Financial Services Authority

FINAL NOTICE

To: **Mr Richard Anthony Holmes**

Of: **14 Falmouth Avenue**
Highams Park
London
E4 9QR

Individual Reference Number: **RAH01211**

Dated: **1 July 2009**

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

1. THE PENALTY

1.1. The FSA gave you, Richard Anthony Holmes, a Decision Notice on [ ] June 2009 ("the Decision Notice") which notified you that, for the reasons set out below and pursuant to section 66 of the Financial Services and Markets Act 2000 ("the Act"), the FSA had decided to impose a financial penalty of £20,020 on you, in respect of breaches of Principles 6 and 7 of the FSA's Statement of Principles for Approved Persons ("APER").

1.2. You agreed to settle at an early stage of the FSA's inquiries and you therefore qualified for a 30% (Stage 1) reduction of the financial penalty under the FSA's executive settlement procedures. The FSA would have otherwise sought to impose a financial penalty of £28,600 on you.

2. REASONS FOR THE ACTION

Summary

2.1 On the basis of the facts and matters summarised below, the FSA is proposing to impose a financial penalty on you for breaches of Principles 6 and 7 of APER in your capacity as holder of Controlled Function 1 (Director) ("CF1") at AIF Limited ("AIF"). In addition to holding CF1, you also hold the following controlled functions at AIF: CF28 (Systems and Controls), CF29 (Significant Management) and you are also responsible for insurance mediation activities.

2.2 The breaches identified in this Notice concern your personal culpability in causing AIF to breach the regulatory requirements relating to the appointment and monitoring of an Appointed Representative (the "AR"). In particular, you failed to carry out the appropriate checks on the AR to determine its suitability and subsequently failed to monitor adequately the activities of the AR following its appointment. You later became aware that the AR had taken clients' premiums and that it had failed to pass these on to the relevant insurer, leaving clients uninsured or at risk of being uninsured.

2.3 You have breached Principle 6 of APER in that you failed to exercise due skill, care and diligence in managing the affairs of AIF for which you were responsible. In particular, you took a personal decision to appoint the AR based on inadequate information. You failed to carry out a detailed assessment to determine whether the AR was solvent, otherwise fit and proper, and suitable to act on behalf of AIF, causing AIF's non-compliance with the rules and guidance set out in Chapter 12.4 in the Supervision Manual ("SUP"), part of the FSA's Handbook of rules and guidance (the "FSA Handbook").

2.4 You have breached Principle 7 of APER in that you failed to take reasonable steps to ensure that the business of AIF, for which you were responsible, complied with the relevant requirements and standards of the regulatory system. In particular, you failed to take reasonable steps to monitor the activities of the AR to ensure its compliance with regulatory requirements. Furthermore, you failed to address regulatory breaches promptly once you had become aware of them, including the AR's failure to pass on client premiums promptly, or take steps to mitigate the risk of further breaches occurring, causing AIF to not satisfy the rules and guidance set out in SUP 12.6.

2.5 Your failings are viewed by the FSA as serious because:

(1) you operate independently of the other director at AIF and you have confirmed that you were personally responsible for the appointment and monitoring of the AR. The FSA places a great deal of emphasis on the responsibilities of senior management as it is senior managers who are responsible for the standards and conduct of the businesses they run;

(2) you failed to monitor adequately the activities of the AR over a period of almost a year and despite identifying a number of concerns early on during the AR agreement, including failure to pass on client premiums promptly, you failed to

act swiftly to rectify the breaches and later failed to increase your level of monitoring of the AR;

(3) you have acknowledged that AIF did not have the resources, and you personally did not have the expertise to monitor any AR. You have confirmed that regular reporting did not take place and that you were reliant on the AR to raise specific issues with you. You have also confirmed that you were dependent on the AR to comply with regulatory requirements;

(4) prior to the AR's appointment, at no stage did you meet with two of the three directors of the AR or carry out a formal assessment of their ability to act as the senior management of the AR. You relied solely on verbal assurances provided to you by two business associates of the directors, individuals who you soon after discovered had been prohibited by the FSA;

(5) you failed to identify that by 24 July 2007, all three of the AR's directors had resigned and that there was no governing body up until the AR agreement was terminated on 21 September 2007; and

(6) your conduct was well below the standard which would have been reasonable in all the circumstances at the time of the conduct concerned.

