

## FINAL NOTICE

To: **Cathedral Motor Company Limited (trading as Arbury) (FSA ref: 308175)**

Of: **366 Nuneaton Road, Bulkington, Bedworth, Warwickshire CV12 9RR**

Date: **26 February 2007**

**TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (the FSA) gives you final notice of the publication of a statement that you have contravened requirements imposed on you under the Financial Services and Markets Act 2000.**

### **1. THE PUBLIC CENSURE**

- 1.1 The FSA gave Cathedral Motor Company Limited (Cathedral or the firm) a Decision Notice on 22 February 2007 which notified Cathedral that, pursuant to section 205 of the Financial Services and Markets Act 2000 (the Act), the FSA had decided to publish a statement (a public censure) that Cathedral had breached Principles 3 and 7 of the FSA's Principles for Businesses (FSA Principles) between 14 January 2005 and 23 May 2006 (the relevant period).
- 1.2 Cathedral has agreed that it will not be referring the matter to the Financial Services and Markets Tribunal. Accordingly, for the reasons set out below and, having agreed with Cathedral the facts and matters relied on, the FSA publishes this Final Notice, which constitutes a public censure or statement, detailing the contravention of requirements imposed on the firm under the Act.
- 1.3 In addition to the above Principle breaches, the following rules are also relevant:

- a. in the part of the FSA Handbook (the Handbook) entitled Senior Management Arrangements, Systems and Controls (SYSC), SYSC 2.1.1R, SYSC 3.1.1R and SYSC 3.2.20R;
- b. in the part of the Handbook entitled Insurance: Conduct of Business (ICOB), ICOB 4.2.2R, ICOB 4.4.1R and ICOB 5.5.14R; and
- c. in the part of the Handbook entitled Training and Competence (TC), TC 2.3.1R, TC 2.6.1R, TC 2.7.5AR and TC 2.8.1R.

## **2. REASONS FOR THE PUBLIC CENSURE**

### *Summary of conduct in issue*

- 2.1 The FSA publishes this public censure of Cathedral for breaches of the Principles referred to in paragraph 1 above. These breaches relate to failures by Cathedral as an authorised insurance intermediary in the sale of payment protection insurance (PPI) in connection with vehicle finance agreements.
- 2.2 These breaches, which are described in more detail in section 5 below, relate to Cathedral's failure to:
  - a. take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems (Principle 3); and
  - b. pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading (Principle 7).
- 2.3 Primarily, Cathedral failed to:
  - a. establish and maintain effective systems and controls, including a written compliance manual;
  - b. clearly and appropriately apportion compliance responsibilities amongst its senior management and to ensure that senior management obtained the necessary degree of regulatory knowledge;
  - c. ensure appropriate training and monitoring of its PPI sales staff;
  - d. keep adequate records, in particular in relation to the PPI sale on customer files but also in relation to the training of staff and internal decisions; and
  - e. provide customers with a copy of the initial disclosure document, a statement of demands and needs, or a statement of the total price, before conclusion of the PPI sale.
- 2.4 These failings resulted in an unacceptable risk of Cathedral's PPI sales leading to consumer detriment. Cathedral could not determine whether its sales staff were conducting sales in a manner which paid due regard to the needs of customers as there was limited or no monitoring of these sales staff. As a result of Cathedral's failure to keep adequate records, sales files held insufficient evidence to demonstrate that individual sales were suitable.

- 2.5 Cathedral's failure to provide customers with a copy of the initial disclosure document, a statement of demands and needs and a statement of the total price before conclusion of the PPI sale created a risk of consumer detriment. The timely provision of this information is important to enable a customer to make an informed decision as to whether to take out the PPI policy.
- 2.6 In deciding upon this disciplinary measure, the FSA recognises the following measures taken by Cathedral (described in more detail in section 6 below) which have served to mitigate the seriousness of its failings:
- a. Following the FSA's thematic visit in May 2006, Cathedral commenced remedial action in June 2006 in conjunction with compliance consultants. It has taken steps to improve its systems and controls, record keeping and training and monitoring arrangements to remedy the deficiencies identified;
  - b. The firm voluntarily suspended sales of PPI whilst it satisfied itself that future sales of PPI would be compliant; and
  - c. Cathedral has co-operated fully with the Enforcement action. Cathedral has agreed the facts quickly, ensuring efficient resolution of the matter, and has also agreed to carry out an appropriate customer contact exercise.

