

08 / 10

Financial Services Authority

**Client Assets sourcebook
(Common platform
provisions)
Instrument 2008**

Feedback on CP08/6 and made rules

September 2008



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This Policy Statement reports on the main issues arising from Consultation Paper 08/6 (*Review of the Client Assets sourcebook (CASS)*) and publishes made rules.

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Part I

1 Overview

Purpose

- 1.1 In Consultation Paper 08/6¹ (CP08/6), we consulted on our proposals to reform the Client Assets sourcebook (CASS). The CP outlined our proposals for modifying CASS to simplify its structure following the implementation of the Markets in Financial Instruments Directive (MiFID) on 1 November 2007. This was an FSA Business Plan objective for 2007/8 as well as a Better Regulation Action Plan obligation. In this Policy Statement, we summarise the submissions to the consultation and our responses, along with made rules which will come into force 1 January 2009.

Our policy approach

- 1.2 Our policy aim in CP08/6 was to simplify the sourcebook's structure, increase the flexibility available to firms by moving to more principles-based regulation and, where possible, provide a common platform for firms based on the MiFID standards. This approach was widely welcomed by industry, as the responses we received confirmed. The result will be a more streamlined and easier-to-use sourcebook, especially for small firms.

As a result of the consultation we have:

- deleted rules and guidance where justified by cost-benefit analysis;
- simplified the wording in CASS by adopting a plain English style; and
- reduced any significant undue burdens on firms.

Within this approach we have maintained carve-outs for non-MiFID scope firms regarding affiliated companies and approved banks.

1 http://www.fsa.gov.uk/pages/Library/Policy/CP/2008/08_06.shtml.

Structure of this Policy Statement

- 1.3 This Policy Statement is divided into three parts:
- Part I provides an overview of the CASS review;
 - Part II details the feedback we received and our responses to submissions; and
 - Part III summarises the discussion surrounding CASS 5, dealing with insurance mediation activity.

Key issues

- 1.4 Despite receiving broad support for CP08/6, there are two areas where we will not follow our proposals – these relate to non-MiFID scope business carve-outs for the ‘approved bank’ exemption and affiliated companies’ provisions. In CP08/6 we proposed to move non-MiFID scope business to the MiFID standard. This would have altered the ‘approved bank’ definition to ‘credit institution’ and required that affiliated companies be treated as any other client of the firm. In contrast with our proposals and consistent with the industry feedback received, we will retain the non-MiFID business carve-outs for approved banks and affiliate companies.

Who should read this Policy Statement?

- 1.5 The changes to CASS described in this paper apply principally to firms that hold client money and/or assets.

Part II

2 The new structure and content of CASS

2.1 In the CP, we outlined our proposals for modifying CASS to simplify its structure. The rationale for extending the application of the MiFID CASS regime, where appropriate, is as follows:

- The MiFID standard is non-derogatable for MiFID firms. As a result, changes cannot be made to the MiFID chapters in CASS. However, the non-MiFID chapters in CASS, are based on the Investment Services Directive which was replaced by MiFID. We consider that the adoption of the MiFID standard will not result in any decrease in the level of consumer protection and will provide firms with a sourcebook which, where possible, focuses upon the outcomes firms are to achieve;
- Where appropriate, the MiFID chapters in CASS were drafted in accordance with our more principles-based regulatory approach. They are less prescriptive, more outcomes-focused and provide some flexibility for firms. Adopting the MiFID approach should therefore prove less onerous and reduce compliance costs for non-MiFID firms; and
- We noted in CP06/14 that although MiFID required some detailed amendment of Handbook provisions relating to the relevant firms, the overall regulatory standard was broadly equivalent to our previously established requirements. It is appropriate that we reiterate our comment made at that time that the additional flexibility available under the MiFID provisions puts more emphasis on the responsibility of firms and their senior management to achieve the outcomes required. That point has added weight given that - as explained in this Policy Statement - we are extending the more principles-based approach to the safeguarding of client assets and money to all firms having the relevant permissions.

2.2 In response to a previous consultation paper, a trade association suggested that we move to a more logical ordering of the chapters in the final rules. We are restrained in re-ordering the sourcebook, because we need to retain the historic presentation of the Handbook for firms' ease of use. However, we have still substantially rationalised the chapters of the sourcebook as proposed in CP08/6. The distribution rules will be split out into a separate chapter in 2009 following our work in this area resulting from the Banking and Compensation Reform Project.

2.3 The proposed structure of CASS is as follows:

Chapter 1	Application and general provisions
Chapter 2	DELETED
Chapter 3	Collateral
Chapter 4	DELETED
Chapter 5	Client Money (general insurance intermediaries only)
Chapter 6	Custody
Chapter 7	Client Money and distribution rules
Chapter 8	Mandates

3 Merging the custody rules

Introduction

- 3.1 In Chapter 4 of CP08/6 we explained that the standard provided in the MiFID custody chapter was consistent with our more principles-based regulatory approach. The requirements are less prescriptive, more outcomes-focused and as a result, provide increased flexibility for firms.
- 3.2 In this chapter we provide feedback on the responses which we have received to questions 1 to 13 in the CP. The responses largely supported our proposals.

Responses to individual questions/comments

1. Exemptions

- 3.3 This question related to the exemption for operators of regulated collective investment schemes ‘in relation to activities carried on for the purpose of, or in connection with, the operation of the scheme’. This exemption implements MiFID and we proposed to carry forward this exemption to non-scope firms in CASS 6.1.16B R.

In the CP we asked:

Q1: Do you agree with the relevant proposals? If not, why not?

Our response: Respondents agreed with our proposals, and therefore, we confirm our policy approach.

2. Concessionary regimes

- 3.4 We consulted on the basis of retaining concessionary regimes which deal with particular areas of the industry - for example, a custodial regime for trustees and depositaries and arrangers.

In the CP we asked:

Q2: Do you agree with the concept of retaining the concessionary regimes? If not, why not?

Q3: Do you agree with the manner with which we have updated the concessionary regimes? If not, why not?

Our response: Respondents agreed with our proposals, and therefore, we confirm our policy approach.

3. *'Holding' safe custody instruments*

- 3.5 We proposed adopting a more principles-based approach to the protection of a client's safe custody instruments for all firms subject to CASS. We explained that we intended to apply the general CASS 6.2.1 R provision to all firms, requiring them (when holding safe custody assets belonging to clients) to 'make adequate arrangements so as to safeguard a client's ownership rights, especially in the event of the firm's insolvency, and to prevent the use of safe custody assets belonging to a client on the firm's own account except with the client's express consent'.

In the CP we asked:

Q4: Do you agree with our proposal? If not, why not?

Our response: Respondents agreed with our proposal, and therefore, we confirm our policy approach.

4. *Client notification and agreements*

- 3.6 In CP08/6 we proposed removing the requirement in CASS 2.2.10 R (5) which requires firms that are registering or recording legal title to a safe custody investment in the name of another person in line with the client's specific written instruction, to notify that other person in accordance with current CASS 2.3.11 R (risk disclosures). While there is no equivalent in the respective MiFID chapter to replace it, we consider that the provision does not, in practice, enhance the standard of consumer protection.
- 3.7 While a small number of firms disagreed with this proposal, most respondents supported us deleting this provision. One respondent noted that a firm would have a duty under CASS 6.2.1 R and CASS 6.2.2 R to consider the appropriateness of a client's request to have its entitlement recorded in the name of another person and make enquiries where the firm has concerns, justifying deleting the provision.

Our response: We confirm that we will delete the provision in line with our proposal.

- 3.8 CASS 2.3.2 R imposes a notification requirement upon a firm to its clients and we consulted on the basis that we would delete it and rely on higher-level requirements set out in COBS 8.1 instead.

In the CP we asked:

Q6: Do you agree with our proposal? If not, why not?

- 3.9 Some firms disagreed with our proposals because they thought it was helpful to have cross-referencing within CASS. Additionally, we received one comment stating that deleting the statement provisions in CASS would mean that it no longer falls within the scope of the CASS auditor's report requirement in SUP 3.10. A trade association opposed the proposal if it were to have the effect of widening the scope to eligible counterparties.
- 3.10 Most respondents agreed with our proposals as long as it was clear that the COBS standards fall within scope.

Our response: We confirm that we will delete the provisions in CASS 2.3.2 R and rely on the higher-level requirements in COBS 8.1. Equally, we will not transpose the statement provisions contained in CASS 2.3.12 R to CASS 2.3.21 R. Rather we will rely on the COBS standard in COBS 16.4.

These standards already apply to firms and deleting the provisions will contribute to a more streamlined and easier-to-use sourcebook. However, firms must still comply with the full Handbook. While we appreciate that an auditor has no direct reporting responsibility in respect of conduct of business rules, we consider that any breaches identified would indicate the extent to which the general atmosphere and controls in the business are conducive to compliance.

5. *Depositing assets with third parties*

- 3.11 We proposed to move to the MiFID standard for firms, rather than maintain a detailed list of provisions for firms to consider when assessing a custodian in CASS 2.2.18 R. CASS 6.3 allows a firm to deposit assets with a third party, but only if the firm exercises all due skill, care and diligence in the selection, appointment and periodic review of the third party and of the arrangement for holding the assets. It also requires the firm to make a record of the grounds upon which it satisfies itself that its selection of a third party is appropriate.

Q7: Do you agree with our proposal? If not, why not?

- 3.12 One trade association suggested that we should not apply CASS 6.3.4 R (1) and (2) to non-MiFID business and that it should carry forward a rule equivalent to CASS 2.2.15(2)(b) in respect of assets held on behalf of professional clients. One firm questioned our approach of maintaining registration and custody of UK assets over and above that required for assets subject to non-UK laws. Another firm also noted that the administration of CASS 6.3.4 R is not insignificant.
- 3.13 Most respondents agreed with the proposals - including responses from firms, consultants, auditors, and trade bodies.

Our response: We confirm that we will apply CASS 6.3 to all firms, consistent with our more principles-based approach to regulation. We consider the recording and registration of assets deposited with third parties as a key provision to reduce counterparty risk and, accordingly, the potential for consumer detriment.

6. *Use of safe custody assets and securities financing transactions*

- 3.14 We proposed to move from CASS 2.2.18 R, which allows firms to use professional clients' or eligible counterparties' safe custody investments for its own account, if they have notified the client, to the MiFID standard. Under CASS 2.2.18 R firms can use retail clients' safe custody investment if they have received prior written consent.
- 3.15 In contrast MiFID requires the express prior consent from clients before the firm's use, or another client's use, of a financial instrument belonging to a particular client in CASS 6.4.1 R (2)(A).
- 3.16 In the CP we stated that under CASS 6.4.1 R (1), 'securities financing transactions' encompasses stock lending and noted that the MiFID standard extended to eligible counterparties a requirement to obtain a client's express prior consent.
- 3.17 The clear majority of firms supported the proposal to move to the MiFID standard. One trade association did not object to our proposal, but suggested that the proposal would require firms to obtain express consent from all existing professional and eligible counterparty clients. The trade association considered that the associated cost of such an exercise could be minimised by delaying the implementation of this provision for six months to coincide with other repapering exercises conducted by firms.

Our response: We confirm our approach but will delay implementing this provision until 1 May 2009 to minimise the impact of this change on firms.

7. *Client asset accounts and reconciliations*

- 3.18 This was one of the key proposals in CP08/6, offering more flexibility to firms that can demonstrate that they are performing the reconciliation as often as is reasonably required in all of the circumstances, as well as the choice of reconciliation method. Accordingly, we proposed to apply CASS 6.5.4 G to CASS 6.5.12 G to all firms.
- 3.19 A small number of auditors and one trade association raised concerns over the different views auditors and firms may have over compliance with the rules, and suggested we impose a 'maximum period' between reconciliations. The respondents realised that this may be super equivalent for MiFID purposes.
- 3.20 However, a clear majority of firms, including an auditor, supported this proposal.

Our response: The primary obligation is for the firm to determine an appropriate method and time scale for performing reconciliations, suitable to their structure and business model. It is then for auditors, in their capacity as an external and independent adviser, to use their professional judgement to offer assurance on the firm's systems and controls. We will not issue further guidance on this matter. To prescribe parameters decreases the flexibility afforded to firms in maintaining systems and controls appropriate to their business model. There is also no justification for super-equivalence with MiFID.

8. *Records and accounts*

- 3.21 In the CP we proposed to require all firms to retain their records made under CASS for five years, increasing the requirement for non-scope firms by two years. As we understand it, most firms keep records for up to seven years for legal and taxation purposes.

Our response: All respondents agreed with our proposal, and therefore, we confirm our policy approach.

9. *Depository receipts*

- 3.22 CASS 2.1.25 R disapples certain provisions in the custody regime because depository receipts purchased in the secondary market results in the buyers only becoming known to the firm after they have become clients. We proposed not to carry the specialist provisions forward because some requirements will be contained in COBS for a MiFID firm's business, and accordingly, the CASS 2 rules and guidance are not required.

Our response: We received general support for our proposal, and therefore, we confirm our policy approach.

10. *Affiliated companies*

- 3.23 In the CP we proposed to apply the MiFID standard to affiliated companies so that the operation of the custody rules in relation to that client is unaffected. This proposal would have removed the carve-out for non-scope firms that disapples the custody rules when the company was an affiliate (unless the firm had been notified that the designated investment belongs to a client of the affiliated company and/or the affiliate was dealt with at arm's length).
- 3.24 We received a small number of responses which disagreed with our proposals. One firm responded by stating that it had no objection to our proposal but questioned the usefulness of removing the carve-out from non-scope firms in practice.

Our response: We confirm that we will maintain the carve-out for non-MiFID scope firms in line with the feedback we received.

4 Merging the client money rules

Introduction

- 4.1 Consistent with our proposals in relation to the custody chapter, the client money rules are being consolidated into Chapter 7, with Chapter 4 being deleted. We received broad support to merge the chapters and generally move non-scope firms to the MiFID standard, both in line with our move to more principles-based regulation and to create a common platform for firms.
- 4.2 As described in the CP, we do not consider that the proposals will result in substantive changes to how we expect firms should treat client money compared to existing practices.

Responses to individual questions/comments

1. *Solicitors*

- 4.3 We stated that the relevant client money requirements provided by these firms under applicable professional requirements continue to provide the requisite degree of consumer protection in the event of a firm's insolvency. We received support for our proposals to retain the current provisions, exempting such firms not carrying out MiFID business from the client money rules.

In the CP we asked:

Q14: Do you agree with our proposal? If not, why not?

