Financial Services Authority

# FINAL NOTICE

To: **HFC Bank Limited**

Of: **North Street**
**Winkfield**
**Windsor**
**Berkshire**
**SL4 4TD**

Date **16 January 2008**

**TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (the FSA) gives you final notice about a requirement to pay a financial penalty:**

## 1. THE PENALTY

1.1 The FSA gave HFC Bank Limited (HFC or the firm) a Decision Notice on 11 January 2008 which notified HFC that pursuant to section 206 of the Financial Services and Markets Act 2000 (the Act), the FSA had decided to impose a financial penalty of £1,085,000 on HFC. This penalty is in respect of breaches of Principles 9 and 3 of the FSA's Principles for Businesses (the Principles) and associated rules between 14 January 2005 and 28 May 2007 (the Relevant Period) in relation to HFC's sale of payment protection insurance (PPI).

1.2 HFC agreed that it will not be referring the matter to the Financial Services and Markets Tribunal.

1.3 Accordingly, for the reasons set out below and having agreed with HFC the facts and matters relied on, the FSA imposes a financial penalty on HFC in the amount of £1,085,000.

1.4 HFC agreed to settle at an early stage of the FSA's investigation. It therefore qualified for a 30% (stage 1) reduction in penalty, pursuant to the FSA's executive settlement procedures. Were it not for this discount, the FSA would have imposed a financial penalty of £1,550,000 on HFC. The level of the penalty reflects the FSA's announcement in the PPI thematic update of 26 September 2007 that higher fines will be imposed where this is warranted by the nature, seriousness and impact of the breach in question, and by the likely impact on deterrence.

## 2. REASONS FOR THE ACTION

### Summary of conduct in issue

2.1 The FSA has imposed a financial penalty on HFC for breaches of the FSA's Principles and rules in relation to its sale of PPI.

2.2 These breaches, which are described in more detail at section 5 below, relate to HFC's:

(1) failure to take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement (Principle 9); and

(2) failure to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems (Principle 3).

2.3 HFC breached Principles 9 and 3 by failing to take reasonable care to ensure that the advice it gave customers was suitable, and to have in place adequate systems and controls for sales of PPI.

2.4 In particular, the following failings in respect of HFC's procedures for dealings with customers and its other systems and controls were identified:

(1) HFC's sales staff were not required to gather, and take into account, sufficient information about customers' personal circumstances and objectives when making sales. HFC's processes did not therefore take adequate steps to ensure that its personal recommendations were suitable;

(2) HFC did not provide its customers with information that adequately set out their demands and needs and explained why HFC was recommending the policy. Nor did HFC require its advisers to identify the customer's demands and needs which would not be met;

(3) HFC did not have effective systems to train and monitor its staff. In particular, it failed to ensure that its procedures for monitoring sales staff effectively identified and investigated potentially unsuitable sales;

(4) Management information provided to HFC's senior management was not sufficient to enable them to identify problems with the sale of PPI. Where management information did indicate particular issues, HFC failed to take appropriate action; and

(5) HFC's records were not sufficient to demonstrate its sales were suitable.

2.5 These failings resulted in an unacceptable risk of unsuitable sales and a failure to treat its customers fairly.

2.6 The need for HFC to have robust and effective systems and controls and sales processes was particularly great because of the complexities in controlling a large branch network (with hundreds of sales staff) and a bonus structure which for the majority of the Relevant Period provided potentially significant incentives to staff (including managers responsible for monitoring sales) to meet sales targets of PPI (amongst other factors).

2.7 HFC's breaches are viewed as particularly serious because:

(1) HFC is a large firm which sold approximately 163,000 PPI policies over the Relevant Period (of which 124,000 were single premium) from 235 branches (136 branches by the end of the period) across the UK;

(2) The financial impact on customers of unsuitable advice relating to the purchase of PPI was likely to be significant. HFC's customer base consisted largely of customers with credit ratings which resulted in them having limited access to consumer finance and included customers with impaired, short or incomplete credit histories. HFC only sold single premium policies in connection with its (predominantly) fixed term, unsecured lending. In a sample of sales reviewed by the FSA, the average cost (including interest) of a usual, single premium policy (i.e. with life cover) was approximately £2,100 (£1,200 excluding interest), adding some 40% on average (23% excluding interest) to the loan to be repaid; and

(3) The problems in HFC's sales process were identified by the FSA, and not by HFC's own systems and procedures. The failings arose against a background of a series of high profile communications by the FSA highlighting the need for firms to ensure their PPI sales processes were meeting FSA requirements, and a letter to HFC in May 2006 detailing some of the FSA's specific concerns relating to HFC's sale of PPI.