### **3. BACKGROUND**

#### *The Firm*

- 3.1 Cathedral is a franchised car dealership group, with four branches, all in the Midlands. Its primary business is the sale of new and used cars, with PPI sold if there is a financing agreement. Cathedral's four branches are each managed by a general manager, three of whom are also directors.
- 3.2 Cathedral has been authorised in respect of its sale of general insurance business, its only activity regulated by the FSA, since 14 January 2005. Four business managers (one at each branch) are responsible for the sale of PPI and the provision of financial advice to customers. No other member of staff is permitted by Cathedral to be involved in a customer-facing PPI role. Each business manager is supervised in relation to PPI matters by the relevant branch general manager. Cathedral's insurance customer base is predominantly retail.

#### *PPI*

- 3.3 Cathedral offers customers four levels of PPI cover: life; life and critical illness; life and disability; and life, accident and sickness and redundancy/business failure. A monthly premium is charged on all policies. The policies are manufacturer backed and are only sold in conjunction with manufacturer finance schemes.

#### *The Firm's Sales Process*

- 3.4 The sales process is conducted face to face between the business manager and the customer. Cathedral provides each business manager with point of sale software to use for each PPI sale. Although it was not consistently used by business managers, when used correctly this software produces and records a customer's statement of

demands and needs and subsequently generates an automated recommendation for the customer with a statement of total price. The sale is concluded when the customer signs the documentation prior to taking delivery of the car. No sales scripts are provided or used. All PPI sales are treated as advised sales and the same sales procedure is adopted at each branch.

#### *FSA thematic visit*

- 3.5 In November 2005 the FSA published on its website a report setting out the findings of the first phase of a thematic project conducted into the sale of PPI with credit arrangements. The FSA also issued in November 2005 a Dear CEO letter to the medium and large firms it regulates and a PPI fact sheet for the small firms it regulates (including Cathedral). The fact sheet was aimed at smaller firms which arranged PPI policies, with a view to such firms taking urgent action to review their sales practices. It made reference to various key ICOB rules and, with the report, highlighted a number of key areas where the FSA considered that firms were not treating customers fairly.
- 3.6 In early 2006 Cathedral was selected as one of 40 firms to be visited as part of the second phase of the FSA's thematic project into the sale of PPI to establish firms' response to the FSA's November 2005 report. FSA supervisors visited Cathedral in May 2006 as part of the thematic review. They identified a number of concerns relating to Cathedral's sale of PPI, including the apparent lack of formal controls and monitoring of PPI business. Cathedral was subsequently referred to Enforcement.

#### *Compliance Audit Report*

- 3.7 Following the FSA's thematic visit in May 2006 and the issues raised by the FSA supervisors, Cathedral commissioned a compliance audit report from external consultants. A compliance audit took place at the firm in June 2006. Its main objective was to review Cathedral's compliance systems and controls to establish if they were adequate and recommend changes where they were considered deficient.
- 3.8 The audit findings were set out in a report dated July 2006. The report stated there was a lack of documentation and record keeping and a lack of appropriate procedures and controls. The report also noted that Cathedral did not appear to have made sufficient resources available to maintain adequate systems and controls in relation to the size and structure of its business.
- 3.9 Cathedral has subsequently taken steps to implement the changes and improvements recommended in the report.

## **4. RELEVANT STATUTORY AND REGULATORY PROVISIONS**

- 4.1 Section 205 of the Act states:

*“If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, the Authority may publish a statement to that effect.”*

## *FSA Rules and Principles*

- 4.2 The FSA's rule making powers are set out in Chapter I of Part X of the Act (Rules and Guidance). In accordance with the powers and provisions under this part of the Act the FSA has made rules in respect of senior management arrangements, systems and controls, conduct of insurance business and training and competence.
- 4.3 The Principles are a general statement of the fundamental obligations of firms under the regulatory system. They derive their authority from the FSA's rule-making powers as set out in the Act and reflect the FSA's regulatory objectives.
- 4.4 The Rules and Principles relevant to this case are listed in full at appendix 1.

## **5. BREACHES OF THE FSA PRINCIPLES**

### **Principle 3**

- 5.1 Principle 3 (Management and Control) provides that:

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

- 5.2 In considering the standards required under Principle 3, the FSA also has considered the specific requirements of SYSC 2.1.1R, 3.1.1R, 3.2.6R and 3.2.20R, TC 2.3.1R, 2.6.1R, 2.7.5AR and 2.8.1R, and ICOB 4 and 5.

### **Facts and matters relied on**

- 5.3 By reason of the facts and matters detailed in paragraphs 5.4 to 5.17 Cathedral has breached Principle 3 of the FSA's Principles by failing to control and organise its affairs responsibly and effectively.

