
FINAL NOTICE

To: Royal Liver Assurance Limited

Of: Pier Head
Liverpool
Merseyside
L3 1HT

Date: 6 April 2006

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

1. THE PENALTY

1.1. The FSA gave Royal Liver Assurance Limited (RLA) a decision notice dated 5 April 2006 which notified RLA that pursuant to section 206 of the Financial Services and Markets Act 2000 (the Act) the FSA had decided to impose a financial penalty of £550,000 ("the penalty") on RLA in respect of breaches of the following rules and principles:

- until 1 December 2001 (N2), paragraph L8(1) and paragraph L12 of Schedule L:2 of the Adopted LAUTRO Rules; rule 7.1.2(1) of the Rules of the Personal Investment Authority (PIA Rules) and principles 2 and 9 of the Statements of Principle of the Securities and Investments Board (SIB Principles); and

- after N2, rules 5.2.5R and 5.3.5R in the part of the FSA's Handbook entitled the Conduct of Business Sourcebook (COB); rule 3.2.6R in the part of the FSA's Handbook entitled the Senior Management Arrangements Sourcebook, Systems and Controls (SYSC); and principles 2 and 3 of the FSA's Principles for Businesses (FSA Principles).
- 1.2 RLA confirmed on 4 April 2006 that it will not be referring this matter to the Financial Services and Markets Tribunal.
- 1.3 Accordingly, for the reasons set out below and having agreed with RLA the facts and matters relied on, the FSA imposes a financial penalty on RLA in the amount of £550,000.

2. REASONS FOR THE PENALTY

Summary of Conduct in Issue

- 2.1 The FSA imposes the penalty on RLA for breaches of the rules and principles referred to in paragraph 1.1 above. These breaches which occurred between 1 July 1999 and 15 September 2003 (the period in issue) relate to failures on the part of RLA in connection with the mis-selling of with profit endowment policies (WPEPs) as general savings vehicles to significant numbers of its older customers. RLA has offered a refund of all premiums paid and interest to all customers aged 59 and over, together with those customers of any age whose policies had been projected to pay, on maturity, a sum which would not exceed the total premiums paid by the customer.
- 2.2 These breaches, which are described in more detail at section 4 below relate to RLA's:
- (a) failure to take reasonable steps to obtain relevant information about customers' financial and other circumstances before making recommendations;
 - (b) failure to make suitable recommendations;
 - (c) failure to establish and maintain adequate systems and controls for ensuring compliance with applicable requirements and standards; and
 - (d) failure to conduct its business with due skill, care and diligence.
- 2.3 The failings in relation to the mis-selling of WPEPs to older customers are viewed as particularly serious for the following reasons:
- (a) The failings resulted in the sale of WPEPs to customers who had no demonstrable need for life cover or where the life cover included in the policy was not suited to their needs. As a result, customers with a general savings need were recommended a product that, on the basis of the FSA's mid growth rate of 6% per annum, projected to pay back less than the total value of premiums paid into the policy.
 - (b) As a result of these failings, RLA carried out a customer compensation exercise (CCE) covering the sale of WPEPs to older customers. While RLA did not review the suitability of each individual sale in the CCE, RLA accepts

that a significant proportion of these sales to customers aged 59 and over are likely to have been unsuitable. As a result, RLA accepts that in a significant number of cases its failings have resulted in the sale of WPEPs to older customers which were unsuitable to meet a general savings need alone. These sales carried a risk of causing financial disadvantage in that, on the basis of the FSA's mid growth rate, the WPEPs projected to pay back less than the total value of premiums paid into the policy. An internal report by RLA in May 2003 concluded that, on the basis of an assumed investment growth rate of 6% per annum, a majority of policies in a sample were projected to suffer losses on maturity of between £2 and £700.

- (c) The failings are systemic in nature, arising from weaknesses in RLA's sales process and compliance monitoring arrangements in relation to WPEPs.
- (d) The failings persisted over a four year period from 1 July 1999 to 15 September 2003.
- (e) RLA failed to notify the FSA of the findings of an internal review of the sale of WPEPs to older customers and to resolve the failings in connection with this issue in a timely manner. RLA became aware of these findings in May 2003, but did not report them to the FSA until October 2003.

