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SPOT INSPECTIONS

Summary of SPOT inspections on the marketing of SCPIs with temporary ownership dismemberment arrangements

Table of contents

1.	CONTEXT.....	3
2.	SCOPE	4
2.1.	REMINDERS ABOUT TEMPORARY OWNERSHIP DISMEMBERMENT	4
2.2.	PRESENTATION OF THE SAMPLE OF ISP INSPECTED	5
2.3.	THEMES AND METHODOLOGY APPLIED.....	6
2.4.	APPLICABLE REGULATIONS	6
3.	FINDINGS AND ANALYSIS	7
3.1.	FRAMEWORK FOR SUBSCRIBING TO SCPI UNITS WITH TEMPORARY OWNERSHIP DISMEMBERMENT ..	8
3.1.1.	Committees, procedures and resources	8
3.1.2.	Governance of financial instruments	9
3.1.3.	Verification of suitability and/or appropriateness	11
3.1.4.	Information on costs and charges.....	13
3.2.	CHARACTERISTICS OF TEMPORARY OWNERSHIP DISMEMBERMENT APPLIED TO SCPI UNITS	14
3.2.1.	Oversight of relations with SGP partners.....	14
3.2.2.	Calculating dismemberment keys	16
3.2.3.	Search for counterparties	17
3.3.	MANAGING CONFLICTS OF INTEREST AND COMPLIANCE PROCEDURES	18
3.3.1.	Managing conflicts of interest	18
3.3.2.	Compliance system	19

1. CONTEXT

In accordance with the supervisory priorities of the Autorité des Marchés Financiers (hereinafter, 'AMF') for 2023¹, a series of short thematic inspections ('SPOT'²) were carried out between April and August 2023 on the marketing of units in SCPIs³ with temporary ownership dismemberment arrangements. The investigations focused on a panel of four investment services providers (hereinafter, 'ISP') and covered the period from 1 January 2020 to 31 December 2022.

Temporary ownership dismemberment is a special form of subscription that splits ownership rights into bare ownership on the one hand, and usufruct on the other. Given the differences, particularly in terms of income received, costs and charges incurred, and liquidity, the acquisition of SCPI units with a temporary ownership dismemberment arrangement cannot be treated in the same way as the acquisition of SCPI units with full ownership.

In early 2023, the AMF Enforcement Committee fined a financial investment advisor (FIA) for failing to inform their clients of commissions received for providing investment advice in connection with the marketing of SCPI units with temporary ownership dismemberment⁴. While this decision served as a reminder of the need to adapt the information provided to the products recommended, the Enforcement Committee also highlighted the "*difficulties in interpreting the provisions [...] relating to the information obligations incumbent on operators in the specific case of the marketing of SCPI units with temporary ownership dismemberment, in the absence of any clarification on this point from the regulator*"⁵.

The inspection observed that institutions take very limited account of the specific features of temporary ownership dismemberment when providing investment services in relation to SCPIs.

This document does not represent an opinion or recommendation. The practices identified as 'good' or 'poor' highlight the approaches observed during the inspections, which are likely to either encourage or discourage compliance with the rules governing the marketing of SCPI units with temporary ownership dismemberment. The regulatory reminders in the boxes in section 3 correspond to regulatory breaches found during inspections of the institutions on the panel.

¹ These supervisory priorities can be consulted at the following link: <https://www.amf-france.org/sites/institutionnel/files/private/2023-01/2023%20AMF%20Supervisory%20Priorities.pdf>

² SPOT: Supervision of Operational and Thematic Practices (Supervision des Pratiques Opérationnelle et Thématique).

³ The SCPI (*Société Civile de Placement Immobilier*) is an unlisted real estate investment vehicle supervised by the AMF.

⁴ Enforcement Committee, decision No. 2 of 15 February 2023, available at the following link: <https://www.amf-france.org/sites/institutionnel/files/private/2023-02/d%C3%A9cision%20pub.pdf>

⁵ *Ibid.*, page 26.

2. SCOPE

2.1. REMINDERS ABOUT TEMPORARY OWNERSHIP DISMEMBERMENT

Temporary ownership dismemberment is a special form of subscription that splits the right of ownership between:

- a bare owner, who holds the bare ownership, i.e. the right to dispose of the property (*abusus*), and;
- a usufructuary, who holds the usufruct, i.e. the rights to use (*usus*) and receive income (*fructus*).

The two parties share the prerogatives associated with ownership of the SCPI units (bare ownership/usufruct) for a fixed period (the duration of the ownership dismemberment), which is determined in advance. While this period can range from 3 to 20 years, the inspection mission found that the average period for the subscriptions of the four institutions was eight years. During the dismemberment period:

- the bare owner holds the bare ownership of the SCPI units, but does not receive any income;
- the usufructuary is the sole beneficiary of any income, particularly dividends, that the SCPI units may generate. In return, they alone pay the indirect costs for the duration of the dismemberment.

