

**CONDUCT OF BUSINESS SOURCEBOOK (AMENDMENT No 7)
INSTRUMENT 2002**

Powers exercised

- A. The Financial Services Authority alters the Conduct of Business sourcebook (COB) and the Glossary in the exercise of the powers listed in Schedule 4 to COB.
- B. The rule-making powers identified above are specified for the purpose of section 153(2) of the Financial Services and Markets Act 2000 (Rule-making instruments).

Commencement

- C. This instrument comes into force on 1 September 2002.

Amendments to the Conduct of Business sourcebook

- D. The transitional rules in the Conduct of Business sourcebook are amended in accordance with Annex A to this instrument.
- E. The Conduct of Business sourcebook is amended in accordance with Annex B to this instrument.
- F. Schedule 1 to the Conduct of Business sourcebook (Record keeping requirements) is amended in accordance with Annex C to this instrument
- G. Schedule 6 to the Conduct of Business sourcebook (Rules that can be waived) is amended in accordance with Annex D to this instrument.

Amendments to the Glossary

- H. The Glossary is amended in accordance with Annex E to this instrument.

Citation

- I. This instrument may be cited as the Conduct of Business Sourcebook (Amendment No 7) Instrument 2002.

By order of the Board
18 July 2002

ANNEX A

Amendments to the Conduct of Business Transitional Rules

In this Annex, underlining indicates new text and striking through indicates deleted text.

1 COB TR 1 Transitional Rules for pre-N2 and ex-Section 43 firms

1.0 Application

...

2.0 Purpose

2.1 G The *FSA* is aware that the introduction of *COB* will impose an additional compliance burden on *firms*, even when there is an underlying continuity of policy. The *FSA* wishes to lighten that burden in a manner consistent with its regulatory objectives and the principles of good regulation under the *Act*. The following *rules* provide transitional relief which takes three distinct forms:

- (a) extra time provisions (ETPs) which, in practice, give firms additional time after *commencement*, ~~until 30 June 2002 (note that for ex-section 43 firms, the relief lasts until expiry of 12 months following commencement)~~, to complete their preparations for the impact of certain provisions in *COB*;

...

4.0 Definitions

4.1 R In these transitional provisions the following words are to have the meaning given to them below:

...

"*transitional period*" means the period starting on *commencement* and finishing on midnight on 30 June 2002, except where otherwise specified.

ANNEX B

Amendments to the Conduct of Business sourcebook

In this Annex, underlining indicates new text and striking through indicates deleted text.

1.4 General application: where?

1.4.3 R This table sets out the application of COB with reference to the location of the carrying on of an activity by a firm.

This table belongs to COB 1.4.1R.

Activity		Application of COB
(b)	<p>An activity carried on:</p> <ul style="list-style-type: none">• otherwise than in (a); and• with or for a <i>client</i> in the <i>United Kingdom</i>	<p>Where, if the office from which the activity is carried on were a separate <i>person</i>, the activity:</p> <ul style="list-style-type: none">• would fall within the <i>overseas persons</i> exclusions in article 72 of the <i>Regulated Activities Order</i>; or• would not be regarded as carried on in the <i>United Kingdom</i>; <p>then only the following apply:</p> <ul style="list-style-type: none">• <i>COB 5.5.7R</i> and <i>COB 5.5.8R</i> (Overseas business);

Activity		Application of COB
		<ul style="list-style-type: none"> COB 6.5, COB 6.7 and COB 6.8 (Content of key features, Cancellation and withdrawal, Insurance contracts—life and general) but only in relation to long term insurance business carried on with a customer habitually resident in the United Kingdom <u>in relation to long term insurance business carried on with a customer habitually resident in the United Kingdom, COB 6 (Product disclosure and the customer's right to cancel or withdraw) except COB 6.3 (Post-sale confirmation: life policies) and COB 6.9 (With-profits guides); and</u> if relevant, the provisions in (c) <p>Otherwise, COB applies in full</p>
(c)	An activity carried on by a UK firm from a branch in another EEA State under an EEA right	<p>Only the following apply:</p> <ul style="list-style-type: none"> for an <i>ISD investment firm</i> (including a <i>credit institution</i> which is an <i>ISD investment firm</i>), COB 9 (Client assets); and if relevant, the provisions in (b)
(d)	An activity carried on otherwise than in (a), (b) or (c)	<p>Only the following apply;</p> <ul style="list-style-type: none"> COB 5.5.7 R and COB 5.5.8 R (Overseas business); and