2.4 RLA's failings are mitigated by the following factors:

- (a) After first identifying sales of WPEPs to older customers as a potential area of misselling, RLA took prompt action on its own initiative to prevent any further such misselling. With effect from 24 March 2003, RLA introduced enhanced procedures for the ongoing sales of WPEPs. This included the reinforcement of an earlier requirement for the adviser to produce comparative illustrations for WPEPs and other savings products, enhanced guidance on the justification of the customer's need for the life cover provided by the WPEP and a requirement that each WPEP sold had to project a return on maturity that would exceed the total premiums payable during the term of the policy (such projection being based on the FSA's mid-rate of projected investment Return of 6% per annum). Furthermore, in September 2003 RLA introduced a further requirement that a WPEP should not be recommended unless the policy projected a net yield of at least 2.5% per annum after deduction of administrative charges other than the cost of life cover, using a projected rate of investment return of 6% per annum.
- (b) In June 2004, RLA agreed with the FSA a timetable for the CCE. RLA decided, on its own initiative and in the interests of its customers, not to conduct file checks in order to determine the suitability of individual sales, but to offer compensation to all customers who had purchased a WPEP at aged 60 years or over (including those customers who were projected to receive upon maturity a sum that would exceed the premiums that they had paid into their policy). RLA completed the first phase of this compensation exercise in December 2004 one month ahead of the timetable agreed with the FSA. RLA extended the scope of the CCE to include all customers who had purchased a WPEP at age 59 and over together with those customers of any age whose

policies had been projected to pay, on maturity, a sum which would not exceed the premiums paid by the customer. This second phase is now substantially completed.

- (c) RLA's handling of the CCE should ensure that customers have been and will be offered redress more efficiently and quickly than if it had not co-operated with the FSA in this way. In relation to WPEP contracts sold during the period in issue, RLA has refunded 2,342 customers premiums totalling £2,245,000 together with interest of £246,000.
- (d) In early 2005, RLA also agreed with the FSA to undertake a Lesson Learned Project in order retrospectively to review issues relating to WPEPs, to review any suitability issues relating to other RLA products and to strengthen RLA's systems and controls. From the outset, RLA engaged the services of an independent third party in order to assist with the project and ensure that it is completed to a high standard. RLA has been proactive in ensuring that the Lessons Learned Project encompasses all of RLA's products and was not limited to WPEPs alone.
- (e) RLA has co-operated fully with the Enforcement action. RLA has agreed the facts quickly ensuring efficient resolution of the matter and has received full credit for settlement at an early stage. Without this level of co-operation the financial penalty would have been higher.

3. FACTS AND MATTERS RELIED ON

Background

- 3.1. RLA is a mutual incorporated friendly society that provides a range of financial service products predominantly in the area of life assurance, savings and pensions, mainly through its direct sales force, but also through independent financial advisers.
- 3.2. RLA has been regulated by the FSA since N2. Prior to authorisation by the FSA, RLA was regulated by the PIA.

The Product – WPEPs

- 3.3. This matter relates to the sale of WPEPs as general savings vehicles to older customers by RLA's direct sales force.
- 3.4. During the period in issue, RLA sold WPEPs to 27,948 customers of whom 3,569 were aged 60 and over (13 %).

PIA Supervision Visit - 17 September 2001 to 5 October 2001

- 3.5. Between 17 September 2001 and 5 October 2001 PIA Supervision conducted a visit to RLA to review its selling practices and compliance arrangements. As part of the visit, PIA reviewed 169 client files of which 39 had also been reviewed by RLA's fact find checking function/compliance department. A number of these files concerned the

sale of regular premium endowment contracts, although the issue of sales of such contracts to older customers was not specifically raised.

- 3.6. A number of concerns were identified and communicated to RLA in a report dated November 2001 together with a list of corrective actions.

