

Reforming Corporate Retail Investor Protection

Regulating to Avert Mis-Selling

Diane Bugeja

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Breadth of Investor Protection Regulation

I. Why Regulate to Protect Retail Investors?

The history of financial services regulation has shown, albeit with the benefit of hindsight, that law and regulation are unlikely to evolve as rapidly as market practices and therefore swiftly become obsolete. This, together with the magnitude of investor detriment that has been registered in recent years, suggests that the need for more effective investor protection regulation has become ‘self-evident.’²

Both the common law and the regulatory framework for investment services are rooted in the neo-classical economic theory. This model is based on the assumption that investors act rationally such that, as long as they are supplied with accurate information, investors are presumed ‘willing and able to use it wisely.’³ Seen from this perspective, investor protection only becomes necessary where market failures arise, which failures are commonly attributed to information asymmetries such that disclosure is used as a central regulatory tool to support better decision-making and stronger market-based investing.⁴ The effectiveness of this approach, which is founded on the notion of *caveat emptor*,⁵ is dampened in the present climate marked due to the ever-increasing number of mis-selling scandals that have caused widespread investor detriment. Although regulators seem to

² Joseph Stiglitz, ‘Regulation and Failure’ in David Moss and John Cisternino (eds), *New Perspectives on Regulation* (The Tobin Project 2009) 22. The Parliamentary Commission on Banking Standards (PCBS) also commented on a ‘widespread appetite’ for measures to constrain the misconduct, complacency and recklessness that fuelled the past mis-selling incidents (PCBS, *Changing banking for good: Report of the Parliamentary Commission on Banking Standards, Volume I* (HL Paper 27-I, HC 175-I, 2013) 16).

³ Donald C Langevoort, ‘Selling Hope, Selling Risk: Some Lessons for Law from Behavioural Economics about Stockbrokers and Sophisticated Customers’ (1996) 84 *California Law Review* 627, 699.

⁴ European Securities and Markets Authority (ESMA), Opening statement of Steven Maijoor (ESMA Investor Day, Paris, 12 December 2012): www.esma.europa.eu/system/files/2012-_818.pdf, accessed 29 June 2015.

⁵ The doctrine of *caveat emptor* has its origin in the famous case of *Chandelor v Lopus* [1603] 79 ER 3 (KB). In its purest form, *caveat emptor* (‘let the buyer beware’) suggests that it is incumbent upon the buyer alone to assess the quality of a purchase (see further Patrick S Atiyah, *The Rise and Fall of Freedom of Contract* (Clarendon Press 1979) 178–79; Gerrit De Geest, ‘The Death of Caveat Emptor’ (2014) University of Chicago Law School, Law and Economics Workshop).

4 Breadth of Investor Protection Regulation

have acknowledged the need for more paternalistic interventionist tools, elements of *caveat emptor* are still evident in the UK's regulatory framework as well as in the deliberations of the English judiciary, particularly where certain categories of investors are concerned.

At a macroeconomic level, mis-selling poses a risk to financial stability and can have a de-stabilising effect on the balance sheets of investment firms, which in turn makes the economy prone to systemic risk.⁶ At a micro level, retail investors may also suffer from significant financial detriment. Indeed, since the pensions mis-selling scandal in the late 1980s, the UK has witnessed numerous incidences of investment products' mis-selling.⁷ These episodes have caused widespread investor detriment and have contributed towards driving the overhaul of the UK's regulatory system throughout the years. Amongst these reforms, one finds the abolition of the concept of self-regulation in the wake of structural changes that led to the establishment of the Financial Services Authority (FSA) in the late 1990s, and, subsequently, the restructuring of the FSA that resulted in the adoption of a 'twin peaks' model of regulation during 2013. The latter was implemented by the Financial Services Act 2012 (FSA 2012) and had the effect of splitting the then FSA into the FCA and the Prudential Regulatory Authority (PRA). The establishment of the FCA meant that investor protection concerns took on a more prominent role on the agenda of a regulator that focuses on conduct regulation and pursues objectives which include the protection of consumers and, therefore, retail investors.⁸ More recently, the increasing use of new interventionist tools by the FCA suggests that the regulatory mind-set that previously promoted *caveat emptor* is shifting towards a more paternalistic approach.

