
FIRST SUPERVISORY NOTICE

To: CFS Management Ltd

Reference Number: 171480

Address: 55 Riding House Street, London, W1W 7EE

Date: **16 March 2023**

1 ACTION

1.1 For the reasons given in this First Supervisory Notice, and pursuant to section 55L(3)(a) of the Financial Services and Markets Act 2000 ("the Act"), the Financial Conduct Authority ("the Authority") has decided to impose the following requirements ("the Requirements") on CFS Management Ltd ("Firm") with immediate effect.

Business Requirements

1. CFS must not accept any new client money or new custody assets, whether from existing or new clients, in any of its business areas.
2. Paragraph 1 above does not apply to the acceptance of new monies or custody assets from existing clients and/or third parties by CFS as a result of or in relation to the following:
 - a. receipt of dividends or coupons;
 - b. rights issues;
 - c. corporate actions including maturing bonds; and
 - d. settlement of trades instructed but not yet settled as at the date of the Requirements.

Asset Requirements

3. CFS must not, without the prior written consent of the Authority, and save as provided for in paragraph 2 above or 4 below, in any way dispose of, withdraw, transfer, deal with or diminish the value of any of its own assets, and any client money and custody assets it holds for clients (whether in the United Kingdom or elsewhere). For the avoidance of doubt, this requirement includes any custodian accounts, client transaction accounts or any other account operated by or held with third parties on CFS's behalf.

4. Paragraph 3 does not apply to:
 - a. monetary payments made by CFS of its own monies, in the ordinary
 - b. course of business, amounting to no more than £5,000 whether as a single transaction or as a combination of related transactions; or
 - c. payment of legal fees in relation to this Notice.

5. For the avoidance of doubt paragraphs 3 and 4 above are an assets requirement within the meaning of section 55P(4)(a) of the Act.

CASS Arrangements

6. By 5pm on 30 March 2023 the Firm must:
 - a. put in place appropriate client bank account segregation arrangements, with each account having the necessary acknowledgement letter in place; and
 - b. provide evidence to the Authority that the appropriate client bank account arrangements are in place, including providing copies of the necessary acknowledgment letters.

7. By 5pm on 23 March 2023 the Firm must submit to the Authority a plan ("the Plan"), to be approved by the Authority, that clearly explains how it will return all client money and custody assets held for its clients in the event that the Firm is unable to meet the Requirement set out in paragraph 6. This will include:
 - a. the process it will use to determine the amount due back to each client;
 - b. a statement as to whether client consent is required in order for client money and assets to be returned;
 - c. an explanation of how the Firm will hold client money and assets for clients in the event that client consent, as detailed in paragraph 6(b) is not forthcoming;
 - d. a timescale for the return of client money and assets.

8. Where the Firm has identified within the Plan, in accordance with paragraph 7(b) that client consent is required in order to return client money and assets, it must seek consent from those clients to which this applies and provide to the Authority by 5pm on 30 March 2023:
 - a. a list of all clients from whom it has obtained consent, or
 - b. for those clients for whom consent has not yet been obtained, an explanation of the steps taken by the Firm to seek to obtain consent together with a copy of any communications sent by the Firm to those clients.

9. If the Firm fails to satisfy the Authority by 5pm on 30 March 2023 that it has met the requirements contained within paragraph 6, the Authority will provide confirmation ("the confirmation") to the Firm whether the Firm must follow the steps laid out within the Plan. Once the Firm has received the confirmation, the Firm must:
 - a. for those clients who have provided consent, return client money and / or assets within two business days of the confirmation;
 - b. for those clients who have not provided consent, hold the client money and / or assets in accordance with the steps set out within the plan;
 - c. submit to the Authority, within three business days of the confirmation, a table containing the following information:
 - i. the clients to whom funds have been returned, including details of the amounts returned to those clients; and

ii.the clients to whom funds have not been returned, including details of the amounts still held for those clients and the account details of the accounts the funds are held in.

10. By 5pm on 20 March 2023, CFS must provide the Authority for approval a draft notification to be set to its clients, custodians, sub-custodians and to be placed on its websites setting out the terms and effects of these Requirements.

