Consultation Paper 11

CIFO Future Funding Structure Options

Issued: 5 December 2017

A: This consultation paper

This consultation paper is part of a multi-stage process to develop a new funding structure for the Channel Islands Financial Ombudsman ['CIFO'] that will apply from 1 January 2019. In the first stage, we held a series of meetings with stakeholders, in order to remind them of the existing funding structure and to help identify their views of the relevant issues. These meetings were attended by 61 individuals from 49 organisations

In the second stage, we issued a discussion paper that summarised the existing structure, suggested some principles and set out a broad range of options. We received formal written responses from nine organisations, with one of them submitted on a confidential basis.

In this, the third stage, we report back on the views expressed by stakeholders and set out a narrower range of options that are informed by those views.

- Section B of this consultation paper gives an overview of the issues.
- Section C explains how to respond to the consultation.
- Section D summarises the background (CIFO's role and relevant legislation).
- Section E sets out emerging themes.
- Section F sets out emerging options.
- Section G poses a series of specific questions.
- Section H explains the next steps.
- Annex 1 shows illustrative high-level options for a new CIFO funding structure.
- Annex 2 covers additional issues that apply irrespective of the illustrative options.
- Annex 3 provides CIFO's formal responses to the Discussion Paper.

In the fourth stage, in the light of the views expressed on this consultation paper, we will issue a further consultation paper that proposes a single future model for consideration.

B: Overview

Feedback from stakeholders following the CIFO discussion paper[1] on future financing structure options showed a consensus on the following points:

[1] https://www.ci-fo.org/wp-content/uploads/2017/07/170710-DP1-funding-structure.pdf.

- The new funding structure should be simple and easy to understand. It should be predictable, so that financial services providers ['FSPs'] can budget ahead, and avoid undue volatility.
- It should be easy and low-cost for CIFO to administer, in order to minimize the administrative cost incurred.
- All FSPs benefit from the shared value of CIFO to the reputation (both locally and internationally) of the financial sectors in the Channel Islands and of FSPs.
- But there should also be some appropriate element in the funding structure, perhaps related to the variable cost of CIFO handling a complaint.
- Any levy should continue to be based on type of registered provider[2]. Calculating it by sector size or individual market share would not be practicable.

Two conflicting points of view emerged on whether levies should be divided first by Bailiwick and then by type of registered provider, or first by type of registered provider and then by Bailiwick.

The feedback was helpful in identifying four key themes:

1. Recognition of the shared value of CIFO to the reputation of the Channel Islands and the financial sectors, both locally and internationally.
2. Desire for a funding structure that would be simple and predictable for FSPs and would be easy for CIFO to implement in order to minimise administrative cost.
3. Two distinct and conflicting options on allocating the reputational component between the two Bailiwicks and their financial sectors.
4. Support for some enhancement of the workload-related variable component currently provided by case fees.

Combining either one of the proposed options for the annual levy with a gradually increasing case fee could provide for the desired complaint volume sensitivity of CIFO's funding structure while maintaining simplicity and predictability, and gives smaller providers who may be generating significant complaint volumes time to adapt.

C: How to respond

Interested parties – including FSPs and representative bodies of FSPs, consumer bodies and the Financial Services Commissions – are invited to respond to the options and questions in Section G and the Annexes. Please send any response in writing by email to consultations@ci-fo.org or by post to Channel Islands Financial Ombudsman, P O Box 114, Jersey, JE4 9QG.

Responses may be published. Any sections that respondents consider to be confidential (for example, because they relate to proprietary information or provide commercially-confidential data) should be clearly marked as such, indicating the reason why they are considered to be

[2] CIFO's levies are payable by 'registered providers', as defined in the Financial Services Ombudsman (Case-Fee and Levy) (Jersey) Regulations 2015 and the Financial Services Ombudsman (Case Fee and Levies) (Bailiwick of Guernsey) Order 2015. Broadly these are providers that, in relation to their carrying out 'relevant financial services business' as defined in article 9 of the Jersey Law and section 9 of the Guernsey Law, are required to register with the Jersey and Guernsey Financial Services Commissions or are licensed or hold a certificate or permit under the regulatory laws as specified.

confidential. The reason will be taken into account by the Principal Ombudsman in deciding what to publish in the response to the consultation.

