
FINAL NOTICE

To: **N-Hanced LLP**
Address: 3 Carlton Court
5th Avenue
Team Valley, Tyne & Wear
NE11 0AZ
FRN: 220519
Date: 21 June 2010

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS (“the FSA”) gives N-Hanced LLP (“N-Hanced”) final notice about a requirement to pay a financial penalty:

1. THE PENALTY

- 1.1. The FSA gave the Firm a Decision Notice on 21 June 2010 notifying that pursuant to section 206 of the Financial Services and Markets Act 2000 (“the Act”), the FSA had decided to impose a financial penalty of £21,000 on N-Hanced LLP (“N-Hanced”), in respect of its failure to comply with Principles 9 and 7 of the FSA’s Principles for Businesses (“the Principles”) between 6 April 2006 and 6 April 2008 (“the relevant period”).

- 1.2. N-Hanced agreed to settle at an early stage of the FSA's investigation. It 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 £30,000 on N-Hanced.
- 1.3. The Firm confirmed by written agreement on 7 June 2010 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 N-Hanced for breaches of the Principles within the relevant period. In summary, the FSA has concluded that:

- (1) N-Hanced failed to take reasonable steps to ensure the suitability of its advice, in breach of Principle 9 (Customers: relationships of trust), by failing to demonstrate the suitability of its advice on pension transfers. In particular N-Hanced failed to:
 - (a) obtain and record relevant information about customers in order to assess suitability of advice and support the recommendation to switch;
 - (b) monitor adequately the quality of its pension switching advice; and
 - (c) record management information on pension switching business.
- (2) N-Hanced failed to communicate information to its clients in a way which is clear, fair and not misleading in contravention of Principle 7 (Communications with clients). N-Hanced's suitability letters omitted relevant information that would have enabled the clients to make properly informed decisions.

- 2.2. N-Hanced's failings are viewed as being particularly serious because:

- (1) its failure to take reasonable care to ensure the suitability of its advice exposed customers to the risk of receiving unsuitable advice and/or advice which did not allow them to make informed decisions about their pensions; and
- (2) the failure to obtain and record relevant KYC information meant that N-Hanced's management team was unable to ascertain whether or demonstrate

that its advice was suitable and also meant that N-Hanced was unable to identify any trends arising from the switches and the failings discussed above.

2.3. The FSA considers, therefore, that N-Hanced's failure merits the imposition of a financial penalty. In determining the level of penalty, the FSA has had regard to the following mitigating factors:

- (1) N-Hanced cooperated fully with the FSA's investigation;
- (2) N-Hanced conducted an internal review of files using the FSA's pension switching template, from which there is no evidence of consumer detriment; and
- (3) N-Hanced acknowledged its record keeping failures and has put in place an extensive new paperless system to ensure that all relevant information is captured for each client. This system demands that all information is recorded on the electronic file before an adviser can move onto writing the business.

3. RELEVANT STATUTORY AND REGULATORY PROVISIONS AND FSA GUIDANCE

3.1. The relevant statutory provisions, regulatory requirements, and FSA guidance are set out at Annex 1 to this Warning Notice.

4. FACTS AND MATTERS RELIED ON

Background

4.1. On 6 April 2006 ("A-Day"), the government introduced changes to simplify the tax rules for personal and occupational pensions in the UK. In particular, limits to the amount that could be paid into a personal pension were removed, although restrictions on the amount of tax-free cash that could be taken from personal pensions remained. Additionally, from A-Day alternatives to drawing a pension as an annuity became available. Following these changes many advisers reviewed their clients' existing pension arrangement. These reviews lead to a significant increase in advice given to customers to transfer their existing pension arrangements into Personal Pension Plans ("PPPs") or Self Invested Personal Pensions ("SIPPs").