11. By 5pm 2 business days from receiving the Authority's approval of the communications (required by paragraph 10) CFS must notify in writing:

- a. all its clients;
 - b. the custodians of all assets held or managed by CFS (including, for the avoidance of doubt, its own funds); and
 - c. the sub-custodians of all assets held or managed by CFS (including for the avoidance of doubt, its own funds);
- of the terms and effects of these Requirements.

12. By 5pm 2 business days from receiving the Authority's approval of the communications (required by paragraph 10) CFS must publish a notice in a prominent place on all of its websites setting out the terms and effects of these Requirements.

13. Once the notifications referred to in paragraphs 11 and 12 have been made, CFS must provide to the Authority:

- a. copies of the template notification sent to all clients, custodians and sub-custodians;
- b. a list of all parties, with their contact details, to whom notifications have been sent pursuant to paragraph 11; and
- c. confirmation that, to the best of its knowledge, CFS has sent notifications pursuant to paragraph 11 to all relevant parties.

14. CFS must secure all books and records and preserve information and systems relating to regulated activities carried on by it and must retain these in a form and at a location, to be notified to the Authority in writing no later than 7 days after the coming into effect of these Requirements, such that they can be provided to the Authority, or to a person named by the Authority, promptly on its request.

15. The SMF3 and SMF16 of CFS Management Ltd shall send to the Authority by email by 12 noon every Tuesday and Friday, until such time as it is notified otherwise in writing by the Authority:

- a. written confirmation that CFS is acting in compliance with the Requirements at paragraphs 3 and 5;
- b. daily bank statements for all CFS firm and client bank accounts;
- c. daily account statements from all custodians or sub-custodians holding custody assets on behalf of CFS; and
- d. a list of holdings per client

1.2 These Requirements shall take immediate effect and remain in force unless and until varied or cancelled by the Authority (either on the application of the Firm or of the Authority's own volition).

2. REASONS FOR ACTION

Summary

- 2.1 The Authority has concluded, on the basis of the facts and matters described below that, in respect of the Firm, it is necessary to exercise its power under section 55L(3)(a) of the Act to impose the Requirements on the Firm because it is failing, or is likely to fail, to satisfy the Threshold Conditions and it is desirable in order to advance one or more of the Authority's operational objectives, which includes securing an appropriate degree of protection for consumers and protecting and enhancing the integrity of the UK financial system.
- 2.2 The Authority has serious concerns relating to the Firm's business and its compliance with the Authority's Principles for Businesses ("PRIN") and the rules in the Authority's Client Assets Sourcebook ("CASS"). In particular, the Authority is concerned that:
- a. The Firm has failed to ensure that client money is held in a properly segregated client money account in breach of the rules in CASS 7.13.3R, 7.13.6R and 7.13.12R.
 - b. The Firm has acknowledged that at present firm money and client money may be held in the same accounts, in breach of the rules in CASS 7.13.12R.
 - c. The Firm has failed to obtain appropriate acknowledgment letters for client bank accounts where client money is held, in breach of the rules in CASS 7.18.2R and 17.18.6R. For example, the Firm had merged the templates in CASS 7 Annex 2 and 3 and amended the prescribed contents of the client bank account letter and client transaction account letter in a way that is not permitted by CASS.
 - d. The Firm has failed to appropriately remediate the CASS failings identified in the feedback letter of March 2022 and has failed to take steps to mitigate the risks that such a failure to remediate poses to client assets and money.
 - e. The Firm has failed to put appropriate resources and systems in place to manage the risks created by its breach of the CASS rules.
 - f. The Firm may be in breach of Principle 3 of PRIN, requiring it to take reasonable care to organise and control its affairs responsibly and effectively and ensure that it has adequate risk management systems to effectively manage risks with its business.
 - g. The Firm may be in breach of Principle 10 of PRIN, requiring it to arrange adequate protection for clients' assets when it is responsible for them.
- 2.3 The Authority considers that imposition of the Requirements should take immediate effect because the matters set out in this First Supervisory Notice demonstrate that the Firm is unable to manage its affairs in a sound and prudent manner and is putting consumers at risk.

