

Appendix 1

In this appendix underlining indicates new text and striking through indicates deleted text.

As a significant number of enhancements are being made to chapter 2 of the current COB Rules, this chapter is shown here as a new chapter and is not underlined or struck through in the usual manner.



The DFSA Rulebook

Conduct of Business Module

(COB)

1 INTRODUCTION

1.1 Application

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Guidance

1. An Authorised Firm may be able to rely on the Transitional Rules in chapter 10 of GEN for the purposes of complying with some of the provisions in this module. The Rules enable Authorised Firms to make a smooth transition to the new regime that came into force 1 July 2008 under rule-making instrument No. 56, following the DFSA's "Key Policy Review" outlined in Consultation Paper 52. ~~Examples of the provisions to which the Transitional Rules apply are the Client classification (Rule 2.3.3(1)), consent and notifications to be treated as a Market Counterparty (Rule 2.3.4), statements required to be included in marketing material (Rule 3.2.4(1)(c)) and requirements for Client Agreement and key information (Rule 3.2.2(1)(b)).~~
2. An Authorised Firm may be able to rely on the Transitional Rules in section 2.6 for the purposes of meeting the client classification requirements in chapter 2.

2 CLIENT CLASSIFICATION

2.1 Application

- 2.1.1** (1) This chapter applies, subject to Rule 2.1.2, to an Authorised Firm, which carries on, or intends to carry on, any Financial Service with or for a Person.
- (2) For the purposes of this chapter, a Person includes a Fund, pension fund or trust, even if it does not have a separate legal personality.

Exclusions

- 2.1.2** (1) This chapter does not apply to a Credit Rating Agency in so far as it carries on, or intends to carry on, the Financial Service of Operating a Credit Rating Agency.
- (2) This chapter does not apply to an Authorised Firm in so far as it carries on the activity described in GEN Rule 2.26.1, provided that no other Financial Service is carried on.
- (3) This chapter does not apply to an Authorised ISPV.

Guidance

1. The activity described in GEN Rule 2.26.1 is marketing of financial services and financial products which are offered in a jurisdiction outside the DIFC. Such marketing activities can be conducted by an Authorised Firm, which holds a Representative Office Licence, provided the financial services or financial products marketed by it are those offered by its head office or a member of its Group.
2. As a Representative Office conducting marketing activities of the kind described in GEN Rule 2.26.1 does not have a client relationship with a Person to whom it markets a financial service or financial product, the client classification requirements in this chapter do not apply to the firm with regard to that Person.
3. Other Authorised Firms can also conduct marketing activities, of the kind described in GEN Rule 2.26.1, under the exclusion in GEN Rule 2.26.2.

2.2 Overview

Guidance

1. This chapter sets out the manner in which an Authorised Firm is required to classify its Clients, as well as good practice it may follow. The scope of application of the Rulebook modules will vary depending on whether the Person with or for whom an Authorised Firm is carrying on Financial Services is classified as a Retail Client, Professional Client or Market Counterparty.

Risk based approach

2. The Rules in this chapter reflect the DFSA's risk based approach to regulation. Therefore, to achieve the underlying objective of client classification, which is to ensure that firms provide to their clients an appropriate level of regulatory protection, the Rules, for example:

- a. take into account the higher degree of knowledge and experience ('expertise') and resources available to certain institutional and wholesale clients (see Rule 2.3.4);
- b. take into account who primarily bears the risk associated with a particular type of a Financial Service (see Rule 2.3.5);
- c. take into account the type of Persons to whom a Financial Service is usually provided (see Rules 2.3.6, 2.3.7 and 2.3.8);
- d. provide flexibility for an Authorised Firm to rely on a client classification made by its head office or a Group member, provided risks associated with such reliance are effectively addressed (see Rules 2.4.4 and 3.3.4);
- e. provide flexibility for group-based Financial Services to be provided where risks associated with such services are effectively addressed (see Rule 2.4.5); and
- f. provide flexibility for look-through arrangements where reliance can be placed on expertise and resources available to a Client, such as at its Holding Company or controller level (see Rule 2.3.8(2)).

Types of clients

3. There are three types of Clients:
 - a. a Retail Client;
 - b. a Professional Client; or
 - c. a Market Counterparty.

However, a Person may be classified as a Professional Client in relation to one Financial Service or financial product, but a Retail Client in relation to another. Similarly, a Person classified as a Professional Client may be classified as a Market Counterparty in relation to some Financial Services or financial products but not others (see paragraphs 8 and 9 below).

Retail Clients

4. A Person who cannot be classified as a Professional Client or Market Counterparty in accordance with the Rules is required to be classified as a Retail Client (see Rule 2.3.2). If an Authorised Firm chooses to provide Financial Services to a Person as a Retail Client, it may do so by simply classifying that Person as a Retail Client without having to follow any further procedures as required for classifying Persons as Professional Clients or Market Counterparties.

Professional Clients

5. There are three routes through which a Person may be classified as a Professional Client:
 - a. 'deemed' Professional Clients under Rule 2.3.4. As these Persons have significant assets under their control, and, therefore, either possess, or have the resources to obtain, the necessary expertise to manage such assets, they can be classified as 'deemed' Professional Clients without having to meet any additional net asset and expertise criteria;

- b. 'service-based' Professional Clients under Rule 2.3.5 or Rule 2.3.6. Due to their inherent nature, certain Financial Services activities such as credit provided to an Undertaking for business purposes ('commercial credit') and advisory and arranging activities relating to corporate structuring and financing are generally provided to Persons with sufficient expertise to obtain such services or are of relatively low risk to the Client. Therefore, a Person to whom such a Financial Service is provided can be classified as a 'service-based' Professional Client; and
- c. 'assessed' Professional Clients under Rules 2.3.7 and 2.3.8. These Persons are either individuals or Undertakings which can be classified as a Professional Client only if they meet the specified net assets and expertise requirements set out in Rules 2.4.2 and 2.4.3.