- 4.2. In light of the significant increase in pension switches, the FSA became concerned that consumers may have been switched into pension products which carried high charges and had features or additional flexibility that customers did not need. The FSA was also concerned about whether firms' controls were robust enough to detect and prevent unsuitable advice and ensure fair outcomes for customers.
- 4.3. In the summer of 2008, the FSA commenced phase 1 of a thematic review ("the thematic review") of pension switching advice, looking at pension switches made since A-Day. The review also looked at firms' management and oversight and compliance monitoring of this type of advice.
- 4.4. In December 2008, the FSA published a report on the findings of phase 1 of the thematic review. The report noted that the FSA had visited 30 firms and assessed 500 customer files. A quarter of the firms visited were assessed as providing unsuitable advice in a third or more of the cases sampled.
- 4.5. Overall unsuitable advice had been found in 16% of cases reviewed. The main reasons the files were assessed as unsuitable were as follows:
- (1) the switch involved extra product costs without good reason;
 - (2) the fund(s) recommended were not suitable for the customer's attitude to risk and personal circumstances;
 - (3) the adviser failed to explain the need for, or put in place, ongoing reviews when these were necessary; and
 - (4) the switch involved loss of benefits from the ceding scheme without good reason.
- 4.6. In February 2009, the FSA published guidance on assessing the suitability of pension switches, setting out the standards the FSA expects in relation to pension switches and the action firms should take to ensure that customers receive suitable advice.
- 4.7. The FSA wrote to over 4,500 firms to summarise its findings, to ask those firms to consider past and future sales in light of the findings, and to take remedial action where necessary. Phase 2 of the thematic review began in the third quarter of 2009

and involved further assessments of firms to review the action they have taken. Any firms that have not taken appropriate action may face further action.

N-Hanced

4.8. N-Hanced is a small IFA firm which is based in Gateshead. N-Hanced became authorised and regulated by the FSA on 17 January 2003 and, during the relevant period, N-Hanced was authorised and regulated to carry on the following regulated activities:

- (1) advising on pension transfers and pension opt outs;
- (2) advising on investments (except on pension transfers and pension opt outs);
- (3) agreeing to carry on a regulated activity;
- (4) arranging (bringing about) deals in investments; and
- (5) making arrangements with a view to transactions in investments.

4.9. On 19 January 2010, N-Hanced voluntarily varied its permissions so that it is no longer authorised to advise on pension transfers and pension opt outs.

4.10. N-Hanced has two partners. During the relevant period there were three individuals at N-Hanced who advised on pension switches. N-Hanced conducted 84 pension switches in the relevant period, with 13 of the switches into SIPPs.

4.11. For the reporting period ending 31 March 2008, N-Hanced's total revenue was £500,000 with a pre-tax profit of £300,000.

Sales process

Obtaining and recording sufficient KYC information to demonstrate suitability of advice

4.12. The FSA reviewed 10 client files selected at random. A number of failures in relation to N-Hanced's record keeping were identified as follows:

- (1) 3 of the files did not contain a fact find document and, in addition, of the 5 files that did contain a fact find, these fact finds were found to be insufficient in terms of the personal information recorded. The advisers may have possessed knowledge in relation to their customers due to their long-standing relationship with the customers, but the FSA requires such information to be obtained and adequately recorded; and
 - (2) in 6 of the files reviewed a client's attitude to risk ("ATR") was documented in either the 'know your client' ("KYC") fact find or the product suitability letter however, there was insufficient information available on the client file to ascertain how this rating had been reached.
- 4.13. The FSA believes that the above failures are particularly serious because without necessary, relevant and up-to-date KYC information, such as the fact find information and ATR, it is hard to establish whether N-Hanced identified the needs and circumstances of the client and taken these into account in recommending the switch.
- 4.14. The FSA recognises that N-Hanced has adopted a new approach to gathering KYC which now involves a core fact find being completed for each client alongside an investment specific fact find for each type of business being written.

