

**Principles for Businesses**

# Chapter 1

## Introduction

## 1.1 Application and purpose

### Application

- 1.1.1 **G** The *Principles* (see ■ PRIN 2) apply in whole or in part to every *firm*. The application of the *Principles* is modified for *firms* conducting *MiFID business*, *incoming EEA firms*, *incoming Treaty firms*, *UCITS qualifiers* and *AIFM qualifiers*. ■ PRIN 3 (Rules about application) specifies to whom, to what and where the *Principles* apply.

### Purpose

- 1.1.2 **G** The *Principles* are a general statement of the fundamental obligations of *firms* under the *regulatory system*. This includes provisions which implement the *Single Market Directives*. They derive their authority from the *FCA's* rule-making powers as set out in the *Act* and reflect the *statutory objectives*.

- 1.1.3 **G** [deleted]

### Link to fit and proper standard in the threshold conditions

- 1.1.4 **G** In substance, the *Principles* express the main dimensions of the "fit and proper" standard set for *firms* in *threshold condition 5* (Suitability), although they do not derive their authority from that standard or exhaust its implications. Being ready, willing and organised to abide by the *Principles* is therefore a critical factor in applications for *Part 4A permission*, and breaching the *Principles* may call into question whether a *firm* with *Part 4A permission* is still fit and proper.

### Taking group activities into account

- 1.1.5 **G** *Principles 3* (Management and control), *4* (Financial prudence) and (in so far as it relates to disclosing to the *FCA*) *11* (Relations with regulators) take into account the activities of members of a *firm's group*. This does not mean that, for example, inadequacy of a *group* member's risk management systems or resources will automatically lead to a *firm* contravening *Principle 3* or *4*. Rather, the potential impact of a *group* member's activities (and, for example, risk management systems operating on a *group* basis) will be relevant in determining the adequacy of the *firm's* risk management systems or resources respectively.

### Standards in markets outside the United Kingdom

**1.1.6** **G** As set out in ■ PRIN 3.3 (Where?), *Principles* 1 (Integrity), 2 (Skill, care and diligence) and 3 (Management and control) apply to world-wide activities in a *prudential context*. *Principle* 5 (Market conduct) applies to world-wide activities which might have a negative effect on confidence in the *UK financial system*. In considering whether to take regulatory action under these *Principles* in relation to activities carried on outside the *United Kingdom*, the *FCA* will take into account the standards expected in the market in which the *firm* is operating. *Principle* 11 (Relations with regulators) applies to world-wide activities; in considering whether to take regulatory action under *Principle* 11 in relation to cooperation with an overseas regulator, the *FCA* will have regard to the extent of, and limits to, the duties owed by the *firm* to that regulator. (*Principle* 4 (Financial prudence) also applies to world-wide activities.)

**1.1.6A** **G** ■ PRIN 4 (Principles : MiFID Business) provides *guidance* on the application of the *Principles* to *MiFID business*.

### Consequences of breaching the Principles

**1.1.7** **G** Breaching a *Principle* makes a *firm* liable to disciplinary sanctions. In determining whether a *Principle* has been breached it is necessary to look to the standard of conduct required by the *Principle* in question. Under each of the *Principles* the onus will be on the *FCA* to show that a *firm* has been at fault in some way. What constitutes "fault" varies between different *Principles*. Under *Principle* 1 (Integrity), for example, the *FCA* would need to demonstrate a lack of integrity in the conduct of a *firm's* business. Under *Principle* 2 (Skill, care and diligence) a *firm* would be in breach if it was shown to have failed to act with due skill, care and diligence in the conduct of its business. Similarly, under *Principle* 3 (Management and control) a *firm* would not be in breach simply because it failed to control or prevent unforeseeable risks; but a breach would occur if the *firm* had failed to take reasonable care to organise and control its affairs responsibly or effectively.

**1.1.8** **G** The *Principles* are also relevant to the *FCA's* powers of information-gathering, to vary a *firm's* Part 4A permission, and of investigation and intervention, and provide a basis on which the *FCA* may apply to a court for an *injunction* or restitution order or require a *firm* to make restitution. However, the *Principles* do not give rise to actions for damages by a *private person* (see ■ PRIN 3.4.4 R).