2.8 HFC's failures therefore merit the imposition of a substantial financial penalty. In deciding upon the level of disciplinary sanction, the FSA recognised the following measures taken by HFC which mitigate the seriousness of its failings:

(1) In June 2007, HFC engaged an independent firm of reporting accountants to review the PPI sales process in place at that time. HFC is in the process of implementing the changes to its sales process recommended by the accountants;

(2) HFC's senior management demonstrated its willingness to co-operate fully with the investigation; and

(3) Following discussions with the FSA, HFC has committed to implement a robust remedial action plan, overseen by third party accountants, involving a programme of customer contact and, if appropriate, steps to ensure that its customers are not disadvantaged.

2.9 The FSA considers that the substantial remedial changes the firm has committed to are significant steps in demonstrating the firm's commitment to complying with its regulatory obligations.

## 3. BACKGROUND

*The firm*

3.1 HFC has been authorised by the FSA in respect of a number of regulated functions since 1 December 2001. It has been authorised to advise on and arrange non-investment insurance contracts since 14 January 2005.

3.2 HFC's branch business is as a provider of unsecured and secured loans. It has a secondary focus on general insurance business, mostly through the sale of PPI. The FSA regulates HFC's general insurance business but not its lending activity, which is outside the scope of the FSA's activities. Over the Relevant Period HFC traded under the "Household Bank" and "Beneficial Finance" names.

3.3 The FSA's investigation has focused solely upon sales made by HFC's branch network.

*The PPI products sold*

3.4 HFC sells PPI through its branch network when arranging personal loans for customers. It offers a bundled policy which provides cover for accident, sickness and involuntary unemployment. It also offers a life policy which can be purchased for joint or single lives. The life policy can be sold on its own or in conjunction with the bundled accident, sickness and involuntary unemployment policy.

3.5 HFC sells single premium PPI policies with unsecured loans. It also sells a limited amount of regular premium PPI with other types of loan. The sales process for regular premium PPI is substantially the same as that for single premium PPI. In the event that a customer claims against the PPI policy, any benefits due are directly payable to HFC to cover the customer's loan repayments. A full refund is given if the customer cancels within 30 days of the start of the policy. A partial, less than pro rata refund is given if the policy is cancelled after that period (eg a quarter of the premium is returned if the policy is cancelled half way through its term).

3.6 HFC also offers critical illness and personal accident cover. These policies provide more limited cover than PPI at a lower cost. Benefits under these insurances are paid to the customer, rather than to HFC.

3.7 PPI was sold in conjunction with 75% of all loans sold by HFC's branch network in the Relevant Period. Out of all PPI sold, 86% of policies covered life, accident, sickness and involuntary unemployment, 6% accident, sickness and involuntary unemployment, and 8% life alone.

*The sales process*

3.8 HFC sells PPI on an advised basis. It receives leads from retailers who have arranged credit with HFC for customers in respect of their retail purchases. These customers' credit arrangements are typically nearing the end of an interest free period. HFC sales staff contact some of these customers to discuss further loans or refinancing existing loans.

3.9 If the customer is interested in a new loan, an appointment is made for the customer to visit an HFC branch. At that meeting the sales adviser will discuss the loan, PPI and other insurance options with the customer and make recommendations.

*FSA work within the Relevant Period*

3.10 During the Relevant Period the FSA has highlighted to firms the importance of having in place robust systems and controls and treating customers fairly when selling PPI and has highlighted various areas where firms are not complying with the FSA's requirements. These concerns have been expressed in reports published by the FSA, individual feedback to firms, a Dear CEO letter and Enforcement actions.