Activity		Application of COB
		<ul style="list-style-type: none"> COB 6.5, COB 6.7 and COB 6.8 (Content of key features, Cancellation and withdrawal, Insurance contracts—life and general) but only in relation to long term insurance business carried on with a customer habitually resident in the United Kingdom <u>in relation to long-term insurance business carried on with a customer habitually resident in the United Kingdom, COB 6 (Product disclosure and the customer's right to cancel or withdraw) except COB 6.3 (Post-sale confirmation: life policies) and COB 6.9 (With-profits guides)</u>

3.2.5 R Exemptions

This table belongs to COB 3.2.4R

Exemptions	
This chapter does not apply to the following:	
(1)	a <i>financial promotion to a market counterparty or an intermediate customer</i> , that is a <i>financial promotion</i> which:
(a)	is made only to recipients who the <i>firm</i> has taken reasonable steps to establish are <i>market counterparties or intermediate customers</i> ; or
(b)	may reasonably be regarded as directed only at recipients who are <i>market counterparties or intermediate customers</i> ;

Exemptions

	when a <i>person</i> is classified as an <i>intermediate customer</i> under COB 4.1.9R (Expert private customer classified as intermediate customer), this exemption applies only for a <i>financial promotion</i> that relates to the <i>designated investments</i> or <i>designated investment business</i> for which he has been so classified;
(2)	a <i>financial promotion</i> which can lawfully be <i>communicated</i> by an <i>unauthorised communicator person</i> without approval;

3.8 Form and content of financial promotions

Real time financial promotions

- 3.8.21 G A *firm* should note that COB 3.10.3R prevents a *firm* from *communicating* an *unsolicited real time financial promotion* other than an exempt *financial promotion* (which is outside the scope of this chapter) or where one of ~~COB 3.10.3 R (1) or (2)~~ COB 3.10.3 R (1), (2) or (3) applies. Many *solicited real time financial promotions* will be exempt *financial promotions* (and, therefore, outside the scope of this chapter). Accordingly, COB 3.8.22 R applies only to *solicited real time financial promotions* which are not exempt *financial promotions* and to *unsolicited real time financial promotions* within ~~COB 3.10.3R (1) OR (2)~~ COB 3.10.3 R (1), (2) or (3).

4 Accepting customers

4.1 Client classification

Requirement to classify

- 4.1.4 R (1) Before conducting *designated investment business* with or for any *client*, a *firm* must take reasonable steps to establish whether that *client* is a *private customer*, *intermediate customer* or *market counterparty*.
- (2) ~~For the purposes of the rules in COB, a firm must ensure that it treats its client in accordance with the classification established~~

~~under (1), or, where relevant, COB 4.1.7 R, COB 4.1.9 R, COB 4.1.12 R, COB 4.1.14 R or COB 4.1.15 R. A firm which takes reasonable steps to classify its clients, as required by the rules in this section, and treats a client in accordance with the classification it has established for that purpose, does not breach any other rule in COB to the extent that the breach arises only from inappropriate classification of that client.~~