Responses must reach CIFO by no later than 7 February 2018.

D: Background

CIFO is the joint operation of the Office of the Financial Services Ombudsman (Jersey) ['Jersey OFSO'] and the Office of the Financial Services Ombudsman (Guernsey) ['Guernsey OFSO']. The joint operation – working from a shared office in Jersey, with the same board, ombudsman and staff – covers complaints about financial services provided in and from Jersey, Guernsey, Alderney and Sark. It began resolving complaints on 16 November 2015.

Jersey OFSO and Guernsey OFSO are independent of the States. They were established by the Financial Services Ombudsman (Jersey) Law 2014 ['the Jersey Ombudsman Law'][3] and the Financial Services Ombudsman (Bailiwick of Guernsey) Law 2014 ['the Guernsey Ombudsman Law'].[4] These laws provide for the resolution of complaints against FSPs – independently, fairly, effectively, promptly, with minimum formality and so as to offer a more accessible alternative to court proceedings.

The current funding structure for Jersey OFSO and Guernsey OFSO is set out in various pieces of legislation in each Bailiwick, including:

- The Financial Services Ombudsman (Case-fee and Levy) (Jersey) Regulations 2015[5] as amended by the Financial Services Ombudsman (Case-Fee and Levy) (Amendment) (Jersey) Regulations 2016[6];
- The Financial Services Ombudsman (Case Fee and Levies) (Bailiwick of Guernsey) Order 2015[7] as amended the Financial Services Ombudsman (Bailiwick of Guernsey) Law, 2014 (Amendment) Ordinance, 2016[8] and the Financial Services Ombudsman (Case Fee and Levies) (Bailiwick of Guernsey) (Amendment) Order, 2016[9].

These provide for Jersey OFSO and Guernsey OFSO to prescribe schemes for levies and case fees to be paid by certain FSPs. Jersey OFSO and Guernsey OFSO are required to produce separate budgets, levy schemes and case fee schemes – but CIFO's expenses are to be divided equally between them until 31 December 2018. The current levy and case fee schemes are published at www.ci-fo.org/resource-room/funding.

E: Emerging themes

CIFO's funding structure is a zero-sum game. It covers the division of a pre-determined total. So any reduction for one type of FSP must be balanced by an increase for another

[3] www.jerseylaw.je/Law/display.aspx?url=lawsinforce%5chtm%5cLawFiles%5c2014%2fL-14-2014.htm

[4] www.guernseylegalresources.gg/article/115617/Financial-Services-Ombudsman-Bailiwick-of-Guernsey-Law-2014

[5] http://www.jerseylaw.je/law/display.aspx?url=LawsInForce\htm\ROFiles%5cR%26OYear2015%2fR%26O-009-2015.htm

[6] https://www.jerseylaw.je/laws/enacted/Pages/RO-117-2016.aspx

[7] http://www.guernseylegalresources.gg/CHttpHandler.ashx?id=95899&p=0

[8] http://www.guernseylegalresources.gg/article/156922/Financial-Services-Ombudsman-Bailiwick-of-Guernsey-Law-2014-Amendment-Ordinance-2016

[9] http://www.guernseylegalresources.gg/article/156055/No-44---The-Financial-Services-Ombudsman-Case-Fee-and-Levies-Bailiwick-of-Guernsey-Amendment-Order-2016

type of FSP. Naturally, this makes it more difficult to reach a consensus amongst FSPs. Nevertheless, following the Discussion Paper, there was broad consensus on the following points:

- The new funding structure should be simple and easy to understand. It should be predictable, so that FSPs can budget ahead, and avoid undue volatility.
- It should be easy and low-cost for CIFO to administer, in order to minimize the administrative cost incurred.
- All FSPs benefit from the shared value of CIFO to the reputation (both locally and internationally) of the financial sectors in the Channel Islands and of FSPs.
- But there should also be some appropriate element in the funding structure, perhaps related to the variable cost of CIFO handling a complaint.
- Any levy should continue to be based on type of registered provider. Calculating it by sector size or individual market share would not be practicable.