Investment vehicles and family member joint account holders of individuals who are themselves Professional Clients can also be classified as Professional Clients where certain conditions are met – see Rule 2.3.7(2) and (3).

Market Counterparties

- 6. A 'deemed' Professional Client under Rule 2.3.4 may be classified as a Market Counterparty provided the Authorised Firm has complied with the procedures set out in Rule 2.3.9(2). When an Authorised Firm carries on Financial Services with a Market Counterparty, only a limited number of requirements in the Rulebook modules apply to such firms. This is because an Authorised Firm transacts with a Market Counterparty on an equal footing and, therefore, most of the client protection provisions in the Rulebook modules are not needed to protect such a party.
- 7. When an Authorised Firm carries on Financial Services with another Authorised Firm or a Regulated Financial Institution, such services would generally qualify as Financial Services that can be carried on with a Market Counterparty (provided the procedures in Rule 2.3.9(2) are met). Examples of such services include:
 - a. providing reinsurance or insurance management services to an insurer; and
 - b. providing one or more Financial Services of custody, managing assets, or fund administration services to a fund manager, collective investment fund or a pension fund.

Such activities would not attract most of the client protection provisions contained in the Rulebook modules for the reasons set out under item 6 above.

Multiple classifications

- 8. In some circumstances, an Authorised Firm may provide a Financial Service to a Person who qualifies under more than one category of Professional Client. For example, a Client to whom an Authorised Firm provides commercial credit or corporate structuring and financing advice or arranging credit, in the circumstances specified in Rule 2.3.5 or Rule 2.3.6, may also be a 'deemed' Professional Client under Rule 2.3.4. In such circumstances, an Authorised Firm can classify such a Person as a 'deemed' Professional Client, in which case the firm may also be able to classify that Client as a Market Counterparty following the procedures in Rule 2.3.9(2).
- 9. It is also possible that an Authorised Firm may provide a range of Financial Services to a single Client. If the Client can be classified as a Professional Client with regard to certain Financial Services (such as Providing Credit under the requirements in Rule 2.3.5, and

similarly providing corporate structuring and financing advice or arranging credit under Rule 2.3.6), and not so with regard to other Financial Services, an Authorised Firm needs to take care that the Client is appropriately and correctly classified with respect to each Financial Service. This may mean that the same Client may receive both Professional Client treatment with regard to some Financial Services and Retail Client treatment with regard to other Financial Services. Where a Client cannot be classified as a Professional Client with regard to some Financial Services, the Authorised Firm can only provide such services to the Client if it has a Retail Endorsement on its Licence.

Client classifications and Client Agreements

10. Rule 2.4.4 provides a degree of flexibility for an Authorised Firm which is a Branch operation or member of a Group to rely on client classifications made by its head office or any other branch of the same legal entity, or by a member of its Group. Where such reliance is placed, the Authorised Firm should be able to demonstrate to the satisfaction of the DFSA that the reliance is reasonable because the applicable requirements are substantially similar and, where this is not the case, any identified differences (i.e. gaps) are suitably addressed to enable the firm to meet its obligations relating to client classification under this chapter.
11. It is also possible that an Authorised Firm which is a member of a Group may have some Clients to whom it provides Financial Services as a Retail Client, whilst other Group members may provide Financial Services to the same Client as a Professional Client. While an Authorised Firm may rely on the client classifications made by a Group member under Rule 2.4.4, it is the responsibility of the firm to ensure that the correct classification is adopted by it for the purposes of the Financial Services it provides to the Client (see Rule 2.4.4). See also Rule 3.3.4, which provides a degree of flexibility for an Authorised Firm which is a Branch to rely on a Client Agreement made by its head office or any other branch of the same legal entity, or by a member of the Group, provided the requirements in that Rule are met.

Group clients

12. Rule 2.4.5 is designed to provide a greater degree of flexibility to an Authorised Firm providing Financial Services to a Client in a Group context, where more than one member of the Group may be providing Financial Services which form a bundle of services. Each Group may have different arrangements to provide a number of services to a Client. Depending on the nature of the arrangement the Group adopts, and the Financial Services involved, risks associated with such arrangements could also differ. Therefore, Rule 2.4.5 sets out the outcomes which need to be achieved by an Authorised Firm where it participates in a Group arrangement under which a bundle of Financial Services is provided to a Client by different members within its Group. See also Rule 3.3.4, which provides a degree of flexibility for an Authorised Firm participating in an arrangement under which a bundle of Financial Services is provided to a Client where reliance can be made on a Client Agreement executed by a Group member, provided the requirements in that Rule are met.

Transitional Rules

13. Section 2.6 contains provisions designed to enable Authorised Firms to make a smooth transition to the new client classification regime that came into force on 1 April 2015. These Rules, among other things:
 - a. keep in force the client classifications made under the old client classification regime for the Financial Services that were provided to those Clients under that regime;
 - b. provide for the increased asset threshold of \$1 million to come into effect on 1 April 2016; and

- c. retain the asset threshold at \$500,000 until 1 April 2016.

2.3 Types of Clients

- 2.3.1** (1) An Authorised Firm must, before carrying on a Financial Service with or for a Person, classify that Person as a:

- (a) Retail Client;
- (b) Professional Client; or
- (c) Market Counterparty,

in accordance with the requirements in this chapter.

- (2) An Authorised Firm may classify a Person as a different type of a Client for different Financial Services or financial products that are to be provided to such a Client.
- (3) If an Authorised Firm is aware that a Person ('the agent'), with or for whom it is intending to carry on a Financial Service is acting as an agent for another Person ('the principal') in relation to the service then, unless the agent is another Authorised Firm or a Regulated Financial Institution, the Authorised Firm must treat the principal as its Client in relation to that service.
- (4) If an Authorised Firm intends to provide any Financial Service to a trust, it must, unless otherwise provided in the Rules, treat the trustee of the trust, and not the beneficiaries of the trust, as its Client.

