
FINAL NOTICE

To: Abbey National plc

Of: Abbey National House
2 Triton Square
Regent's Place
London NW1 3AN

Effective Date: 25 May 2005

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

1. THE PENALTY

- 1.1. The FSA gave you a Decision Notice on 17 May 2005 which notified you that pursuant to section 206 of the Financial Services and Markets Act 2000, the FSA had decided to impose a financial penalty of £800,000 on Abbey National plc ("Abbey/the Firm")
- 1.2. Abbey has confirmed that it will not be referring this matter to the Financial Services and Markets Tribunal. Accordingly, for the reasons set out below and having agreed with the Firm the facts and matters relied on, the FSA imposes on Abbey a financial penalty of £800,000 ("the penalty"). This Notice takes effect on 25 May 2005.
- 1.3. The penalty is imposed in respect of the following conduct:
 - mishandling of customers' mortgage endowment complaints in the period between 1 October 2001 and 30 September 2003;

- providing the FSA with inaccurate and potentially misleading information in response to the April 2002 'Tiner Letter'¹.

2. REASONS FOR THE PENALTY

- 2.1. The firm accepts that in the period from 1 October 2001 to 30 September 2003 (“the relevant period”) it breached relevant regulatory rules and principles in relation to the handling of mortgage endowment complaints received from customers.
- 2.2. In particular, in the period between 1 October 2001 and 30 November 2001 the firm breached Rule 8.2.4 of the Personal Investment Authority rules (“the PIA Rules”) by failing to ensure that it investigated each mortgage endowment complaint adequately; and, in the period from 1 December 2001 to 30 September 2003 the firm breached FSA DISP Rule 1.2.22² by failing to take reasonable steps to ensure that it handled mortgage endowment complaints fairly and consistently.
- 2.3. As a result of concerns identified by FSA supervisors, the firm was required to commission an independent, expert report³ on the handling of mortgage endowment complaints in the relevant period. For the purposes of the report, the independent expert reviewed 371 mortgage endowment complaints handled by Abbey in Q4 2001, Q2 2002, Q4 2002, and Q2 2003 (“the sample”). The detailed findings in relation to the sample are particularised at paragraph 4.18 below but, in summary, the independent expert found complaint handling failures of:
- 22% in Q4 2001 (11 out of the 50 cases reviewed)
 - 30% in Q2 2002 (24 out of the 78 cases reviewed)
 - 22% in Q4 2002 (32 out of the 148 cases reviewed)
 - 29% in Q2 2003 (30 out of the 101 cases reviewed)
- 2.4. In the relevant period Abbey received 37,453 mortgage endowment complaints, decided 20,044 cases and rejected 18,593 (approximately 93%) of total cases decided. Abbey accepts that somewhere in the region of 5,000 of the cases rejected were improperly handled (approximately 26%). The mishandled cases include approximately 3500 complaints which were rejected when they should have been upheld.

¹ John Tiner's letter of 4 April 2002 to major firms emphasised the FSA's concerns about the way in which mortgage endowment complaints were being dealt with and listed 9 action points for firms to follow in order to avoid unfairness in respect of their handling of mortgage endowment complaints – “the Tiner points”.

² “DISP” - FSA Dispute Resolution: Complaints chapter of the FSA Handbook.

³ “The S.166 Report”

- 2.5. Although a detailed investigation of cases from every quarter in the four year period between 1 January 2001 and 31 December 2004 has not taken place, Abbey accepts that it is likely that there were similar levels of failure to handle cases correctly throughout that period. Abbey received approximately 65,000 mortgage endowment complaints in that period between 1 January 2001 and 31 December 2004.
- 2.6. Further, as a result of the nature and extent of the failings identified, it appears to the FSA that the firm has acted in breach of Principle 6 of the FSA's Principles for Businesses by:
- failing to pay due regard to the interests of its mortgage endowment customers and failing to treat such customers fairly.
- 2.7. Further, as a result of the nature and extent of the failings identified, it appears to the FSA that the firm has acted in breach of Principle 2 of the FSA's Principles for Businesses by:
- failing to act and/or conduct its business with due skill care and diligence in its handling of mortgage endowment complaints; and,
 - failing to exercise due skill care and diligence in respect of its written communications with the FSA concerning the handling of mortgage endowment complaints. In particular, in April and May 2002 Abbey wrote to the FSA in response to the Tiner letter confirming that it was already applying the nine 'Tiner points' in the handling of mortgage endowment complaints. In fact, the S.166 Report found material breaches of three of the Tiner Points in all of the three post-Tiner quarters which were sampled by the skilled person and in particular during April and May 2002 when Abbey wrote to the FSA. The FSA considers the Abbey response to have been unacceptable in the circumstances and considers that such conduct fell well below the standards expected of an authorised firm in its communications with the regulator.
- 2.8. The failings in mortgage endowment complaint handling are viewed by the FSA as being particularly serious because:
- (1) the failings related to the handling of complaints about advice which Abbey had given in relation to mortgage endowments - investment policies to be used by customers to repay their mortgage. The purchase of a house is for many people the most significant financial transaction of their lives and where any valid complaint regarding the sale of mortgage endowment policies is unfairly rejected, the consequences may result in serious consumer detriment;
 - (2) in the context of the numbers of complaints received by Abbey, the proportion of complaints that were actually mishandled was unacceptably high and the failings continued over a 2 year period;
 - (3) these failings in mortgage endowment complaints handling resulted in actual financial loss to a large number of Abbey's customers. In practice, the actual loss will be

