
FINAL NOTICE

To: **Hoodless Brennan Plc**
Of: **40 Marsh Wall,
London E14 9TP**
Date: **9 August 2006**

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.

THE PENALTY

1. For the reasons listed below, and having agreed with Hoodless Brennan Plc (formerly Hoodless Brennan and Partners Plc) ("HBP") the facts and matters set out below, the FSA has decided to impose a financial penalty of £90,000 on HBP in respect of breaches of FSA Principles 2, 6 and 7 and Conduct of Business Rule 2.1.3R (as set out in the FSA Handbook).
2. The FSA emphasises that this action relates only to the particular events in 2003 referred to in this Notice. At the time, the management of HBP was in a period of significant transition. This Notice does not contain, and should not be taken to imply, any other findings in relation to HBP.

**RELEVANT STATUTORY PROVISIONS AND REGULATORY RULES/
PRINCIPLES**

3. The FSA is authorised by section 206(1) of the Act to impose a financial penalty of such amount as it considers appropriate if it considers that an authorised person has contravened a requirement imposed on him by or under the Act.

4. The procedure to be followed in relation to the imposition of a financial penalty is set out in sections 207 and 208 of the Act.
5. Principles 2, 6, and 7 of the FSA's Principles for Business ("FSA Principle(s)") are set out below:
 - 5.1 *FSA Principle 2*: A firm must conduct its business with due skill, care and diligence.
 - 5.2 *FSA Principle 6*: A firm must pay due regard to the interests of its customers and treat them fairly.
 - 5.3 *FSA Principle 7*: A firm must pay due regard to the information needs of its customers, and communicate information to them in a way which is clear, fair and not misleading.
6. Conduct of Business rule ("COB Rule") 2.1.3R (Communication with customers) states that when a firm communicates information to a customer, the firm must take reasonable steps to communicate in a way which is clear, fair and not misleading.

REASONS FOR ACTION

Summary

7. The breaches of Principles 2, 6 and 7 and COB Rule 2.1.3.R arose from HBP's handling of information concerning a contract between Hoodless Brennan and Knowledge Technology Solutions plc ("KTS") dated 4 June 2003 for the supply of a price information service known as QuoteTerminal ("the contract") and the way HBP sold KTS shares to its private customers on 12 June and 25 July 2003.
8. In breach of Principle 2:
 - 8.1 HBP did not deal appropriately with the issue of whether information about the contract was not in the public domain.
 - 8.2 HBP did not take adequate steps to ensure that broking staff were fully aware of the contract or to brief them about whether they could mention it to customers when it was not in the public domain.
 - 8.3 HBP did consider whether KTS might make or have to make an announcement about the contract but made assumptions and did not clarify the position with KTS or take professional advice internally or externally. HBP accepts that, while it may have been justified in the assumptions it made, subsequent issues could have been avoided had it clarified the position with KTS.
9. In breach of Principle 6, Principle 7, and COB 2.1.3R:
 - 9.1 HBP broking staff used unacceptable selling practices, which fell below the standard to be expected under the regulatory regime (notwithstanding that only a small number of customers were affected, they did not suffer financial

detriment and no complaints were received), and which also fell below its internal standards, when selling KTS shares to private customers on 12 June and 25 July 2003;

- 9.2 When retailing KTS shares on 12 June and 25 July 2003, HBP broking staff provided personal opinions to customers, conjectured about the shares and mentioned the contract in an inconsistent manner, using it, inappropriately, as a sales aid. HBP broking staff were not in a position to comment on the contract having had no briefing or guidance on the terms of the contract, its relevance to the sale of the KTS shares or what could be said to customers. As a result, they provided unbalanced and potentially misleading information.
10. The FSA agrees that the circumstances relating to the information about the contract were extremely unusual. However, the FSA considers that the unusual nature of the circumstances should have led HBP to take particular care about the status of the information about the contract and does not justify the unacceptable selling practices which are described below.