2.6 The FSA notes that once you became aware that the AR had failed to pass on client premiums, potentially leaving clients uninsured, you, acting on behalf of AIF, did take steps to identify the clients affected and ensured either that the 276 clients remained on cover, or that alternative insurance was arranged, both at a cost to AIF.

2.7 The FSA has taken into account the following considerations, which are regarded as mitigating factors:

(1) the FSA does not consider that you deliberately contravened the requirements in APER;

(2) you have co-operated with the FSA's enquiries and accepted the failings set out in this Notice;

(3) you have terminated AIF's AR agreement with its remaining Appointed Representative, and will vary AIF's permission so as to be subject to a restriction that it may not appoint any further ARs; and

(4) the remedial steps you, acting on behalf of AIF, have taken to ensure that clients were not left uninsured and that their interests were protected.

2.8 The relevant statutory provisions, rules and guidance are set out in the Annex to this Final Notice.

3. FACTS AND MATTERS RELIED ON

Background

3.1 AIF became authorised by the FSA on 14 January 2005 to conduct insurance mediation business. On the same date, you became an approved person, along with another director, and you are currently approved to perform the controlled functions set out in paragraph 2.1 above.

3.2 On 10 November 2006, the FSA registered the AR as an Appointed Representative of AIF, as referred to in more detail below in this section.

3.3 On 14 June 2007, the FSA registered another Appointed Representative of AIF. AIF later terminated the Appointed Representative agreement and the FSA withdrew the Appointed Representative's status on 24 April 2009.

Conduct in issue

Appointment of the AR

3.4 In June 2006 you were approached directly by two business contacts regarding the possibility of the AR acting on behalf of AIF. You have confirmed that you had personally dealt with both individuals in relation to insurance matters over the past ten years and without any undue concern and as such you did not consider it necessary to carry out a detailed assessment of the AR or its staff's suitability prior to the AR's appointment.

3.5 You have confirmed that you relied solely on the verbal references and assurances provided by your business contacts for the AR's staff, including the AR's three directors. You have also stated that given your previous dealings with the staff from a company associated with the AR (who would be transferring to the AR), you were satisfied that they had the appropriate general and professional knowledge and did not consider it necessary to assess their competence or fitness and propriety.

3.6 You have since confirmed to the FSA that you had never met with two of the putative directors of the AR, and you later became aware that one of the directors permanently resides in Malaysia.

3.7 You have told the FSA that prior to the AR's appointment, you considered the AR's un-audited financial statements for the period ended 31 March 2006. Your view was that whilst the AR's balance sheet for the period ended 31 March 2006, which stated that it had started trading on 3 January 2006, showed net liabilities of £19,732, you viewed this as a small deficit, insignificant and unsurprising in a new business. Despite being aware that the AR was balance sheet insolvent after only three months trading, and thereby not meeting the FSA's minimum requirements to become an appointed representative, this did not affect your decision to appoint the AR.

3.8 In November 2006, you became aware that client money had been used to operate the business of a company associated with the AR and insurance premiums had not been correctly passed on to an insurance underwriter.

3.9 On 7 November 2006, you submitted a notification form to the FSA to appoint the AR. The form was signed and dated by you on 1 November. On the form you stated that the Appointed Representative agreement between AIF and the AR had commenced on 1 September 2006. The FSA subsequently registered the AR on 10 November 2006.

3.10 You later provided the FSA with a copy of the agreement between the AR and AIF, which was only apparently signed on 1 November 2007 by you, on behalf of AIF, and on 6 November 2007 by a director of the AR, despite the AR having commenced acting on behalf of AIF on or around 1 September 2006. Given that from 24 July 2007 there were no longer any directors at the AR and its status as an AR was terminated on 21 September 2007, the FSA has concerns about whether the AR agreement you provided to the FSA is genuine.

3.11 You became aware in November 2006 that the FSA had taken enforcement action against the two business contacts through whom you had been introduced to the AR and the company associated with these individuals from which the AR had taken some staff. Despite becoming aware of serious misconduct by the two business contacts, you continued to rely solely on the verbal references previously provided by these individuals in determining the suitability of the AR's staff and you took no specific steps to ensure that the AR was not being managed by those individuals. You still did not consider it necessary to make any further checks even though the staff and structure of the AR would effectively be the same as those of the firm with which it had been associated.

Monitoring of the AR

3.12 In or around February 2007, you became aware that a general insurer had offered the AR a facility to enable it to place tenant's contents insurance on a block cover basis. This enabled the AR to effectively issue policies without the involvement or approval of AIF. Despite becoming aware that the AR was carrying out insurance mediation activities on behalf of another counterparty, which was a breach of the terms of the AR agreement, you did not take steps at the time to prevent the AR from doing so or increase your level of monitoring of the AR.