3.11 In November 2005 the FSA published the results of the first phase of its thematic work on PPI and wrote a Dear CEO letter to the industry outlining the findings of the thematic project and highlighting a number of key areas where firms were not treating their customers fairly.

3.12 This letter stressed that if a firm gives advice it should review how the suitability assessment is made to ensure the adviser fully assesses the customer's needs for PPI. In particular, it noted that many customers arranging loans (particularly those with impaired credit ratings) are likely to be cost-sensitive or need flexibility in terms of the PPI contract (or often both), and it stressed that these factors must be taken into account when assessing the suitability of a policy. The letter also explained that if a firm makes advised sales, it should review the information it provides to customers and make sure it sets out clearly why the firm has concluded that the customer needs PPI and why the firm is recommending the policy. The FSA sent a follow up letter to firms, including HFC, in May 2006, which stressed that firms needed to improve their suitability assessments because they appeared to be making significant assumptions in their approach to judging suitability.

3.13 A second phase of PPI themed work was reported on in October 2006. The FSA highlighted in its report some key areas of widespread concern. These included the FSA's concern that some firms were still failing to establish that the PPI policies they recommended were suitable because they were not collecting sufficient information from the customer.

3.14 In July 2006, between the first two phases of the FSA's thematic work on PPI, the FSA visited HFC and identified a number of concerns relating to the firm's sale of PPI.

## 4. RELEVANT STATUTORY AND REGULATORY PROVISIONS

4.1 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 an amount as it considers appropriate."*

**FSA Rules and Principles**

4.2 The FSA's rule-making powers are set out in Chapter I of Part X of the Act (Rules and Guidance). In accordance with the powers and provisions under this part of the Act the FSA has made rules, in particular, in respect of Senior Management Arrangements, Systems and Controls, and Insurance: Conduct of Business.

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

4.4 The rules and Principles which are relevant to this matter are listed at Appendix 1.

## 5. BREACHES OF THE FSA'S PRINCIPLES FOR BUSINESSES AND RULES

### Principle 9

5.1 Principle 9 (suitability) provides that:

**A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgement**.

5.2 In considering the standards required under this Principle, the FSA also has considered the specific requirements set out in the part of the FSA Handbook (the Handbook) entitled Insurance: Conduct of Business (ICOB).

**<u>Facts and matters relied on</u>**

5.3 By reason of the facts and matters detailed in paragraphs 5.4 to 5.14 the FSA considers that HFC has breached Principle 9 of the FSA's Principles for Businesses and ICOB 4.3.1R, 4.3.2R, 4.3.5R, 4.3.6R and 4.4.1R.

*The suitability assessment*

5.4 Throughout the Relevant Period, HFC's documented procedures (including process guides for sales advisers and training material) and monitoring did not require adequate information to be collected and then properly used when recommending PPI. These failings created an unacceptable risk that advisers might make unsuitable sales. HFC failed, in particular, to require advisers to gather and analyse sufficient information about the following matters:

(1) *A customer's future needs and circumstances:* HFC did not ensure that the customer's intentions regarding the term of the loan and the PPI policy would be taken into account in the suitability recommendation when selling single premium PPI (which accounted for approximately 75% of sales). In the event of early settlement or cancellation of the policy after the initial 30 day period, the customer would receive a refund which was substantially less than pro rata (eg if the policy was cancelled at mid-term, a rebate was given of approximately one quarter of the premium). Likewise, the terms of the financing used to pay for the single premium resulted in the customer paying substantially more than a pro rata

amount of interest if the policy was terminated early. Therefore, HFC's single premium product may not have met the needs of customers who expected (or were likely to want) to refinance the loan from HFC (eg to get a lower interest rate or a larger loan).

HFC's failings were serious given that HFC's business model anticipated refinancing the loans of existing customers (over half the loans sold by HFC were to existing HFC customers).

HFC also did not ensure that any foreseeable alteration in customers' circumstances in relation to the PPI eligibility criteria would be taken into account. This meant that a customer could potentially have been sold a product for which he was eligible at the point of sale but would not be able to claim on later during the life of the loan (eg if a customer was likely to start working less than 16 hours a week).