Our response: All respondents agreed with our proposal, and therefore, we confirm our policy approach.

2. *Concessionary regimes*

- 4.4 While the outcome of the CASS review will result in us removing many of the non-MiFID provisions in CASS and applying many of the MiFID provisions to all firms, we are committed to retaining the current provisions dealing with particular areas of industry. For example, CASS 4 provides a concessionary CASS regime for trustee firms. We proposed to retain these provisions in the new client money chapter, and we received support to do so.

Our response: Respondents agreed with our proposals, and therefore, we confirm our policy approach.

3. *Professional opt-out*

- 4.5 In the CP we described how CASS 4.1.9 R permits a firm to agree with intermediate customers and eligible counterparties, that money that would otherwise be ‘client money’, will not be subject to the protections established by the CASS regime. However, this is not compatible with MiFID segregation requirements. Instead, CASS Chapter 7 (currently the MiFID-scope client money chapter) permits clients to transfer ‘full ownership of money to a firm for the purpose of securing or otherwise covering present or future, actual or contingent or prospective obligations, and that money should no longer be regarded as client money’.

In the CP we asked:

Q17: Do you agree with our proposal? If not, why not?

Q18: Does your firm make use of the opt-out? If not, do you see any reason for it to be kept?

Q19: Do you foresee any difficulty in our removing the opt-out provisions in CASS 4, and making available to all firms the full title transfer collateral arrangements contained in CASS 7?

- 4.6 Following feedback we received from firms to a pre-consultation questionnaire, we consulted on the basis that the professional opt-out provisions will be retained for non-scope firms. The majority of respondents stated that it would be preferable to maintain the status quo to avoid amending client agreements for little realisable benefit.

Our response: We confirm that we follow our proposals and retain the professional opt-out as described in CP08/6. This will maintain the status quo for certain firms, while fully implementing our MiFID obligations. The proposal retains a flexible regime for non-scope business. This approach will allow certain firms to provide service for clients at a reasonable cost, with such firms avoiding the need to repaper client agreements/terms of business documentation.

4. *Records and accounts*

- 4.7 The current CASS 4 and 7 provisions on the keeping of records and accounts are different. Under CASS 4.3.111 R, a firm must ensure that it keeps proper records, sufficient to show and explain the firm’s transactions and commitments regarding its client money, for three years after they were made. The equivalent provision in CASS 7 requires firms to keep ‘such records and accounts as are necessary to enable it, at any time and without delay, to distinguish client money held for one client from client money held for any other client, and from its own money’. Records must be kept for a period of five years after they were made.

In the CP we asked:

Q20: Do you agree with our proposal? If not, why not?

- 4.8 We understand that firms as a matter of course retain such records for up to seven years for legal and tax compliance reasons, and accordingly, as part of the simplification of CASS we proposed to apply the MiFID standard to all firms.

Our response: All respondents agreed with our proposal, and therefore, we confirm our policy approach.

5. *Internal and external reconciliations*

- 4.9 Existing provisions in CASS 4 require firms to undertake internal and external reconciliations in relation to client investments at different frequencies. The MiFID provisions in CASS 7 refer to a requirement to conduct ‘regular’ external reconciliations and make reference to a requirement for internal reconciliations in guidance only. This is owing to the fact that the language used in MiFID did not expressly refer to internal reconciliations. We proposed to remove the prescriptive provisions dealing with reconciliations in CASS 4 and apply the MiFID standard in CASS 7.6.6G to CASS 7.6.16R to all firms.

In the CP we asked:

Q21: Do you envisage there being any difficulty in applying the MiFID standard to all firms?

- 4.10 The majority of firms supported our proposals. However, concerns were raised regarding the divergent positions firms and their auditor’s may take about internal and external reconciliations. Again, a small number of respondents requested a ‘maximum period’ between reconciliations.

Our response: Consistent with our approach in the custody rules, the primary obligation is for the firm to determine an appropriate method and time scale for performing reconciliations, suitable to their structure and business model. It is then for auditors, in their capacity as an external and independent adviser, to use their professional judgement to offer assurance on the firm’s systems and controls. We will not issue further guidance on this matter. To prescribe parameters decreases the flexibility afforded to firms in maintaining systems and controls appropriate to their business model. There is also no justification for super-equivalence with MiFID.

6. *Group banks*

- 4.11 The merger of CASS Chapters 4 and 7 will result in the removal of the ‘group bank’ provisions currently contained in CASS 4.3.46 R and CASS 4.3.47 R, which impose additional requirements on a firm (including disclosure) if they hold client money in a bank in the same group as them. This is largely due to the fact that MiFID does not contain equivalent provisions, although it does provide provisions regarding a firm’s periodic review of its selection of a bank.

In the CP we asked:

Q22: Do you agree with our proposal? If not, why not?

Our response: Respondents agreed with our proposal, and therefore, we confirm our policy approach.

7. *Client bank accounts*

- 4.12 We proposed to offer non-MiFID firms increased flexibility consistent with CASS 7.4.1 R, which provides a firm with a choice between a central bank, a BCD credit institution, a bank authorised in a third country and a qualifying money market fund.

Our response: Respondents agreed with our proposal, and therefore, we confirm our policy approach.

- 4.13 In the CP we proposed to delete the provisions regarding client bank accounts for non-scope firms in CASS 4.3.46 R and CASS 4.3.47 R and give firms greater flexibility offered by the MiFID standard. The equivalent MiFID-based provision in CASS 7.4.11 R is more principles-based, requiring a firm to take ‘necessary steps to ensure that client money which is deposited... in a central bank, a credit institution, a bank authorised in a third country or a qualifying money market fund is held in an account or accounts identified separately from any accounts used to hold money belong to the firm’.

- 4.14 In line with our move to more principles-based regulation, we proposed to adopt the MiFID approach to client bank accounts for all firms

In the CP we asked:

Q24: Do you agree with our proposals? If not, why not?

- 4.15 Our proposal was broadly welcomed by industry. Two responses disagreed with our proposals because designated accounts would be pooled separately in the event of a bank failure or other pooling event.

Our response: We confirm our approach and note that the CASS Distribution Rules are currently being considered following the Banking Reform Project. We will consider the pooling issues in the context of this review.

8. *Business in the name of the firm*

- 4.16 CASS 7.2.2 R provides that money is not client money where the firm carries on business in its own name on behalf of the client where that is required by the very nature of the transaction and the client is in agreement. We proposed to delete this provision as we consider CASS 7.2.8 R deals with delivery versus payment transactions, which are specifically addressed in CASS 7.2.8 R.

In the CP we asked:

Q25: Do you agree with our proposals? If not, why not?

Q26: Do you use CASS 7.2.2 R to exempt any transaction other than DVP transactions?

Our response: Respondents generally agreed with our proposals, and therefore, we confirm our policy approach.

9. *'Approved bank' exemption*

- 4.17 An exemption from the client money regime is provided in CASS 4.1.2 R (3) to 'approved banks', whereas CASS 7.1.8 R refers to 'credit institutions'. The 'credit institutions' exemption is slightly narrower, not exempting those institutions established outside the EEA. In CP08/6 we envisaged that non-EEA entities would, in practice, establish a subsidiary in the UK, allowing us to move to the MiFID standard.
- 4.18 A substantial number of banks established outside the EEA disagreed with the proposal. In particular, some responses stated that a large proportion of their business was conducted through UK branches. It was also noted that branches have higher prudential requirements than subsidiaries. Accordingly, the responses suggest that maintaining the 'approved banks' definition actually strengthens consumer protection and maintains a level playing field.
- 4.19 On the other hand, a smaller number of firms, trade bodies and auditors supported this proposal.

Our response: We do not intend to apply the MiFID standard to firms undertaking non-scope business and will retain the drafting in CASS 4.1.2 R (3), which refers to 'approved banks' as opposed to 'credit institutions'. This approach is similar to our approach for the retention of the professional opt-out for firms undertaking non-MiFID business.

10. *Affiliated companies*

- 4.20 We proposed to apply the MiFID standard whereby a firm that holds money on behalf of, or receives money from, an affiliated company must treat the affiliated company as any other client of the firm for the purposes of the client money chapter.

In the CP we asked:

Q28: Do you agree with our proposals? If not, why not?

- 4.21 We received a small number of responses which disagreed with our proposals. One firm responded by stating that it had no objection to our proposal but did, however, question the usefulness of removing the carve-out from non-scope firms in practice.

Our response: We confirm that we will maintain the carve-out for non-MiFID scope firms in line with the feedback we received.

5 SUP 3.10 audit requirements

Introduction

- 5.1 Auditors' duties to report on client assets are contained in SUP 3.10. Supplementary material is also contained in Practice Note 21, which is issued by the Auditing Standards Board. As we have stated previously, the audit requirement is a key consumer protection requirement and safeguard in ensuring that firms are complying with CASS requirements. The audit report is an important regulatory tool for us, particularly given recent turbulent market conditions.
- 5.2 We consulted on the basis that we would delete guidance contained in CASS 6.5.14 G, CASS 6.5.15 G and CASS 7.6.17 – CASS 7.6.19 G.
- 5.3 We received a balanced response, but note auditors and a trade body disagreed with our proposals. The respondents that disagreed with our proposals suggested that auditors and firms rely on the cross-references contained in the guidance.
- 5.4 Some respondents additionally suggested that we review the requirement to report on compliance with the rules at a point in time, usually the year or period end, as well as the need to provide negative assurance to the FSA where firms are not authorised to hold client money and/or custody assets. One trade association suggested reviewing the scope to return to the materiality test contained in the Securities and Futures Authority rules. And one firm suggested that all of the audit requirements should be contained within the CASS sourcebook itself.

Our response: The client assets auditor's reports is a key safeguard in ensuring that firms are complying with the CASS requirements and accordingly are providing an appropriate degree of consumer protection. We therefore confirm that we will maintain cross-references between CASS and SUP 3.10 to assist firms and auditors.

As the respondents noted, the requirement to report on compliance throughout the year is a non-derogatable MiFID requirement and provides vital supervisory information that the FSA uses. Reporting at a specific period of time allows us to determine quickly whether or not these breaches have been resolved in the year and accordingly, helps us to identify firms requiring further supervisory input in this area.

We do not believe that negative assurance is an onerous administrative burden, which ensures that a firm's senior management has a clear oversight of the firm's systems and controls and are holding the relevant permissions. We consider that it is appropriate for full disclosure of breaches in the CASS auditor's report, which means that the materiality test would be inappropriate.

6 The distribution rules

- 6.1 As noted in the CP, the distribution rules are currently included in CASS 4, 5 and 7. As these provisions only apply in the event of a firm's insolvency, we will move them into a stand alone chapter.
- 6.2 We have not altered the procedures established by these provisions. However, we anticipate further changes will be required to these provisions as a result of the Banking and Compensation Reform Project. We anticipate publishing a Consultation Paper in the second quarter of 2009 on this.

7 Miscellaneous issues

Qualifying money market funds

- 7.1 Two respondents raised the issue of the use of Qualifying Money Market Funds (QMMFs). Despite the language used in MiFID not distinguishing between the short-term and long-term ratings assigned to money market instruments, rating agencies assign such ratings. We do not intend to issue any further formal guidance, but we will contact the respondents to discuss this matter directly. We also take this opportunity to remind firms that utilise the QMMF provisions, to ensure compliance with other relevant Handbook provisions such as COBS.

Part III

8 Client money – insurance mediation activity

- 8.1 In the CP we noted our intention to consult on the regime for general insurance intermediaries in the course of 2009. Our objective is to incorporate the client money rules for general insurance intermediaries into a single client money chapter within CASS. Chapter 7 will then cover those firms currently subject to CASS 4, 5, and 7 client money provisions. Consistent with the approach taken in CP08/6, we will seek to create a common client money platform in line with more principles-based regulation.
- 8.2 While we did not formally consult on CASS 5, we generated discussion on several areas identified in earlier thematic work. For ease of reference, topics discussed in the CP included advancing credit, using firms own ledgers for reconciliations, informed consent, plain English guides, credit write-backs, periodic segregation, risk transfer agreements and audit requirements.
- 8.3 The responses also highlighted additional areas that respondents consider problematic and provided the foundations for issues to be considered in due course. We will be following up individual responses to the paper with respondents as part of our work on a future consultation paper.

List of non-confidential responses to CP08/6

Association of Foreign Banks (AFB)	Layton Blackham Insurance Brokers
AON	London Investment Banking Association (LIBA)
Aviva	Lloyd & Partners
British Insurance Brokers' Association (BIBA)	London Market Insurance Brokers' Committee (LMBC)
BNP Paribas	Lockton Companies International
Bank of New York Mellon Asset Servicing Broker Network	Mitsubishi UFJ Trust and Banking Corporation
British Venture Capital Association (BVCA)	Morse
Citi	Northern Trust
City of London Law Society	Perkins Slade
Commonwealth Bank of Australia	Roger Purcell
Compos Mentis	PricewaterhouseCoopers LLP (Financial Services Regulatory Practice)
Financial Services Consumer Panel	Royal Institute of Chartered Surveyors (RICS)
Davis Corporation	Roland Smith
Deloitte	Schroder & Co. Ltd
Deutsche Bank	Smart & Cook Limited
Friends Provident	State Street Corporation
Institute of Chartered Accounts in England and Wales (ICAEW)	Stuart Alexander
Institute of Insurance Brokers (IIB)	UKGI Ltd
Institutional Money Market Funds Association (IMMFA)	Venture Preference
Investment Management Association (IMA)	
Jardine Thompson	
Jeffries	
Jelf Group PLC	
KPMG	

Compatibility statement

This Policy Statement closely reflects the proposals described in CP08/6. Accordingly, the instrument does not differ significantly from the consultative draft. We have, however, retained carve-outs for non-scope firms in relation to affiliated companies and the ‘approved banks’ exemption, both of which are discussed in more detail in Part II.

Statutory objectives

1. The proposed changes will support our statutory objective of securing the appropriate degree of consumer protection by moving to a common platform for all firms engaged in investment business, which will also reduce the administrative burdens placed on firms.
2. The MiFID standard is non-derogatable for MiFID firms. We consider that the adoption of the MiFID standard for all firms offers an appropriate level of consumer protection that will provide firms with a sourcebook which, as far as possible, focuses upon the outcomes firms are expected to achieve.
3. The proposed rule change removes the existing disparity in regulation between MiFID-scope firms (approximately 1,000 firms) and non-scope firms (we estimate that there are fewer than 100 firms). But it retains key carve-outs for non-scope firms where justified, promoting efficient, orderly and fair markets.