limited to those customers who have suffered loss and whose complaints have been wrongly rejected. Of the 18,593 customers referred to in paragraph 2.4 above, approximately 3,500 of these (19%) had their complaints wrongly rejected. Based upon industry average figures of £5,500 for the average projected shortfall per case⁴, losses of up to £19 million may have been caused to those 3,500 customers. The further 1,500 customers have been exposed to the risk of loss because their complaints were rejected in circumstances where the firm should have sought further information before making its decision to reject, although again the actual loss will be limited to any complaints from the 1,500 which have been wrongly rejected.

- (4) the failings occurred at a time when there was a high level of awareness of the problems surrounding mortgage endowment sales, and a high level of awareness within the financial services industry of the importance of handling mortgage endowment complaints properly;
- (5) the failings at Abbey continued after 'the Tiner letter' and the failings continued notwithstanding Abbey's assurances to the FSA that it was already complying with the Tiner points;
- (6) the failings were not brought to the regulator's attention by the firm, but were discovered by the FSA following enquiries and requests for information.

2.9. Whilst these mortgage endowment complaint handling failings merit a significant financial penalty, the FSA considers that the firm's conduct has been mitigated by the co-operation demonstrated by Abbey and the remedial action proposed. Action taken by the firm includes the following:

- (1) Since becoming aware of the emerging findings of the S.166 Report, the firm has demonstrated a high level of co-operation with the FSA and a willingness to remedy any consumer detriment which may have been caused. The firm has put forward a voluntary proposal to review all mortgage endowment complaints rejected since 1 January 2000 and to pay redress in any case where the complaint has been unfairly rejected. An independent firm of accountants will be appointed to oversee this review of past mortgage endowment complaints. These steps will mean that Abbey will have in place processes which should ensure that past mortgage endowment complainants will be offered redress where appropriate. Further by virtue of the co-operation with the FSA displayed by Abbey and the necessary remedial action being taken, the risk of disadvantage to customers should be minimised.
- (2) On becoming aware of the FSA's intention to investigate the matter, the firm has demonstrated its willingness to co-operate fully with the investigation. Abbey has moved quickly to agree the facts of the case, ensuring efficient resolution of the

⁴ ABI Jan 2005 – "Endowment Mortgages – the facts"

matter, and the firm has received full credit for settlement of the disciplinary case at a very early stage.

(3) Abbey has committed itself to the adoption of a new approach to mortgage endowment complaints through a complete revision of its complaints handling procedures. New processes and training, designed and delivered in conjunction with an independent firm of accountants, were initiated in December 2004 for all complaints handlers. These revisions to Abbey's complaints handling function include the following:

- establishment of a new single complaints handling centre which has been formed by drawing together Abbey's three central complaints handling teams;
- engaging additional resources to meet the demands of the new complaints handling process and the review of past mortgage endowment complaints;
- increase in the level of training provided to staff engaged in complaints handling;
- establishment of a separate group to review past mortgage endowment complaints in order to ensure customers were treated fairly, taking into account the most up-to-date regulatory guidance;
- obtaining external support and guidance to support the required changes to the complaints handling function;
- monitoring of quality assurance work on the new mortgage endowment complaints system by an independent firm of accountants.

These steps are designed to ensure that past mistakes in the handling of mortgage endowment complaints are not repeated in the future.

(4) Abbey has made the issue of mortgage endowment complaints handling a regular item on the agenda of its Board meetings and Executive Committee meetings, until the matter has been concluded in a manner acceptable to the FSA, the Board and the Executive Committee.

