

Informal capital raising and high net worth and sophisticated investors

Changes to the Financial Promotion Order

Government response

November 2004



HM TREASURY



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EXECUTIVE SUMMARY

Following a public consultation, the Government is making changes to simplify the regulatory regime for financial promotions, which will remove barriers that have previously inhibited business angel investment into small and growing firms. The changes will, in particular, make it easier for small, innovative and potentially high-growth firms to attract the funding they need to invest and succeed, and in turn contribute to the UK's economic prosperity.

Respondents to the 'Informal Capital Raising' consultation made it clear that existing regulations were standing in the way of small firms being able to promote investment opportunities to individual investors, often known as business angels. Firms wishing to raise finance from investors have to get their promotional material approved by a person authorised by the Financial Services Authority. This approval is not necessary if the firm promotes to people it knows are certified as high net worth individuals or sophisticated investors. Consultation respondents suggested that the previous certification regime was failing. Would-be investors found it time consuming, costly and inconvenient. In particular, they reported very low levels of certificated sophisticated investors, reportedly due to a fear on the part of some authorised people of being sued for incorrectly certifying individuals as 'sophisticated'.

To overcome these problems, the Government has decided to make two main changes to the current regulatory regime:

- # Firstly, to allow investors to self-certify themselves as high net worth individuals or sophisticated investors, without having to go through an authorised intermediary; and
- # Secondly, to allow firms to promote to individuals that they 'reasonably believe' are self-certified as high net worth or sophisticated

These changes will benefit investors by making it much easier to certify themselves and therefore receive solicitation for investment opportunities. For small firms it means that they will be able to promote to a greater number of potential investors, confident of acting within the law.

Some respondents to the consultation were concerned that these changes could lead people to self-certify themselves inappropriately. By receiving unapproved promotions investors give up certain protections and channels of redress. The Government recognises these concerns and fully accepts the need to maintain adequate protection for investors. To strengthen protection, all unapproved financial promotions made to high net worth individuals and self-certified sophisticated investors will now have to be accompanied by a prominent 'health warning'. The self-certification statements include clear warnings, tested successfully with consumers.

Responses to the consultation also indicated that small firms as well as business angels were uncertain of the requirements of the financial promotions regime. Fears of making unlawful financial promotions may hamper legitimate angel and small business activity. This paper seeks to clarify the regulatory position and to dispel some of the concerns that have been expressed (Chapter 3).

The Government believes the changes to the financial promotions regime will mean that many companies facing difficulties in obtaining funding will find it easier to approach and attract investors. This is an important part of the Government's commitment to building a more enterprising culture, creating the best possible environment in which to start and grow a business, and tackling barriers to successful SME formation and growth.

1

INTRODUCTION

1.1 As part of the two-year review of the Financial Services and Markets Act 2000 (FSMA), the Government consulted on reducing the regulatory burden associated with becoming a certified high net worth individual or sophisticated investor in January this year. The 'Informal Capital Raising' consultation document¹ proposed changes to the Financial Promotion Order² (FPO) and to the Promotion of Collective Investment Schemes Exemption Order³ ('the CIS Order') to make it easier for unlisted firms to raise finance from high net worth individuals and sophisticated investors whilst retaining appropriate consumer protections.

1.2 The Government received 62 responses to the consultation. Detail on the changes to the FPO and the CIS Order is set out in Chapter 2. The draft statutory instrument is at Chapter 4. This is the near final text of the statutory instrument to be made and laid before Parliament shortly. Further technical amendments may be made to this text (following proof-reading and printing) but substantive amendments are not anticipated. Once the statutory instrument has been made the final version of it will be available on HMSO's website (<http://www.legislation.hmsso.gov.uk/stat.htm>).

¹ 'Informal capital raising and high net worth and sophisticated investors: A consultation document on proposed changes to the Financial Promotion Order' HM Treasury, January 2004

² The Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 – S.I. 2001/1335

³ The Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemption) Order 2001 – S.I. 2001/1060

2

CHANGES TO THE CURRENT LEGISLATION

I) Allow promotions on the basis of a reasonable belief that the investor is a self-certified high net worth individual or a self-certified sophisticated investor

2.1 The Government believes that this change will make it easier for unlisted firms to promote to high net worth individuals or sophisticated investors. The practical effect of the current exemptions for certified high net worth individuals and certified sophisticated investors set out in the FPO and the CIS Order is that often an unlisted firm must see a certificate confirming that either an individual is a high net worth individual or that he or she is a sophisticated investor before it can make promotions to one of those individuals. The change to these two Orders will allow promotions to individuals where the person making the communication has a reasonable belief that:

- ⊘ the investor is a self-certified sophisticated investor; or
- ⊘ the investor is a self-certified high net worth individual

2.2 It should be noted that the current certified sophisticated investor exemption, which applies to a wider set of investments than those in unlisted firms, is not being changed to a reasonable belief test .

2.3 Reasonable belief pertains merely to the existence of a signed statement. Although it would ultimately be a matter for the courts as to what reasonable belief means in this context, the Government's intention is that it would be sufficient for an individual to demonstrate that they have taken sufficient steps to form a reasonable belief that a signed statement exists. The Government believes that confirmation (including an oral confirmation) from a potential investor to an individual that he or she has a high net worth or self-certified sophisticated investor statement would probably qualify as forming reasonable belief for this purpose.

2.4 The Government believes that requiring only a reasonable belief of the existence of a signed statement will avoid imposing a burden of having to undertake any due diligence in order to form a reasonable belief that a potential investor qualifies as high net worth or sophisticated (i.e. is correctly certified). The Government considers that a reasonable belief of the existence of a signed statement is necessary to protect those who fit the criteria but do not wish to receive unapproved promotions.

2.5 As outlined in the consultation document this change is not a dramatic departure from current practice as marketing on this basis is already permitted for associations of high net worth and sophisticated investors.

II) Introduce self-certification for high net worth individuals

2.6 The Government will allow high net worth individuals to self-certify that they meet the high net worth criteria of earning at least £100,000 or having net assets of at least £250,000 (excluding their primary residence, rights under certain contracts of insurance and certain benefits in the form of pensions or otherwise). At present, high net worth individuals require an accountant or their employer to sign a statement confirming that they meet the relevant criteria. Self-certification would reduce the costs of enabling high net worth individuals to receive promotions in terms of professional fees, time and inconvenience. The Government considers that this change does not detrimentally reduce consumer protection as the objective tests for high net worth remain the same.

2.7 The Government considers that the introduction of self-certification will mean that there will be no further need for the current high net worth exemption requiring certification by an accountant or employer. Responses to the consultation document highlighted how uptake of the exemption has been low due to the time and costs involved.

III) Introduce self-certification for sophisticated investors

2.8 The Government will allow individuals to self-certify themselves as sophisticated investors. Individuals will be able to self-certify as sophisticated if they meet one or more of the following criteria:

1. member of a network or syndicate of business angels for at least six months;
2. made more than one investment in unlisted companies in the previous two years;
3. working, or have worked in the previous two years in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
4. is currently, or has been in the previous two years, a director of a company with an annual turnover of at least £1 million.

2.9 This change should result in more business angels making use of these exemptions by becoming self-certified sophisticated investors. Responses to the consultation document confirmed that take-up of the current certified sophisticated investor exemption is extremely low. Responses suggested that authorised persons are reluctant to certify investors as sophisticated because of fears of potential liability claims, coupled with uncertainty surrounding what constitutes 'sufficiently knowledgeable'.

2.10 The criteria for sophistication differ from those set out in the original consultation document (as 'Model 2'), following consultation responses and further work with stakeholders. The revised criteria above are more closely tailored to business angel investors. They should therefore prevent inappropriate self-certification while allowing many more business angels to make use of these exemptions.

