

OnPoint

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A legal update from Dechert's Corporate and Securities Group

The Financial Services Act 2012 – Misleading Statements, Impressions and Financial Promotions

Background

In our previous *DechertOnPoints*, [The Draft Financial Services Bill in the Context of the Proposed New UK Financial Regulatory Structure and Draft UK Financial Services Bill and the New UK Financial Regulatory Structure](#), we discussed the new UK financial regulatory structure and the details of the Financial Services Act 2012 (the “FS Act”). The FS Act received royal assent on 19 December 2012, and will come into force from 1 April 2013. This DechertOnPoint focuses on the criminal offences for misleading statements and misleading impressions, including the new offences relating to benchmarks, and the Financial Conduct Authority’s (“FCA”) new powers relating to misleading financial promotions.

Misleading Statements and Misleading Impressions

The FS Act repeals section 397 of the Financial Services and Markets Act 2000 (“FSMA”), pursuant to which it is currently a criminal offence for a person to either:

- make a statement, promise or forecast which he knows to be misleading, false or deceptive in a material particular, or dishonestly conceal any material facts (whether in connection with a statement, promise or forecast made by him or otherwise); or
- recklessly make (dishonestly or otherwise) a statement, promise or forecast which is misleading, false or deceptive in a material particular,

for the purpose of inducing, or being reckless as to whether it may induce, another person (which need not only be the person to whom the statement, promise or forecast is made or from whom the facts are concealed) to enter or offer to enter into, or to refrain from entering or offering to enter into, a relevant agreement or to exercise, or refrain from exercising any rights conferred by a relevant investment.

Sections 89 and 90 of the FS Act include offences very similar to those currently set out in section 397 of FSMA, with a few differences:

- a distinction is drawn between ‘misleading statements’ (section 89) and ‘misleading impressions’ (section 90);
- section 89 (misleading statements) only refers to a “false or misleading statement” whereas the current offence refers also to a “promise or forecast”. Also, the new offence does not refer to “deceptive statements”; and
- section 90 contains an additional offence of knowingly or recklessly creating a false impression for the purpose of (or with the knowledge that it is likely to lead to) personal gain, or the purpose of causing (or with the knowledge it is likely to lead to) a loss to another person (or exposing that person to risk of loss).

The FS Act introduces a new offence in respect of misleading statements and impressions in relation to benchmarks. Under section 91 of the FS Act, a person will commit an offence who either:

- makes to another person a false or misleading statement if he:
 - makes the statement in the course of arrangements for setting of a relevant benchmark;
 - intends that the statement should be used for the purpose of the setting of a relevant benchmark; and
 - knows that the statement is false or misleading or is reckless as to whether it is; or
- does any act or engages in any course of conduct which creates a false or misleading impression as to the price or value of any investment or as to the interest rate appropriate to any transaction if:
 - he intends to create the impression;
 - the impression may affect the setting of a relevant benchmark;
 - he knows that the impression is false or misleading or is reckless as to whether it is; or
 - he knows that the impression may affect the setting of a relevant benchmark.

The Treasury will specify what constitutes a relevant benchmark in secondary legislation. Elsewhere in the FS Act, “benchmark” means an index, rate or price that is (i) determined by reference to the state of the market, (ii) made available to the public and (iii) used for reference for determining the interest due under loan or other investment related agreements, or for determining the price, value or performance of investments.

Penalties

The FCA will have the lead role in investigating and prosecuting these offences. A person guilty of an offence under the FS Act will be liable to imprisonment for a term up to seven years, or a fine, or both. This reproduces the current penalties for breach of section 397 of FSMA.

Misleading Financial Promotions

Under the FS Act, the FCA will also have the ability to ban financial products, publish details of misleading financial promotions, and let people know when they are proposing to take disciplinary action against a firm.

In a paper issued by Financial Services Authority in October 2012, it is stated the FCA will take three steps when using this new power:

- The FCA will ‘give a direction’ to an authorised firm to remove its own financial promotion or one it approves on behalf of an unauthorised firm, setting out its reasons for banning it.
- Firms can make representations to the FCA if they think it is making the wrong decision.
- The FCA will decide whether to confirm, amend or revoke its direction. If it is confirmed, the FCA will publish it, along with a copy of the promotion and the reasons behind its decision.

Following the third step, firms will be able to refer the matter to the Upper Tribunal if the FCA decides not to revoke the direction.

The paper continues to state that promotions where the FCA will use the power will not only be the worst cases, and it will not always measure harm to consumers in terms of actual or potential financial loss. The FCA will also consider promotions that adversely affect consumers’ ability to make informed choices and secure the best deal for themselves.

Comment

The new offence relating to benchmarks was added to the original draft of the Financial Services Bill in October 2012 following recommendations made in the Wheatley LIBOR report. A review, undertaken by Martin Wheatley, Chief-Executive-designate of the FCA, was commissioned in July 2012, in the midst of the investigations into the alleged (and in some cases, later proven) manipulation of LIBOR by UK and overseas authorities. The results of such review were published in September 2012 and the Government accepted all of the report’s recommendations, including that section 397 of FSMA be extended to capture the making of misleading statements to manipulate benchmarks, such as LIBOR, as criminal offences.

The new offence set out in section 91 of the FS Act certainly captures the making of misleading statements

and impressions in relation to LIBOR. Indeed, the breadth of the definition of benchmark extends its application further – it will be interesting to see how the FCA interprets this definition when using its power to prosecute this offence. However, it remains to be seen whether this is an appropriate measure to prevent the manipulation of LIBOR and other benchmarks in the future (as identified in the Wheatley LIBOR report) or an over-reaction; as it is (notwithstanding the general language used to define 'benchmark') a clearly targeted (and therefore narrow) provision.

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