3.13 In mid February 2007, you spoke to the insurance underwriter who had arranged this facility to determine whether the facility was being handled correctly. You were advised by the underwriter that the AR had declarations and premiums outstanding, but you later received and relied on assurances from the AR that the premiums had been brought up-to-date. You have told the FSA that you subsequently questioned the AR on a regular basis regarding the facility, although the FSA has seen no evidence that detailed enquiries were made by you and it appears that you simply accepted the AR's assurances that everything was in order. Although these issues should have prompted you to increase your level of monitoring of the AR, you did not do so.

3.14 You have stated to the FSA that the AR had also experienced problems paying insurance premiums promptly to AIF, for onward payment to the relevant insurer, in or around April 2007. You have also stated to the FSA that during the last six months of the AR agreement, the AR had persistently failed to pass client premiums to AIF

promptly and you subsequently refused to arrange insurance without payment in advance. Despite these problems occurring over a period of several months and given its previous association with a firm who failed to pass on insurance premiums, this did not lead to increased monitoring by you or further investigation into the way in which the AR was conducting its business.

3.15 You initially confirmed you communicated with the AR by telephone on a daily basis regarding administrative matters, but only attended the AR's offices on three occasions to formally discuss the running of the business and compliance issues. You later stated that you attended the AR's offices at regular intervals of four to six weeks, although you have not provided the FSA with any evidence to demonstrate this. You have confirmed to the FSA that you relied on specific issues being raised by the AR rather than having monitoring systems in place, including regular reporting. Furthermore, you have also confirmed that you did not conduct any quality assurance on the AR's activities and relied on the personnel within the AR to carry out that function and ensure compliance with regulatory standards. You have also confirmed to the FSA that AIF did not have sufficient resources to provide any training for the AR's staff and the FSA has seen no evidence that training and competence was assessed on a regular basis, or at all.

3.16 You have informed the FSA that an arrangement was in place whereby the AR was supposed to pay all premiums into a designated client account, but you later suspected that premiums were being paid directly into the AR's own business bank account. The FSA has not received any documentary evidence that the AR held a statutory trust account or that you made regular requests for bank statements or regularly monitored the handling of client monies in any way, despite there being an ongoing regulatory obligation on AIF to do so.

3.17 Following a complaint made by a client of the AR in September 2007, regarding its failure to put insurance in place, you, acting on behalf of AIF, terminated the AR's status as an Appointed Representative of AIF on 21 September 2007. You subsequently became aware that the AR had received clients' premiums but failed to pass them onto the underwriter, leaving the clients uninsured. In addition, the AR had also instructed AIF to arrange insurance policies on behalf of clients but had failed to pass on the client premiums to AIF. The FSA is satisfied that you subsequently ensured that AIF took steps to arrange alternative insurance for the clients known to AIF who had been left uninsured and also ensured that cover was maintained where AIF had already provided instructions to the insurer, at a total direct cost of approximately £38,000. You have confirmed that the cost to AIF of ensuring clients remained on cover was reduced to approximately £27,000, after offsetting commission otherwise payable to the AR but which AIF had retained. You identified that a total of 276 clients were affected.

4. CONCLUSIONS

4.1 The facts and matters described above lead the FSA, having regard to its regulatory objectives which include the protection of consumers and market confidence, to conclude that you have failed to satisfy Principles 6 and 7 of APER. Specifically, you failed to exercise due skill, care and diligence in managing the affairs of AIF, for which you were responsible as a senior manager, in that:

(1) you took a personal decision to appoint the AR based on inadequate information. You failed to conduct a detailed assessment to determine whether the AR was solvent and otherwise fit and proper, and suitable to act on behalf of AIF;

(2) you failed to take reasonable steps to ensure that the business of AIF complied with the requirements and standards of the regulatory system, and

(3) you failed to monitor the activities of the AR and address its regulatory breaches promptly when they arose. You have acknowledged that there were no monitoring systems in place, including any regular reporting, which could have assisted you in detecting and preventing the AR's serious misconduct. This is particularly serious as you hold the controlled function CF28 (Systems and Controls). You also relied on the AR's staff to ensure that regulatory requirements were being met. It therefore appears that you were over reliant on the AR and the FSA considers that your conduct was reckless.

