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By email: cp22-27@fca.org.uk

7 February 2023

Dear Sir or Madam

Introducing a gateway for firms who approve financial promotions: CP22/27

The City of London Law Society ("**CLLS**") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

This letter has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). The Committee not only responds to consultations but also proactively raises concerns where it becomes aware of issues which it considers to be of importance in a regulatory context.

The Committee has considered CP22/27 – Introducing a gateway for firms who approve financial promotions (the "**CP**") and wishes to comment including upon areas where there is the risk of legal uncertainty.

Introductory comments

We note that the FCA asks for input on a number of detailed areas relating to the approach to implementing the financial promotions gateway and ongoing reporting set out in the CP. However, there is no request for feedback on the overall architecture of the gateway itself or the way in which the FCA indicates that it is going to supervise and enforce the gateway, beyond what was described in the original HM Treasury consultation of July 2020 and consultation response of June 2021. We appreciate that much of this is for HM Treasury to consider as part of the Financial Services & Markets Bill which will create the gateway. However, we have identified a number of areas of uncertainty and potential confusion that we consider can be adequately addressed by the FCA, for example in additional PERG guidance or guidance embedded into the relevant Handbook sections.

The regulatory burden may restrict the choice of retail investments

The Committee notes that the FCA acknowledges that its proposals, along with the new rules in PS22/10, are likely to make the approval of financial promotions more costly and resource intensive to undertake and that there is a risk that firms will choose not to provide a financial promotions approval service as a result. We note that the FCA's anticipated total ongoing cost of between £30k and £503k indicates that more work may need to be undertaken to fully understand the anticipated consequences of all relevant rule changes.

Our concern, reflecting that of the FCA, is that the regulatory burdens on gateway firms, and the consequent expense of their services, may well restrict investment choice to retail customers unless there is a clear understanding of the reach and purpose of the gateway. It will be important for the FCA to closely monitor whether the new regulation gives rise to any such effects.

Uncertainties in need for (and use of) gateway given wider regulatory change

A further key concern of the Committee is the lack of visibility that firms and market participants have of the full range of upcoming changes relating to financial promotions. Many of these changes are yet to be implemented fully, or indeed have not yet been announced. We further note the desire of HM Treasury as expressed, inter alia, in its recent consultation on PRIIPs and UK Retail Disclosure, to improve retail investor choice including of overseas investment products. Firms are still in the process of fully implementing the changes to rules on the promotion of what the FCA perceives to be high-risk investments (from PS 22/10) as well as the Duty of Care. The CP itself also notes that HM Treasury is expected shortly to consult on restricting the application of the Financial Promotion Order exemptions for high-net-worth individuals and self-certified sophisticated investors. The CP acknowledges in paragraph 2.18 and 2.19 that, depending on how these exclusions are tightened there "may be an increase in demand for s21 approvals".

The range of changes to the financial promotions regime and related obligations on firms engaging in distribution activities may result in significant confusion and uncertainty across the market. We would therefore request that the FCA uses its powers to provide temporary permission to all firms until these other matters are more fully developed, and the FCA can obtain a better understanding of the broader implications. If the FCA has identified significant specific concerns relating to the approval of financial promotions that are not addressed by measures (such as PS22/10 or the Duty of Care), then these areas could be left outside that temporary permissions regime. We note here the FCA's particular target areas of investment-based crowd-funding, minibonds, cryptoassets and buy-now-pay-later agreements referred to in paragraph 35 of the Cost Benefit Analysis that accompanied the CP. A more proportionate approach may be to apply the gateway in the first instance only to promotions of these types of products, with all other products benefitting from a longer-term transition period.

Uncertainties relating to HM Treasury power to create exemptions

A further area of uncertainty for firms is in understanding what exemptions HM Treasury may provide for. We note that the new s.55NB of FSMA (as provided for in the Financial Services & Markets Bill) gives a power to create exemptions from the need for a firm to have gateway permission to approve financial promotions. We also note that HM Treasury (in its original consultation of July 2020 and consultation response of June 2021) stated that it intended to exempt firms approving promotions for its group members; for firms approving their own promotions for communication by unauthorised persons; and for firms approving communications for their appointed representatives. These exemptions are, of course, referred to in paragraph 3.10 of the CP. However, the text of the exemptions (and therefore their exact scope) remains unpublished.

Until these exemptions are provided for in legislation, it is difficult for firms to assess exactly what this may mean for their business models. Crucially, we anticipate that there will be many firms that

are currently approving financial promotions who are uncertain as to whether they will be required to apply for permission under the gateway or whether their activities will benefit from an exemption once published. The Committee is concerned that many firms may miss the opportunity to submit applications and join the transition period because the exemptions become set (and interpreted) more narrowly than they had anticipated. This is, of course, similar to the concern that is highlighted in the CP that firms currently relying on FPO exemptions for high net worth and sophisticated investors may find themselves in such a position once HM Treasury publishes legislation to amend the FPO.

We note here two particular examples, but there will be many others across the different sub-sectors of regulated firms that will become subject to the gateway.

