

## Chapter 3A

# Shares, deposits and borrowing



## 3A.5 Requirements on the retail distribution and financial promotion of capital instruments

### Application

- 3A.5.1** **R** (1) The requirements in this section apply:
- (a) (excluding the requirements in ■ CREDS 3A.5.6R and ■ CREDS 3A.5.7R) to a *firm* when *dealing* in or *arranging* a deal in a *deferred share* with or for a *relevant credit union client* where the *relevant credit union client* is to enter into the *deal* as buyer; and
  - (b) (excluding the requirements in ■ CREDS 3A.5.3R to ■ CREDS 3A.5.5R) to a *firm* when:
    - (i) *communicating a direct offer financial promotion* relating to *credit union subordinated debt* to a *relevant credit union client*; or
    - (ii) *approving a direct offer financial promotion* relating to *credit union subordinated debt* for *communication* to a *relevant credit union client*.
- (2) The requirements in this section do not apply if the *deal* relates to the trading of a *deferred share* or *credit union subordinated debt* in the secondary market.
- (3) The requirements in this section, other than ■ CREDS 3A.5.8R, ■ CREDS 3A.5.9R and ■ CREDS 3A.5.10R, do not apply if the *firm* has taken reasonable steps to ensure that the *relevant credit union client* is a *certified high net worth investor*, a *certified sophisticated investor* or a *self-certified sophisticated investor* in accordance with ■ COBS 22.2.4R, as adapted by ■ CREDS 3A.5.8R for the purposes of this section.

**3A.5.2** **G** The effect of ■ CREDS 3A.5.1R(1)(a) is that the requirements of this section apply to a *credit union* where it is *dealing* in its own *deferred shares*.

### Statements requirement relating to the retail distribution of deferred shares

- 3A.5.3** **R** (1) The *firm* must:
- (a) give the *relevant credit union client* a risk warning in the form in (2) on paper or another *durable medium*; and

(b) obtain confirmation in writing from the *relevant credit union client* that the *relevant credit union client* has read it, in good time before the *relevant credit union client* has committed to buy the *deferred share*.

- (2) "The investment to which this communication relates is a deferred share. Direct investment in deferred shares can be high risk and is very different to investment in deposit accounts or other savings products. In particular, you should note that:
- (a) the entire amount you pay for the deferred share is at risk;
  - (b) the sum you pay is only repayable to you in limited circumstances, specifically if:
    - (i) the credit union has obtained specific regulatory permission to make the repayment; or
    - (ii) the credit union is wound up, and there are funds remaining after all creditors, including savers and holders of subordinated debt, have been repaid;
  - (c) the sum you pay for deferred shares is not covered by the Financial Services Compensation Scheme;
  - (d) a deferred share may only be sold to a member of the same credit union and may be difficult to sell on; and
  - (e) investing more than 10% of your savings or net investment portfolio in deferred shares issued by a credit union, credit union subordinated debt and mutual society shares is unlikely to be in your best interests."

**3A.5.4**

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- (1) The *firm* must:
- (a) give the *relevant credit union client* a statement in the form in (2) on paper or another *durable medium*; and
  - (b) obtain confirmation in writing from the *relevant credit union client* that the *relevant credit union client* has signed it, in good time before the *relevant credit union client* has committed to buy the *deferred share*.
- (2) "I make this statement in connection with my proposed investment in deferred shares issued by a credit union. I have been made aware that investing more than 10% of my net assets in deferred shares issued by a credit union, credit union subordinated debt and mutual society shares is unlikely to be in my best interests. I declare that the proposed investment would not result in more than 10% of my net assets being invested in deferred shares issued by a credit union, credit union subordinated debt and mutual society shares. Net assets for these purposes mean my financial assets after deduction of any debts I have. My debts for these purposes do not include the outstanding balance of any mortgage I have on my home, unless this is more than the current value of my home, in which case the debts include the amount above the current value. My financial assets for these purposes do not include:
- (a) the property which is my primary residence or any money raised through a loan secured on that property;

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- (b) any rights of mine under a contract of insurance; or
- (c) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are) or may be entitled.

I accept that the investment to which this statement relates will expose me to a significant risk of losing all the money invested.

Signature:

Date: "

- (3) The requirement in (1) to give a *relevant credit union client* the statement, and to obtain written confirmation that the statement has been signed, applies only where the *relevant credit union client*:
  - (a) is an individual; and
  - (b) is not receiving advice that constitutes a *regulated activity* on the *deferred share*.

**Assessing the appropriateness of an investment in deferred shares**

3A.5.5

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If the *relevant credit union client* is not receiving advice that constitutes a *regulated activity* on the *deferred share*, the *firm* must assess whether investment in the *deferred share* is appropriate for the *relevant credit union client*, complying with the requirements in ■ COBS 10 as if the *firm* were providing non-advised *investment services* in the course of *MiFID* or *equivalent third country business*.