**1.1.9** **G** Some of the other *rules* and *guidance* in the *Handbook* deal with the bearing of the *Principles* upon particular circumstances. However, since the *Principles* are also designed as a general statement of regulatory requirements applicable in new or unforeseen situations, and in situations in which there is no need for *guidance*, the *FCA's* other *rules* and *guidance* or *EU regulations* should not be viewed as exhausting the implications of the *Principles* themselves.

**Responsibilities of providers and distributors under the Principles**

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*RPPD* contains *guidance* on the responsibilities of providers and distributors for the fair treatment of *customers* under the *Principles*.

## 1.2 Clients and the Principles

### Characteristics of the client

- 1.2.1 **G** *Principles 6 (Customers' interests), 7 (Communications with clients), 8 (Conflicts of interest), 9 (Customers: relationships of trust) and 10 (Clients' assets) impose requirements on firms expressly in relation to their clients or customers. These requirements depend, in part, on the characteristics of the client or customer concerned. This is because what is "due regard" (in Principles 6 and 7), "fairly" (in Principles 6 and 8), "clear, fair and not misleading" (in Principle 7), "reasonable care" (in Principle 9) or "adequate" (in Principle 10) will, of course, depend on those characteristics. For example, the information needs of a general insurance broker will be different from those of a retail general insurance policyholder.*

### Approach to client categorisation

- 1.2.2 **G** *Principles 6, 8 and 9 and parts of Principle 7, as qualified by ■ PRIN 3.4.1 R, apply only in relation to customers. The approach that a firm (other than for credit-related regulated activities in relation to which client categorisation does not apply) needs to take regarding categorisation of clients into customers and eligible counterparties will depend on whether the firm is carrying on designated investment business, insurance risk transformation and activities directly arising from insurance risk transformation, or other activities, as described in ■ PRIN 1.2.3 G.*
- 1.2.3 **G**
- (1) In relation to the carrying on of *designated investment business, insurance risk transformation* and activities directly arising from *insurance risk transformation*, a firm's categorisation of a *client* under the *COBS client* categorisation chapter (■ COBS 3) will be applicable for the purposes of *Principles 6, 7, 8 and 9*.
  - (1AA) In relation to the carrying on of *insurance risk transformation* and activities directly arising from *insurance risk transformation*, the *COBS client* categorisation chapter (■ COBS 3) applies as modified by ■ COBS 18.6A.3R.
  - (1A) *Client* categorisation under ■ COBS 3 or ■ PRIN 1 Annex 1 is not relevant to *credit-related regulated activities* and therefore the guidance on *client* categorisation does not apply in relation to a *credit-related regulated activity*. The definitions of *client* and *customer* in relation to those *regulated activities* reflect the modified meaning of "consumer" in articles 36J, 39M, 60LA, 60S and 89E of the *Regulated Activities Order*, as well as the definitions of "individual" and of "relevant recipient of credit" in that Order.

- (2) The *person* to whom a *firm* gives *basic advice* on a *stakeholder product* will be a *retail client* for all purposes, including the purposes of *Principles 6, 7, 8 and 9*.
- (3) In relation to carrying on activities other than *designated investment business, insurance risk transformation* or activities directly arising from *insurance risk transformation* (for example, *general insurance business* or *accepting deposits*) the *firm* may choose to comply with *Principles 6, 7, 8 and 9* as if all its *clients* were *customers*. Alternatively, it may choose to distinguish between *eligible counterparties* and *customers* in complying with those *Principles*. If it chooses to make such a distinction, it must comply with ■ PRIN 1 Annex 1 in determining whether that *client* is an *eligible counterparty* (see ■ PRIN 3.4.2 R). In doing so, the requirements in SYSC will apply, including the requirement to make and retain adequate records.
- (4) In relation to carrying on activities that fall within both (1) and (3) (for example, mixed *designated investment business* and *accepting deposits*), a *firm's* categorisation of a *client* under the *COBS client* categorisation chapter (■ COBS 3) will be applicable for the purposes of *Principles 6, 7, 8 and 9*.

