THE APPOINTED REPRESENTATIVE REGIME: REFORMS, LIABILITY AND AGENCY

Tom White and Rob Crossingham, Partners at Clyde and Co, recently presented a Technical Forum that focussed on the FCA's changes to the Appointed Representatives ("**AR**") regime.

This Bulletin summarises the principal points from the forum, the slides and a full recording of the Technical Forum are available on the Member Portal.

AR REGIME – Brief Synopsis

The regime was originally introduced in 1986 to allow self-employed representatives to engage in a limited number of regulated activities on behalf of and under the responsibility of an authorised firm (the Principal), without having to be authorised.

Section 19 of the Financial Services and Markets Act 2000 – (the "**General Prohibition**") allows for performing regulated activities if classed as 'an exempt person'.

Furthermore, since ARs are not fully authorised firms, there are restrictions on the regulated activities they can perform. For general insurance ARs the following are permitted:

- dealing in investments as agent
- arranging (bringing about) deals in investments
- assisting in the administration and performance of a contract of insurance

It is a requirement for all ARs that a contract must be in place with its Principals which deals with, entry on the Financial Services Register, compliance, cooperation, information and termination.

THE CHANGES

The FCA have confirmed a number of changes to the obligations and expectations of Principals. There are no significant changes for the ARs themselves. Where ARs are seeking multiple Principals, the Principals must have an agreement with each other to include, but not limited to:

- Scope of activities
- Complaint handling
- Supervision and monitoring

Such multi-principal arrangements can prohibit certain activities or product types, for example, life assurance or long-term care insurance, unless all of the other Principals are providers of such products.

The majority of changes affect the Principals as follows:

Key Additional Information and Notification Requirements (others apply)

- New AR appointments must be notified to the FCA at least 30 calendar days before the appointment is due to take effect, they must also provide the rationale behind the appointment and details of the financial and non-financial arrangements entered into.
- Details of the AR's business activities and whether they will engage with retail consumers.
- Principals with existing ARs must provide additional information to meet new requirements.
- Principals will need to annually confirm that the AR details on the FS register are correct.
- Report annually on AR key data including complaints and revenue.

Increased Supervisory Responsibilities

- Enhanced assessment and monitoring to "a comparable standard as if they were an individual directly employed by the Principal."
- Conduct an annual review to include but not limited to financial position, and the adequacy of the controls and resources in place to effectively oversee the AR.
- Principals can now conduct ad-hoc reviews.
- Annually assess information held on their ARs that should focus on how the principal itself is meeting its responsibilities in relation to all of its ARs. This document will need to be reviewed and signed-off by the Principal's governing body.
- Be clear regarding the circumstances in which they should terminate an AR relationship and ensure the contract covers this. Principals need to take reasonable steps to ensure they assist ARs with orderly wind down.

LIABILITY CONSIDERATIONS

Members with ARs have to carefully consider how the changes impact their business model and most importantly, potential liability issues.

In common law an agent can have express, implied or ostensible authority. Express authority for a regulated activity is self-explanatory. Implied authority will cover conduct that is incidental to the advice (fact-finding etc) and which is necessary for the service. Ostensible authority is where the AR may give the impression to the client that it has authority but does not.

In **Martin and Another v Britannia Life Ltd** the claimants sought financial advice to enable them to pay off debts and put in place a pension. The AR had express authority to provide investment advice but provided additional mortgage-related products in the package that it had no authority to sell. This was held to be part of the wider work ordinarily required to meet the AR's actual authority.

Additionally, the Principal issued business cards stating the AR was a 'financial advisor' (there was no qualification / limitation of scope on the card). The court held that the claimant had reasonable grounds to believe the AR had ostensible authority from the Principal to provide all the relevant investment advice.

Liability is also covered in FSMA 2000 and in particular ss39/3 and ss39/4.

- **FSMA s.39(3)** *"The principal of an [AR]* ***is responsible****, to the same extent* ***as if he had expressly permitted it****, for anything done or omitted by the [AR] in* ***carrying on the business for which he has accepted responsibility****."*

A number of cases cover this, including **Emmanuel v. DBS Management Plc (pre FSMA 2000)** and **Anderson v. Sense Network**.

These cases examine the detail / scope of the AR agreement. In **Emmanuel v. DBS** there were two transactions: (i) DBS Management was the Principal of the AR; and (ii) an earlier transaction where DBS was not the Principal. While the AR had authority to provide advice on investments, the advice given in the later transaction was to loan money to the AR. It was held that the first investment predated the involvement of DBS and was out of scope and the second did not involve DBS as Principal as it was a matter solely between the client and the AR.

In **Anderson v. Sense**, the AR (MIDAS) was authorised to provide investment advice. Sense was the Principal for at least 7 years. Issues with the scheme were discovered after whistleblowing by a MIDAS employee and a claim was initiated by investors. The AR agreement stipulated that MIDAS must use the services of a particular firm approved by Sense as part of the process. MIDAS did not engage the services of the approved firm and thus acted outside the scope of the AR agreement.

- **FSMA s.39(4)** "*In determining whether an authorised person has complied with … a provision contained in [FSMA] … anything which [the AR] has done or omitted as respects business for which the authorised person has accepted responsibility is to be treated as having been done or omitted by the authorised person*."

This does not relate to whether the acts / omissions of the AR are directly attributable to the Principal.

- **FSMA s.27** applies where an agreement made by an authorised person arises as a result of the act of an unauthorised person acting in breach of the General Prohibition. In such cases the agreement is unenforceable, and the authorised person has to return any money/property paid or transferred under the agreement and pay compensation for any losses.

- **FSMA s.138D where** "*A contravention by an authorised person of a [FCA rule] is actionable [by] a private person who suffers loss as a result of the contravention …*". This is solely a civil right of action against an authorised person for a breach of an FCA **rule** where that breach has **caused** loss.

Both these sections appear for consideration in **Adams v. Options**. An unregulated firm based in Spain (CLP) offered clients the opportunity to invest in 'store pods' via a UK investment firm (Options), whose services were 'execution only'.

The court held that CLP provided investment advice in breach of the General Prohibition and that the case against Options was valid.

Further, as Options were acting on an 'execution only' basis and this was clear to and accepted by the claimant from the outset, there was no obligation for Options to provide any advice or associated services. As such Options had acted in the best of interests of the claimant and so had not caused a loss to the claimant.

CONCLUSION

Continuing use of ARs by Members can cause significant liability issues. The nature and extent of the arrangement between the two parties must be clear and unambiguous, detailing the authority as well as what is in/out of scope – the devil truly is in the detail.

Furthermore, with the new responsibilities, the management of ARs is now more important than before. Simply stating an oversight regime is in place is not sufficient. It must be demonstrated that it is robust and acted upon. The risk management team is happy to provide guidance on what constitutes a robust oversight regime, if required.

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