

Guidance on marketing financial products and services to UK Local Government Pension Scheme (LGPS) clients – May 2018

The following guidance should be used as a guide only. The content is intended to be high level. Being general in nature, it may not give the answers to all of your questions or to the issues specific to your business models. This guide is not legal advice and, where firms have any doubt as to its interpretation, separate legal advice should be sought.

The guidance has been prepared on the assumption that the firms in question are UK authorised firms, with permissions limited to servicing professional clients only.

The guidance assumes firms will be promoting to UK LGPS only. If EU local authorities are targeted, different rules will apply.

While the guidance considers, at a high level, the impact of pooling, it does not provide details on how prospecting with LGPS may be affected by the introduction of pools.

A - Communicating with LGPS prior to opting-up to professional client status

Question 1 ***Can we communicate with LGPS prior to opting them up to professional client status?***

Yes.

Please note however that the (i) content of the communication; and (ii) the range of the underlying products and services being communicated must be considered in more detail.

Question 2 ***How should we approach the nature of the communication when an LGPS has not been opted-up?***

Firms should -

- (i) determine if the communication is a “**financial promotion**”; and
- (ii) if so, ensure that the content of the communication is retail-compliant and underlying products and services are limited to those suitable for retail clients; but
- (iii) if not, still ensure that the content of the communication is retail-compliant.

Question 3 ***What is a financial promotion?***

A financial promotion is “*an invitation or inducement to engage in investment activity that is communicated in the course of business*” (note that the FCA has extensive guidance at PERG 8 of the FCA Handbook as to what a “financial promotion” comprises and firms should use such guidance to judge the status of their communications accordingly).

The UK rules do not contain a definition of an “invitation” or “inducement” and therefore these terms are left to their natural meanings.

An “**invitation**” is capable of meanings ranging from merely “asking graciously or making a request to encouraging or soliciting” and “**inducement**” is given meanings ranging from “merely bringing about to prevailing upon or persuading”. Context, however, will be appropriate in determining whether these elements are satisfied.

A communication is likely to be an invitation or inducement if it (1) has the purpose or intent of leading a person to engage in investment activity and (2) is promotional in nature (it must seek, on its face, to persuade or incite the recipient to engage in investment activity).

This is an objective test and it must be determined as to whether a reasonable observer, taking account of all the

circumstances at the time the communication was made, would consider that the communicator intended the communication to persuade or incite the recipient to engage in investment activity or that that was its purpose and regard the communication as seeking to persuade or incite the recipient to engage in investment activity.

For example:

- Informal and social conversations between investment managers and representatives of local authorities over coffee in the margins of a conference are unlikely to be financial promotions.
- Educational presentations (if purely educational) are also unlikely to be financial promotions where there is no inducement angle to the presentation being delivered. A conversation between an investment manager and the representative of a local authority to walk through marketing material about the specific services that the investment manager can offer them, however, would more likely be a financial promotion.

There are specific requirements which govern communications (including financial promotions) in the FCA Conduct of Business Rules (see COBS 4) that firms will be required to comply with. Where communications are being directed at retail clients, which includes potential clients, specific content requirements are triggered.

Question 4 *What are the implications if we determine that the communication is not a financial promotion?*

If a firm determines that its communication is not a financial promotion, then the communication may be made to a prospective LGPS without requiring the LGPS to opt-up.

Note however that the LGPS remains a retail client and, as such, the content of any communication with a retail client, even where the communication does not go as far as being a financial promotion, should comply with the requirements of the FCA Conduct of Business Rules (particularly COBS 4) which set out requirements for firms when communicating with retail clients. In other words, discussions with LGPS before they are opted-up must be “**retail-compliant**”.

Question 5 *What are the implications if we determine that the communication is a financial promotion?*

If a firm determines that its communication is a financial promotion, further analysis is required (see the flowcharts in the Annex for guidance on the impact of issuing financial promotions to LGPS).

- Where (i) the content of the financial promotion is retail-compliant and (ii) it references an underlying retail-compliant service and/or product (i.e., for example, promoting a UCITS), this can be communicated to an LGPS client. There is no need for an LGPS to be opted-up to elective professional client status in order for that client to receive that communication and make an investment in the UCITS.

- Where (i) the content of the financial promotion is retail-compliant and (ii) it references a “**non-mainstream pooled investment**”¹, this can be communicated to an LGPS. There is no need for an LGPS to be opted-up to elective professional client status in order for that client to receive that communication. However, the LGPS is still likely to be required to be opted-up to elective professional client status in order for it to make an investment in the non-mainstream pooled investment if the non-mainstream pooled investment has professional investor eligibility criteria.