Guidance

- 1. When a Person becomes a Client of an Authorised Firm is a question of fact that needs to be addressed by the firm in light of the nature of the relevant Financial Service (or financial product) involved, and the relations and interactions which the firm has with that Person. For instance, in certain types of Financial Services (such as corporate advisory services), a number of conversations (such as marketing and promotional activities) may occur between an Authorised Firm and a potential client before it may appear to the firm on a reasonable basis that the Person is likely to obtain a Financial Service from the firm, at which point a client classification is required.
- 2. Given the many different circumstances in which interactions between a potential client and an Authorised Firm take place, it is not possible to include a more specific requirement than the current provision which requires the client classification to occur "before" a firm provides a Financial Service to a Person – see Rule 2.3.1(1). This provides an Authorised Firm flexibility to determine when exactly it would be appropriate for the firm to undertake client classification.

3. The DFSA expects Authorised Firms to adopt practices which are consistent with the underlying intent of the client classification provisions, which is to provide Clients an appropriate level of regulatory protection in light of the resources and expertise available to such Clients. Therefore, as soon as it is reasonably apparent that a potential customer is likely to obtain a Financial Service from the firm, it would need to undertake the client classification process relating to that customer (unless such a customer is classified as a Retail Client for the purposes of the Rules – see Rule 2.3.2).
4. For example, an Authorised Firm is not expected to undertake advising or arranging activities relating to a Financial Service or financial product which is suited to Professional Clients (such as complex derivatives) with a potential customer without having a reasonable basis to consider that such a customer has sufficient knowledge and experience relating to the relevant service or product. While a formal client classification may not be needed at the early stages of interaction with a potential customer, a firm is expected to form a reasonable view about the professional status of a potential customer when exposing such a customer to Financial Services or financial products (such as investments in a Qualified Investor Fund) which are intended for Professional Clients.
5. Rule 2.3.1(2) allows an Authorised Firm to classify a Client as a Retail Client in respect of some Financial Services and a Professional Client in respect of other Financial Services. For example, a Client classified as a ‘service-based’ Professional Client under Rule 2.3.5 for the Financial Service of Providing Credit may not necessarily meet the criteria to be classified as an ‘assessed’ Professional Client under Rule 2.3.7 or Rule 2.3.8 in respect of any other Financial Service to be provided to that Client. Therefore, such a Client would need to be classified as a Retail Client with respect to Financial Services other than Providing Credit.

Retail Clients

- 2.3.2** An Authorised Person must classify as a Retail Client any Person who is not classified as a Professional Client or a Market Counterparty.

Professional Clients

- 2.3.3** (1) An Authorised Firm may classify a Person as a Professional Client if that Person:
- (a) meets the requirements to be:
 - (i) a “deemed” Professional Client pursuant to Rule 2.3.4;
 - (ii) a “service-based” Professional Client pursuant to either Rule 2.3.5 or Rule 2.3.6; or
 - (iii) an “assessed” Professional Client pursuant to either Rule 2.3.7 or Rule 2.3.8; and
 - (b) has not opted-in to be classified as a Retail Client in accordance with the requirements in Rule 2.4.1.
- (2) If an Authorised Firm becomes aware that a Professional Client no longer fulfils the requirements to remain classified as a Professional Client, the Authorised Firm must, as soon as possible, inform the Client that this is the

case and the measures that are available to the firm and the Client to address that situation.

Guidance

The measures referred to in Rule 2.3.3(2) may include classifying the Client as a Retail Client with respect to any future Financial Services to be provided to that Client or, if the firm does not have a Retail Endorsement, discontinuing the provision of Financial Services to that Client.

'Deemed' Professional Clients

- 2.3.4** (1) For the purposes of Rule 2.3.3(1)(a)(i), a Person is a 'deemed' Professional Client if that Person is:
- (a) a supranational organisation whose members are either countries, central banks or national monetary authorities;
 - (b) a properly constituted government, government agency, central bank or other national monetary authority of any country or jurisdiction;
 - (c) a public authority or state investment body;
 - (d) an Authorised Market Institution, Regulated Exchange or regulated clearing house;
 - (e) an Authorised Firm, a Regulated Financial Institution or the management company of a regulated pension fund;
 - (f) a Collective Investment Fund or a regulated pension fund;
 - (g) a Large Undertaking as specified in (2);
 - (h) a Body Corporate whose shares are listed or admitted to trading on any exchange of an IOSCO member country;
 - (i) any other institutional investor whose main activity is to invest in financial instruments, including an entity dedicated to the securitisation of assets or other financial transactions;
 - (j) a trustee of a trust which has, or had during the previous 12 months, assets of at least \$10 million; or
 - (k) a holder of a licence under the Single Family Office Regulations with respect to its activities carried on exclusively for the purposes of, and only in so far as it is, carrying out its duties as a Single Family Office.
- (2) A Person is a Large Undertaking if it met, as at the date of its most recent financial statements, at least two of the following requirements:
- (a) it has a balance sheet total of at least \$20 million;

- (b) it has a net annual turnover of at least \$40 million; or
 - (c) it has own funds or called up capital of at least \$2 million.
- (3) In (2):
- (a) a 'balance sheet total' means the aggregate of the amounts shown as assets in the balance sheet before deducting both current and long-term liabilities;
 - (b) 'own funds' mean cash and investments as shown in the balance sheet; and
 - (c) 'called up capital' means all the amounts paid-up on allotted shares, less any amounts owing on allotted shares.

Guidance

1. Although an Authorised Firm is not required to undertake a detailed assessment of a 'deemed' Professional Client's expertise or net assets (as is required in the case of an 'assessed' Professional Client), a firm still needs to have a reasonable basis for classifying a Person as falling within the list of 'deemed' Professional Clients in Rule 2.3.4(1) or (2). For example, in order to verify whether a trustee of a trust can be classified as a 'deemed' Professional Client under Rule 2.3.4(1)(j), an Authorised Firm should obtain a verified copy of the most recent balance sheet of the relevant trust.
2. An individual trustee on the board of a trust where the trust has at least \$10 million assets under its control can qualify as a 'deemed' Professional Client under Rule 2.3.4(1)(j) but only in relation to that particular trust.