2.10. In reaching its decision, the FSA has also taken account of the fact that, following the period in which the failures occurred, Abbey has undergone significant change, in terms of its strategic direction, senior management, and operating model, and the fact that in November 2004, Abbey was acquired by Banco Santander Central Hispano SA "BSCH". BSCH has demonstrated its commitment to treating customers fairly by supporting a comprehensive redress package for customers who have been disadvantaged.

2.11. Accordingly, Abbey has received credit for this in the amount of the financial penalty the FSA has decided to impose. Without this level of co-operation, the financial penalty would have been substantially higher.

3. RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES

3.1. Section 206 of FSMA 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".

3.2. The Financial Services and Markets Act 2000 (Transitional Provisions and Savings) (Civil Remedies, Discipline, Criminal Offences etc (No 2) Order 2001 ("the Pre N2 Misconduct Order") provides, at Article 8(2), that the power conferred by Section 206 of FSMA can be exercised by the FSA in respect of failures by a firm to comply with any provisions specified in Rule 1.3.1(6) of the PIA Rules as if the firm had contravened a requirement imposed by FSMA.

3.3. PIA Rule 1.3.1 (6) provided that a PIA Member which failed to comply with the PIA Rule 1.3.1(2) or any of the SIB Principles is liable to disciplinary action.

3.4. PIA Rule 1.3.1 (2) provided that a PIA Member must obey the PIA Rules.

Complaint handling

3.5. PIA Rule 8.2.4 provided that a PIA Member must ensure that each complaint was promptly and adequately investigated

3.6. FSA Rule DISP 1.2.22 provides that a firm must put in place appropriate management controls and take reasonable steps to ensure that it handles complaints fairly, consistently and promptly and that it identifies and remedies any recurring or systemic problems as well as any specific problem identified by a complaint.

FSA Principles for Businesses

3.7. FSA Principle 2 provides that a firm must conduct its business with due skill, care and diligence.

3.8. FSA Principle 6 provides that a firm must pay due regard to the interests of its customers and treat them fairly.

4. FACTS & MATTERS RELIED ON

Regulated Firm - background

- 4.1. Abbey is a significant provider of personal financial services including mortgages. During the relevant period, it both sold and advised on mortgage endowment policies issued in connection with mortgages.
- 4.2. Up until Q4 2003, Abbey's complaints handling processes were organised in a fragmented manner. However, with effect from Q4 2003, Abbey's various complaints handling functions were brought together under one primary area of responsibility.
- 4.3. Until 30 November 2001, Abbey and its relevant subsidiary companies were regulated by the PIA. Since then they have been authorised and regulated by the FSA.

Regulatory Context

- 4.4. Abbey's failings should be placed in the regulatory context of 1999 to 2003; that is - the failings occurred at a time when there was a high level of awareness within the industry of the issues surrounding mortgage endowment sales and associated concerns regarding the handling of complaints regarding mortgage endowment sales.
- 4.5. Since the introduction of the PIA Rules⁵ firms have been subject to an obligation to ensure that complaints are promptly and adequately investigated. The FSA rules, which replaced the PIA rules, require each firm to take reasonable steps to ensure that it handles complaints fairly, consistently and promptly. This obligation had particular importance in relation to mortgage endowments. In 1999, the FSA and the PIA started a programme of work on mortgage endowments to help ensure that consumers understood the consequences of the changed economic environment and to check that firms' selling practices and complaints handling procedures were adequate.
- 4.6. The FSA publicly stated in December 1999 that an industry-wide review of mortgage endowment sales along the lines of the Pensions Review would be disproportionate and in October 2000 that the appropriate mechanism for delivering redress in relation to mis-sales of mortgage endowments was through the complaints handling processes of firms. The October 2000 statement was contained in the FSA's "Progress Report on Mortgage Endowments" which confirmed that the existing complaints handling process, in conjunction with the issue and promotion of factsheets, was viewed by the FSA as the most effective way of ensuring redress for those consumers who had lost out as a result of mis-selling and that there were no grounds for a blanket industry-wide review.

⁵ PIA rules were introduced in 1994

- 4.7. The FSA's factsheet "Endowment Mortgage Complaints" was also released in October 2000. It explained that the customer may have incurred no loss at that date, but that if a mortgage endowment holder had any complaint, this should be taken up with the firm which sold him the endowment. The factsheet outlined how to take a case to the Financial Ombudsman Service ("the FOS") if the firm's response was unsatisfactory. It included information about how consumers could seek compensation if they felt they were in any way misled at the point of sale and may have lost out financially as a result. This factsheet was updated at regular intervals and was included in the reprojection letters that firms were required to send out to all mortgage endowment holders.
- 4.8. The importance of mortgage endowment complaints-handling processes was highlighted again in November 2000, via PIA Regulatory Update 80, and again in July 2001, via PIA Regulatory Update 91.