The prices paid by the usufructuary and the bare owner are lower than the value of the share in full ownership and result from an allocation key based on the expected duration of the dismemberment, calculated, in principle, on the basis of an economic valuation. Subscription fees are paid by both counterparties in proportion to the allocation key. This offer is available to both natural persons and legal entities.

As regards the search for a counterparty or counterparties, once the client has decided to subscribe to an SCPI unit with temporary ownership dismemberment, the ISP distributor, if it does not itself identify a counterparty, has the option of forwarding the subscription file directly to the corresponding asset management company, which will then be responsible for finding a counterparty to enable the transaction to be carried out.

As a result, the profiles of the bare owner and the usufructuary differ significantly.

The bare owner is generally a taxpayer with substantial income and assets, who is often liable for the tax on property wealth (hereafter, 'IFI') and wishes to have additional future income. In this respect, subscribing for the bare ownership of SCPI units can have the following advantages:

- building up assets (in capital or debt) while paying only a proportion of the price of full ownership;
- not being taxed at the end of the dismemberment when full ownership is reconstituted;
- not being liable for IFI on the investment for the duration of the dismemberment.

On the other hand, the usufructuary is generally a taxpayer wishing to receive additional income with a reduced initial investment, or an institutional investor wishing to make a cash investment. In this respect, subscribing to SCPI units in usufruct can have the following advantages:

- receiving regular income over a fixed period;
- receiving income on the value of full ownership in return for subscribing at a discount to the full ownership subscription price.

The inspection analysed the subscriptions of SCPI units with temporary ownership dismemberment carried out by the four institutions on the panel over the financial years 2021 to 2023. Over this period, 99.3% of the bare-ownership subscriptions of the four institutions (52% of temporary ownership dismemberment subscriptions) were subscribed by natural persons and 0.7% by legal entities (mainly real estate investment companies), while 15.7% of the usufruct subscriptions of the four institutions (48% of temporary ownership dismemberment subscriptions) were subscribed by natural persons and 84.3% by legal entities.

2.2. PRESENTATION OF THE SAMPLE OF ISP INSPECTED

These SPOT inspections were carried out jointly at five credit institutions or investment firms authorised to provide investment services.

To compile its panel, the AMF selected institutions from among the ISPs⁶ that had marketed SCPI units with temporary ownership dismemberment between 1 January 2020 and 31 December 2022 (hereinafter, the ‘**inspected period**’). The selection was sufficiently varied to identify the different practices used in the market. The four institutions selected show a high level of heterogeneity in terms of:

- *size*: the institutions selected vary significantly in terms of NBI, assets under management and staffing levels in this field;
- *target clientele*: three institutions only offer SCPIs using this particular subscription method to wealthy clients, while the fourth sets no restrictions;
- *marketing used*: three institutions have a passive attitude to this particular subscription method, while the fourth actively advertises it;
- *number of subscriptions*: three institutions have only sold a relatively small volume of these products using this particular subscription method, due to the absence of a proactive approach, whereas this subscription method is associated with a larger volume of transactions for the fourth institution on the panel.

The main characteristics of the distribution strategies adopted by the institutions on the panel, together with information on the volumes associated with SCPI unit subscriptions through temporary ownership dismemberment, are summarised in the table below:

**Table 1 - Distribution strategies and sales volumes
for SCPI units with temporary ownership dismemberment**

Item/Institution	ISP A	ISP B	ISP C	ISP D
Investment services used for marketing	Investment advice	Investment advice	Investment advice	Investment advice or RTO
Sales network (internal and/or external ⁷)	Internal	External	Internal	Internal and external
Number of subscriptions with temporary ownership dismemberment ⁸	< 100	< 100	< 100	> 100
Percentage of temporary ownership dismemberment in SCPI unit subscriptions ⁹	25.0%	23.1%	8.5%	9.9%

⁶ The inspections did not therefore cover the practices of portfolio asset management companies or financial investment advisers.

⁷ Some ISP distributors use an external sales network comprised of, for example, ISP or financial investment advisors (FIA).

⁸ This is the number of SCPI units subscribed under temporary ownership dismemberment arrangements during the inspected period.

⁹ This is the percentage of outstanding amounts of SCPI units subscribed under temporary ownership dismemberment arrangements (over the inspected period) out of total SCPI units subscribed over the inspected period.

2.3. THEMES AND METHODOLOGY APPLIED

The following themes were covered during these inspections:

- the framework for subscribing to SCPI units with temporary ownership dismemberment, through a study of:
 - o *the consideration given to temporary ownership dismemberment within the institution's procedures, committees and resources;*
 - o *the governance of financial instruments as applied to subscriptions to dismembered SCPI units;*
 - o *the verification of the suitability/appropriateness of the financial instruments and investment services provided, and;*
 - o *the information provided to clients as regards the costs and charges involved in subscribing to dismembered SCPI units;*
- the features of temporary ownership dismemberment applied to the SCPI units by analysing:
 - o *the oversight of the commercial relationship with partner portfolio asset management companies (AMCs);*
 - o *how dismemberment keys are calculated;*
 - o *the search for a counterparty;*
- the management of conflicts of interest and compliance control mechanisms in relation to this theme.

