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Ottobre 2014

Marketing investment opportunities to UK-based investors: a quick reference guide for non-UK lawyers, investment managers, brokers and bankers

Giuseppe Giusti, M&A and Financial Services, Dickson Minto W.S.

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1. Introduction

This note outlines the key legal restrictions that a person looking to market an investment opportunity to UK-based investors must bear in mind before approaching any such investor.

This note is relevant to persons who are based outside of the UK and are looking to:

1. raise capital by way of a private placement with UK-based investors of shares, bonds or other securities in a trading company;
2. raise capital by way of a private placement with UK-based investors of units in a collective investment scheme, investment company or investment fund, or
3. find a UK purchaser for an asset such as an existing business or the shares in a private company that is being sold by its owners.

The key restrictions that are considered in this note are:

1. the prohibition on making unlawful financial promotions;
2. the prohibition on carrying on regulated activities without authorisation;
3. the requirement to send a marketing notification to the Financial Conduct Authority ("**FCA**") if an alternative investment fund is being marketed; and
4. the requirement to publish an approved prospectus if shares or other transferable securities are being offered to the public in the UK.

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This note assumes that:

1. the person marketing the investment opportunity in the UK is not resident in the UK and does not have a permanent place of business in the UK;

2. the person marketing the investment opportunity in the UK is not authorised by the competent authority of an EEA state under the Markets in Financial Instruments Directive (2004/39/EC) ("**MiFID**") or the Alternative Investment Fund Managers Directive (2011/61/EU) ("**AIFMD**"); and

3. any shares or other transferable securities being offered to UK investors would not be admitted to trading on any regulated market or stock exchange in the UK.

In this note, the word "person" is used to refer to a body corporate as well as a natural person (that is, an individual).

2. Financial Promotions

Overview

Under section 21 of the Financial Services and Markets Act 2000 ("**FSMA**"), a person (whether based in the UK or abroad) must not, in the course of business, communicate to any potential investor in the UK an invitation or inducement to engage in investment activity unless:

1. the person communicating the invitation or inducement is authorised by the FCA to carry on regulated activities in the UK;

2. the content of the communication is approved by an authorised person; or

3. the communication is covered by an exemption.

A breach of the above prohibition constitutes a criminal offence and is punishable with an unlimited fine and/or up to two years imprisonment. In addition, any agreement entered into by a person as a result of an unlawful financial promotion may be unenforceable.

A person based overseas who is looking to market an investment opportunity to UK-based investors is unlikely to be authorised by the FCA or have arranged for the content of its communications to be approved by an authorised person.

In order to avoid breaching the financial promotion prohibition, such person must therefore ensure that any communication made to UK-based investors is covered by one or more of the available exemptions.

Exemptions

The key exemptions on which a person based overseas may be able to rely are:

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1. Investment professionals

Article 19 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the "**FPO**") provides that the financial promotion prohibition does not apply to any communication that is made only to recipients whom the person making the communication believes on reasonable grounds to be "investment professionals".

Investment professionals include:

(i) any person authorised by the FCA or the Prudential Regulation Authority ("**PRA**") to carry on regulated activities in the UK such as authorised corporate finance firms, brokerage firms, investment managers, financial advisers, private wealth managers, commercial banks, investment banks and insurance companies;

(ii) the UK Government, UK local authorities (such as local councils) and certain international organisations; and

(iii) certain persons whose ordinary business activities involve them in carrying on investment activities, even if they are not authorised by the FCA or the PRA such as certain investment companies, family offices and professional firms.

It is possible therefore to approach any of the above categories of investors and discuss with them the terms of a proposed investment opportunity without contravening the financial promotion prohibition.

Whether a prospect is authorised by the FCA or the PRA can be verified easily by making an on-line search of the UK Financial Services Register at the following link: http://www.fsa.gov.uk/register/firmSearchForm.do.

