Financial Services Authority

FINAL NOTICE

To:	**Mr Paul Clark**
Date of birth:	**16 February 1966**
Individual ref:	**PJC00024**
Date:	**25 November 2010**

TAKE NOTICE: The Financial Services Authority of 25 The North Colonnade, Canary Wharf, London E14 5HS ("the FSA") gives you, Mr Paul Clark, final notice about the imposition of a financial penalty and the making of two prohibition orders:

1. ACTION

1.1. On 25 November 2010 the FSA gave you, Mr Paul Clark, a Decision Notice which stated that it had decided:

(1) pursuant to section 66 of the Financial Services and Markets Act ("the Act"), to impose on you a financial penalty of £10,500 for failing to comply with Statements of Principle 2 and 7 of the FSA's Statements of Principle and Code

of Practice for Approved Persons ("APER") while you were an approved person;

(2) pursuant to section 56 of the Act to make an order prohibiting you from performing any significant influence function in relation to any regulated activity carried on by any authorised person, exempt person or exempt professional firm (the "Prohibition Order"); and

(3) pursuant to section 56 of the Act to make a further order prohibiting you for a period of two years from the date of this Final Notice from performing all customer functions (CF30) in relation to sales of unregulated collective investment schemes ("UCIS") (the "Time Limited Prohibition Order").

1.2. You agreed to settle this matter at an early stage of the FSA's investigation and therefore qualified for a 30 per cent (Stage 1) discount under the FSA's executive settlement procedures. Without this discount, the FSA would have sought to impose a financial penalty of £15,000 on you.

2. REASONS FOR THE ACTION

2.1. Between 15 November 2007 and 7 May 2009 ("the relevant period"), you were approved by the FSA to perform the controlled functions of CF4 (Partner) and CF30 (Customer) at the LLP ("the LLP").

2.2. For the reasons set out more fully in section 4 below:

(1) you failed to act with due skill, care and diligence in carrying out your controlled functions (in contravention of Statement of Principle 2) by:

(a) failing to inform yourself about and demonstrate an understanding of the regulatory requirements relating to the promotion of UCIS and, in particular, the statutory restriction on the promotion of UCIS in section 238 of the Act ("the section 238 restriction") and the exemptions to that restriction; and

(b) failing to inform yourself about and apply correctly the rules relating to regulatory capital requirements; and

(2) you failed to take reasonable steps to ensure that the business of the LLP, for which you were responsible in your controlled function of CF4 Partner, complied with the relevant requirements and standards of the regulatory system (in contravention of Statement of Principle 7) by failing to:

a) ensure that the LLP had regard to the section 238 restriction and any relevant exemptions to it before promoting UCIS to its customers;

b) take reasonable steps to ensure that the LLP's personal recommendations to its customers to invest in UCIS were suitable (including a failure to meet the information gathering requirements in section 9 of the FSA's Conduct of Business Sourcebook ("COBS"));

c) demonstrate an understanding of the Treating Customers Fairly principles;

d) ensure that the LLP had an appropriate complaints handling system;

e) ensure that the LLP adequately disclosed and managed a potential conflict of interest arising from the involvement of both partners in a UCIS into which customers of the LLP were advised to invest;

f) ensure that its advisers were properly supervised and had the competence, knowledge, and skills to give investment advice;

g) ensure that the LLP had adequate financial resources and met its regulatory capital requirements since it became authorised by the FSA;

h) ensure that the LLP submitted its Retail Mediation Activities Returns to the FSA in a timely and accurate manner; and

i) ensure that the LLP dealt with the FSA in an open and co-operative way, by disclosing matters relating to it of which the FSA would reasonably expect notice.

2.3. The FSA considered that your conduct was particularly serious because your failures exposed customers to a risk of receiving unsuitable recommendations in relation to retail investment products.

2.4. Due to your failure to take reasonable steps to ensure that the LLP retained appropriate records to demonstrate whether its advisers assessed and, if so, the basis on which its advisers assessed the suitability of the products they recommended, the FSA was unable to satisfy itself that customers were recommended suitable investment products.

2.5. The FSA concluded that your conduct during the relevant period demonstrated that you had failed to comply with Statements of Principle 2 and 7, for which a financial penalty is considered an appropriate sanction. The FSA also concluded that you lack the competence and capability to perform significant influence functions in relation to regulated activities carried on by authorised persons, exempt persons and exempt professional firms. It was therefore also necessary and proportionate to make the Prohibition Order and the Time Limited Prohibition Order, in support of the FSA's consumer protection and market confidence objectives.

