Financial Conduct Authority

This decision notice was superseded by a Final Notice dated 19 May 2015.

DECISION NOTICE

To: **Paul Reynolds (formerly known as Paul Brian Reynolds)**

IRN: **PXR00080**

Date: **05 December 2013**

ACTION

1. For the reasons given in this Decision Notice, the Authority has decided to take the following action:

   a. impose on Mr Reynolds a financial penalty of £290,344 pursuant to section 66 of the Act, for breaches of Statement of Principle 1; and

   b. make an order, pursuant to section 56 of the Act, prohibiting Mr Reynolds from performing any function in relation to any regulated activities carried on by any authorised person, exempt person, or exempt professional firm on the basis that he is not fit and proper because he lacks honesty and integrity.

REASONS FOR THE ACTION

2. Mr Reynolds' conduct, whilst he was an approved person (and significant influence function holder) at Aspire, breached Statement of Principle 1 because he:

   a. recklessly recommended high risk UCIS and GTEPs to eight retail clients, who subsequently invested in the products, when he knew that he could not justify their suitability;

b. deliberately attempted to mislead the Authority by retrospectively creating various documents, including fact finds and suitability reports, and misrepresenting that they were contemporaneous documents/client records;

c. deliberately made false and misleading statements to the Authority, including during a compelled interview;

d. deliberately made investments on behalf of two clients without their knowledge or authorisation;

e. was knowingly involved in the falsification of the signatures of two clients on sophisticated investor certificates to suggest that UCIS products could legitimately be promoted to them;

f. deliberately produced inflated valuations of clients' investments in an attempt to mislead them and conceal the poor performance of the investments he had recommended; and

g. deliberately submitted loan facility and investment applications, on behalf of a number of his clients, which contained inflated incomes and other false and misleading information.

3. The impact of Mr Reynolds' conduct on his clients was particularly serious for the following reasons:

a. Mr Reynolds advised six of the eight clients with which this case is concerned to invest a total of approximately £1.5 million in GTEPs and seven of those clients to invest at least £591,480 in UCIS, either directly with providers or indirectly (through a self-invested personal pension or a wrap platform). A number of the UCIS in which Mr Reynolds' clients invested have been suspended, resulting in financial losses.

b. Six of these clients had low incomes and/or little or no investment experience and these complex and high risk products were likely to be unsuitable for their needs. In addition, in some instances clients were not aware that they had invested in unregulated investments, or of the associated risks.

c. Mr Reynolds recommended that the six clients to whom he recommended GTEPs take out a significant amount of highly-geared finance to fund these. In reliance on this advice, clients re-mortgaged their residential properties, three of which were mortgage-free at the time of seeking advice from Mr Reynolds, to fund these high risk investments.

d. Of the seven clients who invested in UCIS, three were within ten years of retirement age and were encouraged to invest a significant proportion of their pension funds (more than 80%) in these products, with little or no means to make up any shortfall in the event of a loss.

4. In light of Mr Reynolds' misconduct, it appears to the Authority that he is not a fit and proper person, in terms of his honesty and integrity, to perform any function

in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional person.

5. The Authority has therefore decided to impose a financial penalty on Mr Reynolds in the amount of £290,344 pursuant to section 66 of the Act and make a prohibition order pursuant to section 56 of the Act.

6. The Authority considers that this action is necessary and proportionate and that it supports the Authority's operational objective of securing an appropriate degree of protection for consumers.

DEFINITIONS

7. The definitions below are used in this Decision Notice.

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

"Aspire" means the body corporate previously known as Positive Financial Strategies Limited and renamed on 19 February 2008 as Aspire Personal Finance Limited (now dissolved);

"ATR" means attitude to risk;

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

"COBS" means the Conduct of Business Sourcebook section of the Authority's Handbook;

"COB" means Conduct of Business, the predecessor version of COBS that existed prior to 1 November 2007;

"DEPP" means the Authority's Decision Procedure & Penalties Manual;

"Firm A" means the authorised firm of which Aspire was formerly an appointed representative;

"FOREX" means foreign exchange traded currency;

"FOS" means the Financial Ombudsman Service;

"FSCS" means the Financial Services Compensation Scheme;

"GTEPs" means geared traded endowment policies;

"PCIS Order" means the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001;

"Mr Reynolds" refers to Paul Reynolds (formerly known as Paul Brian Reynolds), the subject of this Decision Notice. At all material times, Mr Reynolds was one of two directors at Aspire and owned 50% of the shares.

"the section 238 restriction" means the statutory restriction on the promotion of UCIS in section 238(1) of the Act;

"Statements of Principle" means the Authority's Statements of Principle and Code of Practice for Approved Persons;

"TEPs" means traded endowment policies;

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

"UCIS" means unregulated collective investment scheme.

RELEVANT STATUTORY AND REGULATORY PROVISIONS

8. The relevant statutory and regulatory provisions relevant to this Decision Notice are contained in Annex A to this Decision Notice.

FACTS AND MATTERS

9. Aspire was a small independent financial advisory firm which, between 9 June 2005 and 31 March 2007, operated as an appointed representative of another authorised firm, Firm A. It advised mainly in the areas of mortgages, pensions and investments (both regulated and unregulated). From 21 June 2005 until 31 March 2007, Mr Reynolds was approved by the Authority to perform the CF1 Director (Appointed Representative) controlled function. He also held the CF22 Investment Adviser (Trainee), followed by the CF21 Investment Adviser controlled functions at Firm A.

10. On 2 April 2007, Aspire became directly authorised by the Authority. Aspire had approximately 160 clients.

11. From 2 April 2007 until 20 January 2013, Mr Reynolds was approved by the Authority to perform the CF1 (Director), CF3 (Chief Executive), CF10 (Compliance Oversight) CF11 (Money Laundering Reporting) controlled functions and was responsible for insurance mediation at Aspire. Whilst at Aspire, he also initially performed the CF8 (Apportionment and Oversight) and the CF21 (Investment Adviser) function and later the CF30 (Customer) function.

12. With effect from 6 September 2010, Aspire voluntarily varied its permission by removing all its regulated activities. Aspire was placed into voluntary liquidation on 7 September 2010 and dissolved on 20 January 2013. Aspire's permission was, accordingly, cancelled with effect from that date.

13. On 18 March 2011, Mr Reynolds was declared bankrupt as a result of a petition issued by the liquidator of Aspire for the sum of £255,740, the amount by which Aspire's directors' loan account was overdrawn when it went into liquidation. Mr Reynolds' bankruptcy was automatically discharged after one year, on 18 March 2012.

UCIS

14. A UCIS does not fall within the narrow definition of a recognised collective investment scheme. UCIS are often characterised by high levels of volatility and illiquidity which can in turn entail a higher degree of risk for consumers. Accordingly, the Authority's view is that they are unlikely to be suitable for the vast majority of retail clients. As UCIS fall outside the regulatory regime,

consumers who invest in them may also have limited recourse to the FOS and the FSCS.

15. For these reasons there is a restriction on the categories of investors to whom UCIS can be promoted in the UK. The section 238 restriction provides that an authorised firm must not communicate an invitation or inducement to participate in a collective investment scheme (including UCIS) unless an exemption applies. The relevant regulatory provisions and exemptions relating to the promotion of UCIS are set out in Annex A to this Decision Notice.

16. There are a number of exemptions that may be applied to the section 238 restriction. For example, under the PCIS Order, UCIS may be promoted to persons defined as certified "high net worth individuals" or certified "sophisticated investors". The PCIS Order defines:

    a. "high net worth individuals" as persons who have, during the previous financial year, received an annual income of £100,000 or more and/or held, throughout the previous financial year, net assets to the value of £250,000 or more, not including their primary residence or any loan secured on that residence; and

    b. "sophisticated investors" as individuals who have the appropriate investment expertise, experience and knowledge to understand the risks associated with participating in unregulated schemes.

17. Firms should document the exemption on which they are relying when promoting a UCIS and be able to demonstrate that they have complied with the certification requirements.

