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**FINAL NOTICE**

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To: **Charterhouse Consulting Wealth Management Limited**

Of: **Rood Ashton Hall  
Rood Ashton Park  
Trowbridge  
Wiltshire BA14 6AS**

Date: **11 May 2007**

**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 Charterhouse Consulting Wealth Management Limited ("Charterhouse"/"the firm") a Decision Notice on 27 April 2007 which notified Charterhouse that pursuant to section 206 of the Financial Services and Markets Act 2000 ("the Act"), the FSA had decided to impose a financial penalty of £122,500 on Charterhouse in respect of a contravention of section 20 of the Act and breaches of Principle 3, Principle 6 and Principle 7 of the FSA's Principles for Business ("FSA Principles") that occurred between 1 January 2006 and 31 October 2006 ("the relevant period").
- 1.2. Charterhouse has confirmed that it will not be referring the matter to the Financial Services and Markets Tribunal.
- 1.3. Accordingly, for the reasons listed below, and having agreed with Charterhouse the facts and matters relied upon, the FSA imposes on Charterhouse a financial penalty of

£122,500. Charterhouse has received the maximum discount afforded under the FSA's executive settlement process being a 30% (stage 1) discount, reflecting the fact that Charterhouse agreed to settle at the earliest opportunity. The financial penalty based on the facts and matters described in this Final Notice would otherwise have been £175,000.

## **2. REASONS FOR THE ACTION**

2.1. The FSA decided to impose a financial penalty on Charterhouse in respect of a contravention of section 20 of the Act and breaches of the FSA's Principles, as identified in section 1 above, that occurred during the relevant period. These breaches relate to Charterhouse's failure to establish and maintain effective systems and controls in relation to the conduct of investment business and its failure to ensure that such investment business was conducted in accordance with FSA requirements. These failures are set out in more detail in paragraphs 3.7 to 3.23 below.

2.2. In summary the failings were as follows:

- (1) Charterhouse carried on the regulated activity of Discretionary Portfolio Management without the necessary permission under the Act to perform this regulated activity and thereby contravened a requirement imposed by FSA under the Act in contravention of Section 20 of the Act;
- (2) insufficient personal and financial information about clients was recorded on file and it was not possible without this information to demonstrate that investment advice provided to clients was suitable. Such misconduct arose from the inadequate nature of the firm's fact finding process. As a result the firm failed to take reasonable care to organise and control its affairs responsibly and effectively in breach of Principle 3;
- (3) insufficient consideration was given to a client's risk profile when they were switched between funds, with the consequence that client investments were often switched into funds that had a higher risk profile than the particular client's recorded risk profile. As a result the firm failed to take reasonable steps to ensure that the transaction was appropriate with regard to the client's

attitude to risk and therefore failed to treat its customers fairly in breach of Principle 6; and

- (4) communications with clients did not adequately (i) explain why the relevant transactions were suitable for the clients in question, having regard to their personal and financial circumstances and attitude to risk and/or (ii) contain a summary of the main consequences and possible disadvantages of the recommendation including appropriate explanations of the risks associated with the transaction. As a result, there was a failure to communicate with customers in a way that was clear, fair and not misleading in breach of Principle 7.

2.3. Charterhouse's failings are viewed as being serious because:

- (1) by carrying on a regulated activity without the required permission, Charterhouse has contravened section 20 of the Act and is thereby taken to have contravened a requirement imposed on it by the FSA under the Act.
- (2) the failure to provide adequate suitability letters meant that customers did not receive an adequate explanation as to how the recommended product met their investment objectives and needs and were not provided with an adequate explanation of any risks associated with the recommended product;
- (3) the failure to record sufficient personal and financial information meant that the suitability of investment advice could not be demonstrated and exposed customers to a potential risk of loss; and
- (4) the firm's communications with its clients failed to adequately provide those clients with a sufficient opportunity to consider and provide instructions in relation to the firm's investment decisions.

2.4. The FSA has also taken into account the following steps taken by Charterhouse which have served to mitigate the seriousness of its failings:

- (1) Charterhouse has co-operated with FSA's request to regularise its business activities and ceased to carry on those business activities which fell outside of its permitted activities.
- (2) The firm has also confirmed that, in the future it will take appropriate steps to ensure that it has the required permission before it carries on regulated activities such as discretionary portfolio management.
- (3) The firm has agreed to conduct a Past Business Review ("PBR) in respect of fund switches made during the relevant period. The PBR will be conducted in accordance with a methodology agreed with the FSA with the purpose of reviewing the suitability of clients' investments and taking appropriate remedial action where such investments are deemed not to be suitable for the client.

