

CASS comment – nominee companies

SUP 3.10.5 R (3) requires the CASS audit report to include an opinion on a nominee in whose name client custody assets are registered. However, working out whether the rule applies in particular circumstances, and what the report should say; is less than straightforward.



By Chris Sermon
Senior Manager
[Profile](#) | [Email](#) |

Firm type

Firstly, the rule only applies to audit reports on certain types of investment firm, specifically: an investment management firm; a personal investment firm; a UCITS firm; a securities and futures firm; a firm acting as trustee or depositary of an AIF or UCITS; an IFPRU investment firm or a BIPRU firm. In theory, a regulated firm should know what type of firm they are, but:

It's actually quite difficult to evidence firm type from existing information. I'm not sure there is a definitive list of types/categories of firms beyond SUP 3.1.2 supplemented by knowledge of sub-types (e.g. MiFiD investment firm including BIPRU firms, IFPRU firms and exempt CAD firms). I'm not aware of any better/other way other than through a combination of permissions (including 'requirements'), PERG guidance, capital adequacy returns (sometimes helps), and/or FCA Handbook definitions (sometimes helps).

SUP 3.1.2A guidance indicates that a firm can be in more than one category at once. So, applying this principle, if a firm is a bank (not one of the listed firm types) and also depositary of an AIF, does the rule apply? It would seem sensible to me that the wider application of the rules applies.

Wouldn't it be helpful if the [Financial Services Register](#) actually stated the firm type(s)?

Subsidiary

Second, the rule only applies if the nominee in whose name the custody assets are registered is a subsidiary of the regulated firm. Confusingly, the definition of 'subsidiary' is different for MiFiD business and non-MiFiD business, although the substantive meaning is much the same. What it does mean though is that where a regulated firm uses a nominee company which is owned by an affiliate, rather than being a subsidiary of the regulated firm itself, the audit requirement drops away.

The rationale is presumably that a regulated firm only controls (and can therefore be held accountable for) a nominee company which is a subsidiary; but in practice nominees may be located elsewhere in a group structure. This seems a perverse outcome, where multiple regulated entities in a group use the same nominee, but only one audit report includes it in scope. It also increases the risk of error in the scoping of the audit report, particularly where businesses have been combined over time such that multiple nominees are used – all subsidiaries of different group entities.

Opinion

The required opinion is whether 'that nominee company has maintained throughout the period systems for the custody, identification and control of custody assets which were adequate; and included reconciliations at appropriate intervals between the records maintained (whether by the firm or the nominee company) and statements or confirmations from custodians or from the person who maintained the record of legal entitlement'. This is similar to, but not the same as, the audit opinion given on CASS 6 in the period which states whether 'the firm has maintained systems adequate to enable it to comply with the custody rules'.

You could probably say that systems that are 'adequate' to achieve compliance with the custody rules are therefore adequate for the custody, identification and control of custody assets. Logically then, a firm with a clean audit opinion on CASS 6 systems would also get a clean opinion on the nominee systems. Indeed, it could be argued that the nominee opinion is less demanding, though I would hesitate to say which particular rules are **not** required for the 'custody, identification and control of custody assets'. This is important when it comes to breaches. If the audit report identifies an exception against a particular CASS 6 rule, you might expect a similar exception in the nominee opinion, but:

- Only if the exception relates to assets held by the nominee; and
- That nominee is a subsidiary; and
- The rule in question relates to the 'custody, identification and control of custody assets'.

This could be a significant exercise to conduct. A firm may have some custody assets which are registered in the name of its own nominee: but also assets directly registered in client names; registered in the name of nominees which are controlled by affiliates or third parties; and, if the firm operates outside the UK, registered in the name of third parties or even the firm itself. I don't know of any regulated firm that logs whether a particular breach relates to assets held by a (subsidiary) nominee company, or otherwise.

A further complication is that breach instances with the same root cause are typically combined in the audit report (e.g. 'on 16 occasions the firm...'). If only four of those instances relate to assets held by a (subsidiary) nominee company, does this need to be separately identified in the appendix to the audit report?

One final twist on the opinion: the overall opinion (adverse/except for/clean) is based on an assessment of all of the findings and breaches. If only a proportion of those findings relate to nominee assets, the opinion on the nominee could be different to the opinion on CASS 6.

Template audit report

The requirement is to state **whether**, in the auditor's opinion, the nominee has maintained adequate systems. That opinion could be unmodified, modified 'except for' or even adverse – if the nominee did not maintain adequate systems. However, whilst it is clear in SUP 3.10.5R that this is an opinion, not an affirmation like CASS 5.5.4R, this is not reflected in the template audit report provided in SUP 3 Annex 1, which only provides for an unmodified opinion. To be clear, the template report on compliance with the rules provides alternative wording in square brackets:

In our opinion: [The firm has maintained] [Except for....the firm has maintained] [Because of....the firm did not maintain] systems adequate...

The template opinion on adequacy of nominee systems does not have these options. I do not believe this means that the auditor should give an unmodified opinion even where there are identified failures in the nominee controls or records, but the template is clearly inconsistent or wrong. Ironically, this a case of insufficient square brackets, by contrast to the central counterparty acknowledgement letter, which has unnecessary square brackets (see [LINK](#)). The illustrative reports in the FRC Standard 'Providing Assurance on Client Assets to the Financial Conduct Authority' only contains an unmodified opinion on nominee companies (Appendix 4).

Work required

Although the FRC CASS Standard does (erroneously) state that the auditor is required to give an opinion on 'rules relating to nominee companies' both throughout the period and at period end (para 129 (d) and (e)) no guidance is provided on the work required to support any opinion. I think I would take it that the work required to support a reasonable assurance opinion on the adequacy of systems to comply with CASS 6 rules is, in itself, sufficient to form an opinion on the adequacy of systems for the custody, identification and control of those custody assets which are registered under the nominee; with the proviso that any identified exceptions must be assessed to determine whether or not they apply to nominee-held assets within the population of custody assets as a whole.

Our (PwC) view is that where a regulated firm holds some or all custody assets registered in the name of a nominee which is a subsidiary of the firm:

- All identified breaches or control failures must be assessed to determine whether they relate to nominee assets;
- The aggregate impact of any such items must be assessed by the auditor to determine whether the overall opinion on the nominee systems is unmodified, modified 'except for' or adverse; and
- To facilitate this, the regulated firm should implement procedures within its breach capture process to flag whether individual incidents relate to nominee-registered assets.

It should be recognised that the level of work required to achieve this (both by the firm and the CASS auditor) may be more than has historically been the case.