

EXPLANATORY MEMORANDUM TO
THE FINANCIAL SERVICES AND MARKETS ACT 2000 (FINANCIAL
PROMOTION) (AMENDMENT) (NO. 2) ORDER 2023

2023 No. 1411

1. Introduction

- 1.1 This explanatory memorandum has been prepared by HM Treasury and is laid before Parliament by Command of His Majesty.
- 1.2 This memorandum contains information for the Joint Committee on Statutory Instruments.

2. Purpose of the instrument

- 2.1 The Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (FPO) provides exemptions from the restriction on communicating financial promotions. These include exemptions that enable financial promotions for unlisted companies to be made to high net worth individuals and self-certified sophisticated investors. Following a public consultation, the Government is legislating to make amendments to these exemptions.

3. Matters of special interest to Parliament

Matters of special interest to the Joint Committee on Statutory Instruments

- 3.1 The instrument corrects a defect in the Financial Services and Markets Act 2000 (Exemptions from Financial Promotion General Requirement) Regulations 2023¹ (“the Financial Promotion Gateway Exemptions Regulations”), ensuring that all of the exemptions to the financial promotions gateway have the intended scope. The instrument will be issued free of charge to all known recipients of the Financial Promotion Gateway Exemptions Regulations.

4. Extent and Territorial Application

- 4.1 The territorial extent of this instrument is England and Wales, Scotland and Northern Ireland.
- 4.2 The territorial application of this instrument is England and Wales, Scotland and Northern Ireland.

5. European Convention on Human Rights

- 5.1 The Economic Secretary to the Treasury (Andrew Griffith) has made the following statement regarding Human Rights:

“In my view the provisions of the Financial Services and Markets Act 2000 (Financial Promotion) (Amendment) (No. 2) Order 2023 are compatible with the European Convention on Human Rights.”

¹ S.I. 2023/966.

6. Legislative Context

- 6.1 Section 21 of the Financial Services and Markets Act 2000 (FSMA 2000) provides that a person must not, in the course of business, communicate an invitation or inducement to engage in investment activity, or claims management activity, unless (i) they are an authorised person, (ii) the content of the communication is approved by an authorised person. The Treasury may, by Order, specify circumstances which are exempt from this prohibition. These circumstances are set out in the FPO.²
- 6.2 The FPO provides exemptions for promotions to certified high net worth individuals (Article 48) and self-certified sophisticated investors (Article 50A), referred to in this memorandum as ‘the exemptions’. The exemptions can only be used to market investments related to unlisted companies.
- 6.3 The exemptions were last substantively updated in 2005. Since then, there have been significant economic, social and technological changes to the context in which the exemptions operate. In addition, the government is aware of concerns about misuse of the exemptions, including some businesses seeking to use the exemptions to market products inappropriately to ordinary retail investors. This issue was recognised in the Treasury Select Committee’s report on the failure of London Capital and Finance, and led to a recommendation for the government to “re-evaluate the Financial Promotion Order exemptions to determine their appropriateness and consider what changes need to be made to protect consumers”.³
- 6.4 This instrument amends the exemptions following the government’s review of the exemptions, and applies these changes in relation to the promotion of collective investment schemes, through amending relevant exemptions set out in the Promotion of Collective Investment Schemes (Exemptions) Order 2001 (PCIS).
- 6.5 This instrument also corrects a defect in the Financial Promotion Gateway Exemptions Regulations. This instrument amends those regulations to ensure that all of the exemptions have the intended scope.

7. Policy background

What is being done and why?

- 7.1 A financial promotion is a communication that contains an invitation or inducement to engage in a financial product or service. Such communications can take a wide variety of forms, including advertisements placed through print, broadcast or online media; marketing brochures; direct mail; or use of social media. Financial promotions are often consumers’ first contact with an investment opportunity and so can have a significant influence over the financial decisions they make.
- 7.2 The financial promotions regulatory regime in the UK seeks to ensure that consumers are provided with clear and accurate information that enables them to make appropriate decisions for their individual circumstances. Financial promotions communicated by unauthorised persons (i.e. firms that are not authorised for the purposes of FSMA 2000) must be approved by firms that are authorised by the FCA or PRA, unless the promotion is otherwise subject to an FPO exemption.

² The FPO revoked and replaced the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (S.I. 2001/1335).