There is, of course, an inherent conflict between a simple and easily-administered approach that maintains relatively stable and predictable year-over-year levies to registered providers and an increasing element of user-pays.

Interestingly, two distinct and conflicting points of view emerged on how the reputational element of the funding should be shared:

- One view was that it should continue to be shared equally between the two Bailiwicks before being shared among the FSPs in each Bailiwick. This would reflect the similar benefit that each Bailiwick derives from CIFO's operation. It means that the cost would be borne equally by the financial sectors from each Bailiwick – but, depending on the comparative number of regulated/registered FSPs in each Bailiwick, a Jersey FSP and a similar Guernsey FSP might well bear different shares of the cost.
- The other view was that in future the cost should be shared so that similar FSPs bear a similar share. This would equalise some competitive issues. It means that a Jersey FSP and a similar Guernsey FSP would bear a similar share of the costs – but, depending on the comparative number of registered providers in each Bailiwick, the Jersey financial sector and the Guernsey financial sector collectively might well bear different shares of the overall costs.

On transitional arrangements, some stakeholders considered that any significant changes should be phased in over a few years to avoid undue financial impact on some FSPs. Others suggested an immediate change for the sake of clarity, simplicity and lower cost to administer.

In the light of the feedback received, the CIFO Board has provisionally concluded that:

- There should be a reputational element to the funding, reflecting the reputational benefit that all FSPs receive. This is currently provided by the annual levy. As stakeholders have identified, calculating the levy on the basis of sector size or individual market share would not be practicable.
- There should also be a user-pays element to the funding, reflecting workload involved in handling cases. This is currently provided by the case fee. That is the clearest and

simplest way of collecting a user-pays element. The user-pays proportion could be increased by increasing the case fee.

- The new structure should focus on a balance of fairness, clarity, simplicity, lack of volatility and ease of administration (for both CIFO and FSPs). Phasing in any significant change would help some FSPs and would not create an undue administrative burden.

Both of the options for sharing the levy between the two Bailiwicks are feasible from CIFO's point of view. One important issue will be how to equalise the levy between similar types of registered providers in each Bailiwick. The Jersey OFSO and Guernsey OFSO budgets have to be prepared and approved before the financial year to which they relate, and take account of the numbers of registered providers at that time. By the time the levies are collectable, the numbers of registered providers have usually changed. So it would only be possible to keep the levies equal if it were possible to transfer costs between the Jersey OFSO and Guernsey OFSO budgets. This issue warrants further consideration and may require the States to amend the Jersey Ombudsman Law and the Guernsey Ombudsman Law.

F: Emerging options

Feedback on the Discussion Paper was helpful in identifying four key themes to guide the development of options. These were:

1. Recognition of the shared value of CIFO to the reputation of the Channel Islands and the financial sectors, both locally and internationally.
2. Desire for a funding structure that would be simple and predictable for FSPs and would be easy for CIFO to implement in order to minimise administrative cost.
3. Two distinct and conflicting options on allocating the reputational component between the two Bailiwicks and their financial sectors.
4. Support for some enhancement of the workload-related variable component currently provided by case fees.

Theme 1 – Recognition of the Shared Value of CIFO

Most FSPs and their industry groups recognised the shared benefit of CIFO's creation and continued operation. All FSPs, regardless of their sector, size, domestic or international scope of business, and volume of complaints generated, shared the reputation benefit accruing to the islands and their financial sectors from having a credible and independent financial dispute resolution body. This shared benefit supports the continuation of some form of flat levy payable by all registered providers.

Theme 2 – Simplicity, Predictability, and Low Administrative Cost

Notwithstanding the inherent complexity of the multi-island, multi-sector, diverse financial services environment in the Channel Islands, it was clearly recognised that FSPs and CIFO both benefit from a funding structure that is simple. Simplicity avoids confusion and wasted resources verifying the details of a complex formula and levy payment amounts.

There was also recognition of the value of predictability in the annual funding obligation borne by FSPs. Having an annual CIFO funding obligation that varied significantly (upward or downward) year-over-year was considered less desirable by some FSPs from an expense budgeting perspective. Some FSPs sought a period of adjustment if their levy payments were to change significantly as a result of the new funding structure.