Suitability letters

- 4.15. The FSA found that there were deficiencies in 40% of the suitability letters reviewed. These are discussed in further detail below:
- (1) In 2 of the files reviewed, the suitability letter provided by N-Hanced's compliance consultant stated that the suitability letter contained "significant omissions". The FSA agrees with these findings.
 - (2) In 3 of the files reviewed, the suitability letter was not adequately tailored to the individual client. In 1 of the files, the suitability letter stated that the adviser was aware of the client's history and financial planning needs however these could not be found anywhere else in the file.

- (3) In 3 of the files reviewed, there were insufficient illustrations or explanation of the charges and projections of the ceding scheme and the receiving scheme. In 1 of the files reviewed, the receiving scheme charges were higher than the ceding scheme and whilst the FSA acknowledge that the cost of the scheme is not the only driver for a switch, there was no explanation in the file to justify the switch.
- 4.16. A significant number of the suitability letters reviewed by the FSA were inadequate. They did not contain enough relevant information in order to assess or ensure the suitability of advice given to the clients in questions. The lack of tailoring of suitability letters to individual customers is further evidence that N-Hanced did not gather sufficient KYC information to deal with specific customer requirements.
- 4.17. N-Hanced has acknowledged that prior to the thematic review, it did not do enough in terms of obtaining projections and charging structures for pension switches and recording these on the client file. N-Hanced has since put in place systems to ensure that treating customers fairly is at the forefront of its provision of advice.

Compliance and monitoring of the suitability of advice and communications to clients

- 4.18. N-Hanced admitted that during the relevant period there were no specific compliance reports produced for pension switching business. Prior to 2007 N-Hanced checked approximately 20% of files. In 2007 N-Hanced introduced a 100% file check. Specifically, N-Hanced now operates a 100% internal file check of all client files and 10% of client files are reviewed by N-Hanced's external compliance consultant.
- 4.19. During the relevant period N-Hanced's compliance consultant did not identify any issues in relation to pension switching. Following the thematic review, N-Hanced undertook a review of its pension switching advice using the FSA's pensions switching template. N-Hanced acknowledges that its failings were in terms of record keeping and N-Hanced's compliance consultant did not raise any issues in terms of suitability of advice.
- 4.20. N-Hanced also admitted that, during the relevant period, compliance meetings were held on an ad hoc basis and were not recorded. N-Hanced rectified this issue and now

compliance and general management meetings are held formally and are fully minuted.

Management information

- 4.21. N-Hanced accepts that, during the relevant period, it had no formal procedures in place for recording and reviewing management information. Whilst N-Hanced had some systems in place, the Firm was not able to provide sufficient management information with any ease. N-Hanced also admitted that, during the relevant period, it did not undertake any trend analysis for its pension switching cases. This meant that the firm was unable to identify any issues which arose from pension switching and therefore also ran the risk of being unable to prevent any pension switching issues that did arise from reoccurring.
- 4.22. Therefore the FSA is of the view that during the relevant period the Firm was unable to adequately monitor its sales processes and proactively identify issues as and when they arose and act upon them due to its failure to have an appropriate system of management oversight and management information.
- 4.23. N-Hanced has acknowledged this failing and, since phase 1 of the thematic review, N-Hanced has now adopted a system to record all management information and conduct trend analysis.

5. ANALYSIS OF BREACHES

Breach of Principle 9 (Customers: Relationships of trust)

- 5.1. By reason of the facts and matters referred to in paragraphs 4.12 to 4.23 the FSA considers that N-Hanced failed to take reasonable steps to ensure the suitability of its advice and it therefore breached Principle 9.
- 5.2. In a number of files, N-Hanced could not demonstrate the suitability of its advice to customers on pension switching because it failed to record sufficient KYC information on files including relevant fact find information and assessment of ATR. N-Hanced failed to ensure that it obtained and recorded sufficient information on its customer files to support the recommendation to switch, such as information about the

ceding and receiving schemes and illustrations setting out a comparison between the two schemes in relation to costs, and the associated advantages and disadvantages of switching.