1.2.4 G [deleted]

1.2.5 G [deleted]

1.2.6 G If the *person* with or for whom the *firm* is carrying on an activity is acting through an agent, the ability of the *firm* to treat the agent as its *client* under ■ COBS 2.4.3 R (Agent as client) will not be available. For example, if a *general insurer* is effecting a *general insurance contract* through a general insurance broker who is acting as agent for a disclosed *policyholder*, the *policyholder* will be a *client* of the *firm* and the *firm* must comply with the *Principles* accordingly.

## Non-designated investment business - clients that a firm may treat as an eligible counterparty for the purposes of PRIN

- 1.1 A *firm* may categorise the following types of *client* as an *eligible counterparty* for the purposes of *PRIN*:
- (1) a properly constituted government (including a quasi-governmental body or a government agency) of any country or territory;
  - (2) a central bank or other national monetary authority of any country or territory;
  - (3) a supranational whose members are either countries or central banks or national monetary authorities;
  - (4) a State investment body, or a body charged with, or intervening in, the management of the public debt at national level;
  - (5) another *firm*, or an *overseas financial services institution*;
  - (6) any *associate* of a *firm* (except an *OPS firm*), or of an *overseas financial services institution*, if the *firm* or institution consents;
  - (7) a *client* when he is classified as an *eligible counterparty* in accordance with 1.2; or
  - (8) a *recognised investment exchange, regulated market or clearing house*.
- 1.2 A *firm* may classify a *client* (other than another *firm, regulated collective investment scheme, or an overseas financial services institution*) as an *eligible counterparty* for the purposes of *PRIN* under 1.1(7) if:
- (1) the *client* at the time he is classified is one of the following:
    - (a) a *body corporate* (including a *limited liability partnership*) which has (or any of whose *holding companies* or *subsidiaries* has) called up share capital of at least £10 million (or its equivalent in any other currency at the relevant time);
    - (b) a *body corporate* that meets (or any of whose holding companies or subsidiaries meets) two of the following tests:
      - (i) a balance sheet total of 12.5 million euros (or its equivalent in any other currency at the relevant time);
      - (ii) a net turnover of 25 million euros (or its equivalent in any other currency at the relevant time);
      - (iii) an average number of employees during the year of 250;
    - (c) [deleted]
    - (d) a *partnership* or unincorporated association which has net assets of at least £10 million (or its equivalent in any other currency at the relevant time) (and calculated, in the case of a limited *partnership*, without deducting loans owing to any of the *partners*);
    - (e) a trustee of a trust (other than an *occupational pension scheme, SSAS, personal pension scheme or stakeholder pension scheme*) with assets of at least £10 million (or its equivalent in any other currency), calculated by aggregating the value of the cash and *designated investments* forming part of the trust's assets, but before deducting its liabilities;
    - (f) a trustee of an *occupational pension scheme* or *SSAS*, or a trustee or operator of a *personal pension scheme* or *stakeholder pension scheme* where the *scheme* has (or has had at any time during the previous two years):

- (i) at least 50 members; and
  - (ii) assets under management of not less than £10 million (or its equivalent in any other currency at the relevant time); and
- (2) the *firm* has, before commencing business with the *client* on an *eligible counterparty* basis:
  - (a) advised the *client* in writing that he is being categorised as an *eligible counterparty* for the purposes of *PRIN*;
  - (b) given a written warning to the *client* that he will lose protections under the *regulatory system*;
  - (c) for a *client* falling under (1)(a) or (b):
    - (i) taken reasonable steps to ensure that the written notices required by (a) and (b) have been delivered to a *person* authorised to take such a decision for the *client*; and
    - (ii) not been notified by the *client* that the *client* objects to being classified as an *eligible counterparty*;
  - (d) for a *client* falling under (1)(c), (d), (e) or (f):
    - (i) taken reasonable steps to ensure that the written notices required by (a) and (b) have been delivered to a *person* authorised to take such a decision for the *client*; and
    - (ii) obtained the *client's* written consent or is otherwise able to demonstrate that consent has been given.