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CUMMINGS PEPPERDINE

CUMMINGS PEPPERDINE ON ACTING AS AN INVESTMENT ADVISOR OR ARRANGER IN THE UK

THE VERY BEGINNING - INCORPORATION

An investment advisor and arranger in the United Kingdom ("UK") will generally be set up either as a limited company or as a limited liability partnership ("LLP"). This choice as to formation will depend upon a number of issues, including, but not limited to, management and control, size, key individuals, employees,One of the key factors usually centres around the question of taxation.

Whereas a limited company is taxed separately from its shareholders and is subject to corporation tax and to national insurance contributions in respect of its employees, an LLP is regarded as a corporate entity, which confines the liability of its members to the assets of the LLP, but it is ordinarily tax transparent i.e. it is taxed like a partnership in that each of the members are taxed as partners, each being liable for tax on their share of the income or gains of the LLP.

The accounting and filing requirements for an LLP are broadly the same as those of a limited company, but another important difference is that a shareholder's agreement is a

public document, whereas any agreement between the members of an LLP ("the LLP agreement") is a private document which is confidential to the members.

Thus, before deciding upon which type of entity the advisor and arranger should be, it would be advisable to seek tax advice as to which corporate formation would be beneficial in the particular circumstances.

THE NEXT STEP – IS FCA AUTHORISATION REQUIRED?

The next step for consideration is whether the advisor and arranger will need to be authorised by the Financial Conduct Authority ("FCA") in the UK. Pursuant to the Financial Services and Markets Act 2000 ("FSMA"), a firm carrying out a regulated activity in the UK must be authorised and regulated by the FCA and will be subject to ongoing oversight, supervision and regulation by the FCA.

Unless an exemption applies, advising and arranging will generally be a regulated activity in the UK if carried out in respect of certain Specified Investments, as set out in Financial Services and Markets Act (Regulated Activities) Order 2001 (SI 2001/544) ("RAO").

If authorisation is required, the firm will need to apply for authorisation and individuals who will be carrying out certain key roles at authorised firms must also obtain approval from the FCA before doing so. Approval for both the firm and the individuals is commonly applied for at the same time and the authorisation process commonly takes between six to eight months.

You can find more details about exactly what the FCA authorises in our Pep Publication "Cummings Pepperdine on FCA Regulated Activities and Investments":

www.cummingspepperdine.com/wp-content/uploads/2022/01/Cummings-Pepperine-on-FCA-Regulated-Activities-and-Investments.pdf

WILL YOU BE ADVISING ON INVESTMENTS?

A person must not carry on the activity of advising on investments in the UK unless they are an authorised or exempt person, or an exclusion applies.

The advising on investments activity is set out in article 53(1) of the RAO. Broadly speaking, most regulated firms will only carry on the article 53(1) regulated activity if the advice they provide makes a personal recommendation as defined in the Second Markets in Financial Instruments Directive (2014/65/EU), known as MiFID II

The position is different for firms and individuals that are not authorised under the FSMA (that is, unregulated firms). Those persons are unable to provide advice on financial products and services, regardless of whether it involves a personal recommendation.

To help, the below gives the issues to consider when following a decision tree:

- does the advice concern a relevant investment, a structured deposit or a security?
- does the advice concern an investment type which is specified as such in the RAO?
- does the person provide advice on the merits of dealing in, or exercising (or not exercising) any right to deal, conferred by an investment?
- is the advice given to an investor, potential investor or their agent?
- is the communication advice and not just information?.
- does the advice involve a personal recommendation?
- is the person providing the advice appropriately authorised?
- has the person agreed to advise on investments?
- does the person advise on investments "by way of business"?
- does the person advise on investments in the UK?
- is an exclusion available under the RAO?
- is the person an exempt person.

WILL YOU BE ARRANGING DEALS IN INVESTMENTS?

A person must not carry on the activity of arranging deals in investments in the UK unless they are an authorised or exempt person, or an exclusion applies.

There are two types of arranging activity that are set out in article 25 of the RAO: (i) arrangements bringing about investments (article 25(1)); and (ii) arrangements made with a view to transactions in investments (article 25(2)).

As with giving investment advice, there are potential exclusions and exemptions. And again, to help, here are some of the issues to consider when following a decision tree:

- do the arrangements relate to the relevant categories of specified investments as defined in the RAO?
- do the arrangements "bring about" deals in investments or are they made "with a view to" deals in investments?;
- has the person agreed to make arrangements?;
- does the person arrange deals in investments "by way of business"?;
- does the person arrange deals in investments in the UK?
- is there an exclusion available under the RAO?
- is there an exemption?

THE FCA APPLICATION

An FCA application requires a certain amount of preparatory work and applicants need to familiarise themselves with the FCA Handbook of Rules and Guidance, which contains the rules of the FCA, particularly the Principles for Businesses ("PRIN"), as these are fundamental to the entire regulatory regime.

The FCA requires all applicants to demonstrate the following:

I. that they have adequate financial resources to meet the minimum financial requirements for their particular prudential category ("PRU");
II. that they have determined the systems and controls they will need to put in place in order to support their activities and comply with relevant rules ("SYSC");
III. that the relevant staff are approved or will be approved to carry out controlled functions ("SUP"); and
IV. that they have determined which of their staff will require professional qualifications in order to perform their roles ("TC").

The application process itself is a single process, which means that all applicants have to comply broadly with the same application requirements, but the amount of information required will, of course, depend on the nature of the business. Each applicant has to set out clearly in its application the regulated activities which it requires permission to carry on.

The application is time-consuming and quite complex and certain documents need to be supplied for an investment advisor and arranger. In addition, the applicant must include terms and conditions and an investment advisory agreement, both of which must be FCA compliant as well as being commercially and legally correct. Due to its complexity, it is very common for counsel to be instructed to prepare the application pack.

You can find more details about exactly what the FCA authorises in our PepP Publication "Cummings Pepperdine on Making an FCA Application":

www.cummingspepperdine.com/wp-content/uploads/2022/02/Cummings-Pepperdine-Making-an-FCA-Application.pdf

COSTS TO CONSIDER

The costs of establishing the advisor and arranger in the UK could include the following:

I. incorporation costs (similar for both company and LLP);
II. preparation of articles of association (for company, can be off the shelf) and the cost is included in the incorporation costs above;
III. preparation of shareholders agreement/ LLP agreement which will vary according to structure and complexity;
IV. costs related to FCA application, including application fee and requirement for minimum regulatory capital. Again, this vary depending on complexity and structure and will include the FCA's own fee(s);
V. preparation of an investment advisory agreement and advice on the relevant marketing rules, including those on financial promotions;
VI. costs of introducing systems and compliance; and
VII. taxation and legal costs in relation to advice on the above which again will vary depending on the UK issues as well as any offshore considerations.

Prospective applicants should note that the FCA will require them to maintain regulatory capital and make at least quarterly reports, which will include financial reporting. Some firms may like to take compliance and/or accounting help with the returns.

Accountants will also need to be appointed to conduct an annual audit of accounts.

Other set up and ongoing costs will be those expected in the normal course of commercial events.

For more information, visit our website to read our Pep Publications and listen to The Hugely Popular Cummings Pepperdine Crypto Questions

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The Cummings Pepperdine Online Training Programme, includes sections focussing on Acting as an Investment Advisor or Arranger in the UK, has been designed by a specialist board of compliance consultants, solicitors, chartered accountants, tax advisors and regulatory consultants. We believe that we are the only firm which offers training created by this range of qualified advisors.

Click here now to make it all work

Watch our introductory video

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