

## Chapter 2

# Authorisation and regulated activities

## 2.6 Specified investments: a broad outline

**2.6.1** G The following paragraphs describe the various *specified investments*, taking due account of any exclusion that applies.

### Deposits

**2.6.2** G A *deposit* is defined in article 5(2) of the *Regulated Activities Order*. This focuses on a sum of *money* paid by one *person* to another on terms that it will be repaid when a specified event occurs (for example, a demand is made).

**2.6.3** G Certain transactions are excluded. The definition of *deposit* itself excludes money paid in connection with certain transactions such as advance payments for the provision of goods or services and sums paid to secure the performance of a contract. The circumstances in which payments are excluded from the definition itself are exhaustively stated in article 5(3) of the *Regulated Activities Order* (Accepting deposits). In addition, there is a separate exclusion in article 9 of the Order (Sums received in consideration for the issue of debt securities) and another in article 9A (Sums received in exchange for electronic money). ■ PERG 3A Q4 contains guidance on the exclusion relating to *electronic money*.

**2.6.4** G In addition, several separate exclusions focus on the identity of the *person* paying the *money* or the *person* receiving it (or both).

- (1) Payments by certain *persons* are excluded if they are made by specified *persons* (such as local authorities or national, or supranational, bodies) or by *persons* acting in the course of a business consisting wholly or partly of lending money.
- (2) Exclusions apply for sums paid between certain *persons* who are linked in a specified way (such as *group companies* or *close relatives*).
- (3) Exclusions apply to sums received by *persons* acting for specified purposes. This covers sums received by a practising solicitor acting in the course of his profession or by *authorised* or *exempt persons* carrying on one of a specified range of *regulated activities* and acting within the scope of their *permission* or exemption.

- 2.6.4-A** G (1) A *structured deposit* is a kind of *deposit*.
- (2) A *structured deposit* is a *deposit* which is fully repayable at maturity on terms under which interest or a premium will be paid or is at risk, according to a formula involving factors such as:
- (a) an index or combination of indices; or
  - (b) a *financial instrument* or combination of *financial instruments*; or
  - (c) a *commodity* or combination of *commodities* or other physical or non-physical non-fungible assets; or;
  - (d) a foreign exchange rate or combination of foreign exchange rates.
- (3) A variable rate *deposit* whose return is directly linked to an interest rate index such as SONIA (whether or not adjusted) is not a *structured deposit* under paragraph (2)(a).
- (4) (3) applies whether or not the interest is predetermined and whether it is fixed or variable.

**2.6.4-B** G The reason why there is a definition of a *structured deposit* is that there are a number of *regulated activities* that apply to *structured deposits* that do not apply to other kinds of *deposit*. See ■ PERG 2.7.2-BG for a list.

**2.6.4-C** G Although the definition of a *structured deposit* specifically requires that the principal amount be fully repayable, that does not imply that this feature only applies to *structured deposits*. In the FCA’s view, capital certainty is a feature of any kind of *deposit*.

**Electronic money**

**2.6.4A** G *Electronic money* is specified as an *investment* in article 74A of the *Regulated Activities Order*, but only when issued by:

- (1) a *full credit institution*, a *credit union* or a municipal bank; or
- (2) a *person* deemed to have been granted authorisation under regulation 74 of the *Electronic Money Regulations*; or a *person* who falls within regulation 76(1) of the *Electronic Money Regulations* (see ■ PERG 3A, Q30 and 31).

The authorisation and registration requirements for any other *person* intending to issue *electronic money* are governed by the *Electronic Money Regulations*. Guidance on these regulations is available in ■ PERG 3A.

**Rights under a contract of insurance**

**2.6.5** G *Contract of insurance* is defined to include certain things that might not be considered a *contract of insurance* at common law. Examples of such additions include *capital redemption* contracts or contracts to pay annuities on human life. Detailed *guidance* on identifying a *contract of insurance* is in ■ PERG 6 (Guidance on the Identification of Contracts of Insurance).

**2.6.6** **G** There are two main sorts of *contracts of insurance*. These are *general insurance contracts* and *long-term insurance contracts*. The *Regulated Activities Order* provides that, in certain specified circumstances, a contract is to be treated as a *long-term insurance contract* notwithstanding that it contains supplementary provisions that might also be regarded as relating to a *general insurance contract* (see article 3(3)).

**2.6.7** **G** The *Regulated Activities Order* uses two further terms in relation to *contracts of insurance* to identify those contracts under which rights are treated as *contractually based investments*.

(1) The first term is 'qualifying contracts of insurance' (referred to as *life policies* in the *Handbook*). This identifies those *long-term insurance contracts* under which rights are treated as *contractually based investments*. This term does not cover *long-term insurance contracts* which are contracts of reinsurance or, if specified conditions are met, contracts under which benefits are payable only on death or incapacity.

