Financial Services Authority

FINAL NOTICE

To: **Christchurch Investment Management Limited**

FSA Reference Number: **153730**

Address: 4th Floor
42 Moorgate
London
EC2R 6EL

Date: 29 March 2012

ACTION

1. For the reasons given in this notice, the FSA hereby imposes on Christchurch Investment Management Limited ("Christchurch" or "the Firm") a financial penalty of £26,600.

2. Christchurch agreed to settle at an early stage of the FSA's investigation and qualified for a 30% (stage 1) discount under the FSA's executive settlement procedures. Were it not for this discount, the FSA would have imposed a financial penalty of £38,000.

SUMMARY OF REASONS

3. On the basis of facts and matters described below, the FSA has concluded that Christchurch breached Principles 3 (management and control) and 10 (clients' assets) and associated FSA Rules set out in the Client Assets sourcebook (the "CASS

Rules") between 1 November 2007 until 2 March 2011 (the "Relevant Period") by failing to ensure adequate protection of the Firm's client money during this period.

4. Specifically, Christchurch had insufficient knowledge and oversight of its compliance with the CASS Rules; and, as a consequence Christchurch:

    a) Failed to arrange adequate protection for client money and assets for which it was responsible in that Christchurch:

        i. applied the wrong standard of daily reconciliations of client money;

        ii. carried out inadequate reconciliations of client money with external records; and

        iii. did not have adequate trust status letters in place for each of its each client bank accounts.

    b) Failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems, in that Christchurch:

        i. handled client money without adequate division of duties between staff to prevent the risk of fraud; and

        ii. handled client money without adequate internal checks and balances.

5. The FSA views the Firm's failings as serious because:

    a) the Firm did not take reasonable steps to familiarise itself with the CASS Rules;

    b) the FSA places great importance on the responsibilities of firms to ensure they have adequate compliance oversight, in particular, the CASS Rules are there to ensure firms handle client money in a safe manner and have appropriate controls to mitigate the risk of loss;

    c) the failings placed its client money at risk;

    d) it did not identify its own deficiencies in handling client money, but this was identified by the FSA;

    e) the conduct of its compliance officer, Mr Thornberry, fell far below the standard which would be reasonable in the circumstances; and

    f) the requirements of CASS have been the subject of various publications from the FSA setting out the practical measures a firm should take to safeguard client assets.

6. The FSA has taken into account that whilst client money was at risk there was no actual loss of client money. The FSA has also taken into account the following factors which have served to mitigate the seriousness of the Firm's failings, namely that the Firm:

a) accepted at an early stage that it had not discharged its responsibilities for client money to an appropriate standard;

b) has co-operated fully with the FSA's investigation; and

c) has implemented changes to its handling of client money procedures.

DEFINITIONS

7. The definitions below are used in this Final Notice:

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

"CASS Rules" means Client Assets Sourcebook;

"Christchurch" or "the Firm" means Christchurch Investment Management Limited;

"Dear CEO letter" means a letter issued by the FSA to the Chief Executive Officers of authorised firms holding client money in January 2010;

"Dear CO letter" means a letter issued by the FSA to the Compliance Officers of authorised firms holding client money in March 2009;

"DEPP" means the Decision Procedures and Penalties Manual;

"the FSA" means the Financial Services Authority;

the "Principles" means the FSA's Principles for Businesses;

the "Relevant Period" means the period between 1 November 2007 until 2 March 2011;

"SYSC" means Senior Management Arrangements, Systems and Controls; and

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

FACTS AND MATTERS

8. Christchurch is an investment management business, based in London, specialising in financial planning and portfolio management. Christchurch has been authorised and regulated by the FSA since 1 December 2001 and is permitted to hold client money.

9. In the course of its business, Christchurch receives money on behalf of clients for investment in ISAs and SIPPs and as part of its portfolio management. The money Christchurch receives on behalf of its clients is client money and is subject to the relevant requirements and standards set out in the CASS Rules.

10. Christchurch has around 2,500 clients, of which it handled client money and assets for 227, and calculated that from 30 November 2007 until 28 February 2011 it held an average of £1,242,466 of client money.

