FINANCIAL CONDUCT AUTHORITY

12 Endeavour Square
London
E20 1JN

Tel: +44 (0)20 7066 1000
Fax: +44 (0)20 7066 1099
www.fca.org.uk

FINAL NOTICE

To: Tullett Prebon (Europe) Limited

FRN: 146880

Date: 11 October 2019

1. PROPOSED ACTION

1.1. For the reasons given in this Final Notice, the Authority hereby impose on Tullett Prebon (Europe) Limited ("TPEL") a financial penalty of £15.4 million pursuant to section 206 of the Act.

1.2. TPEL agreed to resolve this matter and qualified for a 30% (stage 1) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £22 million on TPEL.

2. SUMMARY OF REASONS

2.1. TPEL breached Principle 2, Principle 3 and Principle 11 of the Authorities Principles for Businesses.

<u>Breach of Principle 2 and Principle 3</u>

2.1. Principle 2 of the Authority's Principles for Businesses requires a firm to conduct its business with due skill, care and diligence.

2.2. Principle 3 of the Authority's Principles for Businesses requires firms to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

2.3. TPEL is an electronic and voice inter-dealer broker, acting for institutional clients transacting in the wholesale financial markets, typically investment banks. During the Relevant Periods, TPEL was split into a number of divisions, one of which was the Rates Division. The majority of business within the Rates Division involved 'name passing' broking and this comprised a large part of TPEL's overall business, employing many brokers and generating significant revenues for the firm.

2.4. Improper broker conduct was a market risk within the inter-dealer broking business, in particular because:

- the business depended heavily upon strong relationships between brokers and traders being developed and maintained;

- entertainment of traders by the brokers was encouraged as a way for brokers to develop and maintain these broker-trader relationships and entertainment was sometimes lavish; and

- brokers' bonuses were based on the amount of brokerage they personally generated.

2.5. Improper conduct of brokers within an inter-dealer broking firm such as TPEL can have significant consequences in the wider market due to the central role such firms play in the facilitation of trading that is undertaken in the wholesale markets. It is therefore critical that broking firms conduct their business with due skill, care and diligence and that appropriate systems and controls are in place to reduce the risk of broker misconduct, thereby also reducing the risk of wider market issues.

2.6. In relation to the breach of Principle 2, on a number of occasions, Senior Managers at TPEL failed to act with due skill, care and diligence when they were faced with blatant signals of broker misconduct. Rather than taking steps to address the risk presented, they took no action. For example, when significantly high brokerage was generated on a trade and a Senior Manager asked the broker responsible if it was an error, the broker confirmed it was correct and told him "*you don't want to know*"; no steps were taken to explore the obvious risk of broker misconduct. Furthermore, the Compliance Department failed to act with due skill, care and diligence as it assumed certain controls around broker conduct were being operated within the name passing business when in fact such controls were not being effectively used in practice.

2.7. In relation to the breach of Principle 3, adequate systems and controls should have been in place and effectively implemented within the Rates Division to counter the risks arising from the conduct of brokers. Whilst certain systems and processes were available and could have been utilised to address the risk of broker misconduct, they were not used for monitoring and compliance purposes. There was a disconnect between the potential use of such systems and controls to reduce the risk of broker misconduct and the practical reality of what was happening within the business. Whilst the Compliance Department and the Tullett Group Executive Committee thought certain systems and controls around broker conduct were effective within the name passing business, in practice these systems and controls were not effective. The focus of the name passing business in the Rates Division was instead almost exclusively on revenue generation.

2.8. The risk of improper broker conduct crystallised within the Rates Division. Between September 2008 and June 2011, brokers in the Rates Division carrying out name passing business acted with traders to put in place improper trades for the purpose of generating unwarranted brokerage payments for TPEL. This trading activity was carried out by seven brokers across four Desks within the Rates Division and generated a significant amount of unwarranted brokerage for TPEL of approximately £390,000.

2.9. The Authority considers the breaches of Principle 2 and Principle 3 to be serious. The systems and controls around broker conduct in the name passing business of the Rates Division were deficient for several years and there were several instances of Senior Managers failing to act with due skill, care and diligence in response to blatant signals of broker misconduct. It is likely that some of the trading which generated unwarranted brokerage for TPEL would either have been prevented or would have been identified and stopped were it not for these breaches of Principle 2 and Principle 3.

2.10. The Authority hereby impose a financial penalty on TPEL in the amount of £10.5 million pursuant to section 206 of the Act for breach of Principle 2 and Principle 3.

2.11. TPEL agreed to resolve this matter and qualified for a 30% (stage 1) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £15 million in respect of the breach of Principle 2 and Principle 3.

<u>Breach of Principle 11</u>

2.12. Principle 11 requires firms to deal with their regulators in an open and cooperative way, and to disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice.

2.13. The Principle 11 Relevant Period commences when the Authority required TPEL to provide certain broker audio recordings pursuant to its statutory powers. A series of actions and inactions by TPEL followed on from this requirement through which TPEL failed to deal with the Authority in an open and cooperative way and failed to give the Authority notice of matters the Authority would reasonably expect notice. The Principle 11 breach was particularly serious because Senior Managers in the Legal Department ("Senior Manager A") and the Compliance Department ("Senior Manager B") were at the centre of the matters giving rise to the breach.

2.14. In summary:

- The Authority issued a statutory information requirement to TPEL requiring certain broker audio be produced. TPEL told the Authority that the required audio had been deleted in accordance with the firm's audio deletion policy. Whilst it was correct that there was a 12-month audio deletion policy in place, TPEL's Voice Communications Department in fact retained a significant amount of the London broker audio from 2006 onwards and had the majority of the required audio.

- On the same day as the Authority had been told that the audio it required had been deleted in accordance with TPEL's 12-month audio deletion policy, Senior Manager A received an email from TPEL's Voice Communications Department informing him that at least some of the audio required by the Authority was available. Senior Manager A failed to notify the Authority as to the availability of this audio and failed to check to find out whether any further audio was available, despite being on notice that audio had been retained for more than 12 months. A check would have revealed that broker audio was available from 2006 onwards.

- The Authority later asked TPEL to check whether different broker audio was available or whether it had been deleted in line with the firm's audio deletion policy. No such checks were carried out by the Compliance Department and, as a result, the Authority was not provided with this audio (most of which was available) and continued to have incorrect information as to the availability of TPEL broker audio. Again, a simple check with TPEL's Voice Communications Department would have revealed that a significant amount of broker audio was available from 2006 onwards.

- Nearly two years after the Authority's original information requirement, Senior Manager A and Senior Manager B became aware that TPEL had retained historic broker audio. They learned of the audio's existence when a manager in the Voice Communications Department sent an email to them from which it was clear that broker audio from 2006 was retained. There was then a delay of over six months before the Authority was informed that the audio it had previously required had not all been deleted.

- When TPEL notified the Authority and another law enforcement agency about the existence of the audio, TPEL provided an incorrect account as to the circumstances in which the existence of the audio had been bought to the attention of the Legal and Compliance Departments. The explanation given was that the audio had been found by Facilities during an office clear out. Whilst not deliberately intended to mislead, this account created the impression that no one at TPEL had previously known of the audio's existence and that it had been discovered 'by chance'. However, the correct position was that the Voice Communications Department had retained historic broker audio tapes and it was a manager in that department who had bought the audio to the attention of the Legal and Compliance Departments.

- The consequence of TPELs failure to notify the Authority and another law enforcement agency about the existence of the audio was that enquiries into potential broker misconduct continued for two and a half years without the benefit of highly relevant material.

2.15. Pursuant to Principle 11, it is a fundamental obligation that a regulated firm must deal with its regulators in an open and cooperative way. The Authority considers TPEL's failings to be serious because:

- The audio was information the Authority had specifically requested. Checks to confirm the accuracy of TPEL's response to the information requirement were not made even when TPEL was on notice that audio did exist beyond the 12-month audio retention policy and despite TPEL being specifically asked by the Authority to check the position.

- Once Senior Managers A and B were made aware of the existence of the audio by a manager in the Voice Communications Department, they did not inform the Authority of the existence of the audio for several months.

- The Authority was given an incorrect account as to how the audio was discovered, an account which suggested to the Authority that the audio had been discovered 'by chance'.

2.16. The Authority hereby impose a financial penalty on TPEL in the amount of £4.9 million pursuant to section 206 of the Act for breach of Principle 11.

2.17. TPEL agreed to resolve this matter and qualified for a 30% (stage 1) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £7 million in respect of the breach of Principle 11.

3. DEFINITIONS

3.1. The definitions below are used in this Notice:

"Act"	The Financial Services and Markets Act 2000
"Authority"	The body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority
"Desk"	Broking desk that deals in a range of OBS financial products including Interest Rate Swaps and Interest Rate Forward Agreements
"FCA Handbook"	The Authority's handbook of rules and guidance
"LIBOR"	London Interbank Offered Rate
"Desk Head"	A TPEL employee with direct line management responsibility over Brokers
"Divisional Director"	A TPEL employee with responsibility for one or more Desks
"OTC"	Over the counter
"Principles"	The Authority's Principles for Businesses
"Principle 2 and Principle 3 Relevant Period"	September 2008 to September 2013
"Principle 11 Relevant Period"	15 August 2011 to 31 October 2014
"Senior Manager"	Individual with seniority of Desk Head or above
"Tribunal"	The Upper Tribunal (Tax and Chancery Chamber)
"TPEL"	Tullett Prebon (Europe) Limited
"Compliance Department"	Compliance Department of the Tullett Group
"Legal Department"	Legal Department of the Tullett Group
"Tullett Group"	Tullett Prebon Group plc (now TP ICAP plc) of which TPEL is a part
"Voice Communications Department"	The department within TPEL that was responsible for maintaining and retaining audio communications

4. FACTS AND MATTERS

4.1. The facts and matters relevant to the breaches are set out as follows:

Paragraphs 4.2 – 4.18	Background
Paragraphs 4.19 – 4.91	Principle 2 and Principle 3
Paragraphs 4.92 – 4.131	Principle 11

BACKROUND

TPEL's structure

4.2. TPEL was authorised by the Authority on 1 December 2001. During the Relevant Periods, TPEL was part of the Tullett Group which was at that time the world's second largest interdealer broker.

