
FINAL NOTICE

To: **Gillen Farrelly Independent Mortgage Advisers**

Of: Foxhall Business Centre

Foxhall Road

Nottingham

NG7 6LH

Date: **26 January 2009**

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London, E14 5HS ("the FSA") has taken the following action:

1. ACTION

- 1.1. The FSA gave Gillen Farrelly Independent Mortgages Advisers ("Gillen Farrelly"/"the Firm") a Decision Notice on 26 January 2009 which notified the Firm that pursuant to section 206 of the Financial Services and Markets Act 2000 ("the Act") and on the basis that Gillen Farrelly has agreed to conduct a customer remediation exercise, the FSA has decided to impose a financial penalty of £17,500 in respect of breaches of the FSA's Principles for Businesses ("Principles") and related FSA Rules between 1 January 2006 and 25 April 2008 ("the relevant period").

- 1.2. Gillen Farrelly breached Principle 9 (suitability of advice) and Principle 2 (due skill, care and diligence) in relation to advised sales of regulated (self-certified) mortgage contracts.
- 1.3. This penalty also takes into account the fact that Gillen Farrelly has breached FSA Rules 4.7.2R, 4.7.4R, 4.7.6R and 4.7.17R in the part of the Handbook entitled Mortgages and Home Finance: Conduct of Business (“MCOB”). The details of these rules are set out in Annex 1 to this notice.
- 1.4. Gillen Farrelly agreed to settle at an early stage of the FSA’s investigation and therefore 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 £25,000.

2. REASONS FOR THE ACTION

- 2.1. Based on the review of a sample of 20 out of 83 self-certified mortgages completed and a review of the firm’s sales procedures and systems and controls during the relevant period, the FSA has concluded that Gillen Farrelly failed to take reasonable care to ensure the suitability of advice given to customers, and failed to act with the skill, care and diligence appropriate to its business. These breaches relate to the operation of the firm’s self-certified mortgage sales process.
- 2.2. In summary, Gillen Farrelly failed to take reasonable steps to ensure the suitability of its advice in accordance with Principle 9 in that it failed to gather and record sufficient personal and financial information about its customers to demonstrate the suitability of, and the reasons for, its recommendations.
- 2.3. In particular, Gillen Farrelly failed to make appropriate enquiries about customers’ income, expenditure, credit history and debt position, so that it could properly assess the affordability of its recommendations.
- 2.4. Gillen Farrelly also failed to conduct its business with due skill and care in respect of its mortgage advisory process, in accordance with Principle 2, in that it failed to conduct adequate due diligence in respect of a third party introducer and failed to carry out straightforward checks which would have enabled it to assess the accuracy

of information provided by customers referred by that introducer. This increased the risk of the firm being used by third parties to commit financial crime.

- 2.5. The FSA considers that Gillen Farrelly's failings are particularly serious due to the fact that a number of its customers were consolidating debts and/or appeared to have adverse credit histories. Gillen Farrelly's conduct exposed its customers to potentially significant financial detriment by failing to give proper consideration to the long term implications of the products recommended, given their financial circumstances.

3. RELEVANT STATUTORY PROVISIONS AND REGULATORY REQUIREMENTS

- 3.1. The FSA's statutory objectives are set out in section 2(2) of the Act. The relevant objectives for the purpose of this case are public awareness, the protection of consumers and the reduction of financial crime.

- 3.2. Section 138 of the Act provides that the FSA may make such rules applying to authorised persons as appear to be necessary or expedient for the purpose of protecting the interests of consumers.

- 3.3. Section 206 of the Act provides:

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

- 3.4. 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. These Principles are a general statement of the fundamental obligations of firms under the regulatory system and reflect the FSA's regulatory objectives. Breaching a Principle makes a firm liable to disciplinary action.

- 3.5. The Principles and Rules which are relevant to this matter are set out below.

