Feature

KEY POINTS

- Although s 90A is potentially a valuable remedy for investors who have suffered loss as a result of false statements to the market, for example, in the context of high-profile scandals such as Tesco, BT, Carillion and Patisserie Valerie, there have been no reported or unreported decisions under s 90A since it was first enacted more than twelve years ago.
- There are a number of potential reasons for this underutilisation of s 90A, including the challenges for prospective claimants in assessing the merits of a claim (given that much of the relevant evidence will be in the hands of the prospective defendant), the availability of other remedies, and concerns about the solvency of the prospective defendant.
- The lack of judicial decisions on s 90A mean that there remains considerable uncertainty about the meaning and operation of certain aspects of that provision. This uncertainty may be a further reason why s 90A remains such a little used remedy.

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Claims under s 90A of FSMA for dishonest statements made to the market: an underutilised remedy?

This article explores a number of the key concepts that underpin s 90A of the Financial Services and Markets Act 2000 (FSMA) and will consider why it remains such a little used remedy.

All companies with securities traded on a UK securities market are required to make a number of disclosures to the market each year. The Companies Act 2006 (ss 395-396) requires the production of *annual* accounts; the obligation to produce *interim* accounts is derived from the Transparency Directive (EC Directive 2004/109, Arts 5-6); and the obligation to report to the market on a *continuing* basis, eg in relation to inside information, is derived from the Market Abuse Directive (EC Directive 2003/6, Art 6). The prompt and fair disclosure of information to the public enhances consumer protection and market efficiency which are core objectives of these Directives (implemented in the UK via the introduction of the 'Disclosure and Transparency Rules' (DTR) chapter to the FCA Handbook); whereas selective and inaccurate disclosures by securities issuers lead to a loss of investor confidence in the integrity of the financial markets and inefficient decisions by those active in the market.

A number of scandals in recent times have been centred on allegations of false reporting to the market: the Tesco £250m accounting error in 2014, the BT £225m accounting error in 2017, the Petrofac bribery controversy in 2017, allegations of misleading financial reporting by Carillion in the years and months leading to its collapse in 2017, and the Patisserie Valerie £40m accounting error in 2018.

Investors claiming to have suffered loss as a result of such false reporting may seek to take advantage of s 90A of FSMA, a deceit-based statutory cause of action which offers the fraud measure of damages, and thereby allows a successful claimant to seek damages for losses arising from market movements which are unrelated to the false reporting.

However, there have been no reported or unreported decisions in England and Wales under s 90A since it was first enacted in 2006. This article will explore a number of the key concepts that underpin s 90A and will consider why it remains such a little used remedy.

SECTION 90A FSMA

Section 90A provides as follows:

> "Schedule 10A makes provision about the liability of issuers of securities to pay compensation to persons who have suffered loss as a result of –
>
> - A misleading statement or dishonest omission in certain published information relating to the securities; or
> - A dishonest delay in publishing such information."

Initially introduced on 8 November 2006 by s 1270 of the Companies Act 2006, s 90A was substantially revised following the *Davies Review of Issuer Liability* (March 2007) by Professor Paul Davies QC. The current iteration of the provision was introduced on 1 October 2010 by the Financial Services and Markets Act 2000 (Liability of Issuers) Regulations 2010 (2010/1192), the Explanatory Memorandum to which records the following statement of principle:

> "Timely, comprehensive and complete reporting by companies is a crucial element in promoting the allocative efficiency of capital markets. Lack of certainty as to the existing common law position with regard to issuer liability in damages for inaccurate statements made to the market was partially resolved by the introduction of a statutory liability regime. These proposals aim to extend the existing statutory regime to ensure complete clarity."

Section 90A catches all securities (UK and overseas) traded in the UK markets, including the AIM and PLUS markets, as well as UK securities traded on an overseas exchange. It applies to information published by the issuer on "a recognised information service", which includes any service "used by issuers of securities for the dissemination of information required to be disclosed by the rules of the market" (Sch 10A, para 2). It comprises three distinct (although potentially overlapping) causes of action:

- an untrue or misleading statement;
- an omission of required information; and
- a dishonest delay in publishing information.