2.11 The Government consulted on the option of self-certification without detailed criteria to test against ('Model 3'). The Government believes that self-certification without criteria to test against would present a significant risk of individuals claiming they are sophisticated without necessarily understanding the risks of investing in unlisted equity. This would leave open an opportunity for abuse of the self-certification regime, for example if investors are persuaded to sign away their rights by unscrupulous advisors. This risk was highlighted by many respondents.

2.12 One further option raised in the consultation document was to rely solely on the new self-certified high net worth exemption on the assumption that the majority of sophisticated investors would also meet the criteria of high net worth. Consultation responses suggested that the sophisticated investor exemption is a useful and necessary supplement to the high net worth exemption. Feedback suggested that a significant minority of sophisticated investors (or those that would meet the description) would not meet the high net worth criteria. These investors typically bring relatively small sums of money, but significant experience and expertise to small firms. Therefore, removing the sophisticated investor exemption risks excluding exactly those individuals the Government wishes to encourage into the market.

2.13 The current certified (i.e. an authorised third party) sophisticated investor exemption will be maintained alongside the introduction of self-certification for investors who are sophisticated in terms of unlisted equity, e.g. small firm and start up investments. The existing exemption is used for a wider range of investments than unlisted equity, and the Government intends to maintain this option for investors in those instruments. This will also mean that individuals who are uncertain whether they are suitable still have the option of getting themselves signed off by authorised third parties if they wish.

2.14 Promotions to self-certified high net worth or sophisticated investors will be limited only to investments in unlisted equity, or in the case of collective investment schemes, unregulated schemes investing wholly or predominantly in unlisted companies. There will be provisions ensuring that investments made as a self-certified high net worth or sophisticated investor cannot lead to the investor losing more money than he or she invested.

Net assets test **2.15** The Government considers that the current high net worth net assets test of £250,000 is appropriate and should not be changed.

2.16 Some responses to the consultation raised the possibility of introducing a proportional test, which takes account of both an individual's net worth and the amount invested. For example, levels of investment could be set at a certain percentage of net worth. However, it would not be possible to introduce such a requirement under the structure of the current regime as both the FPO and the CIS Order regulate only the promotion of investments, not investments themselves. The Government believes that individuals should be at liberty to make their own investment decisions as regards their own money, with the protection of regulation where appropriate.

Consumer protection **2.17** The Government recognises that the introduction of self-certification is a significant relaxation of the current regime. The primary risk with the changes is that of incorrect self-certification, either through misunderstanding of the high net worth or sophisticated criteria and/or through abuse of the regime by unscrupulous intermediaries or small firms inciting unsuitable individuals to self-certify as sophisticated investors. By its very nature it is impossible for the Government or any other body to police self-certification. This raises consumer protection issues because in relying on unauthorised promotional material to make an investment, an individual may not have recourse to the usual channels of redress (for example, the Financial Ombudsman Scheme, the Financial Services Compensation Scheme or the Financial Services Authority).

2.18 Therefore, to minimise the risk of incorrect self-certification and maintain appropriate investor protection, a requirement for promotional material sent to certified high net worth individuals or self-certified sophisticated investors to carry 'health warnings' will be introduced. This was not something raised in the consultation, but was suggested by a number of respondents. The health warning will consist of a short statement warning that the investment opportunity described carries a significant risk of losing all property and other assets invested. The appearance of the warning will be prescribed so it will appear prominently at the beginning of all promotions. The self-certification statements that high net worth individuals and sophisticated investors will be required to sign also highlight the risks associated with unlisted equity and the loss of regulatory protection and redress under the Financial Services and Markets Act 2000.

2.19 In addition to the introduction of health warnings there are remedies outside the financial promotions regime that will continue to afford protection to investors. These include the common laws of fraud and negligence and section 397 of FSMA which protects investors from misleading statements.

2.20 The Government believes this package most effectively delivers a balance between consumer protection and facilitating investment in small and growing firms.

3

BUSINESS ANGELS, FINANCIAL PROMOTIONS AND AUTHORISATION GUIDANCE

Introduction

3.1 Several responses to the ‘Informal capital raising’ consultation document highlighted uncertainty over the scope of the financial promotions regime. Respondents were also unclear about which, if any, activities commonly undertaken by business angels required them to become FSA authorised. Part of the uncertainty is due to business angels not understanding (or in the most extreme cases, not being aware of) the relevant legislation.

3.2 The guidance given here is not comprehensive, it is merely meant to address a few key areas of particular relevance to small firms and business angels. The views expressed here are also not a substitute for reading the relevant sections of legislation or, where appropriate, seeking professional legal advice. This guidance has been prepared after discussion with the Financial Services Authority (FSA). Further, more detailed, guidance can be found in Chapter 2 of and Appendix 1 to the FSA Authorisation manual, which is available at <http://www.fsa.gov.uk/vhb/html/auth/authtoc.html>. The FSA is also able to provide individual guidance on request. Anyone wishing to seek such guidance should do so in accordance with the procedure set out in Chapter 9 of the FSA Supervision manual, which is available at <http://www.fsa.gov.uk/vhb/html/sup/suptoc.html>.

Box 1.1: Outline of guidance

Do the financial promotion rules apply to me?

CHECKLIST FOR BUSINESS ANGELS/SMALL FIRMS:

- # Am I acting ‘in the course of business’? (see paragraphs 3.7 – 3.10)
- # Am I making an invitation or inducement to engage in investment activity? (see paragraph 3.11)

If I am making an invitation or inducement to engage in investment activity, might I be exempt from the rules because:

- # I am making a promotion to an exempt person? (see paragraphs 3.13, 3.14)
- # I am making a one-off financial promotion? (see paragraph 3.12)

I reasonably believe my audience to be certified high net worth individuals or sophisticated investors? (see paragraphs 3.5 and 3.18 on reasonable belief)

When do I NOT need to be authorised?

CHECKLIST FOR BUSINESS ANGELS:

- # If my activities are not ‘by way of business’ (see paragraphs 3.24, 3.25)
- # If I am not carrying on regulated activities (see paragraphs 3.28 – 3.30)

If I am running an ‘enterprise scheme’ and thereby exempt from authorisation for ‘arranging’ activities only (see paragraph 3.26)

FOR BUSINESS ANGELS and SMALL FIRMS: When am I making a financial promotion?

3.3 The legislation restricts unauthorised persons from “communicating an invitation or inducement to engage in investment activity” (simply referred to as a ‘financial promotion’), in the course of business, unless:

- ☞ an authorised person approves the content of the communication; or
- ☞ it is exempt.¹

3.4 Appendix 1 to the FSA Authorisation manual has detailed guidance on the financial promotion restriction.

3.5 The changes to the legislation set out in this document concern the exemptions for promotions to high net worth individuals and sophisticated investors. The changes will, in most cases, allow unauthorised business angels to promote investment opportunities to other business angels who they reasonably believe to be certified without needing to have the promotion approved by an authorised person. Business angels will not have to satisfy themselves that the recipient actually meets the criteria for high net worth or sophistication, but merely have reasonable grounds to believe that they are certified persons. The exception to this is where the business angel makes an unsolicited real time promotion (for instance, a telephone call or personal visit) to a certified high net worth individual.² The exemption does not apply to such promotions.³ Furthermore, authorised persons are not permitted to approve the contents of real time promotions.

Does the financial promotion restriction apply to me?

3.6 There are several reasons why the financial promotions restriction may not apply to business angel or small firms’ activity:

You are not acting ‘in the course of business’

3.7 For the restriction to apply, the financial promotion must be made ‘in the course of business’.⁴ This requires a commercial interest on the part of the communicator. Genuine non-business communications, for example, friends talking together in a pub, are not captured.