Finally, most FSPs sought a funding structure that was low-cost to administer. Given CIFO's limited staff resources and the desire to focus the limited resources on the core function of dispute resolution, a funding structure that minimised administrative burden for CIFO, and the associated cost for levy-paying FSPs, was preferred.

Theme 3 – Allocating the Reputational Component

The number of variables to be considered in CIFO's funding structure (islands, sectors, number of FSPs in each sector, complaint volumes, etc.) generates considerable complexity. When looked at from a high-level perspective, two distinct levy options emerged. Both appear viable from CIFO's perspective. Both would require minor changes to legislation to either continue the 50:50 cost sharing arrangement or to set a new Bailiwick income split based on the relative number of registered providers.

Option 1 is the continuation of the current 50:50 cost sharing arrangement between Jersey and Guernsey, allocation of a set percentage[10] of the cost within each Bailiwick to the banking sector, and the remainder allocated to other FSPs in accordance with their non-banking licences issued by the respective Financial Services Commissions in each Bailiwick. This requires minor changes to the current legislation and has no incremental impact on CIFO's level of administrative effort and costs. Several FSPs favoured keeping the current funding structure for these reasons and given that industry stakeholders are already familiar with this approach. For an illustration of how this option works, please see Annex 1A.

Option 2 is for a new approach which involves treating FSPs in each sector (banking and non-banking services) the same across both Bailiwicks for levy purposes. Like Option 1, this option is consistent with the pan-island nature of CIFO, but it eliminates the differential competitive impact of having like providers pay a different levy on each island. As in Option 1, a set percentage could still be allocated to the banking sector across both islands with the balance allocated to the licences associated with non-bank financial services business activities. Modest changes would be required to current legislation and this option poses a small incremental impact on CIFO's level of administrative effort and costs. For an illustration of how this option would work, please see Annex 1B.

Theme 4 - Enhanced Workload-Related Component

Industry stakeholders have consistently expressed a desire for a CIFO funding structure that includes some element of user-pays. Having those FSPs that generate more complaints pay more of the cost of CIFO's operation is consistent with CIFO's commitment to fairness and transparency. Reflecting the historical complaint volume of individual FSPs, or sectors, in a levy would add significant complexity and be inconsistent with the collective desire for simplicity and predictability noted above. It would also make administration significantly more challenging for CIFO and would create significant additional cost. Some industry stakeholders noted that having a volume-driven levy and a volume-driven case fee at the same time was unnecessarily duplicative, even punitive. It would also fail to reflect the shared value of CIFO to all FSPs as noted above.

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[10] Currently 50% based on the initial allocation proposed in the consultations conducted by the States of Jersey and States of Guernsey in 2014 prior to CIFO's commencement of operation in November of 2015. Because of the widespread use of banking and the multiplicity of customers, it can be argued that the banks derive maximum reputational benefit.

The existing practice of charging case fees accommodates both objectives, simplicity, and complaint volume-sensitivity. Case fees charged to FSPs based on their actual volume of in-mandate complaints referred to CIFO during the preceding year provides a user-pays basis for cost allocation, provides absolute predictability of the case fees to be charged, and is administratively simple and low-cost for CIFO to administer.

For 2016 CIFO set case fees at £200 per case for FSPs that paid the levy and £600 for other FSPs (which are not charged the levy because, as they could not be identified). This resulted in about 8% of CIFO's revenue being generated through case fees.

For 2017, following consultation and to reflect an increased user-pays component, CIFO increased the case fees to £300 per case for FSPs that paid the levy and £750 for other FSPs. For 2018 CIFO is minded to further increase the case fees to £400 per case for FSPs that paid the levy and £900 for other FSPs. Assuming similar complaint volumes and fee collectability, this will almost double the proportion of CIFO's funding directly derived from complaint volumes since CIFO commenced operation in November 2015.

To further increase the user-pays component of CIFO's funding structure, in conjunction with the implementation of either of the options noted above for annual levies, CIFO could increase case fees incrementally over the next few years, starting in 2019, towards a target by 2021 of £850 per case for FSPs that paid the levy and £1,350 for other FSPs.