The Tiner Letter 4 April 2002

- 4.9. On 4 April 2002, the FSA sent a letter ("the Tiner letter") to all major firms who acted as product providers or financial advisers in relation to mortgage endowment policies. This letter set out the FSA's concerns about the way in which complaints about mortgage endowments were being dealt with. Most notably, its purpose was to accentuate the importance of fair handling of complaints. Firms were asked to respond to the letter and to review and, if necessary, to revise their complaints-handling procedures in the light of the concerns expressed.
- 4.10. The Tiner letter included an annex which listed nine specific action points for firms wanting to avoid unfairness in respect of their handling of mortgage endowment complaints ("the Tiner Points") which advised firms to:
- (1) recognise in the assessment of the complaint that the key risk for the consumer is that the endowment may not repay the mortgage loan ("TP1");
 - (2) avoid too narrow a view of the scope of the advisory duty in the context of mortgage advice ("TP2");
 - (3) recognise that oral evidence can be good and sufficient evidence, avoiding too ready a dismissal of evidence from the consumer which is not supported by documentary proof ("TP3");
 - (4) investigate the issue diligently in particular so as to take into account the selling practices at the time, the training, instruction, sales scripts and incentives given to advisers at the time and the track record of the particular adviser ("TP4");
 - (5) go the extra mile to clarify ambiguous issues or conflicts of evidence before finding against the consumer ("TP5");

- (6) avoid making a conclusive assumption that a pre-existing endowment held at time of sale, whether for purposes of savings or mortgage repayment, is sufficient evidence of understanding and acceptance of the key risk (“TP6”);
- (7) avoid making too literal and narrow an interpretation of the issue of the complaint as expressed by the consumer (“TP7”);
- (8) avoid rejecting complaints solely on the basis that the consumer signed a proposal form or failed to exercise the cancellation right and so must be presumed to have been satisfied with the advice and the product at time of sale (“TP8”); and
- (9) avoid claiming as evidence of risk warning at time of sale (so as to justify rejection of the complaint) either:
 - (a) the absence of a statement in product literature that repayment of the mortgage was guaranteed; or
 - (b) a statement in product particulars that the firm will monitor the plan and advise the consumer if the level of contribution is insufficient for the target amount to be repaid (“TP9”).

Mortgage Endowment Complaint Handling by Abbey

- 4.11. In the period from 1 January 2001 until the end of September 2002 Abbey received approximately 5,900 mortgage endowment complaints. From October 2002, Abbey experienced a sudden increase in the volume of its mortgage endowment complaints, receiving a further 9,653 complaints during Q4 2002 alone. The dramatic rise in the number of mortgage endowment complaints received by Abbey from October 2002 was due to a general increase in awareness on the part of consumers that their endowment policy might not generate enough money to pay off their mortgage loan at maturity. This increased awareness resulted from 'reprojection' letters that were issued to all mortgage endowment policyholders from 2002 onwards. The purpose of the reprojection letters was to provide all mortgage endowment policyholders with clear and timely information about any shortfall they might be facing on their endowment and the options for addressing that shortfall. The reprojection letters were also accompanied by the FSA factsheet “*Endowment Mortgage Complaints*” described at 4.8 above. Complaint volumes continued at a similar level from the period Q4 2002 onwards. During the period 1 October 2001 to 30 September 2003 Abbey rejected approximately 18,500 mortgage endowment complaints. This amounted to a rejection rate of approximately 93% of total mortgage endowment complaints decided in that period. In the four year period from 1 January 2001 to 31 December 2004, Abbey received approximately 65,000 mortgage endowment complaints, it decided 59,917 complaints and it rejected 48,793 of these - approximately 81%.
- 4.12. During the course of monitoring the clearance of Abbey's complaint backlog in about May 2003, the FSA identified an emerging trend of cases where Abbey had previously rejected a

complaint but which on referral to the FOS resulted in either a settlement or ex-gratia payment being offered to the customer ("two-stage cases").

- 4.13. Concerned by this trend, the FSA carried out a qualitative file review of a random sample of 50 "closed" FOS cases that were initially rejected by Abbey but which on referral to the FOS resulted in either a decision being made against the firm or in Abbey offering the customer an ex-gratia payment or settling the complaint.
- 4.14. The FSA's review of a small selection of these two-stage cases identified qualitative complaint-handling failures. In particular, the FSA's review identified that Abbey's complaint files were often incomplete or lacked key point-of-sale documentation such that there was frequently insufficient evidence to support the initial decision reached. In addition, in the FSA's view there were indications of a narrow approach being taken towards complaints with the subject of the complaint not being fully investigated. The FSA concluded that its findings in relation to this sample were sufficiently serious to warrant a wider, independent review.
- 4.15. Under S.166 of FSMA, a skilled person reviewed a sample of Abbey's individual mortgage endowment complaint files to assess their compliance with relevant regulatory requirements and - for complaints handled after the Tiner letter - specifically to assess their compliance with the standards expressed in that letter. The S.166 Report concluded that there were significant levels of failure to handle cases correctly throughout the sample period.