3. RELEVANT STATUTORY AND REGULATORY PROVISIONS

3.1. The relevant statutory provisions and regulatory requirements are set out at Annex A.

4. FACTS AND MATTERS RELIED ON

Background

4.1. The LLP was a small investment partnership based in Cardiff. With effect from 15 November 2007, the LLP was authorised by the FSA to carry on the following regulated activities:

(1) advising on investments (excluding pension transfers/opt outs);
(2) agreeing to carry on a regulated activity;
(3) arranging deals in investments; and
(4) making arrangements.

4.2. The LLP was set up as a limited liability partnership and run by you and Mr Ceri Rees. On 7 May 2009 you withdrew your approved person status. On 22 October 2009, the LLP varied its permission by adding a requirement that it would not undertake any regulated activity. The LLP conducted a low volume of regulated business, completing 50 retail investment sales between 15 November 2007 and 15 July 2010. It had approximately 70 customers of whom 11 invested in one or more of three UCIS.

4.3. During the relevant period, you and Mr Rees were the partners and the approved persons performing significant influence functions at the LLP. During the relevant period, there were between two and four investment advisers at the LLP, including you and Mr Rees. You were both responsible for the day-to-day running of the LLP and for the decision making. As the controlling minds, you were jointly responsible for taking reasonable steps to ensure that the business of the LLP was organised so that it complied with regulatory requirements and the standards of the regulatory system.

4.4. On 8 October 2009, the FSA visited the LLP. During the visit, the FSA reviewed a sample of 16 electronic client files and noted the absence of key information on the client files relevant to demonstrating the suitability of personal recommendations made by the LLP's advisers. The FSA also identified a number of serious concerns about the promotion of and personal recommendations to invest in UCIS, the management and disclosure of a conflict of interest, and the adequacy of the LLP's capital resources.

4.5. For the reasons set out below, the FSA concluded that the LLP fell below the standards expected of authorised firms.

Promotion of UCIS

4.6. The section 238 restriction prohibits authorised persons from communicating an invitation or inducement to participate in a collective investment scheme. There are a number of exemptions to the section 238 restriction which an authorised firm could rely on to promote UCIS to its retail customers.

4.7. By not paying due regard to the statutory and regulatory restrictions on the promotion of UCIS before recommending that its customers invest in UCIS, the LLP may have acted unlawfully and potentially exposed its customers to the risk of receiving

unsuitable investment advice. It may also have failed to comply with Principle 9 of the FSA's Principles for Businesses ("the Principles") which requires it to take reasonable care to ensure the suitability of its advice for any customer who is entitled to rely upon its judgment.

4.8. The relevant regulatory provisions relating to UCIS are summarised in Annex B to this Notice.

4.9. The FSA identified 11 customers (excluding you and Mr Rees) who were advised by the LLP to invest in one or more of three UCIS. One of the UCIS ("the Scheme") was, a scheme that was set up by you and Mr Rees. The FSA found no evidence that the LLP had correctly applied the relevant exemptions before promoting UCIS to customers, thereby contravening the section 238 restriction.

4.10. On 18 March 2010, you admitted that your knowledge of the statutory and regulatory restrictions relating to UCIS was limited to that which you had learnt as a result of the FSA's investigation. You failed to demonstrate an adequate understanding of the specific requirements regarding client certification. The FSA found no evidence that customers of the LLP had been categorised in accordance with the Financial Services and Markets Act 2000 (Promotion of collective investment schemes) (Exemptions) Order 2001 ("the PCIS Order") or COBS 4.12 before they received UCIS promotions from the LLP.

4.11. You also failed to ensure that the LLP made personal recommendations to its customers to invest in UCIS without first adequately assessing and documenting the customers' personal and financial circumstances and knowledge and experience of this type of investment.

Suitability of advice

4.12. You failed to take reasonable steps to ensure that the LLP made suitable recommendations to its customers, in contravention of COBS 9.2.1R. The FSA found no satisfactory evidence that the LLP's advisers had complied with the requirements in COBS 9 as there was an absence of key information on client files such as fact finds, product research and suitability letters. You said that, upon migrating data to a new electronic record keeping system, a number of key documents had gone missing. You provided the investigation team with missing documentation in March 2010, which the FSA also reviewed. Nevertheless, the FSA identified the following deficiencies in the fully assembled client records:

(1) there were missing documents and inadequate information on client files to demonstrate the adviser's awareness and understanding of the customer's financial circumstances, investment objectives and knowledge and experience of financial products;