Conclusion – Possible future funding structure for CIFO

Combining one of the two proposed high-level options for the annual levy with a gradually increasing case fee would provide for the desired complaint volume sensitivity of CIFO's funding structure while maintaining the simplicity and predictability, and giving smaller FSPs who may be generating significant complaint volumes time to adapt.

G: Consultation questions

As CIFO is fully-funded by FSPs, the implications of each funding structure option for individual FSPs may be significant. This is particularly true for possible changes (such as an increase in case fees) that could increase the sensitivity of allocated costs to actual complaint volumes.

It is therefore imperative that industry stakeholders carefully consider the potential implications of the levy options, the potential case fee changes and the additional issues set out in Annex 2 and provide responses to the questions posed below relating to each.

Interested stakeholders are asked to provide their views on the consultation paper, the questions posed below, and the funding structure options in particular. In some cases, interested stakeholders may prefer certain aspects of an option but not the entire option described. In such cases, it would be helpful for the desirable and undesirable aspects of each option to be specifically highlighted.

Q1: Do you have any thoughts on the high-level principles set out in section E or the four themes set out in section F that should be reflected in CIFO's future funding structure? Are the high-level principles and themes set out in this consultation following on from the recent Discussion Paper the correct ones? Are there any other high-level principles and themes that warrant consideration?

Q2: Do you have any clear preference for one of the two funding structure options for the annual levy proposed in Annexes 1A and 1B to this consultation paper? Please explain why you prefer the chosen option.

Q3: Is there another funding structure option that should be considered other than those proposed in this discussion paper? Please be as specific as possible.

Q4: Do stakeholders agree with the proposed approach set out in Annex 2A to address the question of the banking sector's allocation and how the issue was incorporated into the various funding structure options?

Q5: Do stakeholders agree with the proposed approach set out in Annex 2B to secure funding from unregulated sectors?

Q6: Do stakeholders have any feedback on the issues covered under Annex 2C regarding the current zero-rating process and the proposed continuation of the current approach?

H: Next steps

In addition to reviewing the written responses to this consultation paper, CIFO will seek input from stakeholders at public information sessions to be scheduled in Guernsey and Jersey before the consultation closing date.

Informed by the issues set out in this consultation paper, stakeholder responses, and input received at the public meetings, a final proposed funding structure will be developed by CIFO's Board of Directors and published for consultation. Stakeholders will be able to consider that against the background of historical complaint data, showing island-level and sector-level complaint statistics, since CIFO opened for business on 16 November 2015, due to be published in the second quarter of 2018.

Following that consultation, CIFO's Board of Directors will finalise the proposed funding structure to take effect 1 January 2019, and seek approval from the States of Guernsey and States of Jersey for any legislative changes that may be required to accommodate the proposed funding structure.

Annex 1: Funding structure options

<u>Annex 1A</u> – Funding Structure Option 1: Status quo option (pan-island shared cost model, cost allocated per licence, no disruption or incremental complexity)

Overview

Under the current CIFO funding structure:

1. The revenue required to fund the joint operation is first allocated 50:50 to each Bailiwick;
2. One half of the revenue required in each Bailiwick is then allocated to the banking sector (registered providers holding banking licences) in each Bailiwick, the other half to the other sectors in each Bailiwick so that the same size levy applies to each sector;
3. The levy for each sector is calculated by dividing the revenue allocation by the number of registered providers in each sector. The data on registered providers is provided to CIFO (as at a certain date, usually at the beginning of the current calendar year) by the respective Financial Services Commission;
4. The result is four different sectoral levies of differing amounts payable by registered providers for each sector within which they are active:

   - A Jersey banking sector levy;
   - A Jersey levy for each of the other sectors of activity;
   - A Guernsey banking sector levy;
   - A Guernsey levy for each of the other sectors of activity.

The user-pays component of the funding structure is provided by case fees payable by individual registered providers annually in arrears based on their prior year's complaint volumes.

Comments

Several stakeholders in response to the Discussion Paper and in the public consultation meetings suggested that, given the modest amounts involved overall in CIFO's funding, that the effort and cost involved in choosing, adopting and implementing a new funding structure for CIFO was not warranted and it was suggested that the status quo set out in this Option 1 should continue. Several other stakeholders agreed to keep the funding structure simple but advocated for some modest changes.