11. During the Relevant Period Christchurch had 8 investment advisors (CF30), three of whom were its directors (CF1). Christchurch allocated its Compliance Oversight function (CF10) to Mr Thornberry, one of its directors; consequently from 17 September 2007 Mr Thornberry was responsible for the oversight of the Firm's handling of client money.

Client money thematic project

12. In March 2009, the FSA issued a Dear CO letter to all large firms and posted a copy for all firms on its website. The Dear CO letter reminded firms that they should make adequate arrangements to protect client money. The letter highlighted issues for firms to consider and warned firms that visits focusing on client money controls would follow during 2009.

13. In January 2010, the FSA issued a Dear CEO letter and published a Client Money and Asset Report notifying firms of failings indentified during work conducted by the FSA in 2009. The letter warned firms that client money visits would continue through 2010. Small firms, including Christchurch, were notified of the Dear CEO letter and the report through the monthly emailed Regulation round-up in February 2010.

14. As part of enhanced supervision of client assets, the FSA has conducted a thematic project into the management of client money held by small firms. The aim of the project was to:

    a) assess whether client money held by firms was safe and would be returned within a reasonable time in the event that a firm became insolvent; and

    b) ensure firms were taking their responsibilities seriously with regard to client money and had appropriate controls in place to mitigate any risks.

15. On 25 and 26 May 2010, the FSA visited Christchurch to review its client money arrangements. During the visit the FSA identified a number of issues, including:

    a) an inappropriate division of duties for client money processes at Christchurch, with a high concentration of risk given the range and responsibilities of one individual, the compliance manager;

    b) inappropriate systems and controls to oversee the handling of client money;

    c) not performing internal reconciliation of client money in line with the standard method of internal client money reconciliation;

    d) ensuring sufficiently frequent client money reconciliations with external records; and

e) inadequate client trust status letters for each of the 227 client bank accounts opened.

16. As a result the FSA required Christchurch to provide a skilled person's report in respect of the CASS Rules. On 27 November 2010 the skilled person issued a report that focussed on the FSA's concerns from the visit about Christchurch's ability to comply with the CASS Rules as at October 2010, in particular, the requirements relating to client money internal reconciliation (calculations), reconciliations with external records, trust status letters, compliance oversight/segregation of duties/conflicts of interest and client assets. Its purpose was to provide assurance that the firm was conducting its business in compliance with Principle 10 and provide the FSA with assurance that the Firm has taken the necessary steps to remedy the concerns and mitigate the risks identified as a result of the May 2010 visit. Since the FSA visit, the skilled person noted that Christchurch has made "significant progress in improving its controls around client money and assets".

Compliance oversight

17. There was an external and internal component to compliance oversight at Christchurch. The role of the external compliance consultants was significantly reduced in 2008 and during the Relevant Period they did not provide any oversight of the Firm's compliance with the CASS Rules. The internal compliance function was divided between two people: Mr Thornberry and the compliance manager. Christchurch appointed Mr Thornberry to carry out the controlled function of compliance oversight (CF10) and gave him responsibility for oversight of its controls for its handling of client money. Mr Thornberry had no prior experience as a compliance oversight officer.

18. The FSA considers, and Mr Thornberry accepted in interview, that during the Relevant Period, Christchurch failed to ensure that Mr Thornberry:

    a) had formal training for his CF10 role;

    b) was aware of the CASS Rules on trust status letters before the FSA visit; and

    c) reviewed and tested the adequacy of the existing system and controls relating to CASS.

19. The Firm relied on Mr Thornberry, even though he was newly appointed in September 2007 and it did not provide any compliance training to him. The Firm also relied on the compliance manager to raise any discrepancies or deficiencies in client money calculations with Mr Thornberry. The Firm failed to review the division of duties between Mr Thornberry and those carried out by the compliance manager and failed to question the lack of information provided on compliance with the CASS Rules. The Firm relied on the existing systems that it had inherited, without asking critical questions of its compliance function.

20. During the Relevant Period the Board did not ensure it had sufficient information to monitor and assess the adequacy of its client money systems and controls. Any issues with the CASS Rules were raised with the Board in an ad hoc manner. Mr

Thornberry admitted that the Firm did not fulfil its obligations under the CASS Rules before the FSA visit.