4.3. TPEL is an electronic and voice interdealer broking firm, acting for institutional clients transacting in the wholesale financial markets, typically investment banks. TPEL's main business is to provide access to pools of liquidity in these markets, in particular OTC markets, and bring together counterparties for which TPEL arranges trades in return for a brokerage fee.

4.4. In the Relevant Periods, the Tullett Group generated approximately £900 million in annual revenue and employed around 1600 Brokers globally. The Tullett Group managed its broking operations on a regional basis. The Tullett Group's European operations generated approximately £500 million in annual revenue and employed around 800 brokers. TPEL, which was part of the Group's European operations, generated approximately £300 million in annual revenue.

4.5. TPEL was organised into a number of Divisions (including Rates, Treasury and Credit). Brokers were divided into various Desks within each Division. Each Desk specialised in arranging trades in different currencies and financial products on behalf of its clients.

The Rates Division

4.6. The Rates Division in TPEL covered the broking of a number of financial products such as interest rate swaps, interest rate options, Government bonds, repurchase agreements, basis swaps, futures and options. Most of these products were traded OTC, although a few were traded on exchange.

4.7. At the start of the Principle 2 and Principle 3 Relevant Period, the Rates Division had approximately 18 desks and 180 Brokers. The average annual revenue for that Division over that period was approximately £160 million, thus comprising over half the revenue of TPEL and around 18% of the revenue of the Tullett Group. The vast majority of the Rates Division was located in the London office of TPEL.

4.8. The Rates Division was headed by a Managing Director who reported into the Tullett Group CEO for EMEA. Each desk within the Rates Division was assigned to one of a number of Divisional Directors, each of whom reported into the Managing Director of the Rates Division. Additionally, a senior broker on each desk held the position of Desk Head.

The Compliance and Legal Departments

4.9. The Compliance and Legal Departments covering TPEL were both run centrally within the Tullett Group.

TPEL's business activities

4.10. During the Relevant Periods, TPEL arranged trades on both a 'matched principal' and a 'name passing' basis.

4.11. Matched principal broking involves a broker facilitating a transaction by interposing TPEL as counterparty between the buyer and seller in matching and simultaneous back to back trades. In doing so, the broker acts as trade counterparty, but does not take on any market risk and does not make any profit or loss. The broker receives brokerage from the trade counterparties.

4.12. Name passing broking involves a broker providing bid and offer information to potential trade counterparties. Once a broker has arranged a trade and has confirmed trade price, volume and terms with the counterparties, the counterparties' names are disclosed to each other and they enter into a bilateral agreement. The broker will then invoice the clients a brokerage fee arising from the trade.

4.13. Thus, in the name passing business, revenue was generated by brokers earning brokerage on trades they arranged between trade counterparties. This brokerage was paid in accordance with pre-set contractual arrangements between TPEL and the relevant trading firm. The amount of brokerage payable was not therefore the subject of negotiation for the broker.

Relationships between brokers and traders

4.14. An important aspect of the name passing brokerage model was the relationships between the brokers and individual traders at the trading firms, often investment banks. As explained by a Senior Manager in the Rates Division "*this business is a….. people business.*"

4.15. Typically, a broker carrying on name passing business in the Rates Division would have working relationships with a number of traders active in the particular product and currency in which the broker specialised. The flow of business from the trader to the broker was influenced by the strength of the relationship between the broker and trader. Thus, brokers in the name passing business in the Rates Division were expected and encouraged to develop and maintain strong relationships with traders who could bring them business.

4.16. To further the opportunity for brokers to develop and maintain relationships with traders, TPEL would pay the expenses incurred by their brokers entertaining traders. Entertainment would typically involve drinks and dinners, but could also extend to overnight stays and trips abroad (for example, golf trips to Scotland, trips to Monte Carlo, Las Vegas and Ibiza).

4.17. The general guidance for a Desk's permitted expenditure on entertainment was around 3% of that Desk's revenue, although this was not an absolute limit and expenditure on entertainment was permitted to exceed this amount from time to time.

Broker remuneration

4.18. Brokers at TPEL were remunerated by way of a salary and a discretionary bonus. The bonus was calculated on the basis of the brokerage personally generated by the broker. Bonus payments could potentially be many multiples of salary.

PRINCIPLE 2 AND PRINCIPLE 3

4.19. Principle 2 of the Authority's Principles for Businesses requires a firm to conduct its business with due skill, care and diligence.

4.20. Principle 3 of the Authority's Principles for Businesses requires a firm to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

4.21. The Principle 2 and Principle 3 Relevant Period is September 2008 to September 2013.

Overview

4.22. The name passing business within the Rates Division was a large part of TPEL's business, employing many brokers and generating significant revenues for the firm. Improper broker conduct was a clear risk within the Rates Division because:

- the business depended heavily upon strong relationships between brokers and traders being developed and maintained;
- entertainment of traders by the brokers was encouraged as a way to develop and maintain these broker-trader relationships and entertainment afforded to traders was sometimes lavish; and
- brokers' bonuses reflected the amount of brokerage a broker personally generated.

4.23. As such, the name passing business gave rise to a risk of improper broker conduct. For example, there was a risk that brokers and traders may act together to generate unwarranted brokerage for TPEL in return for enhanced entertainment or other favours being provided to the trader. Despite this, the name passing business was considered by TPEL to be lower risk from a compliance perspective and attention to risk was largely focussed on matched principal broking.

4.24. The key failings fall into the following areas:

(i) Monitoring (see paragraphs 4.27 – 4.37 below);

(ii) Compliance responsibilities (see paragraphs 4.38 – 4.52 below); and

(iii) Controls around entertainment expenditure (see paragraphs 4.53 – 4.69 below).

4.25. During the Principle 2 and Principle 3 Relevant Period, the risk of improper broker conduct crystallised. Brokers in the Rates Division carrying out name passing business acted with traders to put in place trading mechanisms for the purpose of generating unwarranted brokerage payments for TPEL. Such trades are described further below. These mechanisms to generate unwarranted brokerage involved seven brokers across four Desks within the Rates Division and took place over nearly three years. This generated a significant amount of unwarranted brokerage for TPEL (see paragraphs 4.70 to 4.81 below).

4.26. Improper broker conduct at TPEL was also illustrated by significant entertainment expenditure being afforded to a trader in return for the trader improving the price of a trade in order that a loss event be avoided by an overseas office of the Tullett Group (see paragraphs 4.82 to 4.91 below).

<u>Monitoring</u>

4.27. As detailed further below, there was no effective monitoring of either brokerage generated or broker communications in the name passing business in the Rates Division. The Compliance Department did not carry out any monitoring of the name passing business in the Rates Division. A system was in place which could have been used by Divisional Directors and Desk Heads within the name passing business to monitor brokerage generated, but in practice the system was not used for this purpose effectively. Divisional Directors and Desk Heads did not consider it their responsibility to monitor broker activity from a compliance perspective and did not know that the available system was meant to be used for this purpose. Therefore, compliance monitoring of this part of the business was non-existent in practice.

No monitoring by Compliance

4.28. There was no form of monitoring by the Compliance Department in respect of the name passing business, either with regard to brokerage generated or broker communications. The Compliance Department did carry out trade monitoring in relation to non-market price transactions for matched principal trades, but there was no monitoring by the Compliance Department of any kind with respect to the name passing business.

4.29. The decision that the Compliance Department should not carry out any monitoring in the name passing business in the Rates Division was initiated within the Compliance Department and approved by an Executive Director of the Tullett Group. This decision was taken on the basis that the risk of market abuse was TPEL's key area of focus and the matched principal desks were considered a higher risk area in this regard.

No monitoring within the name passing business in the Rates Division

4.30. TPEL had an electronic system that captured information about orders, trades and commissions. This system covered the name passing business in the Rates Division. The information captured was fed into a system called the Brokerage Reporting System ("BRS") which was accessible at different permission levels as set by the Managing Director of each Division.

4.31. The BRS provided a number of different views of the information captured. This enabled information to be viewed by region, by client, by desk and by desk blotter (*i.e.,* the desk blotter showed the details of individual orders). As such it was possible for those with the relevant permissions to see each transaction arranged or executed in real time on a day by day basis including details of the client, the broker and the brokerage generated.

4.32. The BRS was rolled out in the Rates Division from 2006.

4.33. Thus, the BRS could have been used within the Rates Division as a tool to monitor the activities of the brokers from a compliance perspective. For example, if a transaction generated an unusually large amount of brokerage, this would appear in real time on the BRS by way of the relevant desk's revenue jumping up. It would then be possible to "click" on tabs in the system to identify what trade or trades had generated the high brokerage and see the relevant broker and client. From that point it would be possible to interrogate the transaction as appropriate, although there was no automated programme to do so and this would have had to have been done manually.

4.34. Between 2008 and 2011, the Compliance Department thought that the BRS was being used by the Desk Heads and Divisional Directors to pick up any unusual transactions on the basis of large amounts of brokerage being generated. The Compliance Department expected the Desk Heads and Divisional Directors would use the BRS system to note such trades and then carry out enquiries in order to check the trade. Equally, the Tullett Group Executive Committee also thought that the BRS was being used for monitoring within TPEL's Rates Division at this time as part of the 'first line of defence' from a compliance perspective.

4.35. However, in practice, there was no effective monitoring of the name passing business in the Rates Division. There were no policies, processes, procedures or training in place regarding the BRS being used to monitor compliance risks in the name passing business.

4.36. The Compliance Department thought that the expected use of the BRS to monitor the name passing business would have been passed down from the Managing Directors to the Divisional Directors and Desk Heads. However, there was no process in place to ensure this message was passed to the Divisional Directors and Desk Heads and, in practice, no such message was cascaded.

4.37. Thus, the Divisional Directors and Desk Heads in the Rates Division were not told that the BRS system should have been used for compliance monitoring purposes and they were not told that they were meant to undertake such monitoring. Rather than being used as a compliance tool, the BRS was used within the Rates Division as a tool to review the level of revenue generation.

Compliance responsibilities

4.38. As detailed further below, a governance structure was in place which intended for Desk Heads and Divisional Directors to undertake compliance responsibilities, including responsibility for broker conduct issues. However, the intended compliance role of Desk Heads and Divisional Directors was not embedded in the name passing business and there was no meaningful 'first line of defence' in practice:

- the Divisional Directors and Desk Managers were not sufficiently aware of their compliance responsibilities (see paragraphs 4.39 to 4.43 below);

- there was an extremely limited relationship between the Rates Division and the Compliance Department (see paragraphs 4.44 to 4.49 below); and

- certain Senior Managers ignored clear 'red flags' that signalled broker misconduct and gave no thought to the risks that should have been apparent to them (see paragraphs 4.50 to 4.52 below).