(2) *Alternative means to protect the loan*: HFC failed to ensure that advisers properly took into account any existing means the customer may have had to protect some or all of the loan. This might have been from another insurer, the customer's employer, or a product which HFC had itself previously sold. When advisers established that the customer had existing means (which they were trained to do), HFC required that the advisers ask customers whether they wanted to rely on them, instead of training and requiring the adviser to take the alternative means into account in making a personal recommendation.

(3) *The type and level of cover required*: HFC's sales procedures did not provide guidance to advisers as to the factors (such as individual circumstances and cost) to be taken into account in assessing whether to recommend life cover on its own, accident, sickness and involuntary unemployment cover on its own or both together or whether another insurance product offered by HFC (see paragraphs 3.4 to 3.6 above) may have been suitable. Further, in respect of life cover, whilst advisers recorded details of how many dependants a customer had, HFC failed to ensure that advisers had regard to how this information might impact on a customer's need for life cover, or the relative benefits (including affordability) of taking the standalone single/joint life cover.

(4) *Pre-existing medical conditions*: Whilst HFC required advisers to make customers aware of the exclusion relating to pre-existing medical conditions, it did not require advisers to explain the meaning of the exclusion. HFC proceeded on the basis that it was the customer's responsibility to understand the limitations attached to PPI and to take account of any pre-existing medical conditions when considering purchasing PPI.

The impact of this failing is potentially serious. Approximately 27% of the claims rejected by HFC (3% of the total claims made by HFC's customers) were as a result of pre-existing medical conditions.

5.5 HFC's failings partially stemmed from an assumption that, provided the customer was eligible, PPI was suitable unless the customer indicated that he wished to use any alternative means he already had. It did not therefore put in place adequate systems and controls to gather and to analyse sufficiently information on its customers' personal circumstances and objectives.

*Communication to the customer of the basis for the personal recommendation*

5.6 HFC used a generic SODAN rather than one tailored for each customer. This failed to:

(1) adequately set out an individual customer's demands and needs;

(2) confirm whether HFC personally recommended the contract;

(3) explain the reasons for the personal recommendation for the PPI policy and why it was suitable; and

(4) record any demands and needs of the customer that the personal recommendation did not meet (nor did HFC require that advisers communicate this in any other way).

5.7 As a result of this failure customers could not see and review the rationale for the recommendation, check its accuracy and give proper consideration to the recommendation and whether they wished to purchase the policy.

5.8 A SODAN is particularly important when PPI is sold as a secondary product where, at the point of sale, the customer may be more focussed on the loan rather than on the associated insurance. The failing undermined the customer's ability to consider fully whether to accept the firm's PPI recommendation and, following the sale, whether it should keep or cancel the policy in the 30 day cancellation period.

*The need for robust procedures to ensure suitability*

5.9 Firms selling PPI must have adequate processes in place to ensure suitable and compliant sales. There were a number of additional factors in respect of the sale of PPI by HFC during the Relevant Period which increased the importance of particularly robust systems and controls to ensure that PPI was only sold when suitable:

(1) Over the Relevant Period HFC's sales force was spread over 235 branch sites in total (136 by the end of the period). This required a significant degree of coordination and monitoring to ensure consistency of standards; and

(2) HFC advisers and branch managers were eligible for bonuses which were, in part, based on reaching a target of selling PPI with 80% of the loans (calculated by loan value, rather than numerical loan sales). For example, during the early part of the Relevant Period (up to June 2005) the attainment of the PPI target penetration rate had a potentially significant impact on bonuses (i.e. it could double and potentially quadruple the value of the bonus). Until August 2006, there were significant disincentives (up to 33% of bonuses) attached to failing to meet certain targets and compliance standards which included PPI sales targets. After August 2006, there was a potential 12-18% uplift to sales advisers' bonuses for reaching PPI targets (although in fact HFC estimates that the PPI element of advisers' bonuses then

averaged approximately £19 per month). Whilst there is nothing inherently wrong with a remuneration policy which recognises and rewards sales, HFC's remuneration structure increased the risk that advisers might make, and branch managers approve, unsuitable sales of PPI to achieve those bonuses. The total amount of bonus available was significant compared to an adviser's basic salary (in 2005 and 2006 an adviser's monthly salary could be increased by up to 25%).