A list of the private equity and venture capital firms that are members of the British Venture Capital Association (BVCA) is available from the BVCA on payment of a small fee. Additional information can be obtained from the following link: http://www.bvca.co.uk/membership/memberdirectory.aspx.

2. High net worth companies and associations

Article 49 of the FPO provides an exemption for communications made only to recipients whom the person making the communication believes on reasonable grounds to be persons within one of the following categories:

(i) companies of a particular size (the company itself must have, or be a member of the same group as an undertaking which has, a called-up share capital or net assets of not less than £500,000 if the body corporate has more than 20 members or £5 million otherwise);

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(ii) unincorporated associations or partnerships with net assets of £5 million or more; and

(iii) trustees of a trust with gross cash and investments of at least £10 million.

The above categories of investors can therefore be contacted in respect of a proposed investment opportunity without contravening the financial promotion prohibition.

The person marketing the opportunity should however verify, when it first approaches such investors, that they indeed meet the size and value requirements outlined above.

3. High net worth individuals and sophisticated investors

Under article 48 and article 50 of the FPO, a communication is exempt from the financial promotion prohibition if it is made to an individual whom the person making the communication believes on reasonable grounds to be a "certified" high net worth individual or sophisticated investor.

Certified means, broadly speaking, that the relevant individual has signed a prescribed declaration of high net worth or has been certified as a sophisticated investor by an FCA authorised person.

The above categories of individuals can therefore be contacted in respect of a proposed investment opportunity without contravening the financial promotion prohibition.

There are however a number of conditions that must be met before any such approach can be made, including the insertion of a prescribed wording in any marketing communication.

For the above reason, we recommend that legal advice is obtained before any high-net worth individual or sophisticated investor is approached. This applies irrespective of how wealthy or experienced such individual might be.

4. Sale of body corporate

Article 62 of the FPO provides that an exemption from the financial promotion prohibition applies to any communication made by or on behalf of a body corporate, a partnership, a single individual or a group of connected individuals that relate to a transaction which is one to acquire or dispose of shares in a body corporate (other than an open-ended investment company) and the object of the transaction may reasonably be regarded as being the acquisition of day to day control of the affairs of the body corporate.

"A group of connected individuals" means, for the above purposes, a single group of persons each of whom is or is to be a director or manager of the body corporate or a close relative of any such person.

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As a result of the above exemption, it is generally possible to approach potential investors (even investors who do not fall within any of the categories of exempt investors referred to in paragraphs 1, 2 or 3 above) in in relation to a transaction involving the disposal of the entire issued share capital of a body corporate.

5. Exempt assets

A communication is caught by the financial promotion prohibition only if it relates to a transaction that consists of or involves the acquisition or disposal of shares, bonds, units in an investment fund or other specified investment instruments.

Such prohibition does not therefore generally apply where the investment opportunity being marketed to UK investors relates to:

(i) the acquisition or disposal of real property (e.g. land and buildings) or tangible assets (e.g. art, wine, precious metals, vehicles or industrial machinery or equipment);

(ii) the acquisition or disposal of the business of an undertaking (but not its share capital) as a going concern;

(iii) the entering into of a joint venture (except a corporate joint venture); or

(iv) the entering into of a commercial contract (other than a contract of insurance, certain credit agreements or a contract entered into for investment purposes such as a derivative contract).

A person who is based outside the UK is therefore generally able to market to UK-based investors investment opportunities concerning any of the above assets without being in breach of the financial promotion prohibition.

Use of Disclaimers

UK law does not require the inclusion of a disclaimer in a financial promotion that is communicated to UK-based investors and generally does not make the availability of an exemption dependent on the use of a disclaimer.

It is customary however to include a disclaimer in a financial promotion because it may assist in establishing that the terms of the FPO have been complied with, particularly where other efforts have been made to ensure that the recipients of the financial promotion fall within the relevant class of exempt recipients.