Separation of duties

21. During the period from 1 November 2007 to 27 November 2010, Christchurch failed to ensure that the responsibility for client money was adequately divided between staff. The FSA considers there was a concentration of risk without adequate oversight from its directors. Prior to the FSA's visit, the extent of the compliance manager's role led to an increased concentration of risk, without adequate checks on the compliance manager's actions. The compliance manager:

    a) provided compliance support to Mr Thornberry and staff;

    b) maintained the internal compliance records and registers;

    c) monitored activities of the staff to ensure company procedures were complied with and staff training was up to date;

    d) conducted a daily review of the clients' balances on the Firm's operating systems and the six- monthly custody reconciliations;

    e) was responsible for the day to day management of accounts;

    f) was responsible for conducting the client money internal reconciliation;

    g) was a signatory for client accounts, which needed two signatories;

    h) as a joint signatory could open client accounts;

    i) received investment cheques;

    j) had verification and update access on the Firm's system and verification authorisation for its Bank's payment system;

    k) was also able to authorise online payments;

    l) held the key to the safe which held the Firm's chequebooks, share certificates and register of holdings;

    m) received advanced notification of any BACS receipts and payments; and

    n) covered for the administration manager and paraplanners in their absence.

22. Whilst it is not possible in a small firm to always achieve a full division of duties, in this case there was a concentration of duties because of the range of responsibilities of the compliance manager. The directors failed to identify the potential risks posed by the concentration of duties.

23. Where one individual has such an extensive range of responsibilities in relation to client money, the FSA considers that there is an increased concentration of risk of:

a) fraud;

b) mistake; and consequently

c) client loss.

Internal reconciliations and calculations

24. During the period from 1 November 2007 to the FSA visit in May 2010 the Firm did not conduct a daily internal reconciliation as required by the CASS Rules. The skilled person's report found that from the date of the visit until 15 November 2010 the Firm did not apply the standard method of internal client money reconciliation as required by the CASS Rules. The Firm appeared to be using a hybrid of the separate client balance and client bank account methods described in CASS 7 Annex 1.

Reconciliations with external records

25. During the period from 1 November 2007 until 24 October 2010, the Firm failed to conduct daily external client money reconciliations, and instead conducted them on a quarterly basis. From 24 October 2010 the Firm started to perform daily external reconciliations.

26. The Firm failed to ensure that its books and records were up-to-date and accurate as the Firm did not record transactional flows on trade dates or recognise dividend receipts until the Firm received a tax voucher. The Firm failed to ensure a sufficiently accurate forward position on client money.

27. The Firm did not have records of client money that it expected to receive on a future date which would have provided the Firm and its clients with an accurate reflection of its clients' forward position. The Firm needed to do so to ensure any client money that arrives can be immediately and properly identified as client money. During the period from 1 November 2007 until 25 May 2010 the Firm failed to post transactions on the day that the transaction occurred and instead delayed in posting transactions until after receipt of contract notes or tax vouchers. The Firm is required to maintain its records and accounts in a way that ensures their accuracy, and in particular to ensure they correspond to the client money held for clients, as is required by CASS 7.6.2. Had the Firm become insolvent it would have been unable to distinguish the client money held for one client from the client money held for another.

Trust Status Letters

28. During the Relevant Period the Firm operated a number of client money bank accounts. For most of the Relevant Period the Firm failed to have any client trust status letters. It is important that firms put adequate trust acknowledgement documentation in place for their client money bank accounts to ensure that client money within the accounts is properly protected in the event of the firm's insolvency. The FSA views the lack of adequate trust status letters as serious because they create a risk that, in the event of insolvency the client would face difficulties and delay in recovering their money and would be exposed to the risk of diminution or loss.

29. Following the issue of a Dear CEO letter by the FSA in January 2010, on 18 March 2010 the Firm contacted its bank to request proper trust status letters as required by CASS 7.8.1(1) R. Before this date the Firm had not notified the Bank or received acknowledgement of trust status for the client bank accounts. The Firm did not have an acknowledgement from the Bank that it had no right of counterclaim or offset against these accounts and that they were sufficiently distinguished from any Firm bank accounts. The bank sent trust status acknowledgement letters to the Firm on 30 March 2010, but these were not sufficient to satisfy the FSA's requirements. The Firm failed to ensure that the word "designated" appeared in the title of the account and the account names and numbers were not included in the trust status letters but were set out separately in an undated list.