*Compliance monitoring*

5.10 HFC's Compliance department was responsible during the Relevant Period for the design and execution of a programme of compliance monitoring. Whilst the compliance monitoring visits and subsequent reports may have indicated general trends in relation to the sale of PPI, the reports did not contain sufficient detail to enable Compliance and/or senior management to obtain a sufficient understanding of the risk of potentially unsuitable sales in the branches. The application of weightings to the areas covered on the monitoring visits meant that a branch could fail "suitability" and/or "fact finding" in relation to PPI sales and still receive a satisfactory rating for insurance compliance and overall. Given that only unsatisfactory reports were escalated to senior management, potentially unsuitable PPI sales or potentially less compliant branches were not escalated, although they were made the subject of mandatory or targeted action for which the branch manager would be responsible. There were also insufficient systems and controls for ensuring that any training needs identified in the reports were followed up properly.

5.11 Even where the monitoring reports did highlight the risk that customers might not have been treated fairly (eg where it was unclear if a customer had existing cover when purchasing PPI), there was no adequate system in place to ensure that such cases were investigated further and customers remediated if appropriate.

*Management information*

5.12 During the Relevant Period senior management did receive certain management information, both orally and in writing. However, the principal management information received by senior management in relation to PPI was the statistical summary of the compliance monitoring visit reports described at paragraphs 5.10 and 5.11 above. There was little commentary to accompany the statistics, effectively limiting senior management's oversight of compliance to a review of compliance trends. Where specific risks were identified by Compliance, there was no procedure by which HFC's senior management would be informed of these or how they were to be followed up (if at all) by the Compliance team.

5.13 The monthly management information produced in relation to complaints was not reviewed by Compliance and was not broken down specifically into complaints relating to PPI. In the majority of cases there was no information about the reason for the complaint. A report on the root cause of complaints was available but most complaints relating to advice fell within the wide category of "point of sale issues" which covered a range of issues including identifying existing benefits, eligibility and affordability. Therefore, senior management were unable to identify any trends or relevant remedial action (eg additional training of sales staff).

5.14 Neither HFC's senior management nor Compliance received or considered claims information in respect of PPI. Consequently, whilst approximately 27% of rejected claims were as a result of pre-existing medical conditions, neither HFC senior management nor Compliance investigated whether the rejections might have been as a result of potential deficiencies in the sales process.

**Principle 3**

5.15 Principle 3 (Management & Control) provides that:

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

5.16 In considering the expected standards required under this Principle, the FSA also has considered the specific requirements of the parts of the Handbook entitled Senior Management Arrangements, Systems and Controls (SYSC) and ICOB.

**<u>Facts and matters relied on</u>**

5.17 By reason of the facts and matters referred to in paragraphs 5.1 to 5.14 above and paragraphs 5.18 to 5.26 below the FSA considers that HFC has breached Principle 3 of the FSA's Principles for Businesses, SYSC 3.2.6R, SYSC 3.2.20R and ICOB 4.4.7R.

5.18 HFC was under an obligation throughout the Relevant Period to take reasonable care to organise and control its affairs responsibly and effectively and, in particular, to take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system.

5.19 The matters set out in paragraphs 5.1 to 5.14 above illustrate a failure by HFC to take reasonable steps through its sales process and its procedures for training, manager oversight, compliance monitoring and management information to ensure the suitability of the advice given by its advisers. Consequently, HFC breached Principle 9 of the FSA's Principles for Business (as detailed above). The design and form of HFC's principal risk management systems in relation to PPI, namely the mandated sales process, compliance monitoring and management information, also show that HFC failed to take reasonable care to organise and control its affairs responsibly and effectively.

5.20 These matters show that, in establishing and maintaining its systems and controls, HFC failed to have proper regard to the nature, scale and complexity of HFC's PPI branch business, its high PPI penetration rate (both targeted and achieved), its customer base, and the nature of the single-premium policy.