It is usual, for example, to see the following language included on the front or at the end of an information memorandum, teaser, offering document, private placement memorandum or investor presentation that is sent or delivered to UK-based investors:

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"This [information memorandum OR other document] is being distributed on the basis that [the Proposed Transaction is one falling within Article 62(2) (Sale of a body corporate) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 OR each person in the United Kingdom to whom it is issued is reasonably believed to be such a person as is described in Article 19 (Investment professionals) or Article 49 (High net worth companies, unincorporated associations etc.) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 or is a person to whom this [information memorandum] may otherwise lawfully be distributed. Persons who do not fall within such descriptions may not act upon the information contained in this [information memorandum] and must return it to the sender immediately."

Language seeking to impose a duty of confidentiality on the recipients or to limit or exclude any liability of the sender for any potentially inaccurate information contained in the communication is also generally included in a disclaimer.

3. Regulated Activities

Overview

Under section 19 of FSMA, a person that is not authorised by the FCA is generally prohibited from carrying on a regulated activity by way of business in the UK. This prohibition is known as the "general prohibition".

A regulated activity is an activity that has been specified as such in the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (the "**RAO**") and is carried on in relation to certain specified investments such as shares, bonds or units in a collective investment scheme.

Among the activities that are regulated, there are the activity of arranging (or bringing about) deals in investments, which is defined as making arrangements for another person (whether as principal or agent) to buy, sell, subscribe for or underwrite a particular investment, and the activity of making arrangements with a view to transactions in investments.

Such activities may be carried on by a person who, acting on behalf of a third party (i.e. a company looking to raise capital or a shareholder looking to sell his shares), markets an investment opportunity to UK-based investors and/or negotiates with such investors the terms of a potential transaction.

A person who contravenes the general prohibition is guilty of a criminal offence and may face up to two years imprisonment and/or an unlimited fine. In addition, any agreement made by an unauthorised person in breach of the general prohibition may be unenforceable.

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Relevant Factors and Exemptions

It is difficult to state in general terms whether a person based overseas who comes to the UK to market an investment opportunity to UK-based investors is likely to carry on a regulated activity in breach of the general prohibition.

This is because whether a person carries on a regulated activity for the purposes of FSMA depends on a number of factors and the application of several exemptions, some of which are very fact specific.

Broadly speaking, however, there is only a relatively low risk of a breach of the general prohibition occurring in any of the following circumstances:

1. Nature of the assets

The arranging activities carried on in the UK relate to categories of assets that are not caught by the RAO.

Accordingly, a person is generally able to arrange the acquisition or disposal of real property, tangible assets, the business and assets of an undertaking and negotiate the terms of a joint venture or other commercial agreement without, in each case, being in breach of the general prohibition.

2. Business test

The person arranging the deal is acting otherwise than by way of business in the UK, i.e. it is not carrying on "the business of engaging in" a regulated activity in the UK.

For the purpose of applying this test, consideration must be given to a number of factors such as the degree of continuity and scale of any relevant activities, whether such activities have a commercial element and the location from which such activities are carried out.

Even though the application of this test is very fact specific, a person based overseas who visits the UK only for a few days to market a specific investment opportunity to a restricted number of UK-based investors is unlikely in our opinion to carry on a regulated activity in the UK.

By contrast, an overseas person who visits the UK on a regular basis to market a range of investment opportunities to UK-based investors, or who spends a prolonged period of time in the UK to arrange a single deal involving a large number of investors, is more likely to do so.

3. Arranging transactions to which the arranger is party

The arranging activities relate to a transaction to which the arranger is a party.

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Accordingly, a company that makes arrangements for the issue of its own shares, or a shareholder who negotiates the sale of his own shares, does not generally carry on the regulated activity of arranging deals in investments.

4. Arranging transactions with an authorised person

The arranging activities are made with a PRA or FCA authorised firm.

A person is less likely to carry on regulated activities in the UK if he negotiates the terms of a proposed transaction that is to be entered into by an authorised firm (such as an investment management firm) acting as principal or agent on behalf of one or more of its clients.

5. Sale of body Corporate

The arranging activities relate to a transaction that benefits from the exemption concerning the sale of a body corporate that is described in the section on financial promotion above.