While the current funding structure is complex and created some unforeseen challenges during the first two years of CIFO's operation, it has now been fully implemented and routinized by CIFO to minimize administrative effort and cost. It combines an equal allocation of costs to each island with a flat levy component. The user-pays component is provided through case fees payable by those FSPs about which complaints are referred to CIFO.

<u>Annex 1B</u> – Funding Structure Option 2: Equal levy across sectors (pan-island consistent levy model, cost allocated per licence, minimal disruption and incremental complexity)

Overview

Under this option for a new CIFO funding structure:

1. The revenue required to fund the joint operation is allocated to each sector on a pan-island basis so that the levies are the same for like activities across both Bailiwicks;
2. One half of the revenue required is allocated to the deposit-taking licences of the banking sectors in both Bailiwicks, the other half to the other sectors in both Bailiwicks;
3. The levy for the banking sectors is calculated by dividing the revenue allocation by the number of registered providers holding banking licences across both Bailiwicks. The levy for the non-bank sectors is calculated by dividing the revenue allocation by the total number of registered providers in the non-banking sectors across both Bailiwicks. The data on registered providers is provided to CIFO (as at a certain date, usually at the beginning of the current calendar year) by the respective Financial Services Commission;
4. The result is two distinct levies of differing amounts payable by registered providers for each sector within which they are active across both islands[11]:

   - The same size levy for each of the Jersey and Guernsey banking sectors in respect of their deposit-taking licence;
   - A second same-sized levy for each of the Jersey and Guernsey non-banking sectors.

The user-pays component of the funding structure is provided by case fees payable by individual registered providers annually in arrears based on their prior year's complaint volumes.

Comments

More stakeholders suggested moving to a funding structure that resulted in levies for like activities being the same across both islands which is set out in Option 2. This option avoids any island-based cost allocation and provides for an equal allocation of costs to licences for like business activities across both islands (i.e., the individual levies for banking and non-banking FSPs would be the same in each Bailiwick). As a result, the total amount paid by the industry in each Bailiwick may be different, reflecting the different number of registered providers in each island in each sector. The levy to each business activity licence across both islands is fixed. The user-pays component is provided through case fees as is the case for Option 1.

[11] For greater clarity, a bank with operations in both Jersey and Guernsey will pay the Jersey banking levy plus the identical Guernsey banking levy. An insurance provider with operations in both Jersey and Guernsey will pay the Jersey non-banking levy plus the identical Guernsey non-banking levy.

Annex 2: Additional issues

<u>Annex 2A</u> – Banking sector share of allocated costs

There are two issues that have been identified regarding the banking sector share of allocated costs. These are each discussed below.

Should banks pay 50% of allocated costs?

In the initial stakeholder discussions in 2014 concerning the establishment of a funding structure for CIFO, it was anticipated that a significant proportion of complaints would involve the provision of banking services. As a result, it was decided to recover 50% of the required revenue each year from the banking sectors on each island. Following the Discussion Document and public consultations, some stakeholders felt this allocation should be driven by actual complaint volumes. But other stakeholders noted that the reputation of the jurisdiction held particular value for the larger bank groups which justified the allocation. Yet another view was that any move away from the current 50% allocation to banks would result in significant increases to the annual levies paid by non-bank registered providers.

The allocation of a set percentage to the banking sector does not affect the levy options proposed as the cost allocation can be incorporated into either proposed option. From comments received from banking sector representatives, there appears to be willingness to retain the 50% allocation to the banking sector in consideration for the retention of a simple and low-cost approach to allocation of CIFO's operating costs. As a result, illustrative options shown in Annexes 1A and 1B continue this 50% allocation.

Should private banks be treated differently from retail banks for levy purposes?

In response to past consultations and in public meetings, some private banks have suggested that including them with the larger retail banks for levy determination purposes was unfair and asked to be treated separately. This proposal raises two significant challenges:

1. Banking licences do not distinguish between private banks and retail banks. What are the criteria that could be used to distinguish between private banks and other banks? How could CIFO distinguish between them fairly, easily, and accurately?
2. Reclassifying private banks to treat them in the same way as non-bank FSPs for levy purposes would have significant effects on the levies payable by the remaining banks and on the levies payable by existing non-bank FSPs.

