FINAL NOTICE

To: **John Joseph Financial Services Limited**

Firm Reference Number: **116018**

Date: **30 September 2015**

1. ACTION

1.1. For the reasons given in this notice, the Authority hereby imposes on John Joseph Financial Services Limited ("JJFS") a financial penalty of £20,000 in respect of breaches of Principle 9 (Customers: relationships of trust) and certain applicable rules set out in COB, COBS and SYSC.

1.2. This notice relates solely to JJFS's conduct and does not make any criticism of Keydata or any person other than JJFS.

1.3. JJFS agreed to settle at an early stage of the Authority's investigation. JJFS therefore qualified for a 20% (stage 2) discount under the Authority's executive settlement procedures. Were it not for this discount, the Authority would have imposed a financial penalty of £25,000 on JJFS.

2. SUMMARY OF REASONS

2.1. JJFS is an independent financial adviser firm based in Borehamwood. It recommended Keydata Products to a total of 29 customers in two periods, between August 2005 and June 2006 and between November 2008 and December 2008. The total amount invested by JJFS's customers was £6.1 million. The Keydata Products were based on investments in corporate bonds which were issued by SPVs incorporated in Luxembourg. The funds raised through the issue of the bonds (i.e. the amount invested by retail customers in the products through Keydata) were then invested in a portfolio of US life insurance policies and cash.

2.2. During the first relevant period, JJFS failed, in breach of Principle 9 and certain rules of COB, to take reasonable care to ensure the suitability of its advice for any customer who was entitled to rely upon its judgment in relation to sales of the Keydata Products, in that it:

(a) failed to properly recognise the risks arising from lack of diversification of investments in a customer's investment portfolio; and

(b) failed to properly disclose to customers the risks arising from lack of diversification of investments in their investment portfolio.

2.3. During the combined relevant period, JJFS failed, in breach of Principle 9 and certain rules of COB and COBS, to take reasonable care to ensure the suitability of its advice for any customer who was entitled to rely upon its judgment in relation to sales of the Keydata Products, in that it:

(a) failed to assess adequately the needs and circumstances of customers, and their appetite for risk; and

(b) failed to disclose adequately all material risks of the Keydata Products, and in some cases in the Authority's view did not disclose the risks at all.

2.4. Further, during the combined relevant period, JJFS failed, in breach of certain rules of SYSC, to take reasonable care to establish and maintain effective systems and controls for compliance with applicable standards and requirements of the regulatory system. JJFS did not take reasonable care to create and retain records of matters and dealings which were the subject of requirements and standards under the regulatory system and its method of monitoring and reviewing its Keydata Product sales process was inadequate.

2.5. The Authority regards these failings as being serious, in particular because:

(a) many of JJFS's customers were approaching or already in retirement and therefore faced greater difficulties in rebuilding their investment portfolios in the event of loss of capital or income; and

(b) the systemic weaknesses across JJFS's systems and controls relating to the sales process for Keydata Products affected all aspects of the sales process, including fact finding, advising, disclosure of risks, and recording and monitoring of sales, much of which went to the heart of the client/advisor relationship.

2.6. The Authority has also taken into account the following factors which mitigate the seriousness of JJFS's failings:

(a) JJFS voluntarily and proactively assisted its customers in obtaining redress as soon as it became aware that Keydata had been placed into administration, including attempting to obtain ex gratia payments for customers from its professional indemnity insurers;

(b) JJFS helped to set up and fund at its own expense a group to fund legal action in the USA to recover assets for investors in the SLS-backed Keydata Products; and

(c) JJFS has taken extensive action to improve its advisory and record keeping processes including: introducing an Investment Committee to review investment policy, providers and products and use of proprietary research tools; replacing its back office systems; introducing a new operations manual, fact finds and procedures for assessing customers' ATR; recruiting an experienced Compliance Officer; and assisting its advisers to obtain additional professional qualifications.

2.7. The Authority therefore imposes a financial penalty on JJFS in the amount of £20,000 pursuant to section 206 of the Act.