FSA's Principles for Businesses

- 3.6. **Principle 2** (Due skill, care and diligence) provides that: *"A firm must act with due skill, care and diligence"*

- 3.7. **Principle 9** (Suitability of advice) provides that: “*A firm must take reasonable care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely on its judgement.*”

FSA Rules and Guidance

- 3.8. The relevant FSA rules are MCOB 4.7.2R, 4.7.4R, 4.7.6R and 4.7.17R. The details of these rules are set out in Annex 1 to this notice.

4. FACTS AND MATTERS RELIED UPON

- 4.1. Gillen Farrelly is a small firm of mortgage advisers based in Nottingham. It provides advice in relation to a range of mortgage products, including (until January 2008) self-certified mortgages. It has been authorised and regulated by the FSA since 31 October 2004. Its authorised business also includes advising on and arranging insurance contracts.
- 4.2. The firm is a partnership consisting of two partners, Mr Joseph Farrelly and Mr Joseph Gillen. The firm has no other permanent staff. During the relevant period, Mr Farrelly and Mr Gillen were the only sales advisers selling mortgages for the Firm.
- 4.3. The FSA visited the firm in December 2005 and January 2006 and again in August 2007, as part of a thematic project looking at the sale of self-certified mortgage products.
- 4.4. During the visits, the FSA identified a number of deficiencies in relation to the recommendation of self-certified mortgages to customers. Following the August 2007 visit, the FSA commenced a formal investigation to ascertain the extent of the issues identified during the thematic project visit.
- 4.5. The FSA reviewed a sample of 20 customer files from a total of 83 self-certified mortgages completed during the relevant period as part of its investigation. The FSA was also provided with a report prepared by external compliance consultants, commissioned by Gillen Farrelly.

4.6. The investigation covered Gillen Farrelly's sales process, and focussed on the main consumer risk issues:

- (1) assessing whether a suitable recommendation could have been made from the information on file;
- (2) establishing the adequacy of the information obtained from the customers; and
- (3) assessing the firm's, procedures and systems and controls for ensuring the suitability of advice.

Summary of investigation findings

4.7. The file review revealed the following:

- (1) 13 of the 20 files (65%) reviewed indicated that the customer was self-certifying because he was self-employed and therefore did not have proof of earnings. However, in 8 of these cases, it was not clear why the customer did not have proof of earnings as the customer had an accountant and/or had been in business for three years or more.
- (2) None of the files (100%) reviewed contained sufficient evidence for the firm to be able properly to assess the plausibility of the income stated.
- (3) 4 of the 20 files (20%) reviewed did not contain evidence of any assessment of plausibility of income.
- (4) 6 of the 20 files (30%) reviewed did not contain any evidence of research of options to be able to demonstrate why the particular mortgage was recommended.
- (5) 5 of the 20 files involved interest-only mortgages. Of these 5 files, only 2 (40%) contained evidence of discussions and disclosure of a capital repayment vehicle.
- (6) 5 of the 20 files (25%) involved remortgaging for reasons of debt consolidation, but the firm was only able to demonstrate in 2 of those 5 files (40%) that it had considered the appropriateness of debt consolidation and the

implications of securing short term debts by adding them to a long term mortgage.

(7) There were affordability concerns in 7 of the 20 files (35%).

5. ANALYSIS OF BREACHES

Principle 9

- 5.1. Gillen Farrelly did not demonstrate that it took reasonable steps to ensure suitable advice was given to customers.
- 5.2. Gillen Farrelly failed to make appropriate enquiries about customers' income, expenditure, credit history and debt position, so that it could properly assess the affordability of its recommendations. The firm did not obtain sufficient information for it to be able properly to assess the plausibility of income in relation to mortgages on a self-certification basis.
- 5.3. Gillen Farrelly's recommendations were sometimes made on the basis of incomplete information and unsigned fact finds. In addition, inadequate consideration was given to customers' ability to repay where interest only mortgage products were recommended.
- 5.4. In 30% of the client files reviewed, there was no evidence of any product research to support the recommendations made by Gillen Farrelly's advisers.
- 5.5. The failure to ensure that sufficient personal and financial information about customers was gathered and recorded meant that Gillen Farrelly's ability to check the suitability of recommendations to enter into mortgage contracts was severely hindered.
- 5.6. Furthermore, Gillen Farrelly was not able to provide sufficient evidence to demonstrate that it had checked self-certification mortgage sales during the relevant period to ensure the quality and suitability of recommendations made.
- 5.7. On the basis of the matters above, Gillen Farrelly could not demonstrate the suitability of its self-certified mortgage recommendations for its customers.

