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**FINAL NOTICE**

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**To: Kilminster Financial Management Limited**

**Of: Portland House  
Portland Square  
Bristol  
BS2 8RZ**

**Date: 11 June 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.**

**THE PENALTY**

- 1.1. The FSA gave Kilminster Financial Management Ltd ("Kilminster") a Decision Notice on 6 June 2007 which notified the firm that pursuant to section 206 of the Financial Services and Markets Act 2000 ("the Act") the FSA has decided to impose a financial penalty of £42,000 on Kilminster in respect of breaches of Principles 3 and 6 of the FSA's Principles for Businesses ("the Principles").
- 1.2. Kilminster agreed to settle this matter at an early stage of the proceedings. It therefore qualified for a 30% reduction in penalty pursuant to the FSA's executive settlement procedures. Were it not for this discount the FSA would have sought to impose a financial penalty of £60,000 on Kilminster.
- 1.3. Kilminster confirmed on 4 June 2007 that it will not be referring the matter to the Financial Services and Markets Tribunal.

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

2.1. The FSA has decided to impose a financial penalty on Kilminster for breaches of the Principles referred to paragraph 1.1. These breaches, which are described in more detail at Section 4 below, relate to failings in relation to its complaints handling, its failure to monitor adequately a member of its staff and failings in its training and competence arrangements during the period from 1 January 2004 to 23 August 2006 (the "relevant period") or as otherwise stated.

2.2. These failings are viewed by the FSA as particularly serious in light of Kilminster's previous regulatory history which is set out in paragraphs 4.3 to 4.6 below.

### **Summary of Kilminster's breaches**

#### *Complaints Handling*

2.3. During the relevant period Kilminster breached Principles 3 and 6 of the Principles by failing to operate:

- (1) an appropriate and effective internal complaints handling system to ensure the timely resolution of complaints; and
- (2) appropriate procedures and processes which promoted co-operation with the Financial Ombudsman Service ("FOS").

#### *Failure to monitor adequately a member of its staff*

2.4. From 1 December 2001 to 23 August 2006 Kilminster breached Principle 3 of the Principles because it failed to monitor adequately a member of its staff in relation to the administration of a small self administered pension scheme.

#### *Training and Competence*

2.5. During the relevant period Kilminster breached Principle 3 of the Principles by failing to:

- (1) carry out supervision of its employees, based upon their risk rating, as frequently as required by Kilminster's Training and Competence Scheme; and

- (2) make appropriate training and competence records.

### **3. RELEVANT STATUTORY PROVISIONS**

#### **Statute**

- 3.1. 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 amount as it considers appropriate."*

#### **Principles**

- 3.2. Principle 3 states:

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

- 3.3. Principle 6 states:

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

#### **Rules**

- 3.4. In concluding that Kilminster has breached these Principles, the FSA has also had regard to the requirements of the following relevant rules:

- (1) in the part of the FSA Handbook (the "Handbook") entitled Dispute Resolution: Complaints ("DISP"), DISP 1.2.1R, DISP 1.2.22R, DISP 1.4.1R, DISP 1.4.4R, DISP 1.4.5R and DISP 1.6.1R;
- (2) in the part of the Handbook entitled Principles for Businesses, ("PRIN"), PRIN 3.2.1R and PRIN 3.2.3R; and
- (3) in the part of the Handbook entitled Training and Competence ("TC"), TC 2.7.5AR and TC 2.8.1R.

## **Legal effect of Principles and Rules**

- 3.5. Kilminster is an Authorised Person within the meaning of the Act. The FSA's Principles and Rules constitute requirements imposed on authorised persons under the Act.

## **Guidance**

- 3.6. The FSA's policy in deciding whether to take disciplinary action in general is set out in the Handbook at Chapter 11 of the Enforcement Manual ("ENF") and in respect of determining the appropriate level of financial penalty, the FSA's policy is set out at Chapter 13 of ENF. The FSA has had particular regard to the factors listed at ENF 13.3. Guidance on discount for early settlement is set out at ENF 13.7.