Breach of Principle 7 (Communications with clients)

- 5.3. By reason of the facts and matters referred to in paragraphs 4.15 to 4.17 the FSA considers that N-Hanced failed to communicate information to customers in a way which is clear, fair and not misleading, in breach of Principle 7. A number of suitability letters issued lacked relevant information.
- 5.4. In particular, a number of N-Hanced's suitability letters were largely generic and contained limited tailoring to the customers' circumstances. A number of the suitability letters failed to discuss crucial information in relation to the recommended pension switch, including a comparison of the costs of the ceding and receiving schemes.
- 5.5. N-Hanced also failed to implement adequate procedures for reviewing the suitability of advice given in relation to its pension switching business. As a consequence N-Hanced lacked the appropriate management information and were unable to conduct trend analysis to assess the suitability of its recommendations to customers.

6. ANALYSIS OF THE SANCTION

- 6.1. The FSA's policy on whether to issue a financial penalty is set out in Chapter 6 of the Decision Procedures and Penalties Manual ("DEPP"), which forms part of the FSA's Handbook. In determining the appropriate level of financial penalty the FSA has also had regard to Chapter 13 of the Enforcement Manual ("ENF"), the part of the FSA's Handbook setting out the FSA's policy on the imposition of financial penalties in force until 27 August 2007, and therefore part of the relevant period. The relevant sections of DEPP and ENF are set out at Annex 1.
- 6.2. 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.

- 6.3. The FSA will consider all the relevant circumstances of the case when deciding whether or not to impose a financial penalty. In light of the systemic weaknesses identified above the FSA considers it appropriate to impose a financial penalty on N-Hanced.
- 6.4. The FSA will also consider all the relevant circumstances of the case when deciding on the level of financial penalty.
- 6.5. The FSA considers the following factors to be particularly relevant in this case:

Deterrence

- 6.6. A financial penalty will deter N-Hanced from further breaches of regulatory rules and Principles. In addition, other firms will be deterred from allowing similar failings to occur and it will therefore 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

- 6.7. 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 failings in N-Hanced's systems and controls and the number of customers who were affected and/or placed at risk of loss. The FSA has concluded that there was a significant risk to customers of unsuitable advice arising from the significant deficiencies in respect of pension switching recommendations.

The extent to which the contravention or misconduct was deliberate or reckless

- 6.8. The FSA has not determined that N-Hanced deliberately or recklessly contravened regulatory requirements.

The size and financial resources of N-Hanced

- 6.9. The FSA has not sought information regarding N-Hanced's financial circumstances as there is no indication at present that it would be unable to pay a penalty of the level proposed.

The loss or risk of loss caused to consumers

- 6.10. Despite the problems encountered, the FSA is not aware of any consumer that has suffered any loss as a result of the Firm's breaches.

N-Hanced's conduct following the breach

- 6.11. N-Hanced acknowledged the majority of its failings in relation to pension switches during the relevant period and implemented new systems and controls to address the FSA's concerns. It moved to an electronic based system for compliance and monitoring. N-Hanced also conducted a review of the pension switches carried out during the relevant period.

Disciplinary record and compliance history

- 6.12. N-Hanced has not been the subject of any previous disciplinary action.

The FSA's approach in similar previous cases

- 6.13. In determining that a financial penalty is appropriate, the FSA has taken account of sanctions against other authorised persons for similar conduct. In the circumstances, the FSA considers that a financial penalty is a proportionate and appropriate outcome to the case.
- 6.14. Having considered all the circumstances above, the FSA has determined that £30,000 (before any discount for early settlement) is the appropriate financial penalty to impose on N-Hanced.

7. DECISION MAKERS

- 7.1. The decision which gave rise to the obligation to give this Final Notice was made on behalf of the FSA by members of the FSA Executive, being Settlement Decision Makers for the purposes of DEPP.

8. IMPORTANT

- 8.1. This Final Notice is given to N-Hanced in accordance with section 390 of the Act.

Manner of and time for payment

- 8.2. The financial penalty must be paid in full by N-Hanced to the FSA by no later than 15 July 2010.