'Service-based' Professional Clients**Guidance**

Rule 2.3.5 and Rule 2.3.6 each set out different circumstances in which a Person can be classified as a 'service-based' Professional Client. The professional status allowed under these two 'service-based' Professional Client categories can only be used for those two Financial Services and not for any other Financial Service provided to the same Client. If such a Client also obtains other Financial Services from the same firm, unless the Client can qualify either as a 'deemed' or 'assessed' Professional Client, that Client will need to be classified as a Retail Client for those other Financial Services.

- 2.3.5** (1) For the purposes of Rule 2.3.3(1)(a)(ii), a Person is a 'service-based' Professional Client if:
- (a) the Financial Service provided to that Person is Providing Credit;
 - (b) the Person is an Undertaking; and
 - (c) the Credit Facility in question is provided for use in the business activities of:
 - (i) the Person;

- (ii) a controller of the Person;
 - (iii) any member of the Group to which the Person belongs; or
 - (iv) a joint venture of a Person referred to in (i) – (iii).
- (2) In (1)(c)(ii), a controller is an individual who:
- (a) owns a majority of the shares of the Undertaking;
 - (b) is able to appoint or remove a majority of the board members of the Undertaking; or
 - (c) controls a majority of the voting rights of the Undertaking (or that of a Holding Company of the Undertaking).

Guidance

1. Rule 2.3.5(1)(c) enables an Authorised Firm to classify an Undertaking as a Professional Client for the purposes of Providing Credit for businesses purposes, not only for the Undertaking itself, but also for its related entities (such as a controller or member of its Group) as specified in that Rule, provided that the Undertaking has not opted-in to be classified as a Retail Client.
2. It is possible that an Undertaking obtaining credit may also fall within the category of a ‘deemed’ Professional Client under Rule 2.3.4 – see, for example, a Large Undertaking under Rule 2.3.4(2). An Authorised Firm may Provide Credit to such a Person without having to meet the requirements in Rule 2.3.5.
3. Joint ventures are generally contractual arrangements under which parties contribute their assets and/or expertise to develop or to undertake specified business activities. An Undertaking can be set up by a number of joint venture partners for obtaining credit for use in the ordinary course of their joint venture business. Although joint venture partners would themselves not have a controlling interest in the joint venture, as credit is obtained for use in the joint venture business, they have the benefit of the professional client status available to the Undertaking under Rule 2.3.5.
4. While an Authorised Firm is not required to undertake a detailed assessment of a ‘service-based’ Professional Client’s expertise or net assets (as required in the case of an ‘assessed’ Professional Client), a firm still needs to have a reasonable basis for classifying a Person as falling within the circumstances specified in this Rule (or Rule 2.3.6). For example, to verify that an Undertaking is obtaining credit for use in the business of its Holding Company or another member of its Group, a firm would need some documentation to demonstrate the Group member relationship. Such documents may include a diagram of the Group structure and copies of certificates of incorporation and shareholdings of the relevant companies.

- 2.3.6** (1) For the purposes of Rule 2.3.3(1)(a)(ii), a Person is a ‘service-based’ Professional Client if:
- (a) the Financial Service provided to that Person is “Advising on financial products or credit” or “Arranging credit or deals in Investments”; and

- (b) the service in (a) is provided for the purposes of 'corporate structuring and financing'.
- (2) In (1), 'corporate structuring and financing':
 - (a) includes:
 - (i) providing advice relating to an acquisition, disposal, structuring, restructuring, financing or refinancing of a corporation or other legal entity; or
 - (ii) arranging credit for a purpose referred to in (i); and
 - (b) excludes any advice on financial products or arranging of credit or deals in Investments given to an individual for the purposes of, or in connection with, the management of that individual's investments.

Guidance

1. This Rule enables an Authorised Firm to classify a Person obtaining advice or arranging credit for the purposes of corporate structuring and financing as a Professional Client based on the nature of such activities, which are generally sought by Persons with greater expertise and resources than Retail Clients. Such advice and arranging occurs in the context of takeovers and merger activities and capital raising activities of companies, including any Initial Public Offerings or other offers of securities for capital raising purposes.
2. If a Client seeking corporate structuring and financing services is also a Person who falls within the category of a 'deemed' Professional Client under Rule 2.3.4, an Authorised Firm may provide to such a Person those services without having to meet the requirements in Rule 2.3.6.
3. Under Rule 2.3.6(2)(b), any advisory and arranging services given to an individual who is a wealth management Client for the purposes of their investment activities or portfolio management are excluded because such Clients are not necessarily Professional Clients. Therefore, for such a Client to qualify as a Professional Client, he would need to be an 'assessed' Professional Client, which requires an assessment of his net assets and expertise against the requirements in Rules 2.4.2 and 2.4.3.

'Assessed' Professional Clients**Individuals**

- 2.3.7** (1) For the purposes of Rule 2.3.3(1)(a)(iii), an individual is an 'assessed' Professional Client if:
- (a) the individual has net assets of at least \$1 million calculated in accordance with Rule 2.4.2; and
 - (b) either:

- (i) the individual is, or has been, in the previous two years, an Employee in a relevant professional position of an Authorised Firm or a Regulated Financial Institution; or
 - (ii) the individual appears, on reasonable grounds, to have sufficient experience and understanding of relevant financial markets, products or transactions and any associated risks, following the analysis set out in Rule 2.4.3.
- (2) An Authorised Firm may classify any legal structure or vehicle, such as an Undertaking, trust or foundation, which is set up solely for the purpose of facilitating the management of an investment portfolio of an individual assessed as meeting the requirements in (1) as a Professional Client.
- (3) An Authorised Firm may also classify as a Professional Client another individual (the “joint account holder”) who has a joint account with an individual assessed as meeting the requirements in (1) (the “primary account holder”) if:
 - (a) the joint account holder is a family member of the primary account holder;
 - (b) the account is used for the purposes of managing investments for the primary account holder and the joint account holder; and
 - (c) the joint account holder has confirmed in writing that investment decisions relating to the joint account are generally made for, or on behalf of, him by the primary account holder.
- (4) In (3), a ‘family member’ of the primary account holder is:
 - (a) his spouse;
 - (b) his children and step-children, his parents and step-parents, his brothers and sisters and his step-brothers and step-sisters; and
 - (c) the spouse of any individual within (b).

