
FINAL NOTICE

To: Mr Neale Andrew Morton

Of: Beckley Farm
Tanfield
Stanley
DH9 9QN

Dated: 24 June 2010

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London, E14 5HS (the "FSA") gives you final notice about the following action:

1. ORDER

1.1. The FSA gave you a Decision Notice dated 12 June 2009 ("the Decision Notice") which notified you that the FSA had decided to:

- (1) impose a financial penalty of £130,192 on you, Mr Neale Andrew Morton ("Mr Morton") pursuant to section 66 of the Financial Services and Markets Act 2000 ("the Act") in respect of a failure to comply with Statements of Principle 1, 4 and 7 of the FSA's Statements of Principle and Code of Practice for Approved Persons ("APER"); and
- (2) make a prohibition order, pursuant to section 56 of the Act, prohibiting you from performing any function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm (the "Prohibition Order").

1.2. The financial penalty consists of the following:

- (1) a disgorgement of financial benefit of £5,192 arising from Neale Morton IMS Limited ("IMS") obtaining procurement fees from two regulated mortgage contracts obtained by you for your own benefit at a time when you were performing the controlled function of CF1 (Director) at IMS; and

- (2) a penalty element of £125,000 for a failure to comply with Statements of Principle 1,4 and 7.

1.3. You referred the matter to the Financial Services and Markets Tribunal, but your reference was subsequently struck out.

1.4. Accordingly, the FSA has today imposed a financial penalty of £130,192 on you and hereby makes an order, pursuant to section 56 of the Act, prohibiting you from performing any function in relation to any regulated activity carried out by an authorised person, exempt person or exempt professional firm. The Prohibition Order takes effect from 24 June 2010.

2. REASONS FOR THE ORDER

2.1. On the basis of the facts and matters described in the Warning Notice (“the Warning Notice”) and in the Decision Notice, the FSA concluded that you pose a risk to consumers and, therefore, to confidence in the financial system. Action should be taken against you in support of the FSA’s financial crime objectives because you failed to meet minimum regulatory standards in terms of honesty and integrity, which includes an obligation to comply with the requirements and standards of the regulatory system.

2.2. In summary, you:

- (1) obtained a mortgage for yourself, through Neale Morton IMS Limited (“IMS”), the firm of which you were formerly principal, based on false and misleading information about your earnings;
- (2) failed to take reasonable steps to prevent IMS being used as a vehicle for financial crime by its customers and the mortgage advisers working there; and
- (3) failed to disclose matters of material significance to the FSA, namely that one of the advisers working at IMS had been arrested and charged with mortgage fraud and money laundering and that another adviser working at IMS had been arrested on suspicion of money laundering, and failing honestly to answer questions posed by the FSA about the structure of your business.

3. STATUTORY PROVISIONS, REGULATORY GUIDANCE AND POLICY

Statutory provisions

3.1. The FSA’s statutory objectives, set out in section 2(2) of the Act, include the protection of consumers and the reduction of financial crime.

3.2. The FSA has the power, by virtue of section 66 of the Act, to impose a penalty on you of such amount as it considers appropriate where it appears to the FSA that you are guilty of misconduct and it is satisfied that it is appropriate in all the circumstances to take action against you.

3.3. You are guilty of misconduct if, while an approved person, you fail to comply with a statement of principle issued under section 64 or have been knowingly concerned in a

contravention by the relevant authorised person of a requirement imposed on that authorised person by or under the Act.

- 3.4. The FSA has the power, by virtue of section 56 of the Act, to make an order prohibiting you from performing a specified function, any function falling within a specified description or any function, if it appears to the FSA that you are not a fit and proper person to perform functions in relation to a regulated activity carried on by an authorised person. Such an order may relate to a specific regulated activity, an activity falling within a specified description or all regulated activities. The power to withdraw approval arises from section 63 of the Act.