18. Mr Reynolds recommended UCIS products to his clients. The UCIS most commonly recommended by Mr Reynolds were funds that chiefly invested in "right to purchase" contracts in overseas property developments in Spain, Cape Verde, Mexico and Morocco. The "right to purchase" contracts gave the UCIS funds the right and obligation to purchase properties when the developments completed. These contracts were generally purchased at a 20-30% discount to the anticipated market value at completion, with a view to selling the contracts on at a later date for a profit. Between January 2007 and November 2009, Mr Reynolds, acting on behalf of Aspire, advised on at least 171 transactions in which UCIS products were recommended to clients. These clients invested a total of approximately £12.8 million in UCIS funds during this period. In addition, some clients ultimately invested in multiple UCIS funds following Mr Reynolds' recommendation.

GTEPs

19. TEPs form the basis of a typical GTEPs plan. TEPs are with-profits endowment policies which are no longer required by their original holders and have been sold on the secondary market. The purchaser of such policies agrees to pay the remaining premiums on the policy and in return receives the value of the policy at maturity (or when the original owner dies, if this occurs first) together with applicable bonuses, though not all such bonuses are guaranteed.

20. Investment in GTEPs involves gearing and is typically funded by the investor using cash savings, funds raised through a mortgage on the investor's home or a charge on an investment already owned by the investor. These funds are used together with a GTEPs loan facility taken out by the investor to purchase a portfolio of TEPs. The TEPs are then used as security for the loan facility, and part of the loan is used to fund the TEP premiums and sometimes purchase additional TEPs. The GTEPs loan is used to fund the TEP premiums, annual review fees payable on the TEPs, and monthly withdrawals of income payable to the investor (often used to pay monthly mortgage payments) where required. The GTEPs loan facility and mortgage (if one is taken out to raise capital to invest) is designed to be repaid by the maturity values of the TEPs within the portfolio. The investment rationale is that by the time the final TEP matures, the loan and mortgage will be repaid and any additional capital remaining can be taken as profit by the holder of the GTEPs or used to pay any mortgage that remains outstanding.

21. The gearing element introduces an interest rate risk and increased exposure to the usual risks of the investment (such as fluctuations in the performance of the underlying TEPs and secondary market demand). These varying levels of gearing are effectively using the strategy of borrowing to invest, which can be a high risk strategy, particularly where clients have no other means to repay the mortgage or loan facility if the investment return is insufficient. In order for the investor to make a profit, the product has to outperform the interest rate payable on the loan/mortgage.

22. In addition, since the loan facility must be renewed on an annual basis, there is the risk, if the loan to value ratio is not maintained within agreed parameters, that the lending institution refuses to extend the facility. The consequence for the client is serious, given that the loan is usually used to pay TEP premiums and, in some cases, mortgage payments. In some circumstances, investors may be required to inject further capital or assign additional assets to the provider of the loan facility as security in order to maintain the required loan to value ratio.

23. Consequently, it is the Authority's view that GTEPs are generally only suitable for investors who have a high risk tolerance and are able to bear the losses that may occur.

24. According to the key features documents of the GTEPs products which Mr Reynolds typically recommended, the purpose of these products, amongst other things, was to enable investors to buy a portfolio of specially selected TEPs to meet their needs and achieve greater risk diversification as the policies could be spread over several of the best performing life companies. The plans aimed to produce tax efficient withdrawals of up to 10% per year and to return the original capital invested at the end of the selected term, although neither outcome was guaranteed. Between January 2006 and October 2008, Mr Reynolds, acting on behalf of Aspire, advised at least 41 clients to invest a total of approximately £8.3 million in GTEPs products. The total amount of commission paid to Aspire by the GTEPs provider was £606,824.53.

Mr Reynolds' reckless recommendations of UCIS and GTEPs

25. Mr Reynolds knew that he was unable to justify the suitability of his recommendations of UCIS and GTEPs to the following eight of his clients. Specifically, in all of the instances below, Mr Reynolds knew that he could not justify the suitability of the recommendations for each of the clients in question because the risk of the product did not match the clients' ATR, but he proceeded to make the recommendations anyway.

Client A

Between August 2006 and February 2008, Mr Reynolds recommended to Client A, who had been diagnosed with prostate cancer, that he invest £365,000 in GTEPs, arranging an interest only mortgage against his home to raise these funds. In December 2007 he recommended that Client A invest pension funds in a UCIS investment. Client A asserts that he told Mr Reynolds that he was not willing to take risks, but Mr Reynolds characterised him as a sophisticated investor and recommended GTEPs and UCIS to him.

Client B

In or about October 2005, Mr Reynolds recommended to Client B, who was retired with no income other than her state pension, that she re-mortgage her house on an interest only basis in order to invest in TEPs, as well as taking out a life insurance policy. She asserts that the risks of GTEPs were not explained to her and that she was not told that she was taking out an additional building society loan. In or about April 2007 Mr Reynolds also advised Client B to transfer her pension funds into a UCIS.

Client C

In or about August 2008, Mr Reynolds recommended to Client C, a hairdresser earning approximately £3,000 per year, that she re-mortgage her home on an interest only basis for £130,000 and invest the proceeds in FOREX and TEPs. He also recommended that she invest £20,000 in UCIS. At the time of the recommendations, Client C asserts that Mr Reynolds knew about her financial situation and that she was not willing to take any risk. He was also knowingly involved in the forgery of her signature on a sophisticated investor certificate, apparently after recommending UCIS to her.

Client D

In or about March 2008, Mr Reynolds recommended to Client D, a part time accounts assistant earning approximately £3,000 per annum and her husband, a chef, that she take out an interest only mortgage on her home for £507,000 and invest £500,000 of the proceeds in FOREX and TEPs. Mr Reynolds also advised her to take out a loan facility for approximately £15,000. He did not undertake a risk assessment and Client D asserts that he recommended GTEPs without explaining the impact of gearing to her.

Client E

In or about December 2005, Mr Reynolds recommended that Client E re-mortgage his house on an interest only basis and invest £200,000 in GTEPs. Between June 2007 and November 2008, Mr Reynolds recommended that Client E invest about £176,500 from his pension fund in UCIS. Client E asserts that Mr Reynolds asked him about the level of risk which he was willing to take and was told that Client E was not willing to take risks. On Mr Reynolds' fact find documentation (which was not completed in Client E's presence) Client E's ATR is recorded as a medium to high ATR. Mr Reynolds was knowingly involved in the forgery of Client E's signature on a sophisticated investor certificate.

Client F

In about January 2008, Mr Reynolds recommended that Client F re-mortgage his house and invest £150,000 in FOREX and TEPs. He also advised Client F to take out a gearing loan in order to repay the mortgage and the premiums due on the TEPs. In addition, Mr Reynolds advised Client F to transfer his pension funds worth approximately £57,000 into a UCIS. Client F asserts that Mr Reynolds never assessed his attitude to risk and did not explain the risks of the GTEP loan facility. He further did not explain to Client F that the UCIS investment was unregulated and gave Client F insufficient time to understand the nature of the investment. Mr Reynolds asked Client F to sign a sophisticated investor certificate even though he did not meet the relevant criteria, so that Mr Reynolds could recommend UCIS to him. When Client F enquired about the reasons why he was being asked to sign the certificate, he was told "not to worry about it".

Client G

In or about March 2007, Mr Reynolds recommended that Client G re-mortgage on an interest only basis to invest approximately £100,000 in a UCIS. He further recommended that this investment be partly encashed and re-invested in two other UCIS funds a year later. Client G made it clear to Mr Reynolds that she was not generally willing to take risks, although she and her husband were prepared to take some risk with the £300 a month they invested in a savings plan, but Mr Reynolds recorded a medium to high ATR. The fact finds in respect of these recommendations recorded income, expenditure, assets and liabilities as not disclosed.