The requirements for a successful claim in respect of each of these causes of action are as follows:

- Untrue or misleading statement (Sch 10A, para 3):
  - a dealing in securities issued in a securities market in reliance upon published information (eg the purchase, holding or disposal of such securities);
  - an untrue or misleading statement in the published information;
  - a person discharging managerial responsibility (PDMR) knew or was reckless as to the untrue or misleading statement; and
  - the claimant has suffered loss:
    - as a result of the untrue or misleading statement; and
    - it was reasonable for him to rely upon the statement at the time of suffering the loss.
- Omission of required information (Sch 10A, para 3):
  - a dealing in securities issued in a securities market in reliance upon published information;
  - an omission of information required to be included in the published information;
  - a PDMR knew the omission was a dishonest concealment of a material fact; and
  - the claimant has suffered loss:
    - as a result of the omission; and
    - it was reasonable to rely upon the omitted information at the time of suffering the loss.
- Dishonest delay in publishing information (Sch 10A, para 5):
  - a dealing in securities issued in a securities market;
  - a delay in publishing information of which Sch 10A applies;
  - a PDMR dishonestly delayed the information being published; and
  - the claimant has suffered loss as a result of the delayed publication.

This article will address certain of the key concepts which underpin s 90A. Before doing so, it is worth noting that whilst this provision offers an attractive solution to investors who have suffered losses as a result of false reporting to the market, it curtails the non-FSMA causes of action available to such investors. Schedule 10A provides a blanket exclusion for any liability in respect of loss suffered as a result of reliance by any person on an untrue or misleading statement in published information to which the schedule applies (para 7), subject to certain specified carve-outs.

Of those carve-outs, the following remain actionable:

> ... at least two important issues relating to the requirement of falsity remain to be determined by the courts.

- claims for civil liability under the Misrepresentation Act 1967; and
- claims for civil liability arising from a person's having assumed responsibility to a particular person for a particular purpose, for the accuracy or completeness of the information concerned.

Neither of these carve-outs is, however, likely to be of any assistance for most claimants. Damages are only available under the 1967 Act where it is established that the *other contracting party* made or adopted a relevant misrepresentation; such claims have no relevance to dealings on the secondary market. As to the latter, this appears to be a reflection of the pre-s 90A position at common law, where a duty of care was, by and large, only owed where financial statements were given to specified persons for specified purposes of which the persons making those statements were aware (eg *Galoo v Bright Grahame Murray* [1992] 2 B.C.L.C 492); such claims have no relevance to statements addressed to the markets as a whole.

UNTRUE OR MISLEADING STATEMENTS

A statement that is factually incorrect will *prima facie* satisfy the requirement contained in para 3(1)(b)(i) of Sch 10A that the published information contained an "untrue or misleading statement". This basic starting point aside, at least two important issues relating to the requirement of falsity remain to be determined by the courts.

First, it is unclear whether the statement in question must be untrue or misleading in a *material* way. No such words appear in the statute and, as such, materiality is unlikely to be regarded as a constitutive element of the cause of action (not least when the legislature expressly uses the word "material" for the cause of action based on omission as explained below).

However, in certain instances, the statements which are the subject of the claim may themselves be imbued with an element of materiality such that, properly understood, they are not false unless they are incorrect by a sufficiently large margin (ie quantitative materiality), or are otherwise such that they would, if properly disclosed, likely affect the judgment of users of the published information (ie qualitative materiality). Moreover, the materiality of the relevant statement may, of course, have a bearing on whether the claimant can satisfy the requirements of reliance and causation, which are considered below.

Second, leaving to one side the specific requirements of the material omissions cause of action discussed below, it is unclear whether a claim may successfully be advanced on the basis that, by reason of certain omissions from the published information (including the omission of information *not* required to be included in it), express statements contained within it were themselves untrue or misleading. Claims of this nature are actionable at common law (eg *R v Klysant* [1932] 1 K.B. 442), with the consequence that if such claims were not available under s 90A, relief under the statute would be more narrowly drawn than that which would otherwise (ie were it not for the abrogating effect of para 7 of Sch 10A) be available at common law. In this regard, there appears to be no principled rationale why an issuer should be held liable for a complete omission of a matter required to be included in a piece of published information; but should escape liability where it has omitted to include in that information a matter which renders misleading express statements contained in it.