(2) The second term is '*relevant investments*'. This term applies to:

- (a) *contractually based investments*, which includes rights under *life policies*, and rights to or interests in such *investments* under article 89 of the *Regulated Activities Order* (Rights to or interests in investments); and
- (b) rights under *contracts of insurance* other than *life policies* (but not rights to or interests in such rights).

This term is used in connection with the treatment, under various parts of the *Regulated Activities Order*, of *persons carrying on insurance distribution activities* (see further ■ PERG 5 (Guidance on insurance distribution activities)).

**2.6.8** **G** Certain arrangements in relation to funeral plans are specifically excluded from being *contracts of insurance* if they would otherwise be so. The exclusion applies to arrangements that fall within the definition of a *funeral plan contract* (see ■ PERG 2.6.26G).

**Shares etc**

**2.6.9** **G** *Shares* are defined in the *Regulated Activities Order* as shares or stock in a wide range of entities; that is, any *body corporate* wherever incorporated and unincorporated bodies formed under the law of a country other than the *United Kingdom*. They include deferred shares issued by *building societies* as well as transferable shares in *industrial and provident societies*, *credit unions* and equivalent *EEA* bodies. These shares are transferable and negotiable in a way similar to other shares or stock and are treated as such for the purposes of defining *regulated activities*. They are specifically mentioned as being within the *specified investment* category of *shares* because other types of share issued by these mutual bodies are not transferable and are expressly excluded (see ■ PERG 2.6.10 G).

**2.6.10** **G** The following are excluded from the *specified investment* category of *shares*. Shares or stock in all *open-ended investment companies* are excluded from being treated in this particular category (but see ■ PERG 2.6.17 G). Exclusions

from this category also apply to shares or stock in the share capital of certain mutuals or in equivalent EEA bodies. This takes out *building society* or *credit union* accounts and non-transferable shares in *industrial and provident societies*. These may nevertheless be *specified investments* in another category (such as *deposits* in the case of *building society* accounts).

**Debt instruments**

2.6.11

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Two categories of *specified investments* relating to debt instruments are dealt with under this heading. They broadly split into private debt and public sector debt.

- (1) The first category of 'instruments creating or acknowledging indebtedness' (defined in article 77 of the *Regulated Activities Order* and referred to in the *Handbook* as *debentures*) expressly refers to a range of instruments such as *debentures*, bonds and loan stock and contains a catch-all reference to 'any other instrument creating or acknowledging indebtedness.'
- (2) The second category (defined in article 78 of the *Regulated Activities Order* and referred to in the *Handbook* as *government and public securities*) refers to loan stock, bonds and other instruments creating or acknowledging indebtedness which are issued by or on behalf of any government, the assemblies for Scotland, Wales or Northern Ireland, a local authority or an international organisation.

An instrument cannot fall within both categories of *specified investments* relating to debt instruments. 'Instrument' is defined to include any record whether or not in the form of a document (see article 3(1) of the *Regulated Activities Order*).

**Alternative finance investment bonds**

2.6.11A

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Alternative finance investment bonds (defined in article 77A of the *Regulated Activities Order* and referred to in the *Handbook* as *alternative debentures*) are a form of Sharia compliant bond (known as *sukuk* in the plural or *sakk* in the singular) which are intended to be regulated in an equivalent manner to conventional debt securities, where appropriate. *Sukuk* arrangements allow assets to be held for the benefit of investors in certificates issued by a company. The benefits may include the payment of a return that is economically equivalent to interest and redemption of the certificates out of the proceeds from the disposal of the assets. *Alternative debentures* are not limited to those wishing to issue Sharia compliant *sukuk*.

2.6.11B

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The arrangements which grant rights under *alternative debentures* are similar to the tax definition of arrangements relating to alternative finance investment bonds at section 48A of the Finance Act 2005 (see [www.opsi.gov.uk/acts/acts2007/ukpga\\_20070011\\_en\\_5#pt3-pb9-l1g53](http://www.opsi.gov.uk/acts/acts2007/ukpga_20070011_en_5#pt3-pb9-l1g53)) . However the purposes of the two provisions are not the same. One of the objectives of the *FCA* under the *Act* is consumer protection. Accordingly, secondary legislation made under the *Act*, like article 77A of the *Regulated Activities Order*, is likely to be interpreted by the *FCA* with consumer protection in mind. This may mean that whilst the arrangements described at section 48A of the Finance Act 2005 and those described at article 77A of the *Regulated Activities Order* are similar, they are likely to be construed differently by the courts. ■ PERG 2.6.11FG and ■ PERG 2.6.11GG explain the

consumer protection features in the definition of *alternative debentures* in more detail.