Client H

Between December 2006 and August 2008, Mr Reynolds recommended that Client H invest in several UCIS funds. Client H asserts that Mr Reynolds did not discuss either Client H or his wife's ATR with them, and did not discuss the fact that UCIS are high risk investments. Instead Client H asserts that Mr Reynolds told him that there was no risk to capital and that there was a guaranteed 15% return. Mr Reynolds' records described Client H as a sophisticated investor when he did not meet the criteria.

26. Mr Reynolds knew that the UCIS investments were high risk, because he had read the relevant information memoranda on which risk warnings were displayed prominently. He was also aware, at the time that he made the GTEPs recommendations, that his clients had limited income and modest assets apart from their residential properties. In the circumstances raising an interest only mortgage secured against these properties and taking on additional GTEP loan facilities to embark on highly geared speculative investments involving TEPs and/or FOREX was a high risk strategy, as such large amounts of gearing could greatly magnify any potential losses in the future. As the risk of the products did not match the relevant client's ATR, Mr Reynolds knew that he was unable to justify the suitability of these investment products for the clients to whom he recommended them. Notwithstanding this, Mr Reynolds recklessly proceeded to make the recommendations anyway (in breach of Statement of Principle 1). In addition, Mr Reynolds classified clients A, C, E, F and H as sophisticated investors (in two instances he was knowingly involved in forging the client's signature on the certificate) so that he could justify his recommendation of UCIS to them, when in fact they did not meet the appropriate criteria defined in Article 23(1) of the PCIS order. His actions in this regard were also reckless and breached Statement of Principle 1. A further indicator that Mr Reynolds knew that GTEPs products were not suitable for his clients is that he falsified details of client income and/or assets on GTEPs and, in some cases, the associated facility application forms for Clients A, B, C, D, E and F to enable them to make the investments he had recommended.

Mr Reynolds' deliberate attempts to conceal his reckless conduct

Attempting to mislead the Authority

27. Mr Reynolds deliberately attempted to mislead the Authority and conceal the misconduct outlined above both before and during its investigation, in that he:

    a. altered, or instructed staff to alter, client files by producing fact finds and suitability letters retrospectively, following notice of a supervisory visit by the Authority; and

    b. presented these documents to the Authority in client files as contemporaneous documents.

28. Mr Reynolds did not always prepare full fact finds at the time when he gave investment advice to clients and issue suitability letters to them shortly thereafter. Ahead of the Authority's scheduled supervisory visit to his offices in August 2010, Mr Reynolds embarked on a process of creating these documents retrospectively. He asked administration staff at Aspire to update client files and produce fact finds and suitability letters. He personally dictated the fact find documents to be produced and later started to produce these documents himself. Further, as Mr Reynolds was unable to create these documents in time for the supervisory visit, he asked a member of staff to telephone the Authority and explain that the visit would have to be rearranged because he was ill.

29. Documents found on Mr Reynolds' clients' files that were clearly not contemporaneous included the following:

a. in relation to two clients, fact finds and suitability letters that referred only to the products which the clients ultimately invested in and did not mention the products which Mr Reynolds recommended to the clients at the time, as established by other contemporaneous documents; and

b. several suitability letters that specifically referred to a dated supplemental memorandum on key risk factors which the letters asserted had already been sent to the clients. The specified risk memorandum did not exist at the time the letter was purportedly sent. In two cases, the suitability letters pre-dated it by almost five months. In one of those letters there is a caveat about the accuracy of a valuation which had purportedly been provided earlier, but the date of the valuation post-dates the letter by more than two months.

30. Further, Mr Reynolds deliberately provided false and misleading information during a compelled interview with the Authority. In particular he said that:

a. a full fact find was completed at all times;

b. the risks inherent in the investments recommended were set out in suitability letters which were issued to clients, typically within one or two weeks of the recommendation;

c. he had never produced documents retrospectively and/or misrepresented when any documents had been produced;

d. he had never made investments on behalf of clients before seeking their authorisation or agreement to doing so; and

e. the unauthorised investment in a FOREX product for one of his clients was an error made by the product provider which he had no involvement in or awareness of.

31. These statements were not truthful for the reasons set out in this Decision Notice.

Investments made without clients' authority

32. Aspire was not authorised as a discretionary investment manager and Mr Reynolds accordingly was not approved to carry out this regulated activity. Nevertheless, Mr Reynolds deliberately applied for investments, or directed applications for investments to be made, on behalf of at least two clients without their prior knowledge or authorisation. He therefore acted outside the scope of his approval and of Aspire's authorisation. The fact that he did so without his clients' knowledge has led the Authority to consider that this conduct lacked integrity.

33. In one example, Mr Reynolds recommended that his client invest half of her portfolio in GTEPs and the remaining half in a FOREX product. The client later discovered that the entire value of her portfolio had been invested in the high risk FOREX product without her knowledge or authorisation. The GTEPs application form found on the client file showed that Mr Reynolds had himself completed the application form and instructed that all of the amount should be invested in the FOREX product. Mr Reynolds did not seek the client's consent to this change.

Falsification of signatures on sophisticated investor certificates

34. Mr Reynolds deliberately falsified, or directed the falsification, of the signatures of two clients on sophisticated investor certificates in order to suggest that UCIS products could legitimately be promoted to them.

Inflation of clients' investment valuations

35. Mr Reynolds deliberately produced, or directed the production of, inflated valuations for at least two clients in an attempt to mislead them and conceal the poor performance of the investments that he had recommended.

36. In one example, the client's investment in a UCIS fund was valued with reference to the net asset value of another fund. As the second fund had a higher net asset value, it meant that the client's valuation was almost double its true value.

False and misleading information entered on loan and investment applications

37. Mr Reynolds was knowingly involved in submitting false and misleading income and asset related information to the providers of the GTEPs product and the associated gearing loan facility on behalf of several clients. In particular:

    a. two applications on behalf of client D declared her income to be £85,000; in fact it was less than a twentieth of that;

    b. an application on behalf of client E declared inaccurate income figures. Mr Reynolds sent a follow-up email to the product provider which more than tripled the value of his clients' assets; and

    c. three applications on behalf of client A declared inaccurate incomes and significantly inflated assets (e.g. cash deposits of £276,000 when the client only had savings of approximately £5,000).

38. These loan applications were completed by Mr Reynolds in his own handwriting and/or were personally signed by him.

REPRESENTATIONS

39. Annex B contains a brief summary of the key representations made by Mr Reynolds and how they have been dealt with. In making the decision which gave rise to the obligation to give this Decision Notice, the Authority has taken into account all of the representations made by Mr Reynolds, whether or not set out in Annex B.

FAILINGS

40. For the reasons given above, Mr Reynolds' conduct, whilst he was an approved person (and significant influence function holder) at Aspire, breached Statement of Principle 1 because he:

    a. recklessly recommended high risk UCIS and GTEPs to eight retail clients when he knew that he could not justify their suitability;

b. deliberately attempted to mislead the Authority by retrospectively creating various documents, including fact finds and suitability reports, and misrepresenting that they were contemporaneous documents/client records;

c. deliberately made false and misleading statements to the Authority, including during a compelled interview;

d. deliberately made investments on behalf of two clients without their knowledge or authorisation;

e. was knowingly involved in the falsification of the signatures of two clients on sophisticated investor certificates to suggest that UCIS products could legitimately be promoted to them;

f. deliberately produced inflated valuations of clients' investments in an attempt to mislead them and conceal the poor performance of the investments he had recommended; and

g. deliberately submitted loan facility and investment applications, on behalf of a number of his clients, which contained inflated incomes and other false and misleading information.

41. Mr Reynolds' actions in recommending UCIS and GTEPs when he knew that he could not justify the suitability of the personal recommendations he made and that there was a risk of unsuitable sales were reckless and lacked integrity, in contravention of Statement of Principle 1.

42. Mr Reynolds' actions in attempting to conceal his reckless selling were dishonest and lacked integrity in breach of Statement of Principle 1.

43. Further, from the conduct described above, it appears to the Authority that Mr Reynolds is not a fit and proper person in terms of his honesty and integrity. In particular, Mr Reynolds actively sought to mislead the Authority, his clients and product providers.