(2) there was insufficient evidence of product research, consideration of alternative products and/or independent due diligence on files, and no evidence of research to compare the recommended product with the customer's existing investment in cases where transfers/switches had been recommended;

(3) in some cases, the advice was inconsistent with the customer's stated needs and preferences;

(4) assessments of customers' attitude to risk were missing or inadequate, and there was insufficient evidence to show that customers understood the risks involved in recommended transactions;

(5) there were no documented assessments of the risk of exposing significant proportions of customers' assets to UCIS investments;

(6) there was no evidence of a policy on the diversification of customer portfolios to mitigate the risks associated with investments in UCIS and manage concentration risk;

(7) one customer who was near to retirement invested 60% of his portfolio in UCIS and another retired customer invested 55% of his (tax-free) retirement lump sum in UCIS and, in both cases, there was no evidence to show that they could tolerate a partial or complete loss of the capital invested; and

(8) UCIS customers were issued with letters wrongly classifying them as "sophisticated and experienced investors", with insufficient explanations as to how the recommended product was suitable for them.

4.13. As a result of the failings in the LLP's sales process identified above, at least 11 customers were exposed to the risk of receiving unsuitable advice and put in a position in which they made investment decisions based on incomplete and/or misleading information.

Capital adequacy/ reporting to the FSA

4.14. The FSA concluded that, during the relevant period, you failed to act with due skill, care and diligence by failing to inform yourself about the FSA's capital requirements and to take reasonable steps to ensure that the LLP met its capital requirements. You also failed to ensure that the LLP submitted accurate and complete reports to the FSA by the due date, in breach of section 16.12 of the FSA's Supervision manual ("SUP"). These failings are as follows.

(1) The LLP's Retail Mediation Activities Return ("RMAR") for 31 March 2008 showed that it had wrongly relied on its partners' personal assets to meet regulatory capital requirements. You understood that RMARs were a means of submitting financial information to the FSA, but you did not know any more about this matter.

(2) As at September 2009, the LLP had failed to submit RMARs for the periods ending 30 September 2008 and 31 March 2009. These RMARs fell within the time period in which you were an approved person of the LLP. You were aware that the LLP had had some IT problems when trying to submit information, but that was the extent of your knowledge.

(3) A review of the information underpinning the March 2009 RMAR identified the inclusion of a debt owed to the LLP by a connected company, Company A.

You and Mr Rees were also directors of Company A and as such you knew the LLP had no realistic prospect of recovering the debt because Company A had gone into administration. When the LLP revised its accounts and removed the debt, it was evident that it did not have sufficient capital.

(4) The LLP's complaints returns for the reporting period April to September 2008 and October 2008 to March 2009 were incorrectly completed and inconsistent with the LLP's own complaints register.

Potential conflict of interest

4.15. For the reasons set out below, the FSA concluded that you failed to adequately recognise, disclose and manage potential conflicts of interest.

4.16. The Scheme was an offshore UCIS set up by you and Mr Rees in 2008. You were also the two directors of the investment manager for the Scheme. In December 2009 Mr Rees resigned from the investment manager as a director and shareholder. As the founder shareholders of the Scheme, you had the right to appoint and replace the Scheme's directors. The Scheme's Private Placement Memorandum ("PPM") dated 28 July 2008 stated that the Scheme would pay fees to the investment manager for its services. During the relevant period, the Scheme invested in a particular partnership on the investment manager's recommendation.

4.17. While the partners were directors of the investment manager, which was responsible for the Scheme's investment management operations, the LLP promoted the Scheme to some of its customers and purported to provide them with independent advice in relation to it. Since December 2008, eight customers invested in the Scheme.

4.18. Although the PPM records the Scheme's approach to potential conflicts of interest, the FSA considered that it did not adequately disclose the potential conflict of interest between the partners' investment management role for the Scheme and their role as independent financial advisers at the LLP. During an interview you stated that the potential conflict of interest was also disclosed verbally to customers, but there was no confirmation or evidence of this recorded.

4.19. In May 2009 you and Mr Rees took another view of the potential conflict, which resulted in your resignation as an IFA from the LLP on 7 May 2009.

4.20. The FSA considered that between July 2008 and June 2009 your role as director of the investment manager raised a potential conflict of interest between the independent advice given by the LLP to its customers and the financial incentives to increase the funds under management by the investment manager. In addition, the LLP failed to manage this potential conflict and adequately disclose it to its customers.

Misleading customer communications

4.21. You failed to ensure that the LLP communicated with customers in way that was clear, fair and not misleading, in breach of Statement of Principle 7.