Reforms were also evident at an EU level to the MiFID regime,⁹ in response to the investor detriment caused by the global financial crisis as well as numerous other incidences of retail market detriment. These measures were dominated by

⁶ The financial crisis of 2007/08 has shown that certain financial products can be a destabilising factor and contribute significantly to global financial and economic instability when these are inappropriately sold to investors. This trend is also noted in mis-selling of payment protection insurance (PPI) and interest rate hedging products (IRHPs), with the latter being used as a case study. These cases have cost banks and building societies in the UK over £50 billion in fines and other penalties since 2000 (see further European Parliament, 'Consumer Protection Aspects of Financial Services' (2014); FCA, 'Annual Report and Accounts 2016/17' (2017)).

⁷ These include pensions; the marketing of home income plans or equity release mortgages to consumers considered to be vulnerable; endowment policies in the retail mortgage sector; 'with profits' life insurance products; PPI-related products; and IRHPs.

⁸ The FCA's consumer protection objective is set out under s 1C of the Financial Services and Markets Act 2000 (FSMA), as inserted by the FSA 2012. Whilst responsibility for conduct regulation rests with the FCA, the PRA's focus lies in addressing systemic and prudential regulatory concerns, including those related to financial stability, as set out in FSMA, s 2B and 2C, and as inserted by the FSA 2012.

⁹ The EU regime for the provision of investment services is set out in the MiFID framework, which is composed MiFID II (Directive 2014/65/EU, repealing the original MiFID I, Directive 2004/39/EC) and MiFIR (Regulation (EU) No 600/2014).

the introduction of regulatory reforms aimed at enhancing the safety of financial products as well as improving their transparency and accessibility.

Despite these regulatory reforms and the imposition of hefty penalties on the industry the familiar cycle of investment product mis-selling, massive investor detriment, and the problems of securing redress for corporate retail investors, has proved particularly hard to break. Rather than simply being reduced to ‘coincidental cocktail of circumstances’,¹⁰ these events can be described as classic characteristics of mis-selling driven by the complexities of regulation and the novelty surrounding certain intricate investment products. Further, these episodes also have one common fact at their core – the retail investor being sold a product that could place him at an actual or potential financial disadvantage primarily triggered by a mismatch between the product’s complexity and the investor’s financial acumen, circumstances, and risk appetite.

Investor protection, as one of the core objectives of investment services regulation, remains dominated by a ‘complex blend of statutory and non-statutory’¹¹ instruments, primarily inspired by reactions to major market events. These measures however do not fully address the disparities between investor protection frameworks applicable to different categories of retail investors (and which render corporate retail investors more vulnerable to registering financial losses as a result of mis-selling, in comparison to individual retail investors). Indeed, as also acknowledged by the FCA itself, these regulatory developments have come about as a ‘mechanistic response’¹² to scandals and crises, as regulators were more concerned with fighting fires rather than analysing the root causes giving rise to mis-selling. In consequence, the combination of opaque products, a competitive selling environment, and increasing retail investor participation in financial markets, remains an intractable challenge that requires the regulators’ attention and that has put to the test the robustness of past and present regulatory frameworks, particularly insofar as corporate retail investors are concerned.

Against this backdrop, the diverging treatment of different categories of retail investors emerges as one of the primary root causes of the mis-selling of complex investment products. Indeed, the position of corporate retail investors underlines a number of lacunae in the application of the investor protection framework to the needs and circumstances of this category of retail investors, as their exposure to the risk of mis-selling is further exacerbated by the principles underpinning the common law regime.

¹⁰ Julia Black and Richard Nobles, ‘Personal Pensions Misselling: The Causes and Lessons of Regulatory Failure’ (1998) 61 *The Modern Law Review* 789, 817.