5.21 In particular, in determining how frequently branches needed to be visited, the monitoring process was not designed to take account of risk factors in individual branches such as the proportion of customers purchasing PPI, complaints and cancellations when deciding where to target resources. This meant that branches where there were more potentially serious problems were treated in the same way as other branches where there may have been potentially less serious issues, although a risk based approach to a review of files within branches was applied. Similarly, as noted above, HFC's principal management information in relation to PPI comprised a statistical summary of the compliance monitoring visits, with little commentary to accompany the statistics, effectively limiting senior management's oversight of compliance to a review of compliance trends.

5.22 These failings therefore constitute a breach of Principle 3 (in addition to Principle 9).

*Record keeping*

5.23 HFC's record keeping was also inadequate and in breach of Principle 3. Its failure to generate proper SODANs, which were the only record of advice given to its customers, impacted on HFC's ability to monitor its sales force.

5.24 In addition, out of 139,144 sales of all types of PPI policy between 14 January 2005 and 31 December 2006, HFC estimates on the basis of its own sampling that there were some 10,000 cases where no soft or hard copy SODAN was retained (7% of such sales). This was caused by the loss of data from local servers which were not centrally backed up at the time of the merger of two separate strands of HFC's branch network in 2006. While the information itself was retained, this failing prevents HFC (or the FSA) from being able to review sales transactions quickly and effectively.

5.25 Moreover, during the Relevant Period, when an adviser entered information about a customer during the sales process, if that customer was an existing customer, any information previously contained on the system about them was overwritten.

5.26 As a consequence of the above failings HFC is unable to demonstrate the suitability of its sales of PPI during the Relevant Period.

## 6. RELEVANT GUIDANCE ON PENALTY

### Determining the level of the financial penalty

6.1 The FSA's policy in relation to the imposition of financial penalties is set out in Chapter 6 of the Decision Procedure and Penalties Manual (DEPP) which forms part of the FSA Handbook. It was previously set out in Chapter 13 of the Enforcement Manual (ENF). These Manuals set out the factors that may be of particular relevance in determining the appropriate level of financial penalty for a firm or approved person. The criteria are not exhaustive and all relevant circumstances of the case will be taken into consideration.

### Deterrence

6.2 A financial penalty is required to strengthen the message to the industry that it is vital to take proper steps to ensure in advised sales that the advice a firm gives customers is suitable and that a firm has in place adequate systems and controls in relation to the sale of PPI.

6.3 As communicated to the market in the FSA's thematic update on the sale of PPI published on 26 September 2007, in line with its general approach, the FSA is seeking to increase the level of fines in PPI cases where this is warranted by the nature, seriousness and impact of the breach in question, and by the likely impact on deterrence. Firms have been given due warning of their obligations to treat customers fairly, both generally and on PPI in particular. Consequently, the FSA will now seek to impose higher fines for firms in the PPI market where standards fall below required levels.

**The seriousness of the breaches**

6.4 The FSA has had regard to the seriousness of the breaches, including the nature of the requirements breached, the number and duration of the breaches, the number of customers who were exposed to risk of loss and whether the breaches revealed serious or systemic weaknesses of the management systems or internal controls. For the reasons set out at paragraph 2.7 above and having regard to the impact on HFC's customers, the FSA considers that the breaches are of a particularly serious nature. The seriousness is further increased by the fact that the breaches occurred over a period of 28 months.

**The extent to which the breach was deliberate or reckless**

6.5 The FSA does not consider that HFC acted in a deliberate or reckless manner.

**The size, financial resources and other circumstances of the firm**

6.6 HFC has a prominent position in the consumer finance market with a significant degree of public recognition. During the Relevant Period approximately 163,000 PPI policies were sold (including approximately 124,000 single premium policies) on approximately 216,000 loans.

6.7 There is no evidence to suggest that HFC is unable to pay the penalty.

**The amount of profits accrued or the loss avoided**

6.8 HFC derived considerable revenues through sales of PPI through its branch network, both through profit on the sale of the PPI product and from giving customers a larger loan to pay for the single premium policy. Further, since the policies were underwritten by subsidiary companies of HFC, further group profits were derived from HFC's sales.

