Financial Services Authority

# FINAL NOTICE

To: **Thinc Group Limited;**

**Thinc Assured Network Limited; and**

**Thinc Network Services Limited**

Of: **6th Floor**

**47 Mark Lane**

**London EC3R 7QQ**

Date: 15 May 2008

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

## 1. THE PENALTY

1.1. The FSA gave Thinc Group Limited, Thinc Assured Network Limited and / or Thinc Network Services Limited (hereafter referred to collectively as the "the Firm") a Decision Notice on 14 May 2008 which notified the Firm 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 £900,000 in respect of breaches by the Firm of Principles 9 (Customers: relationships of trust) and 3 (Management and Control) of

the FSA Principles for Businesses ("Principles") during the period from 1 January 2006 to 30 September 2007 ("the relevant period").

1.2. The Firm agreed that it will not be referring the matter to the Financial Services and Markets Tribunal.

1.3. Accordingly, for the reasons set out below and having agreed with the Firm the facts and matters relied on, the FSA imposes a financial penalty on the Firm in the amount of £900,000.

1.4. The Firm agreed to settle this matter at an early stage of the proceedings. It therefore received a 30% ("Stage 1") reduction in penalty pursuant to the FSA's executive settlement procedures. Were it not for this discount, the FSA would have sought to impose a penalty of £1,285,000 on the Firm.

## 2. REASONS FOR THE ACTION

### Introduction

2.1. The breaches of Principles 9 and 3 during the relevant period arise from the Firm's regulated sub prime mortgage business and in respect of weaknesses in its compliance systems and controls.

### Customers: Relationships of Trust

2.2. The Firm breached Principle 9 during the relevant period in that it failed to take reasonable care to ensure the suitability of its advice given to some of its customers in relation to the sale of regulated mortgage contracts in the sub prime market. In particular, the Firm:

(1) failed to obtain adequate financial information about those customers prior to giving advice;

(2) failed to demonstrate that those customers' credit histories merited the sale of a sub prime mortgage;

(3) failed to demonstrate why the particular sub prime mortgage products that it recommended matched those customers' needs and circumstances;

(4) failed to demonstrate that it had considered the affordability of the sub prime mortgage contracts that it recommended to those customers; and

(5) provided some of those customers with a 'Record of Suitability' letter that did not correspond to the product advised / taken.

**Management and Control**

2.3. The Firm breached Principle 3 in that it failed to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems with regards to its sub prime mortgage business. In particular, the Firm:

(1) failed to make and/or retain adequate records relating to sales of sub prime mortgages; and

(2) failed to implement an effective system for compliance checking the suitability of the advice in relation to sub prime mortgage sales.

**Seriousness of the findings**

2.4. The FSA considers that the Firm's failings are serious because:

(1) the Firm's failings occurred after the FSA had published its concerns to the regulated IFA sector in September 2005 about the need for firms to make and retain sufficient records to ensure that they are able to demonstrate the suitability of their advice;

(2) the Firm is one of the largest IFA groups, acting as the principal for a large network of IFAs and is, therefore, responsible for ensuring that its representatives comply with their regulatory requirements;

(3) its conduct could have an adverse effect on the customers concerned, many of whom were recorded as having adverse credit histories and/or were consolidating debts; and

(4) the failings continued after the FSA Thematic Visit of February 2007 because the remedial action implemented by the Firm was ineffective and the Firm's sales practices and the compliance regime did not improve.

2.5. The Firm's failings are mitigated by the following:

(1) the FSA has not determined that the Firm mis-sold sub prime mortgages to its customers;

(2) the Firm has received few complaints in relation to regulated mortgage business undertaken during the relevant period;

(3) the Firm has been open and co-operative with the FSA and agreed the facts quickly ensuring early resolution of the matter; and

(4) the Firm has agreed to implement a comprehensive remedial plan to:

(a) appoint an independent third party to review its sub prime business conducted during the relevant period to determine if there is any customer detriment and to identify if compensation should be paid where appropriate;

(b) restructure its mortgage advice sales processes for all mortgage business;

(c) re-train and if necessary dismiss sub-standard mortgage advisers;

(d) overhaul its compliance checking processes for all mortgage business; and

(e) restructure its compliance department.