Analysis of the sanction

4.2 The FSA's policy on the imposition of financial penalties as at the date of this Notice is set out in Chapter 6 of the Decision Procedures and Penalties Manual ("DEPP"), which forms part of the FSA Handbook. The relevant sections of DEPP are set out in more detail in the Annex to this Notice.

4.3 In determining the appropriate level of financial penalty the FSA has also had regard to Chapter 7 of the Enforcement Guide ("EG"), the part of the FSA's Handbook setting out the FSA's policy on the imposition of financial penalties. The FSA has also had regard to Chapter 13 of the Enforcement Manual ("ENF"), which was in force until 27 August 2007, and therefore effective during the time of the conduct described above in this Notice.

4.4 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).

4.5 The FSA will consider the full circumstances of each case when determining whether or not to impose a financial penalty. DEPP 6.5.2G sets out guidance on a non-exhaustive list of factors that may be of relevance in determining the level of a financial penalty. The factors include:

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

4.6 Your failings left a number of clients uninsured or at risk of being uninsured. The loss or risk of loss to clients was subsequently remedied by the steps that you took on behalf of AIF.

4.7 However, the FSA has considered the serious nature and long duration of the breaches which could have resulted in serious consumer detriment had a large number of claims been made or if AIF had not been able to afford the cost of taking remedial action.

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

4.8 Whilst the FSA does not consider that you deliberately contravened regulatory requirements, it considers that your conduct was reckless and fell well below what would have been considered reasonable in all the circumstances.

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

4.9 In determining the level of the financial penalty to be imposed on you, the FSA has taken into account that your resources are limited compared to those of a body corporate and that any penalty would potentially have a greater impact on you. However, the FSA has also had regard to your position and responsibilities at AIF and believes that the breaches are serious and the level of the financial penalty reflects this.

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

4.10 The FSA has assessed your financial position and considered your ability to pay the financial penalty. The FSA's view is that the penalty is proportionate to the seriousness of the breach and you have indicated that you are able to pay the penalty.

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

4.11 The FSA has taken into consideration the financial benefit AIF, and ultimately Mr Holmes as a director of AIF, gained as a result of the breach, in particular commission AIF would have received from insurers as a result of business introduced by the AR.

DEPP 6.5.2G(8): Conduct following the breach

4.12 The FSA has taken into account your co-operation with the FSA's inquiries and your willingness to take all reasonable steps to ensure that clients interests were not adversely affected and your willingness to satisfy the FSA that regulatory requirements will be met in the future. You have also voluntarily agreed that AIF will be subject to a restriction whereby it will not be permitted to appoint any further ARs.

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

4.13 The FSA has taken into account the fact that you have not been the subject of previous disciplinary action by the FSA.

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

4.14 The FSA has also had regard to the penalties imposed on other approved persons for similar and more serious conduct and also previous cases where Private Warnings were given to approved persons for less serious conduct.

4.15 The FSA, having regard to all the circumstances, considers the appropriate level of financial penalty to be £20,020, after a 30% discount for early settlement.

5. DECISION MAKERS

The decision which gave rise to the obligation to give this Final Notice was made by the Settlement Decision Makers on behalf of the FSA.

6. IMPORTANT

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

Manner of and time for payment

6.2 The financial penalty must be paid in full by you to the FSA by no later than 29 July 2009, 28 days from the date of this Final Notice.

If the financial penalty is not paid

6.3 If all or any of the financial penalty is outstanding on 30 July 2009, the FSA may recover the outstanding amount as a debt owed by you and due to the FSA.

Publicity

6.3 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.

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

FSA contacts

6.5 For more information concerning this matter generally, you should contact Lehong Mac at the FSA (direct line: 020 7066 5742, or fax: 020 7066 5743).

Jonathan Phelan
Head of Department
FSA Enforcement Division

ANNEX TO THE FINAL NOTICE ISSUED BY THE FINANCIAL SERVICES AUTHORITY TO RICHARD ANTHONY HOLMES ON 1 JULY 2009

Relevant Statutory Provisions

1. The FSA's statutory objectives, as set out in Section 2(2) of the Act include market confidence, public awareness, the protection of consumers and the reduction of financial crime.

2. Section 66 of the Act provides that:

> "(1) The Authority may take action against a person under this section if –
>
> (a) it appears to the Authority that he is guilty of misconduct; and
>
> (b) the Authority is satisfied that it is appropriate in the circumstances to take action against him.
>
> (2) A person is guilty of misconduct if, while an approved person -
>
> (a) he has failed to comply with a statement of principle issued under section 64…
>
> (3) If the Authority is entitled to take action under this section against any person, it may –
>
> (a) impose a penalty on him of such amount as it considers appropriate; or
>
> (b) publish a statement of his misconduct."

