Overview

Regulations published this month, will from October 2010, change the liability under English law of companies for information they publish to the market. Where a company has securities traded in the UK or its home state is the UK, the Regulations will:

- extend the existing statutory liability regime (for fraud and recklessness) to cover all information published via a RIS (currently just financial reports);
- create new liability for dishonest delay in disclosing information;
- extend the liability so that it is owed to persons who hold or sell securities in reliance on misleading information (currently liability is only to buyers of securities); and
- exclude all other liability under English law for information published or announced to the market, subject to a limited number of exceptions.

The Regulations thus limit when issuers or their directors can be sued for negligent errors or omissions in market announcements. The higher standard, requiring knowledge, dishonesty or recklessness before liability can arise, is intended to help ensure good quality reporting which is not made over-defensive through fear of litigation.

Introduction

On 9 March 2010, HM Treasury published its response to its July 2008 consultation paper entitled “Extension of the Statutory Regime for Issuer Liability”, together with the final draft of The Financial Services and Markets Act 2000 (Liability of Issuers) Regulations 2010 (the “Regulations”), which propose to amend Section 90A of, and insert new Schedule 10A into, the Financial Services and Markets Act 2000 (the “FSMA”).

Section 90A of FSMA established a statutory civil liability regime for misleading statements in periodic disclosures to the market by issuers of securities admitted to trading on EEA regulated markets as required by

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1 The response to the consultation paper is available at: http://www.hm-treasury.gov.uk/d/consult_issuerliability_response.pdf
2 The consultation paper is available at: http://www.hm-treasury.gov.uk/d/issuerliability_170708.pdf
3 The Regulations are available at: http://www.hm-treasury.gov.uk/d/consult_issuerliability_regs080310.pdf

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Changes to the statutory regime for issuer liability

The Regulations will apply to information first published on or after 1 October 2010. The current version of Section 90A of the FSMA, as inserted by the Companies Act 2006, applies to information published before then. The changes follow the report by Professor Paul Davies QC published in June 2007.

Set out below is a summary of the key changes made by the Regulations.

**The Financial Services and Markets Act 2000 (Liability of Issuers) Regulations 2010**

The Regulations provide that an issuer of securities to which the regime applies is liable to pay compensation to a person who acquires, continues to hold or disposes of the securities in reliance on published information to which the regime applies and who suffers loss in respect of the securities as a result of either (i) any untrue or misleading statement in that published information, or (ii) the omission from that published information of any information required to be included in it.

**Basis of liability**

Fraud will remain the basis of liability. Liability will arise (i) where there is an untrue or misleading statement and a person discharging managerial responsibilities (a "PDMR") in the issuer knew of this fact, or was reckless as to its existence; and (ii) where there is an omission of information and a PDMR knew that the omission was a dishonest concealment of a material fact. For most issuers, the PDMRs will be the directors (and not any wider group of managers).

**Markets**

The new regime applies to all securities which, with the issuer's consent, are admitted to trading on a securities market where (i) that market is situated and operating in the UK, or (ii) the issuer's home State is the UK. For these purposes a "securities market" includes a regulated market (such as the Main Market of the London Stock Exchange), an MTF (such as the London Stock Exchange's Professional Securities Market, AIM and the PLUS-quoted market) or an equivalent market or facility outside the EEA. In particular, the new regime has the potential to apply extra-territorially, for example where a UK issuer has securities admitted to trading on a US market.

**Securities**

The regime is extended to transferable securities as defined in Section 102A(3) of the FSMA. Liability attaches solely to the issuer of those securities.

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4 The report is available at: [http://www.hm-treasury.gov.uk/d/davies_review_finalreport_040607.pdf](http://www.hm-treasury.gov.uk/d/davies_review_finalreport_040607.pdf)

5 Paragraph 3(1) of the Schedule to the Regulations.

6 As defined in paragraph 8(5) of the Schedule to the Regulations.

7 Paragraphs 3(2) and 3(3) of the Schedule to the Regulations.

8 See paragraph 1(2) of the Schedule to the Regulations.

9 An issuer's home State will be the UK if (i) the securities in question are subject to the Transparency Directive and the UK is the home State for the purposes of that directive; or (ii) the issuer has its registered office (or if none, its head office) in the UK. See paragraph 1(3) of the Schedule to the Regulations.

