Investment business

A brief guide as to whether you are conducting investment business and whether you need a DPB licence

This helpsheet has been produced in conjunction with the ICAS Quality Assurance Department (Quality Review and Audit Monitoring)
This helpsheet is intended to help members in practice determine whether they are conducting investment business and whether they need a DPB licence.

Introduction

The Financial Services and Markets Act 2000 allows firms to conduct investment business, only if they are regulated by either the Financial Services Authority (FSA), or a Designated Professional Body (DPB) such as ICAS, or are an appointed representative of another FSA firm. Firms cannot be licensed by a DPB and authorised by the FSA.

Only certain types of investment business work may be undertaken by firms holding a DPB licence. The “regulated activity” must be complementary to, or arise out of other professional services provided to the client, i.e. it cannot be the only service provided to the client. Both your firm and the Institute must be satisfied that the regulated activities can be conducted in a manner which is incidental to your other professional activities.

Firms which require to be authorised by the FSA must be authorised for the categories of work that they conduct. Full details of FSA authorisation can be obtained at www.fsa.gov.uk.

To undertake a regulated activity without the appropriate level of regulation is a criminal offence.

We don't get involved in Investment Business or do we?

When firms are asked about investment business they often indicate that they don’t get involved in investment business. They think that because they involve or introduce clients to an Independent Financial Advisor (IFA) or suitably authorised persons for investments (such as shares and debentures; managed funds; pensions; and sophisticated financial instruments or arrangements) then they are not involved in investment business. Where you introduce a client to an IFA by contacting the IFA and this is not with regard to a particular type of investment, then this is correct. However, in many cases, you may be introducing the client with regard to a particular type of investment, being mainly pensions and insurance contracts. If you simply telephone the IFA on behalf of the client, this is regulated and you will require a licence. You can, however, ask the client to contact the IFA themselves to avoid falling within the legislation.

Types of “investments” and situations that you may come into contact with are:

(1) Regulated mortgage contract

You have prepared cashflow projections, the funding is being put into place and your client asks that you accompany him to the bank for some support. At the meeting, the bank, requests a mortgage on the property. Could this be a regulated mortgage contract and would you recognise it if it were? Would you be expected to help and comment on the bank’s request?

Could this be a regulated mortgage contract?

A regulated mortgage contract exists when:
• the borrower is an individual or trustee;
• the lender takes a first charge over property in the UK;
• the secured property is at least 40% occupied by the borrower or a member of his immediate family.

What the borrowed money is used for, is not relevant in deciding whether the mortgage is regulated or not. A loan obtained by an individual (sole trader, partner or director) to invest in a business will be regulated if, in all other respects, it meets the above definition. Sound familiar, or something that you are likely to come across?

Would your client expect you to comment or add your advice?

You cannot do either if you are not DPB licensed or FSA authorised. You will not be able to comment on the advice given by a mortgage adviser. Please note second charges, unsecured lending and loans to limited companies are not regulated.

The good news is that there are some activities that you can do without a licence or authorisation. Here are some examples:
• prepare a cashflow and discuss general financing options, as long as these do not amount to a recommendation to take out a specific regulated mortgage contract.
• discuss with client the implications of the various terms of a mortgage contract.
• provide generic advice e.g. fixed or variable rate, provided not linked to a specific contract (i.e. not about a specific mortgage).
• make the introduction to an independent mortgage adviser.
(2) Contracts of general insurance

Will clients ask for advice or help regarding contracts of general insurance?

When people think of regulated contracts of insurance, they often think of long-term insurance contracts (e.g., pensions) but all types of insurance are regulated, e.g., key man, life and medical.

Regulated activities, i.e. activities that you cannot do without being DPB licensed or FSA authorised include:

• giving specific advice on any type of insurance contract.
• assisting putting in place any type of insurance contract.
• contacting an insurer or an independent financial adviser to introduce a client.
• negotiating claims on behalf of a client.
• where the insurance is a long-term contract, such as an endowment, a pension contract or a whole life contract, FSA authorisation will be needed to give advice.

Providing generic advice (i.e. not about a specific insurance contract) or providing information to a client about insurance, including giving the name of an independent insurance broker to contact (but not contacting the broker on behalf of the client) will not be regulated. Nor will explaining the terms of an insurance contract.

If, however, the client asks you to advise him on loss of profits insurance and to arrange the contract, this is a regulated ‘investment’ and both advising and arranging insurance are regulated activities (regulated firms can assist their client by contacting the insurer, complete proposal forms etc, unregulated firms cannot).

Helping your client to determine the amount of an insured loss will not be regulated, provided you do not negotiate a settlement for the client. Also, if the insurance company contacts you regarding the financial position of the client, you may provide this information. These are professional services.

If the insurance company has queries regarding the quantum of the claim, e.g. in a loss of profits claim, you may support the client, but direct contact with the insurer, answering queries and discussing the quantum, could result in negotiation and therefore be regulated.