Lack of awareness of compliance responsibilities

4.39. The Compliance Department and the Tullett Group Executive Committee considered that Divisional Directors had central compliance responsibilities within the business. These responsibilities were reflected within a "Statement of Responsibilities" which was an initiative of the Compliance Department in 2009 in order to document the responsibilities of senior staff. A Statement of Responsibilities was sent to each of the Managing Directors and Divisional Directors in 2009 for them to sign and return to the Compliance Department. The Statement of Responsibilities included the following standard wording:

> *"Legal and regulatory responsibilities of a director, joint responsibilities with other directors for compliance, and overall responsibility for [relevant desks]."*

4.40. However, in practice, the Statement of Responsibilities was signed and returned to the Compliance Department with limited understanding as to its actual meaning with regard to compliance. One Senior Manager commented, "*I don't think there was any clear understanding from anyone exactly what, what we were signing to be quite honest*."

4.41. The Divisional Directors did not consider compliance to be one of their responsibilities and, save for it appearing in the Statement of Responsibilities, compliance responsibilities were not discussed with them or communicated to them.

4.42. Divisional Directors and Desk Heads had no training of any nature in relation to compliance responsibilities. The only training that reached the Rates Division was periodic market abuse emails and training targeted at personal account dealing, the Bribery Act and anti-money laundering.

4.43. As such, the 'first line of defence' was little more than a theoretical notion and, other than the Statement of Responsibilities, no steps were taken to ensure that this was an effective tool to deal with compliance risks, such as the risk of improper broker conduct. The Divisional Directors and Desk Heads in the Rates Division essentially did not all appreciate that compliance responsibilities fell to them.

Lack of relationship between Compliance Department and business

4.44. The Compliance Department was located within the same building as the Rates Division, but on a different floor. The Compliance Department had no formal presence on the broking floor and there were minimal interactions between members of the Compliance Department and the Rates Division.

4.45. There was a meeting structure in place that could have been used to cascade compliance issues from the Compliance Department and the Executive Committee to the business and vice versa. However, this did not work in practice as a method of enabling communications about compliance issues.

4.46. There was no other process in place whereby compliance issues would be discussed between the Compliance Department and members of the Rates Division.

4.47. As one Senior Manager in the Rates Division commented on the Compliance Department:

> "*So as a function of actually overlooking the business and giving us the direction and steer from a compliance perspective, we didn't have one*."

4.48. Another Senior Manager said of compliance issues:

> *"[it was] never anything that was really talked about on any sort of basis at all"* and *"[there] wasn't any feed down of compliance issues anywhere, it just wasn't there*."

4.49. As a result, awareness of the Compliance Department and compliance issues within the Rates Division was extremely limited. Furthermore, this meant that the business was not consulted on potential compliance risks, but also was not engaged with the Compliance Department in order to establish what compliance risks might arise and how they could be addressed.

Senior Managers ignored red flags

4.50. When certain Senior Managers in the Rates Division encountered 'red-flags' which should have led to a recognition of risk and further action, they gave little or no thought to the possible risks and took no action.

4.51. On a number of occasions, information signalling the risk of improper broker conduct came to the attention of Senior Managers:

- In December 2008, a Senior Manager noticed that brokerage of £15,000 had been generated on a trade. The Senior Manager contacted the broker responsible for the trade and was told by the broker that further brokerage in the same amount had also been generated on a different trade that day. The Senior Manager congratulated the broker. He did not make any enquires regarding the trades, despite the unusually large brokerage generated on two different trades on the same day. These trades were both part of a wash trade (see further paragraphs 4.72 to 4.77 below).

- In February 2009, a Senior Manager noticed that brokerage of £35,000 had been generated on a trade and phoned the broker concerned to find out if it was an error. The broker confirmed that the brokerage was correct and he said to the Senior Manager "*you don't want to know alright*". The Senior Manager did not ask any further questions about the trade. This trade was also part of a wash trade (see paragraph 4.76 below).

- Also in relation to this wash trade in February 2009 that generated £35,000 in brokerage, another Senior Manager noticed this brokerage and was told by the broker involved in arranging the trade "*you don't really want to know*" to which the Senior Manager said "*that is exactly what [another broker] said as well so I definitely don't want to know*." The broker involved in the trade then immediately asked if the Senior Manager would "*look after*" the expenses claim he made for boxing tickets, to which the Senior Manager said "*I will try*". The Senior Manager failed to take any steps to consider the legitimacy of the trade or the size of the brokerage generated.

4.52. The average amount of brokerage generated per trade in the Rates Division during the Principle 2 and Principle 3 Relevant Period was between £764 and £1,427 (depending on the Desk). Thus, brokerage in the sums of £15,000 and £35,000 was extremely high and represented the highest brokerage generated by the relevant Desk in 2008 and 2009 respectively. The large size of the brokerage combined with the other red flags (such as the cryptic comments from the brokers) should have immediately raised concerns with the Senior Managers and led to a chain of enquiry.

<u>Controls around entertainment expenditure</u>

4.53. The main control for entertainment expenditure was the Expenditure Control Framework ("the ECF"), which established a framework of delegated authorities within TPEL for, amongst other things, the 'authorisation' and 'approval' of entertainment expenses. In addition, relevant policies on entertainment expenditure were set out in the Compliance Manual and the Staff Handbook, which were available to TPEL employees on the intranet.

4.54. Entertainment expenses were recorded and processed on an electronic system called iExpense.

Inadequate policies and guidance around entertainment expenditure

4.55. The ECF stated that it contained the principles, policy and pre-authorisation/approval limits that were to be applied in relation to entertainment expenditure. However, the section on entertainment expenditure lacked detail and did not adequately address compliance risks arising from entertainment. For example:

- It stated that all entertainment of clients should be carefully evaluated, but did not specify who was to make the evaluation and what factors were to be taken into account when making such an evaluation. This evaluation focussed on tax issues rather than compliance risks;

- Although the ECF stated that entertainment expenditure will be reviewed for 'appropriateness' at the approval stage, the only guidance as to what was appropriate was that the expense of the occasion must be appropriate to the revenue generating potential and according to local custom; and

- There were no policies or processes whereby entertainment expenditure was to be looked at on a 'by broker' or 'by trader' basis.

4.56. TPEL had a Compliance Manual which also set out some rules and procedures in relation to entertainment. However, the policies contained in the Compliance Manual were inadequate in the following ways:

- There was one example of receipt of entertainment from a client being used to show an improper inducement, but the policy failed to explain the risks and consequences associated with providing inappropriate entertainment to clients (other than from a tax perspective); and

- There was an obligation on employees to report to a Divisional Director any offers of lavish entertaining received and for the Compliance Department to be consulted over doubtful or lavish entertaining being offered, but there was no explanation or guidance as to what amounted to doubtful or lavish entertaining.

4.57. TPEL's Staff Handbook also set out some rules and procedures in relation to entertainment. And although (unlike the Compliance Manual) the Staff Handbook did refer to the requirement for entertainment expenditure to be reasonable and proportionate, it did not provide any meaningful explanation or guidance on what this meant in practice; this was simply left to an individual's own judgment.

4.58. Overall, TPEL lacked a clear and coherent entertainment expenditure policy that adequately addressed the compliance risks associated with the potential abuse of entertainment expenditure. As a result, brokers who incurred entertainment expenses and Divisional Directors who approved them were unable to access clear information and guidance about their respective duties and responsibilities in this regard.

4.59. The policies that were in place were not properly embedded such that certain brokers and Divisional Directors in the Rates Division were not even aware of the entertainment expenditure policies found in the Compliance Manual and Staff Handbook.

No monitoring of entertainment expenditure by Compliance

4.60. During the Principle 3 Relevant Period, the monitoring controls designed to address the risks arising from entertainment expenditure were heavily focused on financial matters (*i.e.,* the entertainment spend from an accounting perspective).

4.61. The responsibility for monitoring entertainment expenditure at TPEL was divided between Senior Managers in the Rates Division and the EMEA Finance Department as follows:

- Senior Managers were responsible for:

  (i) authorising overall Desk budgets, which included entertainment expenditure incurred by desks;

  (ii) authorising and approving brokers' entertainment expenses (via iExpense) – this was primarily undertaken by Divisional Directors; and

  (iii) reviewing a monthly 'doughnut report' which tracked entertainment expenditure as a percentage of revenue by Desk.

- The Finance Department was responsible for processing the requests for expenses to be paid and ensuring that approval of expenses on IExpense was in line with the ECF.

4.62. There was no monitoring at all of entertainment expenditure by Compliance. The lack of involvement and engagement by the Compliance Department meant that there was a fundamental weakness in TPEL's ability to monitor and detect entertainment abuse from a compliance risk perspective.

Ineffective primary monitoring of entertainment expenditure by Senior Managers

4.63. Entertaining was allowed and encouraged for the purpose of building client relationships with the ultimate aim of generating business for TPEL. The level of entertainment expenditure was measured by reference to a guidance ratio of 3% of desk revenue.

4.64. The focus on entertainment expenditure as a percentage of monthly desk revenue resulted in Senior Managers taking a numbers-orientated and process-driven approach to supervision of client entertainment. There was no oversight or monitoring of the form, frequency and cost of entertainment being provided by individual brokers to individual traders. There were no processes in place to assist in detecting potential abuse of entertainment from a compliance risk perspective (for example, a broker providing frequent and lavish entertainment to a trader in return for some form of 'kick back').

4.65. Senior Managers adopted a lax approach to expenses through the authorisation and approval process. For example, versions of the ECF in force between 2008 to 2011 required entertainment expenses to be pre-authorised by a Divisional Director for sums in excess of £500 and by a Managing Director for sums in excess of £1,500. However, a 2012 Internal Audit noted that in practice, no such pre-authorisation was taking place. As a result, the policy was revised to require that only expenses over £10,000 required pre-authorisation. As a result, there was no opportunity for Senior Managers to consider items of entertainment expenditure under £10,000 before the cost was incurred.

4.66. The review of expenditure at the approval stage (*i.e.,* once the expense had been incurred) essentially involved 'ticking off' the expense claim on iExpense without any engagement or possible challenge in relation to the expenses being claimed.

