23 August 2013

Behind the Curve – Are Legal & Regulatory Concerns Preventing UK Financial Service Companies from Fully Harnessing Social Media?

By Susan McLean

Today's consumers want to engage in a new way with the companies from which they buy goods and services. Although some UK financial services organisations are leading the way in terms of their use of social media, on the whole, engagement in social media by UK financial services firms is still relatively limited. This is particularly evident when compared against activity in other sectors and when compared against the level of social media engagement by U.S. and Asian firms. Are legal & regulatory concerns to blame?

CURRENT STATE OF MARKET

How financial services ("FS") organisations engage with social media can help differentiate them from their peers. Particularly when dealing with younger consumers such as the student market, FS organisations need to engage with consumers in the most effective way, which could be by placing a topical blog on Pinterest, a fun video on YouTube or interacting with consumers via Twitter or Facebook (rather than running a traditional print or broadcast campaign). Simply having a Twitter account or Facebook page which pushes out information is no longer enough. Genuine interactive engagement is what consumers are looking for and is the key to the most successful social media strategy.

The best users of social media in the FS sector appreciate that harnessing of social media is as much about raising your brand profile, as promoting specific products or services. Consider the huge success of Comparethemarket.com's Russian meercat brand ambassador who has almost 60,000 followers on Twitter. Also, consider that the winner of the Shorty Award 2013 for Best Use of Social Media for Financial Services was Citi for its Citi-Connect: Professional Women's Network on Linked-In. Neither of these campaigns directly relates to the products and services offered by the relevant firm, but both have been very successful in terms of brand awareness. Social media can also be used to good effect to highlight organisations' corporate social responsibility and philanthropy initiatives – to help counteract the 'fat cat' perception of bankers and financiers. Given that social media enables disgruntled consumers to find a louder voice and journalists are increasingly using social media to get stories, firms need to use social media to try to change the online conversation about their organisations. In fact, the best social media strategies can go beyond engaging consumers and actually convert them into advocates for a brand. The perceived benefits of brand advocacy are huge. According to research, recommendations from personal acquaintances or opinions posted by consumers online are the most trusted forms of advertising. But social media is not just a marketing tool - it can bring wider business value. For example, it can be used in recruitment, customer insights, research and development, issue/crisis management and customer services. (It is also worth pointing out that social media is not just for retail banks and consumer-focused FS firms. It can also be harnessed by firms in the B2B sector. For example, some companies are creating networking and educational communities for their target audience (*e.g.* SMEs, IFAs, *etc*) within more business-focused social media platforms such as Linked-In.)

However, despite the myriad of opportunities that social media offers and the size of the UK FS sector compared to other sectors, the use of social media by FS organisations still appears to be in its infancy. The reluctance by UK financial organisations to fully engage with social media may be down to general conservatism on the part of the sector, a fear of public dialogue with customers and a lack of understanding and expertise in-house in terms of social media and its value. However, it also appears in no small part to be down to uncertainty as to the application of financial laws and regulations to social media. So, what are the legal and regulatory considerations that UK FS organisations have to consider when embarking on a social media strategy and, with the recent replacement of the Financial Services Authority ("FSA") by the Financial Conduct Authority ("FCA") and the Prudential Regulatory Authority ("PRA")[1], will we see any change?

FINANCIAL RULES

In the U.S. various regulatory guidance, including from FINRA, FFIEC and the SEC, on the use of social media has been published. However, to date, in the UK, there has been very limited regulatory guidance regarding social media and the FCA has recently reiterated that it has no current plans to issue any further guidance on the basis that it believes that its rules are media neutral. So it remains up to firms to evaluate their activities carefully against the applicable rules. Some of the key issues for firms to consider include the following.

PRINCIPLES FOR BUSINESS

In terms of overarching obligations, when operating online, a firm must pay attention to the fundamental principles contained in the FCA Handbook, in particular, to treat customers fairly[2] and provide information that is clear, fair and not misleading.[3]

COMMUNICATIONS AND PROMOTIONS

Firms need to ensure that all social media activities comply with the applicable rules concerning communications and promotions ("FCA Promotion Rules").[4] A financial promotion is a communication that is an invitation or inducement to engage in investment activity that is communicated or approved by an authorised person.[5] Financial promotions must comply with all of the applicable FCA Promotion Rules, with the overriding requirement

[1] From 1 April 2013, the FSA's responsibilities were split between two new regulators; the FCA and the PRA. The PRA, which forms part of the Bank of England, is the prudential regulator for banks, building societies, credit unions, insurers and major investment firms. The FCA will regulate the conduct of all financial services firms and will regulate the prudential standards of financial services firms not regulated by the PRA.