Guidance

1. Under Rule 2.6.3, the net asset test referred to in Rule 2.3.7(1)(a) remains \$500,000 until 1 April 2016.
2. An individual can generally only be classified as a Professional Client if he meets the requirements in Rule 2.3.7(1) or (3). This is because all the other criteria relevant to Professional Clients in this chapter apply to Undertakings and not to individuals, with the possible exception of a trustee of a trust under Rule 2.3.4(j).
3. An individual classified as a Professional Client may operate a joint account with more than one family member. Under the general principle of interpretation that the singular includes the plural, provided each such family member meets the requirements set out in Rule 2.3.7(3), they can all be classified as Professional Clients.

4. A legal structure or vehicle of a Professional Client, which is itself classified as a Professional Client under Rule 2.3.7(2), does not have a right to opt-in as a Retail Client, as that right belongs to the Professional Client for whose purposes the vehicle is set up.
5. A family member of a Professional Client classified as a Professional Client under Rule 2.3.7(3) also does not per se have a right to opt-in to be classified as a Retail Client with regard to the operation of the joint account. However, such an individual has the right to withdraw his confirmation given under Rule 2.3.7(3)(c) to have decisions on behalf of him made by the Professional Client who is the primary account holder of the joint account. An Authorised Firm must ensure that once such a withdrawal is made, the withdrawing individual is no longer classified as a Professional Client. The joint account arrangements would also need to be reviewed as the primary account holder would no longer have the power to make decisions on behalf of the withdrawing individual.
6. In the case of a joint account operated by a primary account holder who is a parent or legal guardian of a minor, the procedures for obtaining the formal consent referred to in Rule 2.3.7(3)(c) would generally not be required, as such parent or guardian would have the authority to act for the minor where he is the joint account holder.

Undertakings

- 2.3.8** (1) For the purposes of Rule 2.3.3(1)(a)(iii), an Undertaking is an ‘assessed’ Professional Client if the Undertaking:
- (a) has own funds or called up capital of at least \$1 million; and
 - (b) appears, on reasonable grounds, to have sufficient experience and understanding of relevant financial markets, products or transactions and any associated risks, following the analysis set out in Rule 2.4.3.
- (2) An Authorised Firm may also classify an Undertaking as a Professional Client if the Undertaking has:
- (a) a controller;
 - (b) a Holding Company;
 - (c) a Subsidiary; or
 - (d) a joint venture partner,
- who meets the requirements to be classified as an ‘assessed’ Professional Client pursuant to either Rule 2.3.7(1)(a) and (b)(ii) or Rule 2.3.8(1) as applicable, or a ‘deemed’ Professional Client pursuant to Rule 2.3.4(1).
- (3) In this Rule:
- (a) the terms ‘own funds’ and ‘called up capital’ in (1)(a) have the meaning given under Rule 2.3.4(3)(b) or (c) as the case may be; and

- (b) the term 'controller' in (2)(a) means an individual who meets the criteria in Rule 2.3.5(2).

Guidance

1. Under Rule 2.6.3, the asset test referred to in Rule 2.3.8(1)(a) remains \$500,000 until 1 April 2016.
2. Where an Authorised Firm proposes to classify an Undertaking as a Professional Client under (2), the firm must assess whether the Person on whom reliance is placed, i.e. a Person referred to in (2)(a) to (d) as is relevant, meets the Professional Client criteria, unless that Person falls within a category of 'deemed' Professional Client.
3. Where an Undertaking is set up by partners in a joint venture for the purposes of their joint venture, the Undertaking itself can be treated as a Professional Client provided a joint venture partner meets the Professional Client criteria (see Guidance paragraph 3 under Rule 2.3.5 for a description of a joint venture). To be able to rely on a joint venture partner's Professional Client status, such a partner should generally be a key decision maker with respect to the business activities of the joint venture, and not just a silent partner.

Market Counterparties

- 2.3.9** (1) An Authorised Firm may classify a Person as a Market Counterparty if:
- (a) that Person is either:
 - (i) a 'deemed' Professional Client pursuant to Rule 2.3.4; or
 - (ii) an 'assessed' Professional Client pursuant to Rule 2.3.8(2)(b) which is wholly owned by a Holding Company that is a 'deemed' Professional Client pursuant to Rule 2.3.4(1)(g) or (h); and
 - (b) the requirements in (2) have been met.
- (2) For the purposes of (1)(b), an Authorised Firm must, before classifying a Person as a Market Counterparty, ensure that:
- (a) the Person has been given a prior written notification of the classification as a Market Counterparty; and
 - (b) that Person has not requested to be classified otherwise within the period specified in the notice.
- (3) The notification in (2)(a) may be given in respect of particular Financial Services or Transactions or in respect of all Financial Services and Transactions.
- (4) The notification in (2)(a) need only be given:
- (a) in the case of a Fund, either to the Fund or its Fund Manager; and

- (b) in the case of a pension fund, either to such fund or its management company.

Guidance

When an Authorised Firm carries on, or provides or obtains, Financial Services with or from another Authorised Firm or a Regulated Financial Institution, as those entities are 'deemed' Professional Clients under Rule 2.3.4(1), they could be classified as Market Counterparties, provided the procedures set out in Rule 2.3.9(2) are complied with. Examples of such services are:

- a. providing reinsurance or insurance management services to an insurer; and
- b. providing one or more Financial Services of custody, managing assets, or fund administration services to a Fund Manager of a Collective Investment Fund or a pension fund.