10 Paragraph 8(2) of the Schedule to the Regulations clarifies the identity of the issuer in respect of depositary receipts, derivative instruments or other secondary securities (together,
Disclosures
The Regulations cover a much broader range of disclosures than under the current regime. Paragraph 4 of the Schedule to the Regulations extends the regime to cover all information disclosed by “recognised means”. This broadly encompasses an RIS or other means of disclosure used to communicate information to the relevant market. It also includes other methods used when an RIS is unavailable. The person claiming damages would not have to show that the relevant information was actually obtained from the RIS, only that he or she suffered loss as a result of relying upon a fraudulent misstatement in that information.

The Regulations extend also to information which has been disclosed by a means other than recognised means, but where the availability of that information has been announced by recognised means. An example is where an issuer announces the publication of documents, such as its annual accounts, by RIS announcement - the Regulations extend the liability regime to the whole text of those documents.

Extension to sellers and holders of securities
The Regulations permit those who acquire, sell or continue to hold securities to recover losses incurred through reliance on fraudulent misstatements in information published by the issuer of the securities. This represents a significant extension to the current liability regime (under which only purchasers of securities may make such a claim). However, in practice, it may be difficult to prove that a decision to continue to hold securities was made in reliance on the issuer’s fraudulent misstatement.

Liability for dishonest delay
To encourage issuers to make prompt disclosures to the market, an issuer may be liable under the Regulations to a person who acquires, continues to hold or sells securities, and in doing so, suffers loss in respect of those securities as a result of a dishonest delay by the issuer in publishing the relevant information. The test for dishonesty in this context turns upon whether (i) the relevant PDMR’s conduct is regarded as dishonest by those persons who regularly trade in the relevant securities market, and (ii) the PDMR was aware that the conduct would be regarded as dishonest.

Limitation of liability
An important benefit of the regime created by Section 90A is that, as well as establishing when issuers will be liable, it excludes liability in other cases. The Regulations have a number of exceptions to this exclusion of liability. These include liability under Section 90 of FSMA (in respect of a misleading prospectus or listing particulars), civil liability for breach of contract, civil liability under the Misrepresentation Act 1967 and criminal liability.
exception is where liability arises “from a person’s having assumed responsibility, to a particular person for a particular purpose, for the accuracy or completeness of the information concerned”. This preserves the principles of the Caparo case\textsuperscript{16} that to be liable for negligent misstatement the defendant must have assumed responsibility to the claimant for the accuracy of the information. In other words, it prevents an investor claiming against the company for economic loss caused by misstatements arising from general governance rights, where no assumption of responsibility has been made.

Practical Implications for Issuers

Issuers should welcome the Regulations. They clarify the scope of liability and set the trigger high, requiring knowledge, recklessness or dishonest concealment rather than mere negligence.

The creation of a new liability to investors for delays in publishing information was a particular concern to issuers when it was proposed, on the basis that it could encourage speculative litigation and put undue pressure on them to make announcements in circumstances where delay is legitimate. However, for the issuer to be liable, there has to have been dishonesty on the part of a PDMR and this is a considerably higher threshold than the standard of care required under the Listing and Disclosure Rules, under which issuers and their directors can be fined for failure to announce material information promptly to the market.

Although directors may not have liability directly to investors under the new statutory liability regime, as a matter of English law, they may be liable to the issuer. Furthermore, there may be additional consequences for directors under other countries’ laws. For example, they may be liable as a result of being named in the responsibility statement if the issuer’s securities are traded on exchanges outside the UK. Finally, companies may wish to consider reviewing their insurance cover for directors and officers to reflect the new regime.

\textsuperscript{16} [1990] 1 All ER 568