4.22. The LLP issued letters to all its UCIS customers which described them as "sophisticated and experienced", although the LLP purported to rely on the COBS

4.12 exemption categories. The letters stated that a customer should only invest in such holdings if they regarded themselves as a sophisticated and experienced investor; the LLP regarded these long-standing customers as sophisticated and experienced due to their attitude to risk and because they had built up money in pensions and had other investments. It then stated that since there was no clear definition of a sophisticated and experienced investor, the LLP felt that a key component to this was that the customer must regard himself or herself as a sophisticated and experienced investor.

4.23. The FSA considered this statement to be misleading because:

(1) it gave customers the impression that they had been categorised as sophisticated and experienced, when you stated that the LLP relied on the COBS 4.12 exemptions;

(2) "sophisticated and experienced" is not a category of exemption under the PCIS Order or COBS 4.12;

(3) there are two types of sophisticated investors referred to in the PCIS Order – certified and self-certified and there are specific definitions and requirements for each type (however you state in some of your suitability letters that you consider the customers as sophisticated investors because they hold pensions and investments which does not comply with any of the requirements); and

(4) the letters were confusing because they inferred that customers should assess their own eligibility for UCIS, yet they stated that the LLP also assessed them. (Further to the PCIS Order, a customer is either a self-certified sophisticated investor or certified by a firm as a sophisticated investor).

Compliance management oversight

4.24. The LLP did not employ an external compliance consultancy firm due to the low volume of business, although it had used one during the authorisation process. The FSA considered that you failed to implement and monitor effective compliance monitoring procedures to ensure that the LLP complied with the relevant requirements of the regulatory system. The FSA noted deficiencies in the following areas.

File checking

4.25. The FSA concluded that, in practice, there was no process to ensure that files were adequately reviewed, that issues were identified and that remedial action was recommended and completed by advisers. During interview, you said that the LLP's compliance checks were ad hoc. Some customer files, relating to advice given by Mr Rees, were not checked at all.

4.26. You did not know about the FSA's Treating Customers Fairly principles. Therefore you failed to equip yourself with the basic knowledge to effectively assess and monitor the LLP's treatment of its customers.

Complaints

4.27. The LLP's complaint handling policy was inadequate. You failed to ensure that the LLP's procedures allowed complaints to be made by any reasonable means. You did not know how a complaint against the complaints officer (Mr Rees) would be dealt with.

Management information

4.28. You failed to adequately monitor business written at the LLP. Consequently you failed to identify that the LLP's recommendations resulted in an excessive concentration of some customers' overall savings and investment portfolio in UCIS.

4.29. You told the FSA that, during the relevant period, you just operated as a financial adviser within the LLP. However, this did not release you from the responsibilities of the significant influence function that you held. Whilst Mr Rees was specifically approved to oversee the LLP's compliance function, you had a responsibility as a CF4 Partner to take reasonable steps to implement and monitor effective compliance arrangements. There was no evidence that you sought to fulfil this responsibility.

5. ANALYSIS OF THE SANCTIONS

Imposition of financial penalty

5.1. The FSA's policy on the imposition of financial penalties relevant to the misconduct as detailed in this Notice is set out in Chapter 6 of the version of the Decision Procedure and Penalties Manual ("DEPP") in force prior to 6 March 2010, which formed part of the FSA Handbook. All references to DEPP in this section are references to that version of DEPP.

5.2. 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.

5.3. In determining whether a financial penalty is appropriate the FSA is required to consider all the relevant circumstances of a case.

5.4. DEPP 6.5.2G sets out a non-exhaustive list of factors that may be of relevance in determining the level of a financial penalty. The FSA considered that the following factors are particularly relevant in this case.

Deterrence (DEPP 6.5.2(1))

5.5. In determining the level of the financial penalty, the FSA had regard to the need to ensure those who are approved persons exercising management functions act with the businesses in accordance with regulatory requirements and standards and to behave towards the FSA in an open and cooperative manner. The FSA considered that a penalty should be imposed to demonstrate to you and others the seriousness with which the FSA regards such behaviour.

The nature, seriousness and impact of the breach in question (DEPP 6.5.2(2))

5.6. Your failures exposed customers to a risk of receiving unsuitable recommendations in relation to retail investment products. Due to your failure to take reasonable steps to ensure that the LLP retained appropriate records to demonstrate whether its advisers assessed and, if so, the basis on which its advisers assessed the suitability of the products they recommended, the FSA was unable to satisfy itself that customers were recommended suitable investment products.

The extent to which the breach was deliberate or reckless (DEPP 6.5.2(3))

5.7. The FSA concluded that your contraventions were not deliberate. However, the FSA considered that the nature of your actions (and inaction) as set out in section 4 of this Notice amounted to serious misconduct.