Other relevant regulatory provisions

3. In exercising its power to impose a financial penalty, the FSA must have regard to the FSA Handbook. The Principles and guidance which the FSA considers relevant are set out below.

Relevant Statements of Principles and Code of Practice for Approved Persons

Statement of Principle 6

4. Statement of Principle 6 in APER states that "*an approved person performing a significant influence function must exercise due skill, care and diligence in managing the business of the firm for which he is responsible in his controlled function*".

5. APER 4.6.2E states that:

"*In the opinion of the FSA, conduct of the type described in APER 4.6.3 E, APER 4.6.5 E, APER 4.6.6 E or APER 4.6.8 E does not comply with Statement of Principle 6 (APER 2.1.2 P).*"

6. APER 4.6.3E states that:

"*Failing to take reasonable steps to adequately inform himself about the affairs of the business for which he is responsible falls within APER 4.6.2E.*"

7. APER 4.6.4E states that:

"*Behaviour of the type referred to in APER 4.6.3 E includes, but is not limited to:*

(1) permitting transactions without a sufficient understanding of the risks involved;

(2) permitting expansion of the business without reasonably assessing the potential risks of that expansion;

(3) inadequately monitoring highly profitable transactions or business practices or unusual transactions or business practices;

(4) accepting implausible or unsatisfactory explanations from subordinates without testing the veracity of those explanations;"

8. APER 4.6.5E states that:

"*Delegating the authority for dealing with an issue or a part of the business to an individual or individuals (whether in-house or outside contractors) without reasonable grounds for believing that the delegate had the necessary capacity, competence, knowledge, seniority or skill to deal with the issue or to take authority for dealing with part of the business, falls within APER 4.6.2E (see APER 4.6.13 G).*"

9. APER 4.6.6E states that:

"*Failing to take reasonable steps to maintain an appropriate level of understanding about an issue or part of the business that he has delegated to an individual or individuals (whether in-house or outside contractors) falls within APER 4.6.2E (see APER 4.6.14G).*"

10. APER 4.6.7E states that:

"*Behaviour of the type referred to in APER 4.6.6 E includes but is not limited to:*

(1) disregarding an issue or part of the business once it has been delegated;

(2) failing to require adequate reports once the resolution of an issue or management of part of the business has been delegated;

(3) accepting implausible or unsatisfactory explanations from delegates without testing their veracity."

11. APER 4.6.8E states that:

"*Failing to supervise and monitor adequately the individual or individuals (whether in-house or outside contractors) to whom responsibility for dealing with an issue or authority for dealing with a part of the business has been delegated falls within APER 4.6.2E*."

12. APER 4.6.12G(1) states that:

"(1) *It is important for the approved person performing a significant influence function to understand the business for which he is responsible (APER 4.6.4 E). An approved person performing a significant influence function is unlikely to be an expert in all aspects of a complex financial services business. However, he should understand and inform himself about the business sufficiently to understand the risks of its trading, credit or other business activities.*

(2) *It is important for an approved person performing a significant influence function to understand the risks of expanding the business into new areas and, before approving the expansion, he should investigate and satisfy himself, on reasonable grounds, about the risks, if any, to the business.*"

13. APER 4.6.14G states that:

"*Although an approved person performing a significant influence function may delegate the resolution of an issue, or authority for dealing with a part of the business, he cannot delegate responsibility for it. It is his responsibility to ensure that he receives reports on progress and questions those reports where appropriate. For instance, if progress appears to be slow or if the issue is not being resolved satisfactorily, then the approved person performing a significant influence function may need to challenge the explanations he receives and take action himself to resolve the problem. This may include increasing the resource applied to it, reassigning the resolution internally or obtaining external advice or assistance. Where an issue raises significant concerns, an approved person performing a significant influence function should act clearly and decisively. If appropriate, this may be by suspending members of staff or relieving them of all or part of their responsibilities (see APER 4.6.6 E).*"

Statement of Principle 7

14. Statement of Principle 7 in APER states 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*".

15. APER 4.7.4E states that:

> "*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 its regulated activities falls within APER 4.7.2E (see APER 4.7.12G).*"

16. APER 4.7.7E states that:

> "*Failing to take reasonable steps to ensure that procedures and systems of control are reviewed and, if appropriate, improved, following the identification of significant breaches (whether suspected or actual) of the relevant requirements and standards of the regulatory system relating to its regulated activities, falls within APER 4.7.2 E (see APER 4.7.13 G).*"

17. APER 4.7.8E states that:

> "*Behaviour of the type referred to in APER 4.7.7 E includes, but is not limited to:*
>
> *(1) unreasonably failing to implement recommendations for improvements in systems and procedures;*
>
> *(2) unreasonably failing to implement recommendations for improvements to systems and procedures in a timely manner*."

