Factsheet 4: Financial promotions

4.1 Promoting community investment

Encouraging people to invest in an enterprise must be undertaken in a responsible manner because it can result in them losing their money. The Financial Services and Markets Act 2000 created a regulatory framework governing the promotion of investment opportunities, including shares and bonds. This legislation applies just as much to community investment as it does to any private investment that is promoted to the public. The main aim of this legislation is to make the public aware of the risks and benefits associated with different kinds of investment, to protect the public from misleading financial promotions, and generally to establish and maintain public confidence in the financial system.

It is important that community investment is promoted in a way that is not misleading, and fully informs the community it is targeted at about the risks associated with the investment, as well as the potential financial and social returns. Establishing and maintaining public confidence in community investment is vital. Experience has shown that many people are willing to accept a limited financial return where the social returns on the investment are clear and strong.

Unlike private investment opportunities, which are based on the principle of maximising financial returns, community investment is based on the principle of aligning social and commercial objectives. This dual focus on social and commercial objectives is recognised and supported by legislation governing community interest companies (CICs) and industrial and provident societies (IPSs). Both bodies of legislation place limitations on the financial return on investment, but differ in the provisions covering the amount that can be invested, the membership rights of investors, and the objects of the enterprise.

The Financial Services and Markets Act 2000 sets out the legal and regulatory requirements covering the offer of securities, including shares and bonds, for sale to the general public. Complying with these regulations can be relatively expensive if the amount of capital being raised is less than £1m. In recognition of this, and the fact that not all financial promotions are driven by profit-maximising motives, the Act identifies a series of "exempt offers" which are exempt from having to comply with the regulations.

4.2 Exempt offers

The Financial Services and Markets Act 2000 sets out the legal and regulatory requirements covering the offer of securities, including shares and bonds, for sale to the general public. It also describes what it calls "exempt offers" which are exempted from these regulatory requirements. Some categories of exempt offers are relevant to community investment; most notably:

> **Offers to limited numbers**: Defined as offers made to fewer than 50 people. However, most community investment offers will be targeted at communities of more than 50 people, so this exemption will rarely apply.
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> **Clubs and associations**: Where the offer is made exclusively to members of a club or association, where the members can be regarded as having a shared interest and say in what can be done with the proceeds of the offer. This could apply to community investment offers which are restricted to the membership of an existing community club or association.
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> **Maximum consideration**: Exemption is given if the total amount being sought is less than the sterling equivalent of €40,000 in any twelve month period. This could provide exemption for some very small community investment initiatives.
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> **Charities**: Registered charities are exempt when offering securities, which for other reasons must be bonds or some other type of loan agreement.
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> **Industrial and Provident Societies**: The exemptions apply specifically to IPS community benefit societies. Other legal provisions mean that the offer of withdrawable share capital in any type of IPS is not considered to be a controlled investment. These exemptions do not apply to IPS co-operatives issuing transferable share capital.

4.3 Regulation of financial promotions

Unless an offer is exempt (see above), any corporate body offering shares or bonds for sale to the public is engaging in a regulated activity, requiring the organisation to use the services of an FSA approved person. The role of this person is to approve all the financial promotions leading up to an investment. The Financial Promotion Order 2005 exempts IPSs offering bonds, and places

IPS withdrawable share capital outside the scope of what constitutes a controlled investment.

The Financial Services and Markets Act 2000 also prohibits transferable shares being offered to the public without an approved prospectus. If the promotion is seeking to raise more than the equivalent of €100,000 or is made to more than 100 people, the organisation is required to publish a prospectus authorised by the FSA. However, the Prospectus Regulations 2005 provides exemption for IPS community benefit societies (but not co-operative societies) issuing transferable share capital.

Investors in financial promotions that are communicated or approved by firms authorised by the FSA have two important rights: they can make complaints to the Financial Ombudsman Scheme, and they may be eligible for compensation from the Financial Services Compensation Scheme. Investors in exempt promotions do not have these rights.