First, where a fund manager wishes to approve promotions relating to a fund that it manages. The fund will not be a group member but will it relate to the promotion of its own business or that of the fund? We note in this regard that the changes in PS 22/10 will already have imposed considerable new constraints on a fund manager wishing to promote its unauthorised products to a non-institutional audience.

Second, we note the increase in retail investment platforms seeking to allow retail investors to participate in the capital markets. Indeed, we note that involving retail investors in all capital raisings was a recommendation of the July 2022 UK Secondary Capital Raising Review. In that report, it was noted that communications often need to be approved for distribution to a retail audience to allow this wider participation. This is also in line with the experience of members of the Committee who are advising on these types of issues. Firms approving communications in these scenarios will often be either the retail investment platform facilitating the involvement of retail investors into the capital raising, or the corporate finance bank acting for the issuer. Again, it is not immediately clear whether either firm in this situation would be considered to be approving its own communications or not.

We would welcome guidance from the FCA on its expectations for the exemptions from the gateway, for example in the form of additional commentary in PERG 8 to allow firms to assess whether they will be required to apply for permission under the gateway for the types of communications that they are currently approving.

<u>Response to specific questions in the CP</u>

Question 1 – Do you agree with our proposed approach to assessing applications?

We note and agree with the FCA's proposal to allow firms to continue approving promotions during that transitional period provided that they have submitted an application to join the gateway. However, we have two practical concerns with the stated approach.

First, as is noted above, given the continued uncertainty for firms on their likely need to join the gateway, there may be firms that either do not apply or who apply only because they wish to wait and see whether they will in fact need the VOP. We have highlighted two areas above where firms are waiting to understand the exact scope of the proposed exemptions from the regime and firms are also anticipating, as yet undetermined, changes to the application of articles 48 and 50A of the FPO (or any other articles that are amended once that review is published). If firms are required to pay a fee and prepare detailed processes and procedures in circumstances where they are unclear as to whether they will actually need to progress with the application, this will result in disproportionate cost and require firms to spend time and resources on activities that do not enhance their overall compliance framework or business.

Secondly, we note that a firm which has applied for a VOP will leave the transition period once it is determined. This raises a concern with the proposed approach of the FCA to the content of applications and their assessment. Many members of the Committee have noticed change in the

approach of the Authorisations Team and an increase in challenges to applications in all areas by FCA case-officers, and of applicants being requested to withdraw applications where the submissions were not considered complete or capable of being passed. This is something which has been increasingly noticed and in situations where case-officers would previously have provided written feedback to the applicants and allowed an opportunity to amend and resubmit the deficient parts of their application.

Whilst we understand and appreciate that the FCA wishes to improve standards and is actively seeking to challenge applicants, in circumstances such as this, where a refusal or forced withdrawal could have a significant impact on the firm's existing business, it would appear to be a disproportionate approach. Since both firms and the FCA will be working with new requirements we consider that the risks of such outcomes are even higher than in applications which may be more familiar. Given the uncertainties that firms face in applying for a VOP to join the gateway and the unfamiliar nature of these requirements, we would ask that the FCA considers either requesting that the transition period for firms ends only after they have had an opportunity to resubmit applications and address deficiencies, or otherwise apply different standards and means of assessing the applications to its current approach in other areas.

One specific comment that the Committee has relates to the information that applicant firms are expected to address in their procedures. In the second bullet in paragraph 4.5, the FCA states that it will expect firms to demonstrate "*how [they] will consider the commercial viability of the proposition described in the promotion*". We do not consider that commercial viability is or should be an appropriate matter for a firm approving a financial promotion, beyond assessing whether any information on commercial matters is clear, fair and not misleading. Furthermore, the Committee wondered if an explicit requirement to consider commercial viability could produce the side-effect that the approving firm would be seen by recipients of the communication as itself endorsing the quality of the product concerned (not merely vetting the quality of the promotion). For example an approval from a firm could be perceived by the recipient as expressing a view that the proposition is viable, which might be viewed as tantamount to an investment research type recommendation (thereby imposing additional conduct of business obligations on the approving firm), or as constituting a personal recommendation.

More generally, we note that the factors to be addressed in an application as outlined in paragraph 4.5 of the CP are not replicated in the proposed Rulebook changes. If the FCA expects applicant firms to meet these standards in their applications, it should be signposted in the Handbook.

Question 7 – Do you intend to apply for permission to approve financial promotions?

The Committee cannot comment on whether individual firms are planning to make an application. However, we repeat our concerns that, given the lack of clarity on: (i) the likely exemptions from the gateway itself; and (ii) the likely changes to FPO exclusions (particularly 48 and 50A), the anticipated number of applications may under-represent those firms that may need the new permission. Unless there is clarity before the application window opens, we are concerned that many firms who need to be within the gateway will not apply because they do not yet realise that their business is in scope.

Conclusion

If you would find it helpful to discuss any of these comments then we would be happy to do so. Please contact Karen Anderson by telephone on +44 (0) 20 7466 2404 or by email at Karen.Anderson@hsf.com in the first instance.

Yours faithfully

Karen Anderson
Chair, CLLS Regulatory Law Committee

THE CITY OF LONDON LAW SOCIETY
REGULATORY LAW COMMITTEE

Individuals and firms represented on this Committee are as follows:

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