Note that the premise under which this communication can be issued is the relevant exemption available under COBS 4.12.4 R (restrictions on promotion of non-mainstream pooled investments). Firms can rely on the “**excluded communications**” exemption in COBS 4.12.4 R. This exemption provides that where a financial promotion would benefit from an exemption under the Promotion of Collective Investment Schemes Order 2001 (“**PCISO**”), that financial communication can be made. The PCISO has an exemption available when communicating to “**investment professionals**”. Unlike the definition of “professional clients” under the FCA Handbook rules, the definition of “investment professionals” includes “local authorities” (Art 14(5)(d) PCISO). We are of the view that it is possible that firms, where they can rely on the PCISO (or “**safe harbour**”), will not be in breach of the restrictions on promoting non-mainstream pooled investments to local authority clients provided they remain within this “safe harbour”.²

- Where (i) the content of the financial promotion is not retail-compliant; or (ii) it references products which are neither retail-compliant nor non-mainstreamed pooled investments, then this cannot be communicated to an LGPS.

Question 6 ***Do different restrictions apply depending on whether a firm wants to promote a segregated mandate or a commitment to a fund?***

No.

However, in practice where a manager’s regulatory permissions are limited to servicing professional clients only, there will be a natural restriction on them taking on an LGPS mandate unless and until the LGPS has been opted-up. In contrast, where a

¹A “**non-mainstream pooled investment**” includes any of the following investments: (a) a unit in an unregulated collective investment scheme; (b) a unit in a qualified investor scheme; (c) a security issued by a special purpose vehicle, other than an excluded security; (d) a traded life policy investment; (e) rights to or interests in investments that are any of (a) to (d). Note that we have not considered in detail any restrictions on the distribution of certain regulatory capital instruments (including contingent convertible instruments and CoCo funds). These should be considered in more detail if intended to be offered to LGPS.

² This point only considers the issue of communicating with non-opted-up LGPS clients. Therefore, before the actual provision of a service or an investment is made, further analysis must be undertaken as to whether the LGPS client should be opted-up.

manager is promoting a retail-compliant fund (such as a UCITS), provided the financial promotion is retail-compliant, an LGPS may buy units in such funds without having to be opted-up.

Question 7 *Can managers send factual information to un-opted-up LGPS clients or prospects on demand (e.g. leaver records)?*

Yes, but only if the content is purely informational and is not considered as a financial promotion. Firms should ensure that the materials are appropriate for a retail client.

Question 8 *When providing financial services to LGPS clients, firms will be required to provide the LGPS with certain information prior to the provision of the service³. Can this information be provided after an LGPS has been opted-up to professional client status?*

There are no hard and fast rules as to when exactly prior to the provision of the financial service that the information should be provided. Equally, there are no hard and fast rules as to when an LGPS may request to be opted-up from retail client to elective professional status.

Opting-up the LGPS client (and the provision of the information per COBS 3.3.1B) may occur at any time between the initial prospecting up until the point before executing the IMA, IAA or any other agreement.

Opting-up at the early stages of prospecting would reduce regulatory risk of a firm being deemed to be dealing with a retail client and would allow firms to provide information which is appropriate for professional clients.

It is appreciated that this may be impractical at the early stages of prospecting but generally, the earlier a firm opts-up a client, the lower the regulatory risk.

Question 9 *Can firms complete RFPs for anonymous LGPS investors via a consultant where they do not know who the underlying client is?*

A completed RFP would be deemed a financial promotion. Where the underlying client of the RFP is a retail client, the content of the RFP should be retail-compliant.

This becomes challenging for a firm when they have no visibility as to who the client is. As a potential solution and in order to lower risks, managers might wish to consider asking consultants to include LGPS funds' opt-up documentation in a RFP. By

³ Per COBS 3.3.1B

doing this, by the time the RFP has been responded to, the manager is able to opt-up the potential client (and would know the identity of the underlying client) in preparation of its pitch. They should then be able to market on a professional basis once the client has been opted-up.

Question 10 *Can firms request LGPS to opt-up for marketing purposes only?*

Firms should not induce or entice an LGPS to opt-up to professional client status. Any request to be opted-up should come from the LGPS. Where an LGPS does seek to be opted-up to professional client status, this can be done with prospecting in mind and not only in respect to a concluded mandate/investment.

Question 11 *If firms have separately opted-up the local authority in respect of its treasury assets, can the LGPS be treated as a professional client?*

No, the LGPS will need to be opted-up separately.