## 3. RELEVANT STATUTORY PROVISIONS AND GUIDANCE

### Provisions of the Act

3.1. Section 206 of the Act provides that:

*If the Authority considers that an authorised person has contravened a requirement imposed on him by or under this Act, it may impose a penalty, in respect of the contravention, of such amount as it considers appropriate.*

3.2. The Firm is an authorised person for the purposes of section 206 of the Act.

3.3. The procedures to be followed in relation to the imposition of a financial penalty are set out in Sections 207 and 208 of the Act. The Principles for businesses, as set out in the FSA Handbook, are a general statement of the fundamental obligations of firms under the regulatory system. The Principles derive their authority from the FSA's rule making powers as set out in Section 138 of the Act.

**Principles for Businesses**

3.4. Principle 9 provides that:

*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.*

3.5. Principle 3 provides that:

*A firm must take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems.*

## 4. BACKGROUND

4.1. The Firm grew out of the merger in 2000 with The Destini Group and it has been authorised by the FSA since 31 October 2004 to carry on the following regulated activities in relation to mortgage contracts:

(1) advising on regulated mortgage contracts;

(2) agreeing to carry on a regulated activity;

(3) arranging regulated mortgage contracts; and

(4) making arrangements.

4.2. Thinc Group Limited is the parent company for the group which includes Thinc Network Services Limited ("TNS") and Thinc Assured Network Limited ("TAN"). Regulated mortgage business is conducted through all three entities. The Firm’s administrative centre is in Telford, Shropshire and during the relevant period its structure can be summarised as follows:

(1) TNS is a network made up of 126 appointed representatives consisting of approximately 420 advisers. It advises on pensions and investments and it offers some mortgage and general insurance services.

(2) TAN is a network made up of 84 appointed representatives consisting of approximately 180 advisers. It advises on mortgage and general insurance services and offers some pension and investment services.

4.3. In the period 1 January 2006 to 30 September 2007 the Firm acted as broker in the sale of 18,015 regulated mortgage contracts, representing total consumer borrowings of £2,706 million, of which £76.9 million was loaned to customers with an impaired credit rating. These mortgage sales generated revenue for the Firm of almost £36 million during the relevant period (£16.7 million in the year ended 31 December 2006 and £19.2 million in the 9 month period from 1 January 2007 to 30 September 2007).

4.4. During the relevant period, the Firm gave advice in respect of 840 sub prime mortgage cases which are the subject of this Final Notice. Of this number, 775 (around 4% of the total mortgage sales) were completed. The term sub prime generally refers to regulated mortgage contracts targeted at consumers with an impaired or low credit rating as a result of an adverse credit history. Sub prime regulated mortgage contracts are generally more expensive than other regulated mortgage contracts available on the market as a higher interest rate is usually charged due to a perceived higher risk of default.

4.5. During the relevant period, the sub prime mortgage business generated revenue of approximately £0.7 million for the Firm.

**Background to the investigation**

4.6. As previously referred to at paragraph 2.4 (4), in September 2005 following a thematic review of the sub prime mortgage market, the FSA published its concerns about inappropriate sales practices in connection with sub prime mortgage products. The publication informed regulated firms of the issues to consider when advising customers about sub prime mortgages. One of the key findings was that in 80% of the 210 files reviewed by the FSA as part of the industry-wide thematic work, there was a

lack of evidence to demonstrate how the sub prime products met the customer's needs and circumstances.

4.7. As part of a follow up thematic review of the sub prime mortgage market, the FSA visited the Firm on 13 and 14 February 2007 and reviewed a sample of customer files that involved the advised sale of a sub prime mortgage.

4.8. As a result of failings identified during the visit to the Firm, the FSA commenced an investigation on 30 July 2007. The investigation has been confined to the Firm's sub prime mortgage business.

4.9. As part of the investigation, the FSA required the Firm to provide a sample of 50 sub prime mortgage cases spanning February 2006 to July 2007. The Firm was unable to produce one of the files requested and in 2 cases the file supplied had been reconstructed as the original documents prepared at the point of advice were lost.

4.10. All of the 49 sub prime files that were reviewed by the FSA lacked information that was fundamental to demonstrating the suitability of the Firm's advice. The failings identified in the FSA's review of the 49 files are outlined below.

## 5. BREACHES OF REGULATORY REQUIREMENTS

**Principle 9**

***Failure to obtain adequate financial information about customers prior to giving advice***

5.1. The FSA considers that the Firm persistently failed to:

(1) Obtain information about the customer's monthly outgoings in order that the adviser was in a position to determine affordability. In many cases the factfind contained little or no information about the customer's monthly expenditure.