The Statements of Principle

- 3.5. APER sets out the Statements of Principle for approved persons. It also describes factors the FSA will take into account by the FSA in determining whether an approved person's conduct complies with a particular Statement of Principle.
- 3.6. APER 3.1.3G states that, when establishing compliance with, or breach of, a Statement of Principle, account will be taken of the context in which a course of conduct was undertaken, the circumstances of the individual case, the characteristics of the particular controlled function and the behaviour expected in that function.
- 3.7. In this case, the FSA considers the most relevant Statements of Principle to be Principles 1, 4 and 7.

Statement of Principle 1

- 3.8. Principle 1 requires an approved person to act with integrity in carrying out their controlled function.

Statement of Principle 4

- 3.9. Principle 4 provides that an approved person must deal with the FSA and other regulators in an open and cooperative way and must disclose appropriately any information of which the FSA would reasonably expect notice.

Statement of Principle 7

- 3.10. Principle 7 provides that an approved person performing a significant influence function must take reasonable steps to ensure that business of the firm for which he is responsible in his controlled functions complies with the relevant requirements and standards of the regulatory system.

FSA guidance

- 3.11. FSA guidance relevant to the above statutory provisions and regulatory requirements are set out in Annex A to this notice.

4. FACTS AND MATTERS RELIED ON IN THE WARNING NOTICE

5. Background

- 5.1. You were the principal, sole director and sole shareholder of IMS, a mortgage broker operating in the Gateshead area and, when it was authorised, were its only approved person. From 31 October 2004 to 13 August 2008, you were approved to perform the controlled function of CF1 (Director) and CF8 (Apportionment and Oversight) at IMS. In the period between 31 October 2004 and 13 August 2008, you also worked as a mortgage adviser at the firm.
- 5.2. IMS was authorised by the FSA on 31 October 2004 to carry on the following regulated activities in relation to regulated mortgage contracts:
 - (1) advising on regulated mortgage contracts;
 - (2) agreeing to carry on a regulated activity;
 - (3) arranging (bringing about) regulated mortgage contracts, and
 - (4) making arrangements with a view to regulated mortgage contracts.
- 5.3. In October 2007, Northumbria Police notified the FSA that it had arrested an IMS adviser on suspicion of mortgage fraud, money laundering and obtaining property by deception. In response, the FSA visited IMS on 31 October 2007. During the visit the FSA identified a number of concerns relating to the systems and controls at IMS.
- 5.4. On 14 February 2008 the FSA commenced a formal investigation of IMS and your conduct in relation to IMS. During the course of its investigation, the FSA reviewed a sample of 63 customer mortgage files selected at random. The FSA also reviewed your personal mortgage applications, which you submitted through IMS.
- 5.5. You applied to the FSA to voluntarily cancel IMS's Part IV permission in August 2007. The FSA processed this application and cancelled IMS's Part IV permission on 13 August 2008.

Personal mortgage application and loan advances

- 5.6. In June 2006, you applied to Bank B for a mortgage. On the mortgage application form submitted to Bank B, you declared your income to be £264,000 for the tax year ended 2004 and £265,000 for each of the tax years ending 2005 and 2006.
- 5.7. The FSA sent your details to Her Majesty's Revenue and Customs ("HMRC") and Companies House for verification. According to HMRC and Companies House records, your total (taxable and non-taxable) income was £103,256 for the tax year ending April 2004, £170,444 for the tax year ending April 2005, and £167,147 for the tax year ending April 2006.
- 5.8. The inconsistencies between the income information you declared on your mortgage application forms and HMRC and Companies House records, together with the inconsistency between the income amounts you disclosed for the tax year ended 2004 on your mortgage application to Bank B, suggest that you deliberately entered false

income information on your mortgage applications and, in submitting them to lenders, committed mortgage fraud.

- 5.9. You were given opportunities to provide an explanation of the inconsistencies set out above in person and in writing. However, the FSA has considered the explanations that you provided and concluded that none of them is satisfactory.
- 5.10. As a result of your mortgage application to Bank B you obtained two mortgages and, by successfully remortgaging your property in June 2006, were able to raise an additional £20,000 of capital.