Whether the person on whom the penalty is to be imposed is an individual (DEPP 6.5.2(4))

5.8. When determining the appropriate level of financial penalty, the FSA will take into account that individuals will 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 will also consider whether the status, position and/or responsibilities of the individuals 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.

5.9. The FSA recognised that the financial penalty imposed on you was likely to have a significant impact on you as an individual but it was 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 the LLP.

The size, financial resources and other circumstances of the person on whom the penalty is to be imposed (DEPP 6.5.2(5))

5.10. The FSA considered that the financial penalty described above was appropriate, having taken account of all relevant factors.

The amount of benefit gained or loss avoided (DEPP 6.5.2.G(6))

5.11. The FSA did not establish that you obtained any financial benefit or avoided any loss as a result of the breaches.

Conduct following the breach (DEPP 6.5.2G(8))

5.12. The FSA took into account your co-operation with the FSA's investigation.

Disciplinary record and compliance history (DEPP 6.5.2G(9))

5.13. The FSA took into account the fact that you have not been the subject of previous disciplinary action by the FSA.

Other action taken by the FSA (DEPP 6.5.2G(10))

5.14. The FSA has taken action against other approved persons for similar conduct.

5.15. The FSA therefore decided to impose a financial penalty of £15,000 on you, reduced to £10,500 to take account of the settlement discount described above.

Prohibition

5.16. The FSA had regard to the guidance in Chapter 9 of the Enforcement Guide (EG) in deciding that a Prohibition Order is appropriate in this case. The relevant provisions of EG are set out in Annex A of this notice.

6. CONCLUSIONS

6.1. On the basis of the facts and matters described above, the FSA concluded that your conduct fell short of the minimum regulatory standards required of an approved person and that you have breached Statements of Principle 2 and 7.

6.2. The FSA, having regard to all the circumstances, therefore decided that it was appropriate and proportionate to impose a financial penalty of £10,500 on you and to make the Prohibition Order and the Time Limited Prohibition Order.The effective date of the sanctions in this Final Notice is 25 November 2010.

7. DECISION MAKER

7.1. The decision which gave rise to the obligation to give this Final Notice was made on behalf of the FSA by Settlement Decision Makers for the purposes of the FSA's Decision Procedure and Penalties Manual.

8. IMPORTANT

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

Manner and time of payment

8.2. The financial penalty must be paid in full by you to the FSA by no later than 9 December 2010, 14 days after the date of this Final Notice.

If the financial penalty is not paid

8.3. If all or any of the financial penalty is outstanding on the due date, the FSA may recover the outstanding amount as a debt owed by you and due to the FSA.

Publicity

8.4. Sections 391(4), 392(6) and 391(7) of the Act apply to the publication of information about the matter to which this Final Notice relates. Under those provisions, the FSA must publish such information about the matter to which this 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, you should contact Chris Walmsley at the FSA (direct line: 020 7066 5894/ fax: 020 7066 5895).

Tom Spender
Head of Department
Enforcement and Financial Crime Division

ANNEX A

RELEVANT STAUTORY PROVISIONS, REGULATORY REQUIREMENTS AND FSA GUIDANCE

1. Statutory provisions

1.1. The FSA's statutory objectives, set out in Section 2(2) of the Act, include the protection of consumers.

1.2. The FSA has the power, by virtue of section 66 of the Act, to impose a financial 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.

1.3. 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.

1.4. Pursuant to section 63 of the Act, the FSA has the power to withdraw the approval given to you under section 59 of the Act – to perform the significant controlled functions of CF4 Partner, CF10 Compliance Oversight and CF11 Money Laundering Reporting – if it considers that you are not a fit and proper person to perform them.

2. APER Statements of Principle for Approved Persons

2.1. APER is issued pursuant to section 64 of the Act. It sets out Statements of Principle with which approved persons are required to comply when performing a controlled function for which approval has been sought and granted. They are general statements of the fundamental obligations of approved persons under the regulatory system. APER also contains descriptions of conduct which, in the opinion of the FSA, constitutes a failure to comply with a particular Statement of Principle and describes factors which the FSA will take into account in determining whether an approved person's conduct complies with it.

2.2. APER 3.1.3G states, as guidance, 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 precise circumstances of the individual case, the characteristics of the particular controlled function and the behaviour expected in that function.

2.3. APER 3.1.4G states, as guidance, that an approved person will only be in breach of a Statement of Principle if they are personally culpable, that is in a situation where their conduct was deliberate or where their standard of conduct was below that which would be reasonable in all the circumstances.