### *The sale of PPI*

- 5.4 As part of the advised sale process described in paragraph 3.4 above, Cathedral used a series of questions generated by its point of sale insurance software, which the business manager then discussed with the customer, to establish demands and needs. Each question required a "yes" or "no" or "not applicable" answer. A significant failing in the process was the absence of questions to enable the business manager to obtain sufficient information on the customer's personal circumstances prior to making a recommendation.
- 5.5 There was also insufficient process to check an individual's eligibility for any of the four levels of PPI cover available prior to making a recommendation. However, remedial action undertaken by Cathedral indicates that the only ineligible sales that took place were two identified by the FSA and in respect of which the firm has taken action to ensure that the customers did not lose out. These two customers were sold a PPI policy which Cathedral should not have recommended (as in accordance with the usual terms of the policy they would have been ineligible on age grounds), but suffered no detriment since the insurer nevertheless extended cover to them. Cathedral's systems did not identify the fact that these two customers were outside the usual policy age criteria nor was any procedure in place for the firm or these

customers to be advised of the extended terms put in place on these occasions by the insurer. The firm only learned of this failing and the insurer's ad hoc extension of coverage to the above two customers as a result of the FSA's inquiries.

#### *Senior Management Arrangements*

- 5.6 One of Cathedral's four directors held the Apportionment and Oversight control function. Another director was in charge of compliance, a role which included overall responsibility for ensuring compliance with FSA regulations. This director, despite having no experience of the FSA handbook or FSA regulation, undertook no formal training in compliance oversight before or during the relevant period.
- 5.7 Compliance responsibilities at senior management level were not sufficiently clear. In particular, there was uncertainty about which director held responsibility for complaint handling.
- 5.8 Cathedral's failure to establish clear and appropriate apportionment of significant responsibilities among its general managers resulted in inadequate monitoring of the business managers and consumers were placed at increased risk of being sold inappropriate PPI policies.

#### *Record keeping*

- 5.9 There was inconsistent and inadequate record keeping on customer files. Many of the customer files reviewed by the FSA contain no record of the PPI sale and where there is a record of the sale, there is often no indication of the level of cover purchased.
- 5.10 Senior management accordingly had no means of ensuring business managers were conducting compliant PPI sales. Cathedral's inability to establish what information had been provided to the customer or the precise type of cover purchased placed customers at risk in the event of a disputed claim or complaint. There is also no means of verifying what information was given to each customer and in what format.
- 5.11 The firm also held inadequate records of its internal decisions. In addition, there was a lack of fundamental management information, which might otherwise have been used by management to identify potential compliance issues.

#### *Training and Monitoring*

- 5.12 There was no proper system in place for recording or checking the adequacy of the training of either the business managers responsible for the sale of PPI or the general managers responsible for overseeing the business managers.
- 5.13 There was also no differentiation in the training provided to business managers and general managers, despite the fact that the overseeing general managers have different and greater compliance responsibilities. It is essential that training is provided according to individual responsibilities.
- 5.14 Cathedral had no appropriate arrangements in place to ensure that monitoring of the business managers selling PPI occurred on a regular basis. General managers aimed

to monitor one in every ten finance agreements, but paid little or no attention to the compliance of any corresponding PPI sale.

- 5.15 Cathedral was new to regulatory requirements and standards and there was a significant risk that business managers were unlikely to have the necessary knowledge or skills consistently to conduct compliant sales. The absence of an effective monitoring regime and the failure to ensure that the business managers were sufficiently trained at the start of regulation undermined Cathedral's attempts to comply with the FSA's requirements.

#### *Systems and Controls*

- 5.16 Cathedral had no compliance manual or written procedures and relied on the business manager completing the sales process for each sale as prescribed by the firm's point of sale insurance software. In the majority of files reviewed by the FSA, which relate to sales prior to May 2006, there is no evidence that the point of sale software was used by the branch business manager. As a result, Cathedral is unable to evidence the suitability of the advice given and the adequacy of the information provided to the customer at the point of sale in those cases.
- 5.17 Ensuring that there are adequate written procedures is an important part of a firm's risk management systems. Cathedral's failure to keep proper written procedures placed customers at increased risk of suffering detriment from being sold an unsuitable policy, not being provided with important policy information by the business managers or by the firm being unable to investigate a complaint properly.

### **Principle 7**

- 5.18 Principle 7 (Communications with clients) provides that:

*A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.*

- 5.19 In considering the standards required under Principle 7, the FSA also has considered the specific requirements of ICOB 4.2.2R, 4.4.1R and 5.5.14R.