2.6.11C

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The arrangements which grant rights under an *alternative debenture* arise where:

- (1) the arrangements provide for a person (the bond-holder) to pay a sum of money (the capital) to another (the bond-issuer);
- (2) the arrangements identify assets, or a class of assets, which the bond-issuer will acquire for the purpose of generating income or gains directly or indirectly (the bond assets);
- (3) the arrangements specify a period at the end of which they cease to have effect (the bond term);
- (4) the bond-issuer undertakes under the arrangements:
  - (a) to make a repayment in respect of the capital (the redemption payment) to the bond-holder during or at the end of the bond term (whether or not in instalments); and
  - (b) to pay to the bond-holder other payments on one or more occasions during or at the end of the bond term (the additional payments);
- (5) the amount of the additional payments does not exceed an amount which would, at the time at which the bond is issued, be a reasonable commercial return on a loan of the capital; and
- (6) the arrangements are a security admitted to:
  - (a) an *official list*; or
  - (b) trading on a *regulated market* or on a *recognised investment exchange*.

2.6.11D

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Different types of *alternative debentures* are permitted so that, for example:

- (1) the assets of the arrangement may be acquired before or after it commences;
- (2) the bond-holder may (but need not) be entitled under the arrangements to terminate them, or participate in terminating them before the end of the bond term;
- (3) the return may be fixed, floating or determined in some other way;
- (4) the amount of the redemption payment may (but need not) be subject to reduction in the event of a fall in the value of the bond assets or in the rate of income generated by them.

2.6.11E

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As these arrangements might amount to a collective investment scheme (see ■ PERG 9.4.2 GG for a broad description) a consequential amendment to the Financial Services and Markets Act 2000 (Collective Investment Scheme) Order 2001 (SI 2001/1062) has been made so that, like conventional bonds,

*alternative debentures* are excluded from the definition of collective investment scheme.

**2.6.11F** **G** The range of instruments that are caught by the *alternative debenture* definition have been tightly circumscribed to ensure that only those arrangements that grant, in substance, debt-like returns are captured. This is because arrangements giving rights under an *alternative debenture* cannot amount to a *collective investment scheme* (see ■ PERG 2.6.11EG). If other types of investments were covered by the *alternative debenture* definition this could have the effect of undermining the regime for regulating *collective investment schemes*, which is primarily aimed at protecting the consumer from investing in unsuitable products. For example, under section 238 of the Act (Restrictions on promotion) an *authorised person* cannot *communicate* an invitation or inducement to participate in an *unregulated collective investment scheme*.

**2.6.11G** **G** The condition set out at ■ PERG 2.6.11CG (6) is also intended to protect consumers. This provides that *alternative debentures* must be listed on an *official list* or traded on a *regulated market* or *recognised investment exchange*. This is because there is a risk that *alternative debentures* could lead to regulatory arbitrage (i.e. the risk that the exclusion from being classified as a *collective investment scheme* is exploited by instruments not intended to be excluded). Mandatory listing is aimed at ensuring an enhanced level of transparency, reducing the likelihood of regulatory arbitrage.

**2.6.11H** **G** (1) The main provision within the definition of *alternative debenture* arrangements that seeks to ensure that only instruments that display the characteristics of a debt security can be *alternative debentures* is set out at ■ PERG 2.6.11CG (5). It provides that the amount of additional payments under the arrangements must not exceed an amount which would, at the time the bond is issued, be a reasonable commercial return on a loan of capital. Where the return is not fixed at the outset, it is the maximum possible amount of the additional payments that must be considered in deciding this question. The following example demonstrates how this condition should be approached.

**Example**

ABC Ltd is a property development company. It wishes to increase its portfolio on a short-term basis. It issues 5-year sukuk to investors and uses the proceeds to buy the head lease of a commercial property. The rental income from the lease is distributed to investors in proportion to their holdings without a cap on the level of return. After 5 years, the head lease is sold on at a profit and the proceeds shared between investors.

In this example, the investors participate directly in the success or failure of the underlying property business. The sukuk is not really in the nature of a debt instrument. It is unlikely to be an *alternative debenture* as:

(a) additional payments under the arrangements would exceed a reasonable commercial return on a loan of the capital.

Further, where the return is not fixed at the outset, it is the maximum possible amount of the additional payments that must be considered. Here,

the issue terms of the sukuk impose no upper limit on the amount of the periodic distributions: a sakk holder subscribing 1,000 may, in a year, get back 200 or 2,000 or nothing depending on the rental market. The maximum potential return is clearly in excess of a reasonable commercial return on a loan of 1,000; and

(b) the arrangements have not been admitted to an *official list* or admitted to trading on a *regulated market* or *recognised investment exchange* (see PERG 2.6.11CG (6)).