[2] Principle 6 (a firm must pay due regard to the interests of customers and treat them fairly).

[3] Principle 7 (a firm must pay due regard to the information needs of its clients and communicate information in a way which is clear, fair and not misleading).

[4] The rules are contained in the FCA Handbook at COBS4, BCOBS2, ICOBS2 and MCOB3. Guidance is provided in the Perimeter Guidance Manual. In addition, in June 2010, the FSA issued some high level guidance specifically on financial promotions communicated using new media.

[5] Section 21 of FSMA.

that promotions must be "fair, clear and not misleading."

As indicated above, the FCA believes that its rules apply in a way that is media neutral; the rules focus on the content of communications and not on the medium used. Therefore, in its opinion, applying the rules to financial promotions using new media is no different to financial promotions made using any other medium. (However, this is easier said than done – the FCA Promotion Rules were created to apply to traditional forms of advertising, but now, for example, need to be interpreted in terms of a 140 character tweet!)

Organisations should note that:

1. banner ads, tweets, sponsored links, hyper-text links, posts on Linked-In and Facebook and other communications made using social media may all be considered promotions. (There are certain exceptions in relation to image advertisements (see below));

2. tweets posted by customer would not be financial promotions, but re-tweets by a firm could be;

3. just because products or services are not explicitly mentioned in a communication does not mean that the communication is not a promotion;

4. in terms of references to past performance, firms will need to include a 5-year chart plus suitable risk warning;

5. risk warnings must be displayed prominently and clearly. (Be aware that roll-over type risk warnings will not be sufficient as the FCA considers that many people may read an advert without hovering over it);

6. there is no "one-click" rule; being one-click away from the necessary information does not automatically make a promotion requirement. Each promotion must be "standalone compliant" - it is not acceptable for a firm to omit important information or risk statements from promotions on the basis that the information will be provided later on in the process; and

7. even if a communication is not classed as a promotion (*e.g.*, it's a response to a query, complaint or general correspondence, *etc.*) it will still need to be clear, fair and not misleading.

An image advertisement will not be considered a promotion in terms of investment and mortgage products, but there is no equivalent exception for insurance products. However, note that an image advertisement is narrowly construed and is limited to an advertisement which contains (i) the name of the firm, (ii) a logo or other image, (iii) contact details and (iv) a reference to the types of regulated activities the firm provides or its fees or commissions (investments) or a brief factual statement of the firm's main occupation (mortgages). Anything more and the communication will fall into the category of promotion.

The potential consequences for breaching the FCA Promotion Rules include: (a) criminal penalties;[6] (ii) agreements entered into as a result of the promotion being unenforceable and compensation payable;[7] and/or

[6] *e.g.,* unlimited fine and up to 2 years imprisonment (section 25 of FSMA)

[7] section 30 of FSMA

(iii) the promotion being banned.[8]

To ensure compliance with the FCA Promotion Rules, firms should:

a. have appropriate policies and procedures in place;

b. consider whether social media is a suitable method for the communication, taking into account the nature and complexity of the product or service (*e.g.*, given the space limitations of the particular channel);

c. consider whether the promotion meets the requirements for standalone compliance;

d. be mindful of the rules when purchasing (or instructing third parties to purchase) search terms from search engine providers;

e. keep appropriate records of all financial promotions; and

f. review communications regularly to ensure that promotions posted via social media remain up-to-date (new media may date more quickly than traditional media).

COMPLAINTS HANDLING

When handling complaints, firms must: (i) investigate each complaint competently, diligently and impartially, (ii) assess each complaint fairly, consistently and promptly, (iii) provide fairly and promptly a clear assessment of the complaint and an offer of redress or remedial action, if appropriate and (iv) ensure any offer of redress or remedial action that is accepted is settled promptly.[9] The FCA classes a complaint as any oral or written expression of dissatisfaction, whether justified or not, about the provision of, or failure to provide, a financial service or a decision by a firm in relation to a consumer redress scheme. Generally the complaint must allege that the complainant has suffered (or may suffer) financial loss, material distress or material inconvenience. In the context of social media, the challenge for firms is whether they can identify when complaints are being made via social media and whether their complaint handing procedures capture such complaints.

OUTSOURCING

If a firm outsources any critical activities as part of its social media strategy it will need to take account of the applicable outsourcing rules and guidance contained in SYSC 8 of the FCA and PRA Handbook.[10]

MARKET ABUSE

A firm is required to comply with applicable market abuse and related rules, including:

1. not make false or misleading statements or omit material information;[11]

---

[8] section 137S of FSMA http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted

[9] DISP

[10] For firms subject to the EU Markets in Financial Instruments Directive (MiFID) or the Capital Requirements Directive (CRD), SYSC 8 is mandatory and non-compliance could result in sanctions.