For each of the institutions inspected, the inspection mission analysed in particular:

- any existing documentation governing the specific arrangements for subscribing to SCPI units by means of temporary ownership dismemberment (committee minutes, procedures, operating methods, training modules, internal documents, etc.);
- subscription forms, questionnaires for assessing the suitability and/or appropriateness of the financial instruments and investment services provided;
- distribution agreements between the ISPs on the panel, the distributors of the SCPI marketed, and the investment management companies responsible for managing these collective investments;
- the mapping of conflicts of interest;
- audit plans, priority risk maps and lists of second-level controls that have covered the theme, where applicable.

In addition, in order to deepen its investigation and assess the operational implementation of the aforementioned obligations and measures, the inspection mission analysed samples of subscription files.

2.4. APPLICABLE REGULATIONS

The inspection mission based its work in particular on:

- Articles L. 533-10, II. 1) of the Monetary and Financial Code (hereinafter, '**CMF**') and 22 of Delegated Regulation (EU) No. 2017/565 on the obligation to have operating rules and procedures;
- Article 313-19 of the AMF General Regulation (hereinafter, '**AMF GR**') on the obligation to set up an appropriate system of governance for financial instruments, in light of ESMA Guidelines No. 35-43-620;
- Articles L. 533-13 and L. 533-15 of the CMF on the requirements for assessing the suitability of the services provided or the financial instruments recommended, and Articles 54 and 55 of Delegated Regulation (EU) No. 2017/565 in light of points 33 to 43 of ESMA Guidelines No. 35-43-1163¹⁰;
- Article 55 of Delegated Regulation (EU) No. 2017/565, in light of points 35 and 36 of ESMA Guidelines No. 35-43-3006 on the requirements related to the assessment of the appropriateness of the investment service provided;
- Articles L. 533-12 of the CMF and 50 of Delegated Regulation (EU) No. 2017/565 on the obligation to provide full ex-ante information relating to the costs and charges associated with the financial instrument and the investment service provided;

¹⁰ Version valid until 2 October 2023.

- Articles L. 533-1 of the CMF and 314-3 of the AMF GR on the obligation to act honestly, fairly and professionally in the best interests of clients and the integrity of the market;
- Articles L. 533-12-4 of the CMF and 314-14 of the AMF GR on the requirements relating to fees, commissions and non-monetary benefits, in light of AMF Position-Recommendation DOC-2013-10;
- Articles L. 533-10 II. 3) of the CMF and 33 of Delegated Regulation (EU) No. 2017/565 on identifying and managing conflicts of interest;
- Articles L. 533-10. II, 1) of the CMF, 22 2) of Delegated Regulation (EU) No. 2017/565 and 312-1 of the AMF GR on requirements relating to the compliance mechanism.

3. FINDINGS AND ANALYSIS

It should be noted at the outset that the marketing of SCPI units with temporary ownership dismemberment is marginal within the business of the four institutions on the panel in two respects. Firstly, SCPI-backed assets do not make up the majority of their assets in real estate vehicles. Secondly, of the SCPI-backed assets, only a minority (between 9% and 25%, see Table 1) are backed by subscriptions in temporary ownership dismemberment. This marginal nature was put forward by the institutions to justify the absence of specific due diligence for this particular subscription method.

However, temporary ownership dismemberment does constitute a special subscription method that does not have the same impact on clients' investments as full ownership. These significant differences can be seen in:

- *the income received*: subscribing to the bare ownership of SCPI units means forgoing the income distributed by the SCPI throughout the dismemberment period;
- *the costs and charges incurred*: costs and charges are divided differently between the bare owner and the usufructuary during the dismemberment period;
- *liquidity*: while SCPI are already financial instruments with low liquidity, dismembering them further reduces the liquidity of the SCPI units held for the duration of the dismemberment period;
- *the investment horizon*: while the recommended holding period for an SCPI is approximately 10 years, the dismemberment period applied to investments does not necessarily match, and may therefore be shorter or longer.

The inspection mission noted that the institutions on the panel have not always taken the consequences of these major differences into account in their arrangements for marketing SCPI units with temporary ownership dismemberment. The low volume of this activity should not exempt institutions from their professional obligations. In the course of its investigations, the inspection mission issued eight regulatory reminders, and identified four good practices and ten poor practices. The graph below compares the situation of each of the institutions inspected.



3.1. FRAMEWORK FOR SUBSCRIBING TO SCPI UNITS WITH TEMPORARY OWNERSHIP DISMEMBERMENT

The marketing of SCPI units with temporary ownership dismemberment requires institutions to check in advance that the specific features of this particular subscription method are covered by operational rules and procedures that ensure compliance with professional obligations, particularly with regard to the governance of financial instruments, the suitability of the financial instrument recommended and the information provided to clients.

3.1.1. Committees, procedures and resources

Issues and focus

Faced with the complexity of this type of marketing, which is recognised by the institutions, they cannot rely on a culture of verbal communication to ensure that clients take these specific features into account. Therefore, the inspection mission analysed all the documentation available on the subject at the institutions on the panel (minutes of new product committee meetings, procedures, operating methods, training modules, internal documents, etc.), in order to assess whether it reflected the different methods of subscribing to SCPI units.