Facts and matters relied on

11. HBP is a stockbroking firm that specialises in the Alternative Investment Market (“AIM”) of the London Stock Exchange (“LSE”). It has been authorised by the FSA since 1 December 2001, having previously been regulated by the Securities and Futures Authority from 3 December 1998.
12. KTS is a technology and software solutions company traded on AIM which provides a real time price information system for market professionals called “QuoteTerminal”.
13. On 13 November 2002, HBP agreed to trial QuoteTerminal.
14. On 28 November 2002, bought 2 million KTS penny shares as principal which it had sold on to retail customers by 3 December 2002.
15. On 14 January 2003, HBP bought a further 400,000 KTS shares as principal.
16. On 15 January 2003, KTS offered to supply HBP with QuoteTerminal.
17. HBP decided not to sell the KTS stock purchased on 14 January 2003 to its customers but to sell it to the market. The reason given by HBP for this is that it was to enable the firm to make the decision whether to take QuoteTerminal without being influenced by its shareholding in KTS. The stock was sold to the market on 28 and 29 January 2003.
18. Following discussions between KTS and HBP in March 2003, HBP decided that it would enter into the contract.
19. On 12 May 2003, HBP was offered more shares in KTS. HBP decided not to buy these shares on the basis that it was about to enter into the contract with KTS and this might require a regulatory announcement by KTS.

20. On 22 May 2003, there was a series of communications between staff at HBP concerning the purchase and sale of KTS stock in view of the Contract and a possible announcement by KTS. A certain member of HBP staff was asked to clarify with KTS whether it would announce the contract or not, since HBP took the view that, if KTS was not going to make an announcement, there was no reason why HBP should not deal in KTS shares. However, this request was not followed up.
21. On 4 June 2000, HBP signed the contract with KTS for the supply of QuoteTerminal.
22. On 12 June 2003, HBP purchased 900,000 KTS shares with a view to selling them to its customers immediately.
23. By close of business that day, HBP had sold its entire holding of KTS shares to eleven advisory customers for a total consideration of £58,000 generating a gross profit of £15,750.
24. On 13 June 2003, KTS requested approval from HBP for a draft press announcement which KTS hoped to release on 16 June 2003. HBP decided not to agree to an announcement as it had just dealt in KTS stock.
25. On 24 July 2003, HBP repurchased 120,000 KTS shares from two of its customers. These were sold to two further customers on 25 July 2003.
26. Communications between KTS and HBP indicate that KTS sought to obtain HBP's permission in order to put out an announcement about the contract. Indeed, in addition to the 13 June request referred to above, KTS sought HBP's approval in relation to an announcement on 1, 2 and 28 July 2003 and 6 and 14 August 2003. HBP finally agreed to the publication of a "press announcement" on 14 August 2003, but did not clarify with KTS whether a regulatory announcement would be made.
27. On 19 August 2003, KTS announced the contract with HBP on the Regulatory News Service ("RNS"). The announcement stated that KTS had secured a contract to provide HBP with QuoteTerminal. In the immediate aftermath of the announcement there was a rise of about 1% in KTS's share price, although the share price had doubled since 31 July 2003.

Particulars of breaches

i. FSA Principle 2

HBP's handling of information about the contract and the discussions about the contract

28. The FSA considers that HBP's handling of information about the contract and the discussions leading to the signing of the contract, as well as its decision-making regarding purchases of KTS shares in the light of that information, were inadequate.
29. HBP was aware that the information it held in relation to KTS and the contract was not in the public domain and that this could raise issues that they should address.

30. There appears to have been uncertainty within HBP as to whether the contract would be price sensitive. Whilst one person appeared to recognise the possibility, others expressed the view that the contract would not be price sensitive because, in their view, HBP was such a small stockbroker that the market was not likely to be influenced by an announcement of the contract. HBP did not clarify the position.
31. The FSA is therefore of the view that HBP did not demonstrate sufficient due skill, care and diligence in relation to the status of information about the contract. The FSA considers that HBP should not have made assumptions in relation to whether or not KTS would make a press or regulatory announcement about the contract, but should have taken steps to clarify the position, formed its own view and then ensured that the information was handled appropriately. Further, the FSA considers that HBP should have asked KTS specifically about whether a regulatory announcement would be required once the contract was signed, having identified itself that this would be appropriate, and acted accordingly. Had HBP done so, some of the later difficulties surrounding knowledge and use of the information about the contract which are identified in this Notice, could have been avoided. The FSA accepts that if HBP had asked KTS it would have been entitled to rely on KTS's answer so far as Principle 2 is concerned, whether or not that answer was correct under the relevant rules of AIM.