Failure to demonstrate suitability

- 3.7. In relation to the 130 files not checked by compliance, PIA queried 87 customer files. In respect of these files, PIA made the following findings:

- (1) RLA had failed to record sufficient customer information to demonstrate the suitability of the recommendation. In particular, PIA identified that, in general, RLA's advisers had failed to explain the recommendation by reference to the customer's financial and other circumstances.
- (2) Specifically concerning the sale of regular premium endowment contracts, PIA identified that there was often no rationale for the inclusion of the life cover, the term of the contract or the purpose for which the customer was saving.
- (3) RLA's reason why letters failed adequately to explain why the recommendation was suitable for the customer taking into account their personal and financial circumstances.

- 3.8. In relation to the 39 customer files that had been fact find checked, 23 had been passed as "compliant". Of those 23 cases, PIA identified 13 that required corrective action. In respect of the remaining "non-compliant" cases, PIA identified further issues that required remedial attention.

Compliance arrangements

- 3.9. PIA also identified a number of issues in relation to RLA's compliance arrangements. These included, in particular, the following:

- (1) RLA had insufficient resource to carry out routine monitoring of its selling practices. RLA confirmed that the fact find checking team was required to prioritise any general compliance queries over routine fact find checks. If the pressure of this work demanded, fact find checks would not be carried out.
- (2) Procedures for monitoring RLA's investment staff were considered to be inadequate. This was demonstrated by inconsistencies in the method and quality of business assessments carried out at branch level and by the head office.
- (3) The Compliance Department also failed to adopt a sufficiently pro-active approach to communicating best practice and standards to investment staff

Firm's response to PIA Visit 2001

- 3.10. In respect of sales of regular premium endowment contracts, RLA replied that as the cost of life cover below a certain age (approximately age 40) was negligible, the effect of these deductions was unlikely to result in any material consumer detriment.
- 3.11. Concerning the failure to explain why other savings products had been discounted, RLA explained that it had now implemented the FSA's recommendation of using comparative illustrations to determine the most suitable savings product available. This recommendation now formed part of RLA's sales process and was incorporated within its Best Advice Guidelines and Standards document (BAGS). Finally, RLA confirmed that BAGS also now included a requirement for the recommendation of any savings contract with a term in excess of ten years to be documented clearly by way of a separate meeting note. RLA also engaged external consultants to review and update BAGs.

Findings of Annual External Audit, in respect of sales of WPEP - January 2003

- 3.12. In early 2003, RLA's external auditors as part of the year end audit reviewed a sample of 20 advised sales made during the course of 2002. This sample included two sales of WPEPs to customers aged 60 years and over of which both were queried as potential mis-sales.
- 3.13. In April 2003, the external auditor presented its Report to RLA's Audit Committee for the year ended 31 December 2002. The section on Compliance and Regulation noted that in assessing the compliance of its direct sales force RLA's senior management relied to a significant extent on the management information produced by the compliance function. However, the quality of this management information was directly dependent on the effectiveness of the compliance checks carried out both centrally and at the regional office level. To address this risk, the external auditors advised RLA to undertake an independent review of the suitability of product sales, in particular sales of higher risk products such as 10 year endowment savings contracts and whole of life policies.

Internal RLA Report on sales of WPEPs - May 2003

- 3.14. Following the identification by RLA's external auditors of concerns in early 2003, RLA's Business Quality Unit (BQU) carried out a review of all sales of WPEPs to customers age 60 and over effected during the last quarter of 2002. The results of this review and the concerns it raised were summarised in a report produced by the BQU in May 2003 (the May 2003 Report).
- 3.15. RLA reviewed a sample of sales of WPEPs to customers who were 60 or older at the time of sale as issues of suitability were likely to be most significant in this group. This sample was constructed from sales of WPEPs made during the last quarter of 2002. Choosing a sample from this period also enabled RLA to assess cases against BAGS, the sales guidance which had been introduced in 2002 to address the concerns raised by the 2001 PIA Visit. The final sample amounted to 155 cases of which each was reviewed for the purpose of assessing suitability.
- 3.16. The May 2003 Report contained the following findings.