¹¹ Julia Black, *Rules and Regulators* (Clarendon Press 1997) 46.

¹² FCA, ‘Building on experience’ Speech by Martin Wheatley (The future of financial services conference, Lansons, London 17 April 2013): www.fca.org.uk/news/speeches/building-experience, accessed 5 May 2015.

II. Categorising Retail Investors

A. Individual v Corporate Retail Investors

A ‘retail’ investor’ is defined in MiFID II by opposition to, or exclusion of, a ‘professional investor’.¹³ For the purposes of this definition, retail investors include both natural persons (what this book terms ‘individual retail investors’) as well as corporate entities (referred to in this book as ‘corporate retail investors’), unless these fall within the de facto definition of ‘professional’ investor,¹⁴ or otherwise request to waive some of the protections afforded by the conduct of business rules by electing to be treated as professional investors subject to meeting certain criteria (known as ‘elective professional investors’).¹⁵

Professional investors typically include institutional investors whose main activity is to invest in financial instruments, as well as large undertakings meeting specific size requirements. The size-based thresholds set out in the MiFID definition of ‘professional investors’ are lower than those set out in the Commission’s definition of micro, small and medium-sized enterprises (SMEs),¹⁶ meaning that corporate entities that do not meet the thresholds attached to the ‘professional investor’ definition under MiFID are small, unsophisticated entities that are presumed to have the same (relatively low) level of financial acumen and sophistication, that generally lack access to financial and professional resources, and that do not engage in complex investment transactions on a regular and habitual basis.

It is pertinent to note that, prior to the MiFID regime coming into force in the UK on 1 November 2007,¹⁷ UK investors were categorised in a different manner. The client classification provisions in the then FSA’s Conduct of Business Sourcebook (COB)¹⁸ provided for three categories of clients, being private customers, intermediate customers, and market counterparties. Private customers included the least sophisticated investors who were accordingly entitled to the greatest degree of regulatory protection; intermediate customers comprised the more experienced investors generally having either appropriate expertise in-house or the means to

¹³ MiFID II, Art 4(1). This definition replicates the MiFID I definition and is also mirrored in the definition of ‘retail’ client set out in the FCA Handbook Glossary.

¹⁴ As defined under MiFID II, Annex II, Section I.

¹⁵ As prescribed by MiFID II, Annex II, Section II.

¹⁶ The EU definition of ‘SME’ is set out in European Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, and has been replicated in ss 382 and 465 of the UK Companies Act 2006. The definition adopts upper-most thresholds for balance sheet total and net turnover of €43,000,000 and €50,000,000 respectively. The related MiFID thresholds tied to the ‘professional’ investor definition are of €20,000,000 and €40,000,000 respectively. As a third test to these definitions, MiFID uses the ‘own funds’ amount, whereas the European Commission Recommendation uses ‘staff headcount’ and hence this third limb is not directly comparable.

¹⁷ In the UK, MiFID was implemented through the Conduct of Business Sourcebook (COBS).

¹⁸ COB 4.1.

pay for professional advice when needed;¹⁹ and market counterparties included those investors who were experienced in financial products and markets (and hence sufficiently sophisticated to operate within a ‘light-touch’ regime without the application of most regulatory protections) as well as authorised counterparties operating within the inter-professional regime. Once the MiFID classification took effect, private customers were generally grandfathered to the retail category under MiFID; intermediate customers were classified as either retail or professional clients depending on the applicable quantitative thresholds; and market counterparties were mapped onto the eligible counterparty category under MiFID²⁰ (with some being classified as professional clients in certain circumstances).