MATERIAL OMISSIONS

To satisfy the requirement contained in para 3(1)(b)(ii) in respect of material omissions, there must be an omission of a matter "required to be included in published information", and a PDMR must have known that the omission was a dishonest concealment "of a material fact" (para 3(3)).

No guidance is given by the statute as to the meaning of these two aspects of the cause of action. The first is likely a reference to the matrix of legislative provisions which prescribes the required content of an issuer's financial reporting. On this footing, the omission of *any* matter required by a legislative provision to be included in a piece of published information would engage the court's jurisdiction under para 3(1)(b)(ii).

As to the second (ie a material fact), the legislature's intention appears to have been to rein in the scope of an otherwise wide-ranging (or at least potentially so) provision, given the volume of matters required to be included in any item of published information. Were it not for this requirement, an omission claim would potentially lie in all circumstances where a matter, whether important or insignificant, required to be included by a regulation or accounting standard was omitted. To require an issuer to check for immaterial non-disclosures would potentially impose a very high regulatory burden and lead to a mass of unhelpful (for market users) information being included in every market disclosure. That is in contrast to a positive statement, when an issuer can be expected to choose carefully and correctly the statements it decides to release to the market. It may therefore be the case that an omitted *material* fact is one which, had it been disclosed, could have had a material effect on an investor's decision to buy, sell or hold the securities in question.

> ... it is not clear whether persons who would be considered *de facto* or shadow directors of the issuer may also be PDMRs.

The most common example of this is likely to be the omission of a matter that affects the price of the securities in question by more than a *de minimis* amount. In principle, however, other types of omissions are potentially capable of being material in this sense. For example, the omission of information about breaches of ethical/environmental/regulatory standards may be important to the investment decisions of certain classes of investors, including so-called "ethical investors".

Guidance as to what constitutes a *dishonest* concealment for the purposes of an omissions claim may be found in para 6 of Sch 10A:

> "For the purposes of paras 3(3) and 5(2) a person's conduct is regarded as dishonest if (and only if) –
>
> - It is regarded as dishonest by a person who regularly trades on the securities market in question, and
> - The person was aware (or must be taken to have been aware) that it was so regarded."

Modelled on the old *R v Ghosh* [1982] Q.B. 1053 test for dishonesty, the subjective aspect of the second limb of this test now stands at odds with the common law, following the Supreme Court's restatement of the position in *Ivey v Genting Casinos UK Ltd* [2018] A.C. 391. However, until the statute is amended there is scope for defendants to run and potentially succeed upon subjective perceptions as to what traders would consider to be honest.

PERSONS DISCHARGING MANAGERIAL RESPONSIBILITIES (PDMRs)

A partial explanation of the novel expression "persons discharging managerial responsibility" is given in para 8(5) of Sch 10A:

> "For the purposes of this Schedule the following are persons "discharging managerial responsibilities" within an issuer –
>
> - any director of the issuer (or person occupying the position of director, by whatever name called);
> - in the case of an issuer whose affairs are managed by its members, any member of the issuer;
> - in the case of an issuer that has no persons within paragraph (a) or (b), any senior executive of the issuer having responsibilities in relation to the information in question or its publication."

This aside, at least two significant points concerning the identification of PDMRs and their knowledge/mental state requirement remain to be addressed by the courts.