3. DEFINITIONS

3.1. The definitions below are used in this Final Notice.

"the Act" means the Financial Services and Markets Act 2000

"the Authority" means the body corporate previously known as the Financial Services Authority and renamed on 1 April 2013 as the Financial Conduct Authority

"ATR" means attitude to risk or the degree of risk that a customer is willing to accept in connection with the purchase of an investment product

"COB" means the Conduct of Business Sourcebook, which formed part of the Authority's Handbook and was in force until 31 October 2007

"COBS" means the Conduct of Business Sourcebook, which forms part of the Authority's Handbook and has been in force from 1 November 2007

"combined relevant period" means the period of time consisting of the first relevant period and the second relevant period

"DEPP" means the Authority's Decision Procedure and Penalties manual, in force from 28 August 2007

"EG" means the Authority's Enforcement Guide, in force from 28 August 2007

"ENF" means the Authority's Enforcement manual, in force prior to 28 August 2007 "first relevant period" means 1 July 2005 to 2 June 2006

"FOS" means the Financial Ombudsman Service

"FSCS" means the Financial Services Compensation Scheme

"investment portfolio" means the investment assets held by a customer of which, at the time JJFS recommended to the customer that they invest in Keydata Products, JJFS was aware and had been given details

"ISA" means Individual Savings Account

"JJFS" means John Joseph Financial Services Limited

"Keydata" means Keydata Investment Services Limited (dissolved)

"Keydata Products" means products offered by Keydata that were based on investments in corporate bonds which were issued by SPVs incorporated in Luxembourg

"Lifemark" means Lifemark SA, the SPV incorporated in Luxembourg which issued bonds backing the Secure Income Bond 4, the Secure Income Plan and the Defined Income Plan

"PEP" means Personal Equity Plan

"Principle 9" means Principle 9 of the Principles for Businesses set out in PRIN 2.1.1R (Principles for Businesses) of the Authority's Handbook

"second relevant period" means 4 November 2008 to 13 February 2009

"SLS" means SLS Capital SA, the SPV incorporated in Luxembourg which issued bonds backing the Secure Income Bond 1, 2 and 3

"SPV" means a special purpose vehicle

"SYSC" means the Senior Management Arrangements, Systems and Controls Sourcebook

"the Tribunal" means the Upper Tribunal (Tax and Chancery Chamber)

"Traded Life Policy Investments" or "TLPI" means pooled investments in life assurance policies sold either directly or indirectly through other investments such as funds of funds

4. FACTS AND MATTERS

4.1. JJFS is an independent financial adviser firm based in Borehamwood.

JJFS's Keydata sales

4.2. During the combined relevant period, JJFS sold Keydata Products to 29 customers, who invested a total of £6.1 million in those products. 27 of these sales were in the first relevant period and two of these sales were in the second relevant period. At least 27 of these customers received advice and a recommendation from JJFS. JJFS received 3% initial commission and 0.5% annual renewal commission in relation to Keydata Products. JJFS generated a total of £296,937.81 in commission (£183,423.75 in gross initial commission and approximately £30,000 per year totalling £113,514.06 in annual renewal commission) from the sale of Keydata Products during the combined relevant period. Annual renewal commission payments stopped in June 2009 when Keydata went into liquidation.

4.3. All except perhaps two of JJFS's customers have received compensation from the FSCS in relation to Keydata Products. The FSCS in separate litigation sought repayment of this sum plus additional sums from JJFS to cover the losses suffered by JJFS's customers. 18 customers' investments exceeded the FSCS compensation threshold of £48,000, by a total of over £4.9 million.

The Keydata Products

4.4. Keydata was an authorised product provider that designed and distributed structured investment products both directly and via an extensive network of independent financial advisers. The Keydata Products offered investors an income or growth investment, by way of ISA, PEP or direct investment. The income option paid a specified percentage income (payable monthly, quarterly or annually) and aimed to ensure the full return of capital to the investor at the end of a five or seven year term. The growth option rolled up and reinvested the income payments to provide compound growth over the life of the product and similarly aimed to provide full return of capital at the end of the term.

4.5. The Keydata Products were based on investments in corporate bonds. On behalf of investors, Keydata purchased bonds which were issued by SPVs incorporated in Luxembourg. The funds raised through the issue of the bonds (i.e. the amount invested by retail customers in the products through Keydata) were then invested by the SPV in a portfolio of US life insurance policies and cash. The Keydata Product marketing materials stated that the investment mix was intended to be 60% policies / 40% cash for the bonds issued by SLS, and 70% policies / 30% cash for the bonds issued by Lifemark. SLS and Lifemark each purchased life insurance policies taken out by US citizens, paid the premiums due on those policies, and collected the maturity payment due under the policy when the individual died.