SANCTION

Imposition of financial penalty

44. The conduct at 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 both to the penalty regime which was effective before 6 March 2010 and the penalty regime which was effective after 6 March 2010.

Financial penalty under the old penalty regime

45. The Authority's policy on the imposition of financial penalties relevant to the misconduct prior to 6 March 2010 is set out in the version of Chapter 6 of DEPP that was in force prior to 6 March 2010. All references to DEPP from this paragraph to paragraph 52 are references to that version of DEPP.

46. The following misconduct by Mr Reynolds occurred before 6 March 2010 and falls to be considered under the old penalty regime:

    a. being knowingly involved in the falsification of client signatures on sophisticated investor certificates to suggest that UCIS products could legitimately be promoted to them;

    b. making investments on behalf of two clients without their knowledge or authorisation;

    c. deliberately submitted loan facility and investment applications, on behalf of a number of his clients, which contained inflated incomes and other false and misleading information; and

    d. recommended UCIS and GTEPs when he knew that he could not justify the suitability of the personal recommendations he made and that there was a risk of unsuitable sales.

47. To determine whether a financial penalty is appropriate, the Authority considers all the relevant circumstances of a case. DEPP 6.5.2G sets out a non-exhaustive list of factors that may be relevant to determine the level of a financial penalty. Applying those factors here, the appropriate level of penalty to be imposed under the old penalty regime is £150,000. The Authority considers that the following factors are particularly relevant to this case.

Deterrence (DEPP 6.5.2G(1))

48. The Authority has had regard to the need to ensure that those who are approved persons exercising significant influence functions act in accordance with regulatory requirements and standards. The Authority considers that a penalty should be imposed to demonstrate to Mr Reynolds and others the seriousness of failing to meet these requirements.

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

49. The Authority has had regard to the nature, seriousness and impact of Mr Reynolds' breaches (as set out above) in determining the level of the financial penalty.

The extent to which the breach was deliberate or reckless (DEPP 6.5.2G(2))

50. Where the Authority decides that a breach was deliberate or reckless, it is more likely to impose a higher penalty on a person than otherwise. The Authority considers that Mr Reynolds' actions were reckless in that he recommended UCIS and GTEPs when he knew that he could not justify the suitability of the personal recommendations he made and that there was a risk of unsuitable sales. The Authority considers that Mr Reynolds' actions in attempting to conceal his reckless selling were dishonest.

Whether the person on whom the penalty is to be imposed is an individual (DEPP 6.5.2G(4))

51. When determining the appropriate level of financial penalty, the Authority will take into account the fact that: an individual will not always have the same resources as a body corporate; an enforcement action may have a greater effect on an individual; and that it may be possible to achieve effective deterrence by imposing a smaller penalty on an individual rather than a body corporate. The Authority will also consider whether the status, position and/or responsibilities of the individuals are such to make a breach committed by the individual more serious and whether the penalty should therefore be set at a higher level.

52. The Authority recognises that the financial penalty is likely to have a significant effect on Mr Reynolds as an individual. It is aware that Mr Reynolds was declared bankrupt on 18 March 2011 and that his bankruptcy was discharged after one year, on 18 March 2012. However, the Authority, considers the financial penalty to be proportionate in relation to the seriousness of Mr Reynolds' misconduct.

Financial penalty under the new penalty regime

53. All references to DEPP from this paragraph to paragraph 77 are references to the version of DEPP implemented as of 6 March 2010 and currently in force.

54. In respect of conduct occurring on or after 6 March 2010, the Authority applies a five-step framework to determine the appropriate level of financial penalty. DEPP 6.5B sets out the details of the five-step framework that applies to financial penalties imposed on individuals in non-market abuse cases.

55. The following misconduct occurred after 6 March 2010 and thus falls to be considered under the new penalty regime:

    a. deliberately attempting to mislead the Authority by creating various documents, including fact finds and suitability reports, and misrepresenting that they were contemporaneous client records;

    b. producing an inflated valuation of a client's investments in an attempt to mislead them and conceal the poor performance of the investments he had recommended; and

    c. making numerous false and misleading statements to the Authority including during a compelled interview.

Step 1: disgorgement

56. Pursuant to DEPP 6.5B.1G, at Step 1 the Authority seeks to deprive an individual of the financial benefit derived directly from the breach where it is practicable to quantify this.

57. The period of Mr Reynolds' breach for the purposes of calculating his penalty under the new penalty regime was from 6 March 2010 to 31 August 2010. It is not possible to quantify any specific sum of financial benefit that Mr Reynolds derived directly from the breach during this period.

58. Accordingly, the Step 1 figure is nil.

Step 2: the seriousness of the breach

59. Pursuant to DEPP 6.5B.2G, at Step 2 the Authority determines a figure that reflects the seriousness of the breach. That figure is based on a percentage of the individual's relevant income. The individual's relevant income is the gross amount of all benefits received by the individual from the employment in connection with which the breach occurred, and for the period of the breach.

60. The period of Mr Reynolds' breach for the purposes of calculating his penalty under the new penalty regime was from 6 March 2010 to 31 August 2010.

61. DEPP 6.5B.2G states that where the individual was in the relevant employment for less than 12 months, his relevant income will be calculated on a pro rata basis to the equivalent of 12 months' relevant income. In light of this, the Authority has included Mr Reynolds' income from 1 September 2009 to 31 August 2010 in the calculation of Mr Reynolds' relevant income. Consequently, the relevant income for the purposes of Step 2 is £155,937.

62. In deciding on the percentage of the relevant income that forms the basis of the Step 2 figure, the Authority considers the seriousness of the breach and chooses a percentage between 0% and 40%. 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 individuals in non-market abuse cases there are the following five levels:

Level 1 – 0%

Level 2 – 10%

Level 3 – 20%

Level 4 – 30%

Level 5 – 40%

63. 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. DEPP 6.5B.2G(12) lists factors likely to be considered "level 4 factors" or "level 5 factors". Of these, the Authority considers the following factors to be relevant:

a. Nature of breach:

i. Mr Reynolds failed to act with integrity by preparing non-contemporaneous documents to disguise his misconduct. Mr Reynolds created fact finds and suitability letters retrospectively prior to a supervisory visit by the Authority and included information which would help justify the past recommendations he had made and create the impression that he had fully advised clients of the risks inherent in the high risk UCIS and GTEPs investments that he had recommended. He then attempted to mislead the Authority in an interview to conceal the fact that these

documents had not been produced at the relevant time. His lack of integrity was also demonstrated by his actions in producing inflated valuations to mislead clients.

b. Whether the breach was deliberate:

i. Mr Reynolds' actions in creating non-contemporaneous fact finds and suitability letters were calculated to disguise his misconduct and amounted to a deliberate attempt to mislead the Authority;

ii. Mr Reynolds' further sought to conceal his misconduct during his compelled interview; and

iii. Mr Reynolds' actions were repeated. He misled the Authority when he created non-contemporaneous documents in August 2010 and continued to mislead the Authority in his interview in March 2012.

64. Guidance in DEPP notes the factors which are likely to be considered "level 4 factors" or "level 5 factors". These include the following:

a. the individual failed to act with integrity; and

b. the breach was committed deliberately or recklessly.

65. Taking all of these factors into account, the Authority considers the seriousness of the breach to be level 4 and so the Step 2 figure is 30% of £155,937.

66. Step 2 is therefore £46,781.

Step 3: mitigating and aggravating factors

67. Pursuant to DEPP 6.5B.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.

68. Aspire was placed into voluntary liquidation on 7 September 2010 and the directors' loan account was overdrawn by £255,740 as of November 2010. Mr Reynolds drew a significant sum from the directors' loan account in the five months immediately before Aspire went into liquidation and the amount remains outstanding. The Authority considers that this conduct aggravates the breach as it suggests that Mr Reynolds arranged his resources in such a way as to avoid payment of a financial penalty.