- (1) In a large number of cases WPEPs had been sold to customers where there was no documented need for life cover endowment or where the life cover was not appropriate for the customer's needs.
- (2) In a large number of cases an endowment had been recommended when the information contained within the fact find did not support the recommendation and in fact seemed to suggest that an alternative product from within RLA's product range e.g. a Personal Investment Plan would have been more suitable.
- (3) In a large number of cases WPEPs with a term in excess of ten years e.g. 17 years, had been sold to customers with a general savings need. Assuming that a WPEP was suitable for the customer in all other respects, it was not clear in such cases why a shorter term (e.g. ten years) had not been recommended.
- (4) In over 90% of the cases sampled, with a projected growth rate of 6%, the WPEP was projected to yield less than the total premiums paid into the policy. The May 2003 Report observed that the principal purpose of any savings contract is to assist the customer in saving for the future. Therefore where the client specific illustration shows that the customer is projected to get back less than the total premiums paid over the term of the policy, the suitability of the recommendation must be called into question.
- (5) In a number of cases the customer had an identified savings need for which, according to their circumstances, a suitable RLA product appeared to be available. However the suitability letter confirmed that no recommendation was made and that the customer had simply "chosen" to purchase an endowment. The suitability letter, however, did not record why a recommendation was not made.

3.17. The May 2003 Report noted that three of the five issues identified by the review had been previously identified by the PIA Visit in October 2001 and were now addressed by BAGS. It concluded that these issues were still occurring due to either a lack of understanding or a misinterpretation of RLA's current sales guidelines.

RLA's Response to the May 2003 Report

- 3.18. Following the May 2003 Report RLA's Compliance Department immediately issued a communication to each of the UK sales regions to clarify current standards as set out in BAGS and to provide additional guidance on how these standards should be applied in practice.
- 3.19. As a further step RLA began to tighten up its current sales guidelines to prevent the sale of any long-term savings contracts unless, using a growth rate of 6%, the product was projected to produce a net yield of at least 2.5%. BAGS was revised to reflect this new requirement and was implemented from 15 September 2003 onwards.
- 3.20. RLA decided that further discussions should take place within senior management to determine what action should be taken in connection with past sales of WPEPs to older customers. However, at this time, no decision or action was taken to review past sales of WPEPs or to remedying any past potential mis-selling.

FSA Risk Mitigation Visit - October 2003

- 3.21. During October 2003 the FSA carried out a routine supervision visit to RLA. The FSA notified RLA of its findings in a letter dated 13 November 2003. In respect of RLA's compliance arrangements, the FSA notified RLA that it did not appear to have a robust system in place for regularly reviewing its sales process or related documentation.
- 3.22. Furthermore, the FSA confirmed that it had also identified a possible trend of sales of WPEPs to older customers, in particular customers over the age of 65. A number of RLA's client files indicated that customers within this category were projected to receive substantially less than the total value of premiums paid into the policy and that cancellation and lapses within this group also appeared high. While the FSA noted that RLA was aware of this issue and had taken action to correct its sales procedures it queried why RLA had not yet taken any action to review past sales of WPEPs to older customers or to remedy any possible mis-selling.
- 3.23. In view of its findings the FSA notified RLA that it should carry out a full investigation into the matter and report back to the FSA. In particular, RLA's investigation should seek to identify the total population of customers who, on realistic growth rates, have or are projected to receive negative returns on their endowment policies. Once this population has been identified, RLA should provide its conclusions in relation to the suitability of these sales and provide proposals for remedying any mis-selling.