18. APER 4.7.10E states that:

> "*In the case of an approved person performing a significant influence function responsible for compliance under SYSC 3.2.8 R, failing to take reasonable steps to ensure that appropriate compliance systems and procedures are in place falls within APER 4.7.2 E (see APER 4.7.14 G).*"

19. APER 4.7.11G states that:

> "*The FSA expects an approved person performing a significant influence function to take reasonable steps both to ensure his firm's compliance with the relevant requirements and standards of the regulatory system and to ensure that all staff are aware of the need for compliance*."

20. APER 4.7.13G states that:

> "*Where the approved person performing a significant influence function becomes aware of actual or suspected problems that involve possible breaches of relevant requirements and standards of the regulatory system falling within his area of responsibility, then he should take reasonable steps to ensure that they are dealt*

with in a timely and appropriate manner (APER 4.7.7 E). This may involve an adequate investigation to find out what systems or procedures may have failed and why. He may need to obtain expert opinion on the adequacy and efficacy of the systems and procedures."

The Supervision Manual ("SUP")

21. SUP 12.3.2G states that the firm is responsible, to the same extent as if it had expressly permitted it, for anything the AR does or omits to do, in carrying on the business for which the firm has accepted responsibility.

22. SUP 12.4.2R states that before a firm appoints an AR, and on a continuing basis, it must establish on reasonable grounds that: the appointment does not prevent the firm from satisfying the threshold conditions, the AR is solvent and otherwise suitable to act for the firm in that capacity.

23. SUP 12.4.2R(3) states that the firm should have adequate controls over the AR's regulated activities for which the firm has responsibility and adequate resources to monitor and enforce compliance by the AR with the relevant regulatory requirements.

24. SUP 12.4.4G specifies that in assessing whether an AR is suitable to act for the firm in that capacity, the principal firm should consider whether the AR is fit and proper and also consider the fitness and propriety (including good character and competence) and financial standing of the controllers, directors, partners, proprietors and managers of the AR. SUP 12.4.4G(2) further states that the information which firms should take reasonable steps to obtain and verify is set out in the Fit and Proper Test for Approved Persons ("FIT").

25. SUP 12.4.8AR states that before a firm appoints an AR to carry on insurance mediation activity, it must in relation to the insurance mediation activity ensure that the person will comply on appointment, and continue to comply, with the provisions of FSA Rules 2.3.1 and 2.3.3 in the Prudential Sourcebook for Mortgage and Home Finance Firms, and Insurance Intermediaries ("MIPRU"). MIPRU 2.3.1R and MIPRU 2.3.3R set out that a firm must establish on reasonable grounds that persons involved in insurance mediation activity demonstrate the knowledge and ability necessary for the performance of their duties and are of good repute.

26. SUP 12.6.1R(1) states that if a firm has reasonable grounds to believe that the conditions in SUP 12.4.2R, SUP 12.4.6R or SUP 12.4.8AR (as applicable) are not satisfied, or are likely not to be satisfied, in relation to any of its ARs, the firm must take immediate steps to rectify the matter.

27. SUP 12.6.5R(2)(b) states that the firm must take reasonable steps to ensure that if client money is received by the AR, it is paid into a client bank account of the firm, or forwarded to the firm, in accordance with the rules set out in the Client Assets Sourcebook ("CASS").

The Enforcement Guide ("EG")

28. The FSA's policy in relation to exercising its power to impose a financial penalty on an approved person is set out in EG.

29. EG 7.1 explains the purpose of imposing financial penalties on approved persons in relation to the FSA's regulatory objectives. In particular, EG 7.1 states that imposing financial penalties shows that the FSA is upholding regulatory standards and helps to maintain market confidence, promote public awareness or regulatory standards and deter financial crime. An increased public awareness of regulatory standards also contributes to the protection of consumers.

