

Chapter 3

Client categorisation

3.5 Professional clients

3.5.1 **R** A *professional client* is a client that is either a *per se professional client* or an *elective professional client*.

[Note: article 4(1)(11) of *MiFID*]

Per se professional clients

3.5.2 **R** Each of the following is a *per se professional client* unless and to the extent it is an *eligible counterparty* or is given a different categorisation under this chapter:

- (1) an entity required to be authorised or regulated to operate in the financial markets. The following list includes all authorised entities carrying out the characteristic activities of the entities mentioned, whether authorised by an *EEA State* or a third country and whether or not authorised by reference to a directive:
 - (a) a *credit institution*;
 - (b) an *investment firm*;
 - (c) any other authorised or regulated financial institution;
 - (d) an insurance company;
 - (e) a collective investment scheme or the management company of such a scheme;
 - (f) a pension fund or the management company of a pension fund;
 - (g) a commodity or commodity derivatives dealer;
 - (h) a local;
 - (i) any other institutional investor;
- (2) in relation to *MiFID* or equivalent *third country business* a large undertaking meeting two of the following size requirements on a company basis:
 - (a) balance sheet total of EUR 20,000,000;

- (b) net turnover of EUR 40,000,000;
 - (c) own funds of EUR 2,000,000;
- (3) in relation to business that is not *MiFID or equivalent third country business* a large undertaking meeting any of the following conditions:
- (a) a *body corporate* (including a *limited liability partnership*) which has (or any of whose *holding companies* or *subsidiaries* has) (or has had at any time during the previous two years) called up share capital or net assets of at least £5 million (or its equivalent in any other currency at the relevant time);
 - (b) an undertaking that meets (or any of whose *holding companies* or *subsidiaries* meets) two of the following tests:
 - (i) a balance sheet total of EUR 12,500,000;
 - (ii) a net turnover of EUR 25,000,000;
 - (iii) an average number of employees during the year of 250;
 - (c) a *partnership* or unincorporated association which has (or has had at any time during the previous two years) net assets of at least £5 million (or its equivalent in any other currency at the relevant time) and calculated in the case of a limited *partnership* without deducting loans owing to any of the *partners*;
 - (d) a trustee of a trust (other than an *occupational pension scheme*, *SSAS*, *personal pension scheme* or *stakeholder pension scheme*) which has (or has had at any time during the previous two years) assets of at least £10 million (or its equivalent in any other currency at the relevant time) calculated by aggregating the value of the cash and *designated investments* forming part of the trust's assets, but before deducting its liabilities;
 - (e) a trustee of an *occupational pension scheme* or *SSAS*, or a trustee or *operator* of a *personal pension scheme* or *stakeholder pension scheme* where the scheme has (or has had at any time during the previous two years):
 - (i) at least 50 members; and
 - (ii) assets under management of at least £10 million (or its equivalent in any other currency at the relevant time);
 - (f) a local authority or public authority.
- (4) a national or regional government, a public body that manages public debt, a central bank, an international or supranational institution (such as the World Bank, the IMF, the ECP, the EIB) or another similar international organisation;

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- (5) another institutional investor whose main activity is to invest in *financial instruments* (in relation to the *firm's MiFID or equivalent third country business*) or *designated investments* (in relation to the *firm's other business*). This includes entities dedicated to the securitisation of assets or other financing transactions.

[Note: first paragraph of section I of annex II to *MiFID*]

In relation to *MiFID or equivalent third country business* a local authority or a public authority is not likely to be a regional government for the purposes of ■ COBS 3.5.2 R (4). In the FSA's opinion, a local authority may be a *per se professional client* for those purposes if it meets the test for large undertakings in ■ COBS 3.5.2 R (2) .

3.5.3

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Elective professional clients

A *firm* may treat a *client* as an *elective professional client* if it complies with (1) and (3) and, where applicable, (2):

- (1) the *firm* undertakes an adequate assessment of the expertise, experience and knowledge of the *client* that gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the *client* is capable of making his own investment decisions and understanding the risks involved (the "qualitative test");
- (2) in relation to *MiFID or equivalent third country business* in the course of that assessment, at least two of the following criteria are satisfied:
 - (a) the *client* has carried out transactions, in significant size, on the relevant market at an average frequency of 10 per quarter over the previous four quarters;
 - (b) the size of the *client's financial instrument* portfolio, defined as including cash deposits and *financial instruments*, exceeds EUR 500,000;
 - (c) the *client* works or has worked in the financial sector for at least one year in a professional position, which requires knowledge of the transactions or services envisaged;
 (the "quantitative test"); and
- (3) the following procedure is followed:
 - (a) the *client* must state in writing to the *firm* that it wishes to be treated as a *professional client* either generally or in respect of a particular service or transaction or type of transaction or product;

- (b) the *firm* must give the *client* a clear written warning of the protections and investor compensation rights the *client* may lose; and
- (c) the *client* must state in writing, in a separate document from the contract, that it is aware of the consequences of losing such protections.

[Note: first, second, third and fifth paragraphs of section II.1 and first paragraph of section II.2 of annex II to *MiFID*]

3.5.4 **R** If the *client* is an entity, the qualitative test should be performed in relation to the *person* authorised to carry out transactions on its behalf.

[Note: fourth paragraph of section II.1 of annex II to *MiFID*]

3.5.5 **G** The fitness test applied to managers and directors of entities licensed under directives in the financial field is an example of the assessment of expertise and knowledge involved in the qualitative test.

[Note: fourth paragraph of section II.1 of annex II to *MiFID*]

3.5.6 **R** Before deciding to accept a request for re-categorisation as an *elective professional client* a *firm* must take all reasonable steps to ensure that the *client* requesting to be treated as an *elective professional client* satisfies the qualitative test and, where applicable, the quantitative test.

[Note: second paragraph of section II.2 of annex II to *MiFID*]

3.5.7 **G** An *elective professional client* should not be presumed to possess market knowledge and experience comparable to a *per se professional client*

[Note: second paragraph of section II.1 of annex II to *MiFID*]

3.5.8 **G** *Professional client* are responsible for keeping the *firm* informed about any change that could affect their current categorisation.

[Note: fourth paragraph of section II.2 of annex II to *MiFID*]

3.5.9 **R**

- (1) If a *firm* becomes aware that a *client* no longer fulfils the initial conditions that made it eligible for categorisation as an *elective professional client*, the *firm* must take the appropriate action.
- (2) Where the appropriate action involves re-categorising that client as a *retail client*, the *firm* must notify that *client* of its new categorisation.

[Note: fourth paragraph of section II.2 of annex II to *MiFID* and article 28(1) of the *MiFID implementing Directive*]