Lack of guidance to brokers

32. HBP's brokers were aware of the contract because they had been trained to use QuoteTerminal and had been provided with passwords. However, they were not provided with appropriate guidance and/or advice in relation to the contract and HBP did not ensure that broking staff knew of the contract's potential impact on the sale of KTS shares and what they could or should say to customers. This resulted in the contract being used inappropriately as a sales aid and disclosed to customers in an ad hoc manner. All this is notwithstanding the fact that the FSA accepts that the circumstances surrounding the contract were highly unusual.

ii. FSA Principle 6, Principle 7, COB 2.1.3R and COB 5.4.3R .

33. Having reviewed the telephone transcripts for the sales by HBP's brokers to twelve of the thirteen customers to whom KTS shares were sold on 12 June and 25 July 2003, the FSA considers that, in relation to these twelve sales, HBP's brokers used unacceptable selling practices to sell KTS shares to private customers and as a result did not pay due regard to the interests of customers and treat them fairly, did not pay due regard to the information needs of those customers and did not take reasonable steps to communicate with them in a way which was clear and fair and not misleading. The FSA will not tolerate this kind of practice or these methods of selling shares to private customers.
34. These unacceptable selling practices included:
- persuading customers to buy stock when they were not ready to do so;
 - persuading customers to take more stock than they appeared to want;

- referring to the contract when talking to customers when it was not in the public domain;
 - using the fact of the contract as an inappropriate sales aid;
 - providing customers with unsubstantiated and, at times, speculative personal opinion about KTS which was potentially misleading;
 - not ensuring that customers were provided with all appropriate information about investing in KTS' penny shares, as was required by HBP's own internal standards.
35. Specific examples of these unacceptable selling practices are given below.

Persuasion of customers

36. One broker persuaded his customer to buy 100,000 shares rather than the 50,000 shares the customer had requested. The customer made it clear that he wanted to take 50,000 shares both before and after receiving some of HBP's internal required risk warnings, but his wishes were overridden by the broker who told him, "they've already gone. I've taken them off the board". This comment implied that it was too late for the customer to change his mind regarding his purchase of the stock even though at this stage of the conversation he had not received all the required risk warnings and he could, indeed, change his mind.
37. In another instance, a broker spoke to a customer who was a doctor, whilst the customer was at work in a hospital. The broker persuaded the customer to purchase KTS shares even though the customer had explained that he did not want to make a decision until the afternoon as he wanted to find out more about KTS from the internet, and because he was in hospital and unable to concentrate on two things at once. He was told by the broker that, "You don't need to concentrate all you need to be able to do is say okay ... that's fine."
38. In a further example, a customer was persuaded to increase his order of KTS shares from 50,000 to 100,000 shares despite his reluctance to do so, on the basis that the broker was "comfortable" with 100,000.
39. The FSA considers that it is important that a firm treats its customers fairly on all occasions of its dealings. Each transaction must therefore be of the requisite standard of behaviour. While the FSA accepts that advice should be considered in light of the overall relationship with the client (to the extent that it exists), the FSA considers that this does not allow a firm to seek to excuse unacceptable standards of behaviour on the grounds that a customer expects those unacceptable standards and has not objected. Whilst only a small number of customers were affected, they did not suffer financial detriment and HBP has not received any complaints from any of the customers who bought KTS shares, these factors in themselves are not a measure of fair treatment. The FSA is satisfied that the standards of behaviour in these telephone calls, even in the light of the wider relationship between the firm and the relevant customers, were below the standard to be expected under the regulatory regime and indeed fell below the standards set by HBP's internal procedures.

