

FCA considers regulating all promotions and warns of “high risk” mini-bonds and peer-to-peer IFISAs

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Following an “explosion” in online promotions for high yield investment opportunities, the FCA says a “strong case” could be made for regulating how investment products are marketed to retail investors. This would represent a widening of the FCA’s regulatory scope to allow the FCA to prevent and control the promotion of certain investments to individuals, including some high yield and high risk products. The FCA says a range of options “must be in the mix”, including a US style regulatory approach where products must have a regulator awarded license in order to be marketed to retail investors.

The FCA’s consideration forms part of its current policy work on its regulatory perimeter – which dictates what is and is not regulated, and also follows the FCA’s warnings to customers that mini-bonds and peer-to-peer loans held within Innovative Finance ISAs (IFISAs) are “high risk” investments. These kinds of investments can be marketed to retail customers, sometimes by regulated firms, without an accompanying clear statement as to their regulatory status.

While there is no legal definition for mini-bonds, they usually refer to illiquid debt securities that may be marketed to retail consumers. What has proved confusing for consumers is the fact that the mini-bonds themselves do not inevitably attract FSCS protection, even if the firm selling the mini-bonds is authorised and regulated. In particular, where an authorised firm markets or sells its own mini-bonds (say, securities in respect of its own debt), that is not a regulated activity such that FSCS protection could accrue. By contrast, if an authorised firm provides advice about its mini-bonds, this will be a regulated activity which will attract FSCS protection.

Similarly, the FCA has pointed to examples of investment returns from peer-to-peer loans held within IFISAs being described in adverts as superior to the returns from cash ISAs but without adequate risk warnings being given, especially as to the limitations on FSCS protection. The FCA has therefore recently sought to limit retail investors’ exposure to the risk of peer-to-peer investments by restricting investment to a maximum 10% unless investors have obtained financial advice.

Mini-bonds and other unregulated high risk appointments have been thrust in to the spotlight following the collapse of London Capital & Finance Ltd (LCF) which resulted in the loss of around £236m of investors’ funds in securities issued by LCF. The fallout from LCF has prompted the Treasury to undertake a separate review to consider whether the regulatory framework surrounding mini-bond investments is sufficient and appropriate for the protection of customers.

Pending the outcome of the FCA’s policy work on its perimeter and the Treasury’s report we expect to see continued significant regulatory developments going forward.

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