3.8 Therefore, individual business angels interacting with one another, for example by discussing investment opportunities, are unlikely to be making financial promotions ‘in the course of business’ as there may be no business which they will be carrying on at that stage.

3.9 Similarly, individual business angels introducing others to a particular investment opportunity, a potential investee firm or other like-minded investors are also unlikely to be making financial promotions in the course of business.

¹ Section 21 FSMA and the Financial Promotion Order (FPO)

² Article 48(1) FPO

³ However, for the financial promotion restriction to apply the business angel must make the communication ‘in the course of business’. See generally paragraphs 3.7 – 3.10 below

⁴ FSMA section 21 and AUTH App 1.5

3.10 In determining whether a financial promotion is made in the course of business, account may need to be taken of the regularity of the activity. For example, individuals who are merely seeking to make personal investments will not be acting ‘in the course of business’ by approaching a company about making an investment in its shares. However, it is possible that an individual who regularly seeks to invest in companies who are seeking to raise venture capital with a view to becoming a director and influencing their affairs may be regarded as acting in the course of business.

You are not making an invitation or inducement to engage in investment activity

3.11 The FSA guidance indicates that a communication will only be a financial promotion if it is made with the purpose or intent of leading a person to engage in investment activity and is promotional in nature. Therefore, individual business angels communicating purely factual information, or merely inducing another person to make contact for further information, or providing contact details of, for example, a small firm seeking business angel investment, should not involve financial promotions.

You are making a one-off financial promotion

3.12 Business angels and firms should be able to make good use of the existing exemption for one-off promotions.⁵ The FSA guidance (at section 1.14.5) indicates that there are two essential elements to an exempt one-off promotion. These are that it is tailored to the circumstances of the recipient and that it is individual in nature (for instance, that it is not simply a personalised mailshot). For example, communicating details of a particular investment opportunity to members of your family or friends will generally be a one-off promotion. The full conditions that apply to this exemption are explained in the FSA guidance.

You are making a promotion to exempt persons

3.13 Generally, financial promotions made by or to exempt persons (persons who are exempt from the need to be authorised) are not subject to the restriction on financial promotions. This is because there are specific exemptions for such persons in the Financial Promotion Order.⁶ Companies who operate business angel networks on a not-for-profit basis are likely to be exempt persons⁷ (this is explained in greater detail below), and so promotions made to them (for instance, by business angels looking for investment opportunities) are allowed. Similarly, most promotions made by them for the purposes of their exempt business are allowed.

3.14 Even if the financial promotions rules still apply to you, you may be able to make an exempt financial promotion, and therefore not to have to get the contents of the promotion approved by an FSA-authorized person.

⁵ FPO article 28 and AUTH App 1.14

⁶ FPO articles 16 (exempt persons) and 19 (investment professionals)

⁷ Paragraph 40 of the schedule to the Exemption Order

When can I make an exempt financial promotion?

3.15 There are exemptions for promotions to high net worth individuals and sophisticated investors. These promotions do not have to be approved by an authorised person.

3.16 The Government's latest changes now allow, in most cases, unauthorised business angels or small firms to promote investment opportunities to people who they reasonably believe to have high net worth or sophisticated certificates. Business angels, firms or their advisors will not have to satisfy themselves that the recipient actually meets the criteria for high net worth or sophistication. They will have to have reasonable grounds to believe that they are certified persons.

3.17 The exemption does not apply to unsolicited real time promotions to certified high net worth individuals. This means that business angels are unable to make unannounced and unasked for telephone calls or personal visits to persons they know or believe to be certified high net worth. Real time promotions also cannot be approved by authorised persons⁸.

FOR SMALL FIRMS:

What do I need to do to communicate my investment opportunity to business angels?

3.18 The Government's changes to the legislation apply to promotions made by businesses themselves as well as business angels. So if you are a small firm making a financial promotion and you reasonably believe all recipients of the communication to be either certified high net worth individuals or certified sophisticated investors, then you do not have to have your promotional material approved. The restrictions under the financial promotions regime only apply to promotional material, so supplying merely factual information about your business does not require approval.

3.19 It should be noted that although unapproved promotions are permitted on the above basis for both individuals and businesses, this does not mean that false or misleading information within the promotion is permitted. Further, the unapproved promotional material must contain certain warnings to investors. These are set out in the legislation and the changes set out in this response document prescribe the wording and form that one of these warnings must take.

Do I need to ask potential investors whether they are certified before I send them financial information?

3.20 One situation that can be a cause of confusion is where a small business merely asks potential investors if they are certified high net worth individuals or sophisticated investors. FSA guidance is clear that enquiries about a person's high net worth or sophisticated status do not amount to a financial promotion. These enquiries can also be accompanied by a brief explanation of why it is being made – referring, for example, to information about the type of investment that any subsequent financial promotion would relate to – and still remain outside the regulation.

⁸ FSA handbook, COB 3.12.2R

FOR BUSINESS ANGELS:

Do I need to be authorised?

3.21 One of the key changes brought in to make this process easier for small firms is allowing promotions to be made to people that you reasonably believe are certified high net worth or sophisticated. Under the current regulations, small firms have felt obliged to see a certificate before making a promotion. The change to allowing promotions on the basis of reasonable belief is intended to make it easier for unlisted firms to seek, and receive, investment. The Government believes that requiring a reasonable belief of the existence of a signed statement, rather than of the individual being correctly certified, will avoid imposing a burden of due diligence on the small firm.

3.22 Certain activities, 'regulated activities', require persons carrying them on to be authorised by the FSA. Regulated activities include dealing, arranging, advising, managing, custody and operating a collective investment scheme.⁹ Chapter 2 of the FSA Authorisation manual outlines each of these in further detail.

3.23 Undoubtedly business angels, especially lead angels, are likely to get involved in regulated activities. They may, for example, give advice to other angels or arrange a syndicate of angels. However, this does not mean that they necessarily need to be authorised. In many cases, they may not satisfy the 'by way of business test'¹⁰ as the test requires that investment business activity must be engaged in as a business and therefore requires a degree of regularity.¹¹

Do I need to be authorised – are my activities 'by way of business'?

3.24 There is general guidance on the business test in the FSA Authorisation manual. See for example section 2.3 and Appendices 4.3 and 5.4. The FSA guidance indicates that, to satisfy the business test, an activity would, as a general rule, need to be undertaken with some degree of frequency or regularity and for commercial benefit of some kind. This is ultimately a judgment that takes into account several factors none of which is likely to be conclusive.

3.25 As a general rule, you will be deemed to be doing something 'by way of business' if you provide a service on a regular basis in return for reward of some kind. In general terms, you are unlikely to be acting 'by way of business' if your regulated activities are one-off or infrequent. You are also unlikely to be regarded as acting 'by way of business' if your activities do not represent the provision of a service to other angels in return for reward beyond that which you may expect to obtain as a result of your investment in the relevant business. A business angel will not be regarded as being rewarded for providing services to other angels simply because he receives recompense for his out-of-pocket expenses. Were an angel to receive some token reward for his efforts (such as a few additional share options) that also may be insufficient to cause him to make the activity 'by way of business', but inevitably this depends on the particular circumstances.

⁹ AUTH 2.7

¹⁰ FSMA section 22 and AUTH 2.3

¹¹ It should be noted that this is a narrower test than the 'in the course of business' test that applies to financial promotions as that is capable of applying to a single action

Do I need to be authorised – am I running an ‘enterprise scheme’?

