** from holding client assets by virtue of a condition of registration.

2 The Commission

2.1 Overview

2.1.1 The Commission is a statutory body corporate established under the Financial Services Commission (Jersey) Law 1998, as amended (the “**Commission Law**”). It is responsible for the supervision and development of financial services provided in or from within Jersey.

2.2 Commission’s functions

2.2.1 The Commission Law prescribes that the Commission shall be responsible for:

2.2.1.1 the supervision and development of financial services provided in or from within Jersey;

2.2.1.2 providing the States, any Minister or any other public body with reports, advice, assistance and information in relation to any matter connected with financial services;

2.2.1.3 preparing and submitting to the Minister recommendations for the introduction, amendment or replacement of legislation appertaining to financial services, companies and other forms of business structure;

2.2.1.4 such functions in relation to financial services or such incidental or ancillary matters:

- as are required or authorised by or under any enactment, or
- as the States may, by Regulations, transfer; and

2.2.1.5 such other functions as are conferred on the Commission by any other Law or enactment.

2.3 Guiding principles

2.3.1 The Commission’s guiding principles require it to have particular regard to:

2.3.1.1 the reduction of risk to the public of financial loss due to dishonesty, incompetence, malpractice, or the financial unsoundness of persons carrying on the business of financial services in or from within Jersey;

2.3.1.2 the protection and enhancement of the reputation and integrity of Jersey in commercial and financial matters;

2.3.1.3 the best economic interests of Jersey; and

2.3.1.4 the need to counter financial crime in both Jersey and elsewhere.

3 The Review of Financial Advice Proposals – Expected Outcome

- 3.1.1 The Commission’s view is that the RFA changes will contribute to the fulfilment of the Commission’s guiding principles, as detailed under paragraph 2.3 above. The changes have been proposed in an effort to reduce the risks of significant bias from remuneration structures which, when combined with the highest professional qualifications, should limit the potential for mis-selling, enable more sustainable businesses and ultimately increase client confidence in the investment business sector.
- 3.1.2 The Commission’s final position, as set out in Section 4 of Position Paper 2, will have a direct impact on Jersey’s investment business sector and on those clients that are affected by the changes to be introduced.

4 The Review of Financial Advice – Final Position

4.1 Background

- 4.1.1 Between August 2011 (when the Commission published Position Paper 1) and November 2012 (when it published the Feedback Paper), the Commission engaged with industry in relation to its review of the provision of financial advice. The review related to business within Class C and/or D of Part 1 of the Schedule to the Financial Services (Financial Services Business) (Jersey) Order 2009, in or from within Jersey and the work was carried out under the title “Review of Financial Advice”.
- 4.1.2 The date for implementation of the changes prompted by the RFA has consistently been, and continues to be, 1 January 2014. This paper sets out in one convenient place the position which will apply from 1 January 2014, following the implementation of the Commission’s policy in relation to the RFA. It is possible that the Commission will issue further guidance in relation to the implementation of the changes brought about as result of the RFA.
- 4.1.3 Some of the changes arising out of the RFA will require amendments to the IB Codes. The Commission will consult publicly, in due course, in relation to any proposed changes to the IB Codes arising out of the RFA; it is intended that such changes will apply from 1 January 2014.
- 4.1.4 The references preceded by “F” are to the corresponding paragraphs of the Feedback Paper.
- 4.1.5 References to the IB Codes are to the IB Codes (issued on 1 July 2008) in force at the date of this note. References in *italics* are to the draft IB Codes attached to Consultation Paper No. 4 2011: Proposed Amendments to Codes of Practice.
- 4.1.6 A “decision tree” is attached (see Appendix A) which is intended to assist registered persons in understanding how the Commission’s policy set out in Position Paper 2 will apply in practice. The decision tree does not cover every possible step and circumstance mentioned in Position Paper 2. Moreover, in the case of any inconsistency between the decision tree and the text of Position Paper 2, the text of Position Paper 2 is to prevail.

4.2 Qualification Requirements - General

- 4.2.1 The Commission’s position is that advisers of retail clients (that is, all clients that are not Professional Clients, defined below), wherever resident, will be required to hold a qualification referred to in its Guidance Note: “Professional Qualifications (Investment Business)” at Qualifications and Credit Framework (“QCF”) level 4 or above [Paragraphs: F1.3.2.2; F2.2.9; and F2.2.11]. The Commission’s general intention is that its requirements in

relation to the level of qualifications and gap-fill will be broadly the same as those which apply in the United Kingdom.