2.4 Procedures relating to client classification**Option for a Professional Client to be classified as a Retail Client**

- 2.4.1** (1) For the purpose of Rule 2.3.3(1)(b), an Authorised Firm must, subject to (4), when first establishing a relationship with a Person as a Professional Client, inform that Person in writing of:
 - (a) that Person's right to be classified as a Retail Client;
 - (b) the higher level of protection available to Retail Clients; and
 - (c) the time within which the Person may elect to be classified as a Retail Client.
- (2) If the Person does not expressly elect to be classified as a Retail Client within the time specified by the Authorised Firm, the Authorised Firm may classify that Person as a Professional Client.
- (3) If a Person already classified as a Professional Client by an Authorised Firm expressly requests the Authorised Firm to be re-classified as a Retail Client, the Authorised Firm must, subject to (4), re-classify such a Person as a Retail Client.
- (4) If an Authorised Firm does not provide Financial Services to Retail Clients, it must inform the Person of this fact and any relevant consequences.

Guidance

- 1. The obligation in Rule 2.4.1(1) applies to an Authorised Firm when it first provides, or intends to provide, a Financial Service to a Professional Client.
- 2. Once an Authorised Firm has first classified a Person as a Professional Client, under the procedures in Rule 2.3.3(1), that Professional Client has a right at any subsequent time to

ask, under Rule 2.4.1(3), to be re-classified as a Retail Client to obtain a higher level of protection. Although the right to ask the firm to be re-classified as a Retail Client is available to the Professional Client, as a matter of good practice:

- a. the firm should also periodically review whether the circumstances relating to the particular Client remain the same; and
 - b. if the firm becomes aware of any circumstances which would warrant a re-classification of the Client, initiate the process with the Client to give that Client a more appropriate classification.
3. Where an existing Professional Client is offered a new Financial Service or new financial product, a re-classification might be appropriate if:
- a. the new Financial Service or financial product is substantially different to those previously offered to that Client; and
 - b. the Client's experience and understanding appears not to extend to the new Financial Service or financial product.
4. An Authorised Firm cannot provide Financial Services to a Retail Client unless it has a Retail Endorsement on its Licence. However, such a firm may refer to another appropriately licensed firm any Person who elects to opt-in as a Retail Client.

Assessment of net assets

2.4.2 An Authorised Firm, when calculating net assets of an individual for the purposes of the requirement under Rule 2.3.7(1)(a):

- (a) must exclude the value of the primary residence of that Person; and
- (b) may include any assets held directly or indirectly by that Person.

Guidance

1. The reference to "assets held directly or indirectly" is designed to include assets held by direct legal ownership, by beneficial ownership (for example, as a beneficiary in a trust), or by both legal and beneficial ownership. Such assets may be held, for instance, through a special purpose or personal investment vehicle, a foundation, or the like. Similarly, any real property held subject to an Islamic mortgage, where the lender has the legal title to the property, may be counted as indirectly held property of a Client, less the amount owing on the mortgage, where it is not a primary residence.
2. As the test is to determine the net assets (not gross assets) of an individual, any mortgages or other charges held over the property to secure any indebtedness of the individual should be deducted from the value of the assets.
3. An individual's primary residence is excluded from the calculation of their net assets. If an individual who is an expatriate has a primary residence in his home country, such a residence should not generally be counted for the purposes of meeting the net asset test, particularly if the current residence in their host country is rented. However, if the current residence in the host country is owned by the individual, then that may be treated as their primary residence and the value of the residence in the home country of the individual

may be counted for the purposes of meeting the net asset test, provided there is sufficient evidence of ownership and an objective valuation of the relevant premises.

4. An Authorised Firm should be able to demonstrate that it has objective evidence of the ownership and valuation of any assets taken into account for the purposes of meeting the net asset test.

Assessment of knowledge and experience

- 2.4.3** (1) For the purpose of the analysis required under Rules 2.3.7(1)(b)(ii) and 2.3.8(1)(b), an Authorised Firm must include, where applicable, consideration of the following matters:
- (a) the Person's knowledge and understanding of the relevant financial markets, types of financial products or arrangements and the risks involved either generally or in relation to a proposed Transaction;
 - (b) the length of time the Person has participated in relevant financial markets, the frequency of dealings and the extent to which the Person has relied on professional financial advice;
 - (c) the size and nature of transactions that have been undertaken by, or on behalf of, the Person in relevant financial markets;
 - (d) the Person's relevant qualifications relating to financial markets;
 - (e) the composition and size of the Person's existing financial investment portfolio;
 - (f) in the case of credit or insurance transactions, relevant experience in relation to similar transactions to be able to understand the risks associated with such transactions; and
 - (g) any other matters which the Authorised Firm considers relevant.
- (2) Where the analysis is being carried out in respect of an Undertaking, the analysis must be applied, as appropriate, to those individuals who are authorised to undertake transactions on behalf of the Undertaking.

Guidance

Generally, an Authorised Firm may consider a Person to have relevant experience and understanding where such a Person:

- a. has been involved in similar transactions in a professional or personal capacity sufficiently frequently to give the Authorised Firm reasonable assurance that the Person is able to make decisions of the relevant kind, understanding the type of risks involved; or
- b. is found to be acting, in relation to the particular transaction involved, in reliance on a recommendation made by an Authorised Firm or Regulated Financial Institution.

Reliance on a classification made elsewhere

- 2.4.4** (1) This Rule applies to an Authorised Firm which is a Branch or is a member of a Group.
- (2) An Authorised Firm may, subject to (3), rely on a client classification made, if it is a Branch, by its head office or any other branch of the same legal entity, or if it is a member of a Group, by any other member of its Group, if it has reasonable grounds to believe that such a client classification is substantially similar to the client classification required under this chapter.
- (3) If any gaps are identified between the requirements applicable to the Authorised Firm under this chapter and the requirements under which the client classification is carried out by another entity referred to in (2), the Authorised Firm may only rely on such a client classification if it has effectively addressed the identified gaps.