(2) Consider the plausibility of customers' declarations about their monthly expenditure. In a number of cases the stated monthly outgoings were not plausible in the context of the customer's sub prime profile.

(3) Obtain information about the customer's existing lending arrangements and the costs associated with their redemption.

***Failure to demonstrate that customers' credit histories merited the sale of a sub prime mortgage***

5.2. In the cases reviewed by the FSA there were frequent instances where the Firm failed to obtain and verify any background information about the customer's adverse credit history and to obtain a credit report to confirm sub prime status. In some cases the customer's adverse credit history was historic and may have been repaired with the passage of time, yet the Firm's records did not show why a sub prime mortgage was still justified.

***Failure to demonstrate why the particular sub prime mortgage that it recommended matched customers' stated needs and circumstances***

5.3. The Firm persistently failed to demonstrate how it chose the sub prime mortgage it selected for its customers. In the majority of cases, the files lacked detail of the product research carried out by the adviser or the basis for choosing the product recommended to the customer. On other occasions, the product research on file suggested that a more affordable deal was available to the customer but it had not been recommended by the adviser and there were no notes on file to explain why.

5.4. In a number of cases, the sub prime mortgage eventually taken up by the customer differed from the product initially recommended without documented explanation of the difference from the adviser.

5.5. The FSA also found instances where the Firm failed to demonstrate the rationale for recommending self-certified sub prime mortgages to customers by failing to explain why customers were advised to self certify when the customers were in full time employment or had accounts from which income could be proved.

***Failure to demonstrate that it had considered the affordability of the sub prime mortgage that it recommended to customers***

5.6. In cases where the advice resulted in the mortgage term exceeding the customer's retirement age, the Firm failed to show that the adviser had considered whether the

mortgage was affordable having regard to the customer's anticipated retirement income.

5.7. In many of the cases reviewed, the Firm also failed to show that it had taken account of the customer's ability to meet the extra costs of the sub prime mortgage product that it recommended particularly at the expiry of the period of the introductory fixed / capped interest rate.

5.8. In a number of cases, where an interest only mortgage was advised, the adviser failed to show that the customer's arrangements for repayment of the mortgage loan had been considered.

***Provided customers with a 'Record of Suitability' letter that did not correspond to the product advised / taken***

5.9. The Firm persistently failed to tailor the 'Record of Suitability' letter to the product recommended to the customer. There were also instances where the 'template' letter used by the adviser failed, without explanation, to address the customer's needs and circumstances. For example, there were instances where the customer had stated that they wanted a repayment mortgage but the 'Record of Suitability' letter showed the adviser recommending an interest only mortgage without any explanation of why this differed from the customer's initial requirements.

**Breach of Principle 9**

5.10. The FSA considers that as a result of the failings set out in paragraphs 5.1 to 5.9 above, the Firm breached Principle 9 by failing to take reasonable care to ensure the suitability of its advice.

**Aggravating Factors**

5.11. In response to the FSA's thematic visit findings, the Firm gave a presentation to the FSA on 2 April 2007 setting out its remedial plan to improve its sales practices and compliance regime for its sub prime mortgage business. During the early stages of the FSA investigation, the Firm re-iterated that it had implemented a programme of reform. The FSA considers that the remedial action implemented by the Firm was ineffective and sales practices in respect of sub prime mortgages did not improve.

**Principle 3**

***Failure to make and retain adequate records relating to sales of sub prime mortgages***

5.12. The FSA considers that for the following reasons the firm failed to retain adequate records relating to the sale of sub prime mortgages:

(1) when required to do so by the FSA, the Firm was unable to produce one of the sub prime cases required for review as part of the investigation;

(2) in two of the files reviewed by the FSA, the Firm had reconstructed the file where some or all of the original documents could not be found;

(3) there were many instances of documents being referred to, but not included, in the files supplied to the FSA;

(4) the advisers failed to make adequate records of contact with customers and, with regard to the sample of files requested by the FSA, the firm advised the FSA that it had had to revert to its advisers to obtain further information and had added file notes to make the picture clearer before the files were sent to the FSA ; and

(5) the advisers routinely failed to document the rationale for the recommendations that they made to customers.

5.13. The FSA considers that the above failings demonstrate that the Firm failed to organise and control its record-keeping responsibly and effectively.