RLA's response to FSA Risk Mitigation visit

- 3.24. RLA subsequently confirmed that it was undertaking an investigation into a wider sample of WPEPs sold to older customers in the period from 1 July 1999 to 15 September 2003. The investigation would seek to determine the suitability of these sales and provide information for the purposes of establishing a full past business review. RLA agreed a timetable for this investigation with the FSA.
- 3.25. In a letter dated 7 May 2004, RLA reported on the findings of its investigation into sales of WPEPs to older customers in the period 1 July 1999 to 15 September 2003.
- 3.26. Within this sample the review established that from 1999 until 2003, using a projected growth rate of 6%, the percentage of WPEPs sold to older customers that produced a projected negative return increased significantly.
- 3.27. On the basis of this analysis, RLA concluded that, during the period covered by the sample, sales of WPEPs to address a general savings need alone, to customers who had no requirement for life cover, would not have been justified. RLA concluded that a large percentage of the policies sold to older customers at the average premium level during that period could now be seen to be questionable. RLA therefore proposed to offer all such customers compensation, on the basis set out below.

- 3.28. There was further strengthening of the guidelines covering the sales of WPEPs during the course of 2004. The product was withdrawn from RLA's product range in December 2004.

Action taken by RLA in response to RMP visit

- 3.29. To ensure the fair treatment of customers, RLA decided that where any sales of WPEPs to older customers were identified, it would immediately offer customers an opportunity to cancel the policy and obtain a full refund of premiums plus interest, without first seeking to determine the suitability of the sale. To identify the starting age for the CCE and therefore the total customers affected, RLA confirmed that it would establish a point in time, by reference to the customer's age at the point of sale, the premiums payable and the policy terms, after which a significant proportion of new policies were projected to produce a negative return. On this basis, RLA decided to offer redress to all WPEP customers who were aged 59 years or over at the time of sale.
- 3.30. For cases where the policy was not projected, on maturity, to pay a sum exceeding the total premiums paid, regardless of the age of the customer, RLA agreed to offer the customer the opportunity to cancel their policy and obtain a full refund of premiums plus interest (less the value of any surrender or maturity payment if already made).
- 3.31. In those cases where the WPEP was projected to produce a positive return, RLA agreed to undertake some further sampling to establish the approach that should be taken. The results of this further sampling showed that out of a sample of 148 cases, 145 cases had insufficient documentation on file to demonstrate suitability. RLA accordingly agreed to contact these customers to establish whether they required the life cover in addition to the savings element of the WPEP. Where the life cover was not required customers would be offered the opportunity to cancel the policy and receive a full refund of all premiums paid plus interest.

The CCE

- 3.32. In September 2004, RLA concluded its work on identifying the starting population for the CCE. The total number of policies sold to customers aged 60 or over was 3,569, but after taking account of policies cancelled from outset and the joint life policies RLA identified a starting population of 2,550 sales. There were 2,425 responses from this population (95%), of whom 1,875 chose to cancel their policy (77%) whilst 550 opted to retain it (23%). For these 1,875 customers, RLA refunded £1,771,000 in premiums plus interest of £183,000.
- 3.33. Following further analysis, RLA expanded the CCE to include all sales of WPEPs to customers aged 59 and over. RLA also offered compensation to all remaining customers of any age where the sum payable on maturity was not projected to exceed the total premiums paid. Within these categories 542 customers were offered redress of whom 467 chose to cancel their policy and 75 opted to retain it. The 467 customers have, to date, been offered compensation totalling approximately £474,000 in premiums, plus interest of £63,000. The total amount RLA has paid to all categories of customers who purchased WPEPs during the period in issue is approximately £2,245,000 in returned premiums and approximately £246,000 in interest.

- 3.34. In addition, RLA also refunded premiums and interest to older customers who purchased WPEPs between 1993 and 30 June 1999.

The Lessons Learned Project and Root Cause Analysis

- 3.35. In addition to the CCE, RLA was also required to undertake a programme of work to investigate how the sale of unsuitable WPEPs to older customers had occurred and to put in place appropriate measures to ensure that similar problems did not arise in the future.
- 3.36. In a letter to the FSA dated 30 November 2004, RLA explained that its compliance staff had carried out checks in accordance with internal compliance checking standards. However, RLA had now concluded that its interpretation of the rules on suitability in relation to the WPEP had not been sufficiently robust, particularly in cases where there had been insufficient reasons documented for the recommendation of life cover, or where the cost of life cover may have had a significant impact on the potential returns.
- 3.37. In January 2005, RLA produced the results of its Lessons Learned Project and root cause analysis. In addition to the factors set out above, the root cause analysis identified issues relating to BAGS and RLA's sales process documentation that had contributed to the problems associated with sales of WPEPs to older customers.
- 3.38. The root cause analysis also highlighted RLA's compliance monitoring arrangements as a contributory factor, as well as the content of RLA's management information. Further details of the conclusions reached in the root cause analysis are set out in paragraph 4.13 below.