Loan advances

- 5.11. In February 2007, you applied to your existing mortgage lender, Bank B, for a loan advance of £20,000. On the application form, you made a renewed declaration of your income, stating that you earned £265,000 per annum.
- 5.12. In October 2007, you applied to Bank B for a second loan advance of £120,000. Again, you renewed your declaration of your income, stating that you earned £265,000 per annum.
- 5.13. Bank B approved both loan advances. You therefore obtained £140,000 in loan advances in 2007. Given the facts and matters set out above, the FSA considers that you obtained this sum fraudulently.

Systems and controls at IMS

- 5.14. During the course of its investigation, the FSA has also identified serious systems and controls failings as a result of which IMS has failed to comply with the relevant requirements and standards of the regulatory system. The FSA's concerns relate specifically to the systems and controls that you put in place to mitigate the risk that IMS would be used to perpetrate financial crime by the advisers who worked there.
- 5.15. In September 2004, one of your employees, Mortgage Adviser 1, was convicted of mortgage fraud and theft and sentenced to a term of imprisonment. These offences were committed whilst he was working at IMS as an adviser.
- 5.16. The FSA asked you during an interview, conducted in exercise of its statutory powers, what steps you had taken following the conviction of Mortgage Adviser 1 to ensure that IMS was not used to perpetrate financial crime again in the future. You told the FSA that you had obtained new references for all IMS employees from their previous employers and that you had implemented a more robust recruitment system at IMS, of which obtaining references from applicants' previous employers was a key aspect.
- 5.17. However, you went on to recruit an individual to work as a mortgage adviser at IMS whose two employment references expressed concerns about his overall competence and his ability to comply with regulatory standards. One reference described him as a "high compliance risk" and stated that he was below the firm's "benchmark standards for 3 KPIs [key performance indicators] including the quality of his sales documentation, range of advice given and the spread of advisers used". The second reference stated that the individual had "not attained Threshold

Competence/Competent Adviser level” and that he had four upheld complaints against him, two of which were the result of a failure to give the best advice to the customer. During the course of your interview, investigators asked you why you had recruited somebody who, on the face of it, was not sufficiently competent to give mortgage advice and could not be relied on to conduct himself in compliance with the FSA’s rules. In the FSA’s opinion, your responses demonstrated that you had not taken reasonable steps to satisfy yourself of the individual’s competence or capability or ability and willingness to work compliantly, despite apparently recognising the need for a more robust recruitment system following the successful prosecution of a previous employee for financial crime offences.

- 5.18. The FSA was also very concerned by your approach to assessing the work of your advisers and monitoring of them. In June 2006 another IMS employee, Mortgage Adviser 2, was arrested on suspicion of money laundering. During the course of your interview, investigators asked you how you responded to this. You said that you suspended Mortgage Adviser 2 while you conducted your own investigation of his conduct, the purpose of which was to satisfy yourself that Mortgage Adviser 2 was not guilty of any misconduct and therefore that he did not represent a financial crime risk. Your investigation constituted a review of Mortgage Adviser 2’s customer files, as a result of which you concluded that although his files were “not the best in the office” you were “happy with what was looked at”. On the basis of this review, you re-instated Mortgage Adviser 2, allowing him to return to IMS and continue to provide mortgage advice to customers.
- 5.19. During the course of its investigation, the FSA conducted its own review of Mortgage Adviser 2’s files and found many anomalies and inconsistencies, indicative of mortgage fraud. One customer, for example, stated that she was a self-employed restaurant owner with an annual salary of £45,000 per annum and that she had been in this business for four years. Her file stated, however, that she could not provide any documentation at all to prove her income. This was particularly concerning because her file also stated that she had an accountant who was able to guarantee that she would be able to afford her mortgage repayments. In the FSA’s view, if the customer’s accountant was able to comment on her ability to meet future repayments, he must have seen her accounts or similar documentation, and she should, therefore, have been able to provide such documentation to Mortgage Adviser 2 during the advice process. Other customers were also apparently unable to provide proof of their earnings, despite being employed full time. In the FSA’s opinion, you should have noticed these matters and drawn them to Mortgage Adviser 2’s attention, particularly given that you were aware that he was suspected of financial crime offences and are yourself a qualified and experienced mortgage adviser.
- 5.20. In November 2006 a further mortgage adviser working at IMS, Mortgage Adviser 3, was arrested on suspicion of mortgage fraud, money laundering and obtaining property by deception. It was alleged that these offences were committed through IMS. As in the case of Mortgage Adviser 2, you suspended the adviser while you conducted your own internal investigation in order to satisfy yourself that he would not pose a financial crime risk if he were to return to work pending the outcome of the police investigation.