Distinctive features of the Keydata Products

4.6. The Keydata Products had a number of significant distinctive features which were referred to in the Keydata Product marketing material, including the following:

(a) although the Keydata Products were intended to return capital in full at the end of the investment period and were stated to be backed by assets, they offered no capital guarantee, and put capital invested at potential risk;

(b) successful performance of the Keydata Products depended on the accuracy of an actuarial model used by Keydata. Significant technological or pharmaceutical development could impact on the accuracy of the model and when insurance policies were likely to mature;

(c) the bonds had a fixed term of five or seven years. This meant that Keydata undertook to return funds to investors on the date when the bond matured, even if, at that point in time, it had insufficient funds because the insured individuals were living longer than anticipated;

(d) the underlying life insurance policy assets were illiquid. They were not traded on an exchange. The risk existed that, if it became necessary to sell an insurance policy to make funds available, this might take longer than anticipated, and might only be possible at a reduced value, reducing the value of the portfolio;

(e) the Keydata Products involved investment in a single specialist asset class (US senior life insurance policies) through a single issuer (at first SLS, then Lifemark). Although a percentage of the investment was to be held in cash, this was not held as a separate investment, but was intended to be used to pay the insurance premiums, income payments and operational costs associated with the investment so was not realisable in the same way as cash;

(f) the Keydata Products had a significant international dimension: the underlying assets were US life insurance policies, and the issuers of the bonds were based in Luxembourg. As with other bonds customers would not have recourse to the FSCS statutory compensation scheme in the event of default of the bond issuer; and

(g) the acquisition and administration of the life policies and the bonds depended on the services of a number of professional counterparties. If any of these counterparties failed, losses could be incurred by the investors.

JJFS's sales process for Keydata Products

Advice and recommendations - lack of diversification of investments

4.7. Under 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 relevant COB rules, which applied during the first relevant period, can be summarised as follows:

(a) a firm must take reasonable steps to ensure that if in the course of designated investment business it makes any personal recommendation to a private customer ... the advice … is suitable for the client. (COB 5.3.5R(1))

(b) in making the recommendation … in (1), the firm must have regard to the facts disclosed by the client, and other relevant facts about the client of which the firm is, or reasonably should be, aware. (COB 5.3.5R(3))

4.8. The Authority considers that in taking reasonable steps to ensure that a personal recommendation was suitable under the COB rules summarised above, JJFS should have had regard, amongst other things, to the risks associated with their recommendation. These risks should have been considered against the customer's attitude to risk. One of the risks they should have considered was the risk arising from lack of diversification in the customer's investment portfolio.

4.9. The risk arising from lack of diversification is the risk of loss from a customer's investments being limited in number or variety. For example, if a customer's investments are limited to products from one product provider then if that product provider fails for reasons specific to that provider, the impact on that customer will be far more severe than for customers who have spread their funds amongst other product providers. Similarly, if a customer invests only in products whose underlying assets are the same or of the same class, those investments will be exposed to the same risks and will behave in the same way if the risk materialises. If the risk materialises, the impact will be far less severe on customers who have spread their funds across different assets or asset classes which are affected by different risks.

4.10. 11 of JJFS's customers invested in Keydata through an "Open Annuity", which was a vehicle for investing pension funds. The Authority reviewed four of these cases. In all four, JJFS recommended to clients that they should invest the whole of their funds available for investment in the Open Annuity into Keydata Products. These amounted to between 14% and 31% of the customer's investment portfolio. All these cases arose in the first relevant period.

4.11. 18 customers invested in Keydata Products directly, by purchasing bonds or ISAs/PEPs. The Authority reviewed four advised cases, which included two cases from the first relevant period. In these two cases the customers invested 16% and 28% of their investment portfolio in Keydata Products.

4.12. In conclusion, in all six of the cases from the first relevant period reviewed by the Authority, the Authority considers that JJFS failed to consider properly or at all the risks arising from lack of diversification of their investments, which contributed to customers investing a high proportion of their investment portfolios' funds into Keydata Products.

4.13. In one of these cases JJFS appears to have recognised that lack of diversification of investments might pose a risk, because it recommended, a year before the investment in the Keydata Product was made, that the customer should split the funds to be invested in the Open Annuity between investments in UK and international equities, property and corporate bonds, in order to achieve a diversified portfolio. The following year, JJFS advised the same customer to transfer 100% of her funds invested in the Open Annuity into a single Keydata Product.

4.14. The Authority considers that JJFS failed to take reasonable care to properly recognise the risks to customers arising from lack of diversification of the investments in the customers' investment portfolios and that JJFS thereby breached the requirements of Principle 9 and COB 5.3.5R(1) and 5.3.5R(3).

