Legal update

The marketing of investments and financial services in and from the UK: The new regime

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INTRODUCTION

The financial services industry in the UK is regulated by the Financial Services Authority (FSA) under the Financial Services and Markets Act 2000 (FSMA 2000). The industry breaks down, broadly, as follows: banks, building societies, credit unions, friendly societies, investment businesses and insurers. Investment businesses include: asset managers, broker dealers, corporate financiers, independent financial advisers, life offices and their marketing networks. Persons carrying on financial services business in the UK will generally need to be authorised by the FSA to carry on the relevant regulated activity or activities. In December 2001 the Economic Secretary to the Treasury, Ruth Kelly, announced that mortgage lending businesses, including advising on and arranging mortgages, were scheduled to be brought into the regulatory net for the first time in the second quarter of 2004. Alongside this, the FSA will be given power to regulate the sale of general insurance products.

FSMA 2000 also addresses the marketing of investments (including deposits) and financial services (‘financial promotion’) by persons who are not authorised by the FSA. This regime is an overlay on the regulation of marketing, whatever the nature of the service, by, for example, the codes issued by the Advertising Standards Authority; the Independent Television Commission and the Radio Authority; and the Telecommunications (Data Protection and Primary) Regulations 1999. There is a need for an additional regime on the grounds that financial promotion can lead consumers into making significant, long-term and possibly risky investments.

FSMA 2000 sought to update and modernise the predecessor legislation applying to financial promotions in the UK consolidating the three main predecessor legislative regimes governing the marketing of deposits, insurance and investments (the Insurance Companies Act 1987, the Financial Services Act 1986 [the 1986 Act] and the Banking Act 1987). In drafting the legislation the government was keen to ensure it reflected the growing use of the Internet and other
developing forms of technology in the financial services marketplace. In short, the government wanted to produce legislation which was media-neutral and would not, therefore, become dated by further advances in communications technology.

Persons who are not authorised by the FSA are subject to the restriction on financial promotion set out in Section 21 of FSMA 2000 (the Restriction). It is important to appreciate that a person may become involved in financial promotion without requiring to be authorised by the FSA to conduct regulated business in the UK. For example, companies seeking to raise capital do not require to be authorised by the FSA to do so; journalists may wish to write about specific financial products to enable their readers to make more informed decisions; persons who are exempt from the need for authorisation (eg appointed representatives of authorised persons); persons who have structured their financial business in reliance on an exclusion so as to avoid the requirement to be authorised; and persons who are based outside the UK and therefore do not require to be authorised by the FSA but nonetheless wish to promote investments or services in the UK marketplace (eg an overseas financial services provider or investment fund). Also, financial promotion may take place prior to the conduct of any regulated activity. For example, under FSMA 2000 offering to conduct a regulated activity is not itself a regulated activity (in contrast to the predecessor legislation).

Section 21(1) of FSMA 2000 contains the Restriction, the effect of which is that an unauthorised person must not, in the course of business, communicate or cause to be communicated an invitation or inducement to engage in investment activity unless either the content of the communication is approved by an authorised person or the communication benefits from an exemption made by the Treasury under FSMA 2000. The term ‘financial promotion’ is the shorthand used to describe the communication of an invitation or inducement to engage in investment activity.

It is a criminal offence to breach the Restriction, punishable by a maximum of two years’ imprisonment and an unlimited fine. In a commercial context, when customers enter into an agreement or exercise any rights as a result of a financial promotion made in breach of the Restriction, the agreement will be unenforceable against them. Customers will be entitled to recover any property transferred and to receive compensation for losses incurred but if they choose to recover property transferred or not to continue the contract, they must return any money received. The courts are given a residual jurisdiction to enforce agreements made in contravention of the Restriction if satisfied that this will be just and equitable in the circumstances.

Since authorised persons who communicate or approve financial promotions are not subject to the Restriction, the FSA regulates the communication and approval of financial promotions by authorised persons (see Chapter 3 of the Conduct of Business Sourcebook [COB 3] of the FSA Handbook of rules and guidance [the FSA Handbook]). The FSA, however, is not allowed to make rules regulating financial promotions by authorised persons which could have been made lawfully by an unauthorised person relying on the exemptions. This ensures a level playing field for the authorised and unauthorised community. COB 3 exempts such financial promotions from the requirements that would otherwise apply.

The exemptions from the Restriction are made by the Treasury in secondary legislation issued under the authority of FSMA 2000. The Treasury to date, 1st June, 2002, has made the following