69. The Authority considers that there are no factors that mitigate the breach.

70. Having taken into account the aggravating factors, the Authority considers that the Step 2 figure should be uplifted by 50%. Consequently, the Step 2 figure is increased by £23,391 (50% of £46,781).

71. Step 3 is therefore £70,172.

Step 4: adjustment for deterrence

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

73. As an approved person exercising significant influence functions, Mr Reynolds was required to act in accordance with regulatory requirements and standards. One of his key obligations was to act with honesty and integrity. He failed to discharge this obligation.

74. Given the seriousness of Mr Reynolds' conduct, the Step 3 figure of £70,172 is insufficient to meet the Authority's credible deterrence objective. Consequently, it is appropriate to apply a Step 4 multiple of 2 to the Step 3 figure. This also reflects the fact that the Step 2 figure was net of tax.

75. Step 4 is therefore £140,344 (2 x £70,172).

Step 5: settlement discount

76. This is not applicable so the Step 5 figure remains £140,344.

Serious financial hardship

77. Pursuant to DEPP 6.5D.4G, the Authority will consider reducing the amount of a penalty if an individual will suffer serious financial hardship as a result of having to pay the entire penalty. The Authority has found that Mr Reynolds has provided insufficient evidence to demonstrate that he would suffer serious financial hardship. The Authority considers that Mr Reynolds' conduct is so serious that a penalty should be imposed even if Mr Reynolds would suffer serious financial hardship.

Proposed penalty

78. The Authority considers that combining the two separate penalties calculated under the old and new penalties regimes produces a figure which is proportionate and consistent with similar fines. The Authority has therefore decided to impose on Mr Reynolds a total financial penalty of £290,344.

Prohibition

79. Under section 56 of the Act, the Authority may make a prohibition order if it appears to it that an individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person, a person who is an exempt person in relation to that activity or a person to whom, as a result of Part 20 of the Act, the general prohibition does not apply in relation to that activity. FIT guidance sets out the criteria for assessing fitness and propriety. The criteria include the person's honesty and integrity.

80. Mr Reynolds demonstrated a lack of honesty and integrity for the reasons given above.

81. For these reasons, Mr Reynolds is not fit and proper and it is appropriate to prohibit him from carrying out any function in relation to any regulated activity carried out by an authorised person, exempt person or exempt professional firm.

PROCEDURAL MATTERS

Decision maker

82. The decision which gave rise to the obligation to give this Decision Notice was made by the Regulatory Decisions Committee.

83. This Decision Notice is given under sections 57 and 67 and in accordance with section 388 of the Act. The following statutory rights are important.

The Tribunal

84. Mr Reynolds has the right to refer the matter to which this Decision Notice relates to the Tribunal. Under paragraph 2(2) of Schedule 3 of the Tribunal Procedure (Upper Tribunal) Rules 2008, Mr Reynolds has 28 days from the date on which this Decision Notice is given to him to refer the matter to the Tribunal. A reference to the Tribunal is made by way of a signed reference notice (Form FTC3) filed with a copy of this Notice. The Tribunal's address is: The Upper Tribunal, Tax and Chancery Chamber, 45 Bedford Square, London WC1B 3DN (tel: 020 7612 9700; email financeandtaxappeals@tribunals.gsi.gov.uk). Further details are contained in "Making a Reference to the UPPER TRIBUNAL (Tax and Chancery Chamber)" which is available from the Upper Tribunal website:

    http://www.tribunals.gov.uk/financeandtax/FormsGuidance.htm

85. Mr Reynolds should note that a copy of the reference notice (Form FTC3) must also be sent to the Authority at the same time as filing a reference with the Tribunal. A copy of the reference notice should be sent to Rebecca Irving at the Financial Conduct Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS.

Access to evidence

86. Section 394 of the Act applies to this Decision Notice. In accordance with section 394, Mr Reynolds is entitled to have access to:

    a. the material upon which the Authority has relied in deciding to give this Decision Notice; and

    b. any secondary material which, in the opinion of the Authority, might undermine that decision.

Confidentiality and publicity

87. This Decision Notice may contain confidential information and should not be disclosed to a third party (except for the purpose of obtaining advice on its contents). Section 391 (1A) of the Act provides that Mr Reynolds may not publish the Decision Notice or any details concerning it unless the Authority has published the Decision Notice or those details. The Authority must publish such information about the matter to which a Decision Notice or Final Notice relates as it considers

appropriate. Mr Reynolds should be aware, therefore that the facts and matters contained in this Decision Notice may be made public by the Authority.

Authority contacts

88. For more information concerning this matter generally, contact Rebecca Irving at the Authority (direct line: 020 7066 2334/fax: 020 7066 2335).

Andrew Long
Chairman, Regulatory Decisions Committee

ANNEX A

RELEVANT STATUTORY PROVISIONS, REGULATORY GUIDANCE AND POLICY

STATUTORY PROVISIONS

General

The Authority's statutory objectives, set out in sections 1B to 1E of the Act, include securing an appropriate degree of consumer protection and protecting and enhancing the integrity of the UK financial system.

Section 66 of the Act provides that the Authority may take action to impose a penalty on an individual of such amount as it considers appropriate where it appears to the Authority that the individual is guilty of misconduct and it is satisfied that it is appropriate in all the circumstances to take action. Misconduct includes failure, while an approved person, to comply with a statement of principle issued under section 64 of the Act.

Section 56 of the Act provides that the Authority may make a prohibition order if it appears to the Authority that an individual is not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person. Such an order may relate to a specific regulated activity, an activity falling within a specified description or all regulated activities.

UCIS

Section 238(1) of the Act provides that an authorised person must not communicate an invitation or inducement to participate in a collective investment scheme ("CIS"), and therefore also a UCIS.

Section 238 goes on expressly to carve out circumstances where this prohibition will not apply. These include:

– the Treasury may by order specify circumstances (s238 (6)) (there is a statutory exemption in an order made by the Treasury - the PCIS Order);

– permitted financial promotions under Authority rules exempting the promotion of UCIS under certain circumstances (s238 (5)) (the Authority has made rules exempting the promotion of UCIS in COB 3.11 for the period up to 31 October 2007 and COBS 4.12 for the period from 1 November 2007).

DELEGATED LEGISLATION

Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 ("the PCIS order")

The PCIS Order provides for authorised firms to promote UCIS to individuals if they fall within a particular category of exemption set out in the PCIS Order. These exemptions pertain to certain categories of individuals, for example certified high net worth individuals (article 21), certified sophisticated investors (article 23) or self-certified sophisticated investors (article 23A).

Certified high net worth individuals

Article 21(2) of the PCIS Order defines a certified high net worth individual as an individual who has signed a statement complying with Part I of the Schedule to the PCIS Order in the past 12 months. Essentially this requires that at least one of the following sets of circumstances apply:

(1) the person had, during the previous financial year immediately preceding the date of the statement, an annual income of £100,000 or more; and/or

(2) the person held, throughout the previous financial year immediately preceding the date of the statement, net assets to the value of £250,000 or more, not including that person's primary residence or any loan secured on that residence; that person's rights under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or any benefits (in the form of pensions or otherwise) which are payable on the termination of that person's service or on that person's death or retirement and to which that person is (or that person's dependants are), or may be, entitled.

This exemption also requires that the person signs a statement to indicate he accepts that he can lose his property and other assets from making investment decisions based on financial promotions and is aware it is open to him to seek specialist advice.

If the person making the communication believes on reasonable grounds that he is making it to a certified high net worth individual, then the restriction in section 238 of the Act will not apply as long as the communication:

(1) is a non-real time communication or a solicited real time communication;

(2) relates only to units in a UCIS which invests wholly or predominantly in the shares in or debentures of one or more unlisted companies;

(3) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment;

(4) a specified warning in the following terms is given both orally (in respect of a real-time communication) and in writing in the manner prescribed in article 21:

"Reliance on this promotion for the purpose of buying the units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested"; and

(5) is accompanied by an indication that the promotion is exempt from section 238 on the grounds that it is communicated to a certified high net worth individual, together with details of the requirements for certified high net worth investors and a reminder that the individual should consult a specialist if in any doubt about participating in a UCIS.