3. DEFINITIONS

3.1 The definitions below are used in this First Supervisory Notice:

“the Act” means the Financial Services and Markets Act 2000;

“AIF” means an alternative investment fund;

“the Authority” means the Financial Conduct Authority;

“CASS” means the Client Assets Sourcebook rules, contained with the Handbook;

“CMAR Return” means Client money and assets reporting return made to the Authority;

“the Firm” or “CFS” means CFS Management Ltd;

“FRC” means the Financial Reporting Council;

“P2P” means peer to peer;

“H2” means the second half of the fiscal year from October through to the following March;

“Handbook” means the Authority’s online handbook of rules and guidance (as in force from time to time);

“PRIN” means the Authority’s Principles for Business, contained with the Handbook;

“Requirements” means the terms imposed on the Firm by this First Supervisory Notice as outline in section 1 above;

“SUP” means the Supervision Sourcebook, contained the in Handbook; and

“Tribunal” means the Upper Tribunal (Tax and Chancery Chamber).

4. FACTS AND MATTERS

Background

4.1 CFS is an authorised Wealth Manager and Retail Investment Broker. The Firm has been authorised since 1 December 2011 and currently has permission to conduct the following investment-related regulated activities:

- a. Safeguarding and administration of assets
- b. Arranging safeguarding and administration of assets
- c. Advising on investments (ex-pension transfer/opt outs)
- d. Managing investments

- e. Dealing in investments as agent
- f. Arranging deals in investments
- g. Making arrangements with a view to transactions in investments
- h. Managing an unauthorised AIF
- i. Advising on P2P arrangements

4.2 The Firm has traded as CFS Management Ltd since January 2018, previously trading as CFS Portfolio Management Ltd. The Chief Executive (CEO) has been an approved person at the Firm since from 19 September 2019: first as CF3 (Chief Executive), then from 8 December 2019 as SMF1 (Chief Executive). The CEO has been SMF17 (Money Laundering Reporting Officer) at the Firm since 10 May 2020. The CEO assumed control of the Firm on 25 June 2021.

4.3 The Firm have not had an SMF16 (Compliance Oversight Function Holder) since 13 January 2020. An application for approval of an SMF16 was received from the Firm by the Authority on 17 November 2021. This application remains under consideration. The SMF16 applicant is referred to as Head of Compliance on the Firm's organogram, and appears to have been working for the Firm in this role since May 2021.

4.4 As at 7 March 2023, the Firm had 91 active clients, to whom it provides execution-only services. The Firm has categorised 90 of these clients as professional clients and one as a professional counterparty. The Firm has two custody clients. Of the 91 clients, 45 are individuals and 46 and corporate entities.

4.5 The Firm's client money has reduced significantly since the start of 2023. The Firm reported that it held £13.8m client money on 31 January 2023. This was reduced to £10,087,517 as at the end of February 2023. By 10 March 2023, this had reduced to £2,437,290. The Firm informed the Authority that as 13 March 2023 the client money of £1.4m remaining within one its bank accounts has been withdrawn. The Firm did not specify where it had been withdrawn to. If it has been returned to clients, this would take the total client money held by CFS as at 13 March 2023 to under £1m.

4.6 The Firm has one appointed representative ("AR"), which had a net equity of £7,703 for the year ended 30 June 2022.

Failings and risks identified

Rules and Guidance applicable to CASS firms

4.7 The rules in CASS provide important protections for client money and assets, including keeping these safe if a firm fails and/or exits the market. The purpose of CASS is to ensure that an appropriate level of protection is provided for those assets over which a client gives a firm certain rights. CASS 7 contains the client money rules. These include:

- a. CASS 7.13, segregation of client money: A firm using the normal approach to client money must ensure that all client money it receives is paid directly into a client bank account (CASS 7.13.3R, CASS 7.13.6R). A firm must take necessary steps to ensure that the client money is held in an account identified as a separate account to that used to hold firm money (CASS 7.13.12R).
- b. CASS 7.15, records, accounts and reconciliations: A firm must keep records and accounts to enable it, at any time and without delay, to distinguish client money held for one client from client money held for any other client, and from its own money (CASS 7.15.2R) and allow them to be used as an audit trail (CASS 7.15.3R). Internal client money reconciliations must be performed each business day (CASS 7.15.15R).
- c. CASS 7.18, acknowledgment letters: For each client bank account, a firm must obtain a countersigned acknowledgement letter from the bank agreeing the terms and clearly identifying the client bank account. A firm must not hold or receive client money into a client bank account unless it has received the countersigned acknowledgement letter, which must be in compliance with the template (CASS 7.18.2R, CASS 7.18.6R). The purpose of this is to put the bank on notice that client money has been deposited, to ensure that the client bank account has been opened in the correct form and is distinguished from any account containing money held by the firm, and to ensure that the bank agrees that it will not have any right against the client money (CASS 7.18.1G).

4.8 A "Dear CEO Letter" dated 30 September 2020 was sent to CASS firms (including the Firm), reminding firms that it was *"imperative that the firm continues to maintain adequate arrangements that safeguard the client money and/or custody assets it holds for customers"*. Firms were asked to discuss the contents of the Dear CEO Letter with their boards and agree what further action was necessary to ensure that adequate arrangements were in place, in particular in relation to, amongst other things, governance and oversight, adequate records and reconciliations, and acknowledgement letters for all client money accounts.

4.9 A CASS firm is responsible for appointing an external auditor (Rules 3.1.1R, 3.3.2R of the Supervision Sourcebook ("SUP")). SUP 3.2.1G clarifies that the purpose of requiring auditor reports from CASS firms is that *"Auditors act as a source of information for the appropriate regulator in its supervision. They report, where required, on the financial resources of the firm, the accuracy of its reports to the appropriate regulator and its compliance with particular rules such as client asset rules"*. CASS auditors are subject to specific rules as set out within SUP 3.10.

CASS Concerns

4.10 On 30 October 2020, the Authority commenced a remote desk-based assessment of the Firm's CASS arrangements ("the assessment"). This was undertaken because the Firm had not had previous CASS contact, as it was new to the CASS regime in 2019, and the Authority had identified the Firm was loss making in the previous two reporting periods which can place client money at an enhanced risk.

4.11 As a result of the assessment, the CASS team identified several concerns in relation to the Firm's CASS compliance. On 23 February 2022, CASS held a telephone call with the

Firm during which it outlined the key findings from its assessment. During that call, the Firm provided some initial indications of the actions it would take to address the CASS team's findings.

- 4.12 On 28 March 2022, a feedback letter ("the feedback letter") was sent to the Firm, setting out the Authority's concerns in relation to the Firm's CASS compliance, and the steps which the Firm was required to take to remediate these concerns. The feedback letter stated that the Authority's *"findings indicate significant weaknesses in the Firm's CASS risk framework and its systems, governance, and controls"*. Key feedback provided in the feedback letter is set out in the table below:

Feedback	Action for Firm and deadline to achieve action
<i>Records and reconciliations</i>	
The Firm's amended internal and external client money reconciliation procedures had not been adequately assessed to ensure full CASS 7 compliance.	Engage external resources to commence a review of its CASS arrangement. To confirm to the Authority by 29 April 2022 who the Firm has engaged and the scope of this review.
<i>Segregation of client money: acknowledgment letters</i>	
<p>The Firm does not have appropriate client bank account and client transaction account arrangements in place. <i>"We have raised this issue with the industry before via our 'Dear CEO Letter and therefore deem your inability to comply with our requirements to be a significant failing of the CASS and SYSC rules"</i>.</p> <p>The two acknowledgment letters provided for client transaction accounts were not compliant.</p> <p>No acknowledgement letters were provided for the two client money bank accounts.</p>	<p>Immediately review client bank accounts and the client transaction account to ensure client money is held with compliant acknowledgement letters and update any that require amendment or are missing.</p> <p>Provide a client money bank account and transaction list, client money bank statements, and copies of all acknowledgement letters (if the Firm does not have acknowledgement letters for any client money accounts, it must provide evidence demonstrating that it is in the process of obtaining them) within 5 days of receipt of the feedback letter</p>
<i>Outstanding CASS audit</i>	
Failure to obtain a CASS audit for the period ending 31 March 2021	<p>Provide contact details for the external auditor to discuss the outstanding 2021 client assets report.</p> <p>Be fully compliant with its obligation to ensure that its client assets report for 2022 is received within four months of its period-end date.</p>