Accordingly, activities carried out in relation to a transaction involving the sale of a body corporate are generally exempt from both the general prohibition and the financial promotion prohibition.

In Summary

In summary, there is only a relatively low risk that a person who markets an investment opportunity to UK-based investors could be considered to be in breach of the general prohibition if:

1. his visits to the UK are limited in frequency, continuity and regularity and are made solely to market a specific investment opportunity to a restricted number of UK-based investors; or

2. the marketing activities carried on by him in the UK fall within one or more of the available exemptions (e.g. the sale of body corporate exemption described above); and

in either case, no unlawful financial promotion is communicated to UK-based investors.

If however the marketing activities carried on in the UK are more significant in terms of scope and scale or there is a concern that such activities may not fall within one of the available exemptions, legal advice should be obtained.

Similarly, legal advice should be obtained if an overseas person intends to market an investment opportunity to investors who are individuals.

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4. FCA Marketing Notification

Overview

The need to make a marketing notification to the FCA is a new requirement that was introduced in the UK in July 2013 as part of the UK implementation of the AIFMD.

This new requirement applies where a manager having its registered office outside of the European Economic Area (a "**Third Country AIFM**") wishes to make a direct or indirect offering or placement of units or shares of an alternative investment fund managed by it to or with investors domiciled or having their registered office in the UK.

Under regulation 50 of the Alternative Investment Fund Managers Regulations 2013 (the "**AIFM Regulations**"), a Third Country AIFM may not carry on such marketing activities in the UK unless:

1. it sends a marketing notification to the FCA;
2. it complies with certain ongoing obligations in respect of the fund being marketed; and
3. the FCA has not suspended or revoked its entitlement to market the fund in the UK.

This regime is known as the UK national private placement regime.

Legal Advice

Legal advice should be obtained before a Third Country AIFM begins to market a fund managed by it to UK-based investors.

There are two matters, however, that are worth mentioning in this note.

1. Draft documentation

In the FCA's view, any communication to UK-based investors relating to fund documentation that is not yet in materially final form does not generally constitute marketing for the purposes of the AIFM Regulations and does not therefore trigger a requirement to send a marketing notification to the FCA.

Accordingly, a Third Country AIFM is generally able to discuss with UK-based investors the terms of a proposed new fund and provide to such investors a teaser, a term sheet, an investor presentation and even a draft private placement memorandum without sending a prior marketing notification to the FCA.

This is on the assumption that such draft documentation cannot be used by potential investors to make an investment in the fund and draft documentation is not intentionally

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used by the manager in order to circumvent the application of the AIFM Regulations altogether.

A Third Country AIFM marketing its fund in the UK is required in addition to comply with the rules on financial promotion and the prohibition on carrying on regulated activities in the UK, whether or not a marketing notification has been sent to the FCA.

2. Small AIFMs

If the manager of the fund marketed in the UK is a Third Country AIFM that qualifies as a "small AIFM" (see below), sending a marketing notification to the FCA will result in such manager becoming subject to three key obligations.

The first is an obligation to pay to the FCA a notification fee of £125 and an annual periodic fee of £350.

The second is an obligation to submit to the FCA on an annual basis a form containing basic information on the main instruments in which the Third Country AIFM trades and the principal exposures and most important concentrations of the funds that it manages.

The third is an obligation to give written notice to the FCA of any material changes to the information provided in the marketing notification, which notice must be given at least one month before implementing the change in the case of a change planned by the Third Country AIFM or immediately after the change has occurred in the case of an unplanned change.

None of the above obligations is particularly onerous, especially when compared with the obligations that apply to above-threshold Third Country AIFMs marketing their funds in the UK.

Accordingly, a small Third Country AIFM should not be discouraged from marketing its fund to UK-based investors because of the need to comply with the requirements of the UK national private placement regime.

A small Third Country AIFM may find in fact that the cost of complying with such requirements is a cost well worth incurring given the significant opportunities that being able to market its fund in the UK is likely to give rise to.