- (2) If, in the above example, investors returns were capped at 500 per sakk per year, then this is the amount that must be considered in deciding whether the return exceeds a reasonable commercial return on a loan, even where the amounts actually received turn out to be far lower.
- (3) In applying the reasonable commercial return test, the sakk should be compared to a hypothetical loan to the issuer on similar terms and carrying similar risks. For example, a conventional security convertible into shares will normally carry a lower rate of interest because the conversion right has a value. The return on an exchangeable or convertible sakk should be measured against the return on an equivalent exchangeable or convertible debt security.
- (4) The risk to investors in sukuk may vary slightly from that of a conventional bond in some instances. This may be due to the fact that sukuk holders only have recourse to the bond assets or some other structural feature which results in the risk profile being higher. In such instances it may be justifiable for the rate of return to be slightly higher than that of a conventional loan.
- (5) As with any financial instrument, the pricing of sukuk will depend on the issuers view of the market at the time of issue and reasonable commercial return may vary depending on the issuer and the economic circumstances prevalent at the time of issue.

2.6.12

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Certain instruments are excluded from both of the categories of *specified investments* referred to in ■ PERG 2.6.11 G. These include trade bills, specified banking documents (such as cheques and banknotes though not bills of exchange accepted by a banker) and *contracts of insurance*. There is a further exclusion from this category of *specified investment* dealing with public debt for National Savings deposits and products. However, for the purposes of article 78 of the Financial Services and Markets Act (Regulated Activities) Order 2001, this exclusion does not apply to instruments that meet the requirements of ■ PERG 2.6.11CG (1) to ■ (5).

**Warrants**

2.6.13

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The category of *specified investment* of instruments giving entitlements to investments (referred to in the *Handbook* as *warrants*) covers warrants and other instruments which confer an entitlement to subscribe for *shares*, *alternative debentures*, *debentures* and *government and public securities*. This is one of several categories of *specified investments* that are expressed in terms of the rights they confer in relation to other categories of *specified investment*. The rights conferred must be rights to 'subscribe' for the relevant investments. This means that they are rights to acquire the investments directly from the *issuer* of the *investments* and by way of the



issue of new investments (rather than by purchasing investments that have already been issued).

- 2.6.14 **G** To keep clear distinctions between the different *specified investment* categories, instruments giving entitlements to investments are not to be regarded as *options, futures* or *contracts for differences*.

**Certificates representing securities**

- 2.6.15 **G** The *specified investment* category of *certificates representing certain securities* covers certificates or other instruments which confer rights in relation to *shares* and *debt securities*. It includes depositary receipts.

- 2.6.16 **G** There is an exclusion for any instrument that would otherwise fall within the *specified investment* category of *units* in a *collective investment scheme*. But the exclusion does not apply where the underlying investments covered by the certificate are issued by the same (non-public sector) *issuer* or constitute a single issue of public sector debt (such as a single issue of gilts). Certificates or other instruments conferring rights in respect of investments in these two cases continue to be treated as *certificates representing certain securities*.

**Units**

- 2.6.17 **G** The *specified investment* category of *units* in a *collective investment scheme* includes *units* in a *unit trust scheme* or *authorised contractual scheme*, *shares* in *open-ended investment companies* and rights in respect of most limited *partnerships* and all *limited partnership schemes*. *Shares* in or *securities* of an *open-ended investment company* are treated differently from *shares* in other *companies*. They are excluded from the *specified investment* category of *shares*. This does not mean that they are not investments but simply that they are uniformly treated in the same way as *units* in other forms of *collective investment scheme*. The effect is that an *open-ended investment company* will, in issuing its *shares*, be subject to the restrictions on promotion of *collective investment schemes* in section 238 of the *Act* (rather than to restrictions that apply to other forms of body corporate). For exclusions from the restrictions on the provisions of *collective investment schemes*, see the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (SI 2001/1060). *Guidance* on the meaning of *open-ended investment company* is in ■ PERG 9 (Meaning of open-ended investment company).

- 2.6.18 **G** There are no exclusions in the *Regulated Activities Order* for this *specified investment* category. This is because '*collective investment scheme*' is defined in section 235 of the *Act* (Collective investment schemes) for the purposes of the *Act* generally. But there is a separate power to provide for exemptions from that definition and the Treasury have exercised it (see the Financial Services and Markets Act 2000 (Collective Investment Schemes) Order 2001 (SI 2001/1062)). The result is that *units* in certain arrangements are excluded from being *collective investment schemes* (for example, closed-ended *bodies corporate*, franchise arrangements, timeshare schemes).