***Failure to implement an effective system for compliance checking the suitability of the advice in relation to sub prime mortgage sales***

*Adviser Rating*

5.14. The Firm employs a risk-based Red-Amber-Green or 'traffic light' system to assess compliance. Advisers are classed as Red, Amber or Green (or a mixture of two – e.g. Red-Amber) and the number of their files checked by the compliance team is

dependent on their status. All new advisers are assessed as Red in their first six months of employment with the Firm.

5.15. In the absence of an event requiring the immediate intervention by the compliance team, advisers who are rated as Green are visited by the Firm's field supervisors every six months. In contrast, advisers rated as Red are visited on a monthly basis.

5.16. The usual rating pattern was as follows:

(1) Green – 60%

(2) Amber – 30%

(3) Red/Amber – 9%

(4) Red – 1%

5.17. The Firm has told the FSA that advisers who are rated Red have their commission withheld until the reason(s) for the rating has been remedied.

*File Checking.*

5.18. The Firm has accepted that, prior to being acquired by AXA in November 2006, financial constraints resulted in the Compliance team being inadequately resourced.

5.19. Until April 2007 the Firm's compliance team aimed to check 10% of all mortgage business written. However, the Firm has accepted that in 2006 it abandoned checking a backlog of 325 mortgage files (which included 6 sub prime cases). Following the FSA's Thematic Visit in February 2007, the Firm started checking 100% sub prime (and lifetime) mortgage sales.

5.20. During the relevant period the Firm used five grades for file checking:

(1) **Pass** – where no further action is required;

(2) **Pass remedial** – where the adviser needs to undertake further contact with the client, usually in the form of an addendum or obtaining missing documentation required to evidence the suitability of the advice;

(3) **Mandatory Fail** – where a mandatory area has not been completed and requires amendment;

(4) **Potential Best Advice Fail** – where there is insufficient evidence on file to ascertain that best advice has been given. The adviser is given the opportunity to provide additional clarification on the points raised within the file review.

(5) **Best Advice Fail** – where the adviser is unable to provide any additional evidence to justify that best advice has been given.

5.21. Until April 2007 the Firm's compliance checking systems and controls did not differentiate between a sub prime mortgage and a prime mortgage. In the aftermath of the FSA Thematic Visit, the Firm changed its file review procedures to check 100% of sub prime mortgages.

5.22. The FSA considers that the Firm has failed to operate an effective system for compliance checking the suitability of advice in respect of sub prime mortgage sales for the following reasons:

(1) The file checkers in compliance failed to use the grading system appropriately. In all of the sub prime mortgage files supplied to the FSA which had been compliance checked, the Firm acknowledged that the grading 'Pass with Remedial' was wrong and the files ought to have been failed because the file lacked fundamental information to demonstrate the suitability of the advice given.

(2) In those cases where the file had been checked and remedial action had been imposed on the adviser, the file checkers failed to follow up on the remedial action that they imposed. In those cases which were graded (inappropriately or not) as 'Pass with Remedial' the file checker required the adviser either to provide fundamental information about the advice given or to make material changes to the letter of suitability to the customer. In most cases the adviser failed to comply with the remedial action required but the Firm failed to follow this up and there is no evidence that the Firm imposed sanctions on any advisers for non-compliance.

(3) The file checking procedure was carried out some time after the mortgage had been recommended and in the majority of cases after completion. In consequence, the compliance check was ineffective as it came too late to correct any procedural defects and / or potentially unsuitable advice. The Firm has acknowledged this flaw in its compliance control and has adjusted its procedures so that cases are referred for checking at a much earlier stage in the sales process.

5.23. In addition, the FSA considers that the Firm's decision in 2006 to abandon its review of a backlog of 325 mortgage files demonstrates that its affairs were not organised and controlled responsibly and effectively and that compliance checking was not given sufficient priority.

5.24. As outlined above at paragraph 5.21, in response to the FSA's findings from the Thematic Visit of February 2007, the Firm changed its compliance checking procedures in April 2007 so that all sub prime mortgage business written was checked. The FSA's investigation found that the increased file checking of sub prime cases since April 2007 had not curtailed the inadequate sales practices and the failings highlighted in paragraphs 5.1 – 5.9 which were apparent when the FSA investigation commenced in August 2007.

**Breach of Principle 3**

5.25. For the reasons set out in paragraphs 5.12 – 5.24, the FSA considers that the Firm has failed to take reasonable care to organise and control its record-keeping and file checking procedures in relation to sub prime mortgage business responsibly and effectively and such a failure amounts to a breach of Principle 3.

