Financial Services Authority

FINAL NOTICE

To:	**Wills & Co Stockbrokers Limited**
Of:	**33 Queen Street** **London, EC4R 1AP**
Date:	3**1 October 2007**

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. ACTION

1.1. The FSA gave Wills & Co Stockbrokers Limited ("Wills & Co") a Decision Notice on 25 October 2007 which notified Wills & Co 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 £49,000 on Wills & Co for breaches of the FSA's Principles for Businesses ("the Principles") in relation to advising, arranging and selling certain higher risk smaller capitalised securities to private customers. In particular, Wills & Co failed:

(1) to pay due regard to the information needs of its clients, and communicate information to them in a way which is clear, fair and not misleading in breach of Principle 7; and

(2) to take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems in breach of Principle 3.

1.2. In addition, Wills & Co breached the rule in the part of the FSA Handbook ("the Handbook") entitled Conduct of Business ("COB") 5.4.3R, which is set out in paragraph 3.4 below.

1.3. Wills & Co confirmed on 23 October 2007 that it will not be referring the matter to the Financial Services and Markets Tribunal.

1.4. Accordingly, for the reasons set out below and having agreed with Wills & Co the facts and matters relied on, the FSA imposes a financial penalty on Wills & Co in the amount of £49,000.

1.5. Wills & Co agreed to settle this matter at an early stage of the proceedings. It therefore qualified for a 30% (stage 1) reduction in penalty, pursuant to the FSA's executive settlement procedures. Were it not for this discount, the FSA would otherwise have sought to impose a financial penalty of £70,000 on Wills & Co.

2. REASONS FOR THE ACTION

2.1. The breaches of the Principles and COB 5.4.3R outlined above relate to Wills & Co failing to organise and control its sales process and practices in relation to advising and arranging for private customers to purchase higher risk securities issued by five new or emerging smaller capitalised companies ("the Securities") between April and October 2006 ("the Relevant Period"). All of the Securities were penny shares.[1]

2.2. During the Relevant Period, the conduct of Wills & Co fell below the standard reasonably to be expected under the regulatory system for the following reasons:

(1) Wills & Co failed to take reasonable steps to ensure customers understood the nature of the risks involved, immediately prior to and at the time of purchasing the Securities, as they were not provided with risk warnings and/or sufficient risk information before the point of sale (Principle 7);

(2) Wills & Co did not pay due regard to the information needs of its customers as it failed to communicate clear, fair and not misleading information about the Securities and necessary information was communicated in an ambiguous and rushed manner. In addition, some of the information provided to customers undermined or obscured important characteristics of the Securities by focusing only on the positive aspects and/or by providing necessary information only after the customer had agreed a purchase (Principle 7); and

(3) Wills & Co failed to take reasonable care to organise and control its affairs responsibly and with adequate risk management systems, as it did not establish and maintain robust systems and controls that were appropriate for the business of recommending higher risk securities to private customers (Principle 3). In particular it failed to:

[1] Penny Shares are a readily realisable security in relation to which the bid-offer spread is 10 per cent or more of the offer price but not: (a) a government and public security; or (b) a share in a company quoted on the Financial Times Stock Exchange 100 Index; or (c) a security issued by a company which, at the time that the firm deals or recommends to the client to deal in the investment, has a market capitalisation of £100 million or more (or its equivalent in any other currency at the relevant time).

(a) maintain appropriate and documented procedures detailing its approach to compliance monitoring;

(b) maintain centralised and complete records of its compliance monitoring findings to identify and assess the ongoing and emerging risks posed to its business. As a result, identified risks may not have been remedied and/or acted upon; and

(c) establish and implement a comprehensive compliance monitoring programme and robust compliance controls that were sufficiently tailored to its regulated business.

The seriousness of Wills & Co's misconduct

2.3. The FSA views Wills & Co's failings as serious in view of the following considerations:

(1) customers may have purchased the Securities without fully understanding or being sufficiently aware of the associated and higher risks;

(2) Wills & Co provided customers with information about the Securities in a rushed manner, which meant that the information was unclear and customers were not able to discern properly the key features and associated risks before agreeing to the purchase;

(3) despite the high risk nature of its business there were weaknesses in the way that Wills & Co operated and maintained its compliance monitoring systems which meant that poor sales practices were not readily recognised and the risk to customers was not identified promptly; and

(4) Wills & Co only recognised certain deficiencies in its sales processes and procedures as a result of the FSA thematic visit, and the subsequent investigation, rather than through the operation of its systems, controls and procedures. In addition, Wills & Co did not commit to and/or undertake a course of remedial action until after intervention from the FSA.