30. EG 7.2(2)(a) states that the FSA has the power to impose a financial penalty on an approved person, under section 66 of the Act.

31. EG 7.4 states that the FSA's statement of policy in relation to the imposition of financial penalties is set out in DEPP 6.2 (Deciding whether to take action), DEPP 6.3 (Penalties for market abuse) and DEPP 6.4 (Financial penalty or public censure).

Decision Procedure and Penalties Manual ("DEPP")

32. DEPP 6.2 sets out the considerations taken into account by the FSA in deciding whether to impose a financial penalty.

33. DEPP 6.2.1G states that the FSA will consider the full circumstances of each case when determining whether or not to take action for a financial penalty or public censure, including:

    (1) The nature, seriousness and impact of the suspected breach, including:

        (a) whether the breach was deliberate or reckless;

        (b) the duration and frequency of the breach;

        …….

        (f) the loss or risk of loss caused to consumers or other market users;

        (g) the nature and extent of any financial crime facilitated, occasioned or otherwise attributable to the breach;

        ……

    (5) Action taken by the FSA in previous similar cases.

34. DEPP 6.2.4G states that the primary responsibility for ensuring compliance with a firm's regulatory obligations rests with the firm itself. However, the FSA may take disciplinary action against an approved person where there is evidence of personal culpability on the part of that approved person. Personal culpability arises where the behaviour was deliberate or where the approved person's standard of behaviour was

below that which would be reasonable in all the circumstances at the time of the conduct concerned.

35. DEPP 6.2.5G states that in some cases it may not be appropriate to take disciplinary measures against a firm for the actions of an approved person (an example might be where the firm can show that it took all reasonable steps to prevent the breach). In other cases, it may be appropriate for the FSA to take action against both the firm and the approved person. For example, a firm may have breached the rule requiring it to take reasonable care to establish and maintain such systems and controls as are appropriate to its business (SYSC 3.1.1 R or SYSC 4.1.10 R), and an approved person may have taken advantage of those deficiencies to front run orders or misappropriate assets.

36. DEPP 6.2.6G states that there are some additional considerations that may be relevant when deciding whether to take action against an approved person pursuant to section 66 of the Act:

    (1) The approved person's position and responsibilities. The FSA may take into account the responsibility of those exercising significant influence functions in the firm for the conduct of the firm. The more senior the approved person responsible for the misconduct, the more seriously the FSA is likely to view the misconduct, and therefore the more likely it is to take action against the approved person.

    (3) Whether disciplinary action would be a proportionate response to the nature and seriousness of the breach by the approved person.

37. DEPP 6.2.7G states that the FSA will not discipline approved persons on the basis of vicarious liability (that is, holding them responsible for the acts of others), provided appropriate delegation and supervision has taken place (see APER 4.6.13 G and APER 4.6.14 G). In particular, disciplinary action will not be taken against an approved person performing a significant influence function simply because a regulatory failure has occurred in an area of business for which he is responsible. The FSA will consider that an approved person performing a significant influence function may have breached Statements of Principle 5 to 7 only if his conduct was below the standard which would be reasonable in all the circumstances at the time of the conduct concerned (see also APER 3.1.8 G).

38. DEPP 6.5 sets out the FSA's policy in determining the appropriate level of financial penalty.

39. DEPP 6.5.2G states that the following factors may be relevant to determining the appropriate level of financial penalty to be imposed on a person under the Act:

    (1) *Deterrence*

When determining the appropriate level of penalty, the FSA will have regard to the principal purpose for which it imposes sanctions, namely to promote high standards of regulatory and/or market conduct by deterring persons who have committed breaches from committing further breaches and helping to deter other persons from committing similar breaches, as well as demonstrating generally the benefits of compliant business.

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

The FSA will consider the seriousness of the breach in relation to the nature of the rule, requirement or provision breached. The following considerations are among those that may be relevant:

(a) the duration and frequency of the breach;

(d) the loss or risk of loss caused to consumers, investors or other market users;

(e) the nature and extent of any financial crime facilitated, occasioned or otherwise attributable to the breach.

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

The FSA will regard as more serious a breach which is deliberately or recklessly committed. The matters to which the FSA may have regard in determining whether a breach was deliberate or reckless include, but are not limited to, the following:

(b) where the person has not followed a firm's internal procedures and/or FSA guidance, the reasons for not doing so;

(c) where the person has taken decisions beyond its or his field of competence, the reasons for the decisions and for them being taken by that person.