The inspection mission found that **most of the institutions on the panel did indeed identify the subscription of SCPI units with temporary ownership dismemberment as a special case requiring the addition of specific conditions**, and did so as early as the committee overseeing the marketing of a new product, either by distinguishing the decision to market SCPI units with temporary ownership dismemberment from the decision to

market them under full ownership, or by restricting dismemberment to SCPI with a track record of performance and no liquidity problems.

However, the inspection mission found that two institutions did not have procedures governing the specific terms and conditions for subscribing to SCPI units with temporary ownership dismemberment, which could contravene the provisions of Articles L. 533-10, II. 1) of the CMF and 22, 1. of Regulation (EU) No. 2017/565.

Lastly, three institutions have stepped up support for their clients by providing a training module specific to dismemberment or the services of a wealth management specialist prior to subscription.

Regulatory reminder 1:

- **Article L. 533-10 of the CMF:** "[...] II.-Investment services providers other than portfolio asset management companies shall: 1) Implement rules and procedures to ensure compliance with the provisions applicable to them [...]"
- **Article 22 of Regulation (EU) No. 2017/565:** "1. Investment firms shall establish, implement and maintain adequate policies and procedures designed to detect any risk of failure by the firm to comply with its obligations under Directive 2014/65/EU, as well as the associated risks, and put in place adequate measures and procedures designed to minimise such risk [...]"

Good practices:

- Having a training module for clients on the specific conditions of temporary ownership dismemberment.
- Organising a consultation with a wealth management specialist before offering clients the special subscription option of temporary ownership dismemberment.

Poor practice:

- Failing to address the issue of the marketing of SCPI units with temporary ownership dismemberment during the committee meeting held to oversee the marketing of a new product.

3.1.2. Governance of financial instruments

Issues and focus

The distributor must ensure that the financial instrument and the service it intends to provide or recommend are compatible with the needs, characteristics and objectives of the defined target market, and that the distribution strategy is compatible with this target market. Temporary ownership dismemberment has an impact on client investment characteristics and warrants a critical analysis of the distribution strategy adopted as compared with the full ownership subscription method. Institutions must be able to demonstrate that their governance arrangements for financial instruments take due account of these specificities.

Therefore, the inspection mission checked whether the ISPs had carried out an analysis to verify that dismemberment was compatible with the positive target markets, the negative target markets and the distribution strategy in force at their institution.

The inspection mission found that **only one institution had carried out such an analysis**, and that this had led it to adapt its financial instrument governance system, in particular because of the tax advantages that may justify the use of this particular subscription method. This institution then tightened the conditions for marketing SCPIs with temporary dismemberment by excluding SCPIs during their first year of existence (in particular, due to the absence of a performance history) or those experiencing liquidity problems (in particular, those that have a redemption fund¹¹).

By failing to take account of the specific features of temporary ownership dismemberment in their financial instrument governance arrangements, three other institutions might fail to comply with Articles L. 533-24-1 of the CMF and 333-19 of the AMF GR in light of ESMA Guidelines No. 35-43-620.

Regulatory reminder 2:

- **Article L. 533-24-1 of the CMF:** *"Investment services providers offering, recommending or marketing financial instruments shall:

 - 1) Ensure that they understand the characteristics of these financial instruments and assess their compatibility with the needs of the clients to whom they provide investment services, in particular in relation to the defined target market;
 - 2) Ensure that financial instruments are offered or recommended solely in the interests of the client;
 - 3) Regularly review these financial instruments, taking into account any event that could significantly influence the potential risk to the defined target market, in order to assess, as a minimum, whether these instruments continue to meet the needs of the defined target market and whether the planned distribution strategy remains appropriate;
 - 4) If they do not devise these financial instruments, have appropriate systems for obtaining the information referred to in 3) of Article L. 533-24 and for understanding the characteristics and identifying the target market defined for each financial instrument "*
- **Article 313-19 of the AMF GR:** *"The distributor shall put in place adequate financial instrument governance arrangements to ensure that the financial instruments and services it intends to offer or recommend are compatible with the needs, characteristics, and objectives, including any sustainability objectives, of an identified target market and that the intended distribution strategy is consistent with the identified target market. [...] As part of this process, it shall define any group(s) of clients that have needs, characteristics and objectives that are not compatible with the financial instrument or service distributed [...]"*
- **Guideline 21 of ESMA Guidelines No. 35-43-620:** *"21. The identification of the potential target market should be done in an appropriate and proportionate manner, considering the nature of the investment product. This means that the target market identification should consider the characteristics of the product including its complexity (including costs and charges structure), risk-reward profile or liquidity, or its innovative character"*

Poor practice:

- Not strengthening the conditions required to market SCPIs with temporary ownership dismemberment.

¹¹ For example, the general meeting of shareholders of an SCPI may decide to set up a redemption fund in order to contribute to the fluidity of the unit market. In practice, this reflects a lack of liquidity on the market for the SCPI units.