Principles of good regulation

1. The review of the Client Assets sourcebook was a Better Regulation Action Plan obligation for us to review our rules and simplify the structure of CASS following the implementation of MiFID in November 2007.
2. The proposed changes will simplify and streamline the sourcebook and will reflect our move to a more principles-based approach to the regulation of clients’ assets and client money.
3. We estimate that of the 25,000 firms we regulate, only 1,500 firms have our permission to hold client assets/money. Of these firms, 1,000 are estimated to be subject to the MiFID chapters and 500 to the non-MiFID chapters. Included within the latter 500

firms are a substantial number which are subject to CASS 5 (which was not included within the scope of the consultation). Proportionate to the total number of regulated firms, the number of firms subject to the non-MiFID CASS chapters is minimal.

4. The proposals will make the CASS sourcebook more practical and easier for firms to understand and comply with our principles and requirements. The proposals should therefore be less onerous and reduce compliance costs whilst maintaining an appropriate level of consumer protection.

Cost-benefit analysis

In CP08/6 we stated that the policy proposals brought no significant impacts to the regime because:

- the MiFID provisions we have moved to are substantively equivalent in effect as the existing standard; and
- we have retained existing provisions for certain firms where our cost benefit analysis indicates the MiFID standard may not be justified (e.g. professional opt-out provisions).

Since the CP we have made two changes to our proposals. We intend to retain carve-outs for non-MiFID scope business in relation to the 'approved banks' exemption and the treatment of affiliated companies. These carve outs allow firms a continuing degree of flexibility. Since we do not expect either of these changes to lead to significant additional compliance costs relative to our CP proposals, we have not conducted a new CBA.

Made Handbook rules and guidance

**CLIENT ASSETS SOURCEBOOK (COMMON PLATFORM PROVISIONS)
INSTRUMENT 2008**

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 138 (General rule-making power);
 - (2) section 139 (Miscellaneous ancillary matters);
 - (3) section 156 (General supplementary powers); and
 - (4) 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 on 1 January 2009.

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 of definitions	Annex A
Conduct of Business sourcebook (COBS)	Annex B
Client Assets sourcebook (CASS)	Annex C

Notes

- E. In this instrument, the “notes” (indicated by “**Note:**”) are included for the convenience of readers but do not form part of the legislative text.

Citation

- F. This instrument may be cited as the Client Assets Sourcebook (Common Platform Provisions) Instrument 2008.

By order of the Board
25 September 2008

Annex A

Amendments to the Glossary of definitions

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

<u>applicable asset</u>	(a)	<u>in relation to MiFID business, a financial instrument; or</u>
	(b)	<u>in relation to safeguarding and administering investments that is not MiFID business, a designated investment.</u>
client bank account	(1)	(other than in CASS 7 and <u>CASS 7A</u> and principally in CASS 4 and CASS 5):
	(a)	an account at a bank which:
	(i)	holds the <i>money</i> of one or more <i>clients</i> ;
	(ii)	is in the name of the <i>firm</i> ;
	(iii)	includes in its title an appropriate description to distinguish the <i>money</i> in the account from the <i>firm's money</i> ; and
	(iv)	is a current or a deposit account; or
	(b)	a money market deposit of <i>client money</i> which is identified as being <i>client money</i> .
	(2)	(in CASS 7 <u>and CASS 7A</u>)
	(a)	an account at a bank which:
	(i)	holds the money of one or more <i>clients</i> ;
	(ii)	is in the name of the <i>firm</i> ; and
	(iii)	is a current or a deposit account; or
	(b)	a money market deposit account of <i>client money</i> which is identified as being <i>client money</i> .
client money	(1)	(in CASS 2 and CASS 4, and, in so far as it relates to matters covered by CASS 2 or CASS 4, COBS) subject to the <i>client money rules</i>, money of any currency which, in the course of carrying on <i>designated investment business</i> that is not <i>MiFID business</i>, a <i>firm</i>

holds in respect of any *investment agreement* entered into, or to be entered into, with or for a *client*, or which a *firm* treats as *client money* in accordance with the *client money rules*. [deleted]

(2) (in CASS 5) subject to the *client money rules*, money of any currency which, in the course of carrying on *insurance mediation activity*, a *firm* holds on behalf of a *client* or which a *firm* treats as *client money* in accordance with the *client money rules*.

(2A) (in CASS 6, ~~and~~ CASS 7 and CASS 7A and, in so far as it relates to matters covered by CASS 6, ~~or~~ CASS 7, or COBS) subject to the *client money rules*, money of any currency:

(a) that a *firm* receives or holds for, or on behalf of, a *client* in the course of, or in connection with, its *MiFID business*; and/or

(b) which, in the course of carrying on *designated investment business* that is not *MiFID business*, a *firm* holds in respect of any *investment agreement* entered into, or to be entered into, with or for a *client*, or which a *firm* treats as *client money* in accordance with the *client money rules*.

(3) (in MIPRU):

(a) in relation to an *insurance intermediary* when acting as such, money which is *client money* in (2);

(b) in relation to a *home finance intermediary* when acting as such, money of any currency which in the course of carrying on *home finance mediation activity*, the *firm* holds on behalf of a *client*, either in a bank account or in the form of cash.

(4) (4) (in UPRU) *client money* for the purposes of the *client money rules*.

client money
chapter CASS 7.

client money
(MiFID
business)
distribution
rules CASS 7.9.

Client client
money
distribution CASS 4.4 CASS 7A.

- (2) (in CASS 5) an event that occurs in the circumstances described in CASS 5.6.5R (Failure of the authorised firm: primary pooling event).
- (3) (in CASS 7 and CASS 7A) an event that occurs in the circumstances described in ~~CASS 7.9.4R~~ 7A.2.2R (Failure of the authorised firm: primary pooling event).

safe custody
asset

- (a) in relation to MiFID business, a financial instrument; or
- (b) in relation to safeguarding and administering investments that is not MiFID business, a safe custody investment.

secondary
pooling event

- (1) ~~(in CASS 4) an event that occurs in the circumstances described in CASS 4.4.14R (Failure of a bank, intermediate broker, settlement agent or OTC counterparty: secondary pooling events).~~ [deleted]
- (2) (in CASS 5) an event that occurs in the circumstances described in CASS 5.6.14R (Failure of a bank, other broker or settlement agent: secondary pooling events).
- (3) (in CASS 7 and CASS 7A) an event that occurs in the circumstances described in ~~CASS 7.9.14R~~ 7A.3.1R (Failure of a bank, intermediate broker, settlement agent or OTC counterparty: secondary pooling events).

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

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

- 6.1.7 R (1) A firm that holds *designated investments* or *client money* for a *retail client* subject to the ~~*MiFID*~~ *custody chapter* or the ~~*MiFID*~~ *client money chapter* and ~~any third country investment firm~~ that holds ~~*designated investments*~~ or ~~*client money*~~ for a ~~*retail client*~~ must provide that *client* with the following information:

...

...

- 6.1.8 G Paragraphs (1), (3) and (4) of ~~COBS 6.1.7R~~ apply in relation to ~~*MiFID*~~ or ~~*equivalent third country business*~~ and also to ~~*firms*~~ that have elected to comply with the ~~*custody rules*~~ in the ~~*MiFID custody chapter*~~ or the ~~*client money rules*~~ in the ~~*MiFID client money chapter*~~. [deleted]

Annex C

Amendments to the Client Assets sourcebook (CASS)

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

General application: what?

1.2.7 G ...

(3) The ~~non-directive custody chapter~~ and the ~~non-directive client money chapter~~ apply in relation to *regulated activities*, conducted by *firms*, which fall within the definition of ~~designated investment business other than MiFID business~~ and/or designated investment business.

...

(5) ~~The MiFID custody chapter and the MiFID client money chapter apply in relation to regulated activities, conducted by firms, which fall within the definition of:~~

(a) ~~MiFID business; and~~

(b) ~~designated investment business other than MiFID business, where the firm has, in accordance with those rules, opted to comply with the provisions of those rules with respect of this business. [deleted]~~

...

Application for retail clients, professional clients and eligible counterparties

1.2.8 G ...

(2) ~~In CASS, except in the insurance client money chapter, MiFID custody chapter and MiFID client money chapter, the term customer refers to retail clients and professional clients, but not eligible counterparties. Where relevant, each of the provisions of CASS makes clear whether it applies to activities carried on with or for retail clients or professional clients, or both. [deleted]~~

...

(4) Each provision in the *MiFID custody chapter* and the *MiFID client money chapter* makes it clear whether it applies to activities carried

on or for *retail clients, professional clients* or both. There is no further modification of the *rules* in these chapters in relation to activities carried on for *eligible counterparties*. Such *clients* are treated in the same way as other *professional clients* for the purposes of these *rules*.

...

Investments and money held under different regimes

1.2.10 R ~~Where a firm is subject to both the *non-directive custody chapter* and the *MiFID custody chapter*, it must ensure segregation between *designated investments* held under each chapter, including that *designated investments* held under different chapters with the same third party, are held in different, separately designated, accounts. [deleted]~~

1.2.11 R Where a firm is subject to more than one of the *non-directive client money chapter*, and the *insurance client money chapter* and the *MiFID client money chapter*, it must ensure segregation between money held under each chapter, including that money held under different chapters is held, in different, separately designated, *client bank accounts* or *client transaction accounts*.

...

1.2.13 G A firm may opt to hold under a single chapter ~~*designated investments* that would otherwise be held under different chapters (see CASS 6.1.17R)~~. A firm may also opt to hold under a single chapter *money* that would otherwise be held under different chapters (see ~~CASS 4.1.1AR~~, CASS 5.1.1R(3) and CASS 7.1.3R (4)).

...

Stock lending activity with or for ~~customers~~ clients

1.4.2 G (1) The *non-directive custody chapter* and the *non-directive client money chapter* apply in respect of any *stock lending activity* that is ~~not *MiFID business*~~ undertaken with or for a *customer* client by a firm. ~~If the *stock lending activity* involves *MiFID business* or if the firm has opted to comply with the *MiFID custody chapter* or the *MiFID client money chapter* with respect to its non-*MiFID business*, then the *MiFID custody chapter* and the *MiFID client money chapter* apply.~~

(2) The *collateral rules* apply, where relevant, in respect of *stock lending activity*, ~~whether or not the activity amounts to *MiFID business*~~.

Corporate finance business

- 1.4.3 G (1) The ~~non-directive custody chapter~~ and the ~~non-directive client money chapter~~ apply in respect of *corporate finance business* that is ~~not MiFID business~~ undertaken by a firm. If the *corporate finance business* involves *MiFID business* or if the firm has opted to comply with the ~~MiFID custody chapter~~ or the ~~MiFID client money chapter~~ with respect to its ~~non-MiFID business~~, then the ~~MiFID custody chapter~~ and the ~~MiFID client money chapter~~ apply.
- (2) The *collateral rules* apply, where relevant, in respect of *corporate finance business*, ~~whether or not the activity amounts to MiFID business~~.

Oil market activity and energy market activity

- 1.4.4 G (1) The ~~non-directive custody chapter~~ and the ~~non-directive client money chapter~~ apply in respect of *oil market activity* and other *energy market activity* that is ~~not MiFID business~~ undertaken by a firm. If the ~~energy market activity (including oil market activity)~~ involves *MiFID business* or if the firm has opted to comply with the ~~MiFID custody chapter~~ or the ~~MiFID client money chapter~~ with respect to its ~~non-MiFID business~~, then the ~~MiFID custody chapter~~ and the ~~MiFID client money chapter~~ apply.
- (2) The *collateral rules* apply, where relevant, in respect of *energy market activity*, ~~whether or not the activity amounts to MiFID business~~.

...

Depositories

- 1.4.6 R The ~~non-directive client money chapter~~ and the ~~MiFID client money chapter~~ ~~do~~ does not apply to a *depository* when acting as such.

...

- 1.4.8 R (1) Other than the mandate rules, CASS does not apply to a *trustee firm* which is not a *depository*, or the trustee of a *personal pension scheme* or *stakeholder pension scheme*, unless MiFID applies to it, in which case the custody chapter and the client money chapter do apply except for the MiFID custody chapter, the MiFID client money chapter and the mandate rules.
- (2) In the *MiFID custody chapter*, the *MiFID client money chapter* and the *mandate rules*, ‘*client*’ means ‘*trustee*’, ‘*trust*’, ‘*trust instrument*’

or 'beneficiary', as appropriate.

...

CASS 2 is deleted in its entirety. The text of the deleted chapter is not shown.

...

CASS 4 is deleted in its entirety. The text of the deleted chapter is not shown.

...

6 Custody ~~:MiFID business rules~~

6.1 Application

6.1.1 R This chapter (the *custody rules*) applies to a firm:

(1) ~~a *MiFID investment firm*: [deleted]~~

(a) ~~when it holds *financial instruments* belonging to a *client* in the course of its *MiFID business*; or [deleted]~~

(b) ~~that opts to comply with the *custody rules* under this chapter in accordance with CASS 6.1.17R(1), (Opt in to the MiFID custody rules); and [deleted]~~

(1A) when it holds *financial instruments* belonging to a *client* in the course of its *MiFID business*; and/or

(1B) when it is *safeguarding and administering investments*, in the course of business that is not *MiFID business*.

(2) ~~a *third country investment firm* that opts to comply with the *custody rules* under this chapter in accordance with CASS 6.1.17R(2) (Opt in to the MiFID client money rules). [deleted]~~

6.1.1A G The *regulated activity of safeguarding and administering investments* covers both the *safeguarding and administration of assets (without arranging)* and *arranging the safeguarding and administration of assets*, when those assets are either *safe custody investments* or *custody assets*. A *safe custody investment* is, in summary, a *designated investment* which a *firm* receives or holds on behalf of a *client*. *Custody assets* include *designated investments*, and any other assets that the *firm* holds or may hold in the same portfolio as a *designated investment* held for or on behalf of the *client*.

6.1.1B R Firms to which the custody rules apply by virtue of CASS 6.1.1R(1B) must also apply the custody rules to those custody assets which are not safe custody investments in a manner appropriate to the nature and value of those custody assets.

6.1.1C G In accordance with article 42 of the Regulated Activities Order, a firm (“I”) will not be arranging safeguarding and administration of assets if it introduces a client to another firm whose permitted activities include the safeguarding and administration of investments, or to an exempt person acting as such, with a view to that other firm or exempt person:

(1) providing a safe custody service in the United Kingdom; or

(2) arranging for the provision of a safe custody service in the United Kingdom by another person;

and the other firm, exempt person or other person who is to provide the safe custody service is not in the same group as I, and does not remunerate I.