B. Uneven Retail Investor Protection

It has been established that the MiFID regime only distinguishes between the broad categories of ‘retail’ investors and ‘professional’ investors and does not provide for more granular sub-divisions within the ‘retail’ category itself. Any investor falling within the definition of ‘retail’ investor is hence entitled to the same level of protection irrespective of whether the investor is an individual or a corporate. Yet, the protection extended to the corporate sub-set of retail investors through the MiFID regime is diluted by domestic UK legislation that exists alongside the MiFID framework and which has a restricted scope that operates to the exclusion of corporate retail investors.

When individual retail investors purchase investment products, they enjoy certain rights and protections under the UK general consumer protection legislation and also under financial services-specific regulation, which are designed to help these investors make investment decisions without fear of exploitation or misrepresentation. The level of protection that corporate retail investors are entitled to is generally significantly lower, amidst a prevailing *caveat emptor* culture reflective of the view that corporate entities ought to be in a position to look after their own interests, which view is evidently shared by English courts. As a result, relatively small businesses falling within the definition of ‘retail’ investor under MiFID are treated no differently from larger businesses classified as ‘professional’

¹⁹ Body corporates which had called-up share capital or net assets of at least £5 million qualified as an ‘intermediate customer’.

²⁰ According to MiFID II, Art 30(2) eligible counterparties include investment firms, credit institutions, insurance companies, Undertakings for the Collective Investment in Transferable Securities (UCITS) and their management companies, pension funds and their management companies, other financial institutions authorised or regulated under EU law or under the national law of a Member State, national governments and their corresponding offices including public bodies that deal with public debt at national level, central banks, and supranational organisations. In addition to these categories, Art 71 of the European Commission Delegated Regulation supplementing Directive 2014/65/EU of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive (C(2016) 2398 final) (MiFID II Delegated Regulation), allows for certain specific professional clients to be re-categorised as eligible counterparties, subject to these investors fulfilling specific criteria.

investors, such that corporate retail investors do not have recourse to the domestic protection mechanisms that individual retail investors are entitled to and hence receive substantially less protection in comparison to individual retail investors.

Where the transaction relates to complex investment products, the vulnerable position of corporate retail investors becomes even more precarious.²¹ Numerous episodes of mis-selling suggest that these products are increasingly being marketed to retail investors, and the market for these types of products is likely to continue to grow unless measures are taken to contain their proliferation. Complex investment products typically present a convoluted interaction of risks, costs and expected returns with a high probability of causing detriment to retail investors, be they natural persons or corporate entities, in view of their limited financial acumen and experience. Faced with an infinite number of variations of complex investment products, often designed to intensify the obscurity of these products, corporate retail investors are likely to struggle to understand their intricate features and must place reliance on the judgement of investment firms, such that the choice of product is, in reality, made by the latter.²² Therefore, even though additional responsibilities for the assessment of appropriateness or suitability of the product for the retail investor are incumbent upon the investment firm when marketing and selling complex investment products, the importance of more robust investor protection measures especially for corporate retail investors lacking access to alternative redress avenues should not be under-estimated.

III. The IRHPs Mis-selling Scandal

IRHPs are one example of a complex investment product, the purpose of which is purportedly to enable the customer to manage fluctuations in interest rates. These products can be grouped into four broad categories: swaps (allow for a 'fix' in the interest rate); caps (place a limit on any interest rate rises); collars (enable interest rate fluctuations to be limited to a simple range); and structured collars (enable interest rate fluctuations to be limited to a specified range but involve arrangements where, if the reference rate falls below the bottom of the range, the interest rate payable by the investor may increase above the bottom of the range).²³ IRHPs were typically sold separate to, but as a pre-condition of, a loan, with the

²¹ The term 'complex' is not specifically defined in the investment services regulatory regime, however ESMA has provided guidance on the characteristics that investment products typically exhibit when considered as 'complex' (see further: ESMA, 'Opinion: MiFID practices for firms selling complex products' ESMA/2014/146 (2014) 2–3; ESMA, 'Guidelines on complex debt instruments and structured deposits' ESMA/2015/1787 (2016); see also MiFID II Delegated Regulation, Art 57, which lists the criteria that must be satisfied in order for financial instruments to be considered as 'non-complex' in terms of MiFID II, Art 25(4)).