3.26 Persons such as non-profit making organisations who run business angel networks may be able to use the specific exemption for enterprise schemes (paragraph 40 of the Schedule to the Exemption Order). Where this applies, the person becomes an exempt person in respect of any arranging activity only, for example, organising an event for companies to present to an audience of potential investors. Such networks will often be self-financing through fees charged to entrepreneurs and angels. If this is so the ‘by way of business’ test will be met and the networks will be unable to carry on other regulated activities apart from arranging - such as advising or dealing. As regards informal networks of business angels, it is likely that these may not need to be authorised because their activities are not ‘by way of business’ (see paragraphs 3.24 and 3.25).

3.27 Even where business angels are undertaking activities ‘by way of business’, some of their activities may not be regulated

Do I need to be authorised – am I undertaking regulated activities?

3.28 The following activities of business angels may not amount to a regulated activity:

I am merely passing details of investment opportunities to other business angels

3.29 This would generally not constitute ‘arranging deals’ as it would simply involve providing information.

I am exchanging views on the merits of particular investment propositions with other business angels – does this constitute advising on investments?

3.30 Business angels who provide information to other investors (for example, listings or company news) will not be giving advice unless the information is part of or is accompanied by comment on the merits of the subject company as an investment opportunity. However, the context in which information is provided may affect whether it amounts to advice. The FSA guidance gives a helpful example of information that involves the provision of advice. This is where a person gives information on share price movements against the background that, when he does so, that will be a good time to sell the shares.

3.31 But, in any event and as explained above, business angels would not need authorisation (or exemption) if they do not satisfy the business test.

 STATUTORY INSTRUMENTS

2004 No.

FINANCIAL SERVICES AND MARKETS

The Financial Services and Markets Act 2000 (Financial
Promotion and Promotion of Collective Investment Schemes)
(Miscellaneous Amendments) Order 2004

<i>Made</i> - - - -	2004
<i>Laid before Parliament</i>	2004
<i>Coming into force</i> - -	2004

The Treasury, in exercise of the powers conferred upon them by sections 21(5) and (6), 238(6) and (7) and 428(3) of the Financial Services and Markets Act 2000(a), hereby make the following Order:

Citation, commencement and interpretation

1.—(1) This Order may be cited as the Financial Services and Markets Act 2000 (Financial Promotion and Promotion of Collective Investment Schemes) (Miscellaneous Amendments) Order 2004 and comes into force on [enter date].

(2) In this Order—

“the Financial Promotion Order” means the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001(b); and

“the CIS Exemptions Order” means the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001(c).

Amendments to the Financial Promotion Order

2. The Financial Promotion Order is amended in accordance with Schedule 1 to this Order.

Amendments to the CIS Exemptions Order

3. The CIS Exemptions Order is amended in accordance with Schedule 2 to this Order.

(a) 2000 c.8.

(b) S.I. 2001/1335, amended by S.I. 2001/2633, S.I. 2001/3650, S.I. 2001/3800, S.I. 2002/1310, S.I. 2002/1777, S.I. 2002/2157 and S.I. 2003/1676.

(c) S.I. 2001/1060, amended by S.I. 2002/1310, S.I. 2002/2157, S.I. 2003/2067

Transitional provision: Financial Promotion Order

4.—(1) Paragraph (2) applies where, immediately before the coming into force of this Order, an individual is a certified high net worth individual within the meaning of article 48 of the Financial Promotion Order.

(2) That individual must, for so long as he holds a current certificate of high net worth, be treated as a certified high net worth individual for the purpose of article 48 of the Financial Promotion Order as substituted by this Order.

(3) For the purposes of this article, a certificate of high net worth—

- (a) means a certificate of high net worth which, immediately before the coming into force of this Order, satisfies the criteria in article 48(3)(a), (c) and (d) of the Financial Promotion Order; and
- (b) is current if it is signed and dated—
 - (i) within the period of twelve months ending with the day on which the communication (referred to in article 48 of the Financial Promotion Order) is made; and
 - (ii) prior to this Order coming into force.

Transitional provision: CIS Exemptions Order

5.—(1) Paragraph (2) applies where, immediately before the coming into force of this Order, an individual is a certified high net worth individual within the meaning of article 21 of CIS Exemptions Order.

(2) That individual must, for so long as he holds a current certificate of high net worth, be treated as a certified high net worth individual for the purpose of article 21 of the CIS Exemptions Order as substituted by this Order.

(3) For the purposes of this article, a certificate of high net worth—

- (a) means a certificate of high net worth which, immediately before the coming into force of this Order, satisfies the criteria in article 21(3)(a), (c) and (d) of the CIS Exemptions Order; and
- (b) is current if it is signed and dated—
 - (i) within the period of twelve months ending with the day on which the communication (referred to in article 21 of the CIS Exemptions Order) is made; and
 - (ii) prior to this Order coming into force.

Signatory text

Two of the Lords Commissioners of Her Majesty's Treasury

Address

Date

SCHEDULE 1

Article 2

Amendments to Financial Promotion Order

2. For article 48 of the Financial Promotion Order substitute—

“Certified high net worth individuals

48.—(1) If the requirements of paragraphs (4) and (7) are met, the financial promotion restriction does not apply to any communication which—

- (a) is a non-real time communication or a solicited real time communication;
- (b) is made only to an individual whom the person making the communication believes on reasonable grounds to be a certified high net worth individual; and
- (c) relates only to one or more investments falling within paragraph (8).

(2) “Certified high net worth individual” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement with the form and content set out in Part I of Schedule 5(a).

(3) The validity of a statement signed for the purposes of paragraph (2) is not affected by a defect in the form of the statement, provided that the defect does not affect the statement’s meaning.

(4) The requirement of this paragraph is that the communication contains a warning in accordance with paragraphs (5) and (6).

(5) The warning must be in the following terms—

“The content of this promotion has not been approved by an authorised person within the meaning of the Financial Services and Markets Act 2000. Reliance on this promotion for the purpose of engaging in any investment activity may expose an individual to a significant risk of losing all of the property or other assets invested.”.

(6) The warning must—

- (a) appear at the beginning of the communication;
- (b) precede any other written or pictorial matter;
- (c) be indelible;
- (d) be legible;
- (e) be in a font size consistent with the text forming the remainder of the communication;
- (f) be printed in black, bold type;
- (g) be surrounded by a black border, not less than 3 millimetres in width, which does not interfere with the text of the warning; and
- (h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

(a) As inserted by paragraph 4 of this Schedule.

(a) that it is exempt from the general restriction (in section 21 of the Act) on the communication of invitations or inducements to engage in investment activity on the grounds that it is made to a certified high net worth individual;

(b) of the requirements that must be met for an individual to qualify as a certified high net worth individual; and

(c) that any individual who is in any doubt about the investment to which the communication relates should consult an authorised person specialising in advising on investments of the kind in question.

(8) An investment falls within this paragraph if—

(a) it is an investment falling within paragraph 14 of Schedule 1 being stock or shares in an unlisted company;

(b) it is an investment falling within paragraph 15 of Schedule 1 being an investment acknowledging the indebtedness of an unlisted company;

(c) it is an investment falling within paragraph 17 or 18 of Schedule 1 conferring entitlement or rights with respect to investments falling within sub-paragraph (a) or (b);

(d) it comprises units in a collective investment scheme being a scheme which invests wholly or predominantly in investments falling within sub-paragraph (a) or (b);

(e) it is an investment falling within paragraph 21 of Schedule 1 to acquire or dispose of an investment falling within sub-paragraph (a), (b) or (c);

(f) it is an investment falling within paragraph 22 of Schedule 1 being rights under a contract for the sale of an investment falling within sub-paragraph (a), (b) or (c);

(g) it is an investment falling within paragraph 23 of Schedule 1 being a contract relating to, or to fluctuations in value or price of, an investment falling within sub-paragraph (a), (b) or (c),

provided in each case that it is an investment under the terms of which the investor cannot incur a liability or obligation to pay or contribute more than he commits by way of investment.”.