Fact finding process

4.15. The relevant COB and COBS rules and guidance in relation to a firm's obligations in this area are as follows:

First relevant period

(a) before a firm gives a personal recommendation concerning a designated investment to a private customer … it must take reasonable steps to ensure that it is in possession of sufficient personal and financial information about that customer relevant to the services that the firm has agreed to provide (COB 5.2.5R);

(b) where the firm advises a private customer on a continuing basis it should keep its information about that customer under regular review. Where it acts for a customer on an occasional basis it should undertake a review whenever that customer seeks advice (COB 5.2.6G);

(c) information collected from a private customer should, at a minimum, provide an analysis of a customer's personal and financial circumstances leading to a clear identification of his needs and priorities so that, combined with attitude to risk, a suitable investment can be recommended (COB 5.2.11G(1)(a);

Second relevant period

(d) when making the personal recommendation, the firm must obtain the necessary information regarding the client's knowledge and experience in the investment field relevant to the specific type of designated investment or service; his financial situation; and his investment objectives; so as to enable the firm to make the recommendation which is suitable for him (COBS 9.2.1R);

(e) the firm must obtain from the client information necessary for them to understand the essential facts about the client and have a reasonable basis for believing that the recommendation meets his investment objectives. In particular the client must be able to bear the risks consistent with his investment objectives and must have the necessary experience and knowledge to understand the risks. Firms should establish how long the client wishes to hold the investment and preferences regarding risk taking, the client's risk profile and the purposes of the investment. Information about the financial situation of a client must include the source and extent of his regular income, assets, investments and real property, and his regular financial commitments (COBS 9.2.2R); and

(f) The information about the client's knowledge and experience includes information on the types of investment the client is familiar with, the nature, volume and frequency of the client's investments and the period over which they have been carried out, and the level of education or profession of the client (COBS 9.2.3R).

4.16. The Authority reviewed eight cases where JJFS had made recommendations to customers to invest in Keydata Products. These are the cases referred to in paragraphs 4.10 and 4.11 above, and include two cases from the second relevant period. There was no record of any fact find in two cases. The remaining cases did not have contemporaneous fact finds, and three fact finds were incomplete. For example, on one file there was a partially completed fact find undertaken on the same date as the application for the Keydata Product and some handwritten notes dated one month prior to the application, and also a full fact find undertaken four years before the application date.

4.17. JJFS stated to the Authority that it had acted for the customers for many years and knew them personally, and as a result it had acquired adequate information about their needs and circumstances. It attributed the absence of records to a failure of its IT systems resulting in the partial loss of records stored on the computer of one of its advisers, and also to the fact that in some cases the information was obtained orally or was known to the adviser so did not need to be collected and recorded.

4.18. The Authority considers that the absence of fact finds in some client files and the presence of deficient or out of date fact finds in other client files indicates that JJFS did not obtain sufficient information about its customers' needs and circumstances to enable a suitable recommendation to be made. The Authority considers that, in respect of all eight fact finds, JJFS breached both the requirement in COB 5.2.5R in relation to the first relevant period to take reasonable steps to ensure it was in possession of sufficient personal and financial information about the customer, and the requirement in COBS 9.2.1R and 9.2.2R in relation to the second relevant period to obtain the necessary information to enable a suitable recommendation to be made. For this reason during the combined relevant period JJFS also breached the Principle 9 requirement to take reasonable care to ensure the suitability of its advice for any customer who was entitled to rely upon its judgment.

Assessment of customers' ATR

4.19. The information required by COB 5.2.5R, COBS 9.2.1R and COBS 9.2.2R summarised above includes a customer's preferences regarding risk taking, such information being necessary to enable an adviser to make a suitable recommendation.

4.20. JJFS stated that it questioned customers in order to assess their ATR, including the use of questionnaires produced by third party product providers. In the eight cases reviewed by the Authority, one customer's ATR was assessed as "*cautious",* one *"cautious to moderate*", no ATR was recorded in two cases, and in four cases there was no contemporaneous record of the ATR. Of the two cases where contemporaneous records of customers' ATRs were recorded, one was in the first period and one in the second period.

4.21. The Authority considers that in six of the eight cases, JJFS did not obtain adequate information about the customer's preferences regarding risk taking to enable it to make a suitable recommendation. Accordingly, in the Authority's view, JJFS breached the requirements in Principle 9 to take reasonable care to ensure that its advice was suitable, and the COB and COBS rules set out in paragraph 4.19 above to obtain the necessary information about a customer's preferences as to risk taking to enable a suitable recommendation to be made.

Risk disclosure

First relevant period

4.22. COB 5.4.3R requires firms to take reasonable steps to ensure that customers understand the nature of the risks involved before making a recommendation, and COB 2.1.3R requires firms to take reasonable steps to ensure that communications with clients concerning investment business are clear, fair and not misleading.

Second relevant period

4.23. COBS 4.5.2R requires firms to take reasonable steps to ensure that information given to retail customers about investments is accurate and, in particular, does not emphasise any potential benefits without also giving a fair and prominent indication of any relevant risks.