Classification of another firm or an overseas financial services institution

- 4.1.7 R (1) When a *firm* ("F") conducts *designated investment business*, or related *ancillary activities*, with or for:
- (a) another *firm*; or
 - (b) an *overseas financial services institution* ("C1"), C1 is a *market counterparty* of F, unless (2), (3), (4) ~~or (5)~~ applies.
- (2) C1 is an *intermediate customer* of F when the activity carried on by F would be *inter-professional business* (if C1 were a *market counterparty*), and:
- (a) C1 is acting for an underlying *customer* ("C2"); and
 - (b) ~~[deleted]-C1 has decided that, for the interests of C2 to be properly protected under the applicable rules in COB, C1 should benefit from the protections available to intermediate customers; and~~
 - (c) F and C1 have agreed that F should classify C1 as an *intermediate customer* when C1 is acting for C2.
- 4.1.8 G (1) Any agreement under COB 4.1.7 R (2) (c) may be in relation to a particular underlying *customer* of C1's or in relation to all cases in which C1 acts on behalf of its *customers*.
- (2) When deciding whether it should be classified as an *intermediate customer* under ~~COB 4.1.7 R (2) (b)~~ COB 4.1.7R (2), C1 should have regard to the fact that it will be responsible to C2 for delivering applicable protections under *COB* (or, if C1 is an *overseas financial services institution*, under any relevant overseas provisions). C1 should also remember that F is entitled to refuse to agree to classify C1 as an *intermediate*

customer; and, in such a case, it may be appropriate for C1 to obtain services from a different *firm*.

- (3) C1 is may be an intermediate customer under COB 4.1.7 R (2) or (3), but remains a *market counterparty* for other purposes. For example, for *designated investment business* which is not *inter-professional business*, C1 is a *market counterparty* for transactions for C1's own account.
- (4) In relation to activities other than *designated investment business*, and related *ancillary activities*, C1 is a *market counterparty* in accordance with the definition of "*market counterparty*".
- (5) When C1 is a *market counterparty*, then only limited parts of *COB* will apply to F's business with C1. The *Principles* (other than 6, 8 and 9 and most of 7) will also apply, as will MAR 3 (Inter-professional conduct) for *inter-professional business*. See MAR 3 Ann 1 for further *guidance* on the application of the *Principles*, *COB* and MAR 3 for *inter-professional business*.
- (6) COB 4.1.7R does not preclude F from offering C1 protections over and above those that are owed to C1 as a market counterparty. However, any such protections would be a matter between F and C1 (for example, in contract) and would not confer the benefits owed to an intermediate or private customer under COB.

Classification of an exchange or clearing house

4.1.8A R A firm must classify a client which is a recognised investment exchange, designated investment exchange, regulated market or clearing house as either a market counterparty or an intermediate customer.

- 4.1.11 E (1) In the written warning required by COB 4.1.9 R (1) (b) (i), a *firm* should, where relevant:
- (a) advise the *client* that he will lose the protection afforded by the following *rules* in *COB* applicable exclusively to *private customers*:

- (i) ~~COB 3.9 (Direct offer financial promotions);~~
~~COB 3.12 (Communication and approval of financial promotions of an overseas or an unauthorised person) and COB 3.13 (Additional requirements for financial promotions for an overseas long term insurer)~~ COB 3 (Financial promotion);
 - (ii) COB 5.4 (Customers' understanding of risk);
 - (iii) COB 5.7 (Disclosure of charges, remuneration and commission);
 - (iv) COB 6.1: (Packaged product and ISA disclosure);
 - (v) COB 7.9 (Lending to private customers);
 - (vi) COB 7.10 (Margin requirements);
 - (vii) COB 7.11 (Non-exchange traded securities);
- (b) explain any consequences to the *client* in respect of the following *rules* in *COB* which are limited or modified in their application to *intermediate customers*:
- (i) ~~[deleted]-COB 3 (Financial promotion)~~;
 - (ii) COB 5.1 (Polarisation and status disclosure);
 - (iii) COB 8.1 (Confirmation of transactions);
 - (iv) COB 8.2 (Periodic statements);

Record keeping

- 4.1.16 R (1) A *firm* must make a record of the classification established for each *client* under this section ~~COB 4.1.4 R (1), or, where relevant, under COB 4.1.7 R, COB 4.1.9 R, COB 4.1.12 R, COB 4.1.14 R or COB 3.1.15 R,~~ including sufficient information to support that classification.