3. After paragraph (1) of article 50 of the Financial Promotion Order insert—

“(1A) The validity of a statement signed in accordance with paragraph (1)(b) is not affected by a defect in the wording of the statement, provided that the defect does not alter the statement’s meaning.”.

4. After that article, insert—

“Self-certified sophisticated investors

50A.—(1) “Self-certified sophisticated investor” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement with the form and content set out in Part II of Schedule 5.

(2) The validity of a statement signed for the purposes of paragraph (1) is not affected by a defect in the form of the statement, provided that the defect does not alter the statement’s meaning.

(3) If the requirements of paragraphs (4) and (7) are met, the financial promotion restriction does not apply to any communication which—

(a) is made only to an individual whom the person making the communication believes on reasonable grounds to be a self-certified sophisticated investor; and

(b) relates only to one or more investments falling within paragraph (8).

(4) The requirement of this paragraph is that the communication contains a warning in accordance with paragraphs (5) and (6).

(5) The warning must be in the following terms—

“The content of this promotion has not been approved by an authorised person within the meaning of the Financial Services and Markets Act 2000. Reliance on this promotion for the purpose of engaging in any investment activity may expose an individual to a significant risk of losing all of the property or other assets invested.”.

(6) The warning must—

- (a) appear at the beginning of the communication;
- (b) precede any other written or pictorial matter;
- (c) be indelible;
- (d) be legible;
- (e) be in a font size consistent with the text forming the remainder of the communication;
- (f) be printed in black, bold type;
- (g) be surrounded by a black border, not less than 3 millimetres in width, which does not interfere with the text of the warning; and
- (h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

- (a) that it is exempt from the general restriction (in section 21 of the Act) on the communication of invitations or inducements to engage in investment activity on the ground that it is made to a self-certified sophisticated investor;
- (b) of the requirements that must be met for an individual to qualify as a self-certified sophisticated investor;
- (c) that any individual who is in any doubt about the investment to which the communication relates should consult an authorised person specialising in advising on investments of the kind in question.

(8) An investment falls within this paragraph if—

- (a) it is an investment falling within paragraph 14 of Schedule 1 being stock or shares in an unlisted company;
- (b) it is an investment falling within paragraph 15 of Schedule 1 being an investment acknowledging the indebtedness of an unlisted company;
- (c) it is an investment falling within paragraph 17 or 18 of Schedule 1 conferring entitlement or rights with respect to investments falling within sub-paragraph (a) or (b);
- (d) it comprises units in a collective investment scheme being a scheme which invests wholly or predominantly in investments falling within sub-paragraph (a) or (b);
- (e) it is an investment falling within paragraph 21 of Schedule 1 to acquire or dispose of an investment falling within sub-paragraph (a), (b) or (c);
- (f) it is an investment falling within paragraph 22 of Schedule 1 being rights under a contract for the sale of an investment falling within sub-paragraph (a), (b) or (c);
- (g) it is an investment falling within paragraph 23 of Schedule 1 being a contract relating to, or to fluctuations in value or price of, an investment falling within sub-paragraph (a), (b) or (c),

provided in each case that it is an investment under the terms of which the investor cannot incur a liability or obligation to pay or contribute more than he commits by way of investment.”.

5. After Schedule 4 to the Financial Promotion Order insert—

“SCHEDULE 5

Articles 48 and 50A

STATEMENTS FOR CERTIFIED HIGH NET WORTH INDIVIDUALS AND SELF-CERTIFIED SOPHISTICATED INVESTORS

PART 1

STATEMENT FOR CERTIFIED HIGH NET WORTH INDIVIDUALS

1. The statement to be signed for the purposes of article 48(2) (definition of high net worth individual) must be in the following form and contain the following content—

“Statement for Certified High Net Worth Individual

I declare that I am a certified high net worth individual for the purposes of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

I understand that this means:

- (a) I can receive financial promotions that may not have been approved by a person authorised by the Financial Services Authority;
- (b) the content of such financial promotions may not conform to rules issued by the Financial Services Authority;
- (c) by signing this statement I may lose significant rights;**
- (d) I may have no right to complain to either of the following—
 - (i) the Financial Services Authority; or
 - (ii) the Financial Ombudsman Scheme;
- (e) I may have no right to seek compensation from the Financial Services Compensation Scheme.

I am a certified high net worth individual because **at least one of the following applies**—

- (a) I had, during the financial year immediately preceding the date below, an annual income to the value of £100,000 or more;
- (b) I held, throughout the financial year immediately preceding the date below, net assets to the value of £250,000 or more. Net assets for these purposes do not include —
 - (i) the property which is my primary residence (or any loan secured on that residence);
 - (ii) any rights of mine under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001(a); or
 - (iii) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are), or may be, entitled.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

(a) S.I. 2001/544, to which there are amendments not relevant to this Order.

I am aware that it is open to me to seek advice from someone who specialises in advising on investments

Signature

Date”.

PART II

STATEMENT FOR SELF-CERTIFIED SOPHISTICATED INVESTORS

2. The statement to be signed for the purposes of article 50A(1) (definition of self-certified sophisticated investor) must be in the following form and contain the following content—

“Statement for Self-certified Sophisticated Investor

I declare that I am a self-certified sophisticated investor for the purposes of the Financial Services and Markets Act (Financial Promotion) Order 2001.

I understand that this means:

- (a) I can receive financial promotions that may not have been approved by a person authorised by the Financial Services Authority;
- (b) the content of such financial promotions may not conform to rules issued by the Financial Services Authority;
- (c) by signing this statement I may lose significant rights;**
- (d) I may have no right to complain to either of the following—
 - (i) the Financial Services Authority; or
 - (ii) the Financial Ombudsman Scheme;
- (e) I may have no right to seek compensation from the Financial Services Compensation Scheme.

I am a self-certified sophisticated investor because **at least one of the following applies—**

- (a) I am a member of a network or syndicate of business angels and have been so for at least the last six months prior to the date below;
- (b) I have made more than one investment in an unlisted company in the two years prior to the date below;
- (c) I am working, or have worked in the two years prior to the date below, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
- (d) I am currently, or have been in the two years prior to the date below, a director of a company with an annual turnover of at least £1 million.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on investments.

Signature

Date”.”.

Amendments to the CIS Exemptions Order

1. For article 21 of the CIS Exemptions Order substitute—

“Certified high net worth individuals

21.—(1) If the requirements of paragraphs (4) and (7) are met, the scheme promotion restriction does not apply to any communication which—

- (a) is a non-real time communication or a solicited real time communication;
- (b) is made only to an individual whom the person making the communication believes on reasonable grounds to be a certified high net worth individual;
- (c) relates only to units falling within paragraph (8); and
- (d) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment.

(2) “Certified high net worth individual” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement with the form and content set out in Part I of the Schedule^(a).

(3) The validity of a statement signed for the purposes of paragraph (2) is not affected by a defect in the form of the statement, provided that the defect does not alter the statement’s meaning.

(4) The requirement of this paragraph is that the communication contains a warning in accordance with paragraphs (5) and (6).

(5) The warning must be in the following terms—

“Reliance on this promotion for the purpose of buying the units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested.”.

(6) The warning must—

- (a) appear at the beginning of the communication;
- (b) precede any other written or pictorial matter;
- (c) be indelible;
- (d) be legible;
- (e) be in a font size consistent with the text forming the remainder of the communication;
- (f) be printed in black, bold type;
- (g) be surrounded by a black border, not less than 3 millimetres in width, which does not interfere with the text of the warning; and
- (h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

- (a) that it is exempt from the restriction on the promotion of unregulated schemes (in section 238 of the Act) on the grounds that the communication is made to a certified high net worth individual;
- (b) of the requirements that must be met for an individual to qualify as a certified high net worth individual;

^(a) As inserted by paragraph 4 of this Schedule.