4.24. Although the COB and COBS rules are differently expressed, as COB requires firms' communications to be clear, fair and not misleading, and COBS refers to the need for accurate and balanced information, the differences are not, in the Authority's view, material to this case; for the information provided to JJFS's customers to be clear, fair and not misleading, it would necessarily have to be accurate and balanced. The same overall standard has to be achieved under both sets of rules.

4.25. JJFS told the Authority that it was the firm's practice when making a recommendation to a client to invest in Keydata Products to provide a suitability letter and a copy of a "Key Features" document produced by Keydata. JJFS also stated that it also provided oral disclosure of risks, and in most cases a document produced by the firm containing questions and answers about certain risks. In respect of the six cases reviewed from the first relevant period:

(a) two cases had no record of the recommendation to invest in Keydata Products, the reasons for the recommendation or any risk disclosure. One of these contained documentation referring to a report having been provided, but not the report itself;

(b) in the other four cases, the customer was provided with a suitability letter, a copy of the Key Features document and the questions and answers document. However:

(i) in one case the suitability letter appeared to post-date the date of investment in the Keydata Products by over a month; and

(ii) in the other three cases some risks were disclosed in JJFS's suitability letter but a number were omitted.

4.26. In both of the two cases reviewed from the second relevant period, the customer was provided with a suitability letter and a copy of the Key Features document. In these two cases, the only risk disclosed in JJFS's suitability letter was that return of capital was not guaranteed, and in one of these cases the reasons for the recommendation were not given.

4.27. The Authority considers that firms may comply with the above rules by providing a suitability letter, oral disclosure, written questions and answers, a Key Features document or a combination of these. If oral disclosure is relied on, firms should make a record of the risk disclosures made.

4.28. In the view of the Authority, none of the methods adopted by JJFS was sufficient to ensure that JJFS complied with the requirements under either COB or COBS. Its suitability letters were deficient for the reasons set out in paragraphs 4.25 and 4.26 above, and if any oral disclosures were made, no records of them were created or retained so there is no evidence to show that JJFS satisfied the requirements.

4.29. Because JJFS failed to properly recognise the risks to customers arising from lack of diversification of the client's investment portfolio, during the first relevant period JJFS also necessarily failed to disclose these risks to customers.

4.30. In the Authority's view, by failing to disclose adequately all material risks of the Keydata Products, and in some cases not disclosing the risks at all, JJFS did not comply with the requirements of COB 5.4.3R(1) and COBS 4.5.2R to take reasonable steps to ensure that customers understood the risks of investing in the Keydata products, and that disclosure of the risks was balanced. In addition, the

Authority considers that JJFS failed to properly disclose to customers the risks arising from lack of diversification of investments in their investment portfolios, in breach of COB 5.4.3R(1). Accordingly, as a result of the breaches of these COB and COBS rules, the Authority considers that JJFS failed to comply with the Principle 9 requirement that a firm take reasonable care to ensure the suitability of its advice for its customers.

Monitoring and oversight of the Keydata Products sales process

4.31. SYSC contains rules and guidance on appropriate systems and controls for regulated firms. The SYSC rules and guidance referred to in this Notice applied throughout the combined relevant period. SYSC 3.2.6R requires firms to take reasonable care to establish and maintain effective systems and controls for compliance with applicable standards and requirements under the regulatory system.

4.32. Throughout the combined relevant period, JJFS did not have sales manuals or written training materials, and did not have a formal procedure for reviewing client files to assess whether recommendations to clients had been suitable or whether fact finding or risk disclosures had been conducted to the required standard or at all. JJFS identified three types of monitoring and review processes at JJFS during the combined relevant period:

(a) client file checks by administration staff to ensure all relevant documentation was present in files;

(b) peer reviews of recommendations and client files by JJFS advisers; and

(c) external compliance reviews by compliance consultants.

4.33. In the eight cases the Authority reviewed, JJFS did not take reasonable care to ensure its recommendations were suitable and records of fact finds and risk disclosures were missing, as described above. The Authority found no evidence of file checking by administration staff or peer reviews having taken place on these cases. The external consultants reviewed cases on a sample basis, and no advised sales of Keydata Products were included in their reviews. However, JJFS did not accept or implement recommendations made by the consultants to remedy deficient records on client files the consultants had reviewed, and which would have been equally applicable to the client files for Keydata Product sales.

4.34. In the Authority's view, JJFS's monitoring and review processes were inadequate to ensure compliance with regulatory requirements and standards. Either they failed to identify breaches of regulatory requirements and standards or, if they did identify breaches, these were not remedied across the firm's business.