4.67. The focus of Senior Managers scrutiny of entertainment expenditure was if a Desk's expenses exceeded the 3% guidance ratio. However, this was undertaken at Desk level rather than in respect of individual brokers. No consideration was given as to whether high entertainment costs in relation to revenue may have been indicative of some form of abuse of entertainment expenditure.

Ineffective secondary monitoring of entertainment expenditure by Finance

4.68. Monitoring of staff adherence to the ECF after expenses had been approved was undertaken by the Finance Department. This monitoring included:

- checking that expenses had been approved correctly on iExpense;
- validating and dip sampling receipts to check whether they were appropriately approved;
- preparing an annual review of the 'Delegation of Authority' to check that the personnel and approval limits continued to be appropriate; and
- preparing the 'doughnut report' for Senior Managers showing what percentage of Desk revenue was being spent on client entertainment.

4.69. None of these controls looked at entertainment expenditure from a compliance perspective, in particular whether a broker's expenditure on entertainment may indicate potential compliance issues. TPEL relied on the Finance Department to undertake monitoring of entertainment expenditure even though this department had no compliance expertise and were not supported in their review by the Compliance Department.

<u>Improper broker conduct at TPEL</u>

4.70. From 2008 to 2011, a number of TPEL brokers in the Rates Division and certain traders acted together to put in place improper trades in order to pay brokerage to TPEL that should not have been paid. The two trade mechanisms identified involved wash trades and three-party switches. Furthermore, on one occasion identified, lavish entertainment was used to improve the price of a trade for the purpose of avoiding a loss event incurred by an overseas office of the Tullett Group.

Wash trades

4.71. A wash trade involves a set of two identical swaps trades between the same two counterparties. The second trade is the equal and opposite of the first trade, thereby cancelling out the first trade so that neither counterparty has any exposure or credit risk. Both trades are a sham and have as their sole purpose the generation of brokerage.

4.72. 17 wash trades were arranged in the name passing business of the Rates Division of TPEL between September 2008 and October 2010. The total brokerage generated for TPEL by these 17 wash trades was over £314,000.

4.73. Five brokers in the Rates Division (one of whom was a Desk Head) received unwarranted payments of brokerage through the arrangement of wash trades. These brokers sat on four different Desks in the Rates Division. A further four brokers (one of whom was a Divisional Director) were involved in the arrangement of these wash trades (although those four did not directly receive any improper brokerage from their clients).

4.74. The motivation of the five brokers at TPEL to arrange these wash trades was clear: to generate brokerage in order to improve the profitability of their books (which would ultimately feed into their own personal remuneration through bonus payments). The motivation of the traders at the banks who paid brokerage to TPEL through these wash trades included the receipt of entertainment and promises of assistance in the attempted manipulation of LIBOR (although such promises were not acted upon). Additionally, it appears that on occasion, brokerage may have been paid through wash trades as a "tip" from the trader to the broker.

4.75. By way of example, a wash trade was arranged on 16 February 2009. This involved two brokers at TPEL arranging for two traders at different banks to enter into two equal and opposite swaps trades. Both traders paid brokerage to their respective brokers. In this example, the motivation for the payment of brokerage by the traders was the broker's promise of assistance in the attempted manipulation of LIBOR on the part of one trader, and receipt of entertainment on the part of the other trader.

- On 10 February 2009, the following telephone conversation took place between one of the brokers and traders:

  Trader: *What I normally do is if I get help on the LIBORS over the month, I normally do, at the end of the month...a couple of like in and outs*

  Broker: *Alright mate, so that's good, because* [another trader] *wants to pay for his* [overseas] *trip already. So he's already been asking us about them anyway so yeah I'll be in touch later on in the month then*

- Then on 16 February 2009, a further communication between the same trader and broker took place via Bloomberg when the trader sought the broker's assistance in trying to manipulate LIBOR. The following exchange then took place:

  Trader: *we getting towards month end…so will cross some stuff up for you then …*

  Broker: [trader is] *back today and hes keen to do something as well*…[he] *wants to do that switch*

- Following this, later on 16 February 2009, the two brokers then proceeded to arrange a wash trade involving two banks. Both traders at the banks paid brokerage on the first trade totalling £35,977. Later that day, the second trade was executed cancelling out the first trade. One trader also paid brokerage on this second trade in the sum of £16,840. Thus, this wash trade had generated over £52,000 of brokerage for TPEL in total.

4.76. As noted at paragraph 4.51 above, two Senior Managers had noticed the large amount of brokerage being generated and asked the brokers involved about it. Despite the size of brokerage and the cryptic answers given by the brokers involved, no further action was taken to investigate these trades.

Improper brokerage paid on three-party switches

4.77. A three-party switch is a trade that takes place where two firms (Firm A and Firm B) want to enter into a trade, but for reasons such as credit limits, they are unable to trade with each other. Therefore, a third party (Firm C) is introduced to act as a counterparty to a trade with Firm A, and then an equal and opposite trade with Firm B. Thus, Firms A and B achieve the trade they want to carry out and Firm C ends up with a flat position.

4.78. In this situation, it would be expected that both Firm A and Firm B would pay brokerage on the trades in the normal way. It would not be appropriate for Firm C to pay any brokerage, as Firm C is assisting the other parties to facilitate their trade with no benefit to Firm C.

4.79. However, on occasion, a trader may proactively make a request to a broker that Firm C be interspersed into a transaction as a way of reducing its own credit risk to another firm. For example, if Firm C buys from Firm A and then sells to Firm B, it has a flat position but has reduced its credit exposure to Firm B. In this situation, Firm C may appropriately be charged brokerage because its participation in the trade is not a 'favour' but is beneficial to Firm C by reducing its credit risk to Firm B.

4.80. A number of three-party switches (or similar variations thereof) were arranged by six brokers on three different desks in the Rates Division between September 2008 and June 2011 where Firm C paid brokerage in circumstances where it should not have done so. Like wash trades, the role of Firm C in these transactions was sometimes used as mechanism for brokerage to be paid to TPEL in return for receipt of entertainment from brokers or as a favour to the broker or a tip.

4.81. The unwarranted brokerage paid to TPEL by way of these three-party switches amounted to around £76,000.

Improved trade price in return for lavish entertainment

4.82. On 24 October 2008, a broker from the overseas office contacted a broker in the Rates Division of TPEL ("Broker A") to ask whether Broker A could find a client willing to pay 15 basis points above the market price for a swap in order to clear a trading loss of £150,000 that the overseas office was potentially going to incur.

4.83. Broker A contacted a trader at a client bank ("Trader A") who agreed to enter into a swap and pay 10 basis points above the swap market price. This would have resulted in the overseas office reducing their potential loss from around £150,000 to £50,000.

4.84. Broker A then convinced Trader A to increase his price and buy the swap at 15 basis points above the swap market price in return for the overseas office paying for Trader A and Broker A's expenses during a 10-day trip to Las Vegas and California they had planned for the following month.

4.85. Trader A agreed to this higher price and the overseas office was thereby able to enter the trade and avoid the entire potential loss.

4.86. On the same day as Broker A had arranged this trade with Trader A, Broker A told a Senior Manager about the deal:

Broker A: *I've got some good news.*

Senior Manager: *Go on, go on, go on, tell me.*

Broker A:	*[the overseas office] fucking fucked some 6 month TONAR up today and basically everyone is going like "oh fuck"… we're stuffed at 40 in 30 yards, 6 months at 40. So they said "Can you get...", because they knew that [Trader B] had been doing me a few favours alright, "Can you get him to give us a dig out?" So he showed a 35 bid as a favour but he wouldn't…take a cheque…would have been a 51 grand cheque and then I said to him, and you might not want to hear this but, I said to him, "How about you just do it at 40 and we get [the overseas branch] to fund our trip to Vegas and LA, San Francisco and that" and he went …*

4.87. At this point, the Senior Manager interrupted Broker A and asked him whether Broker A's conversation with Trader A was on a recorded line ('*I hope you didn't say that to him down the line*'). Broker A then told the Senior Manager more about the deal that had been arranged:

Broker A:	*This is the deal, you guys fund my – pay for all the hotels, meals etc in LA, San Fran and Vegas and you can have the stuff at 40.*
Senior Manager:	*It's fucking great news but I don't want to know about it either*

4.88. The Senior Manager did not take any action in relation to this clear misuse of entertainment expenditure.

4.89. In November 2008, Broker A and Trader A went on a 10-day overseas trip to Las Vegas and California in which Broker A accrued over US$30,000 in expenses for himself and Trader A. These expenses included dinners in expensive bars and restaurants and the hire of two high performance sports cars.

4.90. In the months that followed the trip, several Senior Managers were told about the trip and expenses and given clear signals that the expenses may have been inappropriate due to their connection to a trade which avoided a loss event. Despite this, the matter was not investigated or escalated to Compliance and was not dealt with in accordance with the policies for this level of expenditure that were in place at the time.

4.91. The expenses for the trip were reimbursed to Broker A in late March 2009. The reimbursement was paid in three tranches of approximately US$10,000. Splitting the sum into three tranches avoided the need for higher level authorisation by the Tullett Group CEO.

PRINCIPLE 11

Overview

4.92. Principle 11 of the Authority's Principles for Businesses requires firms to deal with their regulators in an open and cooperative way, and to disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice.

4.93. The Principle 11 Relevant Period is 15 August 2011 to 31 October 2014.

4.94. The following events are described in more detail below:

- TPEL failed to provide audio recordings that the Authority had required it to produce and gave the Authority incorrect information about TPEL's ability to produce audio recordings; and

- There was a dilatory delay in TPEL notifying the Authority that it was able to produce these audio recordings and an incorrect explanation was given to the Authority as to the circumstances in which the audio had come to the attention of the Legal and Compliance Departments.

<u>Background to Principle 11 breaches</u>

4.95. At the start of the Principle 11 Relevant Period, TPEL's policy was to keep audio recordings for 12 months, after which time the audio could be destroyed.

4.96. TPEL used an audio recording platform whereby recordings of brokers' telephone calls were stored on physical tape cassettes until early 2012. From February 2012 onwards, TPEL changed to a fully digitised audio recording platform.

4.97. TPEL had a Voice Communications Department that was responsible for, among other things, ensuring that the audio recording platform operated properly, storing the audio recordings and maintaining records of the audio recordings.