The validity of the statement is not affected by a defect in its form or wording, provided that the defect does not alter the statement's meaning (Article 21(3))

Certified sophisticated investors

Article 23(1) of the PCIS Order defines a "certified sophisticated investor" as a person—

(a) who has a current certificate in writing or other legible form signed by an authorised person to the effect that he is sufficiently knowledgeable to understand the risks associated with participating in unregulated schemes; and

(b) who has signed, within the period of twelve months ending with the day on which the communication is made, a statement in the following terms:

"I make this statement so that I can receive promotions which are exempt from the restriction on promotion of unregulated schemes in the Financial Services and Markets Act 2000. The exemption relates to certified sophisticated investors and I declare that I qualify as such. I accept that the schemes to which the promotions will relate are not authorised or recognised for the purposes of that Act. I am aware that it is open to me to seek advice from an authorised person who specialises in advising on this kind of investment."

The validity of the statement is not affected by a defect in its form or wording, provided that the defect does not alter the statement's meaning (Article 23(1A))

Articles 23(2) and (3) provide that if the communication is made to a certified sophisticated investor (and does not invite or induce the recipient to participate in an unregulated scheme operated by the person who has signed the certificate) then the restriction in section 238 of the Act will not apply as long as the communication is accompanied by the following indications:

(a) that it is exempt from the section 238 restriction on the ground that it is made to a certified sophisticated investor;

(b) of the requirements that must be met for a person to qualify as a certified sophisticated investor;

(c) that buying the units to which the communication relates may expose the individual to a significant risk of losing all of the property invested; and

(d) that any individual who is in any doubt about the investment to which the invitation or inducement relates should consult an authorised person specialising in advising on investments of the kind in question.

REGULATORY PROVISIONS

In exercising its powers the Authority must have regard to the relevant provisions in the Authority Handbook. In deciding on the proposed action, the Authority has also had regard to guidance set out the in the Regulatory Guides, in particular the Decision Procedure and Penalties Manual (DEPP).

The guidance and policy that the Authority considers relevant to this case is set out below.

Statements of Principle and the Code of Practice for Approved Persons ("APER")

APER sets out the Statements of Principle as they relate to approved persons and descriptions of conduct which, in the opinion of the Authority, do not comply with a Statement of Principle. It further describes factors which, in the opinion of the Authority, are to be taken into account in determining whether or not an approved person's conduct complies with a Statement of Principle.

Statement of Principle 1 provides that an approved person must act with integrity in carrying out his controlled function.

APER 3.1.4G provides that an approved person will only be in breach of a Statement of Principle where he is personally culpable, that is in a situation where his conduct was deliberate or where his standard of conduct was below that which would be reasonable in all the circumstances.

APER 3.1.6G provides that APER (and in particular the specific examples of behaviour which may be in breach of a generic description of conduct in the code) is not exhaustive of the kind of conduct that may contravene the Statements of Principle.

APER 4.1 lists types of conduct which, in the opinion of the Authority, do not comply with Statement of Principle 1. Those examples include:

- APER 4.1.3E(1) - deliberately misleading (or attempting to mislead) a client or the Authority by act or omission. APER 4.1.4E(9) clarifies that such conduct includes, but is not limited to, deliberately: falsifying documents; misleading a client about the risks of an investment; providing false or inaccurate information to the Authority.

- APER 4.1.5E - deliberately recommending an investment to a customer where the approved person knows that he is unable to justify its suitability for that customer;

- APER 4.1.8E - deliberately preparing inaccurate or inappropriate records in connection with a controlled function. APER 4.1.9E(1) clarifies that such conduct includes, but is not limited to, deliberately preparing inaccurate performance reports for transmission to customers.

- APER 4.1.15E - deliberate acts, omissions or business practices that could be reasonably expected to cause consumer detriment.

Conduct of Business rules in relation to ensuring suitability of advice

The fact that a customer is eligible to receive a communication promoting a UCIS under one or more exemption does not mean that UCIS will be automatically suitable to that customer. Before making a personal recommendation, a firm is required to obtain and document information about a specific customer to assess the suitability of an investment for that customer. The relevant provisions that applied during the relevant period were set out in the Conduct of Business Sourcebook (COBS) from 1 November 2007 and the Conduct of Business (COB) which applied prior to that date:

Recommendations after 1 November 2007

COBS 9.2.1R(1) requires a firm to take reasonable steps to ensure that a personal recommendation is suitable for its client.

COBS 9.2.1R(2) provides that when making the personal recommendation or managing his investments, the firm must obtain the necessary information regarding the customer'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.

COBS 9.2.2R(1) requires a firm to obtain from the customer 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:

> (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 knowledge in order to understand the risks involved in the transaction or in the management of his portfolio.
>
> 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. COBS9.2.2R(2)

COBS 9.2.3R clarifies that the extent to which a firm must obtain information regarding a customer's knowledge and experience in the investment field varies according to, among other things, the type of product or transaction envisaged, including its complexity and the risks involved.

COBS 9.2.6R provides that if a firm does not obtain the necessary information to assess suitability, it must not make a personal recommendation to the customer or take a decision to trade for him.

A firm is also required to maintain adequate records to support its recommendations.

SYSC 9.1.1R provides that a firm must arrange for orderly records to be kept of its business and internal organisation, including all services and transactions undertaken by it, which must be sufficient to enable the Authority to monitor the firm's compliance with the requirements under the regulatory system, and in particular to ascertain that the firm has complied with all obligations with respect to clients.

COBS 9.5.2R sets out the minimum periods that a firm must retain its records relating to suitability.

Recommendations prior to 1 November 2007

COB 5 applies to a firm which gives advice on investments to a private customer on packaged products. It supports Principle 6 (Customers' interests) and Principle 7 (Communications with clients) which requires firms to have due regard to the information needs of their customers and treat them fairly. The purpose of this section is to ensure that private customers are adequately informed about the nature of the advice on investments which they may receive from a firm in relation to packaged products.

COB 5.2.1R provides that this section applies, inter alia, to a firm that gives a personal recommendation concerning a designated investment to a private customer.

COB 5.2.5R provides that 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 5.2.4G clarifies that Principle 9 (Customers: relationships of trust) requires a firm to take reasonable care to ensure the suitability of its advice and discretionary decisions. To comply with this, a firm should obtain sufficient information about its private customer to enable it to meet its responsibility to give suitable advice.

COB 5.2.11G(1)(a) clarifies that information collected from a 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 5.2.7G states that where a customer declines to provide sufficient information, a firm should not proceed to make a personal recommendation without promptly advising the customer that the lack of such information may adversely affect the quality of the services which it can provide.

COB 5.2.9R provides that, unless the customer does not act on the recommendation, a firm must make and retain a record of a private customer's personal and financial circumstances that it has obtained in satisfying COB 5.2.5 R for a specified minimum period.

Fit and Proper Test for Approved Persons ("FIT")

The Authority has issued specific guidance on the fitness and propriety of individuals in FIT. The purpose of FIT is to outline the main criteria for assessing the fitness and propriety of a candidate for a controlled function and FIT is also relevant in assessing the continuing fitness and propriety of approved persons.

FIT 1.3.1G provides that the Authority will have regard to a number of factors when assessing a person's fitness and propriety. One of the most important considerations will be a person's honesty, integrity and reputation.

FIT 2.1.1G provides that in determining a person's honesty, integrity and reputation, the Authority will have regard to all relevant matters including, but not limited to, those set out in FIT 2.1.3G, including:

> (1) whether the person has contravened any of the requirements and standards of the regulatory system (FIT 2.1.3G(5)); and
>
> (2) whether the person has been candid and truthful in all his dealings with any regulatory body and demonstrates a readiness and willingness to comply with the requirements and standards of the regulatory system and with other legal, regulatory and professional requirements and standards (FIT 2.1.3G(13)).