3.1.3. Verification of suitability and/or appropriateness

Issues and focus

When providing investment advice, or services for the reception and transmission of orders on behalf of third parties, institutions are required to assess the suitability or appropriateness of the financial instrument recommended. It is therefore important that the client understands the characteristics of the financial instrument subscribed. When providing investment advice, institutions must also be able to justify why clients should acquire SCPI units on a temporary dismemberment basis rather than on a full ownership basis.

For the suitability test, points 35 to 43 of ESMA Guidelines No. 35-43-1163 state that **the extent of the information to be gathered from clients must take into account the specific features of the investment advice service and the financial instruments offered.**

For the appropriateness test, points 35 and 36 of ESMA Guidelines No. 35-43-3006 state that **ISPs should not base their appropriateness assessment questions solely on the characteristics of the asset class to which the financial instrument belongs**, but should also include any specific features of the service offered.

Therefore, the inspection mission verified whether the institutions on the panel had taken account of the specific features of temporary ownership dismemberment in assessing the suitability and/or appropriateness of the financial instrument or service provided.

With regard to the assessment of suitability, the inspection mission found that almost no account was taken of the specific features of temporary ownership dismemberment. **By failing to justify the appropriateness of the particular subscription method recommended (temporary ownership dismemberment) for the investor profile of their clients, three institutions might not be complying with the provisions of Articles L. 533-13 and L. 533-15 of the CMF, and Articles 54 and 55 of Delegated Regulation (EU) No. 2017/565 viewed in light of ESMA Guidelines No. 35-43-1163.**

Similarly, with regard to the assessment of appropriateness, the inspection mission found, where relevant, that the system was inadequate. **By not including, in its suitability assessment questionnaire, any question on the specific method of subscribing to SCPI units by means of temporary ownership dismemberment, an institution might fail to comply with Article 55 of Delegated Regulation 2017/565 viewed in light of ESMA Guidelines No. 35-43-3006.**

Regulatory reminders 3 and 4:

- **Article L. 533-13 of the CMF:** "I.-With a view to providing the services mentioned in 4 or 5 of Article L. 321-1, investment service providers other than portfolio asset management companies shall obtain the necessary information about the investment knowledge and experience of their clients, including potential clients, in relation to the specific type of financial instrument or service, their financial situation, including their capacity to bear losses, and their investment objectives, including their risk tolerance, so as to be able to recommend to them the appropriate investment services and financial instruments adapted to their risk tolerance and capacity to bear losses. [...] II. -With a view to providing a service other than those mentioned in I, investment service providers other than portfolio asset management companies shall ask their clients, including potential clients, for information about their investment knowledge and experience in relation to the specific type of financial instrument or service offered or requested, in order to be able to determine whether the service or financial instrument is appropriate".
- **Article L. 533-15 of the CMF:** "I.-Investment service providers other than portfolio asset management companies shall report to their clients, on a durable medium, on the services provided to them. The report shall include periodic communications to clients depending on the type and complexity of the financial instruments concerned, and the nature of the service provided to clients and, where appropriate, the costs associated with the transactions carried out and the services provided on behalf of clients. [...] II. - Investment service providers other than the portfolio asset management companies which provide the investment service referred to in Article L. 321-1 5) shall provide clients, prior to the transaction, with a suitability statement on a durable medium, specifying the advice provided and the extent to which it meets the preferences, objectives and other characteristics of retail clients".
- **Article 54 of Delegated Regulation (EU) No. 2017/565:** "[...] 2. Investment firms shall determine the extent of the information to be collected from clients in light of all the features of the investment advice or portfolio management services to be provided to those clients. Investment firms shall obtain from clients or potential clients such information as is necessary for the firm to understand the essential facts about the client and to have a reasonable basis for determining, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of providing a portfolio management service, satisfies the following criteria:
 - a) it meets the investment objectives of the client in question, including client's risk tolerance;
 - b) it is such that the client is able financially to bear any related investment risks consistent with his investment objectives;
 - c) it is such that the client has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio".
- **Article 55 of Delegated Regulation (EU) No. 2017/565:** "1. Investment firms shall ensure that the information regarding a client's or potential client's knowledge and experience in the investment field includes the following, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved:
 - a) the types of service, transaction and financial instrument with which the client is familiar;
 - b) the nature, volume, and frequency of the client's transactions in financial instruments and the period over which they have been carried out;
 - c) the level of education, and profession or relevant former profession of the client or potential client".
- **Point 36 of ESMA Guidelines No. 35-43-1163:** "36. For example, when providing access to complex or risky financial instruments, firms should carefully consider whether they need to collect more in-depth information about the client than they would collect when less complex or risky instruments are at stake. This is so that firms can assess the client's capacity to understand, and financially bear, the risks associated

with such instruments. For such complex products ESMA expects firms to carry out a robust assessment amongst others of the client's knowledge and experience, including, for example, his ability to understand the mechanisms which make the investment product "complex", whether the client has already traded in such products (for example, derivatives or leverage products), the length of time he has been trading them for, etc."

