

## **Chapter 4 The impact of FSMA on employers offering pension products**

### ***Financial Promotion Order***

We agree with the proposal that an exemption be introduced to the Financial Promotions Order for employers promoting workplace pensions to employees, and that the exemption should cover both real time and non-real time financial promotions.

We do not however agree with all of the conditions to which it is proposed the exemption should be subject and comment as follows:

- We do not think that the exemption should apply only to group personal pension schemes and stakeholder pension schemes but should apply also to other regulated products which are offered by employers to employees; for example, in our own benefits scheme we are allowed to purchase various types of insurance.
- We do not understand the rationale for the condition that the exemption should only apply where the employer itself makes a financial contribution, and therefore do not agree with this condition. In particular, many employers do not contribute to the cost of employees purchasing insurance.
- We do not disagree with the condition that employers must inform employees of their right to seek independent advice although wonder in practice whether such a statement will actually cause more than a tiny number of employees to actually seek advice.
- We agree that, in order to protect employees from unscrupulous employers, the exemption should only apply to the promotion of schemes from which the employer receives no direct commercial benefit; however, there would need to be some detailed guidance about the meaning of “direct commercial benefit to an employers’ business”.

The proviso to the above comments is that product providers’ promotional material must continue to be subject to the financial promotion rules as this is how employees will receive their protection.

We agree that there should be no restriction on which employer’s representatives can promote the employer’s pension schemes.

### ***Regulated Activities Order***

We do not think that that it is necessary to introduce any further restrictions on employers in relation to the advice they can provide to employees on their pension options. As pointed out in the consultation document, the final stage of the transaction, to which the employee and the product provider are parties, is already highly regulated. The additional conditions which have been suggested in the consultation document would be unduly complex and would not add materially to investor protection.

## Chapter 6 Sale of a body corporate

### *Narrowing of the Article 70 exemption under the RAO*

We can see benefits and disadvantages of narrowing the “may reasonably be regarded” test. We can understand the case for increasing the protection for investors although we are unaware of instances of abuse of the current RAO. However, we also question whether the proposed narrowing is an unnecessary extension of regulation particularly with respect to individual small shareholders disposing of their shares when the whole of a body corporate is being sold.

Our overriding concern with the proposals is that they are over-complicated and therefore not easily understood by users - our comments are designed to point out where the proposal needs to be simplified and clarified, and are focused on how the proposed exemptions will affect users in practice and on the need for further guidance in certain areas.

Appendix I provides practical examples of typical transactions and considers whether services provided would fall within the current and the proposed exemptions both for RAO and FPO. The scenarios also consider whether the counterparty to the transaction would fall within the relevant exemption.

Such an analysis reinforces our view that the legislation in this area is overly complicated and demonstrates how, without simplification and clarification, we will, on occasion, need to obtain legal opinion on whether specific proposals fall within the requirements of the regime before we commence the provision of financial advisory services to our clients. This itself is an indicator that the proposals are unacceptable as they stand.

The analysis highlights that the main difference between the current and proposed exemptions is that we can no longer consider whether the object of the **transaction** is acquisition of day-to-day control but rather we need to consider whether the object of our **client** is to acquire or dispose of day-to-day control. This will increase the amount of regulated activities that we undertake, in particular, the number of financial promotions that we will be required to approve (as noted below in “*Narrowing of the Article 62 exemption under the FPO*”).

We can understand that narrowing the exemption in this way would achieve the objective of increasing the protection to individuals whose shareholdings are for investment rather than commercial purposes. However, in the case of small unlisted companies we are not convinced that the benefits of protection to shareholders outweigh the detrimental effect on liquidity and share price that the additional costs associated with the provision of regulated work entails. It should also be noted that the relevant consultation paper notes a lack of evidence of any consumer detriment in this area.

### ***Group of persons acting together***

It seems that, in order to lessen the effect of the narrowing of the Article 70 exemption in certain cases, a new concept has been introduced, namely that of “a group of persons acting together”. The example given concerns management of a company acting with institutional investors as part of a joint takeover bid.

However, our analysis in Appendix I highlights that it is not clear how this concept might apply to a group of shareholders that are considering a potential disposal of shares to a third party. When might a group of shareholders, who do not fall within the definition of a “group of connected individuals”, be considered as a “group of persons acting together”? The concept of “acting together” has not been defined and no guidance has been given to cover this exact situation. Again, this is of particular importance when considering the proposed changes to the Financial Promotion Order. How may a person communicate with persons initially to form a “group of persons acting together”? Would disparate shareholders who accept an offer made to them seeking to acquire 30% of the issued share capital of an unlisted company (where the sale of 30% would be the disposal of day to day control) be considered to be acting together? The answer probably is that it depends on the circumstances; however, in the absence of greater clarity or guidance it will be difficult in many cases to determine whether or not persons are acting together.

In some situations the transaction may only be considered by, and known by, a small group of individuals who would look to represent the remaining shareholders in the disposal and appoint advisers on that basis. At what point would it be appropriate to include the other shareholders within the "group of persons"?

Whilst the "Proposals for Change" document states that the "group of persons acting together" concept is intended to catch a different category of persons to "a group of connected individuals", we would welcome clarification on the relationship between the two concepts and HM Treasury's view in relation to the queries raised. For example, is it reasonable to assume that a “group of connected individuals” will always be a “group of persons acting together”?

### ***Definition of BD***

We understand from Chapter 6 of "Volume 1: Proposals for Change" that one of the aims of HM Treasury is to restrict the sale of body corporate exemption in order to narrow the "may reasonably be regarded test" to apply only in relation to takeovers of small companies and, broadly, to ensure that where transactions are subject to the Takeover Code or the Public Offer of Securities Regulations 1995 ("POS Regs"), this limb of the exemption does not apply. We do not believe that the "either/or" method of defining BD satisfies the apparent legislative intent of HM Treasury as set out at paragraph 6.6 of Chapter 6. For example, takeovers of unlisted Plc's are subject to the Takeover Code but such companies could fall within the definition of BD. Similarly there are a number of unlisted companies with more than 50 shareholders which would also fall within the definition of BD.