Decision Procedure and Penalties Manual (DEPP) and Enforcement ENF

Guidance on the imposition and amount of penalties is set out in Chapter 6 of DEPP. Changes to DEPP were introduced on 6 March 2010 ("the new penalties regime"). Given that the reckless breach of Statement of Principle 1 occurred prior that date, the Authority has had regard to the provisions of DEPP in force prior to 6 March 2010 ("the old penalties regime") in respect of that breach. The deliberate breaches of Principle 1 fall either before or after that date and the Authority has had regard either to the old or new penalties regime as appropriate in respect of these breaches.

Guidance on the imposition and amount of penalties for misconduct that occurred prior to 28 August 2007 is set out in ENF. The Authority has accordingly had regard to the 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.

The Old Penalties Regime

DEPP 6.1.2G 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. Financial penalties are therefore tools that the Authority may employ to help it to achieve its regulatory objectives.

DEPP 6.2.1G provides that the Authority will consider the full circumstances of each case when determining whether or not to take action for a financial penalty.

DEPP 6.5.1G(1) provides that the Authority will consider all the relevant circumstances of a case when it determines the level of financial penalty (if any) that is appropriate and in proportion to the breach concerned.

DEPP 6.5.2G sets out a non-exhaustive list of factors that may be relevant to determining the appropriate level of financial penalty to be imposed on a person under the Act. The following factors are relevant to this case:

Deterrence: DEPP 6.5.2G(1)

When determining the appropriate level of financial penalty, the Authority will have regard to the principal purpose for which it imposes sanctions, namely to promote high standards of regulatory and/or market 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.

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

The Authority will consider the seriousness of the breach in relation to the nature of the rule, requirement or provision breached, which can include considerations such as the duration and frequency of the breach, whether the breach revealed serious or systemic weaknesses in the person's procedures or of the management systems or internal controls relating to all or part of a person's business and the loss or risk of loss caused to consumers, investors or other market users.

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

The Authority will regard as more serious a breach which is deliberately or recklessly committed, giving consideration to factors such as whether the breach was intentional, in that the person intended or foresaw the potential or actual consequences of its actions. If the Authority decides that the breach was deliberate or reckless, it is more likely to impose a higher penalty on a person than would otherwise be the case.

Whether the person on whom the penalty is to be imposed is an individual: DEPP 6.5.2G(4)

When determining the amount of penalty to be imposed on an individual, the Authority will take into account that individuals will not always have the resources of a body corporate, that enforcement action may have a greater impact on an individual, and further, that it may be possible to achieve effective deterrence by imposing a smaller penalty on an individual than on a body corporate. The Authority will also consider whether the status, position and/or responsibilities of the individual are such as to make a breach committed by the individual more serious and whether the penalty should therefore be set at a higher level.

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

The purpose of a penalty is not to render a person insolvent or to threaten a person's solvency. Where this would be a material consideration, the Authority will consider, having regard to all other factors, whether a lower penalty would be appropriate.

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

The Authority may have regard to the amount of benefit gained or loss avoided as the result of the breach, for example the Authority will impose a penalty that is consistent with the principle that a person should not benefit from the breach, and the penalty should also act as an incentive to the person (and others) to comply with regulatory standards and required standards of market conduct.

Conduct following the breach: DEPP 6.5.2G(8)

The Authority may take into account the degree of co-operation the person showed during the investigation of the breach by the Authority.

Other action taken by the Authority (or a previous regulator): DEPP 6.5.2G(10)

The Authority seeks to apply a consistent approach to determining the appropriate level of penalty. The Authority may take into account previous decisions made in relation to similar misconduct.

Enforcement Guide (EG)

The Authority's approach to taking disciplinary action is set out in Chapter 2 of EG. Its approach to exercising its power to make a prohibition order under sections 56 of the Act is set out in Chapter 9 of EG. The Authority has had regard to the appropriate provisions of EG that applied during the relevant period.

EG 9.1 states that the Authority's power under section 56 of the Act to prohibit individuals who are not fit and proper from carrying out controlled functions in relation to regulated activities helps the Authority to work towards achieving its regulatory objectives. The Authority may exercise this power to make a prohibition order where it considers that, to achieve any of those objectives, it is appropriate either to prevent an individual from performing any functions in relation to regulated activities, or to restrict the functions which he may perform.

EG 9.4 sets out the general scope of the Authority's power in this respect. The Authority has the power to make a range of prohibition orders depending on the circumstances of each case and the range of regulated activities to which the individual's lack of fitness and propriety is relevant.

EG 9.5 provides that the scope of the prohibition order will depend on the range of functions which the individual concerned performs in relation to regulated activities, the reasons why he is not fit and proper and the severity of risk which he poses to consumers or the market generally.

EG 9.9 provides that when deciding whether to make a prohibition order against an approved person, the Authority will consider all the relevant circumstances of the case. These may include, but are not limited to, the following:

- whether the individual is fit and proper to perform the functions in relation to regulated activities. The criteria for assessing the fitness and propriety of approved persons are set out in FIT 2.1 (honesty, integrity and reputation), FIT 2.2 (competence and capability) and FIT 2.3 (financial soundness) (EG 9.9(2));

- whether, and to what extent, the approved person has failed to comply with the Statements of Principle issued by the Authority with respect to the conduct of approved persons, or been knowingly involved in a contravention by the relevant firm of a requirement imposed on the firm by or under the Act (including the Principles and other rules (EG 9.9(3)(a) and (b));

- the relevance and materiality of any matters indicating unfitness (EG 9.9(5));

- the length of time since the occurrence of any matters indicating unfitness (EG 9.9(6));

- the particular controlled function the approved person is (or was) performing, the nature and activities of the firm concerned and the markets in which he operates (EG 9.9(7)); and

- the severity of the risk which the individual poses to consumers and to confidence in the financial system (EG 9.9(8)).

EG 9.12 provides a number of examples of types of behaviour which have previously resulted in the Authority deciding to issue a prohibition order to an approved person. The examples include:

- Providing false or misleading information to the Authority (EG 9.12(1)); and

- serious breaches of the Statements of Principle for approved persons, such as acting without regard to instructions, providing misleading information to customers, giving clients poor or inaccurate advice and failing to ensure that a firm acted within the scope of its permission (EG 9.12(5)).

EG 9.23 provides that in appropriate cases the Authority may take other action against an individual in addition to making a prohibition order, including the use of its power to impose a financial penalty.

ANNEX B

REPRESENTATIONS

1. Mr Reynolds made written representations in response to the Authority's Warning Notice dated 31 July 2013.

2. Below is a summary of the key written representations made by Mr Reynolds in response to the allegations and matters in the Warning Notice and how they have been dealt with. In making the decision which gave rise to the obligation to give this Decision Notice, the Authority took into account all of Mr Reynolds' representations, whether or not explicitly set out below.

Limitation

3. Mr Reynolds made representations that the Authority only began proceedings against him after the end of the period of three years beginning with the first day on which the Authority knew of his alleged misconduct. Knowledge for this purpose includes information from which the alleged misconduct can reasonably be inferred. Mr Reynolds asserted that the Authority can reasonably be inferred to have had knowledge of his alleged misconduct by or on 29 July 2010 (through a combination of the correspondence and complaints received by or on that date) and therefore the Warning Notice dated 31 July 2013 was given after the three year limitation period for taking disciplinary action against him pursuant to section 66(4) of the Act. As a result Mr Reynolds contended that the Authority's action against him "is time-barred in its entirety".

4. The Authority has found that the earliest date on which it can reasonably be inferred to have had knowledge of Mr Reynolds' misconduct is 4 August 2010. On that date the Authority became aware of a very specific allegation that Mr Reynolds was in the process of creating client related documents in an attempt to present them as contemporaneous documents when the Authority made a supervisory visit. This was the first allegation of a deliberate attempt to mislead the Authority. The Authority considers that this was the evidence that raised a reasonable suspicion that Mr Reynolds was acting without integrity, sufficient to start time running for the three year limitation period for taking disciplinary action against him in relation to the Statement of Principle 1 allegations against him. Accordingly, the Authority rejects Mr Reynolds' representations that the Warning Notice was given after the three year limitation period for taking disciplinary action against him pursuant to section 66(4) of the Act.