³ This recommendation can be found in paragraph 180 of the Treasury Select Committee report, found at: https://publications.parliament.uk/pa/cm5802/cmselect/cmtreasy/149/14909.htm#_idTextAnchor067.

7.3 The FPO exemptions enable unauthorised persons to communicate financial promotions in certain circumstances, including to defined groups or individual investors, without requiring approval. Since financial promotions which are communicated within the scope of the exemptions do not require the approval of an authorised person, they are also not subject to the detailed FCA rules that authorised firms must otherwise comply with when communicating or approving financial promotions. The scope of the exemptions must therefore be carefully considered given these financial promotions are not subject to the safeguards of the financial promotion regime.

7.4 This instrument amends the certified high net worth individual (Article 48) and self-certified sophisticated investor (Article 50A) exemptions, and also legislates to ensure that the exemptions to the financial promotions gateway apply as intended. These amendments can be summarised as:

- (a) Increasing the financial thresholds to be eligible for the high net worth individual exemption to:
 - o income of at least £170,000 in the last financial year; or
 - o net assets of at least £430,000 throughout the last financial year;
- (b) Amending the criteria to eligible for the self-certified sophisticated investor exemption by:
 - o removing the criterion of having made more than one investment in an unlisted company in the previous two years; and
 - o increasing the company turnover required to satisfy the ‘company director’ criterion to £1.6m (i.e. directors of companies with at least £1.6 million turnover will remain eligible for the self-certified sophisticated investor exemption);
- (c) Requiring natural persons or corporations to provide details of themselves in any communications made using the exemptions;
- (d) Updating the title of the certified high net worth individual exemption by removing ‘certified’;
- (e) Updating the high net worth individual and self-certified sophisticated investor statements;
- (f) Applying the changes to the exemptions in relation to the promotion of collective investment schemes; and
- (g) Ensuring that all of the exemptions to the financial promotions gateway have the intended scope.

(a) Increasing the financial thresholds to be eligible for the high net worth individual exemption

7.5 This instrument will raise the financial thresholds to be eligible for the high net worth individual exemption in line with inflation to £170,000 of income in the previous financial year (from the current threshold of £100,000), or to have held net assets – excluding a primary residence or pension – of £430,000 throughout the previous financial year (from the current threshold of £250,000). These thresholds have not been updated since this exemption was introduced in 2001, while inflation has eroded their value. In addition, following pension reforms (“pensions freedoms”), investors can more easily withdraw from their Defined Contribution pension pots and invest

outside of a pension wrapper, meaning some investors are more likely to meet the thresholds than they would have been in 2001.

(b) Amending the criteria to be eligible for the self-certified sophisticated investor exemption

7.6 One of the four criteria to be classified as a self-certified sophisticated investor is to have made more than one investment in an unlisted company in the previous two years. Following the rise of online investing, it is much easier for individuals to invest in unlisted companies than it was in 2005, when the self-certified sophisticated investor exemption was introduced. This instrument will remove this criterion from the self-certified sophisticated investor eligibility criteria. The government is of the view that this criterion is no longer an indicator of investor sophistication and that on balance it should be removed.

7.7 Another of the tests to be a self-certified sophisticated investor is that an individual has been a director of a company with an annual turnover of at least £1 million in the last two years. Similar to the high net worth individual thresholds, this value has been devalued by inflation since it was introduced in 2005. The instrument raises the annual turnover threshold, in line with inflation since 2005, to £1.6 million. The government considers that being a director of a company with £1.6 million annual revenue is a sufficiently high bar to demonstrate business success and sophistication, and will exclude less experienced directors.

(c) Requiring natural persons or corporations to provide details of themselves in any communications made using the exemptions

7.8 This instrument will require businesses to provide details about themselves in any communications made using the exemptions. This includes company address, contact information, and the company's registration details (i.e. the company's Companies House number, or international equivalent). This aims to help prospective investors undertake basic due diligence on the persons marketing investments. It could also assist the FCA in investigating potential non-compliance with the exemptions.

(d) Updating the title of the certified high net worth individual exemption by removing 'certified'

7.9 As of the coming into force of the FPO in 2005, investors no longer have to be certified by a third party to use the certified high net worth individual exemption. The term "certified" is therefore an outdated description, and so the instrument will remove 'certified' from the title of the exemption.