**Rights under a pension scheme**

- 2.6.19** **G** Three types of *investment* are specified here:
- (1) rights under a *stakeholder pension scheme*;
  - (2) rights under a *personal pension scheme*; and
  - (3) rights or interests under a pension scheme which provides *safeguarded benefits*.
- 2.6.19A** **G** A *stakeholder pension scheme* is defined in section 1 of the Welfare Reform and Pensions Act 1999. Regulations made under that section set out detailed rules under which such schemes will operate (see the Stakeholder Pension Scheme Regulations 2000). Schemes must be registered with The Pensions Regulator.
- 2.6.19B** **G** A *personal pension scheme* is, broadly speaking, a pension scheme which is not an *occupational pension scheme* or a *stakeholder pension scheme*. That is, a scheme or arrangement that is comprised in one or more instruments or agreements, having or capable of having effect so as to provide benefits to or in respect of people:
- (1) on retirement; or
  - (2) on having reached a particular age; or
  - (3) on termination of service in an employment.
- 2.6.19BA** **G** Under section 48(8) of the Pension Schemes Act 2015 *safeguarded benefits* means benefits other than:
- (1) money purchase benefits (defined in section 181 of the Pension Schemes Act 1993 and section 176 of the Pension Schemes (Northern Ireland) Act 1993); and
  - (2) cash balance benefits (defined in section 75 of the Pension Schemes Act 2015).
- 2.6.19C** **G**
- (1) Rights under *stakeholder pension schemes* and *personal pension schemes* are *specified investments* for the purposes of the entire *Regulated Activities Order*.
  - (2) Rights or interests under a pension scheme which provides *safeguarded benefits* as defined by section 48(8) of the Pension Schemes Act 2015 are only *specified investments* for the purposes of article 53E (Advising on conversion or transfer of pension benefits) and not in relation to any other *regulated activity*.
  - (3) There are no exclusions in the Order.

**Emission allowances**

- 2.6.19D** **G** This *specified investment* comprises *emissions allowances* that are auctioned as *financial instruments* or *two-day emissions spots* (together, *emissions auction products*).
- There are two *specified investments* relating to the scheme for *emission allowance* trading within the UK:
- (1) the first kind comprises *emission allowances* that are auctioned as *financial instruments* or *two-day emissions spots* (together, *emissions auction products*); and
  - (2) the second kind is an *emission allowance* itself subject to (2)).
- An *emission allowance* is only a *specified investment* if ■ PERG 2.5.7G (Wider definition of certain *specified investments* when carrying on some kinds of MiFID business) applies.
- An *emission allowance* can also be the underlying for an *option*, *future* or *contract for differences*.
- 2.6.19E** **G** The *emissions auction product* *specified investment* relates only to the *regulated activity of bidding in emissions auctions* (whereby a bid is received, transmitted and submitted on an *auction platform*) and captures the two forms of allowance products that may be auctioned under regulation 4(2) of the *UK auctioning regulations* or the *EU auction regulation*: a two-day spot or a five-day future.
- 2.6.19F** **G** See ■ PERG 2.7.6DG for more about:
- (1) how the *RAO* deals with the overlap between *emission allowances* and *emissions auction products*; and
  - (2) whether these products are a *security*, a *contractually based investment* or a *relevant investment*.
- 2.6.19G** **G** Some other points about *emission allowances* are:
- (1) *Emission allowance* means an allowance as defined in article 3(a) of Directive 2003/87/EC or created under article 18 of the *trading scheme order 2020*. These provisions provide that an allowance is an allowance to emit one tonne of carbon dioxide equivalent during a specified period, only valid for the purpose of meeting the requirements of Directive 2003/87/EC or the *trading scheme order 2020* and only transferable in accordance with the provisions of that directive or order (*emission allowance*).
  - (2) A two-day spot is defined by reference to article 3(3) of the *EU auction regulation* or regulation 2 of the *UK auctioning regulations*. These provisions provide that a two-day spot is an allowance auctioned for delivery at an agreed date no later than the second trading day from the day of the auction (*two-day emissions spot*).
  - (3) A *financial instrument* is defined as any instrument listed in Part 1 of Schedule 2 to the *Regulated Activities Order*.

- (4) The distinction between *emission allowances* that are auctioned as *financial instruments* and those auctioned as two-day spots is no longer relevant as all *emissions auction products* are *financial instruments*.

**Options**

2.6.20 **G** The *specified investment* category of *options* comprises:

- (1) *options* to acquire or dispose of *securities* or *contractually based investments*, currency and certain precious metals and *options* to acquire or dispose of such *options*. *Options* to buy or sell other types of *commodity* will only fall within this *specified investment* category if they are *options* to buy or sell *futures*, or *options* to buy or sell *contracts for differences*, which are based on other *commodities*. But *options* to buy or sell other types of *commodity* may be *contracts for differences* (see ■ PERG 2.6.23 G);
- (2) *options* to acquire or dispose of other property and falling within paragraphs 5, 6, 7 or 10 of Part 1 of Schedule 2 to the *Regulated Activities Order* (see article 83(2) of the *Regulated Activities Order* and ■ PERG 13, Q33A to Q34 for *guidance* about these instruments), but only where they are *options* to which ■ PERG 2.5.7G (Wider definition of certain specified investments when carrying on some kinds of MiFID business) applies; and
- (3) *options* to acquire or dispose of an option to which (2) applies, but only where ■ PERG 2.5.7G applies (see article 83(1)(e) of the *Regulated Activities Order*).