Question 12 *Do placement agents marketing their clients' funds to professional clients in the UK need to obtain written confirmation from a local authority that they have opted-up? Or can publicly available information from the LGA website on [local authorities' opt-up status](#) be relied upon?*

If a placement agent is an authorised firm and communicates with a LGPS, it will be required to categorise the LGPS in its own right in order for it to determine the nature of the communications it is entitled to issue. They cannot rely on an opt-up being carried out by another authorised firm.

B - Practical Application - Conferences

Question 1 *If a firm hosts an event, can they allow LGPS to attend the event where they are not opted-up to professional status?*

This will depend on the nature of the event itself and the scope of what the event is seeking to cover.

If the event is purely educational in nature or the content of the event is informal and only generic discussions are carried out, this may fall outside the scope of “financial promotion”. As long as the material/discussion is retail-compliant, LGPS clients who have not been opted-up can attend.

Care should be taken if these events include promotional elements and if the products and/or services are only suitable for professional investors.

The approach that a firm adopts in relation to LGPS clients should not differ from the approach the firm would otherwise adopt when dealing with any other retail client.

Question 2 *Where such an event will contain financial promotions which are either non-retail-compliant and/or reference products which LGPS cannot acquire, can firms allow LGPS to attend the event where they are not opted-up?*

Firms should not actively permit LGPS to attend such an event if they have not been opted-up to professional client status.

In practice, firms should limit invitations to LGPS attendees who have been opted-up to professional status for the services and funds which are the subject of the event.

Firms could look to hold LGPS specific events, which is a safe, albeit costly, option.

Where firms cannot limit invitations or are actively aware that retail LGPS are attending the event, firms should ensure that all financial promotions are retail-compliant and only reference appropriate products and services.

Question 3 *How should firms approach third party conferences where both professional and retail LGPS are attending?*

When promoting products and/or services to prospective LGPS at third party conferences, firms must treat LGPS as retail clients, unless and until they are opted-up to elective professional client status for the services and/or products in question.

The conference content would need to be suitable for the LGPS clients or potential clients as retail clients (note however in a non-mainstream pooled investments context, the local authorities “safe harbour” exemption explored above should be

available even if they are non-retail products).

The approach that a firm adopts in relation to LGPS clients should not differ materially from the approach that they adopt when dealing with retail clients generally.

Question 4 *When firms attend conferences, can they talk about products aimed solely at professional investors (infrastructure and real estate) or can they only talk about retail products?*

If the discussion is very generic and/or purely educational, with no financial promotion, then it is possible to discuss such products.

If the discussion is a financial promotion, firms must be satisfied that the infrastructure or real estate products are either (i) retail products; or (ii) are exempt from the restrictions on the promotion of non-mainstream pooled investments. If so, firms can discuss these products with LGPS but must still ensure that the nature of discussion is retail-compliant.

Question 5 *Is there a rule of thumb to distinguish between activities that amount to “educating” and those that amount to “promoting”?*

There are no clear regulatory lines distinguishing between activities which are “educating” and those which are “promoting”.

Firms will be required to take a view on a case-by-case basis. Where an activity is intended to procure business for a firm, it is likely to be an inducement. Where it is simply educational and does no more than enable a person, for example, to identify investment options, or educate about mechanics or risks of investments, then this is not likely to be considered as a financial promotion.

Question 6 *How would training, with or without CPD accreditation be viewed? Can firms provide product, strategy and asset class training to LGPS without an opt-up?*

Yes, if the training is purely educational and there is no promotional element. This will need to be considered on a case-by-case basis.

C - Communicating with LGPS funds as part of a pool

Question 1 ***What conversations are permitted when a firm is promoting itself to a professional client (the pool) but there are others in a room/committee that may not be opted-up to professional client status by the firm (i.e. the underlying LGPS fund)?***

Given the firm will contract with the pool and not the LGPS, it could be argued that there is no need to opt-up the LGPS as (1) any financial promotion made in the presence of those investors would be to the pool as a whole (and not to the individual investors, as they would not be able to act upon such financial promotions individually); and (2) there is no direct client relationship between the investor under the pool and the firm.

However, each pool structure is different and this may be dependent on how much discretion each LGPS has within the pool structure, which is likely to vary from pool to pool. This will also be dependent on whether the firm follows up directly with one of the LGPS. The risk would be higher if any of the LGPS funds have retained any or most of their decision-making capacity in relation to their assets in the pool or if a firm subsequently discusses the mandate/investment directly with the LGPS.