30. On 7 and 13 April 2010 the Firm opened two new client bank accounts. Again the Firm did not obtain a trust letter or withdraw all money standing to the credit of the accounts within 20 business days (as required by CASS 7.8.1(2)). The client money held in these accounts was consequently at risk until the Firm received adequate letters from the Bank on 17 August 2010 in respect of the client accounts; and on 13 October 2010 in respect of the settlement account (which was used as a client bank account).

31. Under the CASS Rules, the Firm needed to withdraw any client money from the account if an acknowledgement of trust had not been received within 20 business days of being notified by the Firm. The Firm did not withdraw the money from the Bank.

Remedial steps

32. Following the FSA communications, FSA visit and the skilled persons' report, the Firm undertook the following remedial steps:

    a) in March 2010 contacted the Bank to request proper trust status letters in response to the Dear CEO letter sent by email in February 2010;

    b) since July 2010 it has altered the Board's focus on the CASS Rules and the CASS Rules has featured as an individual agenda item at monthly Board meetings;

    c) since 17 August 2010 and 13 October 2010 respectively, it has ensured that there are appropriate trust status letters in place for each client account and for each settlement account;

    d) since 24 October 2010, it has increased external reconciliations with individual bank accounts to a daily basis;

    e) since 15 November 2010, it has altered the method of daily reconciliation in line with the standard approach outlined in the CASS Rules;

    f) it made changes so that the skilled person concluded on 27 November 2010 they had seen "sufficient controls in place to prevent any one individual completing the whole process" and that Christchurch had "made significant progress in improving its controls around client assets and money";

g) since the May 2010 FSA visit and since the skilled persons report in November 2010, changed the role of the compliance manager so that the compliance manager no longer provides cover for authorisation of payments and cannot release payments on the online system; and

h) since the May 2010 FSA visit, changed the role of the compliance manager so that there is greater division of duties, sufficient for the skilled person to conclude that in October 2010 there is "adequate segregation of duties".

FAILINGS

33. The statutory and regulatory provisions and policy relevant to this Final Notice are referred to in Annex A.

34. The FSA's regulatory objective to maintain confidence in the financial system and the protection of consumers, together with the facts and matters described above, lead the FSA to conclude that the Firm has failed to satisfy Principles 3 and 10.

35. Specifically, in its client money arrangements the Firm breached:

a) Principle 3: by failing to take reasonable care to organise and control its affairs responsibly and effectively with adequate risk management systems to ensure:

i. management oversight was maintained appropriately for client money arrangements; and

ii. division of duties for the handling of client money.

Consequently, the Board was not in a position to monitor and assess the adequacy of its client money arrangements or to identify its own shortcomings.

b) Principle 10: by failing to arrange adequate protection for client assets when it is responsible for them, in particular, the Firm had inadequate:

i. internal reconciliation and calculations of client money;

ii. reconciling between its own internal accounts and those of third parties, by whom client money is held, on a regular basis; and

iii. trust status letters.

The actual impact of Christchurch's failure to arrange adequate protection for client money exposed clients to the risk of financial loss in the event of fraud or insolvency.

36. Having regard to the facts and matters, the FSA has concluded that Christchurch has breached the CASS Rules and Principles 3 and 10. Consequently, it is appropriate

and proportionate in all the circumstances to take disciplinary action against the Firm.

SANCTION

37. The FSA's policy on the imposition of financial penalties is set out in Chapter 6 of DEPP, which forms part of the FSA Handbook. The relevant sections of DEPP are set out in more detail in Annex A.

38. The majority of the Firm's failings occurred before the change in regulatory provisions governing the determination on financial penalties on 6 March 2010. Therefore the FSA has applied the penalty regime that was in force before 6 March 2010. All references to DEPP are to the version that was in force up to 5 March 2010.

39. The principal purpose of a financial penalty is to promote high standards of regulatory conduct by deterring firms which have committed breaches from further breaches, and helping to deter other firms from committing similar breaches, as well as demonstrating generally the benefits of compliant behaviour.