The decision to impose a financial penalty

2.4. In deciding the level of the financial penalty, the FSA recognises some measures taken by Wills & Co which mitigate the seriousness of the failings. In particular Wills & Co:

(1) engaged two separate compliance consultants to review its sales processes, governance structures, procedures and operational practices;

(2) committed to, and implemented, a remedial action plan which involves increasing its compliance resources, retraining all of its investment advisers and conducting on-going internal reviews of its sales procedures, compliance arrangements and sales monitoring. To date, its internal reviews have led to

the implementation of a number of changes to its sales practices, systems and controls; and

(3) co-operating and engaging fully with the FSA and moving quickly to agree the facts and efficiently resolve the case. Without this level of co-operation the financial penalty would have been higher.

3. RELEVANT STATUTORY AND HANDBOOK PROVISIONS

3.1. The FSA is authorised under section 206(1) of the Act to impose a financial penalty, of such amount it considers appropriate, if an authorised person has contravened a requirement imposed on him by or under the Act.

3.2. 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.

3.3. The Principles, as set out in the Handbook, are a general statement of the fundamental obligations of firms under the regulatory system. They derive their authority from the FSA's rule making powers as set out in the Act.

3.4. By virtue of COB 5.4.3R, a firm must not make a personal recommendation with, to or for a private customer unless it has taken reasonable steps to ensure that the private customer understands the nature of the risks involved. COB 5.4.4E indicates what reasonable steps should include, which, in the case of Wills & Co, involves the provision of a specified risk warning to private customers as transactions in the Securities are transactions in penny shares. The version of COB 5.4.5E in force during the Relevant Period stated that compliance with COB 5.4.4E may be relied on as tending to establish compliance with COB 5.4.3R.

4. BACKGROUND

The Firm

4.1. Wills & Co was incorporated in April 1959 and is wholly owned by GHW Group Limited.

4.2. Wills & Co has been authorised by the FSA since 1 December 2001 having previously been regulated by the Personal Investment Authority since 8 August 1994. Wills & Co is an authorised person under the Act with permissions granted for the regulated activities of advising, arranging deals in investments, arranging safeguarding and administration of assets, dealing in investments as agent, dealing in investments as principal, making arrangements and causing dematerialised instructions to be sent.

4.3. Wills & Co is a stockbroking firm and maintains contact with its customers primarily by telephone. Its current business involves advising and dealing as principal in securities that are trading, or seeking admission to trade, on the Alternative

Investment Market ("AIM") and as agent in securities trading on the main market.[2] Wills & Co also deals and advises in the securities of some unlisted companies.[3] AIM specialises in providing primary and secondary trading services for smaller capitalised and/or emerging companies ("small cap securities").

4.4. During the Relevant Period, Wills and Co employed six individuals who held significant influence functions, 24 who held Controlled Function 21 (investment adviser) and 16 who held Controlled Function 22 (trainee investment adviser).

FSA Supervisory Visit

4.5. The FSA's Small Firms Division ("SFD") visited Wills & Co on 11 and 12 October 2006 and conducted a focused on-site review of its small cap securities business. The visit revealed a number of concerns with Wills & Co's selling practices of small cap securities, the information provided to customers and its systems and controls. As a result, the matter was referred to the FSA's Enforcement Division and investigators were appointed on 19 January 2007.

The Securities

4.6. The Securities sold by Wills & Co were all trading on AIM at the point of sale.

4.7. The FSA's findings are based on the results of a detailed review of the recorded telephone calls and customer records relation to 17 transactions in the Securities during the Relevant Period ("the 17 transactions reviewed").

4.8. During the Relevant Period, Wills & Co made a gross profit of £17,216.25 on the sale of the Securities in the 17 transactions reviewed. During the Relevant Period, Wills & Co recorded a total of 8,735 sales of small cap securities to 3,915 different customers, involving 116 different issuers, totalling £28,495,198.

4.9. Insofar as the findings in this Notice relate to Wills & Co's sales practices, they are based only on the 17 transactions reviewed which involved advising and recommending the Securities in the Relevant Period, as set out in paragraph 2.1 above.

5. BREACHES OF THE REGULATORY REQUIREMENTS

Breach of COB 5.4.3R and Principle 7

5.1. During the Relevant Period, advisers were required to provide a risk warning in accordance with COB 5.4.3R ("the Required Risk Warning"). By reason of the facts

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[2] The Main Market is defined within this Notice as the market for companies of the London Stock Exchange (LSE), sometimes known as the Official List.