**Conduct following the breach**

6.9 In June 2007 HFC instructed external reporting accountants to conduct a third party review of HFC's PPI sales processes.

6.10 As a result of the review HFC is in the process of making a significant number of changes to its sales processes. It has also agreed to strengthen its compliance monitoring and oversight arrangements. HFC has also committed to a robust remedial action plan, overseen by third party accountants, involving a programme of customer contact and, if appropriate, steps to ensure that its customers are not disadvantaged.

6.11 HFC has co-operated with the Enforcement action. Following the compliance review, HFC agreed the facts quickly ensuring efficient resolution of the matter and has received full credit for settlement at an early stage. Without this level of co-operation the financial penalty would have been higher.

**Disciplinary record and compliance history**

6.12 HFC has been authorised to conduct insurance business by the FSA since 14 January 2005, and for other regulated activities since 1 December 2001, and has not been the subject of previous FSA disciplinary action.

**Previous action taken in relation to similar failings**

6.13 In determining the level of financial penalty, the FSA has taken into account penalties imposed by the FSA on other authorised persons for similar behaviour. However, when determining the appropriate level of penalty, the FSA had regard to the principal purpose for which it imposes sanctions, namely to promote high standards of regulatory conduct by deterring persons who have committed breaches from committing further breaches and helping to deter other persons from committing similar breaches, as well as demonstrating generally the benefits of compliant business.

**FSA guidance and other published materials**

6.14 In determining the appropriate level of financial penalty, the FSA has had regard to the fact that the FSA has published materials (in particular, as described at paragraphs 3.10 to 3.13 above) which had raised relevant concerns and set out examples of compliant behaviour. As noted at paragraph 2.7(3) above, this significantly increases the seriousness with which the FSA has viewed the breaches.

## 7. CONCLUSION

7.1 Having regard to the seriousness of the breaches and the risk they posed to the FSA's statutory objectives of maintaining confidence in the financial system and securing the appropriate degree of protection for consumers, the FSA has imposed a financial penalty of £1,085,000 on HFC.

## 8. DECISION MAKER

8.1 The decision which gave rise to the obligation to give this Final Notice was made by the Settlement Decision Makers on behalf of the FSA.

## 9. IMPORTANT

9.1 This Final Notice is given to HFC in accordance with section 390 of the Act.

**Manner of and time for payment**

9.2 The financial penalty must be paid in full by HFC to the FSA by no later than 13 February 2008, 28 days from the date of this Final Notice.

**If the financial penalty is not paid**

9.3 If all or any of the financial penalty is outstanding on 14 February 2008, the FSA may recover the outstanding amount as a debt owed by HFC and due to the FSA.

**Publicity**

9.4 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 FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to HFC or prejudicial to the interests of consumers.

9.5 The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

**FSA contacts**

9.6 For more information concerning this matter generally, you should contact Lance Ellison (direct line: 020 7066 2422 /fax: 020 7066 2423) of the Enforcement Division of the FSA.

**William Amos**
**Head of Retail 1**
**FSA Enforcement Division**

## APPENDIX 1

**THE PRINCIPLES**

**Principle 3 –** A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.

**Principle 9 –** A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.

**THE RULES**

**Senior Management Arrangements, Systems and Controls**

**SYSC 3.2.6R Systems and controls in relation to compliance, financial crime and money laundering**

A firm must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system and for countering the risk that the firm might be used to further financial crime.

**SYSC 3.2.20R Records**

(1) A firm must take reasonable care to make and retain adequate records of matters and dealings (including accounting records) which are the subject of requirements and standards under the regulatory system.

(2) Subject to (3) and to any other record-keeping rule in the Handbook, the records required by (1) or by such other rule must be capable of being reproduced in the English language on paper.

(3) If a firm's records relate to business carried on from an establishment in a country or territory outside the United Kingdom, an official language of that country or territory may be used instead of the English language as required by (2).