Record keeping

4.35. SYSC 3.2.20R requires firms to take reasonable care to make and retain adequate records of matters and dealings which are the subject of requirements and standards under the regulatory system. The guidance under SYSC 3.2.21G indicates that firms should retain the records for as long as they are relevant for the purpose for which they were created.

4.36. JJFS relied on electronic and paper-based methods of recording and retaining information about customers, and also relied on personal recollection. In its review of the eight cases mentioned above the Authority found that records were missing or seriously deficient.

4.37. JJFS told the Authority that some records missing from client files had been created or stored in electronic form, but had been lost as a result of an intermittent failure in the firm's IT systems which had gone undetected over an 18 month period. However, the IT failure did not account for all the deficiencies in JJFS's records as in some cases JJFS kept paper files. Where this was the case, the paper files were seriously deficient.

4.38. The fact that the loss of electronic client records was either not identified or not remedied for 18 months itself indicates a lack of adequate systems and controls. Firms should review regularly whether their IT systems are functioning correctly where these are used as a means of performing regulated activities and to remedy promptly any defects in these systems.

4.39. In the Authority's view, JJFS's approach to client records fell short of the requirements in SYSC 3.2.20R to take reasonable care to make and retain adequate records of matters and dealings which are the subject of requirements and standards under the regulatory system, and did not follow the guidance in SYSC 3.2.21G to retain the records for as long as they are relevant for the purpose for which they were created.

5. FAILINGS

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

5.2. JJFS failed, during the first relevant period, in breach of Principle 9 and COB 5.3.5R(1), 5.3.5R(3) and 5.4.3R(1), to take reasonable care to ensure the suitability of its advice for any customer who was entitled to rely upon its judgment in relation to sales of the Keydata Products, in that it:

(a) failed to properly recognise the risks arising from lack of diversification of investments in a customer's investment portfolio; and

(b) failed to properly disclose to customers the risks arising from lack of diversification of investments in their investment portfolio.

5.3. JJFS also failed, during the combined relevant period, in breach of Principle 9, COB 5.2.5R and 5.4.3R(1) and COBS 4.5.2R, 9.2.1R and 9.2.2R, to take reasonable care to ensure the suitability of its advice for any customer who was entitled to rely upon its judgment in relation to sales of the Keydata Products, in that it:

(a) failed to assess adequately the needs and circumstances of customers, and their appetite for risk; and

(b) failed to disclose adequately all material risks of the Keydata Products, and in some cases in the Authority's view did not disclose the risks at all.

5.4. Further, during the combined relevant period, JJFS failed, in breach of SYSC 3.2.6R and 3.2.20R, to take reasonable care to establish and maintain effective systems and controls for compliance with applicable standards and requirements of the regulatory system. JJFS did not take reasonable care to create and retain records of matters and dealings which are the subject of requirements and standards under the regulatory system and its method of monitoring and reviewing its Keydata Product sales process was inadequate.

6. SANCTION

6.1. The Authority's policy on whether to issue a financial penalty is set out in Chapter 6 of DEPP.

6.2. Changes to DEPP were introduced on 6 March 2010. As JJFS's misconduct occurred prior to that date, the Authority has had regard to the provisions of DEPP in force prior to 6 March 2010.

6.3. Guidance on the imposition and amount of penalties for misconduct, in respect of the breaches which occurred prior to 27 August 2007 is set out in ENF. The Authority has accordingly had regard to ENF provisions on penalty policy that were in force at the time of the earlier misconduct as well as to those in Chapter 6 of DEPP.

6.4. The Authority considers the following DEPP factors to be particularly important in assessing the sanction for JJFS's misconduct.

Deterrence: DEPP 6.5.2G(1)

6.5. The principal purpose of a financial penalty is to promote high standards of regulatory and market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter others from committing similar breaches and demonstrating generally the benefits of compliant business.

The nature, seriousness and impact of the breach in question: DEPP 6.5.2G(2)

6.6. In determining the appropriate sanction, the Authority has had regard to the seriousness of the breaches by JJFS, including the duration and frequency of the breaches and whether the breaches revealed serious failings in JJFS's systems and controls, as well as the loss or risk of loss caused to customers.

6.7. JJFS's breaches were serious. Many of JJFS's customers were approaching or already in retirement and therefore faced greater difficulties in rebuilding their investment portfolios in the event of loss of capital or income. JJFS's customers invested £6.1 million in the Keydata Products. The customers' losses exceeded the FSCS compensation limit by over £4.9 million. The misconduct also revealed systemic weaknesses across JJFS's internal systems and controls affecting all aspects of the sales process.