6.1.2 G Firms are reminded that dividends (actual or payments in lieu), stock lending fees and other payments received for the benefit of a client, and which are due to the clients, should be held in accordance with the ~~MiFID~~ client money chapter where appropriate.

6.1.3 G ~~This chapter does not apply where a firm issues depositary receipts. The custody rules in the non-directive custody chapter provide a specialist regime for the issue of depositary receipts (see CASS 2.1.24R to CASS 2.1.26R). [deleted]~~

...

6.1.5 G For example, this chapter does not apply where a firm borrows ~~financial instruments~~ safe custody assets from a client as principal under a stock lending agreement.

Title transfer collateral arrangements

6.1.6 R The custody rules do not apply where a client transfers full ownership of a ~~financial instrument~~ safe custody asset to a firm for the purpose of securing or otherwise covering present or future, actual, contingent or prospective obligations.

[Note: recital 27 to MiFID]

...

Affiliated companies – MiFID business

- 6.1.10 G The fact that a *client* is an *affiliated company* in respect of *MiFID business* does not affect the operation of the *custody rules* in relation to that *client*.

Affiliated companies – non-MiFID business

- 6.1.10A G In respect of business which is not *MiFID business*, the *custody rules* do not apply to a *firm* when it safeguards and administers a *designated investment* on behalf of an *affiliated company*, unless:

- (1) the *firm* has been notified that the *designated investment* belongs to a *client* of the *affiliated company*; or
- (2) the *affiliated company* is a *client* dealt with at arm's length.

- 6.1.11 G ~~A *firm* that holds *financial instruments* on behalf of an *affiliated company* in respect of its *non-MiFID business* and opts under CASS 6.1.17 R to comply with this chapter in respect of that *non-MiFID business*, should refer to CASS 2.1.9 R(1) to determine whether the assets falls within the scope of the *custody rules* in the *non-directive custody chapter* and therefore within the scope of the opt-in. [deleted]~~

Delivery versus payment transactions

- 6.1.12 R (1) A *firm* need not treat this chapter as applying in respect of a delivery versus payment transaction through a commercial settlement system if it is intended that the ~~*financial instrument*~~ *safe custody asset* is either to be:
- (a) ...
- (b) ...

unless the delivery or payment by the *firm* does not occur by the close of business on the third *business day* following the date of payment or delivery of the ~~*financial instrument*~~ *safe custody asset* by the *client*.

- (2) Until such a delivery versus payment transaction through a commercial settlement system settles, a *firm* may segregate *money* (in accordance with the ~~*MiFID client money chapter*~~) instead of the *client's financial instruments* *safe custody assets*.

~~Arranging registration and recommendations~~

- 6.1.13 G ~~This chapter does not apply where a *firm* arranges registration of a *financial instrument*. In such circumstances, a *firm* must comply with the relevant *custody rules* in the *non-directive custody chapter* (see CASS 2.1.22R).~~

[deleted]

- 6.1.14 G ~~This chapter does not apply where a firm recommends to a retail client a third party to hold the assets of that client. In such circumstances, a firm must comply with the relevant custody rules in the non-directive custody chapter (see CASS 2.2.19R). [deleted]~~

Temporary handling of financial instruments safe custody assets

- 6.1.15 G The *custody rules* do not apply if a firm temporarily handles a *financial instrument safe custody asset* belonging to a client. A firm should temporarily handle *financial instrument a safe custody asset* for no longer than is reasonably necessary. In most transactions this would be no longer than one *business day*, but it may be longer or shorter depending upon the transaction in question. For example, when a firm executes an order to sell shares which have not been registered on a de-materialised exchange, handling documents for longer periods may be reasonably necessary. However, in the case of *financial instruments safe custody assets* in bearer form, the firm is expected to handle them for less than one *business day*. When a firm temporarily handles *financial instruments safe custody assets*, it is still obliged to comply with *Principle 10* (Clients' assets).
- 6.1.16 G When a firm temporarily handles a *financial instrument safe custody asset*, in order to comply with its obligation to act in accordance with *Principle 10* (Clients' assets), the following are guides to good practice:
- (1) a firm should keep the *financial instrument safe custody asset* secure, record it as belonging to that client, and forward it to the client or in accordance with the client's instructions as soon as practicable after receiving it; and
 - (2) a firm should make and retain a record of the fact that the firm has handled that *financial instrument safe custody asset* and of the details of the client concerned and of any action the firm has taken.

Exemptions which do not apply to MiFID business

- 6.1.16A R The exemptions in CASS 6.1.16BR to 6.1.16DG do not apply to a MiFID investment firm which holds financial instruments belonging to a client in the course of MiFID business.

Operators of regulated collective investment schemes

- 6.1.16B R The custody rules do not apply to a firm when it acts as the operator of a regulated collective investment scheme, in relation to activities carried on for the purpose of, or in connection with, the operation of the scheme.

Personal investment firms

- 6.1.16C R The custody rules do not apply to a personal investment firm when it temporarily holds a designated investment, other than in bearer form, belonging to a client, if the firm:
- (1) keeps it secure, records it as belonging to that client, and forwards it to the client or in accordance with the client's instructions, as soon as practicable after receiving it;
 - (2) retains the designated investment for no longer than the firm has taken reasonable steps to determine is necessary to check for errors and to receive the final document in connection with any series of transactions to which the documents relate; and
 - (3) makes a record, which must then be retained for a period of 5 years after the record is made, of all the designated investments handled in accordance with (1) and (2) together with the details of the clients concerned and of any action the firm has taken.
- 6.1.16D G Administrative convenience alone should not lead a personal investment firm to rely on CASS 6.1.16CR. Personal investment firms should consider what is in the client's interest and not rely on CASS 6.1.16CR as a matter of course.

Trustees and depositaries

- 6.1.16E R The specialist regime in CASS 6.1.16FR to 6.1.16IG does not apply to a MiFID investment firm which holds financial instruments belonging to a client in the course of MiFID business.
- 6.1.16F R When a trustee firm or depositary acts as a custodian for a trust or collective investment scheme and:
- (1) the trust or scheme is established by written instrument; and
 - (2) the trustee firm or depositary has taken reasonable steps to determine that the relevant law and provisions of the trust instrument or scheme constitution will provide protections at least equivalent to the custody rules for the trust property or scheme property;

the trustee firm or depositary need comply only with the custody rules listed in the table below.

<u>Reference</u>	<u>Rule</u>
<u>CASS 6.1.1R to CASS 6.1.9G and</u>	<u>Application</u>

<u>CASS 6.1.15G to CASS 6.1.16C R</u>	
<u>CASS 6.1.16ER to CASS 6.1.16IG</u>	<u>Trustees and depositaries</u>
<u>CASS 6.1.22G to CASS 6.1.24G</u>	<u>General purpose</u>
<u>CASS 6.2.1R and CASS 6.2.2R</u>	<u>Protection of clients' safe custody assets</u>
<u>CASS 6.2.3R and CASS 6.2.6G</u>	<u>Registration and recording</u>
<u>CASS 6.2.7R</u>	<u>Holding</u>
<u>CASS 6.4.1R and CASS 6.4.2G</u>	<u>Use of safe custody assets</u>
<u>CASS 6.5</u>	<u>Records, accounts and reconciliations</u>

6.1.16G G The reasonable steps referred in CASS 6.1.16FR(2) could include obtaining an appropriate legal opinion to that effect.

6.1.16H R When a trustee firm or depositary within CASS 6.1.16FR arranges for, or delegates the provision of safe custody services by or to another person, the trustee firm or depositary must also comply with CASS 6.3.1R (Depositing and arranging assets to be deposited with third parties) in addition to the custody rules listed in the table in CASS 6.1.16FR.

6.1.16I G A trustee firm or depositary that just arranges safeguarding and administration of assets may also take advantage of the exemption in CASS 6.1.16JR (Arrangers).

Arrangers

6.1.16J R Only the custody rules in the table below apply to a firm when arranging safeguarding and administration of assets.

<u>Reference</u>	<u>Rule</u>
<u>CASS 6.1.1R to CASS 6.1.9G and CASS 6.1.15G to CASS 6.1.16BR</u>	<u>Application</u>
<u>CASS 6.1.16JR</u>	<u>Arrangers</u>
<u>CASS 6.1.22G to CASS 6.1.24G</u>	<u>General purpose</u>
<u>CASS 6.3.1R(1A) and CASS 6.3.2G</u>	<u>Arranging for assets to be deposited with third parties</u>

CASS 6.1.16KR	Records
---------------	---------

6.1.16K R When a firm arranges safeguarding and administration of assets, it must ensure that proper records of the custody assets which it arranges for another to hold or receive, on behalf of the client, are made and retained for a period of 5 years after they are made.

Opt in to the MiFID custody rules

6.1.17 R (1) ~~A firm that holds financial instruments to which this chapter applies and assets in respect of which the non-directive custody chapter applies, may elect to comply with the provisions of this chapter in respect of all assets so held and if it does so, this chapter applies as if all such assets were financial instruments that the firm receives and holds in the course of, or in connection with, its MiFID business.~~ [deleted]

(1A) ~~A third country investment firm that holds designated investments belonging to a client in the course of its equivalent business may elect to comply with the provisions of this chapter in respect of the assets it holds to which the non-directive custody chapter applies. If it does so, this chapter applies as if all such assets were assets that the firm receives and holds in the course of, or in connection with, MiFID business.~~ [deleted]

(2) ~~An election under this rule must be in respect of all the activities of the firm when it is safeguarding and administering investments belonging to a client with the exception of arranging safeguarding and administration of assets within the scope of CASS 2.1.21R and CASS 2.1.22R and depositary receipt business within the scope of CASS 2.1.24R to CASS 2.1.26R.~~ [deleted]

(3) ~~A firm must make and retain a written record of the election it makes under this rule, including the date from which the election is to be effective. The firm must make the record on the date it makes the election and must keep it for a period of five years after ceasing to use it.~~ [deleted]

6.1.18 G ~~A firm cannot rely upon this opt in in respect of arranging safeguarding and administration of assets and depositary receipt business as the custody rules in the non-directive custody chapter provide specialised regimes in respect of these types of business which are outside the scope of this chapter.~~ [deleted]

6.1.19 G ~~If a firm has opted to comply with this chapter, the non-directive custody chapter will have no application to the activities to which the election applies.~~ [deleted]

6.1.20 G ~~A firm (other than a third country investment firm) that is only subject to the non-directive custody chapter may not choose to comply with this chapter. [deleted]~~

6.1.20A G ~~The information requirements concerning the safeguarding of financial instruments belonging to a client (see COBS 6.1.7R) apply to a firm that has elected to comply with this chapter with respect of all assets to which the election applies. [deleted]~~

Disposal of financial instruments

6.1.21 R ~~The custody rules cease to have effect in relation to a financial instrument it has been disposed of in accordance with a valid client instruction. [deleted]~~

General purpose

6.1.22 G Principle 10 (Clients' assets) requires a firm to arrange adequate protection for clients' assets when it is responsible for them. As part of these protections, the custody rules require a firm to take appropriate steps to protect *financial instruments safe custody assets* for which it is responsible.

6.1.23 G The rules in this chapter are designed primarily to restrict the commingling of client and the firm's assets and minimise the risk of the client's *financial instruments safe custody assets* being used by the firm without the client's agreement or contrary to the client's wishes, or being treated as the firm's assets in the event of its insolvency.

6.1.24 G The custody rules also, where relevant, implement the provisions of MiFID which regulate the obligations of a firm when it holds *financial instruments* belonging to a client in the course of its MiFID business.

6.2 Holding of client assets

Requirement to protect clients' ~~financial instruments~~ safe custody assets

6.2.1 R A firm must, when holding *financial instruments safe custody assets* belonging to clients, make adequate arrangements so as to safeguard clients' ownership rights, especially in the event of the firm's insolvency, and to prevent the use of *financial instruments safe custody assets* belonging to a client on the firm's own account except with the client's express consent.

[Note: article 13(7) of MiFID]

Requirement to have adequate organisational arrangements

- 6.2.2 R A *firm* must introduce adequate organisational arrangements to minimise the risk of the loss or diminution of *clients' financial instruments safe custody assets*, or the rights in connection with those *financial instruments safe custody assets*, as a result of the misuse of the *financial instruments safe custody assets*, fraud, poor administration, inadequate record-keeping or negligence.

[**Note:** article 16(1)(f) of the *MiFID implementing Directive*]

Registration and recording of legal title

- 6.2.3 R To the extent practicable, a *firm* must effect appropriate registration or recording of legal title to a *financial instrument safe custody asset* in the name of:

...

- (3) any other third party if:

(a) the *financial instrument safe custody asset* is subject to the law or market practice of a jurisdiction outside the *United Kingdom* and the *firm* has taken reasonable steps to determine that it is in the *client's* best interests to register or record it in that way, or that it is not feasible to do otherwise, because of the nature of the applicable law or market practice; and

(b) ...

- (4) the *firm* if:

(a) the *financial instrument safe custody asset* is subject to the law or market practice of a jurisdiction outside the *United Kingdom* and the *firm* has taken reasonable steps to determine that it is in the *client's* best interests to register or record it in that way, or that it is not feasible to do otherwise, because of the nature of the applicable law or market practice; and

(b) ...

...

- 6.2.5 R A *firm* may register or record legal title to its own *financial instrument applicable assets* in the same name as that in which legal title to a *financial instrument safe custody asset* is registered or recorded, but only if:

- (1) the *firm's financial instruments applicable assets* are separately identified in the *firm's* records from the *financial instruments safe*

custody assets; or

- (2) the *firm* registers or records a *financial instrument safe custody asset* in accordance with CASS 6.2.3R(4).

...

- 6.2.7 R A *firm* must ensure that any documents of title to *financial instruments applicable assets* in *bearer form*, belonging to the *firm* and which it holds in its physical possession, are kept separately from any document of title to a *client's financial instrument safe custody assets* in *bearer form*.