CIFO considers this issue to be one which the financial industry is best positioned to address. Given the implications of any change for different groups of industry stakeholders, can the industry agree on a position and a simple means to implement it?

Annex 2B – Dealing with unregulated sectors

Different case fees for non-levy-paying FSPs

CIFO's current funding structure is dependent upon the ability to identify entities undertaking relevant business for the purpose of CIFO's remit. For those entities where CIFO is unable to identify the levy payer (e.g., credit brokers and pension providers or intermediaries), the current approach is to use a differential case fee to recover a higher amount of revenue from non-levy paying FSPs (currently £700 per case file compared with £300 per case file for levy-paying FSPs with potential future increases as set out in this consultation paper).

It is currently envisaged that this approach should continue, and that the differential should be retained on any increase in case fees. The amount of the case fees can be varied by CIFO, subject to consultation, when setting the Case Fee Scheme. Should a sector demonstrate that a different case fee is warranted given the complexity of those complaints, the amount of the case fee for that sector could be varied by CIFO, subject to consultation.

Banks levied for money service business ['MSB']

CIFO levies are payable per sector of activity. In Jersey, all banks also hold licences for MSB activities in addition to licences for deposit-taking. In Guernsey, most (but not all) banks also hold licences for MSB activities. As a result, they are currently also charged the CIFO MSB sector levy for their MSB activities in addition to the banking levy.

On the one hand, some banks see this as unfairly adding to their share of CIFO's costs and one has asked for banks to be exempted from paying the additional MSB levy. The point was also raised that MSB activities are integral to banking. On the other hand, MSB activities are separately licenced and exempting the banks from the MSB levy would increase the levy for non-bank FSPs. CIFO notes that relevant banks also pay a non-bank levy for other licenced activities (e.g., insurance intermediation).

Questions

1. Do stakeholders agree with the proposed approach to continue to charge a differential case fee to non-levy-paying FSPs?

2. Is the current plan to increase the £700 per case file charged to non-levy-paying FSPs to £900 in 2018 and then by an additional £150 per year through to 2021 sufficient?

3. Should all registered providers with MSB licences continue to pay a separate levy for that MSB activity even if they are already paying a levy to CIFO for their other business activities?

<u>Annex 2C</u> – The zero-rating process

Under the current legislation, there are provisions for CIFO to zero-rate specific FSPs for the levy. CIFO must zero-rate any FSP that does not do business, or deal with customers, within CIFO's jurisdiction.

Application for zero-rating is made by the FSP based on stated criteria for entitlement to zero-rating. CIFO does not validate the FSP's claimed entitlement to zero-rating, but if found later to be wrongly claimed, all previous years' levies would be due.

Initially, this added significant administrative complexity. But the process has now bedded in, and it is not currently proposed to change it. However, there is a periodic administrative burden to reconfirm those FSPs continuing to claim a zero-rating for the levy.

Question

Do stakeholders agree that the current approach to zero-rating should continue?

Annex 3: Formal responses to the Discussion Paper

The Discussion Paper: CIFO Funding Structure was published on 11 July 2017, with a closing date of 11 September 2017. It was published on the CIFO website, highlighted in a newsletter sent out to all subscribers and notified to contacts at specific organisations representing groups of stakeholders, such as industry associations and consumer groups.

The Discussion Paper explained the current funding structure and the various complexities associated with it. It set out the general principles for the future funding of CIFO and addressed how the costs might be shared. Nine formal responses were received from stakeholders, one of which was requested to be treated as confidential.

Apart from the one response which was requested to be treated as confidential, responses were received from the following entities and you can click through on the link to the actual response:

1	Asset Risk Consultants (ARC), Guernsey/Jersey
2	SPF Private Clients, Guernsey
3	Association of Guernsey Banks
4	Northern Trust (Guernsey) Limited (NTGL)
5	States of Guernsey Committee for Employment & Social Security
6	Barclays Bank PLC, Jersey Branch & Barclays Bank PLC, Guernsey Branch
7	Bank Julius Baer, Guernsey
8	Community Savings Ltd, Jersey

The responses were thoughtful and considered and the time taken by stakeholders to provide this input is much appreciated. Overall, there was general appreciation of the need to avoid complexity and associated administrative cost in the CIFO funding approach and that all FSPs gain value from CIFO, even when no complaints are generated for investigation by CIFO.

