

The End for Termination Clauses?

A Court of Appeal judgment in *Towergate Stafford Knight Company (now Folgate London Market) v Chaucer Insurance* has upheld a High Court decision that it is not possible for a broker to enforce a termination clause if the insured goes out of business.

The decision is based upon the common law anti-deprivation principle, which prevents parties from depriving their creditors of the benefits of their assets should they become insolvent. In this case, the insured (Milbank Trucks) had an insurance policy with Chaucer Insurance, arranged through a broker (Towergate).

Milbank were sued in 2005, as a result of a road traffic accident, and following some complications in the case, Towergate signed an agreement to honour the policy, but before payment was made, Milbank became insolvent. Towergate subsequently refused payment, as the agreement contained a termination clause that would release Towergate from its obligation if Milbank became insolvent before any payment was made.

Milbank's administrators assigned Milbank's rights under the agreement with Towergate to Chaucer Insurance, (hence the appearance of their name in the case) who successfully claimed the termination clause was invalid, under the anti-deprivation principle.

Paul Cox, an insurance expert at Browne Jacobson who acted for Chaucer, commented: "This judgment demonstrates the ongoing relevance of the anti deprivation principle and the profound effects that this can have on commercial contracts."

Insurance Brokers hit by PPI Fallout

The British Insurance Brokers Association (BIBA) is demanding revision of the Financial Services Compensation Scheme (FSCS).

The Scheme provides funding to pay compensation to customers where the offending companies cannot, and is split into five broad 'classes', of which insurance is one, being further subdivided into two 'sub-classes', insurers and intermediaries. The latter sub-class includes insurance brokers.

BIBA wants a further subdivision that separates insurance brokers from other intermediaries (such as credit brokers), and an end to cross-subsidies within the Scheme. The move is prompted particularly by the PPI mis-selling scandal, which they maintain "has nothing to do with insurance brokers", but who have seen their levies increase substantially as a result. By way of example, a broker with £20m commission income, paying a levy of £3,000 in 2008, will see that levy increase to £211,000 in 2011.

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2011 Budget

On Wednesday 24 March, Chancellor George Osborne announced his 'budget for growth', aiming to create the 'most competitive tax system in the G20', attracting new business to the UK and promoting exports, whilst developing an 'educated and flexible workforce.'

Keen to be seen softening the effects of cuts, Osborne offered something to 'the squeezed middle', increasing the tax threshold, decreasing fuel duty, and confirming the 50p tax rate is to be temporary. There was also a boost for charity donations and measures to support the green agenda.

For businesses there was an unexpected 2% reduction in the main rate of corporation tax for financial years starting 1 April 2011, with a further 1% reduction in each of the next three financial tax years, whilst the level of corporation tax for small businesses has reduced from 21% to 20% for financial years starting 1 April 2011. New enterprise zones will offer tax and other breaks, the lifetime allowance for entrepreneurs relief on qualifying capital gains has been doubled to £10m, and the maximum investment in Enterprise Investment Schemes has also been doubled to £1m, all of which should support funding for new and small businesses.

Somewhat more controversially, both the rate of writing down allowances on plant and machinery will be reduced from 20% to 18% per annum and the Annual Investment Allowance will be reduced from the current limit of £100,000 to £25,000 from 1 April 2012.

Other changes broadly welcomed are the future integration of the National Insurance and Income tax regimes, the increase of tax free business mileage rate for use of own cars from 40p per mile to 45p per mile from 6 April 2011, for the first 10,000 business miles and several initiatives aimed at tax simplification. Various other reforms related to typical international group financing structures will improve the UK's attractiveness for foreign investors, and bring the UK more into line with international practice.

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Safeguarding Client Money and Assets

The Financial Services Authority (FSA) has recently sent a letter and report to the CEOs of major insurance brokers and investment firms, drawing their attention to the FSA's concerns over the handling of clients' money and assets.

This follows a letter that the FSA originally sent in March 2009, which explained the obligations of such companies to protect their clients' money and assets and warned them of the FSA's intention to make spot checks during 2009.

Subsequently, these checks unearthed a number of failings, which prompted the FSA to write to CEOs with an accompanying report containing details of visit findings, and highlighting some of the weaknesses it discovered. These included poor management oversight and control, the failure to establish trust status for segregated accounts, unclear arrangements for the segregation and diversification of clients' money and incomplete and/or inaccurate record keeping.

The report states that customers must have confidence that their money and assets are safe and that they will be returned within a reasonable timeframe in the event of a firm becoming insolvent. They must also have confidence that firms holding their money and assets have strong management oversight and control over their business. The report reaffirms that the FSA believes that protection of client money and assets is a fundamental

part of regulation and, as a result of the more difficult economic climate it plans to intensify its supervision in this area.

In addition, the report also includes examples of how firms should meet FSA expectations in relation to compliance with its requirements. Over the course of the year, the FSA will be increasing its visits to firms to assess whether these expectations are being fulfilled.

The FSA has already taken measures against a number of the companies that it visited, which included the referral of two firms to enforcement, the freezing of a firm's assets and the commissioning of skilled persons reports.

To find out more about how we can help you, simply contact your nearest Wilkins Kennedy office, or call Dan Graves on 0207 403 1877.