**Insurance: Conduct of Business**

**ICOB 4.3.1R Requirement for suitability**

(1) An insurance intermediary must take reasonable steps to ensure that, if in the course of insurance mediation activities it makes any personal recommendation to a customer to buy or

sell a non-investment insurance contract, the personal recommendation is suitable for the customer's demands and needs at the time the personal recommendation is made.

(2) The personal recommendation in (1) must be based on the scope of the service disclosed in accordance with ICOB 4.2.8 R(6).

(3) An insurance intermediary may make a personal recommendation of a non-investment insurance contract that does not meet all of the customer's demands and needs, provided that:

> (a) there is no non-investment insurance contract within the insurance intermediary's scope, as determined by ICOB 4.2.8 R(6), that meets all of the customer's demands and needs; and
>
> (b) the insurance intermediary identifies to the customer, at the point at which the personal recommendation is made, the demands and needs that are not met by the contract that it personally recommends.

**ICOB 4.3.2R Information about the customer's demands and needs**

In assessing the customer's demands and needs, the insurance intermediary must:

(1) seek such information about the customer's circumstances and objectives as might reasonably be expected to be relevant in enabling the insurance intermediary to identify the customer's requirements. This must include any facts that would affect the type of insurance recommended, such as any relevant existing insurance;

(2) have regard to any relevant details about the customer that are readily available and accessible to the insurance intermediary, for example, in respect of other contracts of insurance on which the insurance intermediary has provided advice or information; and

(3) explain to the customer his duty to disclose all circumstances material to the insurance and the consequences of any failure to make such a disclosure, both before the non-investment insurance contract commences and throughout the duration of the contract; and take account of the information that the customer discloses.

**ICOB 4.3.5R Information about the customer's demands and needs**

If the insurance intermediary is aware that the customer's existing insurance cover is likely to significantly affect the suitability of any personal recommendation that the insurance intermediary might make, the insurance intermediary must either:

(1) not make a personal recommendation until details of the insurance cover are made available to him; or

(2) if it makes a personal recommendation, make clear to the customer that this may not be suitable because the insurance intermediary has not taken into account full details of the customer's existing insurance cover.

**ICOB 4.3.6R Assessing the suitability of a contract against the customer's demands and needs**

In assessing whether a non-investment insurance contract is suitable to meet a customer's demands and needs, an insurance intermediary must take into account at least the following matters:

(1) whether the level of cover is sufficient for the risks that the customer wishes to insure;

(2) the cost of the contract, where this is relevant to the customer's demands and needs; and

(3) the relevance of any exclusions, excesses, limitations or conditions in the contract.

**ICOB 4.4.1R SODAN**

(1) Unless ICOB 4.4.2 R applies, where an insurance intermediary arranges for a customer to enter into a non-investment insurance contract (including at renewal), it must, before the conclusion of that contract, provide the customer with a statement that:

(a) sets out the customer's demands and needs;

(b) confirms whether or not the insurance intermediary has personally recommended that contract; and

(c) where a personal recommendation has been made, explains the reasons for personally recommending that contract.

(2) The statement in (1) must reflect the complexity of the contract of insurance proposed.

(3) Unless (4) applies, the statement in (1) must be provided in a durable medium.

(4) An insurance intermediary may provide the statement in (1) orally if:

(a) the customer requests it; or

(b) the customer requires immediate cover;

but in both cases the insurance intermediary must provide the information in (1) immediately after the conclusion of the contract, in a durable medium.

**ICOB 4.4.7R Record keeping where a personal recommendation is made**

(1) An insurance intermediary that makes a personal recommendation to a customer must, if the customer acts on the personal recommendation by concluding the non-investment insurance contract with that insurance intermediary:

(a) unless ICOB 4.4.2 R(1)(b) applies, retain a copy of the statement required by ICOB 4.4.1 R(1); or

(b) if ICOB 4.4.2 R(1)(b) applies, make and retain, in a durable medium, a record of the reasons for the personal recommendation

(2) Both the copy of the statement in (1)(a) and the record in (1)(b) must be retained for a minimum period of three years from the date on which the personal recommendation was made.