There was not full consensus for any one particular approach, but some options were supported by multiple responses. Most responses did not directly answer the consultation questions and so a summary is provided below.

Regarding general principles, three responses emphasised their support for two of the principles listed in the discussion paper, namely that the funding structure should be straightforward to understand and be simple to assess and collect. One also suggested that the increasing costs of regulation be considered along with various alternative possible approaches for case fees, such as increasing their contribution to CIFO funding, capping them for multiple complaints, and weighting them based on complexity.

Considering possible variables which could be used in sharing CIFO's costs, no responses expressed support for using size or market share data to share costs within or across FSP sectors. However, two bank responses requested that consideration be given to differentiating between retail and private banks, so that retail banks pay a larger levy.

On sharing costs between the islands, one response considered that Guernsey should provide a lower proportion of CIFO costs than Jersey as it is a smaller island and as Jersey has the economic benefit of the CIFO office location; it also suggested a split based on 'size' (the number of levy-payers or registered providers in each island) and workload produced in each island.

Two responses considered that the current 50:50 split should continue for the next few years.

On sharing costs between FSPs, four responses proposed that the island split should be on a size basis (based on the number of levy-payers or registered providers in each island), to enable the levies charged to similar FSPs in each island to be the same. The Association of Guernsey Banks viewed this as a pan-island approach.

The same respondents asked for consideration to be given to a workload or volume-driven component of the funding structure, some giving a range of possible approaches.

Some acknowledged that if it were to be built into the levy, the volume component would need to be at the sector, rather than FSP, level (and across both islands) to enable the levy to be set so that an FSP in one island pays the same levy as a similar FSP in the other island. There was general agreement that the priority was for the revised funding structure to be straightforward to understand and simple to assess and collect.

Two responses considered that the banking sector should continue to contribute 50% of the levy revenue, with the other 50% made up by the other sectors. One put forward that the administrative effort and burden of building the volume element into the levy would be onerous and inefficient and that the volume element should come from case fees, which should be representative of the actual time spent by CIFO on a complaint.

A few responses considered that all FSPs should contribute to CIFO costs, even if they have not generated complaints. The response from the Association of Guernsey Banks stated that "it is accepted that CIFO is necessary, worthwhile and beneficial to the standing of the Channel Islands' financial services industry - it is correspondingly accepted that there is a fixed cost for having that requisite institution".

Two other responses noted that some FSPs are not currently required to pay a levy and requested that this is reviewed. [This relates particularly to the pensions sector where no levy is charged as it was not possible for these providers to be identified by the Financial Services Commissions when the current CIFO funding structure was set.]

Two responses requested that consideration be given to a larger levy for retail banks compared to private banks, as it was felt that the bulk of complaints relate to retail bank products.

Regarding the viability of the status quo, one respondent said that the status quo should be kept in place until 2022.

Four responses addressed the question of a transitional period, with answers ranging from none required to a period of up to three years.

In other areas, one bank response considered the current charging of a levy for the money service sector in addition to a levy for the banking sector to be unfair for banks, when it considered this an integral part of banking and in the light of the banking sector contribution of 50% of levy revenue. Consideration was asked to be given to removing the money service levy for banks and not to introduce a levy on banks for lending with the planned Lending, Credit and Finance Law[12] in Guernsey.

Community Savings Limited noted appreciation in its response for the current levy and fee exemptions extended to this organisation and for these to continue in any revised funding structure.

One response proposed a principle that CIFO would undertake a rebate to the levy if income from levies and case fees has exceeded a certain level. [This is the approach already used when the levy is set each year. See, for example, pages 4-5 of Consultation Paper 10: 2017 Levy Schemes[13].]

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[12] https://www.gfsc.gg/news/article/lending-credit-and-finance-consultation

[13] https://www.ci-fo.org/resource-room/cifo-consultations/closed-consultations/