4.98. During 2011, the Authority and other law enforcement agencies were conducting enquiries and investigations into suspected LIBOR misconduct at various firms. An important source of information that the Authority required were communications between traders and brokers, including email correspondence, Bloomberg and Reuters messages, as well audio recordings of telephone calls made and received by traders and brokers.

<u>Failure to provide audio and provision of inaccurate information to the Authority</u>

The First Information Requirement

4.99. On 15 August 2011, the Authority visited TPEL's office ("the Visit") and served an information requirement on TPEL pursuant to the Authority's statutory powers to compel the production of information ("the First Information Requirement"). TPEL was not under investigation at this time; the First Information Requirement was made in the context of a LIBOR related investigation into a separate investigation subject.

4.100. The First Information Requirement sought various broker communications from TPEL, including all audio recordings of telephone calls made and received by Broker B between 1 January 2007 and 1 October 2010 ("Broker B's Audio Recordings").

4.101. Members of TPEL's Legal and Compliance Departments liaised with the Authority during the Visit, including Senior Manager A. The Authority was informed during the Visit that TPEL operated a 12-month audio deletion policy and that, accordingly, TPEL was unable to provide Broker B's Audio Recordings because such audio was only retained from September 2010 onwards.

4.102. This information given to the Authority regarding the availability of Broker B's Audio Recordings was incorrect. Whilst it was correct that there was a 12-month audio deletion policy, the Voice Communications Department in fact retained the majority of the audio recordings of TPEL's London brokers from 1 January 2006 onwards, thus including the majority of Broker B's Audio Recordings.

4.103. The fact that TPEL held these audio recordings was not known to the Legal and Compliance Departments at the time of the Visit. However, it was known to TPEL's Voice Communications Department at this time (and at all times throughout the P11 Relevant Period).

4.104. Neither on the date of the Visit, nor at any other time thereafter, did anyone at TPEL involved in liaising with the Authority over the First Information Requirement ask the Voice Communications Department whether Broker B's Audio Recordings were available. Instead, TPEL proceeded on the basis that the requested audio had been deleted pursuant to its audio deletion policy.

4.105. On the day of the Visit, shortly after the Authority had been informed that TPEL was unable to provide Broker B's Audio Recordings, Senior Manager A asked a manager in the Voice Communications Department to determine the number of tapes that contained Broker B's telephone calls for 2010. The Voice Communications Department manager advised Senior Manager A, by email, that for the period 1 January 2010 to 31 December 2010 there were 64 tapes that contained Broker B's telephone calls, 51 of which were for the period January to September 2010. It therefore should have been clear to Senior Manager A by 12.30pm on the day of the Visit that the 12-month audio deletion policy had not been applied to Broker B's telephone calls; he had been told in the email that audio for Broker B was available from at least January 2010, and not September 2010 as the Authority had been told.

4.106. Despite Senior Manager A receiving an email on the day of the Visit that Broker B's telephone calls were available from January 2010, the inaccurate information given to the Authority earlier that day was not corrected (*i.e.,* TPEL did not inform the Authority that Broker B's calls were available from January 2010 rather than from September 2010).

4.107. Furthermore, even though Senior Manager A was on notice that the 12-month audio deletion policy had not been applied in relation to Broker B's calls, at no time did he or anyone else make any enquiries of the Voice Communications Department to find out whether any further audio for Broker B was available prior to 2010.

4.108. If steps had been taken to check the position with the Voice Communications Department, it would have been established that the majority of Broker B's Audio Recordings (along with audio of other London Brokers dating back to 2006) were in fact retained by TPEL.

The Second Information Requirement

4.109. In the context of the continuing enquiries and investigations into suspected LIBOR misconduct, in March 2012, the Authority contacted TPEL's Legal Department seeking communications of three other TPEL Brokers ("the Cash Brokers") for the period 1 January 2009 to 31 October 2009.

4.110. In the first instance, on 29 March 2012, the Authority discussed by telephone with Senior Manager A the availability of the communications of the Cash Brokers, including their audio recordings. As was explained to Senior Manager A, the purpose of this discussion was for the Authority to scope an information requirement to TPEL regarding the Cash Brokers' communications.

4.111. During the course of this telephone conversation, the Authority asked Senior Manager A to confirm whether TPEL was able to produce audio recordings of the telephone calls made and received by the Cash Brokers during 2009. The Authority asked for this confirmation because in response to the First Information Requirement, TPEL had told the Authority that it was unable to provide Broker B's

Audio Recordings as all audio was destroyed after 12 months due to the firm's 12-month audio deletion policy. Senior Manager A agreed to check and confirm the position to the Authority.

4.112. Even though Senior Manager A was on notice that TPEL did in fact have Broker B's Audio Recordings for more than 12 months (from January 2010, not from September 2010 onwards as the Authority had previously been told), the Authority was still not told that these further Broker B audio recordings existed.

4.113. Senior Manager A sent Senior Manager B an email summarising his call with the Authority and asking that the Compliance Department deal with the request as he was going on holiday. He noted in this email as follows:

> "[The Authority] *also asked about phone records and said that he was enquiring whether we had phone records for the period '09. On the basis that we did not have records for* [Broker B] *for the period'10 he thought It unlikely but was asking all the same. I said l would check*."

4.114. The following day, 30 March 2012, the Authority sent TPEL an email attaching a statutory information requirement which sought the communications of the Cash Brokers ("the Second Information Requirement"). This was sent by email to Senior Manager A. In the email attaching the Second Information Requirement, the Authority stated:

> *"… you will note that I have not referred to taped telephone lines, as my understanding is that Tulletts do not hold any taped line recordings pre-September 2010. Can you please confirm that this is the case in respect of the three cash brokers referred to in the* [Second Information Requirement]."

4.115. Senior Manager A forwarded the email and the attached Second Information Requirement to Senior Manager B in order for the Compliance Department to oversee TPEL's response. The Compliance Department complied a response, but did not take any steps to establish whether TPEL had audio recordings of telephone calls prior to September 2010.

4.116. Once the Compliance Department had completed the response to the Second Information Requirement, Senior Manager A then sent TPEL's response to the Authority. The response was provided on 26 April 2012. The Compliance Department did not take any steps to check as to the availability of the Cash Broker audio recordings and Senior Manager A did not check to see if this point had been dealt with.

4.117. Therefore, no steps were taken to find out if the Cash Brokers' audio was available; no contact was made with the Voice Communications Department to confirm the position. If the Voice Communications Department had been asked, it would have been confirmed that historic broker audio dating back to 2007 was available.

4.118. Accordingly, the Authority continued with its LIBOR-related enquiries on the basis of the inaccurate information it had previously been given by TPEL in response to the First Information Requirement, namely that TPEL only had audio recordings from September 2010 in accordance with its 12-month audio deletion policy.

<u>Delay in notifying the Authority about the existence of audio recordings and incorrect explanations provided</u>

4.119. Between February and May 2012, TPEL transferred from the old audio recording platform to the new digitised platform. In conjunction with the new platform being installed, TPEL's Legal and Compliance Departments conducted a review of TPEL's record keeping obligations. They concluded that TPEL's record keeping obligations in respect of audio recordings of telephone calls was six months.

4.120. As a result of the review of the record keeping obligations, on 16 July 2013, Senior Manager B emailed the Voice Communications Department and asked for confirmation that the new recording platform would keep audio recordings for "*the required six months period – no longer and no shorter*." This email was copied to Senior Manager A.

4.121. On 18 July 2013, a manager in the Voice Communications Department responded to Senior Manager B's email (with Senior Manager A copied into the response):

> *"Please can you confirm that I can destroy all previous recordings that we have from 2007 – Jan 2012 which are* [stored] *on tapes."*

4.122. This email put both Senior Manager A and Senior Manager B on notice that TPEL had audio recordings of brokers' telephone calls from 2007 to 2012. Senior Manager A and Senior Manager B knew that historic broker audio recordings were relevant to regulatory investigations. The Voice Communications Department was accordingly instructed by Senior Manager A not to destroy the audio recordings and to arrange for the tapes be sent to the Legal Department. The Facilities Department undertook the physical relocation of the tapes to the Legal Department.

4.123. Once the Legal Department had the tapes, checks were carried out to find out what audio was on the tapes. It transpired that tapes contained the audio recordings of the majority of TPEL's London brokers for the period 1 January 2006 to 31 December 2011. These checks were completed by October 2013 at the latest, thus by this date the Legal Department was aware that at least some of Broker B's Audio Recordings were available.

4.124. On 14 October 2013, Senior Manager A notified another law enforcement agency (which was also conducting enquiries into suspected LIBOR misconduct) that TPEL had located audio recordings covering the period 1 January 2006 to 31 December 2011. An email sent by Senior Manager A to the agency provided the following explanation:

> *"The tapes had been left at the back of the main broking floor in a series of boxes along with a number of other items. Following an office clear out these boxes were identified as relating to the old voice recording system and have now been moved over to* [the Legal Department]."

4.125. This account given of the circumstances surrounding the discovery of the audio recordings was incorrect. The boxes had not been identified following an "office clear out" and this explanation created the impression that the existence of the audio recordings was previously unknown within TPEL. However, the Voice Communications Department had known all along that this audio existed, but had not been asked about it. The audio had also come to the attention of the Legal and Compliance Departments as a result of the email from a manager in the Voice Communications Department in July 2013; it had not been discovered during an office clear out.

4.126. Despite ongoing interactions with the Authority throughout 2013 regarding LIBOR investigations, TPEL did not notify the Authority regarding the discovery of historic broker audio tapes until 30 April 2014. This notification was thus finally given to the Authority nine months after the Voice Communications Department had emailed the Legal and Compliance Departments about the existence of historic audio recordings and six months after the Legal Department knew that at least some of Broker B's Audio Recordings were available. Nearly three years had passed since service of the First Information Requirement asking for this audio.