Breaches of Rules

- 4.16. Abbey accepts the findings of the S.166 Report which is relied upon for these purposes by the FSA, and Abbey accepts on the basis of that evidence (the details of which are particularised in paragraphs 4.17 to 4.26 below) that the following breaches have occurred:
 - (1) Breach of PIA Rule 8.2.4 in that Abbey failed to ensure that each complaint that it received was adequately investigated between 1 October 2001 and 30 November 2001;
 - (2) Breach of DISP Rule 1.2.22 in that Abbey failed to take reasonable steps to ensure that it handled complaints fairly and consistently between 1 December 2001 and 30 September 2003.

The S.166 Review

- 4.17. On 8 March 2004, the FSA issued Abbey with a requirement notice under S.166 of FSMA which required the firm to appoint a skilled person to provide the FSA with information, analysis and expert opinions in respect of Abbey's complaint handling framework, consistency of approach with complaint handling procedures, and compliance with appropriate regulations and guidance.
- 4.18. On 9 April 2004 Abbey appointed a skilled person to carry out a review of its complaint handling in accordance with that requirement. On 17 November 2004 the skilled person produced a report based on an analysis of a sample of 484 complaint cases handled by Abbey

in the periods Q4 2001, Q2 2002, Q4 2002 and Q2 2003 ("the sample period"). Of those 484 complaint cases, 371 concerned mortgage endowment complaints ("the sample cases").

Results of the S.166 review - cases wrongly rejected

4.19. The S.166 Report identified significant levels of failure to handle mortgage endowment complaints correctly throughout the sample period. In failing to handle complaints correctly, Abbey either:

- (1) rejected complaints which should have been upheld; or,
- (2) rejected complaints when it should have made efforts to acquire further information before reaching a decision. This information, had it been sought, available and acquired, may have been material to a decision whether or not to uphold the complaint.

The S.166 Report concluded that in relation to the sample cases Abbey failed to handle the mortgage endowment complaints correctly in these respects, as follows:

Sample Period	(a) Rejected complaints that should have been upheld %	(b) Cases where further information should have been sought before decision made %	Total mishandled complaints
Q4 2001	14%	8%	22% (11 out of 50 cases reviewed)
Q2 2002	23%	7%	30% (24 out of 78 cases reviewed)
Q4 2002	16%	6%	22% (32 out of 142 cases reviewed)
Q2 2003	21%	8%	29% (30 out of 101 cases reviewed)

Results of the S.166 review - Inadequate Investigations

4.20. In assessing whether Abbey had handled its mortgage endowment complaints in accordance with regulatory requirements, the skilled person considered whether Abbey had given sufficient and appropriate consideration, amongst other matters, to the following factors:

- (a) Establishing the customer's attitude to risk at the point of sale;
- (b) In cases where point of sale documentation was incomplete and/or missing, not rejecting the complaint without further investigation;
- (c) The overall suitability of the sale, regardless of the subject of the complaint;

(d) Issues outside the subject matter of the complaint.

4.21. Having regard to regulatory requirements and specifically to the factors set out above, the results of the review identified deficiencies which included the following:

Deficiencies	No. of sample cases affected
Cases incorrectly rejected by Abbey where no/little point of sale documentation available	61 (16%)*
Insufficient steps taken to establish the customer's attitude to risk at the point of sale	57 (15%)*
Subject of complaint not fully investigated	29 (8%)*
*as a Percentage of the 371 sample cases.	

Results of the S.166 review - The Tiner letter 2 April 2002

4.22. In relation to mortgage endowment complaints concluded *after* the Tiner letter, the skilled person also considered whether Abbey had given appropriate consideration to the matters set out in that letter.