**Statements requirement in the case of a direct offer financial promotion relating to subordinated debt**

3A.5.6

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- (1) The *firm* must:
  - (a) include a risk warning in the form in (2) for any *direct offer financial promotion* to a *relevant credit union client* relating to *credit union subordinated debt*; and
  - (b) obtain confirmation in writing from the *relevant credit union client* that the *relevant credit union client* has read the risk warning,

in good time before the *relevant credit union client* makes the subordinated loan to the *credit union*.
- (2) "The investment to which this financial promotion relates is credit union subordinated debt. Making a subordinated loan to a credit union can be high risk and is very different to investment in deposit accounts or other savings products. In particular you should note that:
  - (a) the entire amount you lend is at risk;
  - (b) the loan will not be repaid to you until at least five years from the date on which you lend the amount to the credit union;
  - (c) if the credit union is wound up the sum you lend is only repayable to you if there are funds remaining after all creditors (excluding holders of deferred shares) have been repaid;

- (d) the entire amount you lend is not covered by the Financial Services Compensation Scheme;
- (e) to the fullest extent possible, you will be required to waive any right to set off any amount you owe to the credit union against any amount the credit union owes to you under the subordinated loan; and
- (f) investing more than 10% of your savings or net investment portfolio in credit union subordinated debt, deferred shares issued by a credit union and mutual society shares is unlikely to be in your best interests."

**3A.5.7**

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- (1) The *firm* must:
  - (a) include a statement in the form in (2) in any *direct offer financial promotion* to a *relevant credit union client* relating to *credit union subordinated debt*; and
  - (b) obtain confirmation in writing from the *relevant credit union client* that the *relevant credit union client* has signed the statement,
 

in good time before the *relevant credit union client* makes the subordinated loan to the *credit union*.
  
- (2) "I make this statement in connection with my proposed making of a subordinated loan to a credit union. I have been made aware that investing more than 10% of my net assets in credit union subordinated debt, deferred shares issued by a credit union and mutual society shares is unlikely to be in my best interests. I declare that the proposed investment would not result in more than 10% of my net assets being invested in credit union subordinated debt, deferred shares issued by a credit union and mutual society shares. Net assets for these purposes mean my financial assets after deduction of any debts I have. My debts for these purposes do not include the outstanding balance of any mortgage I have on my home, unless this is more than the current value of my home, in which case the debts include the amount above the current value. My financial assets for these purposes do not include:
  - (a) the property which is my primary residence or any money raised through a loan secured on that property;
  - (b) any rights of mine under a contract of insurance; or
  - (c) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are) or may be entitled.

I accept that the investment to which this statement relates will expose me to a significant risk of losing all the money invested.

Signature:

Date: "
  
- (3) The requirement in (1) to include the statement in a *direct offer financial promotion*, and to obtain written confirmation that the statement has been signed, applies only where the *relevant credit union client*:

- (a) is an individual; and
- (b) is not receiving advice that constitutes a *regulated activity* on the *credit union subordinated debt*.

**Application of exemptions in COBS 22.2.4R**

3A.5.8

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- (1) Where a *firm* applies any exemption set out in ■ COBS 22.2.4R under ■ CREDS 3A.5.1R(3), any reference in ■ COBS 22.2.4R to *mutual society share* must be read as though it includes a *deferred share* or *credit union subordinated debt*, as applicable.
- (2) For the purposes of any assessments or certifications required by the exemptions in ■ COBS 22.2.4R, as applied for the purposes of this section under ■ CREDS 3A.5.1R(3), any reference in ■ COBS 4.12 provisions to *non-mainstream pooled investments* must be read as though it is a reference to *deferred shares* or *credit union subordinated debt*, as applicable.
- (3) If the *firm* is relying on the exemptions for *certified high net worth investors*, *certified sophisticated investors* or *self-certified sophisticated investors* to comply with this section, the statement the investor must sign should have any reference to *non-mainstream pooled investments* replaced with a reference to *deferred shares* or *credit union subordinated debt*, as applicable.
- (4) The *firm* must give the *relevant credit union client* a written copy of any risk warning or statement that the *relevant credit union client* has been asked to sign for the purposes of compliance with this section.

3A.5.9

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■ COBS 22.2.4R contains the requirements that must be met before an individual can be exempted from the requirements of this section as a *certified high net worth investor*, a *certificated sophisticated investor*, or a *self-certified sophisticated investor*.

**Record keeping**

3A.5.10

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A *firm* which carries on an activity which is subject to this section must comply with the following record-keeping and disclosure requirements:

- (1) the *firm* must make a record at or near the time of the activity certifying it complies with the requirements set out in this section;
- (2) the record in (1) must include information and evidence demonstrating compliance with each of the requirements in this section, as applicable;
- (3) if the requirements of this section did not apply because the *firm* relied on one of the exemptions, the record in (1) must include which exemption was relied on, together with the reason why the *firm* is satisfied that exemption applies;
- (4) where the *firm* relies on the *certified high net worth investor*, the *certified sophisticated investor* or the *self-certified sophisticated investor* exemption, the record required in (1) must include a copy of

the certificate or investor statement (as signed by the investor) and of the warnings or indications required by the exemption; and

(5) the *firm* must retain the record required in (1) for three years.

**Electronic documents**

**3A.5.11** **G**

In this section:

- (1) any requirement that a document is signed may be satisfied by an electronic signature or electronic evidence of assent; and
- (2) any references to writing should be construed in accordance with **■ GEN 2.2.14R** and its related *guidance* provisions.

**Responsibility of the credit union**

**3A.5.12** **R**

Where the requirements of this section apply to a *firm* other than the *credit union* that issues the *deferred shares* or receives the *credit union subordinated debt*, the *credit union* must ensure that the *firm* complies with the requirements of this section.