4.127. Notification of the existence of Broker B's Audio Recordings was initially given to the Authority in an email from a Senior Manager B. The email gave the same incorrect explanation that tapes containing the audio recordings had been "*discovered in July/August last year following an office clear out.*"

4.128. On 27 June 2014, Senior Manager B reiterated the incorrect account of the discovery of the audio tapes to the Authority by email (also copied to Senior Manager A and another Senior Manager in the Legal Department), stating that:

> *"During 2013 Tullett Prebon was completing the transfer from its old analogue* [voice recording] *system to its digital system and the tapes* [were] *no longer required. There* [were] *24 boxes … and theses were due to be disposed of during an office clear out in August 2013. Facilities, who were dealing with the clear out notified compliance and legal and these are now stored in the legal department."*

4.129. These explanations were again incorrect and suggested that 24 boxes of tapes had been discovered 'by chance', whereas the Voice Communications Department had in fact retained the tapes and had brought the tapes to the attention of the Compliance and Legal departments over nine months earlier.

4.130. TPEL eventually disclosed to the Authority the correct circumstances surrounding the discovery of the audio recordings on 31 October 2014 in response to a request for information from the Authority as to how the audio was discovered, made pursuant to its statutory powers. In this later correspondence, TPEL did not explain or otherwise address the previous incorrect statements TPEL had provided to the Authority about discovering the audio following an office clear out. Senior Manager A later explained that the accounts given to the Authority and the other law enforcement agency were based on his incorrect assumption that Facilities had discovered the tapes, because it was Facilities that moved the tapes to the Legal Department, and that the discovery of the tapes must have been as a result of an office clear out.

4.131. As a result of TPEL's disclosure of Broker B's Audio Recordings, on 24 July 2014 the Authority commenced an Enforcement investigation into TPEL's conduct which included an investigation into improper trades arranged by TPEL's Brokers.

5. FAILINGS

5.1. The regulatory provisions relevant to this Notice are referred to in Annex A.

PRINCIPLE 2 AND PRINCIPLE 3 FAILINGS

5.2. Principle 2 requires a firm to conduct its business with due skill, care and diligence.

5.3. Principle 3 requires a firm to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

5.4. Section 4 of this notice has divided the facts and matters giving rise to the failings into three areas: monitoring, compliance responsibilities and controls around entertainment expenditure. The facts and matters in each of these areas contributes both to the breach of Principle 2 and the breach of Principle 3, as detailed further below.

5.5. These breaches arise in the context of the name passing business where there was a risk of improper broker conduct, in particular because of the close relationships that were encouraged between brokers and traders, together with the provision of significant allowances for the entertainment of traders and the way in which broker bonuses were calculated. The Compliance Department and certain Senior Managers within the Rates Division failed to act with due skill, care and diligence, giving rise to a breach of Principle 2. Inadequate systems and controls were in place to deal with the risk of improper broker conduct, giving rise to a breach of Principle 3.

Breach of Principle 3

5.6. The limited systems and controls that were applicable to the Rates Division of TPEL were inadequate, ineffective and in practice were not used to address the risk of broker misconduct.

Monitoring system

5.7. The BRS was a system that could have been used to carry out some monitoring of brokerage generated on the name passing desks in the Rates Division for the purpose of addressing the risk of broker misconduct. However, the system was not used for monitoring in this way because there were no systems or processes which (i) implemented the use of the BRS to monitor brokerage for this purpose or (ii) checked that the system was being used for monitoring purposes. No explanations or training were given to Senior Managers to set out how they were expected to use the BRS to control risk, there were no policies or procedures in place for Senior Managers to follow and there was no other mechanism through which the Senior Managers were made aware of a requirement for them to monitor brokerage generated from a risk perspective. Furthermore, there was no procedure or system in place for Compliance to check that monitoring was being effectively carried out. Thus, whilst a system was in place that could have been used for monitoring, TPEL did not take reasonable care to implement the system or check the system was being used as expected and it therefore did not operate as an adequate risk management system. As a result of this failing, there was no effective monitoring of name passing broking activity for the purpose of dealing with the risk of broker misconduct.

'First line of defence'

5.8. There was a governance structure in place within the Rates Division comprising Divisional Directors and Desk Heads. It was intended that the Divisional Directors take on compliance responsibilities in overseeing broker conduct on the desks for which they had responsibility. The Divisional Directors signed a "Statement of Responsibilities" in 2009 which purported to give them joint compliance responsibilities with the other directors. However, no explanations or training was given as to how they were expected to carry out this responsibility in practice, there were no policies or procedures in place for them to follow and there was an extremely limited relationship between the Compliance Department and the business. Furthermore, there were no systems in place to check that attention was being paid to compliance issues and risk, or to check how risk was being managed within the business. As such there was ignorance on the part of the Divisional Directors as to what was expected of them and the intended 'first line of defence' failed.

Entertainment expenditure

5.9. Systems to control the risk arising from the abuse of entertainment expenditure comprised the policies and guidance set out in the ECF, the Compliance Manual and the Staff Handbook. However, each of these was inadequate in that they were very high level and did not provide sufficient detail to enable them to be used effectively in practice as a risk control mechanism. Furthermore, there was no effective system in place to monitor expenditure on entertainment from a compliance perspective. The Compliance Department had no involvement in monitoring entertainment expenditure at all and, to the extent this was monitored elsewhere, the monitoring focussed on cost control and paid no attention to compliance or risk of abuse. Thus, there were no systems or controls in place to consider entertainment expenditure from the perspective of risk relating to broker conduct.

<u>Breach of Principle 2</u>

5.10. The Compliance Department was the central function with responsibility for ensuring adequate controls around broker conduct were in place at TPEL. There were clear risks inherent within the name passing business of improper broker conduct, including the risk that brokers and traders may act together to generate unwarranted brokerage (for example, in return for enhanced entertainment or other favours being provided to the trader). Nevertheless, the Compliance Department failed to act with due skill, care and diligence in dealing with risk in the name passing business:

- The Compliance Department assumed for three years that the BRS was being used to monitor brokerage from a risk perspective, but this assumption was wrong. This assumption was not justified given there was nothing in place to embed the use of the BRS for this purpose or to check it was being used for this purpose. Compliance was passive in its approach to ensuring this intended control was effective within the name passing business and instead focussed its attention on other risks in other areas.

- Compliance did not take sufficient care to communicate with the name passing business on compliance issues or establish an effective working relationship with Senior Managers. Having put in place a high-level and vague statement regarding Divisional Directors general compliance responsibilities, it then took no steps to embed this as an effective measure in practice. Nothing was done by Compliance to check that the Divisional Directors understood and were fulfilling their intended compliance roles within the business. Instead, Compliance operated on the basis of a very limited relationship with the name passing business because it considered it to be low risk.

5.11. Certain Senior Managers in the Rates Division also failed to act with due skill, care and diligence.

- On several occasions, 'red flags' signalled a blatant risk of improper broker conduct direct to Senior Managers. In response, they failed to act with due skill or care in assessing the risks that were apparent. The focus of the Senior Managers was on the generation of revenue for the business. They did not take sufficient steps to understand the circumstances behind unusually large brokerage payments, even when the brokers' response to initial questions was highly suspicious (for example "*you don't want to know*").

- The lack of due skill, care and diligence of certain Senior Managers was also apparent from the way in which expenses of over US$30,000 were dealt with. These expenses were linked to a 'deal' between a TPEL broker and a trader whereby the trader would increase the price of a trade to benefit the Tullett

Group in return for expenses being paid on a lavish overseas trip. One Senior Manager was expressly on notice that the expenses were connected to a trade price agreed with a client bank, yet did nothing. Other Senior Managers failed to deal properly with these expenses when bought to their attention and did not escalate the issue to Compliance when it was clearly appropriate for them to do so.

Crystallisation of risk

5.12. As set out in the Facts and Matters section of this Notice, certain brokers in the Rates Division carrying out name passing business acted with traders to arrange improper trades to generate unwarranted brokerage payments for TPEL. This improper conduct was undertaken by seven brokers across four Desks within the Rates Division and took place over nearly three years. This generated a significant amount of unwarranted brokerage for TPEL.

5.13. If there had been effective systems and controls around this part of the business, and if Compliance and Senior Managers had acted with due skill, care and diligence, then it is at least likely that some or all of the improper conduct of the brokers would either have been prevented in the first place, or would have been identified and stopped.

PRINCIPLE 11 FAILINGS

5.14. Principle 11 of the Authority's Principles for Businesses requires firms to deal with their regulators in an open and cooperative way, and to disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice.

5.15. The facts and matters set out above give rise to a number of different issues contributing to a breach of Principle 11 by TPEL.

Failure to provide audio and provision of inaccurate information to the Authority

5.16. Senior Manager A was involved in telling the Authority on 15 August 2010 that TPEL did not retain any audio older than 12 months in response to the First Information Requirement. Senior Manager A then found out that same day from the Voice Communications Department that TPEL had audio for Broker B from January 2010 (not September 2010 as per TPEL's 12-month audio deletion policy). Senior Manager A did not correct the inaccurate information given to the Authority as to the availability of Broker B's audio, nor were any checks carried out to find out if further audio was available for earlier periods.

5.17. This failure to correct the inaccurate information that had been provided to the Authority and failure to check as to the availability of any earlier audio demonstrates a clear failure to be open and cooperative with the Authority, and to disclose to the Authority appropriately information of which the Authority reasonably expected notice.

5.18. The Authority's later question to TPEL in March 2012 about the availability of the Cash Brokers' audio from 2009 reflected the Authority's understanding that the earliest audio recordings of broker telephone calls held by TPEL were from September 2010. The Authority's understanding was based on TPEL's response to the First Information Requirement.

5.19. Despite the Authority directly asking for checks to be undertaken as to the availability of the Cash Brokers' audio both by telephone and by email, no such checks were carried out. This is a clear breach of Principle 11 and left the Authority proceeding on the incorrect basis that no broker audio was available prior to September 2010. Of particular concern are the following aspects:

- Senior Manager A was the person that the Authority spoke to and emailed questioning what audio was available and asking for checks to be carried out. This direct question about the existence of audio prior to September 2010 did not prompt Senior Manager A to tell the Authority that TPEL had audio for Broker B for 2010, not only from September 2010 as it had previously been informed. This is particularly troubling as the Authority specifically linked its query about the availability of the Cash Brokers' audio to its understanding that TPEL could not provide Broker B's Audio Recordings prior to September 2010.

- The Authority's request was passed to the Compliance Department, but no checks were carried out to see if TPEL had the Cash Brokers' audio from 2009 notwithstanding the express assurance given to the Authority that this would be done. The Compliance Department overlooked this aspect of the Authority's email and the Legal Department never checked to find out if this point had been dealt with.