- **Point 35 of ESMA Guidelines No. 35-43-3006:** "35. Depending on the level of complexity of the investment products involved, the firm should assess the client's knowledge and experience more specifically than solely on the basis of the type to which the product belongs (e.g., subordinated debt instead of bonds in general)".

Poor practice:

- Failing to:
 - o talk to clients beforehand to ensure that they understand the consequences of temporary ownership dismemberment;
 - o send clients a presentation of this special subscription option, and a description of the typical profiles of a bare owner and a usufructuary, including the associated benefits and risks.

3.1.4. Information on costs and charges

Issues and focus

When institutions present their calculations of costs and charges *ex-ante*, these must be based on the types of costs actually incurred by the client. Institutions must take account of the impact of temporary ownership dismemberment on the costs and charges borne by investors in their presentation to clients, and present the specific features of a bare ownership or usufruct SCPI unit subscription compared with a full ownership subscription. It is important for institutions to differentiate the profitability profiles of these different subscription method options.

Therefore, the inspection mission set out to check that the institutions on the panel had taken these specific features into account when presenting the costs and charges for subscribing to SCPI units through temporary ownership dismemberment to clients.

- **For a bare ownership investment, a distinction must be made between:**
 - o the dismemberment period: the client does not bear the recurrent costs of the SCPI (management fees, transaction fees, etc.) and in return receives no income;
 - o the full ownership period: the client bears the recurrent costs and receives the dividends paid by the SCPI.
- **For a usufruct investment,** the client only bears the recurrent costs during the dismemberment period. In addition, reference to a '*recommended holding period*' is inappropriate, since the term of the dismemberment determines the term of the investment.

The inspection mission found that **none of the institutions took sufficient account of the specific features of temporary ownership dismemberment in the information provided on costs and charges.** In most cases, the information provided on costs and charges is identical for full ownership, bare ownership and usufruct. In addition, the system remains inadequate when recurrent costs are indeed allocated in full to the usufructuary, but the duration of the dismemberment is not taken into account, or when the information provided takes into account the duration of the dismemberment, but does not mention any of the SCPI's recurrent charges.

By not adapting the information on costs and charges provided to clients to the nature of the ownership of the units subscribed, and by not taking into account the allocation key and the duration of the dismemberment (in particular by not allocating all recurrent costs to the usufructuary for the entire duration of the dismemberment), institutions might be contravening the provisions of Articles L. 533-12 of the CMF and 50 of Delegated Regulation (EU) No. 2017/565.

Regulatory reminder 5:

- **Article L. 533-12 of the CMF:** "I. - All information, including promotional marketing material, sent by an investment services provider other than a portfolio asset management company to clients, including potential clients, shall be accurate, clear and not misleading. Promotional marketing material shall be clearly identifiable as such.
II.- Investment service providers other than portfolio asset management companies shall provide their clients, including potential clients, with appropriate and timely information about the investment service provider other than a portfolio asset management company, and its services, the financial instruments and investment strategies offered, the execution venues and all related costs and charges. [...]
III.- The information referred to in II shall be provided in a comprehensible form so that clients, in particular potential clients, can reasonably understand the nature of the investment service and the specific type of financial instrument offered, as well as the associated risks, in order to enable clients to make informed investment decisions".
- **Article 50 of Delegated Regulation (EU) No. 2017/565:** "[...] 8. Where calculating costs and charges on an ex-ante basis, investment firms shall use actually incurred costs as a proxy for the expected costs and charges. [...]"

Poor practices:

- In the case of bare-ownership subscriptions, the suitability report does not clearly state that no income will be received during the dismemberment period.
- Failing to clearly indicate the absence of recurrent costs for the bare-owner client during the dismemberment period.

3.2. CHARACTERISTICS OF TEMPORARY OWNERSHIP DISMEMBERMENT APPLIED TO SCPI UNITS

3.2.1. Oversight of relations with AMC partners

Issues and focus

Compared to subscribing under full ownership, temporary ownership dismemberment involves additional interaction between the SCPI's AMC and the ISP distributing the SCPI, whether in terms of the dismemberment period offered, calculating the allocation keys for the bare owner and the usufructuary, or finding counterparties. Therefore, institutions need to determine who is responsible for what, otherwise there is a risk that the system will be weakened, to the detriment of investors. It is important for institutions to be aware of this ecosystem and its interdependencies, which could generate conflicts of interest.

The inspection mission ensured that the distribution institutions on the panel had signed a distribution agreement with each asset management company whose SCPI they distribute under temporary ownership dismemberment

arrangements. The inspection mission then analysed these agreements to check whether this particular subscription method was contractually regulated between producers and distributors.