2.6.20A **G** It follows therefore that *options* not falling within ■ PERG 2.6.20G (1), for example physically settled *options* on non-precious metals, such as copper *options*, will not be *options* unless they meet the conditions in ■ PERG 2.6.20G (2). Moreover, where the option in question is one to which ■ PERG 2.6.20G (2) applies, it will be an *option* only in relation to the services referred to in ■ PERG 2.5.8G, provided by that *person*. The same applies in the case of *options* falling within ■ PERG 2.6.20G (3), for example an option on a physically settled copper option traded on a *regulated market*.

**Futures**

2.6.21 **G** *Futures* is the name given to rights under a contract for the *sale* of a *commodity*, or of property of any other description, under which delivery is to be made at a future date and at a price agreed on when the contract is made.

2.6.22 **G** The key issue in determining whether something is an investment in this category for the purposes of the *Regulated Activities Order* is whether the contract is made for investment purposes rather than commercial purposes. Contracts which are made for commercial purposes are excluded from this *specified investment* category and the *Regulated Activities Order* contains several tests as to when that is, or is not, the case (some are conclusive, others only indicative).

**2.6.22A** G As with *options*, there is an additional category of instruments which are *futures* only in limited circumstances. These are contracts as described in ■ PERG 2.6.21 G:

- (1) that would not be regarded as having been entered into for investment purposes because they fail one of the tests mentioned in ■ PERG 2.6.22 G;
- (2) that:
  - fall within paragraph 4 of Part 1 of Schedule 2 to the *Regulated Activities Order* and relate to currencies (see ■ PERG 13, Q31A to Q31S for *guidance* about these derivatives); or
  - fall within paragraphs 5, 6, 7 or 10 of Part 1 of Schedule 2 to the *Regulated Activities Order* (see ■ PERG 13, Q33A to Q34 for *guidance* about these derivatives); and
- (3) to which ■ PERG 2.5.7G (Wider definition of certain specified investments when carrying on some kinds of MiFID business) applies.

See article 84(1A)-(1D) of the *Regulated Activities Order*

**2.6.22B** G [deleted]

**Contracts for differences**

**2.6.23** G The *specified investment* category of *contracts for differences* covers:

- (1) rights under *contracts for differences*;
- (2) rights under other contracts whose purpose or pretended purpose is to secure a profit or avoid a loss by reference to fluctuations in certain factors; and
- (3) derivative contracts for the transfer of credit risk (not within (1) or (2)) falling within paragraph 8 or 9 of Part 1 of Schedule 2 to the *Regulated Activities Order* (see ■ PERG 13, Q31 for *guidance* about these instruments), but only where ■ PERG 2.5.7G (Wider definition of certain specified investments when carrying on some kinds of MiFID business) applies.

The factors mentioned in (2) include the value or price of property of any description or an index or any 'other factor designated in the contract'. This catches a wide range of factors.

**2.6.23A** G All contracts in this category are cash-settled instruments (as opposed to being settled by way of delivering something other than cash). Many would be unenforceable as gaming contracts were it not for section 412 of the *Act* (Gaming contracts). Examples of instruments that count as *specified investments* under this category are *spread bets* and interest rate swaps.

**2.6.24** G There are a number of exclusions. These include a case where the parties intend that the profit is to be secured or the loss to be avoided by taking delivery of property. This avoids overlap with the *specified investment*

categories of *options* and *futures*. Also excluded are index-linked *deposits* and rights under certain contracts connected with the National Savings Bank or National Savings products. There is also provision to ensure that the *specified investment* category of *contracts for differences* does not include rights under *life policies*.

2.6.24A

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- (1) A binary or other fixed outcomes bet is also treated as *contract for differences*. This is defined as something that meets the following conditions:
  - (a) it is a derivative contract of a binary or other fixed outcomes nature;
  - (b) it is not covered by ■ PERG 2.6.23G(1) or (2);
  - (c) it is settled in cash;
  - (d) it is a *financial instrument* that falls within paragraphs 4, 5, 6, 7 or 10 of Part 1 of Schedule 2 to the *Regulated Activities Order* (see ■ PERG 13, Q31A to Q34 for *guidance* about these instruments); and
  - (e) one of the following requirements is met:
    - (i) ■ PERG 2.5.7G (Wider definition of certain specified investments when carrying on some kinds of MiFID business) applies; or
    - (ii) a *person* is *making arrangements with a view to transactions in investments* in relation to it.
- (2) A product is binary (see ■ PERG 2.6.24AG(1) (a)) only if the payout is all or nothing. That is, the overall result will be that one party will pay the other a fixed sum. It is a sort of fixed odds bet.
- (3) The main example of a binary product is a binary or digital option.
- (4) A simple example is a contract between X and Y under which:
  - (a) at the start, X pays Y a fixed sum (equivalent to the stake in a bet);
  - (b) if shares in ABC PLC close above £5.20 per share at close of trading five days later, Y pays X a fixed sum (a multiple of X's original stake), the result being that Y pays X a fixed sum in net terms;
  - (c) if shares in ABC PLC close at or below £5.20 per share at close of trading five days later, X gets nothing, the result being that X pays Y a fixed sum.
- (5) A simple binary sporting bet is not a *contract for differences* as:
  - (a) it is not covered by *MiFID* and so it does not meet the condition in ■ PERG 2.6.24AG(1)(d); and
  - (b) it does not come under any other part of the definition of a *contract for differences*.
- (6) A product that that has fixed outcomes but is not binary (see ■ PERG 2.6.24AG(1)(a)):