7.10 The instrument makes consequential amendments to other legislation to reflect these changes, as well as updating outdated references to predecessors of the FPO and the Financial Conduct Authority.

(e) Updating the high net worth individual and self-certified sophisticated investor statements

7.11 This instrument introduces updated statements that potential investors are required to complete and sign, in order to be classified as high net worth individuals or self-certified sophisticated investors. These changes aim to improve the statement format, simplify the language where possible, and make changes that will require greater engagement from the investors completing them.

7.12 These changes are being made as some investors may not understand or engage with the information that is presented to them in financial promotions, including the investor statements. As a result, some investors may incorrectly certify themselves

and/or not understand the regulatory protections they are giving up when receiving promotions subject to the exemptions.

(f) Applying these changes to the equivalent exemptions for promotion of collective investment schemes

- 7.13 This instrument amends relevant exemptions set out in PCIS, so that these exemptions continue to be aligned with the FPO exemptions amended by this instrument. This involves updating the certified high net worth individuals (article 21) and self-certified sophisticated investors (article 23A) exemptions in PCIS to reflect the changes described above, including updating the investor statements.

(g) Ensuring that all of the exemptions to the financial promotions gateway apply as intended

- 7.14 This instrument also corrects a defect in the Financial Promotion Gateway Regulations. Those regulations provide for exemptions from the requirement to first obtain permission from the FCA before approving financial promotions of an unauthorised person (“gateway exemptions”).
- 7.15 The effect of this correction will be to expand the scope of the gateway exemptions for authorised persons approving financial promotions of unauthorised entities that are part of the same group, and; authorised persons (as a principal) approving financial promotions of their appointed representatives, in relation to regulated activities comprised in the carrying on of the business for which the authorised persons have accepted responsibility.
- 7.16 This correction intends to ensure that where the content of the communication has been approved by an authorised person in those circumstances, any unauthorised person will be able to communicate the financial promotion. This will expand the scope of those gateway exemptions so that they apply as intended and allow onward communication of the promotion by an unauthorised person in a similar way to the other gateway exemption provided for in those regulations (which relates to authorised persons approving financial promotions that they prepare).

What did any law do before the changes to be made by this instrument?

- 7.17 The certified high net worth individual exemption (Article 48) was introduced in 2001 and currently exempts from the financial promotion restriction communications to individuals where investors sign a statement confirming that they meet the relevant criteria by having an income of £100,000 or more in the last financial year, or net assets of £250,000 or more throughout the last financial year.
- 7.18 The self-certified sophisticated investor exemption (Article 50A) was introduced in 2005 and currently allows individuals to self-certify as sophisticated, by signing a prescribed statement, if they meet one of the following four criteria:
- They are a member of a network or syndicate of business angels (and have been for at least six months prior);
 - They have made more than one investment in an unlisted company in the previous two years;
 - They are 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 SMEs; or
 - They are currently or have been in the previous two years a director of a company with an annual turnover of at least £1 million.

- 7.19 The Financial Promotion Gateway Regulations exempt authorised persons from the requirement to obtain permission from the FCA before approving financial promotions of an unauthorised person, in the following circumstances:
- Authorised persons approving the financial promotions that they prepare which are communicated by unauthorised persons;
 - Authorised persons approving financial promotions of unauthorised entities that are part of the same group; and
 - Authorised persons (as a principal) approving financial promotions of their appointed representatives, in relation to regulated activities comprised in the carrying on of the business for which the authorised persons have accepted responsibility.

Why is it being changed?

- 7.20 The certified high net worth individual exemption and the self-certified sophisticated investor exemption have not been substantively updated since 2005. In light of the changes to the context in which the exemptions operate, and concerns about misuse of the exemptions, the Government has reviewed the exemptions with a view to mitigating the risks that had been identified.
- 7.21 Whereas the gateway exemptions provided for in the Financial Promotion Gateway Regulations enable financial promotions that have been prepared and approved by authorised persons to be communicated by any unauthorised person, the gateway exemptions do not enable onward communication by any unauthorised person where an authorised person approves financial promotions of unauthorised entities that are part of the same group, or; where an authorised person (as a principal) approves financial promotions of their appointed representatives, in relation to regulated activities comprised in the carrying on of the business for which the authorised persons have accepted responsibility. This does not meet the intended effect of the exemptions.

What will it now do?