40. In determining whether a financial penalty is appropriate, and if so its level, the FSA must consider all the relevant circumstances of the case. DEPP 6.5.2G sets out a non-exhaustive list of factors that may be of relevance in determining the level of a financial penalty. The FSA considers the following factors to be particularly relevant in this case.

Deterrence (DEPP 6.5.2G(1))

41. Penalties act as a deterrent, and the FSA must ensure that those who are authorised persons have an appropriate level of competence and capability and act in accordance with regulatory requirements and standards. The FSA considers that a financial penalty is an appropriate sanction in this case to demonstrate the seriousness with which the FSA regards the Firm's behaviour.

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

42. The FSA has considered the seriousness of the breach including the nature of the requirements breached and the impact. The FSA considers the following factors to be both serious and aggravating and which impact on the appropriate level of financial penalty:

    i. Christchurch exposed its clients to a serious risk of fraud because of the segregation of duties and heavy reliance on its compliance manager;

    ii. Christchurch failed to take reasonable steps to familiarise itself with the CASS Rules and as a consequence had insufficient knowledge of the CASS Rules;

iii. Christchurch failed to have adequate oversight of its compliance with the CASS Rules which resulted in the Firm failing to comply with the CASS Rules during the Relevant Period of three years;

iv. Christchurch's breaches were not identified through its own compliance monitoring, but by the FSA's visit; and

v. the breaches exposed clients to the potential risk of financial loss in the event of insolvency or fraud.

43. The FSA has taken into account the following factors which have served to mitigate the seriousness of Christchurch's failings:

i. the number of clients affected by the trust status letters was small;

ii. no client money was lost as a consequence of Christchurch's breach; and

iii. Christchurch undertook remedial action and rectified its failing upon identification of the breach.

44. The FSA has considered the above factors, together with the amount of client money held, in assessing the seriousness of the misconduct. The quantum of the financial penalty must amount to a clear and credible deterrent.

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

45. In the FSA's view the Firm's breaches were neither deliberate nor reckless.

The size, financial resources and other circumstances of the Firm (DEPP 6.5.2G(5))

46. The FSA considers the level of financial penalty proposed is appropriate, having considered all relevant factors, including the size and financial resources of the Firm.

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

47. The Firm did not benefit from its breach.

Conduct following the breach (DEPP 6.5.2G(8))

48. The Firm co-operated fully with the FSA's investigation. From the outset it has acknowledged its failure to ensure compliance with the CASS Rules. As set out above, the Firm has taken steps to improve its internal processes and monitoring.

Other action by the FSA (DEPP 6.5.2G(10))

49. In determining the level of the penalty, the FSA has had regard to penalties imposed by the FSA on other authorised persons with similar behaviour. This is considered alongside the deterrent purpose of imposing sanctions.

Conclusion

50. In light of the matters above, the FSA imposes a financial penalty of £26,600 on Christchurch for breaching Principles 3 and 10 and the CASS Rules. Were it not for the early stage at which Christchurch have settled, the penalty would have been £38,000.

PROCEDURAL MATTERS

Decision maker

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

52. This Final Notice is given under, and in accordance with, section 390 of the Act. The following statutory rights are important.

Manner of and time for payment

53. The financial penalty is to be paid in 10 monthly instalments. The first instalment of £2,660 must be paid by Christchurch to the FSA within 14 days of the date of the Final Notice. The following 9 equal instalments of £2,660 each must then be paid on the 1st day of the month following the previous instalment (the "Due Date"). If the Due Date for any given payment falls on a public holiday (including Saturdays and Sundays) in any given month then the Due Date is deemed to be the first business day immediately following the public holiday concerned.

54. If Christchurch realises any assets which enable it to pay the outstanding amount of the financial penalty in full, it will do so within 14 days of those assets being realised.

If the financial penalty is not paid

55. If any instalment is not paid by the Due Date for that instalment then the financial penalty becomes payable immediately and in full. The FSA may recover the outstanding amount as a debt owed by Christchurch and due to the FSA.

Publicity

56. 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.