This analysis showed that **none of the institutions on the panel had a contractual framework for this particular type of subscription**. The distribution agreements only mention the names of the SCPI and the associated remuneration scheme, and say nothing about temporary ownership dismemberment. **The contractual framework between the producer and the distributor contains no provisions to govern the dismemberment periods offered to clients, the calculation and possible transmission of allocation keys, potential conflicts of interest or the additional information to be provided to clients.**

In addition, the inspection mission also identified incentive payments with a threshold effect in the remuneration schemes for marketing SCPI. Investment services providers must not receive any fee or commission in connection with the provision of an investment service, unless the purpose of the payment is to improve the quality of the service concerned to the client and is not detrimental to compliance with the provider's obligation to act honestly, fairly and professionally in the best interests of the client.

In the absence of justification, marketing an SCPI with a remuneration scheme that has a threshold effect might not comply with Articles L. 533-12-4 of the CMF and 314-14 of the AMF GR, in the light of AMF Position-Recommendation DOC-2013-10.

Regulatory reminder 6:

- **Article L. 533-12-4 of the CMF:** *"Investment service providers [...] must not pay or receive any fee or commission, or provide or receive any non-monetary benefit in connection with the provision of an investment or related service to any person other than the client or the person acting on behalf of the client, unless the payment or benefit is intended to enhance the quality of the service concerned to the client and is not detrimental to compliance with the provider's obligation to act honestly, fairly and professionally in the best interests of the client."*
- **Article 314-14 of the AMF GR:** *"A fee, commission or non-monetary benefit shall be considered to be designed to enhance the quality of the relevant service to the client if all of the following conditions are met: 1. it is justified by the provision of an additional or higher level service to the relevant client, proportional to the level of inducements received [...] 2. it does not directly benefit the recipient service provider, its shareholders or employees without tangible benefit to the relevant client [...]"*
- **AMF Position-Recommendation DOC-2013-10 (excerpt):** *"Position: Like the CESR, the AMF considers that an ISP providing investment advice to investors that enters into a distribution agreement with an issuer or producer of products that includes an incentive fee with a threshold effect will be presumed not to be acting in the best interests of its clients and will have to be able to prove that it acted in the best interests of its clients"*.

Poor practices:

- Not regularly updating the distribution agreements entered into with the portfolio asset management companies managing the SCPI whose units are being distributed.
- Failing to provide a framework for temporary ownership dismemberment in the contractual documentation drawn up with the investment management companies of the SCPI marketed, in particular stipulating the dismemberment periods offered to clients, the calculation and possible transfer of allocation

keys, potential conflicts of interest or the additional information to be provided to clients about this particular subscription method.

3.2.2. Calculating dismemberment keys

Issues and focus

Dismemberment keys have two components: the length of the dismemberment period and the associated allocation key. Depending on the dismemberment period desired, the institutions present their clients with an allocation key, which determines the percentage of the price of a share in full ownership that they will have to pay. The counterparty will pay the remaining percentage of the price of a share in full ownership.

Firstly, the inspection mission questioned the division of responsibilities between asset management companies and distributors in calculating the dismemberment keys. In practice, the inspection mission found that the institutions on the panel did not themselves calculate, as distributors, the dismemberment keys offered to their clients. Therefore, the asset management companies choose the number of dismemberment periods for which they provide a distribution key and the value of this key.

Secondly, the inspection mission analysed the distribution keys offered to clients. Dismemberment periods can range from 3 to 20 years and are all offered by at least one institution on the panel. It is therefore interesting to compare the dismemberment period chosen with the recommended holding period for each SCPI, as the majority of subscriptions made with temporary ownership dismemberment have dismemberment periods that differ from the SCPI's recommended holding period (either shorter or longer).

This situation, where two distinct time horizons coexist, adds complexity to the client's investment in an already complex financial instrument:

- if the duration of the dismemberment is less than the recommended holding period, the client should not deduce from this that an exit before the recommended holding period is desirable;
- if the dismemberment period exceeds the recommended holding period, the client must be aware that it will be more difficult to exit before the end of the dismemberment, even if the recommended holding period has been observed.

It is therefore important for investors to be properly informed.

Good practices:

- Tracking the information provided to clients on the specific features of temporary ownership dismemberment and, in particular, providing precise information on the impact of a dismemberment period that differs from the recommended holding period.
- Setting up a system to retrieve the updated values of dismemberment keys and the associated controls.

3.2.3. Search for counterparties

Issues and focus

Each temporary ownership dismemberment subscription requires two parties: a usufructuary and a bare owner. When both parties are identified (temporary ownership dismemberment within the family, for example), institutions do not need to look for a counterparty. If only one of the two parties is identified by the distributing institution, one or more counterparties must be found before the transaction can go ahead.

In practice, with very few exceptions, clients decide to subscribe to SCPI units with temporary ownership dismemberment without first identifying a counterparty, so distributors or producers must find a counterparty for their clients' investment. It is therefore important to know who these counterparties are, how they are identified and what information is passed on to investors.

In the majority of cases, this search for a counterparty is entrusted to the producing asset management companies: three distributing institutions do not allow themselves to search for the counterparty among their clients. The situation is different for one institution, because it has been delegated the task of keeping the register by the asset management company that produces the SCPI it distributes. This institution, unlike the other three, searches for the counterparty itself by issuing search mandates¹².