## 6. RELEVANT GUIDANCE ON PENALTY

6.1. The FSA has considered the disciplinary and other options available to it and has concluded that a financial penalty is the appropriate sanction in the circumstances of this particular case. The principal purpose of a financial penalty is to promote high standards of regulatory conduct. It seeks to do this 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 benefit of compliant behaviour.

6.2. In determining the financial penalty, the FSA has had regard to guidance contained in the Decisions Procedure and Penalties manual ("DEPP") which became part of the FSA's Handbook of Rules and Guidance (the "FSA Handbook") with effect from 28 August 2007, as well as the guidance contained in the Enforcement Manual ("ENF") which formed part of the FSA Handbook during the relevant period.

6.3. DEPP 6.5 sets out some of the factors that may be of particular relevance in determining the appropriate level of a financial penalty, and Chapter 13 of ENF contains the equivalent guidance that was in effect during the relevant period.

6.4. DEPP 6.5.1G and ENF 13.3.4G both state that the criteria listed in DEPP6.5 and ENF 13.3 respectively are not exhaustive and all relevant circumstances of the case will be taken into consideration. In determining whether a financial penalty is appropriate and its level, the FSA is required therefore to consider all the relevant circumstances of the case.

**Deterrence**

6.5. The FSA considers that the sanction imposed will promote high standards of regulatory conduct within the Firm and deter it from committing further breaches. It will also help deter other firms from committing similar breaches as well as demonstrating generally the benefits of a compliant business.

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

6.6. The FSA had regard to the seriousness of the contraventions by the Firm, including the nature of the requirements breached and the duration of the breaches. For the reasons set out in paragraph 2.4 above the FSA considers that the breaches are of a serious nature.

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

6.7. The FSA has taken into account the Firm's financial resources.

6.8. At the time of these breaches the Firm held itself out as one of the top 15 IFA groups in the country and in its position as the principal for a large network of IFAs it is required to promote and maintain high regulatory standards.

6.9. The Firm is able to pay the financial penalty imposed on it.

**Conduct following the breach**

6.10. The FSA considers that the Firm failed to implement an effective plan to correct the failings brought to its attention by the Thematic Visit of February 2007.

6.11. However, as set out in paragraph 2.5 above, the FSA recognises the Firm's significant co-operation and its willingness to give undertakings to implement an effective remedial plan to remedy the failings identified and to comply with its regulatory requirements on an on-going basis. Without the remediation, the FSA would have imposed a significantly higher penalty.

**Disciplinary record and compliance history**

6.12. The Firm has not previously been the subject of disciplinary action by the FSA.

**Previous action taken by the FSA**

6.13. The FSA seeks to ensure consistency when it determines the appropriate level of financial penalty but does not operate a tariff system of penalties for different kinds of breach (DEPP 6.5.1G (2)).

6.14. The FSA has in the past taken action against firms for similar failings and these have been taken into consideration in setting the level of the financial penalty against the Firm.

## 7. CONCLUSION

7.1. Having regard to the matters summarised above, to the guidance set out in DEPP and to the FSA's statutory objectives of the protection of consumers and public awareness, the FSA considers it proportionate and appropriate in all the circumstances to impose on the Firm a financial penalty of £900,000.

7.2. In agreeing to settle at an early stage, the Firm qualified for a 30% reduction in penalty under the provisions of the FSA's executive settlement procedure. Were it not for the discount, the FSA would otherwise have sought to impose a financial penalty of £1,285,000 on the Firm.

## 8. DECISION MAKER

8.1. 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.

## 9. IMPORTANT

9.1. This Final Notice is given to you in accordance with section 390 of the Act. The following statutory rights are important.

**Manner of and time of payment**

9.2. The financial penalty must be paid in full by the Firm to the FSA by no later than 29 May 2008, 14 days from the date of this notice.

**If the financial penalty is not paid**

9.3. If all or any of the financial penalty is outstanding on 30 May 2008, the FSA may recover the outstanding amount as a debt owed by the Firm and due to the FSA.

**Publicity**

9.4. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. 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 the Firm or prejudicial to the interests of consumers.

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

**FSA contacts**

9.6. For more information concerning this matter generally, you should contact Jeremy La Niece at the FSA (direct line: 020 7066 1346 /fax: 020 7066 1347).

**Georgina Philippou**

**FSA Enforcement Division**