### **3. FACTS AND MATTERS RELIED UPON**

#### **Background**

- 3.1. Charterhouse is a small multi-tied financial adviser firm that has been authorised by the FSA since 30 May 2002.
- 3.2. Charterhouse currently holds permissions to undertake the following categories of regulated business in relation to designated investment business:
  - (1) advising on designated investment business (except on Pension Transfers and Opt Outs);
  - (2) making arrangements with a view to transactions in designated investment business; and
  - (3) arranging deals in designated investments.

#### **Investment business activity**

- 3.3. Charterhouse provided, what it described as a tailored service, to its clients whereby financial advice was limited to lump sum investments into a recommended bond

product. Where clients were identified as having other needs or requirements they would be referred to a traditional independent financial adviser.

- 3.4. Charterhouse has approximately 160 clients who were contacted on a regular basis by email to advise them that the firm was proposing to switch from one fund to another within the recommended bond product. Charterhouse monitored investment performance of the various funds within the bond on a daily basis to assist in its recommendations as to when to switch their investment.

#### **Enforcement investigation**

- 3.5. The FSA appointed investigators on 22 November 2006.
- 3.6. As part of its investigation Enforcement reviewed:
- (1) a total of 23 client files where funds had been regularly switched;
  - (2) a total of 24 emails issued by Charterhouse during the relevant period notifying clients of the proposed switching of funds; and
  - (3) Charterhouse's procedures for operating its business.

#### **Discretionary Portfolio Management**

- 3.7. Enforcement's investigation has established that Charterhouse recommended the same bond product provided by one particular product provider to all clients, regardless of their circumstances or the level of funds involved. All the clients were initially invested in the same fund within the recommended bond product and then switched en masse on a regular basis. Enforcement's review of the 24 emails identified 15 emails that had been issued to clients where the firm's practice was to send the client an email before 6.30am in the morning proposing the switching of funds within the bond. A response was required from the client only if they did not wish to proceed with the switch of funds, with the deadline for response usually by 8.00am the same morning. The short time period for response meant that clients were not given a reasonable opportunity to consider the proposed switch and respond to the email and switches would take place without further instruction from the client.

- 3.8. Charterhouse has confirmed to the FSA that no negative responses were received from clients who received such emails. Charterhouse has also confirmed in correspondence with the FSA that there was no system to monitor receipt of the emails by clients.
- 3.9. In order to carry on discretionary portfolio management an agreement must be entered into between the client and the firm which specifically authorises the firm to carry out discretionary management. Clients signed a Terms of Business letter when first taking out their investment with Charterhouse. This letter made no mention of authority being given to Charterhouse to exercise discretion in the management of the client's portfolio. Indeed the letter stated that investments will not be kept under review and that any subsequent advice or recommendation would be based on the client's stated investment objectives and acceptable level of risk. These details would then be included in the suitability letter that would be issued to the client to confirm Charterhouse's recommendation. The letter therefore did not inform Charterhouse's clients that their investments would be managed on a discretionary basis and did not provide Charterhouse with the authority to engage in discretionary portfolio management on behalf of its clients. Additionally the clients had not entered into any other form of agreement which would have authorised the carrying out of discretionary portfolio management by the firm.
- 3.10. It is the FSA's view that the switching process adopted by the firm amounted to discretionary portfolio management. Whilst the process described above allowed clients a limited opportunity to object to the proposed switch of funds, and therefore the composition of the portfolio, it did not require Charterhouse to obtain a client's instructions before proceeding with the switching of funds. By proceeding with the switching of funds without clear instructions from their clients Charterhouse was exercising its discretion in relation to the management of the client's investments. The appropriate permission required by the firm to undertake this regulated activity is that of managing investments which the firm has not and does not currently hold.
- 3.11. It is the FSA's view that Charterhouse carried on the regulated activity of Discretionary Portfolio Management without the necessary permission under the Act

to perform this regulated activity and thereby contravened a requirement imposed by FSA under the Act in contravention of Section 20 of the Act.