4. CONTRAVENTION OF RELEVANT REGULATORY REQUIREMENTS

Breaches of Rules

- 4.1. The penalty is imposed pursuant to section 206 of the Act in respect of breaches by RLA during the period in issue of SIB Principles and FSA Principles and the connected PIA Rules, including Adopted LAUTRO Rules and COB, SYSC and SUP rules, details of which are set out below.
- (1) Failure to take reasonable steps to obtain relevant information about customers' financial and other circumstances before making recommendations.**
- 4.2. In the period prior to N2, RLA was required by L12 of schedule L:2 of the Adopted LAUTRO rules to obtain as per was practicable all details about its customers' particular circumstances to enable it to comply with LAUTRO Rules.
- 4.3. Since N2 RLA has been required to take reasonable steps to obtain sufficient personal and financial information about its customers before making a recommendation.

Facts and matters relied on

- 4.4. A significant number of WPEPs with a term in excess of ten years were sold to customers where there was no information as to the specific purpose for which the customer was saving.
- 4.5. In a large proportion of cases where RLA recommended a WPEP there was no established need for life cover.

(2) Failure to make suitable recommendations

- 4.6. In the period prior to N2, RLA was required by L8(1) of Schedule L:2 of the Adopted LAUTRO Rules to use its best endeavours to ensure that recommendations were suitable for customers having regard to their financial and other circumstances.
- 4.7. Since N2, RLA has been required by COB 5.3.5R to take reasonable steps to ensure that it only made recommendations that were suitable for customers in light of their personal and financial circumstances.

Facts and matters relied on

- 4.8. Within the sample reviewed by RLA in May 2003, in a large number of cases RLA had recommended WPEP where there was no documented need for life cover or where the life cover provided by the policy was not appropriate to the customers needs. For example, there were a large number of instances where WPEPs had been sold to customers who had no financial dependants.
- 4.9. Similarly WPEPs were recommended in many cases where the information concerning the customer's financial and other circumstances did not support the recommendation and, in fact appeared to indicate that an alternative product from within the RLA range was more suitable.
- 4.10. Further, in many cases RLA failed to explain why the recommendation was suitable for the customer having regard to their personal and financial circumstances or why the particular policy term recommended was appropriate.

(3) Failure to establish and maintain adequate systems and controls for ensuring compliance with applicable requirements and standards

- 4.11. In the period before N2, RLA was required by virtue of PIA Rule 7.1.2 (1) to establish procedures with a view to ensuring that it complied at all times with relevant regulatory rules and principles. In the period since N2, RLA has been required by SYSC 3.2.6 R to take reasonable care to establish and maintain effective systems and controls for compliance with applicable requirements and standards.
- 4.12. Before N2, RLA was required by SIB Principle 9 to organise and control its internal affairs in a responsible manner. Since N2, RLA has been required by FSA Principle 3 to take reasonable care to organise and control its affairs responsibly and effectively.

Facts and matters relied on

4.13. RLA's Lessons Learned project, which included a root case analysis of the issues under investigation, concluded in January 2005 that:

- (1) BAGS, which established and governed RLA's sales process, was in some respects too prescriptive. Furthermore, the content of BAGS appeared to have been applied in an inflexible manner and contained insufficient guidance on when no sale may have been the most suitable recommendation. The communication of BAGS could also have been more consistent, controlled and robust.
- (2) The quality and comprehensiveness of RLA's fact finds had improved over time, but the effective use of this documentation had not been given sufficient priority in sales training in previous years.
- (3) RLA's compliance checking standards failed adequately to reflect regulatory requirements, particularly in the area of suitability. As a result, weaknesses in the standards/criteria for the assessment of the need for life cover were such that RLA's Compliance Department failed to identify or query any cases where there was insufficient or no rationale documented for the recommendation of this protection.
- (4) While all fact finds were individually checked by RLA's regional sales managers before submission to the head office, the effectiveness of this sales control was in some cases questionable.
- (5) The management information provided to senior management did not consider whether the product was projected to provide the customer with a positive return on maturity. The Board was not therefore advised when projected returns on savings and investment contracts for certain categories of customer had become negative.
- (6) Appropriate consideration had not been given at the product design stage of the WPEP, and whilst policies were in force, as to the projected returns on policies relative to the premiums customers would pay. As a consequence, RLA failed to identify at an early date, particularly from 2000 onwards, that customers over the age of 60 were likely to get back less than the total value of premiums paid into their policies.

(4) Failure to conduct its business with due skill, care and diligence

4.14. During the period in issue, RLA was required by SIB Principle 2 and FSA Principle 2 to conduct its business with due skill, care and diligence, which included obeying the PIA Rules (including the Adopted LAUTRO Rules) and FSA rules (including COB, SYSC and SUP Rules) and the SIB and FSA Principles.

Facts and matters relied on

4.15 By reason of the matters referred to in paragraphs 4.2 to 4.13 above, RLA failed to conduct its business with due skill, care and diligence in that it did not obey all the rules of the regulatory regimes in place during the period in issue.

5. RELEVANT GUIDANCE ON PENALTY

5.1. The FSA's policy on the imposition of financial penalties is set out in Chapter 13 of the Enforcement Manual which forms part of the FSA Handbook (ENF). The principal purpose of the imposition of a financial penalty is to promote high standards of regulatory conduct by deterring firms who have breached regulatory requirements from committing further contraventions, helping to deter other firms from committing contraventions and demonstrating generally to firms the benefits of compliant behaviour.

5.2. Article 8 (4) of the Pre-N2 Misconduct Order provides that, where the FSA proposes to impose a financial penalty it must have regard to:

“any statement made by the self-regulating organisation ...which was in force when the conduct in question took place with respect to the policy on the taking of disciplinary action and the imposition of, and amount of penalties (whether issued as guidance, contained in the rules of the organisation or otherwise)”.

5.3. Relevant PIA Guidance is contained in Annex D of “PIA's Approach to Discipline – Statement of Policy” that was issued in December 1995. In all material respects this required consideration of the same factors as identified in Chapter 13 of the Enforcement Manual. It has been taken into account by the FSA in determining the appropriate sanction in this case.

5.4. PIA's Statement of Policy makes it clear however that that the criteria for determining the level of sanction are not to be applied rigidly, as stated in paragraph 2 of Annex D:

“Each case is different and needs to be treated on its own merits. It is not possible to apply a mechanistic approach to the determination of the circumstances in which disciplinary action should be taken or of the sanctions to be applied. The criteria...should not be treated as exhaustive. Nor should it be assumed that regard would necessarily be had to a particular criterion in any given circumstances.”

5.5. Similarly, it is stated in Chapter 13 of the FSA Enforcement Manual at clause 13.3.4 that the criteria listed in the manual are not exhaustive and all relevant circumstances of the case will be taken into consideration.

5.6. In determining whether a financial penalty is appropriate and its level the FSA considers all the relevant circumstances of the case. The FSA considers the following factors to be particularly relevant in this case.

ENF13: The seriousness of the misconduct or contravention

PIA Guidance: The seriousness of the breaches. The scale of any investor losses and/or the extent to which investors were exposed to the risk of such losses.