(c) that any individual who is in any doubt about the units to which the communication relates should consult an authorised person specialising in advising in participation in unregulated schemes.

(8) A unit falls within this paragraph if it is in an unregulated scheme which invests wholly or predominantly in the shares in or debentures of an unlisted company.

(9) “Unlisted company” has the meaning given in the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.”

2. After paragraph (1) of article 23 of the CIS Exemptions Order insert—

“(1A) The validity of a statement signed in accordance with paragraph (1)(b) is not affected by a defect in the wording of the statement, provided that the defect does not affect the statement’s meaning.”

3. After that article, insert—

“Self-certified sophisticated investors

23A.—(1) “Self-certified sophisticated investor” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement with the form and content set out in Part II of the Schedule.

(2) The validity of a statement signed for the purposes of paragraph (1) is not affected by a defect in the form of the statement, provided that the defect does not affect the statement’s meaning.

(3) If the requirements of paragraphs (4) and (7) are met, the scheme promotion restriction does not apply to any communication which—

(a) is made only to an individual whom the person making the communication believes on reasonable grounds to be a self-certified sophisticated investor;

(b) relates only to units falling within paragraph (8); and

(c) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment.

(4) The requirement of this paragraph is that the communication contains a warning in accordance with paragraphs (5) and (6).

(5) The warning must be in the following terms—

“Reliance on this promotion for the purpose of buying units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested.”.

(6) The warning must—

(a) appear at the beginning of the communication;

(b) precede any other written or pictorial matter;

(c) be indelible;

(d) be legible;

(e) be in a font size consistent with the text forming the remainder of the communication;

(f) be printed in black, bold type;

(g) be surrounded by a black border, not less than 3 millimetres in width, which does not interfere with the text of the warning; and

(h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

- (a) that it is exempt from the scheme promotion restriction (in section 238 of the Act) on the communication of invitations or inducements to participate in unregulated schemes on the ground that it is made to a self-certified sophisticated investor;
- (b) of the requirements that must be met for an individual to qualify as a self-certified sophisticated investor;
- (c) that any individual who is in any doubt about the investment to which the invitation or inducement relates should consult an authorised person specialising in advising on investments of the kind in question.
- (8) A unit falls within this paragraph if it is in an unregulated scheme which invests wholly or predominantly in the shares in or debentures of an unlisted company.
- (9) “Unlisted company” has the meaning given in the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.”.

4. After article 30 of the CIS Exemptions Order insert—

“SCHEDULE

Articles 21 and 23A

STATEMENTS FOR CERTIFIED HIGH NET WORTH INDIVIDUALS AND SELF-CERTIFIED SOPHISTICATED INVESTORS

PART I

STATEMENT FOR CERTIFIED HIGH NET WORTH INDIVIDUALS

1. The statement to be signed for the purposes of article 21(2) (definition of high net worth individual) must be in the following form and contain the following content—

“**Statement for Certified High Net Worth Individual**

I declare that I am a certified high net worth individual for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a certified high net worth individual because **at least one of the following applies**—

- (a) I had, during the financial year immediately preceding the date below, an annual income to the value of £100,000 or more;
- (b) I held, throughout the financial year immediately preceding the date below, net assets to the value of £250,000 or more. Net assets for these purposes do not include—
- (i) the property which is my primary residence or any loan secured on that residence;

- (ii) any rights of mine under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001(a); or
- (iii) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are), or may be, entitled.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date”.

PART II STATEMENT FOR SELF-CERTIFIED SOPHISTICATED INVESTORS

2. The statement to be signed for the purposes of article 23A(1) (definition of self-certified sophisticated investor) must be in the following form and contain the following content—

“Statement for Self-certified Sophisticated Investor

I declare that I am a self-certified sophisticated investor for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a self-certified sophisticated investor because **at least one of the following applies**—

- (a) I am a member of a network or syndicate of business angels and have been so for at least the last six months prior to the date below;
- (b) I have made more than one investment in an unlisted company in the two years prior to the date below;
- (c) I am working, or have worked in the two years prior to the date below, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
- (d) I am currently, or have been in the two years prior to the date below, a director of a company with an annual turnover of at least £1 million.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date”.”.

(a) S.I. 2001/544, to which there are amendments not relevant to this Order.

EXPLANATORY NOTE

(This note is not part of the Order)

This Order amends the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (S.I. 2001/1335) (“the Financial Promotion Order”) and the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (S.I. 2001/1060) (“the CIS Exemptions Order”).

The Financial Promotion Order, inter alia, sets out, pursuant to the power in section 21(5) and (6) of the Financial Services and Markets Act 2000 (c.8) (“the Act”), a number of exemptions from the restriction on financial promotions in section 21 of the Act. The CIS Exemptions Order sets out, pursuant to the power in section 238(6) and (7) of the Act, a number of exemptions from the restriction on promotions in section 238(1) of the Act.

This Order amends the exemptions contained in both the Financial Promotion Order and the CIS Exemptions Order relating to certified high net worth individuals (article 48 of the Financial Promotion Order and article 21 of the CIS Exemptions Order) and certified sophisticated investors (article 50 of the Financial Promotion Order and article 23 of the CIS Exemptions Order).

Articles 2 and 4 of and Schedule 1 to this Order are made under sections 21(5) and (6) and 428(3) of the Act. Articles 3 and 5 of and Schedule 2 to this Order are made under sections 238(6) and (7) and 428(3) of the Act.

The amendments to the certified high net worth individuals exemptions (paragraph 1(2) of Schedule 1 amends the exemption in the Financial Promotion Order and paragraph 1(2) of Schedule 2 amends the exemption in the CIS Exemptions Order) take the form of revised exemptions being substituted for the previous exemptions so that—

- (a) it will not be necessary for a certified high net worth individual to have a current certificate of high net worth;
- (b) certified high net worth individuals have to sign a revised statement;
- (c) in so far as the meaning is not altered, a defect in the form of that statement shall not affect its validity; and
- (d) a new requirement to include a warning, with a set form and appearance, in any promotion made to a certified high net worth individual is introduced.

The amendment to the certified sophisticated investor exemptions (paragraph 1(3) of Schedule 1 amends the exemption in the Financial Promotion Order and paragraph 1(2) of Schedule 2 amends the exemption in the CIS Exemptions Order) takes the form of inserting an additional paragraph (1A) in to each of those exemptions so as to provide that in so far as the meaning is not altered, a defect in the wording of the statement to be signed by a certified sophisticated investor shall not affect its validity.

Finally this Order inserts into the Financial Promotion Order and the CIS Exemptions Order a new exemption for self-certified sophisticated investors. This exemption has the effect that financial promotions or promotions relating to unregulated collective investment schemes can be made to self-certified sophisticated investors providing they contain a warning and meet certain requirements. A self-certified sophisticated investor is an individual who has signed, within the period of twelve months ending with the day on which a promotion is made, a statement in the form and manner set out in the relevant Order.

A full regulatory impact assessment of the effect that this instrument will have on the costs of business is available from the Enterprise Team, HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ.

A

SELF-CERTIFICATE STATEMENTS

Statement for Self-certified Sophisticated Investor (Financial Promotions)

I declare that I am a self-certified sophisticated investor for the purposes of the Financial Services and Markets Act (Financial Promotion) Order 2001.