	Firm put on notice that if there was any further delay in the Authority receiving the Firm's 2021 client assets report past 29 April 2022 , the Authority may consider the use of further regulatory tools against the Firm.
<i>Governance and oversight</i>	
<p><i>Financial Reporting Council (FRC) CASS Assurance Standard (FRC rule mapping)</i></p> <p>All firms are required to have completed FRC rule mapping.</p> <p>The FRC rule allows the Firm to identify and record where CASS rules are and are <u>not</u> applicable to the Firm and to map the CASS risks and controls to each CASS rule.</p>	<p>Confirm if FRC rule mapping has been completed. If the Firm has not yet completed its FRC rule mapping the Firm should seek to do so immediately.</p>
<p><i>Resources</i></p> <p>During the initial assessment in 2021 the Authority identified that the Firm was operating with resourcing deficiencies</p>	<p>Implement robust knowledge and training procedures to ensure its staff have and retain an appropriate level of CASS knowledge.</p> <p>Review its previous analysis and the contents of the feedback letter to ensure that all areas that required improvements/amendments are appropriately remediated.</p>

4.13 Following the feedback letter being sent, the Authority continued to engage with the Firm in relation to actions required by the feedback letter:

Action	Response from Firm
<p>28 March 2022: Feedback letter sent to Firm with due date for response of 29 April 2022</p>	<p>12 April 2022: Firm acknowledges receipt of the feedback letter.</p> <p>The items requested to be provided by the Firm within five days receipt of the feedback letter were not provided (nor were they provided at a later date).</p> <p>The Firm's CEO states that Bank A had agreed to open a segregated client account for the Firm and that he would share the CASS 7 acknowledgment letter once received.</p>
<p>12 April 2022: Authority confirmed receipt of the Firm's email and reminded the Firm that a full response</p>	<p>Firm fails to respond to feedback letter by due date of 29 April 2022.</p>

was due by 29 April 2022.	
21 December 2022: Authority email to the CEO chasing for 29 April 2022 response and the late CASS Audit for 2022, providing a deadline of 30 December 2022 for a response.	Firm does not respond by deadline of 30 December 2022.
-	6 January 2023: Firm's CASS audit report for the period ending 31 March 2021, due on 31 July 2021 and requested in 21 December 2022 email, was received by the Authority.
17 January 2023: Call to CFS chasing for response to 21 December email.	17 January 2023: Firm emails asking for email of 21 December 2022 to be resent as not received.
18 January 2023: Authority resends email of 21 December 2022, with a new deadline of 1 February 2023.	1 February 2023: Firm response to the Authority

4.14 The email received from the Firm on 1 February 2023 included the following key points:

- a. The Firm acknowledged that the deadlines for the 2021 and 2022 CASS audit reports had been missed. The Firm stated that this was due to "*misrepresentations*" from the respective auditors and that "*CFS foresee that the delay is shortening in a rapid manner thus making 2023 report to be submitted on time*" [sic].
- b. Reconciliation training took place on 26 May 2022. The team at the Firm looking after CASS matters consisted of four people. Some changes had been made to the Firm's documents to reflect recommendations from the Firm's auditors on reconciliations.
- c. An application for approval of the SMF16 had been submitted to the Authority.
- d. Segregated client accounts were set-up with Bank A on 15 September 2022. A professional client account was opened with a separate bank on 15 December 2022. The Firm was awaiting a revised acknowledgment letter (the current version was attached). The Firm had initiated onboarding with two other banks to obtain segregated client accounts, one European (for EUR) and one a British bank (for GBP). The Firm believed that this combination of actions would "*be sufficient to cover any and all requirements for proper segregation of client money and assets supported by CASS 7 Acknowledgment Letters*".

4.15 On 22 February 2023, in response to a request from the Authority, the Firm stated that the Firm's client numbers had increased from 31 in February 2021 to 97 at the end of January 2023.