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

FSA contacts

62. For more information concerning this matter generally, contact Kate Tuckley of the Enforcement and Financial Crime Division at the FSA (direct line: 020 7066 7086 /fax: 020 7066 7087).

……

Tom Spender
Head of Department
FSA Enforcement and Financial Crime Division

ANNEX A

STATUTORY PROVISIONS, REGULATORY GUIDANCE AND POLICY

STATUTORY PROVISIONS

1. The FSA's statutory objectives are set out in section 2(2) of the Act and include the protection of consumers.

2. The FSA has the power under s205 of the Act to publish a statement and under section 206 of the Act to impose a financial penalty against a firm.

REGULATORY PROVISIONS

3. In exercising its power to impose a financial penalty, the FSA has had regard to the relevant regulatory provisions and policy published in the FSA Handbook. The main provisions that the FSA considers relevant to this case are set out below.

Principles for Businesses ("Principles")

4. Under the FSA's rule-making powers, the FSA has published in the FSA Handbook the Principles which apply either in whole, or in part, to all authorised persons. The Principles are a general statement of the fundamental obligations of firms under the regulatory system and reflect the FSA's regulatory objectives. A firm may be liable to disciplinary sanction where it is in breach of the Principles.

5. The Principles relevant to this case are:

    1) Principle 3 **management and control** which states that "A firm must take reasonable care to organise and control its affairs responsibly ad effectively, with adequate risk management systems."

    2) Principle10 **clients' assets** which states that "A firm must arrange adequate protection for clients' assets when it is responsible for them."

Client Assets sourcebook ("CASS")

Segregation of duties and controls

6. CASS 6.5.9G states whenever possible, a firm should ensure that reconciliations are carried out by a person (for example an employee of the firm) who is independent of the production or maintenance of the records to be reconciled.

7. CASS 7.3.2R states that a firm must introduce adequate organisational arrangements to minimise the risk of the loss or diminution of client money, or of rights in connection with client money, as a result of misuse of client money, fraud, poor administration, inadequate record keeping or negligence.

8. CASS 7.4.11R states that a firm must take the necessary steps to ensure that client money deposited in a central bank, a credit institution, a bank authorised in a third

country or a qualifying money market fund is held in an account or accounts identified separately from any accounts used to hold money belonging to the firm.

9. CASS 7.6.1R states that a firm must keep such records and accounts as are necessary to enable it, at any time and without delay, to distinguish client money held for one client from client money held for any other client, and from its own money.

10. CASS 7.6.2R states that a firm must maintain its records and accounts in a way that ensures their accuracy, and in particular their correspondence to the client money held for clients.

Reconciliation of client money

11. In relation to CASS 7.6.2R, CASS 7.6.6G provides that:

    1) Carrying out internal reconciliations of records and accounts of the entitlement of each client for whom the firm holds client money with the records and accounts of the client money the firm holds in client bank accounts and client transaction accounts should be one of the steps a firm takes to satisfy its obligations under CASS 7.6.2R, and where relevant SYSC 4.1.1R and SYSC 6.1.1R.

    2) A firm should perform such internal reconciliations:

        (a) as often as is necessary;

        (b) as soon as reasonably practicable after the date to which the reconciliation relates; and

        to ensure the accuracy of the firm's records and accounts.

    3) The standard method of internal client money reconciliation sets out a method of reconciliation of client money balances that the FSA believes should be one of the steps that a firm takes when carrying out internal reconciliations of client money.

12. The defined term "standard method of internal client money reconciliation" refers to CASS 7 Annex 1, which sets out a method that the FSA believes is appropriate in this case and the fact that the reconciliation should be performed for each business day.

13. CASS 7.6.7R states that a firm must make records, sufficient to show and explain the method of internal reconciliation of client money balances under CASS 7.6.2R used, and if different from the standard method of internal client money reconciliation, to show and explain that the method of internal reconciliation of client money used affords an equivalent degree of protection to the firm's clients to that afforded by the standard method of internal client money reconciliation.

14. CASS 7.6.8R states that a firm that does not use the standard method of internal client money reconciliation must first send a written confirmation to the FSA from the firm's auditor that the firm has in place systems and controls which are adequate to enable it to use another method effectively.