Use of the contract as a sales aid

40. The majority of HBP broking staff retailing KTS shares on 12 June and 25 July 2003 in some way used the fact of the contract as a sales aid. Some brokers told customers that a contract had been agreed between HBP and KTS, but not announced, and did so in a way which suggested that an announcement would be likely to increase the value of the KTS shares. The brokers were not in a position to comment on the contract having had no briefing or guidance on the terms of the contract or its relevance to the sale of the KTS shares. The only briefing the brokers had received in relation to KTS was the research note produced by HBP's analyst, which did not mention the contract.
41. One broker in a call to his customer referred to the contract as a "massive contract for [KTS]". When interviewed by the FSA, this broker admitted that this was "pure speculation" on his part.

Other comments by brokers

42. One broker expressed disagreement with the contents of the analyst's research note on KTS, which had been produced on 12 June 2003, telling his customer, "I'll just go through the weaknesses. Although the full-year results should contain significant new contracts, break even is likely to be shown at the next interims. Turnover and cost projections are cautious but turnover in particular is difficult to predict. I don't know why he's put that on there because turnover is fairly easy to predict based on the contracts that they've won".
43. Another broker admitted in interview to not having read the analyst's research note in detail before calling the customer.
44. One broker provided his customer with generalised and potentially misleading advice, saying: "you will never make as much on the blue chips as you will on the smaller caps, it just doesn't work like that. The blue chips have grown over the last 10/20 years the smaller caps, the one's that will out perform over the next 5, 10, 15 years and beyond."
45. By using the contract as a sales aid, elaborating on the contents of the research note, exaggerating the strengths of KTS shares, undermining what the analyst had said in the research note and making other unsubstantiated comments, HBP brokers were providing customers with potentially misleading information.

Not providing other information about investing in KTS' penny shares

46. HBP's internal procedures required its brokers to give certain information to its customers. The brokers did not follow these procedures on all occasions. For example:
 - Only four customers were given complete information regarding HBP's principal long position in KTS, six were given incomplete information and two were not told anything at all.
 - Only five customers were told the price at which HBP bought the stock.

- Five customers were not told which market KTS shares traded on.
 - Four customers were not told KTS's market capitalisation.
 - Two customers were not told the bid/offer spread in the market.
47. Given that the customers involved were all advisory customers being advised to purchase AIM traded stock, the FSA regards the manner in which the KTS shares were sold as particularly serious.
48. While the FSA accepts that there was some correlation between the frequency of trading by the customer and way that the customer was treated, including the amount of information they were given, this correlation cannot excuse the unacceptable selling practices which are described here.
49. Accordingly, the FSA has concluded that HBP was in breach of Principle 2, Principle 6, Principle 7 and COB 2.1.3R.

RELEVANT GUIDANCE

General

50. In determining whether this action is appropriate, the FSA must have regard to the policy on the imposition of financial penalties as set out in Chapter 13 of the Enforcement Manual (“ENF”).
51. The imposition of a financial penalty is one of the range of regulatory tools available to the FSA. As set out at ENF 13.1.2, the principal purpose of the imposition of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions, and demonstrating generally to firms the benefits of compliant behaviour.
52. In determining whether a financial penalty is appropriate, and if so, its level, the FSA is required to consider all the relevant circumstances of the case. ENF 13.3.3 indicates the factors that may be of particular relevance in determining the level of a financial penalty. They are not exhaustive, and all the relevant circumstances of the case will be taken into consideration (ENF 13.3.4).

Factors the FSA considers to be particularly relevant to this case

i. ENF 13.3.3(1)G: the seriousness of the misconduct or contravention

53. The breaches identified by the FSA are serious not just because they relate to inconsistencies in HBP's handling of information about the contract and weaknesses in its selling practices, but in particular because they relate to the sale of AIM stock to advisory customers who might be persuaded to purchase the stock without understanding all the risks of investing in penny shares and small companies.