#### **Facts and matters relied on**

- 5.20 By reason of the matters and facts referred to in paragraphs 5.21 to 5.27 Cathedral has contravened Principle 7 of the FSA's Principles by failing to pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

#### *Customer Information – Statement of Price*

- 5.21 Customers did not receive all of the information relating to the cost of the insurance premium prior to the conclusion of a PPI sale. Each business manager had access to the point of sale insurance software to generate a monthly premium statement, including the total amount of the premium for the insurance contract, which was then to be provided to customers as part of their contractual documentation. However, in the majority of sales reviewed the point of sale software was not used and customers did not receive a document which set out the total cost of the insurance policy before the sale

was concluded. It was insufficient for Cathedral to provide the cost of the PPI on a monthly basis only. The total cost of the premium is an important matter for customers to consider before purchasing insurance.

*Customer Information – Initial Disclosure Document*

- 5.22 Cathedral used a laminate to show all customers the initial disclosure information. In some cases it also provided customers with a copy of the initial disclosure document in a durable medium before the conclusion of the PPI contract, but only in those sales where the business manager used the point of sale insurance software.
- 5.23 This was not sufficient. The FSA requires all customers to receive a copy of the initial disclosure document before the conclusion of the PPI sale so that they have a proper record of the extent of the services offered by the provider.

*Customer Information –the Statement of Demands and Needs*

- 5.24 Cathedral failed to provide a number of customers with a statement of demands and needs as required by ICOB rules.
- 5.25 Cathedral also failed to ensure that, where a statement of demands and needs was provided, it was given to the customer before the conclusion of the PPI sale.
- 5.26 The timely provision of a statement of demands and needs in durable medium is important to enable a customer to make an informed decision as to whether the PPI policy is suitable for them.

*Customer Information – Eligibility issues*

- 5.27 Cathedral failed to ensure that customers were only recommended a policy for which they were eligible. As set out at paragraph 5.5 above, a review of a limited sample of customer files by the FSA identified two PPI sales where the customers were recommended and sold policies for which they would have been ineligible in accordance with the usual terms of the policy to claim benefits due to their age. However, Cathedral has confirmed that neither of these two customers suffered any actual detriment since the insurer decided to extend cover to them. No similar age eligibility issues arise in respect of any other customers sold PPI policies.

**6. MITIGATING FACTORS**

- 6.1 In determining the disciplinary measure appropriate to the breaches identified, the FSA acknowledges the mitigating factors detailed below:
  - a. the number of PPI policies sold is low. In the relevant period, comprising approximately 16 months, Cathedral sold 257 PPI policies. This represents an average penetration rate of a PPI policy sold on about 12.5% of its vehicle sales.
  - b. of the four levels of cover offered by the firm, the majority of policies recommended were for one of the two lower levels of cover (i.e. life or life and critical illness), which were at a correspondingly lower premium;



- c. on being made aware of the FSA's concerns Cathedral voluntarily suspended sales of PPI whilst it satisfied itself that future sales would be compliant. The firm retained independent compliance consultants in June 2006 to audit its compliance procedures and implemented improvements promptly;
- d. Cathedral cooperated fully with the FSA and has not been subject to investigation or enforcement action before; and
- e. no complaints have been received in relation to PPI cover.

## **7. DISCIPLINARY MEASURE**

- 7.1 The FSA's policy in deciding whether to take disciplinary action in general is set out in the FSA Handbook at Chapter 11 of the Enforcement Manual (ENF) and in respect of a public censure, the FSA's policy is set out at Chapter 12 of ENF. The FSA has had particular regard to the guidance detailed in ENF at 12.2.2 and the factors listed at ENF 12.3.3, in determining whether to issue a public censure.
- 7.2 The FSA has considered the nature and extent of the breaches of FSA Principles and the mitigating factors detailed above in deciding upon a public censure as the appropriate disciplinary measure in this case.
- 7.3 But for the limited number of PPI policies actually sold, a financial penalty would have been imposed.
- 7.4 In accordance with section 390(3)(a) of the Act, the contents of this Final Notice constitute the terms of the published statement detailing Cathedral's contravention of requirements imposed on it under the Act.
- 7.4 In accordance with section 390(3)(b) of the Act, the contents of this Final Notice constituting the terms of the statement detailing Cathedral's contravention of requirements imposed on it under the Act shall be published on the FSA's Website on the business day after the day on which this Final Notice is transmitted to the firm.

## **8. DECISION MAKERS**

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

## **9. IMPORTANT**

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

### **Publicity**

- 9.2 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.

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

**FSA contacts**

9.4 For more information concerning this matter generally, you should contact Steve Page (direct line: 020 7066 1420) of the Enforcement Division of the FSA.