However, the inspection mission identified shortcomings in the information provided to clients:

- in some cases, an SCI belonging to the same group as the AMC managing the SCPI may act as counterparty;
- when multiple counterparties can compensate for their investment.

Poor practices:

- If the SCPI's asset management company is responsible for finding the counterparty, not informing clients that the counterparty may be an entity belonging to the same group as the AMC, which also sets the dismemberment keys.
- Failing to inform the client of the possibility that they may be linked to not just one but several counterparties, which will make it more difficult for them to sell their units if the counterparties have pre-emptive rights: they will have to contact not just one but all the counterparties prior to the sale because of their pre-emptive rights.
- Failing to monitor the procedures for finding counterparties for each SCPI marketed by making an inventory of the various possible scenarios.

¹² Clients instruct the asset management company of the SCPI in which they have subscribed to a dismembered unit to find a counterparty for their subscription that complies with the characteristics of the latter (in terms of the number of units, the dismemberment period or the allocation key, for example). In practice, the mandated asset management company (or the ISP distributor, if the asset management company has delegated the task) issues a search mandate in order to identify a usufructuary counterparty if the client has subscribed to the SCPI units as bare owner, or a bare owner counterparty if the client has subscribed to the SCPI units as usufructuary.

3.3. MANAGING CONFLICTS OF INTEREST AND COMPLIANCE SYSTEM

3.3.1. Managing conflicts of interest

Issues and focus

The marketing of SCPI units through temporary ownership dismemberment is backed by an ecosystem involving a large number of players. Therefore, institutions must be particularly vigilant about the potential conflicts of interest that could arise. The latter must be identified and governed in order to protect clients' interests. By way of an example, the inspection mission noted that a company belonging to the same group as the distributor or the SCPI's AMC could act as usufructuary counterparty for the investments of bare owner clients, or that a distributor could look for a counterparty for an investment among its own clients. These situations are all potential conflicts of interest that require supervision by the institutions.

If the potential conflicts of interest arising from the marketing of SCPIs with temporary ownership dismemberment are not identified and regulated, the institutions on the panel might be in breach of the provisions of Articles L. 533-10, II, 3) of the CMF and 33 of Delegated Regulation (EU) No. 2017/565.

Regulatory reminder 7:

- **Article L. 533-10 of the CMF:** "[...] II.-Investment services providers other than portfolio asset management companies shall: [...] 3) Maintain and apply effective organisational and administrative arrangements to take all reasonable measures to prevent conflicts of interest from adversely affecting the interests of their clients. To this end, they shall take all appropriate measures to identify and avoid, or manage conflicts of interest. These conflicts of interest are those which arise between, on the one hand, the providers themselves, persons under their authority or acting on their behalf, or any other person directly or indirectly linked to them by a control relationship, and, on the other, their clients, or between two clients, in the course of providing any investment or related service or combination of these services, including those arising from the receipt of benefits from third parties or from the remuneration structure and other incentive structures of providers. [...]"
- **Article 33 of Delegated Regulation (EU) No. 2017/565:** "For the purposes of identifying the types of conflict of interest that arise in the course of providing investment and ancillary services or a combination thereof and whose existence may damage the interests of a client, investment firms shall take into account, by way of minimum criteria, whether the investment firm or a relevant person, or a person directly or indirectly linked by control to the firm, is in any of the following situations, whether as a result of providing investment or ancillary services or investment activities or otherwise:
 - a) the firm or that person is likely to make a financial gain, or avoid a financial loss, at the expense of the client;
 - b) the firm or that person has an interest in the outcome of a service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client's interest in that outcome;
 - c) the firm or that person has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client;
 - d) the firm or that person carries on the same business as the client;
 - e) the firm or that person receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monetary or non-monetary benefits or services."

3.3.2. Compliance system

Issues and focus

While it is true that temporary ownership dismemberment is marginal in the marketing systems of the institutions on the panel, the adoption of a risk-based approach does not exempt them from their professional obligations: the marketing of SCPI units with temporary ownership dismemberment requires the traditional marketing process to be adapted. Compliance verification functions must therefore ensure that the specific features of temporary ownership dismemberment are properly managed by specific provisions, and that these provisions are correctly applied.

Should their mapping of compliance risks and their audit plans for the inspected period fail to cover the theme, the institutions on the panel might be in breach of the provisions of Articles L. 533-10 II. 1) of the CMF, 22 (2) of Delegated Regulation (EU) No. 2017/565, and 312-1 of the AMF GR.

Regulatory reminder 8:

- **Article 22 of Delegated Regulation (EU) No. 2017/565:** *"2. Investment firms shall establish and maintain a permanent and effective compliance function [...]"*.
- **Article 312-1 of the AMF GR:** *"To ensure compliance with all of the professional obligations referred to in II of Article L. 621-15 of the Monetary and Financial Code, the investment services provider shall implement the compliance policy and the procedures relative to the responsibilities of the management body laid down in Articles 22 and 25 of Commission Delegated Regulation 2017/565 of 25 April 2016"*.