### **Communication with clients**

- 3.12. All the suitability letters issued to clients that have been reviewed by the Enforcement Team were generic in nature and all failed to adequately explain why the recommended investment bond was considered to be a suitable product for the client having regard to their personal and financial circumstances. The suitability letters reviewed failed to give adequate explanation of the consequences of proceeding with the recommendation and the possible disadvantages, for example, they failed to explain why a lump sum investment had been chosen in preference to alternative forms of investment.
- 3.13. The generic nature of the suitability letters reviewed also meant that there was no adequate explanation as to how the property fund matched a particular client's attitude to risk.
- 3.14. In 16 of the 23 client files reviewed, there was a mismatch between the client's objectives and/or the term of the investment as recorded on the fact find and the details set out in the suitability letter.
- 3.15. The 24 emails issued to clients that were reviewed by FSA contained insufficient information for a client to make an informed decision regarding the proposed switch. For example, the emails generally failed to adequately set out the risks associated with the proposed switch of funds. In this respect only a limited number contained any form of risk warning, whilst some emails contained no risk warnings at all. The email should have explained the risk profile of the funds that it was proposed the client was to be switched into and provided an explanation as to how this matched with the client's own risk profile.
- 3.16. It is the FSA's view that the suitability letters and emails issued to clients did not adequately (i) explain why the relevant transactions were suitable for the client in question, having regard to their personal and financial circumstances and attitude to risk and/or (ii) contain a summary of the main consequences and possible disadvantages of the recommendation including appropriate explanations of the risks associated with the

transaction. As a result, there was a failure to communicate with customers in a way that was clear, fair and not misleading in breach of Principle 7.

### **Know Your Customer ("KYC")**

- 3.17. Charterhouse used a tailored fact find that had been specifically designed for the service it provided to its clients. The level and nature of the KYC information collected was inadequate in that it did not contain sufficient information with regard to outstanding debts, such information being limited to mortgage related information. The assessment of income and expenditure was also poor with few or no details collected regarding the client's outgoings and no proper evaluation of the income available for investment purposes. These failings were a consequence of the inadequate nature of the fact find which meant that such details were not requested from the clients.
- 3.18. Of the 23 client files reviewed, in 3 cases, there was conflicting information recorded with regard to the client's attitude to risk ("ATR"). In the first case, the ATR was recorded as B3 (balanced and medium risk) but it was also recorded that the client would accept "minimal" capital volatility. Whilst the ATR B3 is consistent with the medium risk associated with the property fund into which they invested, an acceptance of only minimal capital volatility is not consistent with the property fund.
- 3.19. In the second case, it was recorded on the fact find that the client was "Cautious" but also as having a B3 ATR (balanced and medium risk). Similarly in the third case, the client's "Low to Medium" risk profile conflicts with the B3 (balanced and medium) ATR also recorded on the fact find.
- 3.20. It is the FSA's view that insufficient personal and financial information about clients was recorded on file and it was not possible without this information to demonstrate that investment advice provided to clients was suitable. Such misconduct arose from the inadequate nature of the firm's fact finding process. As a result Charterhouse failed to take reasonable care to organise and control its affairs responsibly and effectively in breach of Principle 3.

### **Suitable recommendations**



- 3.21. Although in all but 3 of the cases reviewed the initial property fund recommended matched the client's ATR, there was no evidence to show that the firm had considered whether the subsequent fund switches, which were effected in bulk between the Property, UK and Japanese Equity funds, the latter fund being designated medium to high Risk continued to match the client's ATR.
- 3.22. During the relevant period, Charterhouse switched clients with a recorded medium and balanced risk profile into the Japanese Equity fund. As a consequence, clients' funds were often invested into a fund which had a higher risk profile than that which the client had indicated would be acceptable for the investment of their funds.
- 3.23. It is the FSA's view that insufficient consideration was given to a client's risk profile when they were switched between funds, with the consequence that client investments were often switched into funds that had a higher risk profile than the particular client's recorded risk profile. As a result the firm failed to take reasonable steps to ensure that the transaction was appropriate with regard to the client's attitude to risk and therefore failed to treat its customers fairly in breach of Principle 6.