If the FSA decides that the breach was deliberate or reckless, it is more likely to impose a higher penalty on a person than would otherwise be the case.

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

When determining the amount of a penalty to be imposed on an individual, the FSA will take into account that individuals will not always have the resources of 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 on a body corporate. The FSA will also consider 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.

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

(a) The FSA may take into account whether there is verifiable evidence of serious financial hardship or financial difficulties if the person were to pay the level of penalty appropriate for the particular breach. The FSA regards these factors as matters to be taken into account in determining the level of a penalty, but not to the extent that there is a direct correlation between those factors and the level of penalty.

(b) The purpose of a penalty is not to render a person insolvent or to threaten the person's solvency. Where this would be a material consideration, the FSA will consider, having regard to all other factors, whether a lower penalty would be appropriate. This is most likely to be relevant to a person with lower financial resources; but if a person reduces its solvency with the purpose of reducing its ability to pay a financial penalty, for example by transferring assets to third parties, the FSA will take account of those assets when determining the amount of a penalty.

(c) The degree of seriousness of a breach may be linked to the size of the firm. For example, a systemic failure in a large firm could damage or threaten to damage a much larger number of consumers or investors than would be the case with a small firm: breaches in firms with a high volume of business over a protracted period may be more serious than breaches over similar periods in firms with a smaller volume of business.

(d) The size and resources of a person may also be relevant in relation to mitigation, in particular what steps the person took after the breach had been identified; the FSA will take into account what it is reasonable to expect from a person in relation to its size and resources, and factors such as what proportion of a person's resources were used to resolve a problem.

(8) *Conduct following the breach*

The FSA may take the following factors into account:

(a) the conduct of the person in bringing (or failing to bring) quickly, effectively and completely the breach to the FSA's attention (or the attention of other regulatory authorities, where relevant);

(b) the degree of co-operation the person showed. Where a person has fully co-operated with the FSA's enquiries, this will be a factor tending to reduce the level of financial penalty;

(c) any remedial steps taken since the breach was identified, including whether these were taken on the person's own initiative or that of the

FSA or another regulatory authority; for example, identifying whether consumers or investors or other market users suffered loss and compensating them where they have; correcting any misleading statement or impression; taking disciplinary action against staff involved (if appropriate); and taking steps to ensure that similar problems cannot arise in the future.

(10) *Other action taken by the FSA (or a previous regulator)*

Action that the FSA (or a previous regulator) has taken in relation to similar breaches by other persons may be taken into account. This includes previous actions in which the FSA (whether acting by the RDC or the settlement decision makers) and a person on whom a penalty is to be imposed have reached agreement as to the amount of the penalty. As stated at DEPP 6.5.1 G (2), the FSA does not operate a tariff system. However, the FSA will seek to apply a consistent approach to determining the appropriate level of penalty.

(12) *FSA guidance and other published materials*

(a) A person does not commit a breach by not following FSA guidance or other published examples of compliant behaviour. However, where a breach has otherwise been established, the fact that guidance or other published materials had raised relevant concerns may inform the seriousness with which the breach is to be regarded by the FSA when determining the level of penalty.

(b) The FSA will consider the nature and accessibility of the guidance or other published materials when deciding whether they are relevant to the level of penalty and, if they are, what weight to give them in relation to other relevant factors.

(13) *The timing of any agreement as to the amount of the penalty*

The FSA and the person on whom a penalty is to be imposed may seek to agree the amount of any financial penalty and other terms. In recognition of the benefits of such agreements, DEPP 6.7 provides that the amount of the penalty which might otherwise have been payable will be reduced to reflect the stage at which the FSA and the person concerned reach an agreement.

40. In deciding to take this action, the FSA has also had regard to the guidance set out in sections 11.4 and 11.5, and Chapter 13 of the FSA's Enforcement Manual ("ENF"), which is part of the FSA's Handbook and which was in effect during the period of your relevant conduct.

41. ENF 1.3.1(2)G states that the FSA will seek to exercise its enforcement powers in a manner that is transparent, proportionate and consistent with its publicly stated policies. The criteria for determining whether to take disciplinary action are set out in ENF 11.4.1G and ENF 11.5G. ENF 11.4.1G states that the FSA will consider the full facts of each case and that the criteria listed are not exhaustive. In particular, ENF 11.5.3G states that the FSA will only take disciplinary action against an approved

person where there is evidence of personal culpability on his part, which arises where his behaviour, amongst others, fell below that which would be reasonable in all the circumstances.

END OF ANNEX