Guidance

1. Generally, an Authorised Firm relying on this Rule should be able to demonstrate to the DFSA the due diligence process that it had undertaken to assess whether the client classification made by its head office or other branch of the same legal entity or a member of its Group substantially meets the client classification requirements in this chapter and, if any gaps are identified, how those gaps are effectively addressed. See Rule 2.5.3, which requires the provision of unrestricted access to records for demonstrating to the DFSA due compliance with this Rule.
2. If an Authorised Firm wishes to use any client classification undertaken by any third party other than its head office or another branch of the same legal entity, or a member of its Group, such an arrangement is generally treated as an outsourcing arrangement. Therefore, the Authorised Firm would need to meet the GEN requirements relating to outsourcing.

Group clients

- 2.4.5** (1) This Rule applies to an Authorised Firm which:
- (a) is a member of a Group; and
 - (b) provides to a Client one or more Financial Services where the services provided by the firm form part of a bundle of financial services provided to that Client by it and its Group members.
- (2) An Authorised Firm referred to in (1) must ensure that:
- (a) the client classification it adopts for any Financial Service which it provides to the Client is both consistent with the requirements in this chapter and appropriate for the overall bundle of financial services provided to that Client;

- (b) the Client has a clear understanding of the arrangement under which Financial Services are provided to the Client by the Authorised Firm in conjunction with the other members of the Group; and
- (c) any risks arising from the arrangements referred to in (b) are identified and appropriately and effectively addressed.

Guidance

1. The provision of a 'bundle' of financial services may involve different arrangements within different Groups. The DFSA considers that the provision of a 'bundle' of financial services occurs where:
 - a. several members of a Group provide discrete stand-alone financial services to a single Client but do so as part of providing a complete suite of related financial services to that Client. An example would be where one member of the Group gives investment advice to the Client, another member of the Group executes the transaction (based on the advice) relating to a financial product and yet another member of the Group is the issuer of that financial product;
 - b. several members of a Group provide different aspects of the same financial service to a single Client; or
 - c. the bundle comprises any combination of both (a) and (b).
2. A bundle of financial services referred to in 1 above can be project specific. An example is where a number of members within a Group providing discrete aspects of expertise that go to facilitate a merger and acquisition project of a Client. In such a situation, different members of the Group could prepare and provide:
 - a. advice relating to a proposed restructure;
 - b. advice relating to financing of the restructure; and
 - c. arranging credit for financing the restructure.
3. In order to provide flexibility for Authorised Firms which are members of a Group to provide such bundles of financial services to their Clients in a manner that suits the Client's needs and the nature of the service, Rule 2.4.5 sets out the overarching objectives that must be achieved (i.e. outcome based requirements), rather than any detailed requirements. This Rule goes beyond a simple reliance on a 'client classification' made by another member of a Group under Rule 2.4.4.
4. Depending on the nature of the arrangement under which Group members choose to provide to the same Client a bundle of Financial Services, and the nature of the Financial Services involved, the risks associated with such arrangements may vary. Some of the common risks that could arise, and therefore would need to be addressed, include:
 - a. conflicting legal requirements applicable to the provision of the relevant Financial Services, particularly if the members of the Group are located in different jurisdictions; and
 - b. a Client not being able to identify clearly the actual service provider or providers and resulting legal exposure to the Client that may arise for all members of the Group. To address this risk, it is good practice for each member of the Group to set out in

- writing (e.g. in the client agreement) the services for which it is responsible. See also Rule 3.3.4(3)(b) for the firm's obligations.
5. GEN section 5.3 sets out the systems and controls requirements that apply to all Authorised Firms. In order to meet those GEN requirements, an Authorised Firm relying on Rule 2.4.5 should consider, at a minimum, having the following:
 - a. a clear description of the Group arrangement under which a bundle of financial services is provided – such as which member of the Group is responsible for which aspects of the bundle of Financial Service provided to the Client, or alternatively, that collective responsibility would be assumed by all or some members of the Group;
 - b. how the Client is classified for the purposes of the relevant Financial Service provided by the firm;
 - c. identification of where records relating to client classification and Financial Services provided to the Client are maintained;
 - d. which firm, if any, is responsible for the overall bundle of financial services and, if this is not the case, how the accountability for the financial services is apportioned among members within the Group;
 - e. a client agreement (whether entered into by the Authorised Firm or by a member of its Group under Rule 3.3.4) which adequately covers all the financial services provided to the Client, including those provided by the firm; and
 - f. what the identified risks are and how they are being addressed.
 6. See Rule 2.5.3 which requires the provision of unrestricted access to records for demonstrating to the DFSA due compliance with this Rule.
 7. Rule 2.4.5 is not expressly extended to a Branch as it is not a separate legal entity, and hence would generally have greater flexibility than Group members providing a bundle of services when providing Financial Services to a Client in conjunction with its head office or any other branch of the same legal entity. However, to the extent a Branch operates as a stand-alone entity, it may use the same outcome-based approach reflected in Rule 2.4.5 where it provides any Financial Services to a Client in conjunction with its head office or other branches of the same legal entity.

2.5 Record keeping

2.5.1 An Authorised Firm must keep records of:

- (1) the procedures which it has followed under the Rules in this chapter, including any documents which evidence the Client's classification; and
- (2) any notice sent to the Client under the Rules in this chapter and evidence of despatch.