²² Kit Jebens, *LAUTRO: A Pioneer Regulator 1986 to 1994* (C E Jebens 1997) 25–26.

²³ As defined by the FCA (see further www.fca.org.uk/consumers/interest-rate-hedging-products/background-review, accessed 22 October 2016).

objective of enabling the investor to manage future fluctuations in interest rates in connection with the said loan. In this sense, they were marketed as a risk mitigation tool to protect investors against loan interest rate movements.²⁴

IRHPs may therefore be appropriate when properly sold in the right circumstances. Due to their complex nature, however, they require a very finely balanced judgement on the part of the investor and the investment firm as they introduce a degree of interest rate speculation, such that an investor risks paying more in interest if base rates fall below an agreed level. Claims alleging the mis-selling of IRHPs in the UK surfaced during 2012, when it appeared that, since 2001, many corporate retail investors had been mis-sold complex IRHPs by banks (acting in their capacity as investment firms).

Using the 'rising market' as a coercive sales tactic, these products were promoted as protecting corporate retail investors from rising interest rates, since a standalone IRHP creates a separate set of payments to and from the business that aims to offset the variability of the interest rate paid on the underlying loan; allegedly, however, without providing a full explanation of associated risks, particularly in the case of a potential dip in interest rates. Thus, when interest rates plunged in the wake of the global financial crisis, most corporate retail investors that had been coerced into investing in IRHPs ended up paying significantly more in interest than they had originally envisaged. These changes in the economic climate were exacerbated by the complexity of IRHPs, which made them susceptible to mis-selling. It later emerged that investment firms consistently failed to ascertain the investors' understanding of risk, whilst it also became evident that corporate retail investors were advised to engage in IRHP transactions without investment firms taking contractual responsibility for their advice. Hence, although IRHPs may have appeared attractive to borrowers in fixing or limiting interest rate fluctuations within a certain range, their sheer complexity meant that the overall impact was difficult to assess, thereby creating unexpected adverse effects for investors.²⁵ In particular, the widespread sale of IRHPs, coupled with their intricate complexities, meant that a product which was traditionally offered to wholesale market participants was extensively distributed to less experienced investors with largely conservative risk profiles. Against this backdrop, an increasing number of corporate retail investors brought claims against investment firms (the majority of which were also credit institutions) alleging the mis-selling of IRHPs, as a result of which they purportedly suffered considerable financial losses.

The mis-selling of IRHPs is a particularly relevant case because it allows for an analysis of the redress opportunities that corporate retail investors have sought to draw upon with limited success and hence brings to the fore the legal and regulatory obstacles that prevent corporate retail investors from securing adequate compensation. The circumstances surrounding the mis-selling of IRHPs expose

²⁴ FSA, 'Interest rate hedging products: Information about our work and findings' (2013) 1.

²⁵ Rodrigo Momberg, 'Beyond the Risk: Swaps, Financial Crisis and Change of Circumstances; Comparative Case Note: Supreme Court of Portugal – 10.10.2013' (2015) 23 *European Review of Private Law* 81, 81.

evident gaps in the UK's corporate retail investor protection framework and provide a practical dimension to the more abstract and theoretical discussions on mis-selling and investor protection.

IV. The Case for Reform

It is acknowledged that the 'regulatory blindness'²⁶ which has generally exacerbated the factors giving rise to mis-selling is slowly being addressed through a number of regulatory reforms. Yet, the regulatory responses to date are insufficient and generally ineffective, particularly since they are largely short-term in nature and only targeted at a limited category of retail investors (namely individuals), whilst neglecting other equally vulnerable retail investors (including corporate retail investors). Historically, such reforms have been largely piecemeal and *ad hoc*, and have generally been triggered in reaction to crises, scandals and political pressure. Moreover, regulators seem to have been keen to strengthen governance, disclosure, and enforcement stages of the interactions between investment firms and their clients,²⁷ whilst little has been done to enhance the regulatory framework around the middle tier of the product development and distribution chain, that is, the verbal communications and contractual arrangements between the investment firm and the corporate retail investor purchasing the complex investment product, hence remaining an under-regulated area which presents a breathing space for mis-selling.