[3] For the avoidance of doubt, this action is only concerned with Wills & Co's conduct whilst advising and dealing in the Securities during the Relevant Period. The transactions reviewed by the FSA relate to AIM securities.

and matters set out in paragraphs 5.2 and 5.3, Wills & Co breached COB 5.4.3R. In addition, by reason of the facts and matters set out in paragraphs 5.4 to 5.11, Wills & Co breached Principle 7 as it did not pay due regard to the information needs of its customers and communicate information in a way that was clear, fair and not misleading.

Failure to take reasonable steps to provide the Required Risk Warning and pay due regard to the information needs of customers regarding the Securities

5.2. Wills & Co were required to take reasonable steps to ensure that customers understood the Securities (which presented particular and higher risks to customers) and the nature of the associated risks. This includes providing customers with the Required Risk Warning, which Wills & Co failed to provide in all of the 17 transactions reviewed.

5.3. The Required Risk Warning is important as it would have made customers aware, amongst other things, that there is an extra risk of losing money when purchasing securities of some smaller companies including penny shares. There is a big difference between the buying price and the selling price of these securities meaning if they have to be sold immediately the customer may get back much less than they paid for them; and the price of the securities may change quickly and it may go down as well as up.

5.4. In addition, in all of the 17 transactions reviewed, Wills & Co did not pay due regard to its customers' information needs as it communicated largely cursory risk information, which did not give due prominence to the higher risks of the Securities. Instead, Wills & Co relied upon written disclosure to explain to the customer the risks of the Securities. In particular, investment advisers simply advised customers, in a rushed manner, that the warning in its Terms of Business applied to the recommendation and they did not provide any specific risk information for each of the Securities. The Terms of Business were sent to customers at the commencement of their relationship with Wills & Co and the risk information in its Terms of Business would not have been immediately evident and/or accessible during the course of each recommendation. Clear, fair and prominent disclosure immediately prior to and at the time the customer decided to purchase the Securities would have helped the customer to understand the high risk nature of the Securities.

5.5. The abovementioned failures are serious as clear communication, including a fair and adequate explanation of the investment risks, before and at the point of sale, are essential to ensure customers understand the higher risks and characteristics of each of the Securities.

Failure to communicate information about the Securities in a way that was clear, fair and not misleading

5.6. Wills & Co communicated certain information about the Securities in a rushed and unclear manner, which meant that important information was conveyed in an ambiguous and/or confusing way. Although Wills & Co had in place a procedure which required its investment advisers to provide to customers certain information about the Securities as set out in its "Principal Dealing Slip" ("the PDS procedures"),

the 17 transactions reviewed revealed that the following types of information were not always communicated clearly, fairly and in a manner that was not misleading. In particular:

(1) in each of the 17 transactions reviewed Wills & Co failed to communicate clearly the "mark up" on the Securities, this being the difference between the price at which Wills & Co took a principal position in the Securities and the price, of the Securities, at which the transaction was executed for the customer. In particular, investment advisers hurriedly disclosed the two prices after the customer had agreed to purchase the Securities thereby obscuring the exact amount of the "mark up" that Wills & Co would make on the sale. As a result, customers may not have been aware of the nature and extent of the mark up on the Securities, which actually ranged from 23.44% to 66.67%;

(2) in eight of the 17 transactions reviewed, investment advisers provided customers with either unclear or misleading explanations about the principal position that Wills & Co held in the Securities. In particular instances, investment advisers stated that a principal position meant that Wills & Co could purchase large and discounted volumes of securities and pass the discount onto the customer. Alternatively, some of these customers were simply told they needed to understand the difference between an agency and principal trade but were not provided with an explanation or sufficient information in order to gain that understanding. As a result, customers may not have been aware of the potential conflict of Wills & Co selling as principal;[4] and

(3) in three of the 17 transactions reviewed, despite the customer already holding a material amount of their net assets in small cap securities, the investment adviser only informed customers of the their total level of risk exposure after they had agreed to purchase the Securities. As a result, these customers were not able to assess or identify their overall level of risk exposure and assess the potential loss of their total investment with Wills & Co before agreeing to purchase the Securities.

5.7. In many instances, the abovementioned information and/or the information required by the PDS procedures was only provided to customers after they agreed to purchase the Securities and/or was then provided in such a rushed way that its importance was diminished. Such information is important as it ensures that customers are provided with a fair and adequate explanation of the Securities prior to and/or at the time of making decisions to purchase higher risk securities.