5.2 Know your customer

Record keeping: personal and financial circumstances

- 5.2.9 R A *firm* must make and retain a record of a *private customer's* personal and financial circumstances that it has obtained in satisfying COB 5.2.5 R. The record must be retained for a minimum period after the

information is obtained, as follows:

- (1) indefinitely for a record relating to a *pension transfer, pension opt-out or free-standing additional voluntary contribution* (FSAVC);
- (2) six years for a record relating to a *life policy, or pension contract or stakeholder pension scheme*;
- (3) three years in any other case.

5.7 Disclosure of charges, remuneration and commission

Disclosure of charges

- 5.7.3 R (1) Before a *firm* conducts *designated investment business* with or for a *private customer*, the *firm* must disclose in writing to that *private customer* the basis or amount of its *charges* for conducting that business and the nature or amount of any other income receivable by it or, to its knowledge, by its *associate* and attributable to that business.
- (2) If the *designated investment business* in (1) is in respect of an *execution-only transaction*:
- (a) which does not relate to a *packaged product*; and
 - (b) where prior written disclosure would delay the transaction; the *firm* may instead:
 - (c) make the disclosure required by (1) orally before the transaction is *executed*; and
 - (d) provide written confirmation of the matters disclosed to the *private customer* within five *business days* of the execution.

6 Product disclosure and the customer's right to cancel or withdraw

Quality and production of key features

- 6.1.5 R A *firm* must ensure that any *key features* or information document it produces is in writing, whether in printed hard copy or in electronic format, and:
- (1) is produced and presented to at least the same quality and standard as the associated sales or marketing material being used by the *firm* to promote the *packaged product* or *cash*

deposit ISA to customers; and

- (2) is separate from any other material given to the *customer*, unless it is produced for a *collective investment schemes*, *investment trust savings scheme* or *stakeholder pension schemes*; in that case it may be included as part of another item of sales or marketing material, but only if the *key features* or information document appears with due prominence.

6.5 Content of key features and important information: life policies, schemes, ISA cash deposit components and stakeholder pension schemes
Commission and remuneration for life policies, schemes and stakeholder pension schemes

6.5.38 R A *firm* must include under the heading 'How much will the advice cost?' either the statement prescribed in (1) or ~~the details required by (1A)~~, as applicable, or the information required by (2):

(1) for *life policies* or *stakeholder pension schemes*: 'Your adviser will give you details about the cost. The amount will depend on the size of the premium and the length of the policy term. It will be paid for out of the deductions [~~or charges, if more appropriate~~]; or

(1A) for *schemes*: 'Your adviser will give you details about the cost. The amount will depend on the size of your [use: 'investment' or 'contribution'][add if appropriate: 'and in the case of regular savings the period for which you make them']. It will be paid for out of the charges'; or

- (2) (a) the amount or value in cash terms of the *commission* or *remuneration* and an indication of the timing of these payments; and
- (b) a statement that *commission* or *remuneration* is paid for out of 'the deductions [~~or charges, if more appropriate~~]' and, if applicable, that the amount will depend on the size of the *premium* or contribution and the length of the *life policy, scheme* or *stakeholder pension scheme* term.

6.8.8 R If a *pure protection contract* or *life policy* entered into on or after 1

July 1994 provides for the payment of bonuses and the amounts of bonuses are unspecified, the *long-term insurer* must, ~~at least once a year coincident with or immediately following the first contract anniversary, either~~ in every calendar year except the first, either:

- (1) notify the policyholder in writing of the amount of any bonus which has become payable under the contract, and which has not previously been notified under this rule; or
- (2) give the policyholder in writing sufficient information to enable him to determine the amount of any such bonus.

7.3 Dealing ahead

Requirement to postpone own account transactions

7.3.3 R If a *firm* or its *associate* intends to publish to customers a written recommendation, or a piece of research or analysis, ~~to customers~~ that relates to a *designated investment*, unless COB 7.3.4 R applies, the *firm* must:

- (1) not knowingly undertake an *own account transaction* in the *designated investment* concerned or any *related designated investment*; and
- (2) (when the intention to publish is that of, or is known to, the firm) take all reasonable steps to ensure that its *associates* do not knowingly undertake any *own account transaction* in that *designated investment*, or any *related designated investment*;

until the *customers* for whom the publication was principally intended have had (or are likely to have had) a reasonable opportunity to act upon it.