Customers were therefore exposed to the risk of financial loss in the event that they had taken up unsuitable products.

- 5.8. The facts and matters discussed in paragraphs 5.1 to 5.7 above demonstrate that Gillen Farrelly breached Principle 9 of the FSA's Principles for Businesses. The FSA considers that the above paragraphs also demonstrate that Gillen Farrelly breached MCOB 4.7.2R, 4.7.4R, 4.7.6R and 4.7.17R.

Principle 2

- 5.9. Gillen Farrelly failed to conduct its business with due skill, care and diligence, in that it failed to conduct adequate due diligence in respect of a third party introducer and failed to carry out straightforward checks which would have enabled it to ascertain the accuracy of information provided by customers referred by that introducer. This increased the risk of the firm being used by third parties to commit financial crime.

Failure to exercise due diligence in respect of third party introducer and customers introduced by him

- 5.10. Following the FSA's visit to Gillen Farrelly in December 2005, the FSA highlighted concerns to the firm in relation to its arrangements with a third party accountant (the "Introducer"), who introduced to the firm clients seeking self-certified mortgages. Specifically, the FSA noted that Gillen Farrelly had no introducer agreement in place with the Introducer and that no due diligence had been conducted on the Introducer, who was not registered as a certified or as a chartered accountant.
- 5.11. Given the FSA's concerns, Gillen Farrelly was on notice of the importance of due diligence and ensuring that the applications made and information provided by clients introduced by the Introducer were accurate and genuine. Gillen Farrelly stated in a letter to the FSA in March 2006 that it would monitor each individual case received from the Introducer to ensure that it was suitable. However, Gillen Farrelly continued to accept referrals from the Introducer between March 2006 and November 2007 without adequate monitoring or due diligence, despite being aware of the FSA's concerns.

- 5.12. 12 of the 20 files (60%) reviewed (dated between September 2006 and March 2007) indicated that the customer was introduced by the Introducer. The Introducer was the accountant for these customers, yet none of them provided or made reference to any accounts in support of their application. None of the files relating to customers introduced by the Introducer contained adequate evidence in support of the income stated. In the circumstances, Gillen Farrelly should have paid particular attention to querying the information provided by those customers.
- 5.13. In addition, Gillen Farrelly did not query the rationale for seeking mortgages on a self-certified basis or the information given to it by the Introducer's customers in circumstances where there should have been doubt. For instance:
- (1) one customer had been in business for 27 years as an optician and yet could not provide any accounts;
 - (2) it was not clear why another customer had no accounts when he had been in business for 3 years; and
 - (3) the file of another customer contained a credit search showing that several mortgage searches had been done in his name by mortgage and loan companies in the previous 18 months for varying amounts of credit (one of which was for £999,999). This should have alerted the firm about the need for further checks but there was no evidence that the adviser had looked any further into this.
- 5.14. The failures to conduct adequate due diligence in respect of the Introducer and those customers introduced by him meant that Gillen Farrelly could not adequately counter the risk that it might be used in connection with financial crime such as handling fraudulent mortgage applications.
- 5.15. Accordingly, given the conduct set out in paragraphs 5.9 to 5.14 above, Gillen Farrelly breached Principle 2.