**William Amos**

**Head of Retail 1**

**Enforcement Division**

## **APPENDIX 1**

Principles referred to in the Notice

### **Principle 3 Management and control**

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

### **Principle 7 Communications with clients**

A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.

Rules referred to in the Notice

### **Senior Management Arrangements, Systems and Controls**

#### **SYSC 2.1.1R Apportionment of Responsibilities**

A firm must take reasonable care to maintain a clear and appropriate apportionment of significant responsibilities among its directors and senior managers in such a way that:

- (1) it is clear who has which of those responsibilities; and
- (2) the business and affairs of the firm can be adequately monitored and controlled by the directors, relevant senior managers and governing body of the firm.

#### **SYSC 3.1.1R Systems and Controls**

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

#### **SYSC 3.2.20R Records**

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

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

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

## **Insurance Conduct of Business**

### **ICOB 4.2.2R Status Disclosure**

- (1) An insurance intermediary must provide the information in ICOB 4.2.8 R to the customer in a durable medium at any time before conclusion of a non-investment insurance contract, unless an exemption in (2) or (3) applies.
- (2) Exemption: oral disclosure. The information in ICOB 4.2.8 R need not be provided in a durable medium before conclusion of the contract but may be provided orally before the conclusion of the contract if:
  - (a) the customer requests this; or
  - (b) the customer requires immediate cover.
- (3) Exemption: telephone sales
- (4) Where (2) or (3) applies, the customer must be provided with the information in ICOB 4.2.8 R in a durable medium immediately after the conclusion of the contract.

### **ICOB 4.4.1R Statement of demands and needs**

- (1) Unless ICOB 4.4.2 R applies, where an insurance intermediary arranges for a customer to enter into a non-investment insurance contract (including at renewal), it must, before the conclusion of that contract, provide the customer with a statement that:
    - (a) sets out the customer's demands and needs;
    - (b) confirms whether or not the insurance intermediary has personally recommended that contract; and
    - (c) where a personal recommendation has been made, explains the reasons for personally recommending that contract.
  - (2) The statement in (1) must reflect the complexity of the contract of insurance proposed.
  - (3) Unless (4) applies, the statement in (1) must be provided in a durable medium.
  - (4) An insurance intermediary may provide the statement in (1) orally if:
    - (a) the customer requests it; or
    - (b) the customer requires immediate cover;
- but in both cases the insurance intermediary must provide the information in (1) immediately after the conclusion of the contract, in a durable medium.

## **ICOB 5.5.14R Statement of price**

A statement of price must include the following information:

- (1) the total amount of the premium for the non-investment insurance contract or, if the premium cannot be indicated, the basis for the calculation of the premium enabling the retail customer to verify it;
- (2) for non-investment insurance contracts of more than one year, details of the period for which the premium is valid, whether it will be reviewed at a certain time or at set periods and, if so, when it will be reviewed;
- (3) fees, administrative charges and taxes payable by the retail customer via the insurance intermediary in addition to the premium. Fees and administrative charges include any interest payable on the premium, including where the premium is paid by way of a credit agreement taken out either for payment of the premium only or for the purpose of purchasing goods or services as well;
- (4) a statement identifying separately the possibility of any taxes not payable via the insurance intermediary;
- (5) where the non-investment insurance contract is purchased in connection with other goods or services:
  - (a) the premium for the non-investment insurance contract, separately from all other prices in relation to the other goods or services, if an additional price is charged; and
  - (b) whether purchase of the non-investment insurance contract is a requirement of purchasing the other goods or services or not; and
- (6) the total price to be paid by the retail customer for the non-investment insurance contract.

## **Training and Competence (TC)**

### **TC 2.3.1R Training**

If a firm's employees engage in or oversee an activity with or for private customers, the firm must:

- (1) at intervals appropriate to the circumstances, determine the training needs of those employees and organise appropriate training to address those needs; and
- (2) ensure that training is timely, planned, appropriately structured and evaluated.

### **TC 2.6.1R Maintaining competence**

A firm must have appropriate arrangements in place to ensure that an employee who has been assessed as competent to engage in or oversee an activity maintains competence.

### **TC2.7.5AR Monitoring employees assessed as competent**

A firm must have arrangements in place to ensure that an employee who is engaging in an activity with or for private customers and who has been assessed as competent is appropriately monitored.

### **TC2.8.1R Record keeping**

(1) A firm must make appropriate records to demonstrate compliance with the rules in this chapter.

(2) The records in (1) must be retained by the firm for at least three years after an employee ceases to engage in or oversee an activity, except for the records of pension transfer specialists, which must be retained indefinitely.