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

6.8. The Authority has not determined that JJFS deliberately or recklessly contravened regulatory requirements.

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

6.9. The Authority has taken into account the size and financial resources of JJFS. There is no evidence to suggest that JJFS is unable to pay the penalty.

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

6.10. The Authority has had regard to the fact that JJFS earned £296,937 in commission from the sale of the Keydata Products. However, it has paid a FOS award of £100,000 to a customer, has contributed to the cost of funding litigation in the US to recover damages for investors, and was a defendant in litigation brought by the FSCS. JJFS has not ultimately benefited from the sales of Keydata Products.

Conduct following the breach: DEPP 6.5.2G(8)

6.11. In determining the penalty the Authority has had regard to JJFS's conduct following the breaches. JJFS voluntarily and proactively assisted its customers in obtaining redress as soon as it became aware that Keydata had been placed into administration, including attempting to obtain ex gratia payments for customers from its professional indemnity insurers. It also helped to set up and fund at its own expense a group to fund legal action in the USA to recover assets for investors in the SLS-backed Keydata Products. It also took extensive action to improve its advisory and record keeping processes including: introducing an Investment Committee to review investment policy, providers and products and use of proprietary research tools; replacing its back office systems; introducing a new operations manual, fact finds and procedures for assessing customers' ATR; recruiting an experienced Compliance Officer; and assisting its advisers to obtain additional professional qualifications.

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

6.12. JJFS has not been the subject of any previous disciplinary action.

Other action taken by the Authority: DEPP 6.5.2G(10)

6.13. In determining the level of financial penalty, the Authority has taken into account penalties imposed on other authorised persons for comparable behaviour.

6.14. JJFS has agreed to settle at an early stage of the Authority's investigation, and therefore qualifies for a 20% (Stage 2) discount under the Authority's executive settlement procedures.

6.15. The Authority therefore hereby imposes a financial penalty of £20,000 on JJFS for breaching Principle 9 and the relevant COB, COBS and SYSC rules. Were it not for the Stage 2 discount, the Authority would have imposed a financial penalty of £25,000 on JJFS.

7. PROCEDURAL MATTERS

Decision maker

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

Third Party Rights

7.2. No third party rights apply in respect of this Notice.

Manner of and time for Payment

7.3. The financial penalty must be paid in eight instalments by JJFS to the Authority, as follows:

a) £2,500 to be paid by no later than 14 October 2015, 14 days from the date of the Final Notice; and

b) £2,500 to be paid on each of 14 January 2016, 14 April 2016, 14 July 2016, 14 October 2016, 14 January 2017, 14 April 2017 and 14 July 2017.

If the financial penalty is not paid

7.4. If any, or any part of, an instalment is outstanding on the day after it is due to be paid to the Authority (in accordance with paragraph 7.3 above, the Authority may recover the full outstanding amount of the financial penalty as a debt owed by JJFS 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.

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

Contacts

7.7. For more information concerning this matter generally, contact Matthew Hendin (direct line: 0207 066 0236) of the Enforcement and Market Oversight Division of the Authority.

Bill Sillett

Project Sponsor

Financial Conduct Authority, Enforcement and Market Oversight Division

Annex

RELEVANT STATUTORY PROVISIONS, REGULATORY REQUIREMENTS AND AUTHORITY GUIDANCE

1. Relevant statutory provisions

1.1. The Authority's operational objectives are set out in section 1B(3) of the Act. In relation to this case, the most relevant operational objective is the consumer protection objective.

1.2. 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.

JJFS is an authorised person for the purposes of section 206(1) of the Act. The requirements imposed on authorised persons include those set out in the Authority's Principles and Rules made under section 138 of the Act.

2. Relevant Handbook provisions

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

2.2. In deciding on the above action, the Authority has also had regard to guidance published in the Authority's Handbook, in particular DEPP.

2.3. The applicable rules and guidance are those which applied during the relevant period. The rules and guidance that applied during the relevant period are set out below.

Principles for Businesses

2.4. Principle 9 provides:

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.

Conduct of Business Rules

2.5. The Authority has issued Rules under section 138 of the Act relating to the conduct of investment business, including relating to advising customers to purchase investment products. These are set out in COB for products sold before 1 November 2007 and in COBS for products sold from 1 November 2007.

For sales prior to 1 November 2007

2.6. COB 2.1.3R provides:

When a firm communicates information to a customer, the firm must take reasonable steps to communicate in a way which is clear, fair and not misleading.

2.7. COB 5.2.5R provides:

Before a firm gives a personal recommendation concerning a designated investment to a private customer, or acts as an investment manager for a private customer, it must take reasonable steps to ensure that it is in possession of sufficient personal and financial information about that customer relevant to the services that the firm has agreed to provide.