- (a) is like a binary product in that there are fixed number of possible payouts and they are all known in advance; but
  - (b) differs from a binary contract in that the number of possible payouts is three or more rather than just two.
- (7) A simple example of a contract in (6) (although it may not be common in practice) is a contract between X and Y under which:
- (a) at the start, X pays Y a fixed sum (equivalent to the stake in a bet);
  - (b) if shares in ABC PLC close above £5.20 per share at close of trading five days later and (c) does not apply, Y pays X a fixed sum (a multiple of X's original stake), the result being that Y pays X a fixed sum in net terms;
  - (c) if shares in ABC PLC close above £5.20 per share at close of trading five days later and the market as a whole rises by more than ten percent, Y pays X a fixed sum that is:
    - (i) a multiple of X's original stake; but
    - (ii) a different (and usually smaller) multiple from the one in (b); the result being that Y pays X a fixed sum in net terms;
  - (d) if shares in ABC PLC close at or below £5.20 per share at close of trading five days later, X gets nothing, the result being that X pays Y a fixed sum.

2.6.24B

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- (1) Any derivative under *MiFID* will be an *option, future or contract for differences* where ■ PERG 2.5.7G (Wider definition of certain specified investments when carrying on some kinds of EU business) applies.
- (2) So for example the following contract between X and Y would be a *contract for differences*.
  - (a) At the start, X pays Y a fixed sum (equivalent to a stake in a bet).
  - (b) If the ABC index closes above 6,500 when the contract expires, Y pays X a fixed sum being the stake and an additional pay out (determined on the opening of the contract), the result of the contract being that Y pays X a fixed sum.
  - (c) If the ABC index closes below 6,500 when the contract expires, X gets nothing (and pays Y the stake paid when X opened the contract), the result of the contract being that X pays Y a fixed sum.
  - (d) If the ABC index was trading at 6,500 when the contract was opened and closes at 6,500 when the contract expires, Y pays X a fixed sum (being a proportion of the amount paid by X to Y on opening of the contract), the result of the contract being that X pays Y a fixed sum.

**Lloyd's investments**

2.6.25

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Two types of *specified investment* are relevant. These are the *underwriting capacity of a Lloyd's syndicate* and a *person's membership of a Lloyd's syndicate*. There are no exclusions from these *specified investment* categories.

**Rights under a funeral plan**

2.6.26

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- (1) Rights under a *funeral plan contract* are the rights to a funeral obtained by a *person* who pays for the funeral before the death of the *person* whose funeral it will be.
- (2) The definition of *funeral plan contract* excludes those contracts under which the *customer* and the *funeral plan provider* intend or expect that the funeral will be provided within one *month* of the contract being entered into.

**Rights under a regulated mortgage contract**

2.6.27

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In accordance with article 61(3)(a) of the *Regulated Activities Order*, a *regulated mortgage contract* is a contract which, at the time it is entered into, satisfies the following conditions:

- (1) the contract is one where the lender provides credit to an individual or trustees (the "borrower");
- (2) the obligation of the borrower to repay is secured by a mortgage on land:
  - (a) in relation to a contract entered into before *IP completion day*, means land in the *United Kingdom* or, if the contract was entered into on or after 21 March 2016, within the territory of an *EEA state*;
  - (b) in relation to a contract entered into on or after *IP completion day*, means land in the *United Kingdom*; and
- (3) at least 40% of that land is used, or is intended to be used, as or in connection with a dwelling.

Detailed guidance on this is set out in ■ PERG 4.4 (Guidance on regulated activities connected with mortgages). However, generally, the definition of *regulated mortgage contract* does not include certain loans to commercial borrowers, second charge loans by a credit union, exempt consumer buy-to-let mortgage contracts (see ■ PERG 4.4.31G) and second charge bridging loans (see ■ PERG 4.4.1-A G).

