



Statement of Guidance

Classification of Clients – Securities Investment Business

1. Statement of Objectives

To achieve an understanding as to how the classes of clients are defined and referred to under the Securities Investment Business Law and its accompanying Regulations.

2. Introduction

Within the Securities Investment Business regime it is appropriate to make sure that protection is proportionate to needs. This is because there is not only a cost element to protection but also an inverse relationship with freedom. It is therefore desirable that those who do not require high protection are given freedom to trade without the restrictions that certain Regulations bring and also that the Law and Regulations do indeed protect those who require it. The size, financial resources and knowledge of markets of clients will determine the level of protection.

3. Classification of Clients

3.1. It is important to classify clients correctly since the classification of a client will determine the level of protection that they receive.

3.2. As the diagram below shows, there are two client classifications that mark two different levels of protection; professional clients and private clients. There is also a third category that mainly falls outside the definition of ‘client’ and that is that of market counterparty. Though a professional client can in certain circumstances be re-classified as a market counterparty, and a private clients can in certain circumstances be re-classified as a professional client (see Conduct of Business Regulation 12), a private client can never be re-classified as a market counterparty.

3.3. The majority of the Conduct of Business Regulations and the protections afforded by these regulations only apply to a firm’s dealing with private clients and professional clients.



MARKET COUNTERPARTIES	CLIENTS	
(ONLY CONSIDERED CLIENTS FOR THE PURPOSE OF SECTION IV OF THE SIBL CONDUCT OF BUSINESS REGULATIONS)	(TWO TYPES OF CLIENTS EXIST: PRIVATE AND PROFESSIONAL. <u>ALL</u> CONDUCT OF BUSINESS RULES APPLY TO BOTH PRIVATE AND PROFESSIONAL CLIENTS)	
<ul style="list-style-type: none"> • A government (including a quasi-governmental body or a government agency). • A central bank or other national monetary authority • A supranational whose members are countries or central banks (e.g. IMF) • A state investment body or public debt management body • A professional client where classified as a market counterparty under the provisions of Regulation 12 (3) 	PROFESSIONAL CLIENTS	PRIVATE CLIENTS
	<ul style="list-style-type: none"> • A public authority • Securities Investment Business Intermediary • Sophisticated person of category (a), (b) and (c) (see definition in the Law) • A high net worth person which for the purpose of this definition is a person or an individual with total assets of at least 4 million dollars • Closed-ended funds and all other funds that are not required to be licensed, administered or registered under the Mutual Funds Law. • Private client that has been re-classified as a professional client under regulation 12(2). 	<ul style="list-style-type: none"> • All individuals • Small businesses

*High level of knowledge
Low protection*

*Low level of knowledge
High protection*



3.4. Before entering into a securities investment business relationship, a firm must take reasonable steps to determine whether the firm is dealing with a market counterparty, a professional client or a private client.

4. Market counterparties

The reason that market counterparties are excluded from the definition of client is that market counterparties are experienced professionals who have full understanding of the way in which the market works and the risks and rewards involved. Market counterparty dealings are lightly regulated. In the Regulations a market counterparty is listed to be either:

- A government (including a quasi-governmental body or a government agency).
- A central bank or other national monetary authority
- A supranational whose members are countries or central banks (e.g. IMF)
- A state investment body or public debt management body
- A professional client where classified as a market counterparty under the provisions of Regulation 12

5. Client

5.1. Client is an encompassing term that includes everyone from the smallest retail customer through to the largest investment firm. However, for the purpose of this regime, it does not include market counterparties.

5.2. Professional Clients

5.2.1 Professional clients are clients that have more experience than a private client but do not qualify as market counterparties. The Regulations allow the firm to classify clients in the list below as professional clients. Professional clients shall be informed in writing of the protection under the regulatory regime that they lose by being classified as such. They shall be informed that the protection afforded to them is lower than that offered to a private client.



5.2.2 Professional clients are:

- A public authority
- Securities Investment Business Intermediary
- Sophisticated person of categories (a), (b) or (c) (see definition in the Law)
- A high net worth person which for the purpose of this definition is a person or an individual with total assets of at least 4 million dollars.
- Closed-ended funds and all other funds that are not required to be licensed, administered or registered under the Mutual Funds Law.
- Private client that has been re-classified as a professional client under regulation 12(2) This applies only to clients that by virtue of their experience can be re-classified, see definition in the Law under Sophisticated Persons, category (d).

5.2.3 Regulation 12 of the Conduct of Business Regulations under 12(3) allows certain types of professional clients to be re-classified as market counterparties provided that the licensee has advised the professional client in writing of the protections it will lose as a result and the client does not object to being classified as a market counterparty. The types of professional client that can opt up to market counterparty are the following:

- A public authority
- Securities Investment Business Intermediary
- Sophisticated Person by virtue of being regulated by the Authority or by a Recognised Overseas Regulatory Authority.
- Company or partnership with a net worth of 12 million dollars, or a company with a net turnover of 22 million dollars or equivalent in any other currency.

5.3. Private Clients

5.3.1 All persons that are not market counterparties or professional clients are private clients. Typically, this would be individuals and small



businesses.

- 5.3.2 Also, a firm may classify persons who would otherwise have been a professional client as a private client if it notifies the client of this fact. Some firms find it easiest to classify all clients as private clients.
- 5.3.3 Individuals and small businesses are normally considered private clients. However, it is undoubtedly the case that certain private customers have a good appreciation of risks and rewards for investment business.
- 5.3.4 A firm may treat a client who would otherwise be a private client as a professional client if the client is a high net worth individual or a sophisticated person (as defined above) AND the firm has taken reasonable care to determine that the client has sufficient experience and understanding so as not to need the protection afforded to a private client.
- 5.3.5 The exercise of reasonable care in this regard may entail consideration of the following:
- The client's length of time in the market, and whether active dealing in the securities involved can be demonstrated;
 - Frequency of dealings;
 - Size and nature of the transactions;
 - Client's financial standing.
- 5.3.6 If a firm is to treat a private client as a professional client it has to give a written warning of the protections that are lost and get written consent from the private client. By being re-classified, the client receives more freedom to trade and may attract lower commission rates.