4.23. Of the sample cases reviewed, 321 cases were concluded by Abbey in the period after the Tiner letter. In relation to those cases, the results of the skilled person's review identified a high level of failure against 3 of the 9 TPs, across all of the three post-Tiner quarters sampled by the skilled person (i.e. Q2 2002, Q4 2002 and Q2 2003), namely TP 9 (26%), TP 1 (21%) and TP 5 (6%).⁶

4.24. As demonstrated by the findings set out in the tables above, during the relevant period Abbey rejected a high number of mortgage endowment complaints where there was either no or insufficient information on which to assess the suitability of the sale and therefore insufficient information on which to reach a proper conclusion. In particular the section 166 Report identified that in handling mortgage endowment complaints, Abbey:

⁶ TP1: The need to recognise that in the assessment of the complaint that the key risk for the consumer is that the endowment may not repay the mortgage loan;

TP5: the need to go the extra mile to clarify ambiguous issues or conflicts of evidence before finding against the consumer;

TP9: the need to avoid claiming as evidence of risk warning at time of sale (so as to justify rejection of the complaint) either:

(a) the absence of a statement in product literature that repayment of the mortgage was guaranteed; or

(b) a statement in product particulars that the firm will monitor the plan and advise the consumer if the level of contribution is insufficient for the target amount to be repaid.

- (1) failed to recognise and consider that the key risk for the customer is that the endowment may not repay the mortgage at the end of the term ("the shortfall risk");
- (2) took insufficient steps to establish the customer's attitude to risk at the time of sale.

Results of the S.166 review - Communication with customers

- 4.25. The review also highlighted matters in respect of Abbey's communication with customers which the FSA considers to be serious. In particular, in cases of rejected complaints where there was no point of sale documentation, Abbey's decision letters to customers contained the following wording:

"Our advisors are trained to follow company procedures and I have no reason to believe that our advisors recommendation would not have been appropriate for your circumstances"

"It is a requirement of the Financial Services Act that a fact-find is completed by financial advisors prior to making any recommendation for a life assurance product. This would involve a discussion of your personal circumstances and your future plans. To maintain compliance with the Regulators requirement's advisors are trained to high standards and I therefore have no reason to believe that the recommendation provided in [1989] would not have been appropriate for your circumstances at the time".

"Our advisor would not have recommended an endowment mortgage unless it was agreed that you were prepared to accept a degree of risk in respect of the repayment of your mortgage, in return for the potential of a cash surplus at the end of the mortgage term..."

"As maturity values are not guaranteed, regular reviews of endowment plans are carried out as detailed in the provisions booklet issued to you with your plan schedule. These reviews are designed to ensure that our customers can take any necessary action to keep their plans on track to repay their mortgage. Our advisor would have explained this to you as a key feature of the plan and this should hopefully have reassured you that any risks involved could be minimised".

"I have referred to the "cooling off" notice as this gives you a further 14 days to reconsider your decision. As I can find no evidence that you exercised this option or queried the plan, I think it is reasonable to assume that you understood the key features of the plan and were happy to proceed".

The FSA considers that the use of such wording may have discouraged customers from pursuing their complaint further, for example by referring their complaint to the FOS.

Results of the S.166 review: Two-stage cases

- 4.26. In relation to the two-stage cases, the skilled person concluded that in all 20 of the two-stage cases reviewed Abbey could have settled/upheld the complaint based on the information that was available to the case-handler when the complaint was first considered.

Results of the S.166 review – Further conclusions of the FSA

- 4.27. Based on the matters set out above, it appears to the FSA that during the relevant period Abbey's handling of mortgage endowment complaints was indicative of an approach which favoured the firm's interests over those of its customers. In particular, this is demonstrated by the fact that in the absence of any point of sale information, rather than attempting to reconstruct what took place at the time of the sale or resolving any gaps in the point of sale information, Abbey often rejected the customer's complaint.
- 4.28. Furthermore, it appears to the FSA that in circumstances where Abbey found its decision to reject a complaint was challenged, for example, where it became aware of a referral to the FOS or where the customer responded directly to Abbey and disputed the decision reached, Abbey often reversed its decision and offered the customer redress. This course of action appears to have resulted from the challenge to its decision, rather than from any new evidence coming to light, thereby avoiding any adverse finding being made against the firm. As indicated above, the findings of the skilled person's review established that in all 20 of the two-stage cases sampled, Abbey could have upheld/settled the complaint in the first instance.