If the financial penalty is not paid

- 8.3. If all or any of the financial penalty is outstanding on 15 July 2010, the FSA may recover the outstanding amount as a debt owed by N-Hanced and due to the FSA.

Publicity

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

FSA contacts

- 8.6. For more information concerning this matter generally, N-Hanced should contact Paul Howick (direct line: 020 7066 7954 or fax: 020 7066 7955) of the Enforcement and Financial Crime Division of the FSA.

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Tom Spender

Head of Department

FSA Enforcement and Financial Crime Division

Annex 1

1. Statutory Provisions

- 1.1. The FSA's statutory objectives set out in section 2(2) of the Act are maintaining market confidence, ensuring/raising public awareness, the protection of consumers and the reduction of financial crime. In taking action against N-Hanced, the FSA is working towards its objectives of protecting consumers, maintaining market confidence and reducing financial crime.
- 1.2. The FSA is authorised by section 206 of the Act to impose a financial penalty of such amount as it considers appropriate where the FSA considers an authorised person has contravened a requirement imposed upon it by or under the Act.

2. Relevant Handbook provisions

- 2.1. In exercising its power to impose a financial penalty, the FSA must have regard to relevant provisions in the FSA Handbook of rules and guidance ("the FSA Handbook"). The main provisions relevant to the action specified above are set out below.

Principles for Businesses

- 2.2. Under the FSA's rule-making powers as referred to above, the FSA has published in the Handbook the Principles for Business ("Principles") which apply either in whole, or in part, to all authorised persons.
- 2.3. The Principles are a general statement of the fundamental obligations of firms under the regulatory system and reflect the FSA's regulatory objectives. A firm may be liable to disciplinary sanction where it is in breach of the Principles.
- 2.4. The Principles relevant to this matter are set out below:
 - (a) Principle 7 (Communications with clients): *A firm must pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading.*
 - (b) Principle 9 (Customers: relationships of trust): *A firm must take reasonable*

care to ensure the suitability of its advice and discretionary decisions for any customer who is entitled to rely upon its judgment.

Conduct of Business Rules

- 2.5. Guidance on the Conduct of Business Rules is set out in the Conduct of Business manuals of the FSA handbook.
- 2.6. The FSA's Conduct of Business Sourcebook ("COB") was in force for part of the relevant period (until 31 October 2007).
- 2.7. COB 2.1.3R required a firm to take reasonable steps to communicate with its customers in a way which is clear, fair and not misleading.
- 2.8. COB 5.4.3R required a firm to ensure that it takes reasonable steps to ensure that a private customer understands the nature of the risks inherent in certain transactions.
- 2.9. COB 5.2.5R and 5.2.9R required a firm to take reasonable steps to ensure that it is in possession of sufficient personal and financial information about a customer relevant to the services that the firm has agreed to provide and requires a firm to make and retain a record of such information.
- 2.10. COB 5.3.14R required that the firm must, in the stipulated circumstances, provide the customer with a suitability letter.
- 2.11. COB 5.3.16R required that a suitability letter must explain why the firm has concluded the transaction is suitable and contain a summary of the main consequences and any possible disadvantages of the transaction.
- 2.12. The FSA's Conduct of Business Sourcebook ("COBS") applied to firms for part of the relevant period (with effect from 1 November 2007). The most relevant COBS rules are as follows.
- 2.13. COBS 2.1.1R provides that a firm must act honestly, fairly and professionally in accordance with the best interests of its client (the client's best interests rule).
- 2.14. COBS 4.2.1R provides that a firm must ensure that a communication or a financial promotion is fair, clear and not misleading.