2.4. In this case, the FSA considers the most relevant Statements of Principle to be Statement of Principle 2 and Statement of Principle 7.

2.5. Statement of Principle 2 requires that an approved person must act with due skill, care and diligence in carrying out his controlled function.

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

2.7. APER 4.2.2E to 4.2.13E provide examples of the types of behaviour that, in the opinion of the FSA, do not comply with Statement of Principle 2. These include**:**

(1) failing to inform a customer of material information in circumstance where the approved person ought to have been aware of such information and of the fact that he should provide it, including failing to explain the risks of an investment to a customer (APER 4.2.3E and 4.2.4E);

(2) recommending an investment to a customer where the approved person does not have reasonable grounds to believe that it is suitable for that customer (APER 4.2.5E); and

(3) recommending transactions without a reasonable understanding of the risk exposure of the transaction to a customer including where that recommendation is made without a reasonable understanding of the liability (either potential or actual) of the transaction (APER 4.2.6E and 4.2.7E)).

2.8. APER 4.7.2E to 4.7.10E provide examples of the types of behaviour that, in the opinion of the FSA, do not comply with Statement of Principle 7. These include:

(1) 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 the relevant firm's regulated activities (APER 4.7.3E);

(2) failing to take reasonable steps to monitor (either personally or through a compliance department or other departments) compliance with the relevant requirements and standards of the regulatory system in respect of the relevant firm's regulated activities (APER 4.7.4E); and

(3) in the case of an approved person performing a significant influence function responsible for compliance, failing to take reasonable steps to ensure that appropriate compliance systems and procedures are in place (APER 4.7.10E).

3. FSA's policy on exercising its power to impose a financial penalty

3.1. The FSA's statement of policy with respect to the imposition and amount of penalties under the Act, as required by sections 69(1), 93(1), 124(1) and 210(1) of the Act, and guidance on those matters is provided in Chapter 6 of the FSA's Decision Procedure and Penalties Manual ("DEPP"), entitled "Penalties", which is part of the FSA's Handbook. In summary, chapter 6 of DEPP states that the FSA will consider the full circumstances of each case when determining whether or not to take action for a

financial penalty, and sets out a non-exhaustive list of factors that may be relevant for this purpose.

3.2. 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.

3.3. The FSA will consider the full circumstances of each case when determining whether or not to take action for a financial penalty. DEPP6.2.1G 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) DEPP 6.2.1G(1): The nature, seriousness and impact of the suspected breach.

(2) DEPP 6.2.1G(2): The conduct of the person after the breach.

(3) DEPP 6.2.1G(3): The previous disciplinary record and compliance history of the person.

(4) DEPP 6.2.1G(4): FSA guidance and other published materials.

(5) DEPP 6.2.1G(5): Action taken by the FSA in previous similar cases.

4. Determining the level of the financial penalty

4.1. The FSA will consider all the relevant circumstances of a case when it determines the level of financial penalty. DEPP 6.5.2G sets out guidance on a non exhaustive list of factors that may be of relevance when determining the amount of a financial penalty.

4.2. 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 6.5.2(9)(d)).

5. Fit and Proper Test for Approved Persons

5.1. The part of the FSA Handbook entitled “FIT” sets out the Fit and Proper Test for Approved Persons. The purpose of FIT is to outline the main criteria for assessing the fitness and propriety of a candidate for a controlled function. FIT is also relevant in assessing the continuing fitness and propriety of an approved person.

5.2. 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 considerations will be the person's competence and capability.

5.3. As set out in FIT 2.2, in determining a person's competence and capability, the FSA will have regard to matters including but not limited to:

(1) whether the person satisfies the relevant FSA training and competence requirements in relation to the controlled function the person performs or is intended to perform; and

(2) whether the person has demonstrated by experience and training that the person is able, or will be able if approved, to perform the controlled function.

6. FSA's policy for exercising its power to make a prohibition order and withdraw a person's approval

6.1. 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").

6.2. 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.

6.3. 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.

6.4. 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.

6.5. 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, including in relation to the criteria for assessing the fitness and propriety of an approved person in terms of competence and capability as set out in FIT 2.2;

(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.

6.6. 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 serious lack of competence.

7. Conflict of interest

7.1. Statement of Principle 8 requires that a firm must manage conflicts of interest fairly, both between itself and its customer and between a customer and another client.