We are not sure that the definition of BD entirely follows the policy objectives set out in the “Proposals for Change” document.

### *Narrowing of the Article 62 exemption under the FPO*

The areas for comment and the revisions to Article 62 of the Financial Promotion Order reflect the above comments on Article 70 RAO. In particular, it is important to note that the approval of financial promotions is a costly exercise, because of the detailed work involved, and will be particularly burdensome for small value transactions.

As with the new Article 70, the proposed new Article 69 only exempts communications made to S or T (as the case may be). That means that financial promotions in a number of small company transactions would not fall within the exclusion, as financial promotions may be made to parties on the other side of the transaction from S or T. For example, if a management team and venture capitalist (together T for this purpose) wish to issue a financial promotion to two shareholders holding more than 50% of the company they wish to acquire, the promotion to the two shareholders may not be exempt even if there is no regulated activity under Article 70. This is a considerable narrowing of the existing Article 62.

Also, is it sufficiently clear that parties on both sides of a transaction could fall within the definition of S or T? In the previous example, the management team and VC constitute T if their object is to acquire day-to-day control; but the two shareholders could also constitute T if their object is to dispose of day-to-day control. It would seem in this case that the advisers to the management team/VC could issue a promotion to the two shareholders (themselves being T) and make arrangements for/advise them on the sale. This may be what is intended but it will create difficulties and uncertainties if there are, for example, a small number of other shareholders whom one would want to be able to include in the transaction. How could one be sure that the other shareholders would, with the two large shareholders, form a group of persons acting together and that their combined object is the disposal of day-to-day control? For parties involved in these types of transaction there would be greater uncertainty than under the current exemptions.

In Appendix 1 of AUTH 1.14.37G, the FSA state that, in their view, (in relation to the existing Article 62), financial promotions concerning the sale of a corporate business by a person who, either alone or with others, controls the business to another person who, either alone or with others, proposes to control the business, are exempt from the scope of section 21 FSMA. We believe that this concept should be continued in any revision to the RAO and FPO (subject, possibly, to transactions subject to the Takeover Code) but we are not confident that the proposed changes will have this effect.

## **Chapter 7 Investment by occupational pension scheme trustees**

We agree with the proposals that:

- The expression “routine day to day decisions” should be replaced with “day to day decisions”;
- The scope of products in which unauthorised trustees are permitted to invest should include pooled investment vehicles and contracts of insurance;
- The condition under which unauthorised trustees can invest in certain products should be relaxed so they only have to obtain and consider independent advice rather than act in accordance with it; and
- The condition under which unauthorised trustees can invest in certain products should be relaxed so that advice can also be given by professional firms operating under Part XX of FSMA.

## Chapter 9 Other secondary legislation

### *Trustees in bankruptcy*

We do not agree that the exemption currently given to trustees in bankruptcy should be removed for the following reasons:

- The current practice by the Court is to initially appoint the Official Receiver to be trustee and for a commercial trustee to be appointed either by a meeting of the creditors of the estate or by the Secretary of State. If the current exemption in the Exemption Order were removed, either the Official Receiver would also acquire obligations under FSMA or he would require a specific exemption similar to that currently granted to all Insolvency Practitioners by the Exemption Order. The latter case would lead to the result that the person initially appointed as trustee would have an exemption from FSMA and the person subsequently appointed (by creditors or the Secretary of State) would have no such exemption.
- The period of time that elapses between the bankruptcy order and the appointment of a trustee other than the Official Receiver can be one of weeks or months. It is unreasonable to make a commercial trustee subject to regulations and then make him responsible for dealing with issues that occurred "before his watch".
- If an insolvency practitioner is made subject to the regulatory burden that he is not likely to be expert in, it is unlikely that he will be prepared to accept appointments.
- The removal of the current exemption for trustees in bankruptcy would place a compliance burden on trustees out of proportion to the number of insolvent estates of IFAs and others. The insolvency profession is already adequately regulated and the removal of the current exemption would mean that prospective trustees would view the regulatory burden as too high for the economic benefit of the fee income generated from the estate concerned.
- It makes no sense to make a trustee in bankruptcy subject to the regulatory regime of FSMA when other Insolvency Practitioners remain exempt; if the administrator of a corporate IFA does not need to be made subject to the regulations, why should the trustee in bankruptcy of an individual IFA be?

### *NETA advice exemption*

We have the following comments:

*Q44:* We are not aware of investor detriment from unregulated advice in the electricity forward markets. The provision of balancing services to NGC relates to physical delivery and again, we are not aware of investor detriment from unregulated advice.

*Q45:* Yes, we agree that only those investors who have knowledge of the electricity markets i.e. professionals are likely to consider investing in the electricity forward markets. Investors in the electricity forward markets are typically utility companies, specialist financial traders and banks/other financial players.

*Q46:* From a point of view of competition, smaller BSC Parties that enter the market (e.g. renewable plant owners) might benefit from the Electricity Industry advice exemption. FSMA authorisation might be perceived as a barrier to entry by such players. The

Government's increased emphasis on renewable plant makes the arguments outlined in paragraph 9.32 more relevant today than in 2001.

*Q49:* We agree that the Electricity Industry advice exemption should be retained. The status quo appears to be working satisfactorily. There are, as noted, further changes that could impact upon the market. Until these changes and their potential impacts have been assessed, the rationale for changing the status quo is not clear.