[11] section 397 of FSMA;

2. not disclose any inside information or commit any other form of market abuse;[12]

3. not disclose inside information;[13]

4. keep the market reasonably informed;[14] and

5. comply with its obligations in terms of announcements;[15]

To avoid falling foul of the applicable rules via social media communications, firms should: (i) put in place appropriate social media policies, procedures and training for employees, (ii) synchronise any social media release with any formal release to the market; and (iii) carry out appropriate internal and external monitoring (*e.g.,* of employees statements on social media and any statements made on linked third-party sites).

FCA MONITORING

Firms should note that even if they are not monitoring what is being said about them online, the regulator might be. When the Bank of Scotland was fined £4.2 million in 2012 for failing to keep accurate mortgage records,[16] this failure was spotted by the regulator through monitoring complaints posted on a consumer forum website. Indeed, in March 2013, the new FCA chief executive indicated that the FCA plans to carry out pro-active monitoring of firms via social media, both for spotting illegal promotional activity and for wider market trends. "*…What's new is that we won't just be relying on regulatory reports back from firms, but on reports from consumer bodies, internet monitoring, the media and even on Twitter. In the past, the emphasis was on firms' regulatory reporting. We will be much broader in our approach.*"[17]

GENERAL ISSUES

Of course, there are a whole host of general legal issues arising from social media that will also need to be considered, *e.g.*, in terms of:

- employees' use of social media (monitoring, policies, training, liability, disclosure of confidential/proprietary information, *etc*);
- use of social media in recruitment;
- privacy;
- security;
- crisis management and damage to reputation;

[12] section 118 of FSMA, FCA Market Conduct Sourcebook;

[13] Disclosure Rules and Transparency Rules

[14] Listing Rules

[15] Takeover Code

[16] http://uk.reuters.com/article/2012/10/19/uk-bos-fine-idUKBRE89I0GK20121019

[17] http://www.telegraph.co.uk/finance/newsbysector/banksandfinance/9958341/Financial-Conduct-Authority-chief-Martin-Wheatley-will-use-Twitter-to-spot-companies-illegal-activities.html

- protection & infringement of intellectual property rights;
- general advertising and marketing rules;
- consumer protection/unfair terms & trading rules;
- user generated/third party content (user terms & conditions, notice & takedown policies and procedures, disclosure of material connections with third party bloggers, *etc*); and
- insurance.

Lastly, many firms are global institutions and so it is always going to be important for firms to ensure that individuals outside of the UK are not unintentionally targeted by any UK social media campaigns, or if they are intended to be targeted, for firms to consider any specific rules that they will need to comply with in the applicable jurisdiction.

STRATEGY

Above all, if financial organisations want to fully harness the potential of social media, they need to spend time and effort creating a social media strategy which has the full backing of relevant stakeholders. When pulling together their strategy, firms will need to take into account all relevant legal & regulatory issues, but they will also need to consider wider factors such as:

- what they want to stand for in social and what they want to use social media for? What value will it bring to the company? What value will it bring to their customers?
- understanding social media across all business lines – it's no longer just a marketing issue;
- understanding their audience and relevant influencers (*e.g.,* bloggers, journalists, forums, *etc*);
- putting in place adequate and appropriate resources, policies and procedures to manage social media activities;
- thinking like a publisher – what is engaging content for customers and influencers?; and
- how they can respond quickly and appropriately to online criticism.

CONCLUSION

As a result of the recent financial crisis, consumers' trust in financial organisations is at an all-time low and so it is increasingly difficult for financial organisations to get the positive attention of consumers. New competitors (*e.g.,* from retail and telecoms, as well as start-ups) are moving into the FS market, many of which may be more agile and better equipped in terms of a digital strategy than the traditional finance brands. Social media provides great opportunities for firms to engage with customers in a new and interactive way and whilst organisations need to be careful to comply with the relevant laws and regulations, they need to get on board, and fast, if they want to be one of the winners in the new digital world.

Client Alert

Contact:

Susan McLean
44 20 7920 4045
smclean@mofo.com

About Morrison & Foerster:

We are Morrison & Foerster—a global firm of exceptional credentials. Our clients include some of the largest financial institutions, investment banks, Fortune 100, technology and life science companies. We've been included on *The American Lawyer*'s A-List for 10 straight years, and *Fortune* named us one of the "100 Best Companies to Work For." Our lawyers are committed to achieving innovative and business-minded results for our clients, while preserving the differences that make us stronger. This is MoFo. Visit us at www.mofo.com.

Because of the generality of this update, the information provided herein may not be applicable in all situations and should not be acted upon without specific legal advice based on particular situations. Prior results do not guarantee a similar outcome.