7.3.3A G *Firms* are reminded of the *Chinese wall* provisions in COB 2.4.6 R (*Attribution of knowledge*).

Exceptions

7.3.4 R COB 7.3.3 R does not apply if:

- (1) the publication could not reasonably be expected to affect

significantly the price of the *designated investment* concerned or any *related designated investment*; or

- (2) the *firm or its associate* is a *market maker* in the *designated investment* concerned or in a *related designated investment* and undertakes the transaction in good faith and in the normal course of market making; or
- (3) the *firm or its associate* *deals* in order to fulfil an unsolicited *customer order*; or
- (4) the *firm* has taken reasonable steps to ensure that it or its associate needs to *deal* to fulfil a *customer order* that is likely to result from the publication, and that doing so will not cause the price of the *designated investment* or *related designated investment* that is the subject of the written recommendation, or piece of research or analysis, to move against a *customer's* interest by a material amount; or
- (5) the *firm* or its *associate* discloses in the publication that the *firm* or its *associate* has undertaken or may undertake an *own account transaction* in the *designated investment* concerned or any *related designated investment*.

7.5.9 G The evidential provision relating to mark-ups and mark-downs in COB 7.5.6 E (1)(d) does not prevent firms from being remunerated by means of mark-ups or mark-downs provided that such remuneration is disclosed to the customer as required by COB 8.1.15E (Content of a confirmation of transaction: general requirements).

7.5.10 G Where a customer order is subject to a special condition as envisaged in COB 7.5.6E (4)(e), the firm should disclose any additional cost involved in satisfying the special condition or in respect of the non-standard element. If, however, it is not possible for the charge to be "unbundled" from the price itself, firms are permitted to deal on a bundled basis subject to the overriding obligation to provide best execution.

7.12 Customer order and execution records

7.12.6 E Minimum contents of customer order and execution records

This table belongs to COB 7.12.3 R

When:		The firm should record:	
...
(2)	the <i>firm</i> executes a transaction	(a)	The name or other designation and account number of the <i>client</i> (if any) for whom the transaction was <i>executed</i> (unless the transaction was an <i>own account transaction</i>);
		(b)	The name of the counterparty, if known to the <i>firm</i> ;
		(c)	The date and if available, the time of the transaction;
		(d)	The identity of the <i>employee</i> executing the transaction;
		(e)	(i) The <i>designated investment</i> concerned; and
			(ii) The number of, or total value of, the <i>designated investment</i> ;
		(f)	The price and other significant terms (including exchange rate details if relevant); <u>and</u>
		(g)	Whether the transaction was a purchase or a sale; <u>and</u>
		(h)	[deleted] whether the <i>firm</i> was acting as <i>principal</i> as well as on behalf of its <i>customer</i>.
...

8.1.15 E Content of a confirmation of transaction – general requirements

This table belongs to COB 8.1.5 E

Content of a confirmation of transaction – general requirements	
...	...
12.	The amount of any <i>fees</i> , taxes or duties, unless included in <i>remuneration</i> mentioned in 11.
<p><u>Note: If the transaction was for an <i>intermediate customer</i>, the <i>firm</i> need not identify separately the <i>unit price</i> and the <i>remuneration</i> of the <i>firm</i> and that of any <i>associate</i> in connection with the transaction, if the <i>intermediate customer</i> has requested a confirmation combining both of these items.</u></p>	

Client money requirement

9.3.105 R ~~Subject to COB 9.3.119 R, the~~ The *client money* requirement is either the sum of, for all *clients*:

- (1) (subject to COB 9.3.119 R) the sum of, for all *clients* the individual *client* balances calculated in accordance with COB 9.3.106 R, excluding:
 - (a) the individual *client* balances calculated in accordance with COB 9.3.106 R, excluding: individual *client* balances which are negative (that is, debtors); and
 - (i) individual *client* balances which are negative (that is, debtors); and
 - (ii) *clients'* equity balances calculated in accordance with COB 9.3.113 R; and
 - (b) *Clients'* equity balances calculated in accordance with COB 9.3.113 R; and the total *margin*ed transaction requirement, calculated in accordance with COB 9.3.115R; or
- (2) the total *margin*ed transaction requirement, which is calculated in accordance with COB 9.3.115 R the sum of:
 - (a) for each *client bank account*:

- (i) the amount which the *firm's* records show as held on that account; and
- (ii) an amount that offsets each negative net amount which the *firm's* records show attributed to that account for an individual *client*; and
- (b) the total *margin*ed transaction requirement, which is calculated in accordance with COB 9.3.115R.