<u>Delay in notifying the Authority about the existence of audio recordings and incorrect explanations provided</u>

5.20. TPEL's delay in notifying the Authority about the discovery of the audio recordings of brokers' calls is a further aspect of the Principle 11 breach.

5.21. The discovery of the audio calls was certainly a matter of which the Authority expected notice. TPEL's failure to inform the Authority about the audio recordings between July 2013 and April 2014 (9 months) is a clear breach of Principle 11. In particular, from October 2013, TPEL was aware of the existence of broker audio, including that of Broker B, yet it still failed to give notice of this to the Authority until April 2014.

5.22. This aspect of the Principle 11 breach is made significantly worse due to the incorrect account then given to the Authority regarding the circumstances in which the audio had come to the attention of the Legal and Compliance Departments. TPEL's explanation that the audio recordings had been discovered by Facilities following an office clear out was wrong and created the incorrect impression that nobody at TPEL was previously aware of the existence of the audio recordings and that they had been discovered by chance.

5.23. Senior Managers A and B in the Legal and Compliance Departments had directly received the email from the Voice Communications Department manager on 18 July 2013 which expressly told them about the existence of audio recordings from 2007. They each understood from this email that broker audio dating back to 2007 had been retained and, as a result, Senior Manager A took steps to preserve the audio and move the audio tapes to the Legal Department where they were reviewed. Nevertheless, an incorrect explanation was provided to the Authority and another law enforcement agency as to how they had become aware of the audio. Even though the explanation was not intended to be misleading, this aspect of the Principle 11 breach demonstrates serious deficiencies at the time in TPEL's approach and attitude toward regulatory disclosures.

6. SANCTION

6.1. The Authority has concluded that a financial penalty is the appropriate sanction in the circumstances of this case.

6.2. The calculation of the penalties in relation to the breach of Principle 2, Principle 3 and Principle 11 is explained below. The penalty for the breach of Principle 2 and Principle 3 together is £10.5 million. The penalty for the breach of Principle 11 is £4.9 million. This results in a total penalty of £15.4 million.

PRINCIPLE 2 AND PRINCIPLE 3 PENALTY

6.3. The conduct in issue took place both before and after 6 March 2010. As set out at paragraph 2.7 of the Authority's Policy Statement 10/4, when calculating a financial penalty where the conduct straddles penalty regimes, the Authority must have regard to both the penalty regime which was effective before 6 March 2010 ("the old penalty regime") and the penalty regime which was effective after 6 March 2010 ("the current penalty regime").

6.4. The Authority has adopted the following approach:

- Calculated the financial penalty for TPEL's breach of Principles 2 and 3 from September 2008 to 5 March 2010 under the old penalty regime;
- Calculated the financial penalty for TPEL's breach of Principles 2 and 3 from 6 March 2010 to September 2013 under the current penalty regime;
- Added the penalties calculated to produce a total financial penalty for breach of Principles 2 and 3.

<u>Financial penalty under the old penalty regime</u>

6.5. The Authority's policy for imposing a financial penalty under the old penalty regime is set out in Chapter 6 of DEPP as was in force from 27 March 2007 to 5 March 2010. All references to DEPP in paragraphs 6.7-6.15 below, are references to this prior version.

6.6. The Authority has also had regard to the corresponding provisions of Chapter 7 of the Authority's Enforcement Guide in force at the time of the old penalty regime.

Deterrence (DEPP 6.5.2(1))

6.7. A significant penalty will help to promote high standards of regulatory and market conduct, by deterring TPEL from committing any future breaches of Principles 2 and 3 and helping to deter other inter-dealing broking firms from committing similar breaches, as well as demonstrating generally the benefits of compliant business.

The nature, seriousness and impact of the breach (DEPP 6.5.2(2))

6.8. The Authority considers TPEL's breach of Principles 2 and 3 to be serious for the following reasons:

- Core aspects of the breaches were continuous over a period of 18 months;

- There were a number of separate instances of lack of due skill, care and diligence by Senior Managers contributing to the Principle 2 breach over that period;

- The breaches concerned serious and systemic weaknesses in TPEL's systems and controls concerning a large part of its business;

- The breaches resulted in risk of loss to other market users (e.g. through unwarranted brokerage being paid to TPEL by its clients). Significant unwarranted brokerage was generated by brokers at TPEL and this is likely to have been prevented if there had been adequate systems and controls in place at TPEL around broker conduct.

- The breaches gave rise to the risk of financial crime.

The extent to which the breach was deliberate or reckless (DEPP 6.5.2(3))

6.9. Certain aspects of the breach of Principle 2 were reckless (in that Senior Managers at TPEL appreciated there was a risk that their actions or inaction could result in a breach and failed to adequately mitigate that risk – DEPP 6.5A.2(9)(a)). The Senior Managers that were aware of large brokerage payments and then told "*you don't want to know*" were reckless as they must have appreciated the possibility of risk, but took no action. The Senior Manager who was directly told of the 'deal' between the broker and trader to deal with the loss event was also reckless in failing to take any action once he had learned that entertainment expenses were being used to improve the price of a trade.

The size, financial resources and other circumstances of the person on whom the penalty is to be imposed (DEPP 6.5.2(5))

6.10. The degree of seriousness of the breach may be linked to the size of the firm. Breaches in firms with a high volume of business over a protracted period may be more serious than breaches over similar periods in firms with a smaller volume of business. TPEL was the second largest inter-dealer broker (globally) at the time of the breach, conducting significant volumes of business in the wholesale markets and generating significant revenue.

The amount of benefit gained or loss avoided (DEPP 6.5.2(6))

6.11. There was no direct benefit gained by TPEL, however, if adequate systems and controls had been in place it is likely that at least some of the wash trades and three-party switches which generated unwarranted brokerage would have been prevented.

Conduct following the breach (DEPP 6.5.2(8))

6.12. Since the commencement of the Authorities investigation into TPEL (which post-dates the facts and matters giving rise to the Principle 11 breach), TPEL has co-operated with the investigation. TPEL also conducted its own review of the circumstances around the wash trades and disclosed that review to the Authority in advance of the Authority commencing its investigation of TPEL.

Disciplinary record and compliance history (DEPP 6.5.2(9))

6.13. TPEL has not previously been the subject of an adverse finding by the Authority.

Conclusions in relation to the old penalty regime

6.14. The Authority considers that the seriousness of TPEL's breach merits a financial penalty. In determining the financial penalty, the Authority has considered the need to send a clear message to the industry regarding the need to ensure adequate systems and controls are in place.

6.15. The Authority has therefore decided to impose a financial penalty under the old penalty regime of £5.525 million (£7.5 million before application of a 30% penalty discount for agreeing to resolve this matter).

<u>Penalty under the current penalty regime</u>

6.16. Under the current penalty regime, the Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5A sets out the details of the five-step framework that applies in respect of financial penalties imposed on firms.

Step 1: disgorgement

6.17. Pursuant to DEPP 6.5A.1G, at Step 1 the Authority seeks to deprive a firm of the financial benefit derived directly from the breach where it is practicable to quantify this.

6.18. The Authority has not identified any financial benefit that TPEL derived directly from its breach.

6.19. Step 1 is therefore £0.

Step 2: the seriousness of the breach

6.20. Pursuant to DEPP 6.5A.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breach. Where the amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breach may cause, that figure will be based on a percentage of the firm's revenue from the relevant products or business area.

6.21. The Authority considers that the revenue generated by the Rates Division of TPEL is indicative of the harm or potential harm caused by its breach. The Authority has therefore determined a figure based on a percentage of the Rates Division's relevant revenue. The Rates Division's relevant revenue is the revenue derived by the Rates Division during the period of the breach (under the current penalty regime). The period of the breach was from 6 March 2010 to September 2013. The Authority considers the Rates Division's relevant revenue for this period to be £574,000,000.

6.22. In deciding on the percentage of the relevant revenue that forms the basis of the step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 20%. This range is divided into five fixed levels which represent, on a sliding scale, the seriousness of the breach; the more serious the breach, the higher the level. For penalties imposed on firms there are the following five levels:

Level 1 – 0%

Level 2 – 5%

Level 3 – 10%

Level 4 – 15%

Level 5 – 20%

6.23. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, and whether it was committed deliberately or recklessly. Relevant factors are set out at DEPP 6.5A.2G(6)-(9). Of these, the Authority considers the following factors to be relevant:

- Impact: the inadequate systems and controls gave rise to the risk of loss to other market users.
- Impact: the breach had an adverse effect on confidence in the market in question through the existence of unwarranted brokerage generated through broker-trader relationships which risked infecting the wider market.
- Nature: the breach persisted over a period of 43 months.
- Nature: the breach revealed serious and systemic weaknesses in the firm's systems and controls.
- Nature: the breach gave rise to the risk of financial crime.

6.24. DEPP 6.5A.2G(11) then sets out factors that are likely to be considered 'level 4 or 5 factors'. Of these, the Authority considers the following factors to be relevant:

- The breach gave rise to a risk of loss to other market users.
- The breach revealed serious and systemic weaknesses in the firm's systems and controls.
- The breach gave rise to the risk of financial crime.

6.25. DEPP 6.5A.2G(12) lists factors likely to be considered 'level 1, 2 or 3 factors'. Of these, the only factor which is relevant is that the Authority considers the breach was a result of negligence, rather than committed deliberately or recklessly.

6.26. Taking all of these factors into account, the Authority considers the seriousness of the breach to be level 4. The Step 2 figure is therefore 15% of the relevant revenue, resulting in a penalty of £86,100,000.

6.27. DEPP 6.5.3(3) provides that the Authority may decrease the level of penalty arrived at after applying Step 2 of the framework if it considers that the penalty is disproportionately high for the breach concerned.

6.28. The Authority considers that a penalty of £86,100,000 is disproportionately high for the breach concerned. In order to achieve a penalty that (at Step 2) is proportionate to the breach, the Step 2 figure is reduced to £7.5 million.

6.29. Step 2 is therefore £7.5 million.

Step 3: mitigating and aggravating factors

6.30. Pursuant to DEPP 6.5A.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including any amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breach. The Authority does not consider there to be any aggravating or mitigating factors.

6.31. Step 3 is therefore £7.5 million.

Step 4: adjustment for deterrence

6.32. Pursuant to DEPP 6.5A.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.

6.33. The Authority considers that the Step 3 figure of £10 million represents a sufficient deterrent to TPEL and others, and so has not increased the penalty at Step 4.