6.3 **Depositing assets and arranging for assets to be deposited with third parties**

- 6.3.1 R (1) A *firm* may deposit *financial instruments safe custody assets* held by it on behalf of its *clients* into an account or accounts opened with a third party, but only if it exercises all due skill, care and diligence in the selection, appointment and periodic review of the third party and of the arrangements for the holding and safekeeping of those *financial instruments safe custody assets*.
- (1A) A *firm* which arranges the registration of a *safe custody investment* through a third party must exercise all due skill, care and diligence in the selection and appointment of the third party.
- (2) A *firm* must take the necessary steps to ensure that any *client's financial instruments safe custody assets* deposited with a third party, in accordance with this *rule*, are identifiable separately from the *financial instruments applicable assets* belonging to the *firm* and from the *financial instruments applicable assets* belonging to that third party, by means of differently titled accounts on the books of the third party or other equivalent measures that achieve the same level of protection.
- (3) When a *firm* makes the selection, appointment and conducts the periodic review referred to under this *rule*, it must take into account:
- (a) ...
- (b) any legal requirements or market practices related to the holding of those *financial instruments safe custody assets* that could adversely affect *clients'* rights.
- (4) A *firm* must make a record of the grounds upon which it satisfies

itself as to the appropriateness of its selection of a third party as required in this *rule*. The *firm* must make the record on the date it makes the selection and must keep it from the date of such selection until five years after the *firm* ceases to use the third party to hold *financial instruments safe custody assets* belonging to *clients*.

[**Note:** articles 16(1)(d) and 17(1) of the *MiFID implementing Directive*]

6.3.2 G In discharging its obligations under this section, a *firm* should also consider, together with any other relevant matters:

(1) once a *financial instrument safe custody asset* has been lodged by the *firm* with the third party, the third party's performance of its services to the *firm*;

(2) the arrangements that the third party has in place for holding and safeguarding the *financial instrument safe custody asset*;

...

6.3.3 G A *firm* should consider carefully the terms of its agreements with third parties with which it will deposit *financial instruments safe custody assets* belonging to a *client*. The following terms are examples of the issues *firms* should address in this agreement:

(1) that the title of the account indicates that any *financial instrument safe custody asset* credited to it does not belong to the *firm*;

(2) that the third party will hold or record a *financial instrument safe custody asset* belonging to the *firm's client* separately from any *financial instrument applicable asset* belonging to the *firm* or to the third party;

(3) the arrangements for registration or recording of the *financial instrument safe custody asset* if this will not be registered in the *client's* name;

(4) the restrictions over the third party's right to claim a lien, right of retention or sale over any *financial instrument safe custody asset* standing to the credit of the account;

...

(8) the provisions detailing the extent of the third party's liability in the event of the loss of a *financial instrument safe custody asset* caused by the fraud, wilful default or negligence of the third party or an agent appointed by him.

- 6.3.4 R (1) A *firm* must only deposit *financial instruments safe custody assets* with a third party in a jurisdiction which specifically regulates and supervises the safekeeping of *financial instruments safe custody assets* for the account of another person with a third party who is subject to such regulation.
- (2) A *firm* must not deposit *financial instruments safe custody assets* held on behalf of a *client* with a third party in a country that is not an *EEA State* (third country) and which does not regulate the holding and safekeeping of *financial instruments safe custody assets* for the account of another person unless:
- (a) the nature of the *financial instruments safe custody assets* or of the *investment services* connected with those *financial instruments safe custody assets* requires them to be deposited with a third party in that third country; or
 - (b) the *financial instruments safe custody assets* are held on behalf of a *professional client* and the *client* requests the *firm* in writing to deposit them with a third party in that third country.
- (3) ~~In the case of activities a *firm* has opted into this chapter under CASS 6.1.17R(1) and (2) do not apply. However, the *firm* must deposit *financial instruments* belonging to *clients* pursuant to such activities with a *custodian* and must hold any document of title to a *financial instrument* either in the physical possession of the *firm* or: [deleted]~~
- ~~(a) for a *retail client*, with a *custodian*; [deleted]~~
 - ~~(b) for a *professional client*, with one or more of the following: [deleted]~~
 - ~~(i) a *custodian*; [deleted]~~
 - ~~(ii) any *person* whom the *firm* has taken reasonable steps to determine is a *person* whose business includes the provision of appropriate safe custody services; or [deleted]~~
 - ~~(iii) in accordance with the *professional client's* specific written instructions. [deleted]~~

[Note: article 17(2) and (3) of the *MiFID implementing Directive*]

6.4 Use of ~~financial instruments~~ safe custody assets

- 6.4.1 R (1) A *firm* must not enter into arrangements for *securities financing transactions* in respect of ~~financial instruments~~ safe custody assets held by it on behalf of a *client* or otherwise use such ~~financial instruments~~ safe custody assets for its own account or the account of another *client* of the *firm*, unless:
- (a) the *client* has given express prior consent to the use of the ~~financial instruments~~ safe custody assets on specified terms; and
 - (b) the use of that *client's* ~~financial instruments~~ safe custody assets is restricted to the specified terms to which the *client* consents.
- (2) A *firm* must not enter into arrangements for *securities financing transactions* in respect of ~~financial instruments~~ safe custody assets held by it on behalf of a *client* in an omnibus account held by a third party, or otherwise use ~~financial instruments~~ safe custody assets held in such an account for its own account or for the account of another *client* unless, in addition to the conditions set out in (1):
- (a) each *client* whose ~~financial instruments~~ safe custody assets are held together in an omnibus account has given express prior consent in accordance with (1)(a); or
 - (b) the *firm* has in place systems and controls which ensure that only ~~financial instruments~~ safe custody assets belonging to *clients* who have given express prior consent in accordance with the requirements of (1)(a) are used.
- (3) For the purposes of obtaining the express prior consent of a *retail client* under this *rule* the signature of the *retail client* or an equivalent alternative mechanism is required.
- (4) A *firm* which does not undertake *MiFID business* does not need to comply with (1), (2) and (3) until 1 May 2009.

[**Note:** article 19 of the *MiFID implementing Directive*]

- 6.4.2 G *Firms* are reminded of the *client's best interests rule*, which requires the *firm* to act honestly, fairly and professionally in accordance with the best interests of their *clients*. An example of what is generally considered to be such conduct, in the context of *stock lending activities* involving *retail clients* is:
- (1) ...

- (2) the current realisable value of the *financial instrument safe custody asset* and of the *relevant collateral* is monitored daily; and
- (3) the *firm* provides *relevant collateral* to make up the difference where the current realisable value of the collateral falls below that of the *financial instrument safe custody asset*, unless otherwise agreed in writing by the *client*.

6.4.3 R Where a *firm* uses *financial instruments safe custody assets* as permitted in this section, the records of the *firm* must include details of the *client* on whose instructions the use of the *financial instruments safe custody assets* has been effected, as well as the number of *financial instruments safe custody assets* used belonging to each *client* who has given consent, so as to enable the correct allocation of any loss.

[Note: article 19(2) of the *MiFID implementing Directive*]

6.5 Records, accounts and reconciliations

Records and accounts

6.5.1 R A *firm* must keep such records and accounts as necessary to enable it at any time and without delay to distinguish *financial instruments safe custody assets* held for one *client* from *financial instruments safe custody assets* held for any other *client*, and from the *firm's* own *financial instruments applicable assets*.

[Note: article 16(1)(a) of the *MiFID implementing Directive*]

6.5.2 R A *firm* must maintain its records and accounts in a way that ensures their accuracy, and in particular their correspondence to the *financial instruments safe custody assets* held for *clients*.

[Note: article 16(1)(b) of the *MiFID implementing Directive*]

...

Internal reconciliation of *financial instruments safe custody assets* held for clients

6.5.4 G (1) ~~SYSC 4.1.1R requires *firms* to have robust governance arrangements, such as internal control mechanisms, including sound administrative and accounting procedures and effective control and safeguard arrangements for information processing systems. In addition, SYSC 6.1.1R requires *firms* to establish, implement and maintain adequate policies and procedures sufficient to ensure the *firm's* compliance with its obligations under the *regulatory system*. Carrying out~~

internal reconciliations of the *financial instruments safe custody assets* held for each *client* with the *financial instruments safe custody assets* held by the *firm* and third parties is an important step in the discharge of the *firm's* obligations under CASS 6.5.2R, and where relevant, SYSC 4.1.1R and SYSC 6.1.1R.

...

- (3) Reconciliation methods which can be adopted for these purposes include the 'total count method', which requires that all *financial instruments safe custody assets* be counted and reconciled as at the same date.
- (4) If a *firm* chooses to use an alternative reconciliation method (for example the 'rolling stock method') it needs to ensure that:
 - (a) all of a particular *financial instrument safe custody asset* are counted and reconciled as at the same date; and
 - (b) all *financial instruments safe custody assets* are counted and reconciled during a period of six months.

...

Reconciliations with external records

- 6.5.6 R A *firm* must conduct on a regular basis, reconciliations between its internal accounts and records and those of any third parties by whom those *financial instruments safe custody assets* are held.

[**Note:** article 16(1)(c) of the *MiFID implementing Directive*]

- 6.5.7 G Where a *firm* deposits *financial instruments safe custody assets* belonging to a *client* with a third party, in complying with the requirements of CASS 6.5.6R, the *firm* should seek to ensure that the third party will deliver to the *firm* a statement as at a date or dates specified by the *firm* which details the description and amounts of all the *financial instruments safe custody assets* credited to the account, and that this statement is delivered in adequate time to allow the *firm* to carry out the periodic reconciliations required in CASS 6.5.6R.

Frequency of external reconciliations

- 6.5.8 G A *firm* should perform the reconciliation required by CASS 6.5.6R:
- (1) ...
 - (2) ...

to ensure the accuracy of its internal accounts and records against those of third parties by whom ~~financial instruments~~ safe custody assets are held.

Independence of person conducting reconciliations

- 6.5.9 G Whenever possible, a *firm* should ensure that reconciliations are carried out by a *person* (for example an *employee* of the *firm*) who is independent of the production or maintenance of the records to be reconciled (~~see SYSC 5.1.6R~~).

...

7 Client money : ~~MiFID~~ business rules

7.1 Application and Purpose

Application

- 7.1.1 R This chapter (the *client money rules*) applies to a *firm* that receives money from or holds money for, or on behalf of, a *client* in the course of, or in connection with:
- (1) ~~a *MiFID investment firm*: [deleted]~~
 - (a) ~~that holds *client money*; or [deleted]~~
 - (b) ~~that opts to comply with this chapter in accordance with CASS 7.1.3R(1) (Opt in to the MiFID client money rules); and [deleted]~~
 - (2) ~~a *third country investment firm* that opts to comply with this chapter in accordance with CASS 7.1.3R(2) (Opt in to the MiFID client money rules); [deleted]~~
 - (3) its *MiFID business*; and/or
 - (4) its *designated investment business*, that is not *MiFID business* in respect of any *investment agreement* entered into, or to be entered into, with or for a *client*;

unless otherwise specified in this section.

7.1.2 G ~~CASS 7.2 (Definition of client money) sets out the circumstances in which money is considered client money for the purposes of this chapter. [deleted]~~

Opt-in to the ~~MiFID~~ client money rules

7.1.3 R (1) A firm that receives or holds money to which this chapter applies in relation to:

(a) its MiFID business; or

(b) its MiFID business and its designated investment business which is not MiFID business;

~~and holds money in respect of which this chapter applies and money in respect of which the non-directive client money chapter or the insurance client money chapter~~ CASS 5 applies, may elect to comply with the provisions of this chapter in respect of all such money and if it does so, this chapter applies as if all such money were money that the firm receives and holds in the course of, or in connection with, its *MiFID business*.

(1A) ~~A third country investment firm that receives or holds money from, for or on behalf of a client in the course of, or in connection with, its equivalent business of a third country investment firm may elect to comply with the provisions of this chapter in respect of the money it holds to which the non-directive client money chapter or the insurance client money chapter applies. If it does so, this chapter applies as if all such money were money that the firm receives and holds in the course of, or in connection with, MiFID business. [deleted]~~

(1B) A firm that receives or holds money to which this chapter applies solely in relation to its designated investment business which is not MiFID business and receives or holds money in respect of which the insurance client money chapter applies, may elect to comply with the provisions of this chapter in respect of all such money and if it does so, this chapter applies as if all such money were money that the firm receives and holds in the course of or in connection with its designated investment business.

...

7.1.4 G The opt-in to the *client money rules* in this chapter does not apply in respect of money that a firm holds outside of the scope of ~~the non-directive client money chapter or the insurance client money chapter, such as money falling within the scope of the opt out for non-IMD designated investment business (see CASS 4.1.11R).~~

- 7.1.5 G If a *firm* has opted to comply with this chapter, ~~the *non-directive client money chapter* or the *insurance client money chapter*~~ will have no application to the activities to which the election applies.
- 7.1.6 G A *firm* ~~(other than a *third country investment firm*)~~ that is only subject to the ~~*non-directive client money chapter* or the *insurance client money chapter*~~ may not opt to comply with this chapter.
- 7.1.7 G ~~If a *firm* that has agreed with an *insurance undertaking* under the *client money rules* in the *insurance client money chapter* to treat the undertaking's money as *client money*, opts in to this chapter in accordance with this section, the *insurance undertaking's* interest under the trust (or in Scotland agency) will be subordinated to the interests of the *firm's* other *clients*.
[deleted]~~
- 7.1.7A G ~~The information requirements concerning the safeguarding of *client money* (see *COBS* 6.1.7R) apply to a *firm* that has elected to comply with this chapter with respect of all *client money* to which the election applies.
[deleted]~~

Professional client opt-out

- 7.1.7B R *CASS* 7.1.7CG to *CASS* 7.1.7IG do not apply to a *firm* in relation to money held in connection with its *MiFID business* to which this chapter applies or in relation to money for which the *firm* has made an election under *CASS* 7.1.3R(1).

Money that is not client money: 'opt outs' for any business other than *insurance mediation activity*

- 7.1.7C G The 'opt out' provisions provide a *firm* with the option of allowing a *professional client* to choose whether their money is subject to the *client money rules* (unless the *firm* is conducting *insurance mediation activity*).
- 7.1.7D R Subject to *CASS* 7.1.7FR, money is not *client money* when a *firm* (other than a *sole trader*) holds that money on behalf of, or receives it from, a *professional client*, other than in the course of *insurance mediation activity*, and the *firm* has obtained written acknowledgement from the *professional client* that:
- (1) money will not be subject to the protections conferred by the *client money rules*;
 - (2) as a consequence, this money will not be segregated from the money of the *firm* in accordance with the *client money rules* and will be used by the *firm* in the course of its own business; and

- (3) the professional client will rank only as a general creditor of the firm.