- 5.21. The investigation comprised a review of a number of Mortgage Adviser 3's customer files. As in the case of Mortgage Adviser 2, you concluded that his files were satisfactory and allowed him to return to work at IMS.
- 5.22. During the course of its investigation, the FSA undertook its own review of the customer files that you personally passed as satisfactory. As in the case of Mortgage Adviser 2, the FSA found numerous obvious anomalies and inconsistencies, indicative of mortgage fraud, in the files, such as customers whose declared income of their mortgage application forms was directly contradicted by bank statements provided in support of said applications and customers who stated that they were unable to provide documentary evidence in support of their income despite being in full time employment.
- 5.23. Mortgage Adviser 3 has since been charged with all the offences set out above and has pleaded guilty to them.

Compliance

- 5.24. Until December 2007, you delegated partial responsibility for day to day compliance at IMS to a mortgage adviser, Mortgage Adviser 4, who had no compliance experience or training. The FSA found that Mortgage Adviser 4 was knowingly involved in mortgage fraud and the production of false documents, both to support his customers' fraudulent mortgage applications and in an attempt to conceal systems and controls failings at IMS from the FSA. You did not identify any issues with Mortgage Adviser 4's work or any other misconduct, despite working closely with him for a prolonged period.

Financial crime

- 5.25. During the course of its investigation, the FSA submitted the employment and income information from the 63 customer mortgage files it reviewed to HMRC for verification. In 43 of those cases, the details disclosed in support of their mortgage application forms was inconsistent with HMRC's records, indicating that the applicants had disclosed false employment and/or income information on their mortgage applications, thereby committing mortgage fraud.
- 5.26. The FSA found that fraudulent applications were submitted by all of the advisers working at IMS. The fact that this was an endemic problem at IMS is a further indication of a lack of sufficient systems of control in place at the firm.

Failure to disclose matters of material significance to the FSA

- 5.27. You failed to notify the FSA that Mortgage Adviser 2 was being investigated by the police for mortgage fraud and money laundering, despite the fact that your external compliance consultants twice advised you to do so, or that Mortgage Adviser 3 had been arrested on suspicion of money laundering. These are matters of material significance to the FSA because they impact on the integrity of a regulated business.
- 5.28. Furthermore, when the FSA visited IMS on 6 March 2008, you failed to disclose, when asked directly, that IMS had a fully operational second office based at business premises in Skelmersdale from which a large proportion of its business was being

conducted and where a large number of customer files were being stored. You initially told the FSA that all your customer files were stored at IMS's premises in Gateshead, and later told the FSA that some files were stored at the home of one of your advisers. You also failed to inform the FSA of the scale of the second office in Skelmersdale and failed to mention it at all during a compelled interview at the FSA in which you were asked specifically about the structure of your business.