First, it is not clear whether persons who would be considered *de facto* or shadow directors of the issuer may also be PDMRs. Although those expressions are not mentioned in Sch 10A, support for the proposition that *de facto* and shadow directors may be PDMRs may be found in the parenthetical words "(or person occupying the position of director, by whatever name called)". Further, it is not obvious why, as a matter of principle, an issuer should escape liability under s 90A where its *de facto* or shadow directors possessed the requisite mental state, but where its registered directors did not. Although para 8(5)(c) has no direct application outside of a scenario where the issuer lacks any directors or managing members, nonetheless the formulation "any senior executive of the issuer having responsibilities in relation to the information in question or its publication" arguably provides further support (by analogy) for the view that *de facto* and shadow directors ought to be regarded as PDMRs falling within para 8(5)(a).

Second, it is unclear whether the knowledge (or, indeed, recklessness) of several individuals who are PDMRs may be aggregated together to thereby satisfy the requirements of the statute.

RELIANCE/CAUSATION

Like common law deceit, s 90A contains requirements of reliance and causation of loss (save that reliance is not a requirement in delayed publication cases). In particular, the claimant must have acquired, continued to hold or disposed of securities "in reliance on" the relevant published information (para 3(1)(a)); and must have suffered loss "as a result of" the relevant untrue or misleading statement or omission (para 3(1)(b)).

Here, again, a number of points remain to be worked out by the courts.

First, must an investor advancing a claim under s 90A establish causation on a "but for" basis (ie but for the untrue statement, he would not have acquired the securities in question)? Although it is sometimes said that a claimant in common law deceit – upon which the statutory cause is modelled – must make out causation on such a basis (see, eg *Chitty on Contracts*, 32nd ed., at paras 7-038 and 7-054), on the other hand there is case law (including recent case law) which tends to suggest that a less stringent test applies to claims in deceit, such that the claimant only needs to show that he was *influenced* by the defendant's fraudulent misrepresentation *in some degree*, or that he *might* have acted differently if no misrepresentation had been made (see, eg *BV Nederlandse Industrie Van Eikprodukten v Rembrandt Enterprises Inc* [2018] EWHC 1857 (Comm)). It may be that this jurisprudence cross-fertilises the law on s 90A.

Second, what is the relevant counterfactual for a claim under s 90A? In particular, is the appropriate enquiry what the claimant would have done:

(i) if no representation had been made to him at all; or
(ii) if the claimant had been given the true facts.

> ... it remains to be seen whether s 90A requires an investor actually to have read and relied upon the published information.

The weight of authority (particularly recent authority) concerning common law deceit favours the first of these approaches (eg *Rembrandt Enterprises* at [104]).

However, in a common law deceit claim, the defendant is generally under no obligation to speak at all, which makes (i) above the appropriate counterfactual. Accordingly, it is uncertain whether that approach would continue to apply where the untrue or misleading statement was *required* (eg by the Companies Act 2006 or certain statements of accounting principles) to be included in the published information.

Third, claimants in common law deceit benefit from a "presumption of inducement". Once it is shown that the misrepresentation was material in the sense that it was likely to induce entry into the relevant transaction, then it will be presumed that the claimant was so induced unless the defendant is able to rebut that presumption. There is a separate question about whether this presumption applies to a claim under s 90A. As to this, the presumption has been characterised as an inference of fact or evidential tool, rather than a presumption of law: see *Zurich Insurance Co plc v Hayward* [2016] UKSC 48. As such, the courts may be prepared to apply the same approach to s 90A, notwithstanding the absence of any express reference to a presumption of inducement in the text of the statute.

Finally, and importantly for tracker funds and retail investor claims, it remains to be seen whether s 90A requires an investor actually to have read and relied upon the published information. Although reliance is an express requirement of the statute (para 3(4) of Sch 10A), a construction requiring investors to have read the financial statements in question would exclude "fraud on the market" type claims. Such a construction would not sit comfortably with the intention behind the Transparency Director to achieve "a high level of investor protection". Instead, a broader interpretation of reliance may be appropriate where tracker funds and retail investors rely upon the market price as factoring in the as-represented financial position of the issuer, based in part upon published statements of the issuer. Pursuant to such a construction, reliance on the market price would itself constitute reliance (albeit indirectly) upon the published information. This remains a highly controversial and untested question.