- 7.22 Following a public consultation on this policy and careful consideration by the government, this instrument amends the exemptions as outlined above, including by raising the financial thresholds; tightening the eligibility criteria for the self-certified sophisticated investor exemption, and strengthening the investor statements. Overall, these changes aim to both reduce the risk of consumer detriment and preserve the ability of unlisted companies to raise finance under the exemptions.
- 7.23 The instrument also amends the Financial Promotion Gateway Regulations to ensure that the gateway exemptions apply as intended, enabling that where the content of the communication has been approved by an authorised person within the scope of a gateway exemption, any unauthorised person will be able to communicate the financial promotion.

8. European Union Withdrawal and Future Relationship

- 8.1 This instrument does not relate to withdrawal from the European Union.

9. Consolidation

- 9.1 This legislation does not consolidate any other legislation.

10. Consultation outcome

- 10.1 In light of the changing context and the recommendation from the Treasury Select Committee, HM Treasury reviewed the exemptions and developed policy proposals for reform. On 15 December 2021, HM Treasury published a consultation paper⁴ entitled “Financial promotion exemptions for high net worth individuals and sophisticated investors: a consultation”, seeking views and evidence in response to the proposals, including from those who use the exemptions. The consultation period closed on 9 March 2022 and 32 responses were received.
- 10.2 Having carefully considered the different viewpoints from the consultation, the government is bringing forward a balanced set of measures that increase protections for retail investors. Consultation respondents were mostly supportive of the proposals that the government is taking forward through this instrument.
- 10.3 On the same date as laying this instrument to legislate these reforms, HM Treasury has published a consultation response⁵ entitled “Financial promotion exemptions for high net worth individuals and sophisticated investors: Consultation response”.

11. Guidance

- 11.1 No guidance is to be provided by the Government in connection with this instrument.
- 11.2 The Government has published a consultation response that sets out the amendments being made in this instrument, and which displays the new investor statements that should be used when the amendments take effect.

12. Impact

- 12.1 The impact on business, charities or voluntary bodies is that those wishing to make a financial promotion to a prospective investor will need to familiarise themselves with the amended legislation. The costs of familiarisation have been estimated to be £306,619 in the first year that this measure is introduced.
- 12.2 There is no, or no significant, impact on the public sector.
- 12.3 A full impact assessment has not been prepared for this instrument because, in line with Better Regulation guidance, HM Treasury considers that the net impact of this instrument on businesses will be less than net £5 million Equivalent Annual Net Direct Costs to Business. Due to this limited impact, a de minimis impact assessment has been carried out, a copy of which is published alongside this Explanatory Memorandum on the [legislation.gov.uk](https://www.legislation.gov.uk) website.

13. Regulating small business

- 13.1 The legislation applies to activities that are undertaken by small businesses.
- 13.2 No specific action is proposed to minimise regulatory burdens on small businesses.
- 13.3 The basis for the final decision on what action to take to assist small businesses is that this instrument does not increase ongoing regulatory burdens. Instead, it amends the investor eligibility criteria to use the exemptions and updates the investor statements.

⁴ <https://www.gov.uk/government/consultations/financial-promotion-exemptions-for-high-net-worth-individuals-and-sophisticated-investors-a-consultation>

⁵ <https://www.gov.uk/government/consultations/financial-promotion-exemptions-for-high-net-worth-individuals-and-sophisticated-investors-a-consultation>

Small businesses will continue confirming investor eligibility as part of their existing processes when they make a financial promotion to prospective investors.

14. Monitoring & review

- 14.1 The approach to monitoring this legislation is that HM Treasury will keep the overall regulatory framework for financial promotions under review.
- 14.2 The instrument does not include a statutory review clause and, in line with the requirements of the Small Business, Enterprise and Employment Act 2015, the Economic Secretary to the Treasury has made the following statement: “It would be disproportionate to include a statutory review clause in this legislation as it does not introduce new ongoing regulatory burdens on businesses.”

15. Contact

- 15.1 Edwin Ferguson at HM Treasury Telephone: 07971556140 or email: Edwin.Ferguson@hmtreasury.gov.uk can be contacted with any queries regarding the instrument.
- 15.2 Anna Harvey, Deputy Director for Personal Finances and Funds, at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.
- 15.3 Andrew Griffith MP, the Economic Secretary to the Treasury at HM Treasury can confirm that this Explanatory Memorandum meets the required standard.