In summary, unauthorised firms cannot give specific advice or arrange the insurance contract but could give generic advice, e.g. to recommend that loss of profits insurance would be beneficial. A DPB licensed and an FSA authorised firm can give specific advice and arrange the insurance contract.

From the above, you can see that, if you are not DPB licensed or FSA authorised then, you have to be extremely careful regarding the work you carry out for clients. If there is a likelihood that you may carry out regulated activities in future, you should consider becoming DPB licensed / FSA authorised. Even if you do not, you should check annually, to ensure whether there is a need to be regulated.

Do I need to be regulated?

Consider your current and potential client base and the type of professional services that you are likely to undertake on their behalf.

Refer to the DPB handbook on the ICAS website at www.icas.org.uk/site/cms/contentviewarticle.asp?article=5423. This provides detailed information and scenarios of work that a licensed firm can perform, work requiring an FSA authorisation and unregulated work which may appear to be investment business in nature but is not regulated. There are some very helpful tables, providing clear examples.

Examples of professional services which may appear to be investment business but are not regulated investment business are given in Appendix 1 below.

There are a wide range of investments and activities caught by the FSMA 2000. Appendix 2 below, regulated investments and regulated activities, is an extract from the DPB handbook. If you are considering any of these regulated activities, involving regulated investments and you have any doubts regarding whether you can safely undertake the activity without a licence, or being authorised by the FSA, you should contact Emma Reid in the Professional Services department of the Institute on 0131 347 0282 or email ereid@icas.org.uk for advice.

What would be the benefits of my firm holding a DPB licence?

Some of the more common activities that a DPB licensed firm can undertake that an unlicensed firm cannot, are:

Client services involving shares
• Advise on the purchase of shares that are not and will not, be traded on a public market.
• Give advice on the sale of shares including those which are or may be publicly traded.
• Comment on, agree, or disagree with the specific advice of an authorised firm (e.g. IFA).
• Deal in shares as an agent of the client.
• Arrange for the sale or purchase of shares.
• Receive and retain documents of title (safeguarding) and arrange for collection of dividends for onward payment to the client.

Client services involving insurance
• Contact the broker/insurer on behalf of the client to effect an introduction.
• Comment on, agree or disagree with the specific advice of an authorized firm.
• Complete a proposal form and send the form to the broker/insurer on behalf of the client.
• Pay the initial premium on behalf of the client.
• Claims - notify the insurer; complete the claim form; negotiate settlement.
• Recommend a specific general insurance contract to the client.
• Arrange an insurance contract (cannot give advice re life or pension).
• Arrange but not advise a top up to a personal pension contract.

Client services involving home finance (Regulated mortgage contracts, home reversion plans, home purchase plans, sale and rent back agreement)
• Contact a lender to introduce a client for home finance where the firm also handles the client’s money.
• Recommend that a client vary the terms of an existing regulated home finance plan.
• Comment on, agree, or disagree with the advice given by a mortgage broker or lender regarding a specific home finance plan.

Client services involving corporate finance activities
• Advise shareholders to buy or sell shares which are not and will not be traded on a public market.
• Advise shareholders whether to take up a rights issue, where the shares are not and will not traded be on a public market.
• Advise shareholders to sell shares.

The above examples are not exhaustive.

Are there any common problems found during Quality Review visits?

Below are the most common points reported:
• Poor procedures for passing client’s property to a 3rd party.
• Not licensed but should be for the activities being undertaken.
• Letterhead not updated to reflect that regulated for a range of investment business (or not).
• Annual Compliance Review not carried out/not adequately carried out.

• Engagement letter not updated to reflect provision of investment business services.
• No written agreement in place with Permitted Third Parties.
• No permission obtained from client to retain commission.
• Commission not correctly accounted for by firm.
• Inappropriate Fee Protection Insurance arrangements for firm’s level of regulation.

General Comments

A licensed firm can provide a more inclusive service to the client, as there are additional activities that a licensed firm can undertake that an unlicensed firm cannot.

A licensed firm can also fully discuss advice provided to the client by an IFA /authorised person, giving their own views but must not give its own investment recommendations.

Obtaining a DPB Licence

For further advice contact the Professional Services department on 0131 347 0282 or email ereid@icas.org.uk. An application form and a copy of the DPB Handbook which includes the terms and conditions of holding a licence, is available on the ICAS website at www.icas.org.uk/site/cms/contentviewarticle.asp?article=5423.
Appendix 1 Examples of Professional Services which are not regulated and can be performed by any firm:

NB the examples below are not exhaustive

- Generic advice – general discussion with a client about different types of investments (including pensions), but not discussions on the merits of a specific investment.
- Explaining terms of investment or contract of insurance.
- Tax advisory work involving no more than generic investment advice.
- Introducing a client to a permitted third party for the provision of independent advice with no mention of a particular investment (does not apply to insurance contracts).
- Preparation of cash flow/profit projections to support a loan application, even if it is for a regulated mortgage contract.
- Advising on the value of an asset.
- Valuing investments where no advice is given as to the merits of buying or selling the investment.
- Advising on the cancellation of contracts of insurance (such as general insurance contracts and pure protection insurance) but not qualifying contracts of insurance.
- Providing a reference on behalf of a client in support of a mortgage application.
- Advising on obtaining an unsecured overdraft.
- Administration work for a client’s pension scheme (e.g. calculating pension deductions for the payroll and paying over to the insurance company).
- Advice, arranging a deal or dealing as agent regarding the sale or purchase of a body corporate if the transaction may be reasonably regarded as the acquisition of day to day control over the affairs of the body corporate; or the shares (together with ones already held) are 50% or more of the voting rights and the transaction is between two parties each of whom is a body corporate, a partnership, a single individual or a group of connected individuals.
- Arranging for a company to issue its own shares is not engaging in a regulated activity, although arranging for a person to subscribe is a regulated activity.
- Advising a company on the issue of shares is not a regulated activity, but advice to a potential shareholder to subscribe for the shares is.
- Arranging for the transfer of shares for no financial consideration (for example between husband and wife).
- Generally (except for insurance mediation activities conducted by way of business) transactions within a group of companies are not investment business.
- Advising a client about the commercial utility of futures, options and contracts for differences, e.g. to support commercial bank borrowing or as a commercial hedging mechanism.
- Advice to surrender an existing regulated mortgage contract, regulated home purchase plan or regulated home reversion plan.
- A firm can arrange a deal in investments, deal as agent in investments, safeguard and administer investments or give advice, provided:
  - the service may reasonably be regarded as a necessary part of other professional services;
  - the service is not remunerated for this work separately from the other services; and
  - the business or profession does not otherwise consist of regulated activities
  (This exemption is known as the professional firms’ exemption but care is required that all criteria are met.
- Make arrangements for a client to buy, sell, subscribe for or underwrite an investment with or through a permitted third party provided:
  - the transaction is on the advice of a permitted third party; or
  - the client has not requested advice on the merits of the investment from the firm, or if requested, the firm has refused and suggested that the client seek advice from a permitted third party.

The words in italics are defined terms. The definitions can be found in the DPB handbook.

www.icas.org.uk/site/cms/download/RCOM/DPB_regs_booklet_master_1_7_2009.pdf
Appendix 2  Regulated Investments - Extract from DPB Handbook

NB the examples below are not exhaustive

- Deposits
- Rights under contracts of insurance (e.g. general insurance, life and pensions contracts)
- Shares
- Instruments creating or acknowledging indebtedness (e.g. debentures)
- Government and public securities
- Instruments giving entitlement to investments (e.g. warrants)
- Certificates representing certain securities
- Units in a collective investment scheme
- Rights under a stakeholder or personal pension scheme
- Options
- Futures
- Contracts for differences
- Lloyds syndicate capacity and syndicate membership
- Funeral plan contracts
- Regulated mortgage contracts
- Regulated home reversion plan
- Regulated home purchase plan
- Rights to or interests in investments
- Accepting deposits
- Issuing electronic money
- Effecting and carrying out contracts of insurance
- Dealing in investments as principal
- Dealing in investments as agent
- Arranging deals in investments (including some introductions)
- Arranging regulated mortgage contracts
- Arranging regulated home purchase plans
- Arranging regulated home reversion plans
- Managing investments
- Assisting in the administration and performance of a contract of insurance (e.g. claims handling for a client)
- Safeguarding and administering investments
- Sending dematerialised instructions
- Establishing (operating or winding up) a collective investment scheme
- Establishing (operating or winding up) a stakeholder or personal pension scheme
- Advising on buying, selling or subscribing for, or exercising a right to buy, sell or subscribe for, an investment
• Advising on entering into, or varying the terms of, a regulated mortgage contract
• Advising on entering into, or varying the terms of, a regulated home purchase plan
• Advising on entering into, or varying the terms of, a regulated home reversion plan
• Advising on Lloyd’s membership, managing Lloyd’s syndicates underwriting capacity and arranging deals in contracts of insurance written at Lloyd’s
• Entering as provider into a funeral plan contract
• Entering into a regulated mortgage contract as a lender
• Agreeing to carry on a specified activity

The words in italics are defined terms. The definitions can be found in the DPB handbook.  
www.icas.org.uk/site/cms/download/RCOM/DPB_regs_booklet_master_1_7_2009.pdf

For more information regarding Quality Assurance, i.e. Audit Monitoring or Quality Review, contact Lynne Bannan on 0131 347 0284 or email lbannan@icas.org.uk.
For more information regarding the CA Practitioner Service, contact Lesley Amos on 0131 347 0253 or email caps@icas.org.uk.

Disclaimer
This helpsheet is designed to assist members with an important issue of general application and is not intended to be a definitive statement covering all aspects of this area. No responsibility for any person acting or refraining to act as a result of any material in this helpsheet can be accepted by ICAS.