6. REPRESENTATIONS

- 6.1. Your written representations challenged the evidence relied upon by the FSA and sought to explain the reasons for the disputed evidence. Your representations also informed the FSA of the impact of the regulatory process on you and your business. As the firm is now in liquidation, you stated that you can no longer earn a living from the business and it would take you a very long time to recover from this action.
- 6.2. With regard to your personal mortgage application and loan advances, you represented that the discrepancies between the figures stated in your applications and those presented by the FSA were due to your reliance on annualised figures as prepared by your accountant and the omission of rental income. You stated that you were not trying to deliberately withhold relevant information from the lender or the HMRC but had simply relied on the figures provided by your accountant. For these reasons the details of your income held by HMRC did not match those as stated on the application forms. Regardless of this however, you argued that your total income was far in excess of the amount required to enable you to qualify for a mortgage at the level obtained from the lenders. You argued that, in this instance, the discrepancies should not make any difference.
- 6.3. In relation to the systems and controls at the firm, you admitted it was difficult to keep up to date with changes in compliance requirements, even with the assistance of your external compliance advisers. It was for this reason that you were applying to join a network.
- 6.4. In relation to mortgage adviser 1, you stated that his illegal activities did not have anything to do with IMS and were conducted outside the firm. You said that you had informed the FSA as soon as you became aware of what mortgage adviser 1 had done. However, you represented that you were told by the FSA that there was nothing they could do until he had been charged by the police and to inform them if and when he was charged.
- 6.5. You confirmed that the police reviewed two of mortgage adviser 2's files in relation to an investigation into one of his friends. You confirmed that the mortgage adviser was suspended during the course of the police investigation and that you too reviewed some of his files. Mortgage adviser 2 was reinstated after you received confirmation from the police that they were not taking any action against him.
- 6.6. You confirmed that mortgage adviser 3 was personally known to you and in your view he had a solid financial background, without any complaints or concerns being raised as to his ability. You confirmed that mortgage adviser 3 was arrested for mortgage fraud and obtaining money by deception and that you suspended him during the course of the investigation. He was reinstated when the police confirmed that he had not been charged with any offence. You confirmed that following this

investigation you checked a large number of his files and your compliance advisers checked all of his files on their monthly visits.

- 6.7. You asserted that mortgage adviser 4 had the requisite knowledge to assist you with compliance matters at the firm and you informed the FSA of some of his duties to illustrate his contribution to dealing with the firm's compliance requirements.
- 6.8. You challenged the FSA's findings of fraud following its review of your files. You argued that there was very little a mortgage adviser could do if the client did not make complete and accurate disclosure of their financial situation. You suggested it was the client's responsibility to provide this disclosure.
- 6.9. Following your previous dealings with the FSA you did not think it was necessary to inform the FSA of the Police's involvement with mortgage advisers 2 and 3 as they had not been charged.
- 6.10. In relation to the Skelmersdale office, you stated that you had not tried to hide the existence of this office and that it was in fact no more than a working arrangement with one of your advisers. Your adviser would take files he was working on, to that office and you simply contributed towards half of the rent of the premises. This office was ultimately closed down.
- 6.11. You represented that all your mortgage advisers were properly trained, qualified and supervised at the firm. You also said that you had introduced enhanced recruitment processes after the problems with 2 of the advisers.
- 6.12. You also made representations as to your current financial circumstances and the negative impact the fine proposed in the Warning Notice would have on your personal and professional life.

7. FINDINGS AND CONCLUSIONS

- 7.1. Having considered your representations, the FSA is not satisfied that you have adequately addressed the concerns raised by the FSA.
- 7.2. You obtained a mortgage for yourself based on false and misleading information about your earnings. The FSA is not satisfied that your representations adequately explain the discrepancies in the figures provided.
- 7.3. In the FSA's view, by submitting mortgage applications and other declarations based on false and misleading information to lenders you have demonstrated a serious lack of honesty and integrity. You submitted these applications through IMS and thus in exercise of your controlled functions. Your conduct therefore constitutes a breach of Statement of Principle 1. Your lack of integrity means that you have also fallen below the minimum regulatory standards required of approved persons, by the FSA.
- 7.4. The FSA finds that you did not take the necessary steps to prevent IMS being used as a vehicle for financial crime by its customers and mortgage advisers. Despite your claim to have had the necessary systems and controls in place, the activities of 4 separate mortgage advisers were found to be fraudulent and to have exposed the firm to fraudulent financial activity.