## **4. FACTS AND MATTERS RELIED ON**

### **Background**

- 4.1. Kilminster is an IFA network based in Bristol. It has 10 appointed representatives employing 35 investment advisers.
- 4.2. Kilminster has been regulated by the FSA since 1 December 2001. Prior to this date, it was regulated by the Personal Investment Authority ("PIA"). It is an authorised person under the Act with permissions granted by the FSA in the following regulated activities:
- (1) Advising on Pension Transfers and Opt Outs;
  - (2) Advising on investments (except Pension Transfers and Opt Outs);
  - (3) Advising on regulated mortgage contracts;
  - (4) Agreeing to carry on a regulated activity;
  - (5) Arranging (bringing about) deals in investments;
  - (6) Arranging (bringing about) regulated mortgage contracts;
  - (7) Assisting in the administration and performance of a contract of insurance;

- (8) Dealing in investments as agent;
- (9) Making arrangements with a view to regulated mortgage contracts; and
- (10) Making arrangements with a view to transactions in investments.

### **Previous regulatory history**

- 4.3. In April 2000, PIA issued a formal warning to Kilminster for breaches in relation to its selling practices, training and competence arrangements, compliance procedures and recruitment practices. In the context of its selling practices and training and competence arrangements, Kilminster also breached record keeping provisions. These matters were identified during PIA Supervision visits in March 1997, October 1997, October 1998 and August 1999. The breaches had not resulted in consumer loss and as Kilminster had taken remedial action to rectify the problems identified by PIA it was not referred to the PIA's Disciplinary Committee.
- 4.4. Following a PIA Supervision visit in May 2001, PIA raised further concerns in relation to Kilminster's selling practices (including its record keeping), training and competence arrangements (including its record keeping) and compliance procedures. Kilminster took remedial action to rectify the problems.
- 4.5. The FOS referred Kilminster to the FSA on two separate occasions for failure to pay promptly the Ombudsman's awards to the complainants (Kilminster have now paid both awards):
  - (1) referral in September 2005 for failure to comply with an Ombudsman decision made in April 2003; and
  - (2) referral in July 2006 for failure to comply with an Ombudsman decision made in December 2005.
- 4.6. The FSA had written to Kilminster in October 2004 about two further FOS awards with which Kilminster had failed to comply. In the first case the Ombudsman's decision had been accepted by the complainant in July 2003; in the second case a final decision had been made in December 2003. Subsequently, Kilminster complied with both awards and paid both complainants.

### **Failure to handle complaints fairly and effectively**

- 4.7. By reason of the facts and matters set out in paragraphs 4.8 to 4.15 below, Kilminster breached:
- (1) Principle 3 of the Principles as it failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems; and
  - (2) Principle 6 of the Principles as it failed to pay due regard to the interests of its customers and treat them fairly.
- 4.8. During the relevant period Kilminster received 55 complaints, which were handled by Compliance; the FSA reviewed the files for 45 of these complaints.
- 4.9. Kilminster has admitted that it failed to allocate adequate resources to complaints handling. Its resources were particularly stretched in the period from early 2005 to mid 2006.
- 4.10. Kilminster failed to put in place effective controls to monitor its complaints handling process. The firm did not maintain a complete and accurate complaints register to ensure that senior management had appropriate information to monitor effectively and identify any systemic problems in their complaints procedure and delays in complaints handling.
- 4.11. Kilminster recorded information on files which were stored alphabetically. Kilminster only created a central chronological complaints register, which enabled the progress of each complaint to be easily tracked, after the commencement of FSA's investigation. Kilminster provided the FSA with a complaints register in September 2006 and another in November 2006, after the FSA informed Kilminster that the September 2006 register was inaccurate. The FSA found that the November 2006 register was also incomplete; three complaints were not recorded and in ten cases significant dates had not been correctly recorded.
- 4.12. Kilminster had a written complaints procedure in place, which its advisors were aware of. However, Kilminster did not deal consistently with complaints in a way that

adhered to its complaints handling procedure. In particular, during the relevant period the FSA identified from its review of the 45 complaint files that:

- (1) in 18 cases Kilminster failed to send a written acknowledgement letter to the complainant within five business days of receiving the complaint; and
- (2) in 26 cases Kilminster failed to send a holding/final response and final/other response within the time limits of four and eight weeks respectively.

4.13. Kilminster did not have systems in place which ensured that it promptly and effectively dealt with settlement of final awards made against it by FOS. As set out in paragraph 4.5 above, FOS referred Kilminster to the FSA on two separate occasions for failure to pay promptly the Ombudsman's awards. Kilminster failed to deal with correspondence from FOS in a timely manner. Kilminster partly attribute their delays to third parties. However the FSA identified from its review of 45 complaint files that:

- (1) 23 complaints were referred to FOS by the complainants. Out of these 23 referrals, the FSA considers that in 11 cases delays were attributable to Kilminster's failure to deal with correspondence from FOS in a timely manner; and
- (2) out of these 11 cases FOS sent a chasing letter to Kilminster in ten cases and in five cases FOS sent more than one chasing letter to Kilminster.