I understand that this means:

- (a) I can receive financial promotions that may not have been approved by a person authorised by the Financial Services Authority;
- (b) the content of such financial promotions may not conform to rules issued by the Financial Services Authority;
- (c) **by signing this statement I may lose significant rights;**
- (d) I may have no right to complain to either of the following—
 - (i) the Financial Services Authority; or
 - (ii) the Financial Ombudsman Scheme;
- (e) I may have no right to seek compensation from the Financial Services Compensation Scheme.

I am a self-certified sophisticated investor because **at least one of the following applies—**

- (a) I am a member of a network or syndicate of business angels and have been so for at least the last six months prior to the date below;
- (b) I have made more than one investment in an unlisted company in the two years prior to the date below;
- (c) I am working, or have worked in the two years prior to the date below, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
- (d) I am currently, or have been in the two years prior to the date below, a director of a company with an annual turnover of at least £1 million.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on investments.

Signature

Date

Statement for Certified High Net Worth Individual (Financial Promotions)

I declare that I am a certified high net worth individual for the purposes of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

I understand that this means:

- (a) I can receive financial promotions that may not have been approved by a person authorised by the Financial Services Authority;
- (b) the content of such financial promotions may not conform to rules issued by the Financial Services Authority;
- (c) **by signing this statement I may lose significant rights;**
- (d) I may have no right to complain to either of the following—
 - (i) the Financial Services Authority; or
 - (ii) the Financial Ombudsman Scheme;
- (e) I may have no right to seek compensation from the Financial Services Compensation Scheme.

I am a certified high net worth individual because **at least one of the following applies—**

- (a) I had, during the financial year immediately preceding the date below, an annual income to the value of £100,000 or more;
- (b) I held, throughout the financial year immediately preceding the date below, net assets to the value of £250,000 or more. Net assets for these purposes do not include—
 - (i) the property which is my primary residence or any loan secured on that residence;
 - (ii) any rights of mine under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or
 - (iii) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are), or may be, entitled.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on investments

Signature

Date

Statement for Self-certified Sophisticated Investor (Collective Investment Schemes)

I declare that I am a self-certified sophisticated investor for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a self-certified sophisticated investor because **at least one of the following applies—**

- (a) I am a member of a network or syndicate of business angels and have been so for at least the last six months prior to the date below;
- (b) I have made more than one investment in an unlisted company in the two years prior to the date below;
- (c) I am working, or have worked in the two years prior to the date below, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
- (d) I am currently, or have been in the two years prior to the date below, a director of a company with an annual turnover of at least £1 million.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date

Statement for Certified High Net Worth Individual (Collective Investment Schemes)

I declare that I am a certified high net worth individual for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a certified high net worth individual because **at least one of the following applies—**

- (a) I had, during the financial year immediately preceding the date below, an annual income to the value of £100,000 or more;
- (b) I held, throughout the financial year immediately preceding the date below, net assets to the value of £250,000 or more. Net assets for these purposes do not include—
 - (i) the property which is my primary residence or any loan secured on that residence;
 - (ii) any rights of mine under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or
 - (iii) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are), or may be, entitled.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date

B

REGULATORY IMPACT ASSESSMENT

PURPOSE

Objective

- 1 The objective of the changes is to:
 - ⌘ facilitate relatively small levels of capital raising by unlisted companies; and
 - ⌘ make it easier for investors to receive unapproved financial promotions relating to unlisted companies.
- 2 These objectives will be achieved by:
 - ⌘ making it easier for small firms or intermediaries to promote to high net worth individuals or sophisticated investors; and
 - ⌘ allowing investors to self-certify as high net worth individuals or sophisticated investors.
- 3 Those mainly affected by the changes will be:
 - ⌘ unlisted firms seeking to raise equity finance;
 - ⌘ private investors seeking to invest in unlisted firms;
 - ⌘ unauthorised intermediaries arranging investments in unlisted firms;
 - ⌘ individuals or firms authorised by the Financial Services Authority (FSA) able to certify an individual as a sophisticated investor; and
 - ⌘ accountants and employers able to certify an individual as high net worth.

Background

4 Access to finance is essential for growing businesses to invest, to implement new technologies and strategies and to contribute to a more productive economy. A small but important minority of innovative, growth-oriented businesses continue to face difficulties attracting funding. Government analysis has pointed to a shortfall of equity finance that is most acute for businesses seeking between £250,000 and £1 million, but which can also be severe for many seeking up to £2 million¹. This gap in equity finance is a barrier to productivity growth, as it can stifle the development of innovative start-up and early-stage businesses, and can constrain the supply of capital for some established businesses that are seeking to modernise or diversify their activities.

5 Private individuals are an important source of finance for many early-stage firms. Although quantification of the typical size of such investments is difficult because of its informal nature, one recent estimate suggested as much as £12.8 billion was invested in UK small businesses between 1999 and 2000 by friends and family of the business owners, or by individual investors previously unconnected with the entrepreneur, i.e. business angels.²

¹ HM Treasury and the Small Business Service, *Bridging the finance gap: a consultation on improving access to growth capital for small businesses*, April 2003

² Cowling, Murray and Harding, *The virtuous circle of informal investment activity: Evidence from the UK, 2003*

6 The Financial Services and Markets Act 2000 (FSMA) prohibits unauthorised persons (in general terms, those not authorised by the FSA to carry on regulated activities) from “promoting” financial products and services unless:

- ⊘ the content of the communication has been approved by an authorised person; or
- ⊘ the communication falls within one of the exemptions specified in the Financial Promotion Order (FPO).³

7 The general effect of this legislation is that firms wishing to raise informal equity capital have to get their financial promotion approved by an authorised person in order to send it to potential investors. The costs associated with approval are likely to be disproportionately high for firms seeking relatively modest sums of equity finance. To address this, the Financial Promotion Order (FPO), as it is currently, allows unlisted firms to raise equity capital without the substantial costs of getting their financial promotion approved if the promotion is made to potential investors whom the promoter knows are certified as high net worth individuals or sophisticated investors.

8 The current certified high net worth individual exemption requires investors to obtain a certificate signed by either their employer or their accountant, stating that they either earn at least £100,000, or have net assets worth at least £250,000 (excluding their primary residence, rights under certain contracts of insurance and certain benefits in the form of pensions or otherwise). The current sophisticated investor exemption requires an authorised person to certify that the investor is sufficiently knowledgeable to understand the risks associated with the relevant description of investment.

9 The present Promotion of Collective Investment Schemes Exemption Order⁴ also uses the high net worth individual and sophisticated investor provisions as an exemption against the prohibition on authorised persons promoting unregulated or unauthorised collective investment schemes.

Risk Assessment

10 The present FPO exemptions described above were designed to facilitate informal capital raising by unlisted small firms from investors who are likely to be well-informed, experienced and in a position to obtain appropriate investment advice. Although there are no records of the numbers of investors that have certified as a high net worth individual or sophisticated investor, responses to the consultation document and feedback from stakeholders have confirmed previous suggestions that under this current regime take-up has in fact been extremely low.

³ The Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 – S.I. 2001/1335

⁴ The Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemption) Order 2001 – S.I. 2001/1060

11 Responses to the consultation document identified a number of problems with the current certification regime:

- ⊘ time consuming;
- ⊘ complex – requirements are not understood by investors;
- ⊘ authorised persons are reluctant to certify individuals as sophisticated investors because of potential professional liability;
- ⊘ authorised persons are reluctant to certify because of the restriction on promoting to individuals, having certified them as sophisticated or high net worth; and
- ⊘ the financial promotions regime itself is not widely known about (both amongst informal investors and unlisted firms/promoters).

12 Respondents to the consultation document confirmed that the current high net worth individual and sophisticated investor exemptions stand in the way of smaller firms seeking to raise capital via unlisted equity for investors. This is in the context of the equity gap for companies seeking smaller amounts of finance; informal investors are crucial to addressing this gap, however, the current regulatory regime creates a barrier to investment.