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Guidelines Delayed for Bribery Act

The Bribery Act 2010 (the Act), which received Royal Assent last year, was expected to come into effect this April, but guidance on interpretation has not been provided as at March, and as the Act will not come into force for three months thereafter, there is clearly some slippage. It replaces existing anti-corruption legislation and introduces a new offence that is aimed at commercial organisations that negligently fail to prevent bribery.

The only defence for such firms will be if they can demonstrate that they have 'adequate procedures' in place to prevent such conduct by a person

or persons associated with them. The Government is currently defining what constitutes 'adequate procedures'.

This Act does not replace or amend current FSA rules and principles, and authorised firms who fail to adequately address corruption and bribery risks remain liable to regulatory action. It is thus imperative that all firms, and in particular those who use third parties to win business, read and take note of The FSA's Final Notice to Aon, a firm it has taken action against and its recent report findings on anti-bribery and corruption in commercial insurance broking.

The FSA's Anti-bribery report can be found online at this address: http://www.fsa.gov.uk/pubs/anti_bribery.pdf

This is a substantial report, which includes many useful practical examples of problem areas, and indications of best practice and required due diligence. All the evidence, however, seems to indicate widespread shortfalls in this area, so if you feel your organization may be overdue a review, or would simply like to talk through the issues, contact your local Wilkins Kennedy office, or call Dan Graves on 0207 403 1877.

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New FSA Policy Statement on CASS

Revised rules for auditors' client assets reports were issued by the FSA on 25 March, following the consultation paper produced in September last year. The rules are intended to improve the quality and consistency of reports produced for the regulator, and apply to all insurance brokers holding more than £30,000 of client money or which operate a non-statutory trust client bank account.

In particular, the new rules seek to:

- confirm and clarify the standards required for the report;
- increase and make consistent the information provided, to enhance its supervisory value; and
- improve a firm's governance oversight of both its auditors and compliance with the Client Assets sourcebook (CASS).

Note that the FSA does not regulate auditors, and it remains the regulated firm's responsibility to appoint an appropriately qualified auditor, and that their report complies with the FSA's requirements.

The changes required to the auditor's report are as follows:

- **Firms holding client assets to produce a 'reasonable assurance' report.**
- **Firms not holding client assets to produce a 'limited assurance' report.**
- **The report must comply with applicable auditing standards, such as the Auditing Practices Board (APB) standards.**
- **A revised template for the report (see Appendix 1 of the Policy Statement).**
- **The report must be signed by the responsible auditor.**
- **A separate template schedule identifying any breaches of the rules set out in the Client Assets Sourcebook (CASS).**
- **For any identified breaches, firms are expected to provide comments on actions taken and/or mitigating factors.**
- **Mandate rules (CASS 8) will be brought back into scope of the auditor's client assets report.**
- **Auditors are required to deliver reports on client assets within four**

months from the end of the applicable reporting period.

The FSA are prioritising this area somewhat, stating "The protection of client assets will remain a regulatory priority. We will continue our intensive and intrusive approach to identify and mitigate CASS risks." In particular, future policy work mapped out for the FSA includes a review of CASS 5 Client Money – Insurance Mediation Activity.

Any firms considering a review of their own procedures in this area are invited to call their local Wilkins Kennedy office, or contact Dan Graves on 0207 403 1877.

You can read the Full Policy Statement at the FSA's website at this address: http://www.fsa.gov.uk/pubs/policy/ps11_05.pdf

New Regulatory Framework Fleshed Out

Following Chancellor George Osborne's announcement last June that the FSA is to be broken up, some meat was added to the bones in the consultation document issued by the Treasury in February, at least regarding regulatory issues.

Under the outlined proposals, the FSA will see its responsibilities being split between a Financial Conduct Authority (FCA), and a Prudential Regulatory Authority (PRA), which will be a subsidiary of the Bank of England, with financial crime issues to be devolved to the Economic Crime Agency expected to be set up by the Home Office, possibly later this year.

The FCA will take over the FSA's existing responsibility for consumer protection and market conduct, as well as managing the Financial Ombudsman Service, the Financial Services Compensation Scheme, and the recently-created Consumer Financial Education Body. The FCA will regulate all firms, both retail and wholesale, including those regulated by the PRA.

The PRA will be charged with prudential responsibility for deposit takers, insurers and investment banks, although precise definitions as to these entities are still awaited and it is expected that it will prove to be an extremely tough regulator. At the same time, in addition to being subject to prudential oversight from the PRA, the designated entities will also be regulated by the FCA.

For this to work well in practice there will have to be close co-operation between the PRA and FCA. If the activities of the PRA are to be focused on the largest financial institutions, such as the large, consumer focused banks, then the majority of the 25,000 or so firms currently regulated by the FSA are likely to come under the jurisdiction of the FCA, which will be responsible for their prudential supervision, as well as non-prudential supervision. At present, the boundaries between the FCA and the Economic Crime Agency remain unclear and it is not yet certain which of the two organizations

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will take responsibility for criminal market abuse prosecutions.

There is some disquiet at the FSA, which currently has the option of using criminal or civil law in respect of market abuse prosecutions and has recently scored some significant successes. It feels that future prosecutions could be seriously jeopardised if different agencies are responsible for criminal and civil regimes.

Many feel that in future, things will become more complex for the largest firms due to the segregation of prudential regulation from conduct of business and the fact that they will have to deal with multiple regulators. However, for the majority of firms currently regulated by the FSA the changes look much more cosmetic but until the detail is defined it will be hard to tell for sure.