54. However, only a small number of customers were affected and they did not suffer financial detriment. In addition, HBP has not received any complaints from any of the customers who bought KTS shares.

ii. ENF 13.3.3(2)G: the extent to which the contravention is deliberate or misconduct was deliberate or reckless

55. The FSA considers that HBP's broking staff deliberately engaged in the unacceptable selling practices described in this Notice, to the extent that not only did they breach the FSA Principles and COB Rule which are at issue here, but they failed to comply with HBP's own internal standards and procedures.

iii. ENF 13.3.3(3)G: the size, financial resources and other circumstances of HBP

56. In 2003, HBP had an annual turnover of approximately £13 million and pre-tax profits of approximately £3 million.

iv. ENF 13.3.3(4)G: the amount of profit accrued or loss avoided

57. HBP made a gross profit of £15,750 on its purchase and sale of KTS shares. The FSA has been informed that HBP's customers would have made an aggregate profit of £45,000 if they had sold the KTS shares in about mid August 2003. However, the FSA has no information about onward sales by customers.

v. ENF 13.3.3(5)G: conduct following the contravention

58. HBP was open and co-operative with the FSA during the course of its investigation. It instructed its solicitors, Macfarlanes, to undertake an independent review of the matter, produce a report detailing any breaches of FSA Principles or COB rules and provide recommendations for any remedial action deemed necessary. HBP voluntarily provided a copy of this report to the FSA.

59. The firm proactively sought settlement of the case and engaged in settlement discussions with the FSA.

60. The firm has strengthened its senior management since the matters referred to in this Notice.

vi. ENF 13.3.3(7)G: disciplinary record and compliance history

61. The FSA imposed a financial penalty of £150,000 on HBP in December 2003 in respect of breaches of SFA/FSA Principle 1 (integrity); SFA Principle 2 (to act with due skill, care and diligence); SFA Principle 3 (market conduct); SFA Principle 9 (organise and control internal affairs in a responsible manner); and SFA Principle 10 / FSA Principle 11 (dealing with regulators in an open and co-operative way). This decision was made following successful settlement discussions with HBP and the outcome of the Tribunal proceedings against two former directors of HBP.

62. The FSA acknowledges the substantial changes made, including in the firm's senior management, since the earlier action, and that, at the time of these transactions, HBP was in a period of significant transition. The FSA has taken into consideration the fact that this is the second disciplinary action taken against HBP.

vii. ENF 13.3.3(7)G: previous action by the FSA in relation to similar behaviour by other firms

63. In setting the level of the penalty, the FSA has taken into account penalties levied by the FSA in other cases of misconduct.

CONCLUSIONS

64. Taking into account the seriousness of the breaches and the risk they posed to the FSA's statutory objectives, as well as the representations made to it, the FSA has imposed a financial penalty of £90,000 on HBP.

65. In reaching its decision the FSA has concluded, in particular, that the treatment of customers by HBP in these transactions was below the standard to be expected under the regulatory regime, and, indeed, the standard which HBP should expect in the light of its own procedures designed to ensure fair treatment of its customers. The FSA considers that this factor is the most serious aspect of this case.

66. The FSA emphasises that it has taken full account of the systems and controls which were put in place by the firm, but notes that these were not followed by the brokers concerned in these particular circumstances. The FSA would have regarded this matter as even more serious had the firm not had in place appropriate systems and controls.

DECISION MAKER

67. 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.

IMPORTANT

68. This Final Notice is given to you in accordance with section 390 of the Act.

THIRD PARTY RIGHTS

69. The FSA has given a copy of this notice to KTS.

MANNER AND TIME OF PAYMENT

70. The financial penalty must be paid in full to the FSA by no later than 23 August 2006, 14 days from the date of the Final Notice.

IF THE FINANCIAL PENALTY IS NOT PAID

71. If all or any of the financial penalty is outstanding on 24 August 2006, the FSA may recover the outstanding amount as a debt owed by HBP.

PUBLICITY

72. Sections 391(4), 391(6) and 391(7) of FSMA apply to the publication of information about the matter to which this Final Notice relates. Under those provisions, the FSA must publish such information about the matter to which this Final 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 HBP or prejudicial to the interests of consumers.
73. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA CONTACTS

74. For more information concerning this matter generally, you should contact Liz Ludlow at the FSA (direct line: 020 7066 1474 / fax: 020 7066 1475).

Georgina Philippou

Head of Department

FSA Enforcement Division