‘Opt-outs’ for non-IMD business

- 7.1.7E G For a firm whose business is not governed by the Insurance Mediation Directive, it is possible to ‘opt out’ on a one-way basis. However, in order to maintain a comparable regime to that applying to MiFID business, all ‘MiFID type’ business undertaken outside the scope of MiFID, should comply with the client money rules or be ‘opted out’ on a two-way basis.
- 7.1.7F R Money is not client money if a firm, in respect of designated investment business which is not an investment service or activity, an ancillary service, a listed activity or insurance mediation activity:
- (1) holds it on behalf of or receives it from a professional client who is not an authorised person; and
- (2) has sent a separate written notice to the professional client stating the matters set out in CASS 7.1.7DR(1) to (3).
- 7.1.7G G When a firm undertakes a range of business for a professional client and has separate agreements for each type of business undertaken, the firm may treat client money held on behalf of the client differently for different types of business; for example, a firm may, under CASS 7.1.7DR or CASS 7.1.7FR, elect to segregate client money in connection with securities transactions and not segregate (by complying with CASS 7.1.7DR or CASS 7.1.7FR) money in connection with contingent liability investments for the same client.
- 7.1.7H R When a firm transfers client money to another person, the firm must not enter into an agreement under CASS 7.1.7DR or CASS 7.1.7FR with that other person in relation to that client money or represent to that other person that the money is not client money.
- 7.1.7I G CASS 7.1.7HR prevents a firm, when passing client money to another person under CASS 7.5.2R (transfer of client money to a third party), from making use of the ‘opt out’ provisions under CASS 7.1.7DR or CASS 7.1.7FR.

...

Credit institutions and approved banks

...

- 7.1.11A R (1) This rule applies to a firm which is an approved bank but not a BCD credit institution.

(2) The client money rules do not apply to money held by the approved bank if it is undertaking business which is not MiFID business but only when the money is held in an account with itself, in which case the firm must notify the client in writing that:

(a) money held for that client in an account with the approved bank will be held by the firm as banker and not as trustee (or in Scotland as agent); and

(b) as a result, the money will not be held in accordance with the client money rules.

...

Affiliated companies – MiFID business

7.1.12 G A firm that holds money on behalf of, or receives money from, an affiliated company in respect of MiFID business must treat the affiliated company as any other client of the firm for the purposes of this chapter.

Affiliated companies – non-MiFID business

7.1.12A R A firm that holds money on behalf of, or receives money from, an affiliated company in respect of designated investment business which is not MiFID business must not treat the money as client money unless:

(1) the firm has been notified by the affiliated company that the money belongs to a client of the affiliated company; or

(2) the affiliated company is a client dealt with at arm's length; or

(3) the affiliated company is a manager of an occupational pension scheme or is an overseas company; and

(a) the money is given to the firm in order to carry on designated investment business for or on behalf of the clients of the affiliated company; and

(b) the firm has been notified by the affiliated company that the money is to be treated as client money.

7.1.13 G ~~A firm that holds client money on behalf of, or receives money from, an affiliated company in respect of its non MiFID business and opts under CASS 7.1.3R (1) to comply with this chapter in with respect of that non-MiFID business, should refer to the non-directive client money chapter (see CASS 4.1.18 R (Affiliated companies)) to determine whether that money falls within the scope of the non-directive client money chapter and~~

therefore within the scope of the opt-in. [deleted]

...

Solicitors

- 7.1.15 R (1) An *authorised professional firm* regulated by the Law Society (of England and Wales), the Law Society of Scotland or the Law Society of Northern Ireland must comply ~~with the *MiFID client money (minimum implementing) rules* and also~~ with the following rules of its *designated professional body* and, where relevant paragraph (3), and if it does so, it will be deemed to comply with the *client money rules* ~~in this chapter~~.
- (2) The relevant rules are:
- (a) if the *firm* is regulated by the Law Society (of England and Wales):
 - (i) the Solicitors' Accounts Rules 1998; or
 - (ii) where applicable, the Solicitors Overseas Practice Rules 1990;
 - (b) if the *firm* is regulated by the Law Society of Scotland, the Solicitors' (Scotland) Accounts, Accounts Certificate, Professional Practice and Guarantee Fund Rules 2001; and
 - (c) if the *firm* is regulated by the Law Society of Northern Ireland, the Solicitors' Accounts Regulations 1998.
- (3) If the *firm* in (1) is a *MiFID investment firm* that receives or holds *money* for, or on behalf of a *client* in the course of, or in connection with its *MiFID business*, it must also comply with the *MiFID client money (minimum implementing) rules* in relation to that business.

Long term insurers and friendly societies

- 7.1.15A R This chapter does not apply to the *permitted activities of a long-term insurer* or a *friendly society*, unless it is a *MiFID investment firm* that receives *money* from or holds *money* for or on behalf of a *client* in the course of, or in connection with, its *MiFID business*.

Contracts of insurance

- 7.1.15B R This chapter does not apply to *client money* held by a *firm* which:
- (1) receives or holds *client money* in relation to *contracts of insurance*;

but which

(2) in relation to such *client money* elects to act in accordance with the *insurance client money chapter*.

7.1.15C R A firm should make and retain a written record of any election which it makes under CASS 7.1.15BR.

Life assurance business

7.1.15D G (1) A firm which receives and holds *client money* in respect of life assurance business in the course of its *designated investment business* that is not *MiFID business* may:

(a) under CASS 7.1.3R(1B) elect to comply with the *client money chapter* in respect of such *client money* and in doing so avoid the need to comply with the *insurance client money chapter* which would otherwise apply to the *firm* in respect of *client money* received in the course of its *insurance mediation activity*; or

(b) under CASS 7.1.15BR, elect to comply with the *insurance client money chapter* in respect of such *client money*.

(2) These options are available to a *firm* irrespective of whether it also receives and holds *client money* in respect of other parts of its *designated investment business*. A *firm* may not however choose to comply with the *insurance client money chapter* in respect of *client money* which it receives and holds in the course of any part of its *designated investment business* which does not involve an *insurance mediation activity*.

Trustee firms (other than trustees of unit trust schemes)

7.1.15E R A trustee firm which holds *money* in relation to its *designated investment business* which is not *MiFID business* to which this chapter applies, must hold any such *client money* separate from its own *money* at all times.

7.1.15F R Only the *client money rules* listed in the table below apply to a *trustee firm* in connection with *money* that the firm receives, or holds for or on behalf of a client in the course of or in connection with its *designated investment business* which is not *MiFID business*.

<u>Reference</u>	<u>Rule</u>
<u>CASS 7.1.1R to CASS 7.1.6G, and CASS 7.1.8R to CASS 7.1.14R</u>	<u>Application</u>

<u>CASS 7.1.15ER and CASS 7.1.15FR</u>	<u>Trustee firms (other than trustees of unit trust schemes)</u>
<u>CASS 7.1.16G</u>	<u>General principle</u>
<u>CASS 7.7.2R to CASS 7.7.4G</u>	<u>Requirement</u>
<u>CASS 7.4.1R to CASS 7.4.6G</u>	<u>Depositing client money</u>
<u>CASS 7.4.7R to CASS 7.4.13G</u>	<u>A firm's selection of credit institution, bank or money market fund</u>
<u>CASS 7.6.6G to CASS 7.6.16R</u>	<u>Reconciliation of client money balances</u>

General purpose

7.1.16 G (1) ...

(2) The *client money rules* also where relevant implement the provisions of *MiFID* which regulate the obligations of a *firm* when it holds *client money* in the course of its *MiFID* business.

7.2 Definition of client money

7.2.1 R ~~For the purposes of this chapter and the *MiFID* custody chapter, *client money* means any *money* that a *firm* receives from or holds for, or on behalf of, a *client* in the course of, or in connection with, its *MiFID* business unless otherwise specified in this section. [deleted]~~

~~Business in the name of the firm~~

7.2.2 R ~~*Money* is not *client money* where the *firm* carries on business in its own name on behalf of the *client* where that is required by the very nature of the transaction and the *client* is in agreement. [deleted]~~

~~[Note: recital 26 to *MiFID*]~~

...

7.2.8A G The exclusion from the *client money rules* for delivery versus payment transactions under CASS 7.2.8R is an example of an exclusion from the *client money rules* which is permissible by virtue of recital 26 of *MiFID*.

- 7.2.8B **R** Money need not be treated as *client money* in respect of a delivery versus payment transaction, for the purpose of settling a transaction in relation to units in a regulated collective investment scheme, if:
- (1) the authorised fund manager receives it from a *client* in relation to the authorised fund manager’s obligation to issue units, in an AUT or to arrange for the issue of units in an ICVC, in accordance with COLL, unless the price of those units has not been determined by the close of business on the next business day:
- (a) following the date of the receipt of the money from the client; or
- (b) if the money was received by an appointed representative of the authorised fund manager, in accordance with CASS 7.4.24G, following the date of receipt at the specified business address of the authorised fund manager; or
- (2) the money is held in the course of redeeming units where the proceeds of that redemption are paid to a client within the time specified in COLL; when an authorised fund manager draws a cheque or other payable order within these timeframes the provisions of CASS 7.2.17R and CASS 7.2.9R(2) will not apply.

...

Qualifying money market funds

- 7.4.3 **G** Where a firm deposits *client money* with a *qualifying money market fund*, the units in that fund should be held in accordance with ~~the MiFID custody chapter~~ CASS 6.

[Note: recital 23 to the *MiFID implementing Directive*]

...

Payment of client money into a client bank account

- 7.4.14 **G** Two approaches that a firm can adopt in discharging its obligations under the ~~MiFID~~ *client money segregation requirements* are:

(1) ...

(2) ...

...

- 7.4.18 **G** Under the alternative approach, a firm that receives *client money* should:

(1)

(a) ...

(b) perform a reconciliation of records and accounts required under CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1R and SYSC 6.1.1R, adjust the balance held in its *client bank accounts* and then segregate the *money* in the *client bank account* until the calculation is re-performed on the next *business day*; or

...

...

7.4.20 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* should ensure that any *money* other than *client money* deposited in a *client bank account* is promptly paid out of that account unless it is a minimum sum required to open the account, or to keep it open.

...

Automated transfers

7.4.22 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach that receives *client money* in the form of an automated transfer should take reasonable steps to ensure that:

...

Mixed remittance

7.4.23 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach that receives a *mixed remittance* (that is part *client money* and part other *money*) should:

...

Appointed representatives, tied agents, field representatives and other agents

7.4.24 G (1) Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach should establish and maintain procedures to ensure that *client money* received by its *appointed representatives, tied agents, field representatives* or other agents is:

...

...

...

Client entitlements

- 7.4.27 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach that receives outside the *United Kingdom* a *client* entitlement on behalf of a *client* should pay any part of it which is *client money*:

...

- 7.4.28 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach should allocate a *client* entitlement that is *client money* to the individual *client* promptly and, in any case, no later than ten *business days* after notification of receipt.

Money due to a client from a firm

- 7.4.29 G Pursuant to the ~~MiFID~~ *client money segregation requirements*, a *firm* operating the normal approach that is liable to pay *money* to a *client* should promptly, and in any event no later than one *business day* after the *money* is due and payable, pay the *money*:

...

...

- 7.4.33 G A *firm* with a *Part 30 exemption order* undertakes to the *CFTC* that it will refuse to allow any US customer to opt not to have his *money* treated as *client money* if it is held or received in respect of transactions on non-US exchanges, unless that US customer is an “eligible contract participant” as defined in section 1a(12) of the Commodity Exchange Act, 7 U.S.C. In doing so, the *firm* is representing that if available to it, it will not make use of the opt-out arrangements in CASS 7.1.7BR to CASS 7.1.7FR in relation to that business. The ~~MiFID client money chapter does not have the option of allowing the *firm* or the *client* to choose whether *money* belonging to the *client* is subject to the *client money* rules.~~

...

Client entitlements

- 7.6.3 G Pursuant to CASS 7.6.2R, and where relevant SYSC 4.1.1R and SYSC 6.1.1R, a *firm* should take reasonable steps to ensure that is notified promptly of any receipt of *client money* in the form of a *client* entitlement.

...

Internal reconciliations of client money balances

- 7.6.6 G (1) ~~SYSC 4.1.1R requires firms to have robust governance arrangements, such as internal control mechanisms, including sound administrative and accounting procedures and effective control and safeguard arrangements for information processing systems. In addition, SYSC 6.1.1R requires firms to establish, implement and maintain adequate policies and procedures sufficient to ensure the firm's compliance with its obligations under the regulatory system.~~ Carrying out internal reconciliations of records and accounts of the entitlement of each *client* for whom the *firm* holds *client money* with the records and accounts of the *client money* the *firm* holds in *client bank accounts* and *client transaction accounts* should be one of the steps a *firm* takes to satisfy its obligations under CASS 7.6.2R, and where relevant SYSC 4.1.1R and SYSC 6.1.1R.

...

Records

- 7.6.7 R (1) A *firm* must makes records ... to show and explain that:
- (a) ...
- (b) in the event of a *primary pooling event* or a *secondary pooling event*, the method used is adequate to enable the *firm* to comply with the *client money (MiFID business) distribution rules*.

...

...

Requirement

- 7.7.2 R A *firm* receives and holds *client money* as trustee (or in Scotland as agent) on the following terms:
- (1) for the purposes of and on the terms of the *client money rules* and the *client money (MiFID business) distribution rules*;

...

- 7.7.3 R A trustee firm which is subject to the client money rules by virtue of CASS 7.1.1R(4):

- (1) must receive and hold client money in accordance with the relevant

instrument of trust;

(2) subject to that, receives and holds *client money on trust on the terms* (or in Scotland on the agency terms) specified in CASS 7.7.2R.

7.7.4 G If a trustee firm holds *client money* in accordance with CASS 7.7.3R(2), the firm should follow the provisions in CASS 7.1.15ER and CASS 7.1.15FR.

...

Section 7.9 (Client money and distribution) is deleted in its entirety. The text of the deleted section is not shown.

7 Annex 1 Annex 1G

As explained in CASS 7.6.6G, in complying with its obligations under CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1G (General organisational requirements) and SYSC 6.1.1R (Compliance), a *firm* should carry out internal reconciliations of records and accounts of *client money* the *firm* holds in *client bank accounts* and *client transaction accounts*. This Annex sets out a method of reconciliation that the *FSA* believes is appropriate for these purposes (the *standard method of internal client money reconciliation*).

...

10. Segregation in the context of paragraph 9 can take many forms, including the holding of a *safe custody investment* in a nominee name and the safekeeping of certificates evidencing title in a fire resistant safe. It is not the intention that all the *custody rules* in the ~~*MiFID*~~ *custody chapter* should be applied to *designated investments* held in the course of settlement.

Insert the following new chapter after CASS 7. The text is not underlined.