- 4.16 On 28 February 2023, the Authority held a meeting (“the February meeting”) with the Firm to discuss its business model and CASS arrangements. During the February meeting, the Firm provided the following comments on CASS issues which had been raised in the feedback letter:
- a. *Issue raised in the feedback letter:* Firm does not have separate client bank account, does not segregate client money appropriately, and acknowledgement letters are non-compliant. The Firm responded that:
 - (i) Bank A “*hadn’t progressed to the level they wanted*” and the Firm had not started operating this account. The Firm said it was waiting for [an acknowledgment] letter from Bank A and that it would send this [to the Authority]. This letter had been signed and the Firm was in the position to move funds to client accounts. It was “*waiting for [Bank A] to segregate the money*”.
 - (ii) It was “*being transparent*” and that it “*is struggling with client accounts*”.
 - (iii) The accounts held were not segregated client money accounts. One of these held \$13.1m.
 - (iv) In relation to the accounts shown on the Firm’s CMAR return, “*the accounts may hold both firm and client money.*”
 - b. *Issue raised in the feedback letter:* Firm unable to demonstrate how client money reconciliations were performed, and to engage external resources to commence a review of its CASS arrangements.
 - (i) The Firm responded during the February meeting that the third-party CASS review has not been completed.
 - c. *Issue raised in the feedback letter:* Firm was to confirm if FRC rule mapping had been completed.
 - (i) The Firm responded in the February meeting that this was “*ongoing but not complete.*”
- 4.17 On 6 March 2023 the Firm responded to a further information request from the Authority, stating that:
- a. client money held at the end of February 2023 was £10,087,517.28 and that this is the figure that the Firm expected to report on their CMAR;
 - b. the Firm was progressing communications with a compliance for an external review of CASS (and wider regulatory) compliance;
 - c. it was planning to contact clients about withdrawing their funds from the Firm until the Firm completed the process of putting in place new CASS 7 compliant client money acknowledgment letters, remediating existing acknowledgment letters from Bank A, and reviewing the accounts held with two other institutions.

- 4.18 On 13 March 2023, the Firm provided copies of the Exante and Saxo acknowledgment letters. These have been reviewed CASS: both are for client transaction accounts, and should not be used for the holding of client money.
- 4.19 The Firm's CASS audit report for the period ending 31 March 2022, which was due by 31 July 2022, remains outstanding as at 10 March 2023.

"First mover advantage"

- 4.20 Where a firm does not have appropriate segregated client bank accounts with acknowledgment letters in place, client money is not properly protected. This means that if there is a client money shortfall (i.e. the client money reconciliation identifies a client money deficit), and the firm cannot remediate it as it does not have enough firm funds to do so, then the firm is insolvent and under the CASS rules this creates a "pooling event" as the firm enters insolvency. This means that the resulting shortfall should be apportioned equally across all clients.
- 4.21 Supervision is concerned about the risk that if the Firm pays out client money in the interim, this may create *"first mover advantage,"* whereby those clients who are paid first may receive all their money, whereas those clients paid later may receive less as the "pool of assets" becomes smaller (as the costs associated with an insolvency would also be paid for from the pool).
- 4.22 In a call on 9 March 2023, the Authority asked the Firm not to seek to return any client monies to clients while the CASS issues were being resolved.
- 4.23 On 13 March 2023, the Firm informed the Authority that its client money holdings as of 10 March 2023 were £2,437,290 (down from £10,087,517 as at 23 February 2023). The CEO stated that the decrease in client funds *"was mainly to the fact of my initial discussion with clients in relation to their funds withdrawal. the discussion took place prior to our call last Thursday [9 March 2023], so I was not able to stop them withdrawing their funds as discussed with you"*.
- 4.24 The Authority has serious concerns that the Firm appears to have returned more than £7.5m of client monies between 23 February and 10 March 2023, with the CEO indicating by email on 13 March 2023 that this was after the 9 March call (when the Firm was asked not to seek to return funds). The Authority therefore has concerns that the risk of *"first mover advantage"* and dissipation of client monies is active and ongoing.
- 4.25 The Authority's has identified that several of the Firm's clients appear to have links to the Firm or the Firm's CEO (the "connected clients"). The CEO is himself also a client of the Firm. The value of each client's assets with the Firm is unknown and has not been requested from the Firm at this stage. However, this compounds the Authority's concerns in relation to *"first mover advantage"* as funds may be paid to the connected clients in advance of others.