9.3.111 G In determining the *client money* requirement under COB 9.3.105R
~~In calculating its individual *client* balances under COB 9.3.106 R, a~~
firm need not include *money* held in accordance with COB 9.3.15 R
and COB 9.3.16 R (delivery versus payment).

9.3.112 G *Firms* are reminded of the provisions of COB 9.3.44R and COB
9.3.46R which require a *firm* to segregate *client money* into *client*
bank accounts within a certain period. In determining the *client*
money requirement under COB 9.3.105R ~~In calculating its~~
~~individual *client* balances under COB 9.3.106 R, a *firm*:~~

...

ANNEX C

Amendments to COB Schedule 1

In this Annex, underlining indicates new text and striking through indicates deleted text.

COB 5.2.9R	Private customer's details for a life policy, pension contract <u>or stakeholder pension scheme</u>	Personal and financial circumstances	On giving advice	6 years
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<p>COB 7.12.3R and COB 7.12.6E(2)</p>	<p>Execution of a transaction by a firm</p>	<p>Name/other designation of client (if any); name of counterparty (if known); date and time of execution; who executed the transaction; the designated investment; number of/ total value of the designated investment; price and other significant terms; whether sale or purchase; whether the firm was acting as principal</p>	<p>When the firm executes a transaction</p>	<p>3 years (after the date of completion of the transaction)</p>
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ANNEX D

Amendments to COB Schedule 6

In this Annex, underlining indicates new text and striking through indicates deleted text.

6 Rules that can be waived

G

The rules in COB can be waived by the FSA under sections 148 or 250 of the Act (Modification or waiver of rules) or regulation 7 of the OEIC Regulations (Modification or waiver of FSA rules), except for the following rules:

- (a) The rules in COB 1 (Application and general provisions) to the extent that those rules apply or modify other rules in COB which may not be waived;
- (b) The rules in ~~COB 2.1 (Clear, fair and not misleading communication)~~ COB 2.3 (Reliance on others) to the extent that those rules apply or modify other rules in COB which may not be waived;
- (c) COB 2.4.4R(1), and 2.4.4R(3) (~~Chinese walls to the extent that it relates to (1) and (4)~~);
- (d) COB 3.11.2R (Unregulated Collective Investment Schemes);
- (e) [deleted] ~~the rules in COB 6.7 (Cancellation and withdrawal) (other than COB 6.7.11R, COB 6.7.21R)~~;
- (f) [deleted] ~~COB 9.3.1-2, 9.3.31, 9.3.34 and 9.3.59 (Client money) and COB 9.5 (Client money distribution)~~;
- (g) The rules in COB 10 (Operators of collective investment schemes) to the extent that those rules apply or modify other rules in COB which may not be waived;
- (h) The rules in COB 11 (Trustee and depositary activities) to the extent that those rules apply or modify other rules in COB which may not be waived;
- (i) The rules in COB 12 (Lloyd's) to the extent that those rules apply or modify other rules in COB which may not be waived.

ANNEX E

Amendments to the Glossary

In this Annex, underlining indicates new text and striking through indicates deleted text.

intermediate customer (1) ...
(l) a recognised investment exchange, designated investment exchange, regulated market or clearing house, except when it is classified as a market counterparty in accordance with COB 4.1.8A R (Classification of an exchange or clearing house);

but excluding:

...

market counterparty (1) ...
(h) a recognised investment exchange, designated investment exchange, regulated market or clearing house when it is classified as a market counterparty in accordance with COB 4.1.8A R (Classification of an exchange or clearing house);

but excluding:

...