The assumption of investor rationality has 'the virtue of a myth',²⁸ given that numerous behavioural biases undermine the effectiveness of the investment decisions taken by corporate retail investors and their ability to digest the relevant information. This means that the effectiveness of traditional regulatory tools, such as risk disclosures, is undermined by the risk of information overload and other factors, including biases, which affect the investment decisions of these investors. Such conventional tools are unlikely to overcome biases and competence failures on the part of retail investors and should hence not be envisaged as the panacea for investor protection.²⁹ Similarly, financial capability initiatives are unlikely to have

²⁶ Julia Black and Richard Nobles, 'Personal Pensions Misselling: The Causes and Lessons of Regulatory Failure' (1998) 61 *The Modern Law Review* 789, 789.

²⁷ MiFID II has introduced measures around product approval processes (MiFID II, Art 16(3) and Art 24(2)) as well as involvement and accountability of the management body of investment firms (MiFID II, Art 9). Disclosures have also been enhanced including as a result of the PRIIPs Regulation (Regulation (EU) No 1286/2014).

²⁸ Donald C Langevoort, 'Selling Hope, Selling Risk: Some Lessons for Law from Behavioural Economics about Stockbrokers and Sophisticated Customers' (1996) 84 *California Law Review* 627, 699.

²⁹ See eg FSA, 'Consumer Research 5: Informed Decisions? How Consumers use Key Features: a synthesis of research on the use of product information at the point of sale' (2000); Joanna Gray and Jenny Hamilton, *Implementing Financial Regulation: Theory and Practice* (John Wiley & Sons Ltd 2006) 212; FSA, 'Discussion Paper DP07/01, A Review of Retail Distribution' (2007); Niamh Moloney, *How to Protect Investors: Lessons from the EC and the UK* (Cambridge University Press, 2010) 292; Daniel Kahneman, *Thinking Fast and Slow* (Penguin Books Ltd, 2011); Commonwealth of Australia Financial System Inquiry, 'Final Report' (2014) 9.

major lasting effects on retail investors' knowledge and behaviour, and hence should not substitute tougher regulatory interventions.³⁰ In other words, traditional 'softer' approaches to regulation need to be reinforced through more interventionist tools, which are more effective in 'nudging'³¹ corporate retail investors towards investment products and services that are best suited to their needs and circumstances.

Notably, the behavioural biases that the regulator has attributed to individual retail investors are equally experienced by corporate retail investors. In light of these behavioural limitations, corporate retail investors should not be treated in the same way as sophisticated contractual parties of equal bargaining power to investment firms simply because they are acting in a business context and irrespective of their circumstances, size, knowledge and experience, as seems to be implied by the regulator and by the English courts. Rather, a distinction between non-financial services corporate entities that invest, say, to hedge risk (that would typically fall within the definition of 'retail' in terms of MiFID), and larger institutional corporate entities that may be transacting on behalf of their clients (which would generally be categorised as 'professional' for the purposes of MiFID) is promoted based on the MiFID classification. In consonance with the spirit of MiFID, corporate investors are viewed as residing on a spectrum – while corporate professional investors may have sufficient experience and access to expertise (hence justifying a lower degree of regulatory protection), smaller businesses falling within the 'retail' category of MiFID have more in common with individual investors by virtue of their MiFID 'retail' classification and should hence qualify for the same level of regulatory protection to which individual retail investors are entitled; in other words, the principle of *caveat emptor* should not dictate the level of protection offered to corporate retail investors.