5.7. The FSA has had regard to the seriousness of the contraventions, including the nature of the requirements breached, the number and duration of the breaches and the number of customers impacted. The level of financial penalty must be proportionate to the nature and seriousness of the contravention. Details of the breaches identified in this case are set out above. For the reasons set out below the FSA considers that the breaches in this case are of a serious nature:

- (1) The failings persisted over a 4 year period from 1 July 1999 to 15 September 2003.
- (2) The failings are systemic in nature arising from weaknesses in RLA's sales process and compliance monitoring arrangements.
- (3) The failings resulted in the sale of WPEPs to older customers who had no demonstrable need for life cover or where the life cover included in the policy was not suited to their needs. As a result, customers with a general savings need were recommended a product that, using an assumed investment growth rate of 6% per annum, projected to pay back less than the total value of premiums paid into the policy.

ENF13: The extent to which the contravention or misconduct was deliberate or reckless

PIA Guidance: whether this member intentionally or recklessly failed to meet PIA's requirements

- 5.8. The FSA has not determined that RLA deliberately contravened the relevant rules and principles.
- 5.9. However, as a result of the findings of the May 2003 Report, RLA was aware or ought reasonably to have been aware that its actions had resulted in or were likely to have resulted in the unsuitable sale of WPEPs to older customers. Despite the findings of this Report, RLA failed to report the matter immediately to the FSA and to resolve this issue in a timely manner.

ENF13: The size, financial resources and other circumstances of the RLA and the amount of profits accrued or loss avoided

PIA Guidance: The Member's ability to pay: The scale of any investor losses and/or extent to which investors were exposed to the risk of such losses and the extent to which, as a result of the breaches, the Member gained a benefit or avoided suffering a loss.

- 5.10. In June 2004, RLA agreed with the FSA the terms of the CCE. RLA decided not to conduct file checks to determine the suitability of individual sales but instead, in the interests of its customers, offered the repayment of total premiums plus interest, to all customers who had purchased a WPEP at age 59 years or over. RLA completed the first phase of this exercise (involving customers aged 60 and over) in December 2004 and has substantially completed the second phase.
- 5.11. As a result of offering customers a full refund of premiums and interest RLA has incurred a loss as a result of its contraventions.

ENF13: Conduct following the contravention

PIA Guidance: The firm's response once the breaches were identified

- 5.12. Shortly after identifying sales of WPEPs to older customers as a cause of concern, RLA took action to enhance the procedures surrounding such sales (the steps taken by

RLA in this regard are set out in paragraph 2.4 (a) above). RLA did not initially take any steps to identify or remedy any past mis-sales of WPEPs. However, in June 2004 RLA agreed with the FSA a timetable for the CCE and during the period since then RLA has taken effective steps to offer customers appropriate redress.

- 5.13. In early 2005, RLA initiated the Lesson Learned Project in order, pro-actively, to review any suitability issues relating to other RLA products and to strengthen RLA's processes in the areas of product suitability and systems and controls. From the outset, RLA engaged an independent third party in order to assist with the project and ensure that it is completed to a high standard. The Lessons Learned Project encompasses all of RLA's products.
- 5.14. Following its referral to Enforcement, RLA has co-operated fully with the Enforcement action. RLA agreed the facts quickly ensuring efficient resolution of the matter and has received full credit for settlement at an early stage. Without this level of co-operation the financial penalty would have been higher.

Disciplinary record and compliance history

ENF13: Disciplinary record and compliance history

PIA Guidance: RLA's Regulatory History

- 5.15. RLA has not previously been the subject of any disciplinary action.

Previous action taken in relation to similar failings

ENF13: Action taken by other Regulatory Authorities in Relation to Similar Failings

PIA Guidance: The way in which PIA has dealt with similar cases in the past

- 5.16. In setting the level of the proposed penalty, the FSA has taken into account penalties levied by previous regulators and by the FSA.

DECISION MAKER

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

IMPORTANT

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

Manner of and time for payment

The financial penalty must be paid in full by RLA to the FSA by no later than 20 April 2006, 14 days from the date of the Final Notice.

If the financial penalty is not paid

If all or any of the financial penalty is outstanding on 20 April 2006, the FSA may recover the outstanding amount as a debt owed by RLA and due to the FSA.

Publicity

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.

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

FSA contacts

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

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David Bates, FSA Enforcement Division