7A. Client money distribution

7A.1 Application and purpose

Application

- 7A.1.1 R This chapter (the *client money distribution rules*) applies to a *firm* that holds *client money* which is subject to the *client money rules* when a *primary pooling event* or a *secondary pooling event* occurs.

Purpose

- 7A.1.2 G The *client money distribution rules* seek to facilitate the timely return of *client money* to a *client* in the event of the *failure* of a *firm* or third party at which the *firm* holds *client money*.

7A.2 Primary pooling events

Failure of the authorised firm: primary pooling event

- 7A.2.1 G (1) *A firm can hold client money in a general client bank account, a designated client bank account or a designated client fund account.*
- (2) *A firm holds all client money in general client bank accounts for its clients as part of a common pool of money so those particular clients do not have a claim against a specific sum in a specific account; they only have a claim to the client money in general.*
- (3) *A firm holds client money in designated client bank accounts or designated client fund accounts for those clients that requested their client money be part of a specific pool of money, so those particular clients do have a claim against a specific sum in a specific account; they do not have a claim to the client money in general unless a primary pooling event occurs. A primary pooling event triggers a notional pooling of all the client money, in every type of client money account, and the obligation to distribute it.*
- (4) *If the firm becomes insolvent, and there is (for whatever reason) a shortfall in money held for a client compared with that client's entitlements, the available funds will be distributed in accordance with the client money distribution rules.*
- 7A.2.2 R *A primary pooling event occurs:*
- (1) *on the failure of the firm;*
- (2) *on the vesting of assets in a trustee in accordance with an 'assets requirement' imposed under section 48(1)(b) of the Act;*
- (3) *on the coming into force of a requirement for all client money held by the firm; or*
- (4) *when the firm notifies, or is in breach of its duty to notify, the FSA, in accordance with CASS 7.6.16R (Notification requirements), that it is unable correctly to identify and allocate in its records all valid claims arising as a result of a secondary pooling event.*
- 7A.2.3 R *CASS 7A.2.2R(4) does not apply so long as:*
- (1) *the firm is taking steps, in consultation with the FSA, to establish those records; and*
- (2) *there are reasonable grounds to conclude that the records will be*

capable of rectification within a reasonable period.

Pooling and distribution

- 7A.2.4 R If a *primary pooling event* occurs:
- (1) *client money* held in each *client money* account of the *firm* is treated as pooled; and
 - (2) the *firm* must distribute that *client money* in accordance with CASS 7.7.2R, so that each *client* receives a sum which is rateable to the *client money* entitlement calculated in accordance with CASS 7A.2.5R.
- 7A.2.5 R (1) When, in respect of a *client*, there is a positive individual *client* balance and a negative *client equity balance*, the credit must be offset against the debit reducing the individual *client* balance for that *client*.
- (2) When, in respect of a *client*, there is a negative individual *client* balance and a positive *client equity balance*, the credit must be offset against the debit reducing *client equity balance* for that *client*.
- 7A.2.6 G A *client's* main claim is for the return of *client money* held in a *client bank account*. A *client* may be able to claim for any *shortfall* against *money* held in a *firm's* own account. For that claim, the *client* will be an unsecured creditor of the *firm*.

Client money received after the failure of the firm

- 7A.2.7 R *Client money* received by the *firm* after a *primary pooling event* must not be pooled with *client money* held in any *client money* account operated by the *firm* at the time of the *primary pooling event*. It must be placed in a *client bank account* that has been opened after that event and must be handled in accordance with the *client money rules*, and returned to the relevant *client* without delay, except to the extent that:
- (1) it is *client money* relating to a transaction that has not settled at the time of the *primary pooling event*; or
 - (2) it is *client money* relating to a *client*, for whom the *client money* entitlement, calculated in accordance with CASS 7A.2.5R, shows that *money* is due from the *client* to the *firm* at the time of the *primary pooling event*.
- 7A.2.8 G *Client money* received after the *primary pooling event* relating to an unsettled transaction should be used to settle that transaction. Examples of such transactions include:

- (1) an equity transaction with a trade date before the date of the *primary pooling event* and a settlement date after the date of the *primary pooling event*; or
 - (2) a *contingent liability investment* that is ‘open’ at the time of the *primary pooling event* and is due to settle after the *primary pooling event*.
- 7A.2.9 R If a *firm* receives a *mixed remittance* after a *primary pooling event*, it must:
- (1) pay the full sum into the separate *client bank account* opened in accordance with CASS 7A.2.7R; and
 - (2) pay the *money* that is not *client money* out of that *client bank account* into a *firm’s* own bank account within one *business day* of the *day* on which the *firm* would normally expect the remittance to be cleared.
- 7A.2.10 G Whenever possible the *firm* should seek to split a *mixed remittance* before the relevant accounts are credited.
- 7A.2.11 R If both a *primary pooling event* and a *secondary pooling event* occur, the provisions of this section relating to a *primary pooling event* apply.

7A.3 Secondary pooling events

Failure of a bank, intermediate broker, settlement agent or OTC counterparty:
secondary pooling events

- 7A.3.1 R A *secondary pooling event* occurs on the *failure* of a third party to which *client money* held by the *firm* has been transferred under CASS 7.4.1R(1) to CASS 7.4.1R(3) (Depositing client money) or CASS 7.5.2R (Transfer of client money to a third party).
- 7A.3.2 R CASS 7A.3.6R to CASS 7A.3.18R do not apply if, on the *failure* of the third party, the *firm* repays to its *clients* or pays into a *client bank account*, at an unaffected bank, an amount equal to the amount of *client money* which would have been held if a *shortfall* had not occurred at that third party.
- 7A.3.3 G When *client money* is transferred to a third party, a *firm* continues to owe fiduciary duties to the *client*. Whether a *firm* is liable for a *shortfall* in *client money* caused by a third party failure will depend on whether it has complied with its duty of care as agent or trustee.

Failure of a bank

- 7A.3.4 G When a bank *fails* and the *firm* decides not to make good the *shortfall* in the amount of *client money* held at that bank, a *secondary pooling event* will occur in accordance with CASS 7A.3.6R. The *firm* would be expected to reflect the *shortfall* that arises at the *failed* bank in its records of the entitlement of *clients* and of *money* held with third parties.
- 7A.3.5 G The *client money distribution rules* seek to ensure that *clients* who have previously specified that they are not willing to accept the risk of the bank that has *failed*, and who therefore requested that their *client money* be placed in a *designated client bank account* at a different bank, should not suffer the loss of the bank that has *failed*.

Failure of a bank: pooling

- 7A.3.6 R If a *secondary pooling event* occurs as a result of the *failure* of a bank where one or more *general client bank accounts* are held, then:
- (1) in relation to every *general client bank account* of the *firm*, the provisions of CASS 7A.3.8R, CASS 7A.3.13R and CASS 7A.3.14R will apply;
 - (2) in relation to every *designated client bank account* held by the *firm* with the *failed* bank, the provisions of CASS 7A.3.10R, CASS 7A.3.13R and CASS 7A.3.14R will apply;
 - (3) in relation to each *designated client fund account* held by the *firm* with the *failed* bank, the provisions of CASS 7A.3.11R, CASS 7A.3.13R and CASS 7A.3.14R will apply;
 - (4) any *money* held at a bank, other than the bank that has *failed*, in *designated client bank accounts*, is not pooled with any other *client money*; and
 - (5) any *money* held in a *designated client fund account*, no part of which is held by the bank that has *failed*, is not pooled with any other *client money*.
- 7A.3.7 R If a *secondary pooling event* occurs as a result of the *failure* of a bank where one or more *designated client bank accounts* or *designated client fund accounts* are held, then:
- (1) in relation to every *designated client bank account* held by the *firm* with the *failed* bank, the provisions of CASS 7A.3.10R, CASS 7A.3.13R and CASS 7A.3.14R will apply; and
 - (2) in relation to each *designated client fund account* held by the *firm* with the *failed* bank, the provisions of CASS 7A.3.11R, CASS

7A.3.13R and CASS 7A.3.14R will apply.

- 7A.3.8 R *Money held in each general client bank account and client transaction account of the firm must be treated as pooled and:*
- (1) any *shortfall* in *client money* held, or which should have been held, in *general client bank accounts* and *client transaction accounts*, that has arisen as a result of the *failure* of the bank, must be borne by all the *clients* whose *client money* is held in either a *general client bank account* or *client transaction account* of the *firm*, rateably in accordance with their entitlements;
 - (2) a new *client money* entitlement must be calculated for each *client* by the *firm*, to reflect the requirements in (1), and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
 - (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* bank until the *client* is repaid; and
 - (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), for the purposes of reconciliations pursuant to CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1R (General organisational requirements) and SYSC 6.1.1R (Compliance).
- 7A.3.9 G The term “which should have been held” is a reference to the *failed* bank’s *failure* to hold the *client money* at the time of the pooling event.
- 7A.3.10 R For each *client* with a *designated client bank account* held at the *failed* bank:
- (1) any *shortfall* in *client money* held, or which should have been held, in *designated client bank accounts* that has arisen as a result of the *failure*, must be borne by all the *clients* whose *client money* is held in a *designated client bank account* of the *firm* at the *failed* bank, rateably in accordance with their entitlements;
 - (2) a new *client money* entitlement must be calculated for each of the relevant *clients* by the *firm*, and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
 - (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* bank until the *client* is repaid; and
 - (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), for the purposes of reconciliations pursuant to CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1R (General organisational requirements) and SYSC 6.1.1R

(Compliance).

- 7A.3.11 R *Money held in each designated client fund account with the failed bank must be treated as pooled with any other designated client fund accounts of the firm which contain part of the same designated fund and:*
- (1) any *shortfall* in *client money* held, or which should have been held, in *designated client fund accounts* that has arisen as a result of the *failure*, must be borne by each of the *clients* whose *client money* is held in that designated fund, rateably in accordance with their entitlements;
 - (2) a new *client money* entitlement must be calculated for each *client* by the *firm*, in accordance with (1), and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
 - (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed* bank until the *client* is repaid; and
 - (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), for the purposes of reconciliations pursuant to CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1R (General organisational requirements) and SYSC 6.1.1R (Compliance).
- 7A.3.12 R *A client whose money was held, or which should have been held, in a designated client bank account with a bank that has failed is not entitled to claim in respect of that money against any other client bank account or client transaction account of the firm.*

Client money received after the failure of a bank

- 7A.3.13 R *Client money received by the firm after the failure of a bank, that would otherwise have been paid into a client bank account at that bank:*
- (1) must not be transferred to the *failed* bank unless specifically instructed by the *client* in order to settle an obligation of that *client* to the *failed* bank; and
 - (2) must be, subject to (1), placed in a separate *client bank account* that has been opened after the *secondary pooling event* and either:
 - (a) on the written instruction of the *client*, transferred to a bank other than the one that has *failed*; or
 - (b) returned to the *client* as soon as possible.
- 7A.3.14 R *If a firm receives a mixed remittance after the secondary pooling event*

which consists of *client money* that would have been paid into a *general client bank account*, a *designated client bank account* or a *designated client fund account* maintained at the bank that has *failed*, it must:

- (1) pay the full sum into a *client bank account* other than one operated at the bank that has *failed*; and
- (2) pay the *money* that is not *client money* out of that *client bank account* within one *business day* of the day on which the *firm* would normally expect the remittance to be cleared.

7A.3.15 G Whenever possible the *firm* should seek to split a *mixed remittance* before the relevant accounts are credited.

Failure of an intermediate broker, settlement agent or OTC counterparty: Pooling

7A.3.16 R If a *secondary pooling event* occurs as a result of the *failure* of an *intermediate broker*, *settlement agent* or *OTC counterparty*, then in relation to every *general client bank account* and *client transaction account* of the *firm*, the provisions of CASS 7A.3.17R and CASS 7A.3.18R will apply.

7A.3.17 R *Money* held in each *general client bank account* and *client transaction account* of the *firm* must be treated as pooled and:

- (1) any *shortfall* in *client money* held, or which should have been held, in *general client bank accounts* and *client transaction accounts*, that has arisen as a result of the *failure*, must be borne by all the *clients* whose *client money* is held in either a *general client bank account* or a *client transaction account* of the *firm*, rateably in accordance with their entitlements;
- (2) a new *client money* entitlement must be calculated for each *client* by the *firm*, to reflect the requirements of (1), and the *firm's* records must be amended to reflect the reduced *client money* entitlement;
- (3) the *firm* must make and retain a record of each *client's* share of the *client money shortfall* at the *failed intermediate broker*, *settlement agent* or *OTC counterparty* until the *client* is repaid; and
- (4) the *firm* must use the new *client money* entitlements, calculated in accordance with (2), for the purposes of reconciliations pursuant to CASS 7.6.2R (Records and accounts), and where relevant SYSC 4.1.1R (General organisational requirements) and SYSC 6.1.1R (Compliance) .

Client money received after the failure of an intermediate broker, settlement agent or OTC counterparty

- 7A.3.18 R *Client money* received by the *firm* after the *failure* of an *intermediate broker, settlement agent* or *OTC* counterparty, that would otherwise have been paid into a *client transaction account* at that *intermediate broker, settlement agent* or *OTC* counterparty:
- (1) must not be transferred to the *failed* third party unless specifically instructed by the *client* in order to settle an obligation of that *client* to the *failed intermediate broker, settlement agent* or *OTC* counterparty; and
 - (2) must be, subject to (1), placed in a separate *client bank account* that has been opened after the *secondary pooling event* and either:
 - (a) on the written instruction of the *client*, transferred to a third party other than the one that has *failed*; or
 - (b) returned to the *client* as soon as possible.

Notification to the FSA: failure of a bank, intermediate broker, settlement agent or OTC counterparty

- 7A.3.19 R On the *failure* of a third party with which *money* is held, a *firm* must notify the *FSA*:
- (1) as soon as it becomes aware of the *failure* of any bank, *intermediate broker, settlement agent, OTC* counterparty or other entity with which it has placed, or to which it has passed, *client money*; and
 - (2) as soon as reasonably practical, whether it intends to make good any *shortfall* that has arisen or may arise and of the amounts involved.

...

Sch 1 Record keeping requirements

Sch 1.1 G The aim of the guidance in the following table is to give the reader a quick overall view of the relevant record keeping requirements.

Sch 1.2 G It is not a complete statement of those requirements and should not be relied on as if it were.