2.8. COB 5.2.11G(1)(a) provides:

Information collected from a private customer should, at a minimum, provide an analysis of a customer's personal and financial circumstances leading to a clear identification of his needs and priorities so that, combined with attitude to risk, a suitable investment can be recommended.

2.9. COB 5.3.5R provides:

(1) A firm must take reasonable steps to ensure that, if in the course of designated investment business:

(a) it makes any personal recommendation to a private customer to:

(i) *buy, sell, subscribe for or underwrite a designated investment (or to exercise any right conferred by such an investment to do so);*

...

the advice on investments or transaction is suitable for the client.

...

(3) In making the recommendation or effecting the transaction in (1), the firm must have regard to:

(a) the facts disclosed by the client; and

(b) other relevant facts about the client of which the firm is, or reasonably should be, aware.

2.10. COB 5.4.3R provides that:

A firm must not…

make a personal recommendation of a transaction…

with or to a private customer unless it has taken reasonable steps to ensure that the private customer understands the nature of the risks involved.

<u>For sales on or after 1 November 2007</u>

2.11. COBS 4.5.2R provides that:

A firm must ensure that information: …

(1) is accurate and in particular does not emphasise any potential benefits of relevant business or a relevant investment without also giving a fair and prominent indication of any relevant risks;

(2) is sufficient for, and presented in a way that is likely to be understood by, the average member of the group to whom it is directed, or by whom it is likely to be received; and

(3) does not disguise, diminish or obscure important items, statements or warnings.

2.12. COBS 4.5.4G provides:

In deciding whether, and how, to communicate information to a particular target audience, a firm should take into account the nature of the product or business, the risks involved, the client's commitment, the likely information needs of the average recipient, and the role of the information in the sales process.

2.13. COBS 4.5.5G provides:

When communicating information, a firm should consider whether omission of any relevant fact will result in information being insufficient, unclear, unfair or misleading.

2.14. COBS 9.2.1R provides:

(1) A firm must take reasonable steps to ensure that a personal recommendation, or a decision to trade, is suitable for its client.

(2) When making the personal recommendation or managing his investments, the firm must obtain the necessary information regarding the client's:

(a) *knowledge and experience in the investment field relevant to the specific type of designated investment or service;*

(b) *financial situation; and*

(c) *investment objectives;*

so as to enable the firm to make the recommendation, or take the decision, which is suitable for him.

2.15. COBS 9.2.2R provides:

(1) A firm must obtain from the client such information as is necessary for the firm to understand the essential facts about him and have a reasonable basis for believing, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of managing:

(a) *meets his investment objectives;*

(b) *is such that he is able financially to bear any related investment risks consistent with his investment objectives; and*

(c) *is such that he has the necessary experience and knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.*

(2) The information regarding the investment objectives of a client must include, where relevant, information on the length of time for which he wishes to hold the investment, his preferences regarding risk taking, his risk profile, and the purposes of the investment.

(3) The information regarding the financial situation of a client must include, where relevant, information on the source and extent of his regular income, his assets, including liquid assets, investments and real property, and his regular financial commitments.

2.16. COBS 9.2.3R provides:

The information regarding a client's knowledge and experience in the investment field includes, to the extent appropriate to the nature of the client, the nature and extent of the service to be provided and the type of product or transaction envisaged, including their complexity and the risks involved, information on:

(1) the types of service, transaction and designated investment with which the client is familiar;

(2) the nature, volume, frequency of the client's transactions in designated investments and the period over which they have been carried out;

<u>*Senior Management Arrangements, Systems and Controls*</u>

2.17. SYSC 3.1.1R provides:

A firm must take reasonable care to establish and maintain such systems and controls as are appropriate to its business.

2.18. SYSC 3.1.2G(1) provides:

(1) *The nature and extent of the systems and controls which a firm will need to maintain under SYSC 3.1.1R will depend upon a variety of factors including: the nature, scale and complexity of its business; the diversity of its operations, including geographical diversity; the volume and size of its transactions; and the degree of risk associated with each area of its operation.*

(2) *To enable it to comply with its obligation to maintain appropriate systems and controls, a firm should carry out a regular review.*

2.19. SYSC 3.2.6R provides

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.

2.20. SYSC 3.2.20R provides:

(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) *The records...must be capable of being reproduced in the English language on paper.*

2.21. SYSC 3.2.21G provides:

A firm should have appropriate systems and controls in place to fulfil the firm's regulatory and statutory obligations with respect to adequacy, access, periods of retention and security of records. The general principle is that records should be retained for as long as is relevant for the purposes for which they are made.