Whilst the FCA acknowledged the need to assess the extent to which corporate retail investors should benefit from the investor protection measures afforded to individual retail investors as well as the extent to which these investors should be expected to behave like larger, more sophisticated businesses,³² there has generally been little debate over how the domestic investor protection regime operates to secure an appropriate level of protection to all retail investors, and whether any category of retail investors is being impeded from obtaining adequate redress by

³⁰ David T Llewellyn, 'Regulation of Retail Investment Services' (1995) 15 *Economic Affairs* 12, 14; OECD, 'Improving Financial Literacy: Analysis of Issues and Policy' (2005); OECD, 'Recommendation of Principles and Good Practices for Financial Education and Awareness' (2005); FSA, 'Financial capability in the UK: Delivering change' (2006); FSA, 'Consumer Research Paper 69, Financial Capability, A Behavioural Economics Perspective' (2008) 2; Parliamentary Joint Committee on Corporations and Financial Services, 'Inquiry into financial products and services in Australia' (2009); World Bank, 'Policy Research Working Paper, Consumer Protection and Financial Literacy: Lessons From Nine Country Studies' (2010).

³¹ A 'nudge' is defined by Sunstein and Thaler as 'an aspect of choice architecture that alters people's behaviour in a predictable way without forbidding any options or significantly changing their economic incentives' (Cass Sunstein and Richard Thaler, *Nudge: Improving Decisions About Health, Wealth and Happiness* (Penguin Books, 2008) 6).

³² Treasury Committee, *Conduct and competition in SME lending: Written Evidence* (17 June 2014) FCA Written submission SME0140.

national legislation which operates in parallel to the broader regulatory framework, or is otherwise hampered from securing compensation by the interpretation of the UK judiciary of such domestic statutes. To this end, this book challenges the presumption that corporate retail investors are more sophisticated than individual retail investors and therefore less in need of protection and sets out to demonstrate that corporate retail investors not only display vulnerabilities and limitations but also face restrictions in terms of inadequate redress options which cause them extensive detriment, thereby justifying the need for the establishment of suitable safeguards targeted at protecting these investors.

V. Brexit Considerations

On 23 June 2016, the UK voted to exit the European Union (EU) – ‘BREXIT’ – and, on 29 March 2017, Article 50 of the Treaty on European Union was triggered.

The UK’s decision to exit the EU is not believed to impact the ongoing implementation of the EU MiFID regime, not least because MiFID II is based, in part, on the G20 commitments and reform agenda stemming from the financial crisis to which the UK, as a G20 member, is committed.³³ The UK, as a member of the G20, opted to tackle these reforms by adopting a European-wide policy (instead of acting in isolation) – a decision which is highly likely to be upheld post-BREXIT.

Furthermore, BREXIT is not likely to lead to a deviation from the standards and obligations imposed by the MiFID II regime since, for the investment services industry to continue doing business in the EU after BREXIT, it will need ‘equivalency’ of regulation. This can be achieved by implementing MiFID II-like regulation in the UK, with equivalent surveillance, investor protection, and enforcement mechanisms. More importantly, the European Union (Withdrawal) Act 2018 converts existing direct EU legislation into UK law, and preserve existing UK laws which implement EU obligations. The UK Government has also been given powers to amend this retained EU legislation so that it works effectively when the UK leaves the EU. The government’s intention is that the same rules and laws will apply after exit as before, as far as possible. As part of this process, the FCA will amend and maintain EU binding technical standards, as well as amend the FCA Handbook to ensure it is consistent with changes the government is making to EU law. All in all, therefore, close correspondence of UK and EU financial services regulation will be maintained, such that there is no reason to believe that the observations, conclusions, and recommendations made and presented in this book will no longer be relevant once the UK exits the EU or once the transitional period terminates.

³³ See eg European Commission, ‘More transparent and safer financial markets: European Commission welcomes European Parliament vote on updated rules for Markets in Financial Instruments (MiFID II)’ Statement 14/129 (2014); Bloomberg, ‘MiFID still happens with “Brexit”’ (2016); Weston, ‘Brexit: What Does This Mean for MiFID II’ (2016).