4.14. The FSA identified that of the 23 cases referred to FOS by the complainants, seven were upheld by FOS in favour of the complainant, ten were not upheld by FOS and six were ongoing.

4.15. The FSA has not made a finding that Kilminster intentionally or deliberately set out to reject all claims or delay the payment of claims. However, Kilminster failed to put in place and operate an effective internal complaints handling procedure to ensure the timely resolution of complaints and, as a result, failed to pay due regard to the interests of its customers and treat them fairly.

### **Failure to monitor adequately a member of staff**

- 4.16. By reason of the facts and matters set out in paragraphs 4.17 and 4.18 below, Kilminster breached Principle 3 of the Principles as it failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
- 4.17. In particular, senior management failed to ensure that arrangements were in place for the effective monitoring of a member of staff, who was not an approved person, and for handling the subsequent complaint which ensued in relation to the administration of a small self administered pension scheme ("the SSAS").
- 4.18. Kilminster's failure to maintain clear management responsibilities from 1 December 2001 to 23 August 2006 has exposed the firm to a commercial dispute with the SSAS Trustees.

### **Failure to operate training and competence arrangements effectively**

- 4.19. By reason of the facts and matters set out in paragraphs 4.20 to 4.29 below, Kilminster breached Principle 3 of the Principles as it failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.
- 4.20. During the relevant period Kilminster operated a Training and Competence Scheme (the "Scheme") designed to achieve, maintain and enhance the competence of its employees. The level of monitoring and supervision that employees received depended on a risk assessment based on:
- (1) their experience and the qualifications they held;
  - (2) the types of business transacted;
  - (3) the results of monitoring and checking of the business they transacted; and
  - (4) the number and seriousness of complaints received.

### *Record keeping*

- 4.21. To achieve competence a new employee must complete a two stage process. Stage 1 requires employees to demonstrate their competence in “*firm specific knowledge, generic knowledge and application and analysis.*” Stage 2 involves monitoring the performance of an employee when dealing with clients. Completion of Stage 2 can only be achieved when the employee has demonstrated his/her generic knowledge and his/her application and analysis skills.
- 4.22. In the relevant period the firm employed 27 individuals who were classified as trainees and required to complete the two stage process. A review of the personnel and training and competence files of 15 of these individuals identified that only 5 contained the Stage 1 Sign Off form or other assessment required by the Scheme to evidence the satisfactory completion of Stage 1. Similarly only five files contained the completed Stage 2 Sign Off form required by the Scheme.
- 4.23. In the relevant period the firm also employed a further 14 individuals classified as competent when recruited and therefore required to complete a modified two stage process involving an initial assessment. A review of the personnel and training and competence files of 11 of these individuals identified that:
- (1) Only one file contained the initial assessment required by the Scheme detailing the individual’s qualifications, industry experience and previous training and competence records; and
  - (2) Only six files contained an assessment of the individual’s competence.
- 4.24. During the relevant period the Chairman of Kilminster provided investment advice to clients. There was no evidence in his training and competence file that his competence had been assessed, that formal meetings with his supervisor had taken place or that he had undertaken observed sales meetings in accordance with the requirements of the Scheme before November 2005.
- 4.25. There is no record to demonstrate that Kilminster assessed the competence of the individual who oversaw the insurance mediation activity nor that it regularly assessed his knowledge and skills.

- 4.26. Kilminster employed three of its current training and competence supervisors during the relevant period. In only one case is there evidence on their personnel and training and competence file that the skills and knowledge of the supervisor had been assessed.
- 4.27. Kilminster failed to make appropriate records in respect of its training and competence arrangements. Senior management have accepted that the operation of the Scheme during the relevant period was not adequately documented. Furthermore senior management have stated that the remedial action instituted following the issue of a formal warning by PIA in April 2000 had not been totally effective in rectifying the supervision and record keeping matters that had been identified during the PIA Supervision visits in 1997 and 1999. The FSA's 2001 visit had also raised concerns in relation to Kilminster's record keeping.

*Frequency of Supervision*

- 4.28. Under the Scheme once an employee is assessed as competent (s)he is subject to one of three levels of supervision based upon a risk assessment. The risk assessment determines the minimum number of new business transactions that will be checked, the frequency of formal meetings with his/her supervisor and the number of observed sales meetings.
- 4.29. Kilminster failed to supervise its employees based upon their risk rating as frequently as required by the Scheme. Of the 26 individuals employed in the relevant period assessed as competent by Kilminster a review of 22 of the personnel and training and competence files identified that:
- (1) in 12 cases the formal meetings with the supervisors had not taken place as frequently as required by the Scheme; and
  - (2) in only six cases did the observed sales meeting take place as frequently as required by the Scheme.