CONCLUSION

As noted in the introduction, s 90A is potentially a valuable remedy for investors who have suffered loss as a result of false statements to the market, for example in the context of the high-profile scandals mentioned above. However, that remedy is rarely used, and there have been no reported or unreported decisions under s 90A since it was first enacted more than twelve years ago, with the result that none of the issues identified in this article have been tested by the courts to date. While it is difficult to identify the reasons for this underutilisation

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with any certainty, there are at least three possibilities as follows.

First, as explained above, the claimant in a s 90A claim must prove that a PDMR of the defendant has acted dishonestly, ie that he knew that the relevant statement was untrue or was reckless as to the same (or equivalent requirements for delay and omission cases). In most cases, however, all of the evidence relevant to this question will be in the hands of the prospective defendant. This means that prospective claimants are unlikely to be in a position to assess whether there are good grounds for a claim, at least absent regulatory or criminal proceedings against the prospective defendant (or its directors/employees) which results in additional information coming in to the public domain.

Second, s 90A is not the only remedy available for investors who have suffered losses as a result of false statements to the market. In particular, s 384(5) of FSMA empowers the Financial Conduct Authority (FCA) to, *inter alia*, order a person who has engaged in "market manipulation" contrary to the Market Abuse Regulation (EU Regulation No 596/2014) to pay compensation to persons who have suffered loss as a result. This power was exercised for the first time in the context of Tesco's 2014 accounting error referred to above, resulting in the establishment of a compensation scheme for investors. Where the FCA exercises its powers under s 384(5), this will often provide a more straightforward remedy for investors than s 90A for the following reasons.

The test for "market manipulation" is in some respects less stringent than the test imposed by s 90A. In particular, under Art 12(1)(c) of the Market Abuse Regulation, "market manipulation" occurs when there is dissemination of certain types of false or misleading information by a person who "knew, or ought to have known, that the information was false or misleading". Accordingly, it is not necessary to prove knowledge on the part of a PDMR, and knowledge on the part of an individual lower down in the hierarchy of the prospective defendant will suffice. Moreover, the FCA (rather than the prospective claimant) will shoulder the burden of proving that the requirements for an order for compensation under s 384(5) are satisfied, and for that purpose the FCA will be able to call upon investigatory powers and resources that are not available to a private litigant.

Third, if the prospective defendant is insolvent (or if there are concerns about its insolvency), then a claim under s 90A (which, if proven, would rank alongside all of the other unsecured debts of the company) is unlikely to provide an effective remedy for investors. Carillion and Patisserie Valerie provide recent examples of cases where concerns about the issuer's solvency (and therefore its ability to satisfy any judgment against it) may discourage claims under s 90A.

Given the above considerations and the uncertainties surrounding the meaning and operation of s 90A, it remains likely that s 90A will continue to be an underutilised statutory remedy, a least until a great deal of those uncertainties are removed through a reported decision. The forthcoming trial in 2019 of Hewlett Packard's claim against Mike Lynch in connection with its acquisition of Autonomy (which is proceeding in the Financial List in the High Court) includes a claim under s 90A and may therefore provide an opportunity to resolve some of these uncertainties. However, as the RBS Rights Issue litigation demonstrated in respect of s 90 of FSMA (the sister provision of s 90A, which relates to statements in listing particulars/prospectuses)[1] the interests of parties achieving a settlement may continue to keep this provision out of the judicial spotlight. ■

1 The RBS Rights issue settled the day before the trial: see *Prospectus litigation: lessons learned from the RBS Rights Issue litigation* published in the May 2018 issue of this journal, ((2018) 5 JIBFL 288).

Further Reading:

- Prospectus litigation: lessons learned from *The RBS Rights Issue Litigation* (2018) 5 JIBFL 288.
- Extension of the statutory regime for issuer liability (2010) 11 JIBFL 682.
- LexisPSL: Banking & Finance: Issuer liability for ad hoc disclosures and dishonest delay: cause for concern?

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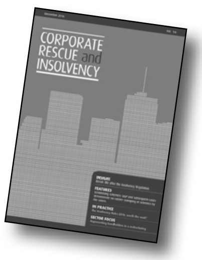

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