Question 2 ***When a LGPS fund joins a pool, can firms talk to those LGPS funds as professional investors under the umbrella of the pool?***

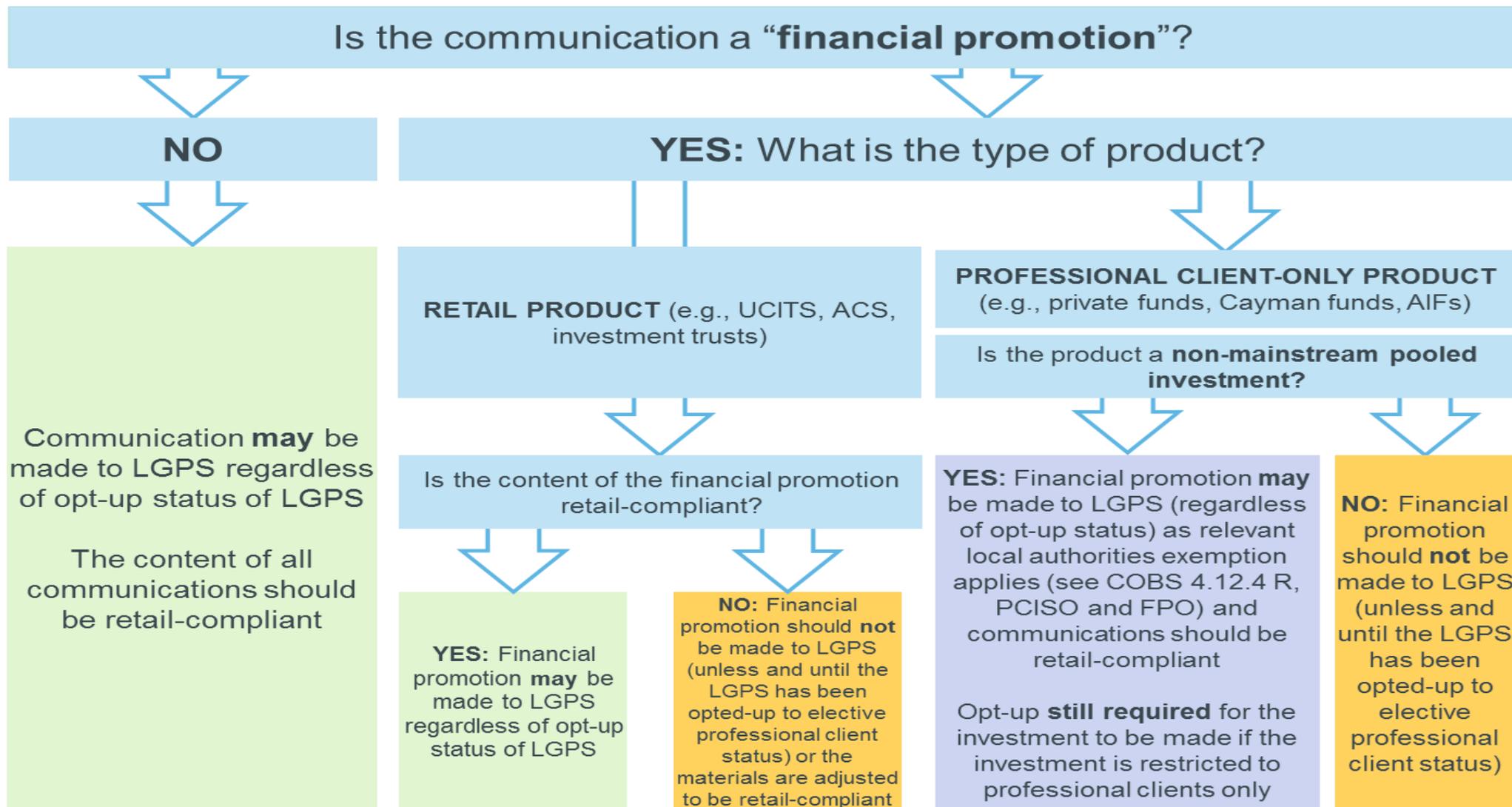
Yes, but only in the context of the investor receiving communications as an investor via the pool vehicles rather than under any separate client relationship.

This is subject to a risk assessment made by a firm if there is any likelihood that the LGPS fund could act independently of the pool as a result of the communications.

Question 3 ***Once pooled, can firms discuss asset classes, economic outlook, market commentary etc. with underlying LGPS funds without opting-up?***

This is subject to the analysis explored above relating to communications to LGPS. In practice it is likely that a firm's level of interaction with investment consultants or investment teams within the pools will increase over time. However, assuming that each LGPS maintains a level of discretion in decision-making over their own assets, any financial promotions suitable for professional clients would require the relevant LGPS fund to be opted-up before it can receive such communications. In the absence of opting-up an LGPS client, communications would have to be retail-compliant.

Communicating a PRODUCT to a retail LGPS scheme



Communicating a SERVICE to a retail LGPS scheme