6.34. Step 4 is therefore £7.5 million.

Step 5: settlement discount

6.35. Pursuant to DEPP 6.5A.5G, if the Authority and the firm on whom a penalty is to be imposed agree the amount of the financial penalty and other terms, DEPP 6.7 provides that the amount of the financial penalty which might otherwise have been payable will be reduced to reflect the stage at which the Authority and the firm reached agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.

6.36. The Authority and TPEL reached agreement at Stage 1 and so a 30% discount applies to the Step 4 figure.

6.37. Step 5 is therefore £5.525 million.

<u>Total Proposed penalty for breach of Principles 2 and 3</u>

6.38. The Authority hereby imposes a total financial penalty of £10.5 million on TPEL for breaching Principle 2 and Principle 3 (£15 million before the 30% discount for settlement).

PRINCIPLE 11 PENALTY

6.39. The Principle 11 Relevant Period falls after 6 March 2010 so the Authority has considered the current version of DEPP in determining the appropriate penalty.

Step 1: disgorgement

6.40. Pursuant to DEPP 6.5A.1G, at Step 1 the Authority seeks to deprive a firm of the financial benefit derived directly from the breach where it is practicable to quantify this. The Authority has not identified any financial benefit that TPEL derived from the Principle 11 breach.

6.41. Step 1 is therefore £0.

Step 2: the seriousness of the breach

6.42. Pursuant to DEPP 6.5A.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breach. Where the amount of revenue generated by a firm from a particular product line or business area is indicative of the harm or potential harm that its breach may cause, that figure will be based on a percentage of the firm's revenue from the relevant products or business area.

6.43. The Authority considers that the revenue generated by TPEL is not an appropriate indicator of the harm or potential harm caused by its breach of Principle 11 and there is no alternative indicator of harm or potential harm. Pursuant to DEPP 6.5A.2G(13), the Authority has determined the appropriate Step 2 amount by taking into account those factors which are relevant to an assessment of the level of seriousness of the breach.

6.44. In assessing the seriousness level, the Authority takes into account various factors which reflect the impact and nature of the breach, and whether it was committed deliberately or recklessly.

6.45. With regard to the impact and nature of the breach, the Authority considers the following factors to be relevant:

- The requirement on firms to deal with their regulator openly and cooperatively is a central element of the Authority's regulatory regime. TPEL failed to act openly and cooperatively on a number of occasions over a period of more than three years in the context of the Authority's enquiries related to LIBOR investigations.

- Proper compliance with statutory information requirements is fundamental to the Authority's approach to investigations which is important to its Enforcement and Supervisory functions. TPEL's Principle 11 breach undermined the effectiveness of this key investigative tool.

- If TPEL had provided a full and accurate response to the First Information Requirement and understood that Broker audio recordings were in fact available, it is highly likely that this would have led to further enquiries.

- Senior managers were involved in central aspects of the Principle 11 breach.

6.46. With regard to whether the breach was reckless or deliberate, the Authority accepts that the breach was not deliberate, nevertheless central aspects of the Principle 11 breach were reckless:

- Senior Manager A proceeded on the basis of an incorrect assumption that audio was only retained for 12 months after receiving an email informing him that Broker B's audio recordings had been retained for longer than 12 months;

- Senior Manager A wrongly assumed that Facilities had found audio tapes as a result of an office clear out based on the fact that Facilities physically moved the audio tapes from the Voice Communications Department to the Legal Department. He provided incorrect explanations to the Authority and another law enforcement agency as to how the audio had been 'discovered' on the basis of this incorrect assumption, without undertaking any checks to verify that this explanation was correct.

6.47. In making these assumptions, Senior Manager A must have appreciated there was a risk that incorrect information of an important nature was given to the Authority, especially given he carried out no checks to confirm whether the information given to the Authority was correct.

6.48. DEPP 6.5AG(11) lists factors that are likely to be considered "level 4 or 5 factors", one of which is that the breach was committed recklessly.

6.49. DEPP 6.5AG(12) lists factors that are likely to be considered 'level 1-3 factors': no profit was made or loss avoided; no loss or a risk of loss to consumers, investors or other market users; no effect or potential effect on the orderliness or confidence in the markets; no indication of widespread problems or weaknesses at the firm; and where the breach was committed negligently or inadvertently. Whilst some of these factors are applicable, compliance with Principle 11 is a fundamental plank of the regulatory regime and a breach of Principle 11 of this nature is inherently serious.

6.50. Taking all of the above into account, the Authority considers the overall seriousness of the Principle 11 breach to be level 4.

6.51. The Step 2 figure is £7 million.

Step 3: mitigating and aggravating factors

6.52. Pursuant to DEPP 6.5A.3G, at Step 3 the Authority may increase or decrease the amount of the financial penalty arrived at after Step 2, but not including any amount to be disgorged as set out in Step 1, to take into account factors which aggravate or mitigate the breach.

6.53. The Authority does not consider that there are any factors which aggravate or mitigate the breach.

6.54. Step 3 is therefore £7 million.

Step 4: adjustment for deterrence

6.55. Pursuant to DEPP 6.5A.4G, if the Authority considers the figure arrived at after Step 3 is insufficient to deter the firm who committed the breach, or others, from committing further or similar breaches, then the Authority may increase the penalty.

6.56. The Authority considers that the Step 3 figure of £7 million represents a sufficient deterrent to TPEL and others, and so has not increased the penalty at Step 4.

6.57. Step 4 is therefore £7 million.

Step 5: settlement discount

6.58. Pursuant to DEPP 6.5A.5G, if the Authority and the firm on whom a penalty is to be imposed agree the amount of the financial penalty and other terms, DEPP 6.7 provides that the amount of the financial penalty which might otherwise have been payable will be reduced to reflect the stage at which the Authority and the firm reached agreement. The settlement discount does not apply to the disgorgement of any benefit calculated at Step 1.

6.59. The Authority and TPEL reached agreement at Stage 1 and so a 30% discount applies to the Step 4 figure.

6.60. Step 5 is therefore £4.9 million.

Proposed penalty

6.61. The Authority hereby imposes a financial penalty of £4.9 million on TPEL for breaching Principle 11.

7. PROCEDURAL MATTERS

This Notice is given to TPEL under section 206 of the Act and in accordance with the section 387 of the Act.

7.1. The following statutory rights are important.

Decision maker

7.2. The decision which gave rise to the obligation to give this Notice was made by the Settlement Decision Makers.

Manner and time for payment

7.3. The financial penalty must be paid in full by TPEL to the Authority no later than 25 October 2019.

If the financial penalty is not paid

7.4. If all or any of the financial penalty is outstanding on 28 October 2019, the Authority may recover the outstanding amount as debt owed by TPEL and due to the Authority.

Publicity

7.5. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the Authority must publish such information about the matter to which this notice relates as the Authority considers appropriate. The information may be published in such manner as the Authority considers appropriate. However, the Authority may not publish information if such publication would, in the opinion of the Authority, be unfair to you or prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.

Authority contacts

7.6. For more information concerning this matter generally, contact Olibhia McGinley at the Authority (direct line: 020 7066 7762, email: Olibhia.McGinley@fca.org.uk).

Sadaf Hussain

Head of Department

Financial Conduct Authority, Enforcement and Market Oversight Division

ANNEX A

RELEVANT STATUTORY AND REGULATORY PROVISIONS

1. Statutory Provisions

Financial Services and Markets Act 2000

The Authority's statutory objectives, set out in section 2(2) of the Act include market confidence.

Section 206 of the Act provides:

> If the Authority considers that an authorised person has contravened *a* requirement imposed on him by or under this Act…it may impose on him *a* penalty, in respect of the contravention, of such amount *as* it considers appropriate.

TPEL is an authorised person for the purposes of section 206 of the Act. The requirements imposed on authorised persons include those set out in the FCA's rules made under section 138 of the Act.

Section 206(1) of the Act provides:

If the Authority considers that an authorised person has contravened *a* requirement imposed on him by or under this Act… it may impose on him a penalty, in respect of the contravention, of such amount as it considers appropriate.

2. Regulatory Provisions

In exercising its power to issue a financial penalty, the Authority must have regard to the relevant provisions in the FCA Handbook.

In deciding on the action, the Authority has also had regard to guidance set out in the Regulatory Guides, in particular the Decision Procedure and Penalties Manual (DEPP).

3. Principles for Businesses

The Principles for Businesses are a general statement of the fundamental obligations of firms under the regulatory system and are set out in the FCA Handbook. They derive their authority from the Authority's rule-making powers as set out in the Act and reflect the Authority's regulatory objectives.

Principle 3 provides:

- A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

Principle 2 provides:

- A firm must conduct its business with due skill, care and diligence.

Principle 11 provides:

- A firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulatory would reasonably expect notice.

4. DEPP

DEPP, which forms part of the FCA Handbook, sets out the Authority's statement of policy with respect to the imposition and amount of financial penalties under the Act.

In respect of breaches which occurred before 6 March 2010, the relevant provisions of DEPP are as set out below.

DEPP 6.1.2 provides that the principal purpose of imposing a financial penalty is to "*promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter other persons from committing similar breaches, and demonstrating generally the benefits of compliant behaviour*."

DEPP 6.5.2 sets out some of the factors that might be taken into account when the Authority determines the level of a financial penalty that is appropriate and proportionate to the misconduct as follows:

(1) deterrence;

(2) the nature, seriousness and impact of the breach in question;

(3) the extent to which the breach was deliberate and reckless;

(4) whether the person on who the penalty is to be imposed is an individual;

(5) the size, financial resources and other circumstances of the person on whom the penalty is to be imposed;

(6) the amount of benefit gained or loss avoided;

(7) difficulty of detecting the breach;

(8) conduct following the breach;

(9) disciplinary record and compliance history;

(10) other action taken by the Authority;

(11) action taken by other domestic or international regulatory authorities;

(12) Authority guidance or other published materials; and

(13) the timing of any agreement as to the amount of the penalty

In respect of breaches which took place after 6 March 2010, the current version of DEPP can be found on the Authority's website.

5. The Enforcement Guide

The Enforcement Guide sets out the Authority's approach to exercising its main enforcement powers under the Act.

Chapter 7 of the Enforcement Guide sets out the Authority's approach to exercising its power to impose a financial penalty.