A "small AIFM" is defined for these purposes as a manager managing one or more alternative investment funds, the value of whose assets:

1. does not exceed EUR 500 million in total where such funds are unleveraged and have no redemption rights exercisable during a period of 5 years following the date of initial investment; or

2. does not exceed EUR 100 million in total in other cases, including any assets acquired through the use of leverage.

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Leverage that exists at the level of a portfolio company does not generally cause a fund to become leveraged and accordingly a private equity or venture capital fund is generally treated as unleveraged for the above purposes.

5. Need for a Prospectus

Overview

Under section 85 of FSMA, an approved prospectus must be published before shares or other transferable securities are "offered to the public" in the UK. This requirement was introduced in the UK on 1 July 2005 as part of the UK implementation of the Prospectus Directive (2003/71/EC).

An approved prospectus means, for these purposes, a prospectus that has been approved by the FCA or an equivalent regulatory authority in a EEA member state.

There is an offer to the public in the UK if there is a communication to any person which presents sufficient information on the transferable securities to be offered and the terms on which they are to be offered to enable an investor to decide to buy or subscribe for the securities in question. Such communication can be made in any form and by any means and includes the placing of securities through a financial intermediary.

A person who contravenes section 85 of FSMA is guilty of a criminal offence and may be liable to imprisonment for a term not exceeding 2 years and/or an unlimited fine.

Section 85 of FSMA is subject to a number of exemptions on which a person based overseas looking to market an investment opportunity in the UK may be able to rely.

Exemptions

The key exemptions are as follows:

1. Total Consideration Of Less Than EUR 5 Million

There is no need to publish a prospectus if the total consideration for the transferable securities being offered in the EEA States is less than EUR 5 million (or an equivalent amount).

This limit was increased to EUR 5 million from EUR 2.5 million on 31 July 2011.

Accordingly, a company looking to raise less than EUR 5 million in total throughout the EEA (including the UK) will not generally be required to publish an approved prospectus.

2. Qualified Investor Exemption

There is no need to publish a prospectus if an offer is made to or directed at "qualified investors" only.

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Qualified investors are defined for these purposes as those persons considered to be or treated on request as "professional clients" in accordance with the Annex II of MiFID.

Among these, there are:

(i) entities which are required to be authorised or regulated to operate in the financial markets, such as credit institutions, investment firms, insurance companies, collective investment schemes and management companies of such schemes, pension funds and management companies of such funds; and

(ii) large undertakings meeting two of the following size requirements on a company basis: balance sheet total of EUR 20,000,000, net turnover of EUR 40,000,000 and own funds of EUR 2,000,000.

There is a certain amount of overlap between the definition of a "qualified investor" for the purposes of the Prospectus Directive and the definition of a "professional investor" for the purposes of the financial promotion prohibition.

The relevant definitions, however, do not overlap completely and therefore a person who is looking to rely on both exemptions should ensure that the recipients of his communications fall within both definitions.

3. 150 Persons Exemption

There is no need to publish a prospectus in relation to an offer made to or directed at fewer than 150 persons, other than qualified investors, per EEA state.

This exemption, which was increased to 150 persons from 100 persons on 31 July 2011, is particularly useful to persons looking to offer shares or other securities to UK-investors that may not fall within the definition of a "qualified investor".

We recommend however that before any such investor is approached, careful consideration is given as to whether such an approach can be made without breaching the financial promotion prohibition in the UK.

4. Offer Size Exemptions

There is no need to publish a prospectus if any of the following applies:

(i) the minimum consideration that may be paid by any person for transferable securities acquired by him pursuant to the offer is at least EUR 100,000 (or an equivalent amount); or

(ii) the securities being offered are denominated in amounts of at least EUR 100,000 (or an equivalent amounts).

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An offer of shares or other securities to UK institutional investors will generally meet at least one of the above requirements and will therefore be exempt from the requirement to publish an approved prospectus.

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