- 4.2.2 In relation to Span of Control, the position set out in paragraph F2.2.1.9 is that there is no change from the position set out in paragraph 3.3.5.3 (3.3.1.4.3) of the IB Codes, namely that directors and senior managers who do not meet the definition of an Investment Employee will be expected to possess professional qualifications and/or experience appropriate to their role.
- 4.2.3 The Commission's position as set out in paragraph 3.3.8 (3.3.3) of the IB Codes, in relation to the consideration of alternative qualifications and paragraph 3.3.10 (3.3.5) of the IB Codes, in relation to an exemption from the requirement to hold qualifications, remains unchanged. The Commission foresees that in exceptional circumstances it may, on application by a registered person, grant an extension of time for named Investment Employees of the registered person to obtain prescribed qualifications as set out in paragraph 3.3.10 (3.3.5) of the IB Codes. Any application should be made as soon as possible, fully explain the reasons for the request and specify the steps taken, and to be taken, to obtain the required qualifications and the date by which it is expected that the qualification will have been obtained. It is likely that any extension of time for obtaining the prescribed qualification will, if granted, be a time-limited exemption from the requirement to hold a qualification.

4.3 Qualification Requirements – Exceptions

- 4.3.1 Although long-term insurance contracts are defined as “investments” within Schedule 1 to the Financial Services (Jersey) Law 1998 (the “FS(J)L”), the Commission's position is that it will not be necessary for a financial adviser to be qualified at QCF Level 4 to advise in relation to the taking out of such contracts, where they fall within classes I, II or IV of Part 1 of Schedule 1 to the Insurance Business (Jersey) Law 1996 and the amount paid out does not depend on investment performance (paragraphs F2.2.18 and F2.2.47). A registered person will, however, still need to comply with paragraph 3.3.5.1 (3.3.1.4.1) of the IB Codes in relation to the individual giving the advice.
- 4.3.2 In relation to advice to Professional Clients (as defined below), the Commission's position is that there is no requirement that Investment Employees be qualified at QCF Level 4; however, it intends that the requirement that they be appropriately qualified within the meaning of paragraph 3.3.5.1 (3.3.4.1) of the IB Codes (paragraphs F1.3.2.4 and F2.2.24) remain unchanged.

4.4 General Ban on Remuneration by Way of Commission

- 4.4.1 The Commission's position is that a registered person will not be permitted to receive remuneration by way of commission for services provided to Jersey-resident retail clients (paragraphs F1.3.2.3 and F1.3.3.1). Please see 4.6 below in relation to guidance on the place of residence of clients.

- 4.4.2 It is also the Commission's position that a registered person will need to be able to demonstrate, in writing, that its clients have been made aware of all associated fees and charges including commissions. The reference in paragraph 4.6 of the IB Codes to commissions should, from 1 January 2014, be construed as references to commissions where permitted.

4.5 General Ban on Remuneration by Way of Commission – Exceptions

- 4.5.1 Notwithstanding that a client is a Jersey-resident retail client, it is the Commission's Position that it will be permissible for a registered person to be paid by way of commission, where adequate disclosure of the commission, or the method of calculating commissions, has been made, in respect of its advice to that client in the circumstances specified in this Section.
- 4.5.2 In relation to long-term insurance contracts, the Commission's position is that the registered person may be paid by way of commission in respect of initial and ongoing advice in relation to long-term insurance contracts (paragraphs F2.2.39 and F2.2.45).
- 4.5.3 In relation to products (that is, investments as defined in Schedule 1 to the FS(J)L) taken out before 31 December 2013 (paragraph F2.2.45), the Commission's position is that the registered person may be paid by trail commission from 2014 onwards where the investment advice is given and a contract taken out before the RFA deadline of 31 December 2013. Trail commission may cease to be eligible where:
- 4.5.3.1 a product is amended post-2013 to the extent that it becomes a new product; or
 - 4.5.3.2 the client is required to sign a new product contract post-2013.
- 4.5.4 In the circumstances where a client changes the registered person from whom it receives investment advice, the Commission's position is that re-registration of the trail commission will be allowed where it is permitted by the investment contract between the product provider and the previous registered person that acted as investment adviser. It is expected that the client be told in a timely fashion when a registered person applies for re-registration and informed of the amount of the trail commission being transferred. The new registered person will also be required to provide the client with an on-going service in return for the trail commission, regardless of whether or not the original contract allowed for this as a condition of transfer.
- 4.5.5 The Commission considers that there is a potential danger that Investment Employees may encourage their clients to enter into transactions with unnecessary frequency, which may be against the client's best interest, with the intent of generating commissions before the RFA is implemented. This practice would be in contravention of paragraphs 2.10 (2.11) and 2.11 (2.12) of the IB Codes.

- 4.5.6 A registered person may be remunerated by way of commission for advice to non-Jersey resident retail clients and for advice to Professional Clients (as defined in paragraph 4.7 below) wherever resident.