- 7.5. In failing to prevent IMS being used as a vehicle for the perpetration of financial crime by the mortgage advisers you employed there and its customers, delegating significant responsibility for compliance to an individual who was not sufficiently qualified or experienced to carry out the role effectively and failing to take reasonable steps to improve the systems and controls at IMS following the police interest in three of your employees, the FSA considers that you failed take reasonable steps to ensure that the business of IMS complied with the relevant standards and requirements of the regulatory system, in breach of Principle 7.
- 7.6. The FSA is further not satisfied with your representations as to the reasons for your failure to disclose matters of material significance to the FSA. Your representations do not disclose any reasonable grounds for failing to do so.
- 7.7. The FSA has concluded that your failure to inform the FSA that mortgage advisers at IMS were being investigated by the police for mortgage fraud and money laundering, which it considers matters of material significance about which it would be expected to be informed, and your failure to honestly answer questions about the structure of your business posed by the FSA, constitute breaches of Statements of Principles 1 and 4 and is further evidence of your lack of fitness and propriety.

Financial penalty

- 7.8. The breaches of APER set out above are sufficiently serious to merit the imposition of a substantial financial penalty. In determining the level of financial penalty, the FSA has had regard to all the relevant circumstances of the case and the factors set out in DEPP 6 and ENF, extracts from which are set out in Annex A.

Deterrence

- 7.9. The principal purpose of the imposition of this penalty is to promote high standards of regulatory conduct by deterring approved 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.
- 7.10. In determining the appropriate level of penalty, the FSA has had regard to the need to ensure those who are approved persons act with honesty and integrity and manage their business in accordance with FSA rules and regulation. The FSA considers that a significant penalty should be imposed to demonstrate to you and others the seriousness with which the FSA regards such behaviour

The extent to which the breach was deliberate or reckless

- 7.11. The FSA considers that the misconduct summarised above which related to your own financial affairs was deliberate and that you intended or foresaw the potential or actual consequences of your actions. Where the FSA decides the breach was deliberate or reckless, it is more likely to impose a higher penalty on a person than would otherwise be the case. Accordingly the FSA considers that a proportion of the penalty should be imposed in respect of your conduct in this regard and should include an element of disgorgement of profit.

- 7.12. In respect of your activities within IMS, the FSA considers that your misconduct was reckless, occurred over a significant period of time, revealed serious and systemic weaknesses of the management systems and internal controls relating to all your business, and facilitated financial crime on a significant scale. The FSA therefore considers that a proportion of the penalty should be in respect of these failures.

The fact that the penalty is being imposed on an individual, rather than a firm

- 7.13. In determining the appropriate level of financial penalty, the FSA has taken into account that individuals do not always have the same resources as a body corporate, that enforcement action may have a greater impact on an individual, and further, that it may be possible to achieve effective deterrence by imposing a smaller penalty on an individual than a body corporate. The FSA has also considered whether the status, position and/or responsibilities of the individual are such as to make a breach committed by the individual more serious and whether the penalty should therefore be set at a higher level.
- 7.14. The FSA recognises that the financial penalty imposed on you is likely to have a significant impact on you as an individual but it is considered to be proportionate in relation to the seriousness of the misconduct and given your position as an approved person performing significant influence functions at IMS and the way you misused your business, using an authorised firm to commit financial crime.
- 7.15. In determining the appropriate level of financial penalty, the FSA has taken account of your representations on your financial circumstances and whether this would result in severe financial hardship.

Previous action taken in relation to similar findings

- 7.16. In determining the appropriate sanction, the FSA has taken into account sanctions imposed by the FSA on other authorised persons for similar behaviour. This was considered alongside the deterrent purpose for which the FSA imposes sanctions.

Prohibition

- 7.17. The FSA has concluded that your conduct demonstrates a lack of honesty and integrity and that you are not therefore fit and proper to carry out any functions in relation to any regulated activities carried on by any authorised persons.
- 7.18. It is, therefore, necessary and proportionate, in order to achieve its regulatory objectives, for the FSA to exercise its powers to make a prohibition order against you. In particular, taking this action against you is consistent with the FSA's policy of seeking to prevent individuals lacking integrity from working in authorised firms.
- 7.19. IMS's Part IV permission was cancelled by the FSA on 13 August 2008, following your submission of an application to voluntarily cancel it. Were it not for this, the FSA would also be withdrawing your approval under section 63 of the Act.