15. CASS 7.6.9R states that a firm must conduct, on a regular basis, reconciliations

between its internal accounts and records and those of any third parties by whom client money is held.

16. CASS 7.6.13R states that when any discrepancy arises as a result of a firm's internal reconciliations, the firm must identify the reason for the discrepancy and ensure that any shortfall is paid into a client bank account by the close of business on the day that the reconciliation is performed.

17. CASS 7.6.14R states when any discrepancy arises as a result of the reconciliation between a firm's internal records and those of third parties that hold client money, the firm must identify the reason for the discrepancy and correct it as soon as possible.

Trust Status letters

18. CASS 7.8.1R states that when a firm opens a client bank account, the firm must give written notice to the bank requesting the bank to acknowledge to it in writing that (a) all money standing to the credit of the account is held by the firm as trustee and that the bank is not entitled to combine the account with any other account or to exercise any right of set-off or counterclaim against money in that account in respect of any sum owed to it on any other account of the firm; and (b) the title of the account must sufficiently distinguish that account from any account containing money that belongs to the firm, and is in the form requested by the firm. In the case of a client bank account in the United Kingdom, if the bank does not provide the required acknowledgement within 20 business days after the firm despatched the notice, the firm must withdraw all money in the account and deposit it with another bank as soon as possible.

Decision Procedure and Penalties Manual ("DEPP")

19. The FSA's policy on the imposition and amount of penalties that applied up to 5 March 2010 was set out in Chapter 6 of DEPP.

20. DEPP 6.1.2G provides that the principal purpose of imposing a financial penalty is to promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches, helping to deter other persons from committing similar breaches, and demonstrating generally the benefits of compliant behaviour. Financial penalties are therefore tools that the FSA may employ to help it to achieve its regulatory objectives.

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

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

Deterrence: DEPP 6.5.2G(1)

23. When determining the appropriate level of financial penalty, the FSA will have regard to the principal purpose for which it imposes sanctions, namely to promote high

standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches and helping to deter other persons from committing similar breaches, as well as demonstrating generally the benefits of compliant business.

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

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

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

25. The FSA will regard as more serious a breach which is deliberately or recklessly committed, giving consideration to factors such as whether the person has given no apparent consideration to the consequences of the behaviour that constitutes the breach. If the FSA decides that the breach was deliberate or reckless, it is more likely to impose a higher penalty on a person than would otherwise be the case.

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

26. The degree of seriousness of a breach may be linked to the size of the firm. For example, a systemic failure in a large firm could damage or threaten to damage a much larger number of consumers or investors than would be the case with a small firm: breaches in firms with a high volume of business over a protracted period may be more serious than breaches over similar periods in firms with a small volume of business.

27. In addition, the size and resources of a person may also be relevant in relation to mitigation, in particular what steps the person took after the breach had been identified; the FSA will take into account what is reasonable to expect from a person in relation to its size and resources, and factors such as what proportion of a person's resources were used to resolve a problem.

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

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

Conduct following the breach: DEPP 6.5.2G(8)

29. The FSA may take into account the degree of co-operation the person showed during the investigation of the breach by the FSA and any remedial steps taken since the breach was identified, including whether these were taken on the person's own initiative or that of the FSA.

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

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

Enforcement Guide ("EG")

31. The FSA's approach to exercising its power in issuing a financial penalty is set out in Chapter 7 of EG. Imposing financial penalties show that the FSA is upholding regulatory standards. An increased public awareness of regulatory standards also contributes to the protection of consumers.

32. EG 7.2 provides that the FSA's power to publish a statement against a firm under section 205 of the Act. It has power to impose a financial penalty against a firm under section 206 of the Act.

Senior Management Arrangements, Systems and Controls ("SYSC")

33. SYSC 3.2.8R(1) states that a firm which carries on designated investment business with or for retail clients or professional clients must allocate to a director or senior manager the function of having responsibility for oversight of the firm's compliance and reporting to the governing body in respect of that responsibility.

34. SYSC 3.2.8R(2)(c) states that "compliance" means compliance with the rules in CASS (Client Assets).

35. SYSC 3.2.9G(2) provides that the rules referred to in SYSC 3.2.8R(2) are the minimum area of focus for the firm's compliance oversight function.