- 2.15. COBS 9.2.1R provides that a firm must take reasonable steps to ensure that a personal recommendation, or a decision to trade, is suitable for its client.
- 2.16. COBS 9.2.2R provides that a firm must obtain from the client such information as is necessary for the firm to understand the essential facts about him and have a reasonable basis for believing, giving due consideration to the nature and extent of the service provided, that the specific transaction to be recommended, or entered into in the course of managing, meets his investment objectives.
- 2.17. COBS 9.4.1R provides that a firm must provide a suitability report to a retail client if the firm makes a personal recommendation to the client.
- 2.18. COBS 9.4.7R provides that the suitability report must, at least:
- specify the client's demands and needs;
 - explain why the firm has concluded that the recommended transaction is suitable for the client having regard to the information provided by the client; and
 - explain any possible disadvantages of the transaction for the client.
- 2.19. COBS 19.2.2R provides that when a firm prepares a suitability report, it must in the case of a personal pension scheme, explain why it considers the personal pension scheme to be at least as suitable as a stakeholder pension scheme.
- 2.20. COBS 19.1.2R provides that a firm must:
- (1) compare the benefits likely (on reasonable assumptions) to be paid under a defined benefits pension scheme with the benefits afforded by a personal pension scheme or stakeholder pension scheme, before it advises a retail client to transfer out of a defined benefits pension scheme;
 - (2) ensure that that comparison includes enough information for the client to be able to make an informed decision;
 - (3) give the client a copy of the comparison, drawing the client's attention to the factors that do and do not support the firm's advice, no later than when the key

features document is provided; and

- (4) take reasonable steps to ensure that the client understands the firm's comparison and its advice

Senior Management Arrangements, Systems and Controls

- 2.21. SYSC 3.1.1R provides that a firm must take reasonable care to establish and maintain such systems and controls as are appropriate to its business.
- 2.22. SYSC 3.2.6R provides that a firm must take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards under the regulatory system.

Financial Penalties

- 2.23. The FSA's approach to taking disciplinary action is set out in Chapter 2 of EG. In deciding to take the proposed action the FSA has also had regard to the appropriate provisions of ENF which was in force until 27 August 2007 and therefore during part of the Relevant Period. Imposing financial penalties and public censures shows that the FSA is upholding regulatory standards and helps to maintain market confidence, promote public awareness of regulatory standards and deter financial crime. An increased public awareness of regulatory standards also contributes to the protection of consumers.
- 2.24. The FSA's policy on the imposition of financial penalties is set out in chapter 6 of DEPP (which came into force on 28 August 2007) which is a module of the FSA's Handbook of rules and guidance (and, previously, 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 (DEPP 6.1.2G and previously ENF 13.1.2).
- 2.25. 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 (and previously ENF

12.3.3) 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:

- (a) DEPP 6.2.1G(1) and previously ENF 12.3.3(2): The nature, seriousness and impact of the suspected breach;
- (b) DEPP 6.2.1G(2) and previously ENF 12.3.3(3): The conduct of the person after the breach;
- (c) DEPP 6.2.1G(3) and previously ENF 12.3.3(4): The previous disciplinary record and compliance history of the person;
- (d) DEPP 6.2.1G(4): FSA guidance and other published materials; and
- (e) DEPP 6.2.1G(5) and previously ENF 12.3.3(5): Action taken by the FSA in previous similar cases.

2.26. 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 13.3.3) sets out guidance on a non-exhaustive list of factors that may be of relevance when determining the amount of a financial penalty, which include:

- (a) DEPP 6.5.2G(1): Deterrence;
- (b) DEPP 6.5.2G(2) and previously ENF 13.3.3(1): The nature, seriousness and impact of the breach in question;
- (c) DEPP 6.5.2G(5) and previously ENF 13.3.3(3): The size, financial resources and other circumstances of the person on whom the penalty is to be imposed;
- (d) DEPP 6.5.2G(8) and previously ENF 13.3.3(5): Conduct following the breach;
- (e) DEPP 6.5.2G(9) and previously ENF 13.3.3(6): Disciplinary record and compliance history; and
- (f) DEPP 6.5.2.G(10) and previously ENF 13.3.3(7): Other action taken by the FSA.