Breaches of Principles

- 4.29. The extent and seriousness of Abbey's failings in connection with its handling of mortgage endowment complaints together with its failure to identify or remedy the problems prior to the intervention of the FSA, indicate that Abbey also failed to meet the regulatory standards required of it by the FSA Principles.
- 4.30. The seriousness of Abbey's failings are further demonstrated by the fact that they occurred during a period when there was a high-level of industry awareness of the importance of fair and adequate complaint-handling. Despite a number of specific measures (e.g. RU91, RU80 and the FSA's October 2000 Announcement) aimed at raising standards in the area of complaint-handling and which highlighted regulatory expectations, Abbey failed to ensure that it handled its mortgage endowment complaints fairly and adequately.
- 4.31. In addition, Abbey's failings continued after and notwithstanding the detailed guidance set out in the Tiner letter and notwithstanding Abbey's express assurances to the FSA that its practice in relation to the handling of mortgage endowment complaints was consistent with the standards expressed in that letter. As outlined above, the results of the skilled person's review identified high levels of failure against three of the nine Tiner points at both the time of and in the sample period post the Tiner letter.
- 4.32. Accordingly, by virtue of the failings identified above, it appears to the FSA that Abbey has breached the following regulatory principles:
- In breach of FSA Principle 2, Abbey failed to conduct its business with due, skill care and diligence in relation to its handling of mortgage endowment complaints. Further, Abbey failed to exercise due skill care and diligence in respect of its written communications with the FSA concerning the handling of mortgage endowment

complaints. In particular, in April and May 2002 Abbey wrote to the FSA in response to the Tiner letter confirming that it was already applying the nine 'Tiner points' in the handling of mortgage endowment complaints. In fact, the S.166 Report found material breaches of three of the Tiner Points in all of the three post-Tiner quarters which were sampled by the skilled person and, in particular, during April and May 2002 when Abbey wrote to the FSA. The FSA considers Abbey's response to have been unacceptable in the circumstances and considers that such conduct fell well below the standards expected of an authorised firm in its communications with the regulator.

- In breach of FSA Principle 6, Abbey did not, in relation to its handling of mortgage endowment complaints, pay due regard to the interests of its customers and treat them fairly; in particular it did not assess mortgage endowment complaints in accordance with the standards set out in the Tiner letter, on occasions Abbey placed its own interests above those of its customers and it communicated with customers in such a manner that may have discouraged customers from exercising their rights and referring their complaints to the FOS.

5. RELEVANT GUIDANCE ON PENALTY

- 5.1. The principal purpose of the imposition of a financial penalty is to promote high standards of regulatory conduct. It seeks to do this by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefit of compliant behaviour.
- 5.2. The FSA's policy on the imposition of financial penalties is set out in Chapter 13 of the Enforcement manual ("ENF 13") which forms part of the FSA Handbook. Paragraph 13.3 of the Enforcement Manual sets out the factors that may be of particular relevance in determining the appropriate level of financial penalty.
- 5.3. Article 8(4) of the Pre-N2 Misconduct Order provides that, where the FSA decides to impose a financial penalty it must have regard to:

"any statement made by the self-regulating organisation...which was in force when the conduct in question took place with respect to the policy on the taking of disciplinary action and the imposition of, and amount of penalties (whether issued as guidance, contained in the rules of the organisation or otherwise)".
- 5.4. In all material respects, the relevant PIA guidance, contained in Annex D of "PIA's Approach to Discipline – Statement of Policy" issued in December 1995, required consideration of the same factors as are identified in Chapter 13 of the Enforcement Manual. Both have been taken into account by the FSA in determining the appropriate sanction in this case. Chapter 13 of the Enforcement Manual at paragraph 13.3.4 states that the criteria listed in the Manual are

not exhaustive and all relevant circumstances of the case will be taken into consideration. PIA's Statement of Policy also makes it clear that the criteria for determining the level of sanction are not to be applied rigidly, as stated in paragraph 2 of Annex D:

“Each case is different and needs to be treated on its own merits. It is not possible to apply a mechanistic approach to the determination of the circumstances in which disciplinary action should be taken or of the sanctions to be applied. The criteria... should not be treated as exhaustive. Nor should it be assumed that regard would necessarily be had to a particular criterion in any given circumstances”.

- 5.5. In determining whether a financial penalty is appropriate and its level, the FSA is required therefore to consider all the relevant circumstances of the case. The FSA considers the following factors to be *particularly* relevant in this case:

Seriousness

- 5.6. The FSA has had regard to the seriousness of the contraventions, including the nature of the requirements breached, the number and duration of the breaches, the number of consumers who were exposed to risk of loss and the number of consumers to whom actual loss will have been caused. The level of financial penalty must be proportionate to the nature and seriousness of the contravention. Details of the breaches identified in this case are set out above. For the reasons detailed below the FSA considers that the breaches identified in this case are of a serious nature:

- (1) The failings in complaints handling related to mortgage endowments – investment policies to be used by customers to repay their mortgage loan at maturity;
- (2) In the context of the numbers of complaints received by Abbey, the proportion of complaints mishandled was unacceptably high;
- (3) The failings in mortgage endowment complaints handling continued over a 2 year period and in the context of a 4 year period in which it is likely that there were similar levels of failure;
- (4) The failings in mortgage endowment complaints handling resulted in actual loss to a large number of Abbey's mortgage endowment customers, the details of which are set out in paragraphs 2.4 and 2.7(3) above;
- (5) The failings occurred at a time when there was a high level of industry awareness about the importance of proper mortgage endowment complaint handling; and,
- (6) The failings continued after the April 2002 Tiner letter and notwithstanding Abbey's assurances to the FSA that it was already complying with the Tiner points.