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[4] For the avoidance of doubt, a Principal Trade is an order carried out by an investment adviser which involves the investment adviser buying or selling securities on behalf of a Firm's own account and at its own risk. However, an Agency Trade is executed by an investment adviser on behalf of and under the instruction of a customer. The investment adviser does not act in a principal capacity and may be compensated by a commission or fee (which must be disclosed to the party for whom it is acting) rather than by a mark-up.

5.8. Wills & Co also failed to provide customers with balanced information about the Securities in all of the 17 transactions reviewed. In particular, customers were provided with information about unrelated securities (which was also inadequate) and, in certain instances, investment advisers sought to accentuate the benefits of investing in the Securities. For example:

(1) in four of the 17 transactions reviewed, Wills & Co provided unbalanced and unclear information about the past performance of unrelated securities it had previously recommended to support an indication of future performance of the Securities. Past performance of unrelated securities is not an indicator of future performance of the Securities, especially where there are no direct business or commercial factors in common with the Securities and it is not balanced against small cap securities that did not perform as predicted; and

(2) in one of the 17 transactions reviewed, Wills & Co communicated unsupported information about its expectations of the performance of one of the Securities. In particular, the customer was advised that the price of the security would increase by 40% over a six-month period. No publicly available information indicated or anticipated such an increase nor could the accuracy of the statement be substantiated.

5.9. The abovementioned conduct is serious as it created an unrealistic expectation of the potential performance of the Securities without also giving a fair indication of the associated risks. Such statements may have unduly influenced a customer's decision to purchase the Securities.

Failure to communicate information about charges in a way that was clear, fair and not misleading

5.10. Wills & Co make a £15 compliance charge for the clearing service provided to customers. This charge is waived for the first three trades executed by a new customer. Wills & Co failed to communicate information about this charge in a way that was clear, fair and not misleading. In particular:

(1) in ten of the 17 transactions reviewed, customers were advised that the transaction was "commission free" or stated that there is no commission payable by the client. Such statements may have led customers to believe that there were no additional charges or fees for the transaction, particularly in circumstances where the nature and extent of the mark up, on the Securities, was also not explained. However, as previously indicated Wills & Co applied a mark up to the initial costs of the Securities; and

(2) in two of the 17 transactions reviewed customers were advised that because the transaction was "commission free" they should purchase more of the Securities. However, the customer was not advised that, in reality, the amount saved was a fixed amount that was not dependent on, or proportionate to, the number of securities being purchased.

5.11. The abovementioned information is important as customers need to be made aware of the costs to them, directly or indirectly, in order for them to make an informed choice about purchasing the Securities and engaging the services of Wills & Co.

Breach of Principle 3

5.12. By reasons of the facts and matters set out in paragraphs 5.13 to 5.17, Wills & Co breached Principle 3.

Failure to take reasonable care to implement adequate compliance monitoring arrangements and controls covering its small cap securities business

5.13. Despite recommending higher risk securities, Wills & Co did not establish and implement comprehensive compliance arrangements and did not have in place an adequate monitoring programme to cover its business of small cap securities to ensure compliance with the FSA's regulatory requirements. The compliance monitoring process was inadequate because:

(1) the number of transactions reviewed was not proportionate to the overall volume of monthly small cap securities sales. Each month, Wills & Co reviewed only five sales for each trainee investment adviser (CF22) and three sales for each investment adviser (CF21) it had classified as competent. This was inadequate given the high number of small cap securities sales it conducted per month and the fact that it conducted a higher risk business;

(2) Wills & Co failed to demonstrate that it assessed all aspects of its business against the regulatory requirements and this, combined with its inadequate compliance monitoring rate, meant that it was not able to identify failures to adhere to these requirements and/or its own internal procedures. As a result, it was unable to ensure that all regulatory rules were complied with;

(3) the extent and scope of its compliance monitoring undertaken was not risk based nor did it consider the risk that each investment adviser posed to its business. For example, Wills & Co failed to undertake increased monitoring of individual investment advisers that were identified as posing particular and higher risks to its business; and

(4) Wills & Co failed to identify that customers were not always being provided with appropriate information about investing in the Securities and that many investment advisers were not complying with its own internal standards.

5.14. Wills & Co had a Compliance Manual which stipulated the role of its Compliance department. However, it did not have documented procedures in relation to the extent and scope of the monitoring to be undertaken, the sampling methodology used to identify calls for review and/or the associated risks to all aspects of its business. As a result, Wills & Co was unable to ensure consistency in its approach to monitoring and identifying the risks to its business.