8. DECISION MAKER

- 8.1. The decision that gave rise to the obligation to give this Final Notice was made by the Regulatory Decisions Committee.

9. IMPORTANT

- 9.1. This Decision Notice is given to you in accordance with section 390 of the Act.

Manner and time of Payment

- 9.2. The financial penalty must be paid in full by you to the FSA by no later than 8 July 2010, 14 days from the date of the Final Notice.

If the financial penalty is not paid

- 9.3. If all or any of the financial penalty is outstanding on 8 July 2010, the FSA may recover the outstanding amount as a debt owed by you and due to the FSA.

Publicity

- 9.4. 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.
- 9.5. The FSA intends to publish such information about the matter to which this Final Notice relates as it considers appropriate.

FSA contacts

- 9.6. For more information concerning this matter generally, you should contact Catherine Harris of the Enforcement Division of the FSA (direct line: 020 7066 4872 / fax 020 7066 4873).

Tom Spender
Head of Department
FSA Enforcement Division

Annex A: Rules and guidance on the imposition of financial penalties

1. The FSA's policy on the imposition of financial penalties

- 1.1. The FSA's policy in relation to the imposition of financial penalties is set out in Chapter 6 of the Decision Procedure and Penalties Manual (DEPP) which forms part of the FSA Handbook. It was previously set out in Chapter 13 of the Enforcement Manual (ENF). The principal purpose of imposing a financial penalty is to promote high standards of regulatory 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.
- 1.2. The FSA will consider the full circumstances of each case when determining whether or not to take action for a financial penalty. DEPP 6.2.1G sets out guidance on a non-exhaustive list of factors that may be of relevance in determining whether to take action for a financial penalty, which include the following.
 - (1) DEPP6.2.1G(1): The nature, seriousness and impact of the suspected breach.
 - (2) DEPP6.2.1G(2): The conduct of the person after the breach.
 - (3) DEPP6.2.1G(3): The previous disciplinary record and compliance history of the person.
 - (4) DEPP6.2.1G(4): FSA guidance and other published materials.
 - (5) DEPP6.2.1G(5): Action taken by the FSA in previous similar cases.

2. Determining the level of the financial penalty

- 2.1. The FSA will consider all the relevant circumstances of a case when it determines the level of financial penalty. DEPP 6.5.2G, and previously ENF 13.3.3G, sets out guidance on a non-exhaustive list of factors that may be of relevance when determining the amount of a financial penalty.
- 2.2. Factors that may be relevant to determining the appropriate level of financial penalty include:
 - (1) whether the breach revealed serious or systematic weaknesses in the person's procedures or of the management systems or internal controls relating to all or part of a person's business (DEPP 6.5.2G(2)(b)); and
 - (2) the general compliance history of the person, including whether the FSA has previously brought to the person's attention, issues similar or related to the conduct that constitutes the breach in respect of which the penalty is imposed (DEPP 6.5.2G(9)(d)).
- 2.3. Corresponding provisions are set out in ENF 13.3.3G, which sets out factors that may be relevant when determining the appropriate level of financial penalty for a firm including the following:

- (1) whether the misconduct or contravention revealed serious or systematic weaknesses of the management systems or internal controls relating to all or part of the firm's business (ENF 13.3.3G(1)(c)); and
- (2) disciplinary record and compliance history. This will include whether the FSA has previously requested the firm to take remedial action, and the extent to which that action has been taken (ENF 13.3.3G(6)).

3. Guidance on application of APER

- 3.1. APER 4.7 provides examples of the types of behaviour that constitute breaches of Statement of Principle 7.
- 3.2. APER 4.7.3E provides that failing to take reasonable steps to implement (either personally or through a compliance department or other departments) adequate and appropriate systems of control to comply with the relevant standards of the regulatory system in respect of its regulated activities constitutes a breach of Statement of Principle 7.
- 3.3. Failing to take reasonable steps adequately to inform himself about the reason why significant breaches (whether suspected or actual) of the relevant requirements and standards of the regulatory system in respect of its regulated activities is a further example, set out at APER 4.7.5E. According to APER 4.7.6E, behaviour of this kind includes, but is not limited to, failing to investigate what systems or procedures may have failed including, where appropriate, failing to obtain expert opinion on the adequacy of systems and procedures.