6. ANALYSIS OF SANCTION

6.1. The FSA's policy on the imposition of financial penalties is set out in Chapter 6 of the Decision Procedures and Penalties Manual ("DEPP"), which forms part of the FSA Handbook and came into force on 28 August 2007. It was previously set out in Chapter 13 of the Enforcement Manual ("ENF"). As neither ENF nor DEPP were in force throughout the entirety of the relevant period, the FSA considered both ENF and DEPP in deciding upon the outcome. Both manuals set out the factors that may be of particular relevance in determining whether it is appropriate to impose a financial penalty. The criteria are not exhaustive and all relevant circumstances of the case will be taken into consideration. The principal purpose of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have committed breaches from committing further breaches and helping to deter other firms from committing similar breaches, as well as demonstrating generally the benefits of a compliant business.

6.2. The FSA considers that the following factors are particularly relevant in this case.

Deterrence

6.3. A financial penalty will deter Gillen Farrelly from further breaches of regulatory rules and Principles. Equally, other firms will be deterred from following Gillen Farrelly's practices and this will promote the message to the industry that the FSA expects firms to maintain high standards of regulatory conduct.

The nature, seriousness and impact of the breach in question

6.4. In determining the appropriate sanction, the FSA has had regard to the seriousness of the breaches, including the nature of the requirements breached, the duration and frequency of the breaches, whether the breaches revealed serious or systematic failings and the number of customers who were affected and/or placed at risk of loss. For the reasons set out below the FSA considers that the breaches in this case are of a serious nature.

6.5. Gillen Farrelly's failings are viewed as being serious because:

- (1) the failings impacted customers who were financially vulnerable;
- (2) failures in information gathering were widespread and systemic in nature;
- (3) due to deficiencies in fact finding, in recording of customers' personal and financial information (including evidence and reasons for recommendations) and verification of self-certified income, it was not possible for Gillen Farrelly to demonstrate that it had considered the interests of its customers or that its customers had been treated fairly in terms of the affordability and suitability of recommendations; and
- (4) the failure to conduct adequate due diligence in respect of the Introducer and customers introduced by him meant that Gillen Farrelly could not adequately counter the risk that it might be used in connection with financial crime.

The extent to which the breach was deliberate or reckless

- 6.6. The FSA has found no evidence to show that Gillen Farrelly acted in a deliberate or reckless manner.

The amount of benefit gained or loss avoided

- 6.7. The total fees and commissions from the total self-certified business written in the relevant period is £36,539.

Conduct following the breach

- 6.8. Gillen Farrelly has undertaken the following steps in the period since the breach. The firm:
- (1) voluntarily engaged a firm of external compliance consultants to conduct a compliance audit in May 2008;
 - (2) has terminated its arrangements with the Introducer and has not accepted any referrals of mortgages from the Introducer since November 2007;
 - (3) no longer sells self certification mortgages; and

- (4) has agreed to undertake a customer contact and remediation exercise (Annex 2).

Disciplinary record and compliance history

- 6.9. Gillen Farrelly has not been the subject of previous disciplinary action.

Other action taken by the FSA

- 6.10. In determining whether to impose a financial penalty, the FSA has taken into account penalties imposed by the FSA on other authorised persons for similar behaviour.

The size, financial resources and other circumstances of the firm

- 6.11. The FSA has taken into account the firm's size and financial resources and considers that it is able to pay the financial penalty imposed on it.

7. DECISION MAKERS

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

8. IMPORTANT

- 8.1. This Final Notice is given to Gillen Farrelly under section 390 of the Act.
- 8.2. Gillen Farrelly must pay to the FSA £8,750.00 of the financial penalty within 14 days of the date on which this Final Notice is given to it. The remaining balance of the financial penalty must be paid to the FSA by no later than 23 July 2009.
- 8.3. If all or any part of the financial penalty is outstanding after the agreed date of payment, the FSA may recover the outstanding amount as a debt owed by Gillen Farrelly and due to the FSA.
- 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.

FSA contacts

- 8.5. For more information concerning this matter generally, please contact Francesca Harte at the FSA (direct line: 020 7066 1482 / fax: 020 7066 1483).

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Georgina Philippou

Project Sponsor, for and on behalf of the FSA