Proof

5. Mr Reynolds made representations as to the applicable standard of proof. Mr Reynolds asserted that in light of the seriousness of the allegations and matters set out in the Warning Notice, as well as the very significant financial, reputational and personal consequences of a finding of a breach of Statement of Principle 1, the Authority should require "more" by way of proof in the circumstances of his case. In support of this assertion, Mr Reynolds submitted that:

    a. cogent evidence is required to satisfy a civil tribunal that a person has been fraudulent or behaved in a reprehensible manner;

    b. when making an inference, a court should be sure that there are no co-existing circumstances that would weaken or destroy the inference; and

    c. the more serious the charges against an individual, the more robust the evidence must be against him to support this.

6. The Authority has found that its administrative decision making process in the circumstances of Mr Reynolds' case is not subject to a higher standard of proof. The Authority has made its decision having regard to the following:

    a. the Authority, in accordance with section 66 of the Act, may impose a penalty if it considers that Mr Reynolds has contravened a requirement imposed on him by or under the Act;

    b. the Authority, in accordance with section 56 of the Act, may make a prohibition order if it appears to it that an individual is not a fit and proper person; and

    c. the Tribunal, in regulatory cases, applies the civil standard of proof - i.e. the balance of probabilities (is it 'more likely than not' that what is alleged actually occurred?).

Financial Hardship

7. Mr Reynolds made representations that he will suffer serious financial hardship if he has to pay any financial penalty. Mr Reynolds asserted that he has provided the Authority with verifiable evidence (where possible) which establishes that payment of the financial penalty will cause him serious financial hardship. Mr Reynolds stated that: (i) he and his wife were only discharged from bankruptcy last year; (ii) his house was repossessed on August 2011 (he and his family have been in rental accommodation since then); and (iii) he has no capital assets which he is able to sell to pay any financial penalty imposed on him. Mr Reynolds went on to assert that as his annual liabilities exceed £50,000 and because he has not only to provide for himself but also his wife and children, his income and capital will be reduced to nil and he will be bankrupt if he has to pay any financial penalty. Mr Reynolds also asserted that his alleged misconduct is not serious enough to warrant the imposition of a financial penalty notwithstanding the fact it will cause him serious financial hardship.

8. The Authority has found that it does not accept Mr Reynolds' representations that he is unable to pay any financial penalty due to reasons of serious financial hardship. The Authority rejects Mr Reynolds' assertion that he has provided full, frank disclosure of verifiable evidence that he will suffer serious financial hardship. The Authority notes that Mr Reynolds has not provided a recent 'Statement of Means' form (or any equivalent documentation) setting out his full financial circumstances. At best, Mr Reynolds has only provided partial disclosure of his financial position. Accordingly, the Authority has found that Mr Reynolds has provided insufficient evidence to demonstrate that he would suffer serious financial hardship. Further (and notwithstanding the foregoing), the Authority considers that Mr Reynolds misconduct is serious enough such that a financial penalty should be imposed on him even if it would cause him serious financial hardship.

Mr Reynolds' recommendations of UCIS and GTEPs

9. Mr Reynolds made representations that sought to justify the suitability of his recommendations of UCIS and GTEPS to the eight clients whose files were examined by the Authority. Mr Reynolds stated that all his clients received a suitability letter from him prior to deciding to invest in products that he recommended and that copies of the suitability letters to the eight clients whose files were examined by the Authority were held on those clients' files

10. Mr Reynolds also made representations that those eight clients' ATR were higher than the Authority contended and that therefore the clients' ATR did match the risk of the products he had recommended to them. In support of his assertion, Mr Reynolds variously alleged that those clients had undeclared income, were investors with a high risk tolerance who fully understood the risks they were

running or have changed their account after the event/are now lying. Mr Reynolds also suggested that the fact that his clients were long standing and sought advice from the product providers (or were in business) was sufficient to establish that they had a high tolerance for risk.

11. The Authority has found that notwithstanding Mr Reynolds' representations, he is unable to justify the suitability of his recommendations of UCIS and GTEPS to the eight clients whose files were examined by the Authority. The Authority accepts Mr Reynolds' representations that all but one of the eight client files examined by the Authority contained copies of suitability letters. However, the Authority notes that the allegations and matters in the Warning Notice in relation to the suitability letters is not that they did not exist on the office files, but rather that they were not sent to Mr Reynolds' clients and that a number of them were prepared retrospectively. The Authority notes that Mr Reynolds has not addressed the latter allegation or matter in his written representations. Further, the Authority notes that seven of the eight clients whose files were examined by the Authority informed the Authority that they did not receive suitability letters from Mr Reynolds. This has led the Authority to reject Mr Reynolds representations that the eight clients whose files were examined by the Authority received a suitability letter from him prior to deciding to invest in the products he recommended.

12. The Authority also rejects Mr Reynolds representations in which he variously alleges that those eight clients had undeclared income, were investors with a high risk tolerance who fully understood the risks they were running and have changed their account after the event/are now lying on the basis of all the information provided to it during the course of its investigation. The Authority notes that Mr Reynolds' allegations against his former clients are uncorroborated whilst the eight clients' accounts of Mr Reynolds' conduct are supported (amongst other things) by other witnesses. Further, the Authority has found no documentary evidence on the client files (other than the suitability letters which the Authority has found were prepared retrospectively) which demonstrate that risks were explained. The Authority rejects Mr Reynolds' suggestion that the fact that his clients were long standing and sought advice from the product providers (or were in business) was sufficient to establish that they had a high tolerance for risk. Mr Reynolds' clients were entitled to rely on him to ensure that the recommendations he made to them were suitable, but he recommended the products knowing that he could not justify their suitability. It was Mr Reynolds' responsibility to ensure that any recommendations he made were suitable. For the foregoing reasons, the Authority has concluded that Mr Reynolds knew he could not justify the suitability of the recommendations he made to each of the eight clients whose files were examined by the Authority, because the risk of the product did not match the clients' ATR, but he proceeded to make the recommendations anyway.

Mr Reynolds' falsification of signatures on sophisticated investor certificates

13. Mr Reynolds made representations that he did not falsify or direct the falsification of the signatures of two clients on sophisticated investor certificates in order to suggest that UCIS products could legitimately be promoted to them. Mr Reynolds did not deny that the signatures of the two clients on the sophisticated investor certificates were forged - he simply asserted that he did not forge them himself.

14. The Authority has found that although there is no direct evidence that Mr Reynolds personally falsified or directed the falsification of the signatures of the two clients on the sophisticated investor certificates, both clients maintain that they did not sign the certificates and that their signatures have been forged. Further, the Authority notes that the allegations and matters in the Warning Notice in relation to the forged signatures of the two clients on the sophisticated investor certificates is that Mr Reynolds deliberately falsified them or directed the falsification of the signatures. In light of the fact that both the sophisticated investor certificates are

countersigned by Mr Reynolds, the Authority has found that Mr Reynolds was knowingly involved in the falsification of the signatures of the two clients on the sophisticated investor certificates.

Mr Reynolds' inflation of clients' investment valuations

15. Mr Reynolds made representations that he had not as alleged deliberately produced, or directed the production of, inflated valuations for at least two clients in an attempt to mislead them and conceal the poor performance of investments he had recommended.

16. The Authority has found that although there is no direct evidence that Mr Reynolds deliberately produced, or directed the production of, inflated valuations for at least two clients, it is clear that inflated valuations were in fact produced by Aspire. In the circumstances set out in this Decision Notice, the Authority has found that Mr Reynolds was knowingly involved in the production of inflated valuations for at least two clients in an attempt to mislead them and conceal the poor performance of investments he had recommended.