8. Complaints handling rules

8.1. DISP 1.3.1 R in the part of the Handbook entitled Dispute Resolution: Complaints ("DISP") requires that effective and transparent procedures for the reasonable and prompt handling of complaints must be established, implemented and maintained by the respondent.

8.2. DISP 1.4.1 R requires that once a complaint has been received by a respondent, it must

(1) investigate the complaint competently, diligently and impartially,

(2) assess fairly, consistently and promptly the subject matter of the complaint, whether the complaint should be upheld, what remedial action or redress (or both) may be appropriate and, if appropriate, whether it has reasonable grounds to be satisfied that another respondent may be solely or jointly responsible for the matter alleged in the complaint.

8.3. DISP 1.6.1 R requires that on receipt of a complaint:

(1) a respondent must send the complainant a prompt written acknowledgement providing early reassurance that it has received the complaint and is dealing with it, and

(2) ensure the complainant is kept informed thereafter of the progress of the measures being taken for the complaint's resolution.

8.4. DISP 1.6.2 R requires that the respondent must, by the end of eight weeks after its receipt of the complaint, send the complainant:

(1) a final response; or

(2) a written response which explains why it is not in a position to make a final response and indicate when it expects to be able to provide one, inform the complainant that he may now refer the complaint to the FOS, and enclose a copy of the FOS standard explanatory leaflet.

ANNEX B

9. Promotion of collective investment schemes

9.1. Section 238(1) of the Act provides that an authorised person must not communicate an invitation or inducement to participate in a collective investment scheme ("CIS"), and therefore also an UCIS. Section 21 of the Act imposes an equivalent restriction in relation to unauthorised persons.

9.2. Section 238 goes on expressly to carve out circumstances where this prohibition will not apply. These include:

(1) Where the CIS in question is an authorised unit trust/open ended investment company or a recognised scheme (s238 (4)).

(2) The Treasury may by order specify circumstances (s238 (6) - i.e. there is a statutory exemption in an order made by the Treasury - the FSMA 2000 (Promotion of Collective Investment Schemes (Exemptions) Order 2001 ("PCIS Order");

(3) The financial promotion is permitted under FSA rules exempting the promotion of UCIS under certain circumstances (s238 (5) (COBS 4.12)

9.3. The PCIS Order provides for authorised firms to promote UCIS to individuals if they fall within a particular category of exemption set out in the order.

9.4. These exemptions pertain to a certain category of individuals, for example certified high net worth individuals, certified sophisticated investors or self-certified sophisticated investors (articles 21, 23 and 23A of the PCIS Order).

10. The PCIS Order exemptions - Certified high net worth individuals

10.1. Article 21(2) defines a certified high net worth individual as being an individual who has signed a statement complying with Part I of the Schedule to the PCIS Order in the past 12 months. Essentially this requires that at least one of the following sets of circumstances apply:

(1) The person had, during the previous financial year immediately preceding the date of the statement, an annual income of £100,000 or more; and/or

(2) The person held, throughout the previous financial year immediately preceding the date of the statement, net assets to the value of £250,000 or more, not including that person's primary residence or any loan secured on that residence; that person's rights under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (a); or any benefits (in the form of pensions or otherwise) which are payable on the termination of that person's service or on that person's death or retirement and to which that person is (or that person's dependants are), or may be, entitled.

10.2. The statement also requires that the person signs a statement to indicate he accepts that he can lose his property and other assets from making investment decisions based on financial promotions and is aware it is open to him to seek specialist advice.

10.3. If the person making the communication believes on reasonable grounds that he is making it to a certified high net worth individual, then the section 238 restriction will not apply as long as the communication:

(1) is a non-real time communication or a solicited real time communication;

(2) relates only to units in a UCIS which invests wholly or predominantly in the shares in or debentures of one or more unlisted companies;

(3) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment;

(4) a specified warning in the following terms is given both orally (in respect of a real-time communication) and in writing in the manner prescribed in Article 21:

"Reliance on this promotion for the purpose of buying the units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested."; and

(5) is accompanied by an indication that the promotion is exempt from section 238 on the grounds that it is communicated to a certified high net worth individual, together with details of the requirements for certified high net worth investors and a reminder that the individual should consult a specialist if in any doubt about participating in a UCIS.