The fit and proper test for approved persons

- 3.4. The module of the FSA's Handbook known as Fit and Proper Test for Approved Persons ("FIT") contains guidance on the fit and proper test. FIT 1.3.1G provides that the FSA will have regard to a number of factors when assessing a person's fitness and propriety. One of the most important considerations will be the person's honesty, integrity and reputation.
- 3.5. In determining a person's honesty, integrity and reputation, FIT 2.1.1G provides that the FSA will have regard to matters including, but not limited to, those set out in FIT 2.1.3G. The guidance includes:
 - (1) whether the person has contravened any of the requirements and standards of the regulatory system (FIT 2.1.3G(5)); and
 - (2) whether, in the past, the person has been candid and truthful in all his dealings with any regulatory body and whether the person demonstrates a readiness and willingness to comply with the requirements and standards of the regulatory system and with other legal, regulatory and professional requirements and standards (FIT 2.1.3G(13)).

4. FSA's policy for exercising its power to make a prohibition order

- 4.1. The FSA's approach to exercising its powers to make prohibition orders and withdraw approvals is set out at Chapter 9 of the Enforcement Guide ("EG").

- 4.2. EG 9.1 states that the FSA's power to make prohibition orders under section 56 of the Act helps it work towards achieving its regulatory objectives. The FSA may exercise this power where it considers that, to achieve any of those objectives, it is appropriate either to prevent an individual from performing any functions in relation to regulated activities or to restrict the functions which he may perform.
- 4.3. EG 9.4 sets out the general scope of the FSA's powers in this respect, which include the power to make a range of prohibition orders depending on the circumstances of each case and the range of regulated activities to which the individual's lack of fitness and propriety is relevant. EG 9.5 provides that the scope of a prohibition order will vary according to the range of functions which the individual concerned performs in relation to regulated activities, the reasons why he is not fit and proper and the severity of risk posed by him to consumers or the market generally.
- 4.4. In circumstances where the FSA has concerns about the fitness and propriety of an approved person, EG 9.8 to 9.14 provides guidance. In particular, EG 9.8 states that the FSA may consider whether it should prohibit that person from performing functions in relation to regulated activities, withdraw that person's approval or both. In deciding whether to withdraw approval and/or make a prohibition order, the FSA will consider whether its regulatory objectives can be achieved adequately by imposing disciplinary sanctions.
- 4.5. EG 9.9 states that the FSA will consider all the relevant circumstances when deciding whether to make a prohibition order against an approved person and/or to withdraw that person's approval. Such circumstances may include, but are not limited to, the following factors:
- (1) whether the individual is fit and proper to perform functions in relation to regulated activities. (The criteria for assessing the fitness and propriety of an approved person in terms of honesty, integrity and reputation are set out in FIT 2.1 (Honesty, integrity and reputation) and include an individual's openness and honesty in dealing with consumers, market participants and regulators and an ability and willingness to comply with requirements placed on him by or under the Act as well as with other legal and professional obligations and ethical standards); and
 - (2) the relevance and materiality of any matters indicating unfitness;
 - (3) the length of time since the occurrence of any matters indicating unfitness;
 - (4) the particular controlled function the approved person is (or was) performing, the nature and activities of the firm concerned and the markets in which he operates;
 - (5) the severity of the risk which the individual poses to consumers and to confidence in the financial system; and
 - (6) the previous disciplinary record and general compliance history of the individual.

- 4.6. EG 9.10 provides that the FSA may have regard to the cumulative effect of a number of factors and may take into account the particular controlled function which an approved person is performing for a firm, the nature and activities of the firm concerned and the markets within which it operates.
- 4.7. EG 9.12 provides a number of examples of types of behaviour which have previously resulted in the FSA deciding to issue a prohibition order or withdraw the approval of an approved person. The examples include severe acts of dishonesty, for example those which may have resulted in financial crime.