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
€ASS	A personal	Client details and		3 years

2.1.9R	investment firm that temporarily holds a client's designated investments	any actions taken by the firm		(from the making of the record) [deleted]
CASS 2.3.6 R(1)(e)	Safe custody arrangements for clients ordinarily outside the United Kingdom	The steps taken and result under CASS 2.3.6 R(1)(e)	On determination that client does not wish to execute agreement	3 years [deleted]
CASS 2.6.15R	Client custody assets held or received by or on behalf of a client or which the firm has arranged for another to hold or receive	Full details	On receipt	3 years [deleted]
CASS 2.6.16R	Safe custody investments used for stock lending activities	The identity of safe custody investments available to be lent, and those which have been lent	On receipt	3 years [deleted]
CASS 4.3.11R	Client money	Sufficient records to show and explain firm's transactions and commitments	Maintain current full details	3 years (after records made) [deleted]
CASS 4.4.24R(3)	Client money shortfall	Each client's entitlement to client money shortfall at the failed bank	Maintain up to date records	Until client repaid [deleted]
CASS	Client money	Each client's entitlement to	Maintain up to date	Until client repaid

4.4.25R(3)	shortfall	client money shortfall at the failed intermediate broker, settlement agent or OTC counterparty	records	[deleted]
CASS 4.4.31R(3)	Client money shortfall	Each client's entitlement to client money shortfall at the failed intermediate broker, settlement agent or OTC counterparty	Maintain up to date records	Until client repaid [deleted]
CASS 5.1.1R(4)	Record of election of compliance with CASS 5.8 to CASS 5.8 provisions with <u>specified CASS rules</u>	Record of compliance with CASS 5.8 to CASS 5.8 provisions on <u>client money specified CASS rules</u>	Not specified	Not specified
CASS 5.2.3R(2)	Holding <i>client money</i> as agent	The terms of the agreement	Not specified	Six years
CASS 5.4.4R(2)	Adequacy of systems and controls	Written confirmation of adequate systems and controls from its auditor	Not specified	Not specified
CASS 5.5.84R	<i>Client money</i> calculation	Whether the <i>firm</i> calculates its <i>client money</i> requirements according to CASS 5.5.84 R or CASS 5.5.84 R	Not specified	Not specified
CASS 5.5.84R	Transactions and commitments for <i>client</i>	Explanation of the <i>firm's</i> transactions and commitments for	Not specified	Three years

	<i>money</i>	<i>client money</i>		
CASS 5.8.3R(1)	Client's title to a <i>contract of insurance</i>	Identity of such <i>documents</i> and/or property and dates received and delivered to <i>client</i>	Not specified	Three years
<u>CASS 6.1.16CR(3)</u>	<u>A personal investment firm that temporarily holds a client's designated investments which is not in the course of MiFID business</u>	<u>Client details and any actions taken by the firm</u>		<u>5 years (from the making of the record)</u>
<u>CASS 6.1.16KR</u>	<u>Client custody assets which the firm has arranged for another to hold or receive</u>	<u>Full details</u>	<u>On receipt</u>	<u>5 years</u>
CASS 6.1.17R	Record of election to comply with the <i>MiFID custody chapter</i>	Record of election to comply with the <i>MiFID custody chapter</i> , including the date from which the election is to be effective	Date of the election	5 years (from the date the <i>firm</i> ceases to use the election) [deleted]
CASS 6.3.1R(4)	Appropriateness of a <i>MiFID investment firm's</i> selection of a third party	Grounds upon which a <i>MiFID investment firm</i> satisfies itself as to the appropriateness of the <i>firm's</i> selection of a third party to hold <i>financial</i>	Date of the selection	5 years (from the date the <i>firm</i> ceases to use the third party to hold <i>financial instrument s-safe</i>)

		instruments -safe <u>custody assets</u> belonging to <i>clients</i>		<u>custody</u> <u>assets</u> belonging to <i>clients</i>)
CASS 6.4.3R	Details of <i>clients</i> and financial instruments <u>safe custody assets</u> used for the <i>firm's</i> own account or the account of another <i>client</i> of the <i>firm</i>	Details of the <i>client</i> on whose instructions the use of the financial instruments <u>safe custody assets</u> has been effected and the number of financial instruments <u>safe custody assets</u> used belonging to each <i>client</i>	Maintain up to date records	5 years (from the date the record was made)
CASS 6.5.1R	Financial instruments <u>Safe custody assets</u> held for each <i>client</i> and the <i>firm's</i> own financial instruments <u>applicable assets</u>	All that is necessary to enable the <i>firm</i> to distinguish financial instruments <u>safe custody assets</u> held for one <i>client</i> from financial instruments <u>safe custody assets</u> held for any other <i>client</i> , and from the <i>firm's</i> own financial instruments <u>applicable assets</u>	Maintain up to date records	5 years (from the date the record was made)
CASS 6.5.2R	Financial instruments <u>Safe custody assets</u> held for <i>clients</i>	Accurate records to which ensure the their correspondence between to the financial instruments <u>safe custody assets</u> held for <u>clients</u> each client and	Maintain up to date records	5 years (from the date the record was made)

		the financial instruments held by the firm and third parties		
CASS 7.1.3R(32)	Record of election to comply with the <i>MiFID</i> client money chapter	Record of election to comply with the <i>MiFID</i> client money chapter, including the date from which the election is to be effective	Date of the election	5 years (from the date the firm ceases to use the election)
<u>CASS 7.1.15CR</u>	<u>Record of election in relation to CASS 7.1.15CR</u>	<u>Record of election in relation to CASS 7.1.15CR</u>	<u>Date of election</u>	<u>Not specified</u>
CASS 7.4.10R	Appropriateness of a <i>MiFID</i> investment firm's selection of a third party	Grounds upon which a <i>MiFID</i> investment firm satisfies itself as to the appropriateness of the firm's selection of a third party to hold client money	Date of the selection	5 years (from the firm ceases to use the third party to hold client money)
CASS 7.6.1R	Client money held for each client and the firm's own money	All that is necessary to enable the firm to distinguish client money held for one client from client money held for any other client, and from the firm's own money	Maintain up to date records	5 years (from the date the record was made)
CASS 7.6.2R	Client money held for each client	Accurate records to ensure the correspondence between the records and	Maintain up to date records	5 years (from the date the record was made)

		accounts of the entitlement of each <i>client</i> for whom the <i>firm</i> holds <i>client money</i> with the records and accounts of the <i>client money</i> the <i>firm</i> holds in <i>client bank accounts</i> and <i>client transaction accounts</i>		
CASS 7.6.7R	Internal reconciliation of <i>client money</i> balances	Explanation of method of internal reconciliation of <i>client money</i> balances used by the <i>firm</i> , and if different from the <i>standard method of internal client money reconciliation</i> , an explanation as to how the method used affords equivalent degree of protection to <i>clients</i> , and how it enables the <i>firm</i> to comply with the <i>client money (MiFID business) distribution rules</i>	Date the <i>firm</i> starts using the method	5 years (from the date the <i>firm</i> ceases to use the method)
CASS 7.9.21R(3) 7A.3.8R(3)	<i>Client money shortfall</i>	Each <i>client's</i> entitlement to <i>client money shortfall</i> at the failed bank	Maintain up to date records	Until <i>client</i> is repaid
CASS 7.9.23R(3) 7A.3.10R(3)	<i>Client money shortfall</i>	Each <i>client's</i> entitlement to <i>client money</i>	Maintain up to date records	Until <i>client</i> is repaid

		<i>shortfall</i> at the failed bank		
CASS 7.9.24R(3) <u>7A.3.11R(3)</u>	<i>Client money shortfall</i>	Each <i>client's</i> entitlement to <i>client money shortfall</i> at the failed bank	Maintain up to date records	Until <i>client</i> is repaid
CASS 7.9.30R(3) <u>7A.3.17R(3)</u>	<i>Client money shortfall</i>	Each <i>client's</i> entitlement to <i>client money shortfall</i> at the failed intermediate broker, <i>settlement agent</i> or OTC counterparty	Maintain up to date records	Until <i>client</i> is repaid
CASS 8.1.5R	Adequate records and internal controls in respect of the <i>firm's</i> use of mandates (see CASS 8.1.5R(1) to CASS 8.1.5R(4))	Up to date list of <i>firm's</i> authorities and any conditions regarding the use of authorities, all transactions entered into, details of procedures and authorities for giving and receiving of instructions under authorities, and important <i>client</i> documents held by the <i>firm</i>	Maintain current full details	Not specified

Sch 2 Notification requirements

Sch 2.1 G	Handbook reference	Matter to be notified	Contents of notification	Trigger event	Time allowed
	CASS 2.6.14R(1)	Non-compliance with reconciliation requirements in CASS 2.6.2R, CASS 2.6.4R, CASS	Reason for Non-compliance	Non-compliance	Immediately [deleted]

	2.6.6R, CASS 2.6.8R, CASS 2.6.10R			
CASS 2.6.14R(2)	Non-compliance of reconciliation requirements in CASS 2.6.11 R	Reason for Non-compliance once reconciliation carried out	Non-compliance	Immediately [deleted]
CASS 4.3.64R	Failure of a third party with which money is held—ie: bank, intermediate broker, settlement agent or OTC counterparty or other entity with which it has placed or to which it has passed client money	Full details	When firm becomes aware of the failure of the entity	Immediately [deleted]
CASS 4.3.64R	Failure of a third party with which money is held—ie: bank, intermediate broker, settlement agent or OTC counterparty or other entity with which it has placed or to which it has passed client money	Intentions regarding making good any shortfall that has arisen or may arise, and of the amounts involved	Failure of third party with which money is held	As soon as reasonably practical [deleted]
CASS 4.3.87R	Daily calculation required by CASS 4.3.66R or CASS 4.3.6R	Inability to perform daily calculation	Inability to perform daily calculation	Immediately [deleted]
CASS 4.3.88R	Daily calculation required by CASS 4.3.66R or CASS 4.3.67R	Inability to make good any shortfall identified by daily calculation	Inability to make good any shortfall identified by close of business on the day of	Immediately [deleted]

			calculation	
CASS 4.3.97R	Requirements detailed in CASS 4.3.89R, CASS 4.3.91R, CASS 4.3.92R, CASS 4.3.94R and CASS 4.3.95R.	Inability to comply with any of the requirements	Inability to comply with any of the requirements	As soon as possible [deleted]
CASS 4.3.110R	LME bond arrangements	Issue of an individual letter of credit issued by the firm	Upon issue of an individual letter of credit under an LME bond arrangement	Immediately [deleted]
CASS 4.4.33R (see CASS 4.3.64R)	Failure of a third party with which money is held – i.e. bank, intermediate broker, settlement agent or OTC counterparty or other entity with which it has placed or to which it has passed client money	Full details	When the firm becomes aware of the failure of the entity	Immediately [deleted]
CASS 4.4.33R (see CASS 4.3.64R)	Failure of a third party with which money is held – i.e. bank, intermediate broker, settlement agent or OTC counterparty	Intentions regarding making good any shortfall that has arisen or may arise, and of the amounts involved	Upon first delegation of regulated activity	As soon as reasonably practical [deleted]
CASS 5.5.84R	Failure of <i>bank, broker or settlement agent</i>	Full details including whether it intends to make good any <i>shortfall</i> that may	As soon as the <i>firm</i> becomes aware	Immediately

		have arisen in the amounts involved		
CASS 5.5.84R	Inability to perform the calculation required by CASS 5.5.84R	Inability to perform the calculation	Inability to perform the calculation	Immediately
CASS 5.5.84R	Inability to make good any <i>shortfall</i> identified by CASS 5.5.84R	Inability to make good any <i>shortfall</i> in <i>client money</i>	Inability to make good any <i>shortfall</i>	Immediately
CASS 5.5.84R	Inability to comply with the requirements in CASS 5.5.84R; CASS 5.5.84R; CASS 5.5.84R; CASS 5.5.84R	Inability to comply with the requirements of the <i>rules</i> listed	Inability to comply with the requirements of the <i>rules</i> listed	As soon as reasonably practicable
CASS 6.5.13R(1)	Non-compliance or inability, in any material respect, to comply with the requirements in CASS 6.5.1R (Records and accounts), CASS 6.5.2R (Records and accounts, including internal reconciliations) or CASS 6.5.6R (Reconciliations with external records)	The fact that the <i>firm</i> has not complied or is unable, in any material respect, to comply with the requirements and the reasons for that	Non-compliance or inability, in any material respect, to comply with the requirements	Without delay
CASS 6.5.13R(2)	Non-compliance or inability, in any material respect, to comply with the requirements in CASS 6.5.10R (Reconciliation	The fact that the <i>firm</i> has not complied or is unable, in any material respect, to	Non-compliance or inability, in any material respect, to comply with	Without delay

	discrepancies)	comply with the requirements and the reasons for that	the requirements	
<u>CASS 7.4.35R</u>	<u>LME bond arrangements</u>	<u>Issue of an individual letter of credit issued by the <i>firm</i></u>	<u>Upon issue of an individual letter of credit under an LME bond arrangement</u>	<u>Immediately</u>
CASS 7.6.16R(1)	Non-compliance or inability, in any material respect, to comply with the requirements in CASS 7.6.1R (Records and accounts), CASS 7.6.2R (Records and accounts, including internal reconciliations) or CASS 7.6.9R (Reconciliations with external records)	The fact that the <i>firm</i> has not complied or is unable, in any material respect, to comply with the requirements and the reasons for that	Non-compliance or inability, in any material respect, to comply with the requirements	Without delay
CASS 7.6.16R(2)	Non-compliance or inability, in any material respect, to comply with the requirements in CASS 7.6.13R to CASS 7.6.15R (Reconciliation discrepancies)	The fact that the <i>firm</i> has not complied or is unable, in any material respect, to comply with the requirements and the reasons for that	Non-compliance or inability, in any material respect, to comply with the requirements	Without delay
CASS	Failure of a third party with which	Full details	<i>Firm</i> becomes	As soon as the <i>firm</i>

<p>7.9.32R(1) <u>7A.3.19R(1)</u></p>	<p>money is held - i.e.: bank, <i>intermediate broker, settlement agent</i> or OTC counterparty or other entity with which it has placed or to which it has passed <i>client money</i></p>		<p>aware of the <i>failure</i> of the entity</p>	<p>becomes aware</p>
<p>CASS 7.9.32R(2) <u>7A.3.19R(2)</u></p>	<p><i>Failure</i> of a third party with which money is held - i.e.: bank, <i>intermediate broker, settlement agent</i> or OTC counterparty or other entity with which it has placed or to which it has passed <i>client money</i></p>	<p>Intentions regarding making good any <i>shortfall</i> that has arisen or may arise, and of the amounts involved</p>	<p><i>Failure</i> of third party with which <i>client money</i> is held</p>	<p>As soon as reasonably practical</p>

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