#### **4. RELEVANT STATUTORY PROVISIONS**

- 4.1. Section 206 of the Act provides:

*"If the Authority considers that an unauthorised person has contravened a requirement imposed on him by or under this Act, it may impose on him a financial penalty, in respect of the contravention, of such an amount as it considers appropriate".*

- 4.2. Section 20 of the Act states:

*"(1) If an authorised person carries on a regulated activity in the United Kingdom, or purports to do so, otherwise than in accordance with permission –*

- (a) given to him by the Authority under Part IV, or*
- (b) resulting from any other provision of this Act,*

*he is to be taken to have contravened a requirement imposed on him by the Authority under this Act".*

### **Principles for Business**

- 4.3. Under the FSA's rule making powers, the FSA has published in the FSA Handbook the "Principles for Business" which apply either in whole, or in part, to all authorised persons.
- 4.4. These Principles are a general statement of the fundamental obligations of firms under the regulatory system.
- 4.5. Breaching a Principle makes a firm liable to disciplinary sanctions.
- 4.6. The Principles, which are relevant to this matter, are as set out below.

## **5. RELEVANT REGULATORY REQUIREMENTS**

### **Principles for Business**

- 5.1. Principle 3 provides that:

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

- 5.2. Principle 6 provides that:

*A firm must pay due regard to the interest of its customers and treat them fairly.*

- 5.3. Principle 7 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.*

## **6. ANALYSIS OF THE SANCTION**

- 6.1. The FSA's policy on the imposition of financial penalties is set out in Chapter 13 of the Enforcement Manual which is part of the FSA's rules and guidance. The principal purpose of financial penalties is to promote high standards of regulatory conduct by

detering firms and approved persons who have breached regulatory requirements from committing contraventions, and demonstrating generally to firms and approved persons the benefits of compliant behaviour (ENF 13.1.2G).

- 6.2. In determining whether a financial penalty is proportionate the FSA will take into account all the relevant circumstances of a case. ENF 13.3.3 sets out a non-exhaustive list of factors that may be of relevance in determining the amount of a financial penalty, which include the following:

**ENF 13.3.3(1): The seriousness of the misconduct or contravention**

- 6.3. 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 and the number of customers affected and/or placed at risk. For the reasons set out at paragraph 2.3 above, the FSA considers that the breaches in this case are of a serious nature.

**ENF 13.3.3(2): the extent to which the misconduct was deliberate or reckless**

- 6.4. The FSA has found no evidence that Charterhouse acted in a deliberate or reckless manner. Charterhouse was however responsible for ensuring that its business was organised and controlled in a manner that complied with FSA's requirements.

**ENF 13.3.3(3): Size, financial resources and other circumstances of the firm**

- 6.5. The FSA is satisfied that Charterhouse has the means to pay the level of financial penalty imposed on it.

**ENF 13.3.3(4): The amount of profits accrued or loss avoided**

- 6.6. The activity identified as Discretionary Portfolio Management made up almost the entirety of Charterhouse's business during the relevant period and therefore made a significant contribution to the firm's profits.

**ENF 13.3.3(5): Conduct following the contravention**

- 6.7. The FSA has taken into account Charterhouse's co-operation with the FSA's investigation. Charterhouse has co-operated with FSA's request to regularise its business activities and ceased to carry on those business activities which fell outside of its permitted activities. The firm has also confirmed that, in the future it will take appropriate steps to ensure that it has the required permission before it carries on regulated activities such as discretionary portfolio management.

**ENF 13.3.3(6): Disciplinary record and compliance history**

- 6.8. Charterhouse has not been the subject of previous disciplinary action.

**ENF 13.3.3(7): Previous action taken by the FSA**

- 6.9. The FSA has taken into account penalties imposed by the FSA on other authorised persons for similar misconduct.

**7. DECISION MAKERS**

- 7.1. 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.

**8. IMPORTANT**

- 8.1. This Final Notice is given to you in accordance with sections 390 of the Act. The following statutory rights are important.

**Manner of and time for Payment**

- 8.2. The financial penalty must be paid in full by Charterhouse to the FSA by no later than 25 May 2007, 14 days from the date of the Final Notice.

**If the financial penalty is not paid**

- 8.3. If all or any of the financial penalty is outstanding on 26 May 2007, the FSA may recover the outstanding amount as debt owed by Charterhouse and due to the FSA.

**Publicity**

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

**FSA contacts**

- 8.6. For more information concerning this matter generally, you should contact Boura Tomlinson at the FSA (direct line: 020 7066 5528/fax: 020 7066 5529).

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Jonathan Phelan

**Head of Department**  
**FSA Enforcement Division**