4.6 Guidance in Relation to Place of Residence of Clients

- 4.6.1 The Commission's position is that a registered person carrying out Class C and/or D investment business will need to establish and maintain procedures to determine where its clients are resident.
- 4.6.2 The Commission considers that it is not appropriate or possible to give guidance on what constitutes "residence" in every possible circumstance.
- 4.6.3 The Commission would not expect to find that a client resident for tax purpose in Jersey, whose correspondence address in the registered person's records was in Jersey and whose address had been verified by the use of a means or document which provided a Jersey residential address, was not treated by the registered person as resident in Jersey. Where a client has both a Jersey address and a non-Jersey address, it will be for the registered person to demonstrate that it has established with which address (and therefore with which jurisdiction) the client has his or her most substantial connection and the registered person should treat the client as resident in the jurisdiction of that address.
- 4.6.4 The Commission is likely to conclude that any behaviour by a registered person to encourage or enable a finding as to a client's residence which is not consistent with the guidance, above, will raise a question as to whether the registered person is complying with Principle 1 of the IB Codes ("A registered person must conduct its business with integrity").

4.7 Client Classification - Retail and Professional Clients

- 4.7.1 The Commission's position is that a registered person carrying out Class C and/or D investment business will need to establish and maintain appropriate written internal policies, procedures and controls to categorise its clients.
- 4.7.2 The Commission's position is that the following definitions should apply in relation to the classification of clients:
- 4.7.2.1 A "retail client" is a client who is not a Professional Client.
- 4.7.2.2 A "per se Professional Client" or an "elective Professional Client" is a Professional Client.
- 4.7.2.3 Each of a "Large Undertaking" and a "Professional Investor" (defined below) is a "per se Professional Client".

4.7.2.4 “Large Undertaking” means a body in relation to which two of the following three criteria are satisfied:

- balance sheet total of not less than £13,000,000;
- net turnover of £26,000,000 or greater; or
- own funds of £1,300,000 or greater.

4.7.2.5 “Professional Investor” means:

- a government, local authority, public authority or supra-national body (wherever established); or
- a person, partnership, unincorporated association or body corporate whose ordinary business or professional activity includes or it is reasonable to expect that it includes acquiring, underwriting, managing, holding or disposing of investments whether as principal or agent or the giving of advice on investments.

4.7.2.6 A registered person may treat a client as an “elective Professional Client” if it undertakes an adequate assessment of the expertise, experience and knowledge of the client that gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the client is capable of making his/her or its own investment decisions and understanding the risks involved. If the client is an entity, (for example a company, a foundation, a trust or a partnership) the assessment should be performed in relation to the person(s) authorised to carry out transactions for it. In making this assessment the registered person should have regard *inter alia* to:

- the frequency of the client’s or authorised person’s dealings in the kind of investments which are the subject matter of the registered person’s advice;
- the size of the client’s portfolio; it is unlikely that a client with a portfolio of less than £500,000 could properly be categorised as an elective professional client; and
- the client’s or authorised person’s relevant professional expertise.

4.7.3 The Commission’s position is that a procedure along the following lines should be followed if a client is to be treated as an elective Professional Client:

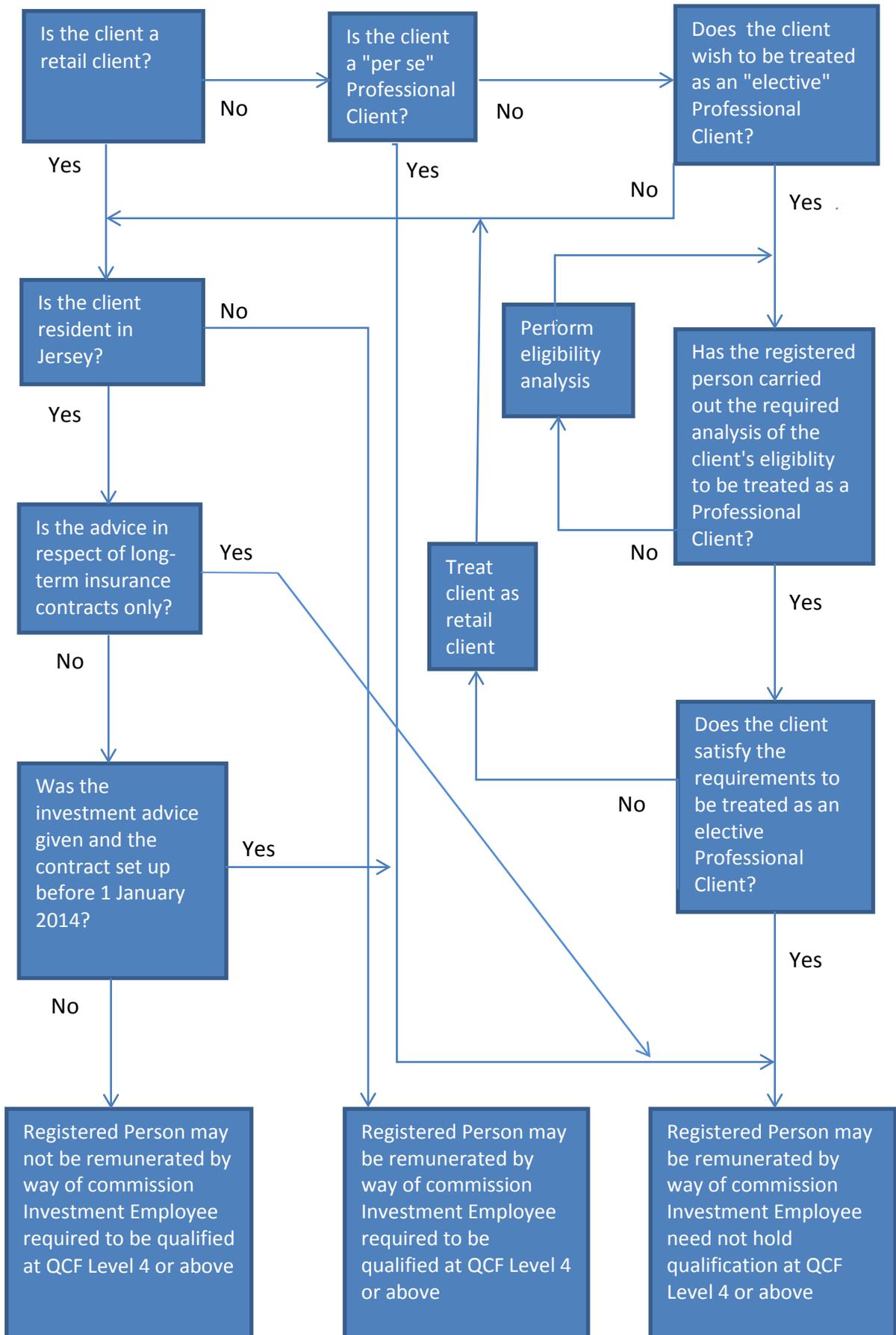
4.7.3.1 the client needs to state, in writing, to the registered person in advance of the transaction being carried out that he/she or it wishes to be treated as a Professional Client either generally or in respect of a particular service or transaction or type of transaction or product;

- 4.7.3.2 the registered person needs to give the client a clear written warning of any protections and investor compensation rights the client may lose; and
 - 4.7.3.3 the client needs to state, in writing, in a separate document from the contract of engagement of the registered person, that he/she or it is aware of the consequences of losing any such protections.
- 4.7.4 If the registered person becomes aware that a client no longer fulfils the initial conditions that made him/her or it eligible for categorisation as a Professional Client, it is expected that the registered person should cease to treat the client as a Professional Client and treat the client as a retail client, and inform the client accordingly and within a reasonable time of the change.

4.8 Statement of Professional Standing

- 4.8.1 There is no current requirement for investment employees to hold any form of Statement of Professional Standing (“SPS”) (paragraphs F2.1.31, F2.1.33, and F2.1.35). However, the Commission’s intention is that the holding of an SPS by investment employees qualified at QCF Level 4 will be required at some future stage. The Commission will keep under review the experience in the United Kingdom in relation to SPSs and intends to make an announcement as to its plans in this area in due course.

Appendix A - Decision Tree



Appendix B

List of representative bodies and other organisations who have been sent Position Paper 2.

Persons that submitted responses (in some cases anonymised, at the respondent's request) to Position Paper 1:

- Standard Chartered (Jersey) Limited
- Barclays Bank PLC
- Royal Bank of Canada (Channel Islands) Limited
- Lloyds TSB Offshore Limited
- HSBC Private Bank (C.I.) Limited
- HSBC Bank Middle East Limited
- Citibank N.A.
- Royal Bank of Scotland International Limited
- Alexander Forbes Channel Islands Limited
- Spearpoint Limited
- Cenkos Jersey Limited
- Bridport & Co. (Jersey) Limited
- Collins Stewart (C.I.) Limited
- Heritage Insurance Limited
- Homebuyer Financial Services Limited
- Personal Finance Society, Jersey
- Personal Finance Society Member "A"
- Personal Finance Society Member "B"
- Aviva Insurance (UK) Limited
- Chartered Institute for Securities and Investment
- Chartered Financial Advisers
- Jersey Finance Limited

Additional recipients of this paper:

- JFA – Jersey Funds Association
- JCOA – Jersey Compliance Officers' Association
- JIBS – Jersey International Business School
- BPP Jersey
- Standard Bank Jersey Limited