Nature of conduct – ENF 13.3.3(2)

- 5.7. The FSA has not determined that Abbey deliberately breached the relevant rules and principles. However, it appears to the FSA that during the relevant period Abbey's handling of mortgage endowment complaints was indicative of an approach which, when relevant evidence was absent or when the available evidence inconclusive, resulted in the interests of the firm being favoured over those of the customer. The firm continued to mishandle mortgage endowments complaints in this way; despite being put on notice of the risks of such an approach by the April 2002 Tiner letter, and notwithstanding Abbey's assurances to the FSA that in handling individual mortgage endowment complaints it was already applying the Tiner points.

The size, financial resources and other circumstances of the firm, and the amount of profits accrued or loss avoided

- 5.8. Abbey received approximately 65,000 mortgage endowment complaints between 1 January 2001 and 31 December 2004.
- 5.9. The FSA has had regard to the fact that the firm has sufficient resources to pay the penalty in addition to the substantial sums which will be paid to customers as a result of the redress exercise which the firm proposes to undertake. The FSA has also taken account of the fact that Abbey has incurred substantial costs as a result of the s.166 Report which was required by the FSA and the fact that the firm will incur further cost as a result of carrying out the redress exercise.
- 5.10. The FSA has not determined that Abbey deliberately set out to accrue additional profits or avoid a loss through the mishandling of mortgage endowment complaints. Nevertheless, the effect of rejecting complaints which should have been upheld was that the firm in fact avoided the cost of having to make redress payments at the time of the complaints. As a result of the FSA intervention Abbey now proposes to review all of the mortgage endowment complaints which it rejected since 1 January 2000 and will be paying redress to every customer whose complaint should have been upheld. This, along with the cost to Abbey of conducting the redress exercise and section 166 review, will mean that there will be no net gain to the firm as a result of the complaints mishandling.

Conduct following the contravention

- 5.11. The FSA has had regard to the firm's conduct following the discovery and reporting of the complaint handling deficiencies by the FSA Supervision team. Following initial enquiries and analysis by Supervision, in early 2004 the FSA required the firm to appoint a s.166 skilled person to review the firm's handling of mortgage endowment complaints.
- 5.12. Since the delivery of the report by the skilled person, Abbey has demonstrated a high level of co-operation with the FSA. Based on the findings of the report, Abbey has proposed to review and revise its procedures for dealing with mortgage endowment complaints. The firm has proposed a comprehensive review of all mortgage endowment complaints rejected since

1 January 2000, and has agreed to pay full redress to customers whose complaints should have been upheld.

- 5.13. Following its referral to Enforcement, the firm has been fully co-operative with the Enforcement action. Abbey agreed the facts quickly ensuring an efficient resolution of the investigation and full credit is given for settlement at the earliest opportunity.
- 5.14. The level of financial penalty imposed in this case reflects the co-operative approach adopted by the firm during the enforcement process as well as its agreement to conduct a review and redress exercise for its mortgage endowment customers. In the absence of such co-operation a significantly higher financial penalty would have been imposed.

Disciplinary record and compliance history

- 5.15. On 9 December 2003 the FSA imposed a financial penalty in the sum of £2m on Abbey National plc in respect of breaches relating to the firm's former systems and controls and anti-money laundering arrangements. On the same date a financial penalty in the sum of £320,000 was imposed upon Abbey National Asset Managers Limited in respect of breaches relating to the company's former systems and controls arrangements.

Previous action taken in relation to similar failings

- 5.16. In deciding on the level of penalty, the FSA has taken into account penalties levied by previous regulators and by the FSA.

6. IMPORTANT

This Final Notice is given to the Firm in accordance with section 390 of the Act

Manner of and time for Payment

The Penalty must be paid in full by the Firm to the FSA no later than 9 June 2005.

If the Penalty is not paid

If all or any of the Penalty is outstanding on 10 June 2005, the FSA may recover the outstanding amount as a debt owed by the Firm and due to the FSA.

Publicity

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

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

FSA contacts

For more information concerning this matter generally, you should contact Martin Cole at the FSA (direct line: 020 7066 1706 /fax: 020 7066 1707)

Julia MR Dunn

Enforcement Division

The Financial Services Authority