- 2.5.2** (1) The records in Rule 2.5.1 must be kept by an Authorised Firm for at least six years from the date on which the business relationship with a Client has ended.
- (2) In complying with (1), an Authorised Firm may, if the date on which the business relationship with the Client ended is unclear, treat the date of the completion of the last Transaction with the Client as the date on which the business relationship ended.
- 2.5.3** (1) Without limiting the generality of the record keeping requirements applicable to an Authorised Firm, an Authorised Firm must, where it relies on Rule 2.4.4 and Rule 2.4.5, ensure that the DFSA has unrestricted access to all the records required for the firm to be able to demonstrate to the DFSA its compliance with the applicable requirements, including any records maintained by or at its head office or any other branch of the same legal entity, or a member of its Group.
- (2) An Authorised Firm must notify the DFSA immediately if, for any reason, it is no longer able to provide unrestricted access to records as required under (1).

Guidance

1. See GEN Rules 5.3.24 – 5.3.27 for the requirements relating to record keeping. These Rules require, among other things, that Authorised Firms be able to produce records, however kept, within a reasonable period not exceeding three business days.
2. If an Authorised Firm is aware of any restrictions that prevent it from being able to produce relevant records relating to a client classification referred to in Rule 2.5.3(1), that firm would need to undertake its own client classifications.

2.6 Transitional Rules

- 2.6.1** An Authorised Firm may continue to treat a Person as a Retail Client, Professional Client, or Market Counterparty, as the case may be, without having to re-classify the Person under section 2.3:
- (a) where the Authorised Firm was treating that Person as such a Client (including under a waiver or modification in force) immediately prior to 1 April 2015; and
 - (b) with regard to the Financial Services carried on with or for that Client prior to that date.
- 2.6.2** Without limiting the generality of Rule 2.6.1, and for the avoidance of doubt, any client classification adopted, Transaction carried on with or for a Client, or Client Agreement entered into with a Client for the purposes of section 3.3, prior to 1 April 2015, remains in force on and after that date.

Guidance

1. The introduction of the new client classification regime does not trigger the need to re-classify existing Clients. However, with regard to an existing Client who has been grandfathered under Rule 2.6.1, the need for a re-classification may subsequently arise in a number of circumstances such as those set out in paragraphs 2, 3 and 4.
2. Where a Professional Client grandfathered under Rule 2.6.1 subsequently requests to opt-in as a Retail Client under Rule 2.4.1(3), the Authorised Firm will need to re-classify that Client in accordance with the requirements in that Rule.
3. Where a grandfathered Client wishes to obtain a new Financial Service after the new regime came into force, an Authorised Firm will not be able to rely on the existing client classification relating to that Client in respect of the new Financial Service. This is because Rule 2.6.1 only applies in respect of the Financial Services carried on with or for a Client before the new regime came into force. Therefore, the firm will need to make a new classification relating to such a Client in respect of the new Financial Service and do so under the new client classification regime.
4. If an Authorised Firm becomes aware that a grandfathered professional client no longer fulfils the requirements to remain classified as a Professional Client, it will need to comply with the requirements in Rule 2.3.3(2).

- 2.6.3** (1) For the purposes of classifying a Person as an ‘assessed’ Professional Client under either Rule 2.3.7 or Rule 2.3.8, the reference to \$1 million in each of Rules 2.3.7(1)(a) and 2.3.8(1)(a) is to be read as a reference to \$500,000 on and before 31 March 2016.
- (2) An Authorised Firm may continue to treat a Person as an ‘assessed’ Professional Client in reliance on the lower asset threshold specified in (1) on and after 1 April 2016 provided:
- (a) it is in respect of the Financial Services carried on with or for the Client prior to that date; and
 - (b) the firm continues to ensure that all the other applicable requirements in this chapter are met in respect of that Client.

3 CORE RULES - INVESTMENT BUSINESS, ACCEPTING DEPOSITS, PROVIDING CREDIT AND PROVIDING TRUST SERVICES

...

3.3 Key information and Client Agreement

...

3.3.2 (1) Subject to (2), an Authorised Firm must not carry on a Financial Service with or for a Person unless:

(a) there is a Client Agreement containing the key information specified in App2 which is either entered into:

(i) between the Authorised Firm and that Person containing the key information specified in App2; and or

(ii) in accordance with the requirements in Rule 3.3.4; and

(b) before entering into the Client Agreement with the Person, the Authorised Firm has provided to that Person the key information referred to in (a) in good time to enable him to make an informed decision relating to the relevant Financial Service.

...

Reliance on a Client Agreement made by another entity

3.3.4 (1) An Authorised Firm may, for the purposes of Rule 3.3.2(1)(a)(ii), rely on a Client Agreement executed in accordance with the requirements in either (2) or (3).

(2) For the purposes of (1), an Authorised Firm which is a Branch may rely on a Client Agreement, executed by its head office or any other branch of the same legal entity, if:

(a) the Client Agreement adequately and clearly applies to the Financial Services provided by the Branch; and

(b) the Authorised Firm ensures that the Client Agreement is available to the DFSA on request.

(3) For the purposes of (1), an Authorised Firm may rely on a Client Agreement, executed by a member of its Group if:

(a) it is providing a Financial Service pursuant to Rule 2.4.5;

- (b) the Client Agreement clearly sets out:
 - (i) the Financial Service provided by the Authorised Firm and;
 - (ii) that the Client's rights in respect of (i) are enforceable against the Authorised Firm; and
- (c) the Authorised Firm ensures that the Client Agreement is available to the DFSA on request.
- (4) An Authorised Firm must notify the DFSA immediately if, for any reason, it is no longer able to provide unrestricted access to a Client Agreement as required under (2) or (3).

...

9 ADDITIONAL RULES: OPERATING AN ALTERNATIVE TRADING SYSTEM

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9.3 Member access criteria

- 9.3.1** (1) An ATS Operator may, subject to (2) and (3), only accept as a member a Person if that Person:
- (a) is an Authorised Firm;
 - (b) is a Recognised Member;
 - (c) meets the criteria in GEN Rule 2.3.2(2); or
 - (d) is classified as a Professional Client pursuant to COB Rule ~~2.3.2(2)~~ 2.3.4 (1) (g), (h) and (i).

...