5.15. Wills & Co recorded summary details of calls reviewed in a spreadsheet and it summarised general findings in a monthly report. However, there were no central records amalgamating the issues and/or any compliance failings that might be

identified nor could it establish that it conducted trend analysis reporting. As a result, it was unable to identify fully the ongoing and emerging regulatory risks facing its business.

5.16. Wills & Co produced monthly compliance monitoring reports, a breach register and an action log. However, these lacked significant detail, containing summary results, with limited details of the compliance monitoring conducted, the findings identified and/or any remedial action taken. As a result, there was insufficient and inadequate information to allow Wills & Co to identify, measure and manage properly all regulatory risks nor could it be sure that it was fully aware of risks as and when they arose.

5.17. Wills & Co did not conduct comprehensive assessments and/or analysis of the findings of its compliance monitoring work. Whilst it had procedures in place that sought to address individual adviser failings by getting advisers to call customers and correct any errors/omissions and/or fining advisers, in practice, it was unable to demonstrate that appropriate action had been taken and/or the identified failings had been remedied. As such, it could not ensure that issues of regulatory concern regarding all aspects of its business and/or failings were dealt with appropriately and/or in a timely fashion.

6. RELEVANT GUIDANCE ON PENALTY

6.1. The FSA's general approach in deciding whether to take action and the imposition and amount of penalties is set out in Chapter 6 of the Decision Procedure and Penalties Guide ("DEPP"), which is part of the Handbook of Rules and Guidance. The principal purpose of imposing a financial penalty is to promote high standards of regulatory conduct by deterring firms and approved persons who have breached regulatory requirements from committing further contraventions, helping to deter other firms and approved persons from committing contraventions and demonstrating, generally, to firms and approved persons, the benefit of compliant behaviour (DEPP 6.1.2G).

6.2. In determining whether a financial penalty is appropriate and proportionate, the FSA will consider all the relevant circumstances of the case. DEPP 6.5.2G sets out guidance on a non-exhaustive list of factors that may be of relevance in determining the amount of a financial penalty, which include the following:

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

6.3. The FSA had regard to the seriousness of the contraventions by Wills & Co, including the nature of the requirements breached and the duration of the breaches. For the reasons set out in paragraph 2.3 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: DEPP 6.5.2G (5)

6.4. The FSA has taken into account Wills & Co's financial resources. Wills & Co's total revenue for the 12 months ending 31 December 2006 was £12,083,399 and its profit before tax for the same period was £3,775,211.

6.5. There is no evidence to suggest that Wills & Co is unable to pay the level of financial penalty imposed on it.

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

6.6. The FSA has had regard to the £17,216.25 profits that Wills & Co made on the 17 transactions reviewed during the Relevant Period.

Conduct following the breach: DEPP 6.5.2G (8)

6.7. As set out in paragraph 2.4 above, the FSA has taken into account Wills & Co's significant co-operation and its willingness to take all reasonable steps to satisfy the FSA that it will seek to comply with regulatory requirements on an on-going basis.

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

6.8. Wills & Co has not previously been the subject of disciplinary action by the FSA.

Previous action taken by the FSA: DEPP6.5.3G (10)

6.9. The FSA seeks to ensure consistency when it determines the appropriate level of financial penalty. The FSA has in the past taken action against firms for similar findings and these have been taken into consideration in setting the level of financial penalty against Wills & Co.

7. DECISION MAKERS

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

8. IMPORTANT

8.1. This Final Notice is given to Wills & Co under in accordance with section 390 of the Act.

Manner and time for payment

8.2. The financial penalty must be paid in full by Wills & Co to the FSA by no later than 14 November 2007, 14 days from the date of the Final Notice.

If the financial penalty is not paid

8.3. If all or any of the financial penalty is outstanding on 15 November 2007, the FSA may recover the outstanding amount as a debt owed by Wills & Co and due to the FSA.

Publicity

8.4. Sections 391(4), 391(6) and 391(7) of the Act apply to the publication of information about the matter to which this notice relates. Under those provisions, the FSA must publish such information about the matter to which this notice relates as the FSA considers appropriate. The information may be published in such manner as the FSA considers appropriate. However, the FSA may not publish information if such publication would, in the opinion of the FSA, be unfair to Wills & Co or prejudicial to the interests of consumers.

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

FSA contacts

8.6. For more information concerning this matter generally, please contact Stephen Robinson (direct line: 020 7066 1338) of the Enforcement Division of the FSA.

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Georgina Philippou
Head of Department
FSA Enforcement Division