Options

13 There are two options:

- ⊘ not to legislate, in which case the situation would remain as it is; or
- ⊘ legislative change.

14 Legislation will mean a number of changes to the existing regime:

1) Promotions will be allowed on the basis of a reasonable belief that an individual is a self-certified high net worth or a self-certified sophisticated investor. (The practical effect of the current exemptions in the FPO is that an unlisted firm must actually see a certificate before it can send promotional material to a potential investor).

2) A self-certification exemption for high net worth individuals will replace the current high net worth exemption. The current exemption requires an accountant or employer to sign a statement.

3) A self-certification exemption for sophisticated investors will operate alongside the current exemption. Self-certification as a sophisticated investor will be on the basis of an individual signing a statement to the effect that they meet one or more of the following criteria:

- ⊘ member of a network or syndicate of business angels for at least six months;
- ⊘ made more than one investment in unlisted companies in the previous two years;
- ⊘ working, or have worked in the previous two years, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;

are currently, or have been in the previous two years, a director of a company with an annual turnover of at least £1 million.

4) A requirement for promotional material to carry a statement, the wording and appearance of which will be prescribed, warning of the risks in investing in unlisted equity (see further below).

15 The changes to the FPO are set out in further detail in the response document. These changes are intended to facilitate investment in small firms, by making it easier for investors to become certificated and therefore receive unapproved financial promotions. However, it is important to note that introducing self-certification potentially lessens investor protection.

16 There are risks to consumer protection inherent in the existing regime by allowing investors to receive unapproved promotions. This is because an investor who has received an unapproved promotion may be unable to seek redress if things go wrong through some of the usual avenues, for example, the Financial Ombudsman Service or the FSA.

17 Allowing self-certification potentially carries an increased risk to consumer protection because of the possibility of individuals signing a statement incorrectly. To minimise the risk of incorrect self-certification and maintain appropriate investor protection, there is a requirement for promotional material sent to certified high net worth individuals or self-certified sophisticated investors to carry 'health warnings'. The health warning consists of a short statement warning that the investment opportunity described carries a significant risk of losing all property invested. The wording and appearance of the health warning is prescribed by legislation so it appears prominently at the beginning of financial promotions. Further, the self-certification statements that high net worth individuals and sophisticated investors will be required to sign also highlight the risk of losing property and other assets when relying on financial promotions and highlight the loss of regulatory protection and redress under FSMA.

18 Promotions to self-certified high net worth or sophisticated investors are to be limited only to investments in unlisted equity, or in the case of collective investment schemes certain types of scheme. There are provisions ensuring that investments made as a self-certified high net worth or sophisticated investor cannot lead to the investor losing more money than he or she invested.

19 Investors will continue to have recourse to protections that lie outside the financial promotions regime, such as civil claims based on fraud and negligence and the offence of misleading statements and practices contained in section 397 of FSMA.

Promotion of Collective Investment Schemes Exemption Order

20 Section 238 of FSMA precludes an authorised person from inviting or inducing someone to participate in a collective investment scheme unless that scheme is an authorised unit trust scheme, a scheme constituted by an open ended investment company authorised pursuant to regulations made under section 262 of FSMA or an overseas scheme recognised pursuant to section 264, 270 or 272 of FSMA. The Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 ('the CIS Order') provides exemptions from this prohibition, including the high net worth individual and sophisticated investor exemptions. For reasons of consistency between the FPO and CIS Order, the consultation document suggested that equivalent amendments be made to the exemptions.

Costs and benefits

21 The costs and benefits described below are of the changes to legislation compared with the option of not legislating.

22 The sectors affected will be:

- €# unlisted firms;
- €# private investors ('business angels');
- €# unauthorised intermediaries;
- €# firms or individuals who are FSA-authorised to certify an individual as a sophisticated investor; and
- €# accountants and employers able to certify an individual as high net worth.

Benefits 23 The immediate benefit is that high net worth and sophisticated investors will save the costs of certification by a third party. Further, the change allowing promotion on the basis of a reasonable belief that an individual is certified high net worth or sophisticated will mean that small firms are able to promote to a greater number of potential investors. The wider implications of this are:

- €# more investors are likely to sign a statement that they are high net worth or sophisticated;
- €# more investors are likely to receive promotions from unlisted companies; and
- €# ultimately more private capital will be available to unlisted companies currently affected by the equity gap.

Costs 24 The changes to the FPO and the CIS Order are deregulatory measures designed to decrease the costs of compliance with both Orders. They are intended to reduce the total costs associated with promoting and investing in unlisted equity for small firms. Investors will save the costs of third party certification by being able to self-certificate.

Equity and fairness

25 It is not expected that any particular group or business sector will be disproportionately affected by the legislative changes.

Small firms' impact test

26 The proposed changes in legislation to the FPO and the CIS Order are expressly designed to impact positively on small firms by facilitating greater investment in them.

26 The Small Business Service (SBS) has been consulted on the impact on small firms of the proposed changes and are happy that they will not adversely affect small firms, but rather see them being of benefit in the longer term.

Competition assessment

28 The impact on competition is believed to be relatively small; the changes to the FPO and the CIS Order will continue to apply to the same groups of individuals or firms under the current legislation.

29 It could be argued that the changes will have a positive impact on competition as they are designed to boost the start up and growth of new businesses, any other impact on competition will be on the position of those authorised firms or individuals that currently offer a service of certification as high net worth or sophisticated. The replacement of certification for high net worth individuals with self-certification will remove this market for authorised third parties. The introduction of self-certification for sophisticated investors is also likely to decrease the demand for certification services. As feedback from stakeholders and responses to the consultation document suggests that current levels of certification are very low and that authorised third parties are often reluctant to offer certification services, the impact of the changes is expected to be low.

Enforcement and sanctions

30 Responsibility for enforcement of the FPO will remain with the FSA. The FSA has a large range of sanctions at its disposal, including the criminal law and powers to levy fines.

Consultation

31 There were 62 responses from interested parties on the ‘Informal capital raising’⁵ consultation. The consultation period closed on 19 April 2004. The Government took due account of consultation responses in developing the legislation set out in this document. Overall, the response provided a sound basis to proceed with the changes.

32 The FSA and the SBS have also been consulted.

Monitoring and review

33 The proposals for changes to the FPO and the CIS Order are part of the two-year review of FSMA.

34 The Treasury updates FSMA secondary legislation when it is appropriate to do so.

Summary and recommendation

35 To ensure small businesses have access to the finance they need to invest and grow, it is important that the regulatory regime under which these firms can raise relatively small levels of capital strikes an appropriate balance between consumer protection for those investors who are likely to be well-informed, experienced and in a position to obtain appropriate advice, and access to finance for small and growing firms. The current exemptions from the restrictions on financial promotions are not working as intended.

36 To facilitate investment in small firms, the introduction of self-certification for high net worth individuals and sophisticated investors will make it easier for investors to self-certify and therefore receive unapproved financial promotions. The changes would also make it easier for small firms to promote to high net worth individuals and sophisticated investors by allowing promotions on the basis of a reasonable belief that an investor is certified as such.

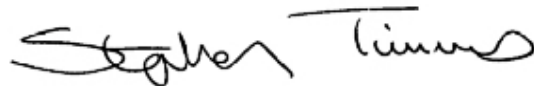
37 The changes will be implemented via secondary legislation under FSMA.

⁵ http://www.hm-treasury.gov.uk/media/195F1/changes_FPO_condoc_240103.pdf

MINISTERIAL DECLARATION

I have read the Regulatory Impact Assessment and I am satisfied that the benefits justify the costs.

Signed by the responsible Minister, Stephen Timms MP, Financial Secretary to the Treasury.



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