**Rights under a home reversion plan**

2.6.27A

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In accordance with article 63B(3)(a) of the *Regulated Activities Order*, a *home reversion plan* is an arrangement under which, at the time it is entered into:

- (1) a *person* (the "reversion purchaser") buys all or part of a qualifying interest in land (other than timeshare accommodation) in the *United Kingdom* from an individual or trustees (the "*reversion occupier*");
- (2) the *reversion occupier* (or, where trustees are concerned, an individual who is a beneficiary of the trust), or a related *person* of either, is entitled, and intends, to use at least 40% of that land as or in connection with a dwelling; and
- (3) the entitlement to occupy ends on the occurrence of any one or more of the following events:
  - (a) the end of a specified period of at least twenty years; or



- (b) the death of the individual; or
- (c) the individual enters a care home.

Detailed *guidance* on this is set out in ■ PERG 14.3 (Guidance on home reversion and home purchase activities).

**Rights under a home purchase plan**

**2.6.27B**

**G**

In accordance with article 63F(3)(a) of the *Regulated Activities Order*, a *home purchase plan* is an arrangement under which, at the time it is entered into:

- (1) a *person* (the "*home purchase provider*") buys a qualifying interest in land or an undivided share of a qualifying interest in land (other than timeshare accommodation) in the *United Kingdom*;
- (2) where an undivided share of a qualifying interest is bought, the interest is held on trust for the home purchase provider and the individual or trustee as beneficial tenants in common;
- (3) an individual or trustees (the "*home purchaser*") is obliged to buy the interest bought by the *home purchase provider* over the course of or at the end of a specified period; and
- (4) the *home purchaser* (or, where trustees are concerned, by an individual who is a beneficiary of the trust), or a related *person* of either, is entitled, and intends, to use at least 40% of that land as or in connection with a dwelling.

Detailed *guidance* on this is set out in ■ PERG 14.4 (Guidance on home reversion and home purchase activities).

**Rights under a regulated sale and rent back agreement**

**2.6.27C**

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In accordance with Article 63J(3)(a) of the *Regulated Activities Order*, a *regulated sale and rent back agreement* is an arrangement under which, at the time it is entered into:

- (1) a *person* (the *SRB agreement provider*) buys all or part of the qualifying interest in land (other than timeshare accommodation) in the *United Kingdom* from an individual or trustees (the agreement seller); and
- (2) the agreement seller (if he is an individual) or an individual who is the beneficiary of the trust (if the agreement seller is a trustee), or a related person, is entitled under the arrangement to occupy at least 40% of the land in question as or in connection with a dwelling, and intends to do so;

but excluding any arrangement that is a regulated *home reversion plan*.

Detailed *guidance* on this is set out in ■ PERG 14.4A (Activities relating to regulated sale and rent back agreements).

**Rights to or interests in investments**

2.6.28 **G** Rights to, or interests in, all the *specified investments* in ■ PERG 2.6 (except rights to, or interests in, rights under a *home finance transaction*) are themselves treated as *specified investments*. The effect is that, in most cases, an activity carried on in relation to rights or interests derived from any of those *investments* is also a *regulated activity* if the activity would be regulated if carried on in relation to the investment itself. The exception is where the rights or interests relate to a *pure protection contract* or a *general insurance contract*.

2.6.29 **G** (1) There are several things that are not covered by this category (other than rights to, or interests in, rights under a mortgage contract). Anything that is covered by any other *specified investment* category is excluded, as are interests under the trusts of an *occupational pension scheme*.

(2) There are also excluded from this category rights or interests acquired as a result of entering into a *funeral plan contract*. Where the *funeral plan contract* is trust or insurance-backed (see ■ FPCOB 3), the effect of this exclusion is that rights to, or interests in, the *contract of insurance* or interests under trust to which the contract relates are excluded from this *specified investment* category. Rights under the *funeral plan contract* itself which a *person* obtains when they enter into a *funeral plan contract* are covered by the *specified investment* category described in ■ PERG 2.6.26G.

**Rights under a credit agreement and an article 36H agreement**

2.6.30 **G** In accordance with article 60B (3) of the *Regulated Activities Order*, a *credit agreement* is an agreement between an *individual* ("A") and any other *person* ("B") under which B provides A with *credit* of any amount. In accordance with article 36H (10) of the *Regulated Activities Order*, rights under an article 36H agreement are also *specified investments*. The definition of an article 36H agreement is set out in ■ PERG 2.7.7H G. In addition and in accordance with article 53(5) of the *Regulated Activities Order*, rights under a 'relevant article 36H agreement' (within the meaning of that Order) are also *specified investments*.

**Rights under a consumer hire agreement**

2.6.31 **G** In accordance with article 60N(3) of the *Regulated Activities Order*, a *consumer hire agreement* is an agreement between a *person* ("the owner") and an *individual* ("the hirer") for the bailment or, in Scotland, the hiring, of *goods* to the hirer which:

(1) is not a *hire-purchase agreement*; and

(2) is capable of subsisting for more than three months.