10.4. There are similar provisions for high net worth companies and associations at Article 22.

11. The PCIS Order exemptions - Sophisticated investors

11.1. There are two sorts of sophisticated investors referred to in the PCIS Order – certified and self-certified.

Certified sophisticated investors

11.2. A certified sophisticated investor is defined in Article 23(1) as someone:

(1) Who has a current certificate (signed and dated in the past three years) in writing or other legible form signed by an authorised person to the effect that he is sufficiently knowledgeable to understand the risks associated with participating in a UCIS; and

(2) Who has signed, within the previous 12 months, a statement in the following terms

"I make this statement so I can receive promotions which are exempt from the restriction on promotion of unregulated schemes in the Financial Services and Markets Act 2000. The exemption relates to certified sophisticated investors and I declare that I qualify as such. I accept that the schemes to which the promotions will relate are not authorised or recognised for the purposes of that Act. I am aware that it is open to me to seek advice from an authorised person who specialises in advising on this kind of investment."

11.3. The communication must be accompanied by an indication that section 238 does not apply, of the requirements to be a certified sophisticated investor, a prescribed risk warning and a reminder to seek independent advice.

11.4. Provided all this is met, and the communication is not to participate in a UCIS carried on by the person who certified the investor as sophisticated, then the section 238 restriction will not apply.

Self-certified sophisticated investors

11.5. Article 23A defines a self-certified sophisticated investor as an individual who has signed a statement complying with Part II of the Schedule to the PCIS Order in the past 12 months. Essentially this requires that at least one of the following sets of circumstances applies to the investor:

(1) He is a member of a network or syndicate of "business angels" and has been so for at least the last six months;

(2) He has made more than one investment in an unlisted company in the past two years;

(3) He is working, or has worked in the past two years, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;

(4) He is currently, or has been in the two years before signing the statement, a director of a company with an annual turnover of at least £1 million.

11.6. As with high net worth individuals, the statement also requires the investor to sign a statement that he accepts he can lose his property and assets from making investment decisions based on financial promotions and that he is aware that it is open to him to seek specialist advice.

11.7. If the person making the communication believes on reasonable grounds that he is making it to a self-certified sophisticated investor, then the section 238 restriction will not apply as long as the communication:

(1) relates only to units in a UCIS which invests wholly or predominantly in the shares in or debentures of one or more unlisted companies;

(2) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment;

(3) a specified warning in the following terms is given both orally (in respect of real time communications) and in writing in the manner prescribed in Article 23A:

"Reliance on this promotion for the purpose of buying the units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested."; and

(4) is accompanied by an indication that the promotion is exempt from section 238 on the ground that it is made to a self-certified sophisticated investor, together with details of the requirements for self-certified sophisticated investors and a reminder that the individual should consult a specialist if in any doubt about participating in a UCIS.

12. The COBS exemptions

12.1. A firm may communicate an invitation or inducement to participate in a UCIS without breaching the section 238 restriction if the promotion falls within an exemption listed in the table at 4.12.1R(4) of the Conduct of Business Sourcebook (COBS).

12.2. The inducement or invitation must be made only to recipients whom the firm has taken reasonable steps to establish are persons in that category or be directed at recipients in such a way as to reduce, as far as possible, the risk of participation in the CIS by persons not in that category. There is no provision for these steps to be taken retrospectively.

12.3. Category 1 covers people who are already participants in a UCIS or have been so in the last 30 months. An authorised person can promote to these persons the UCIS in which they are already participants (and any successor scheme) or one whose underlying property and risk profile are both "substantially similar" to those of the UCIS in which they participate.

12.4. Category 2 deals with those persons for whom the firm has taken reasonable steps to ensure that investment in the UCIS is suitable and who is a client of the firm or a company in its group.

12.5. Category 7 provides that if a client is categorised as a professional client or eligible counterparty then an authorised person can promote to that client any UCIS in relation to which the client is so categorised.

12.6. Category 8 allows financial promotion of UCIS to a person:

(1) In relation to whom the firm has undertaken an adequate assessment of his expertise, experience and knowledge and that assessment gives reasonable assurance, in light of the nature of the transactions or services envisaged, that the person is capable of making his own investment decisions and understanding the risks involved;

(2) To whom the firm has given a clear written warning that this will enable the firm to promote UCIS to the client; and

(3) Who has stated in writing, in a document separate from the contract, that he is aware of the fact the firm can promote certain UCIS to him.

13. Suitability of advice

13.1. The fact that a customer is eligible to receive a communication promoting a UCIS under one or more exemptions does not mean that UCIS will be automatically suitable to that customer.

13.2. Principle 9 of the FSA's Principles for Businesses states 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.

13.3. In considering the suitability of a particular scheme for a specific client, a firm is required by COBS 9 to obtain the necessary information to understand the essential facts about the client (COBS 9.2.2R).

13.4. COBS 9.2.6R provides that if a firm does not obtain the necessary information to assess suitability, it must not make a personal recommendation to the client.