## 5. ANALYSIS OF PROPOSED SANCTION

### **Factors the FSA considers to be particularly relevant to this case**

#### *The seriousness of the misconduct or contravention*

- 5.1. The matters set out in paragraphs 4.3 to 4.6 above add to the seriousness of Kilminster's breaches. Whilst Kilminster took remedial steps to rectify the problems identified by the regulator in 2000 and 2001 and settled the awards as a result of the FOS referrals in 2005 and 2006, it is the FSA's view that despite the earlier warnings, Kilminster failed properly to maintain adequate systems and controls, complaints handling procedures and training and competence arrangements. Furthermore the FSA has had regard to Kilminster's tendency to take remedial steps after the FSA's intervention rather than being proactive in identifying and addressing areas of potential risk. The FSA considers that Kilminster's failings, particularly in the context of its previous regulatory history, merit a more serious financial penalty.
- 5.2. The systemic weaknesses in Kilminster's senior management systems and controls meant that Kilminster's business and affairs were not adequately monitored. In particular, its failure to monitor adequately a member of staff has resulted in senior management being unaware that the Complaint remained unresolved and outstanding and has exposed Kilminster to a commercial dispute with Trustees.
- 5.3. Key compliance arrangements and controls in relation to complaints handling and training and competence were not effectively implemented. This meant that there was a lack of key safeguards to ensure that customers were treated fairly by being dealt with by appropriately trained and supervised advisers.

#### *The duration and frequency of the misconduct*

- 5.4. Kilminster was unaware of its failures and they were only discovered as a result of FSA intervention rather than through the operation of its systems, procedures and internal reviews. In relation to Kilminster not monitoring adequately a member of staff, the breaches occurred over a prolonged period of more than four years. As regards complaints handling and training and competence the breaches occurred over a period of 18 months.

*The extent to which the misconduct was deliberate*

- 5.5. The FSA considers that despite Kilminster having allowed the failings to persist over several years its contraventions were not deliberate.

*The size, financial resources, and other circumstances of the firm*

- 5.6. The FSA has taken into account Kilminster's financial resources. It has discussed with Kilminster its ability to pay the penalty and has reviewed its most recent financial statements.

*Conduct following the contravention*

- 5.7. Following the FSA's visit in January 2006, Kilminster engaged an independent consultant to review its training and competence arrangements. Kilminster provided a copy of the independent consultant's report to the FSA and agreed to remedy the inadequacies identified.
- 5.8. Kilminster has agreed to engage an independent consultant to review its complaints handling records and procedures, and adopt recommendations from the review.
- 5.9. Kilminster has upgraded its compliance functions by employing more compliance staff and has increased its management oversight of compliance.
- 5.10. Senior management have now accepted that there was a failure in their management of systems and controls in their handling of the complaint.
- 5.11. Kilminster has co-operated fully with the FSA during the course of its investigation and agreed the facts promptly thereby ensuring efficient resolution of this matter.

*Disciplinary record and compliance history of the firm*

- 5.12. Kilminster has not previously been the subject of disciplinary action by the FSA or by the previous regulator. The FSA has taken into account Kilminster's previous compliance history as set out in paragraphs 4.3 to 4.6 above.

*Previous action taken by the FSA in relation to similar findings*

- 5.13. The FSA seeks to ensure consistency when it determines the appropriate level of penalty. The FSA has in the past taken action against firms for similar failings and these have been taken into consideration in setting the level of penalty against Kilminster.

**6. DECISION MAKER**

- 6.1. 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.

**7. IMPORTANT**

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

**Manner of and time for payment**

- 7.2. The financial penalty must be paid in full by Kilminster by no later than 11 June 2008. It will be paid in three equal instalments of £14,000.

**If the financial penalty is not paid**

- 7.3. If all or any of the financial penalty is outstanding on 11 June 2008, the FSA may recover the outstanding amount as a debt owed by Kilminster and due to the FSA.

**Publicity**

- 7.4. 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. 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.
- 7.5. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

**FSA contacts**

- 7.6. For more information concerning this matter generally, you should contact John Tutt of the Enforcement Division of the FSA (direct line: 020 7066 1240 /fax: 020 7066 1241).

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Georgina Philippou

**FSA Enforcement Division**