Risk and control framework Not Commensurate with Growth

- 4.26 The feedback letter identified that the Firm was operating with resourcing deficiencies. The Firm has not had an approved SMF16 (Compliance Oversight Function Holder) in the role since 13 January 2020.
- 4.27 The Firm's revenue increased significantly over this period from £65,121 for the year ended 31 March 2020, to £1,279,697 for the year ended 31 March 2021. Its total revenue for the year ended 31 March 2022 was £770,000, with the reduction reflecting the cessation of a relationship with one large client. The revenue remains significantly higher than pre-31 March 2020.
- 4.28 The Firm's growth in revenue and trading volume has not been mirrored by development in its risk and compliance framework including a growth in risk and compliance resource.
- 4.29 During the February meeting, the CEO stated that the Head of Compliance was responsible for compliance, that two other individuals were responsible for reconciliations, and that there are currently eight employees. This appears to be inconsistent with the information provided by the Firm in its data survey response and its Companies House accounts for four consecutive years from the year ended 31 March 2018 to the year ended 31 March 2021, which show the Firm as having five employees.

5. CONCLUSION

- 5.1 The regulatory provisions relevant to this First Supervisory Notice are set out in the Annex.

Analysis of failings and risks

- 5.2 The Authority considers that the Firm is failing, or is likely to fail, to satisfy the Suitability Threshold Condition (paragraph 2E of Schedule 6 of the Act) on the basis that the Firm does not appear to be a fit and proper person having regard to all the circumstances including:
- a. The Firm may be in breach of Principle 3 of PRIN, requiring it to take reasonable care to organise and control its affairs responsibly and effectively and ensure that it has adequate risk management systems to effectively manage risks with its business.
 - b. The Firm may be in breach of Principle 10 of PRIN, requiring it to arrange adequate protection for clients' assets when it is responsible for them
 - c. The Firm has failed to ensure that client money is held in a properly segregated client money account in breach of the rules in CASS 7.13.3R, 7.13.6R and 7.13.12R.
 - d. The Firm has acknowledged that at present firm money and client money may be held in the same accounts, in breach of the rules in CASS 7.13.12R.

- e. The Firm has failed to obtain appropriate acknowledgment letters for client bank accounts where client money is held, in breach of the rules in CASS 7.18.2R and 17.18.6R. For example, the Firm had merged the templates in CASS 7 Annex 2 and 3 and amended the prescribed contents of the client bank account letter and client transaction account letter in a way that is not permitted by CASS.
 - f. The Firm has failed to appropriately remediate the CASS failings identified in the feedback letter of March 2022, and has failed to take steps to mitigate the risks that such a failure to remediate poses to client assets and money.
 - g. The Firm has failed to put appropriate resources and systems in place to manage the risks created by its breach of the CASS rules.
- 5.3 The Authority considers that imposition of the proposed requirements is also desirable to secure an appropriate degree of protection for consumers (section 1C of the Act) and to protect and enhance the integrity of the UK financial system (section 1D of the Act).
- 5.4 The loss to clients could be considerable in the event of the Firm's insolvency: while client funds are held in a non-CASS unprotected environment these funds would be considered part of the Firm's general estate. This would mean that if the Firm failed, client funds would not be ring-fenced from that of the firm and would not be protected. The Firm's categorisation of its clients as elective professionals rather than retail clients exposes those clients to greater risk since elective professionals are afforded a reduced level of consumer protection.
- 5.5 The Authority has concluded, in light of the matters set out above, that it is necessary to exercise its own-initiative power under section 55L(3)(a) of the Act by imposing the Requirements to stop the Firm accepting any new client money or new custody assets, stop the firm dissipating any client money that it currently holds without prior approval of the Authority and undertake certain actions to ensure compliance with CASS.
- 5.6 The Authority considers that the Requirements are a proportionate and appropriate means to address the current and immediate risks and are desirable in order to advance the Authority's operational objectives of consumer protection and protecting and enhancing the integrity of the UK financial system.

Timing and duration of the Requirements

- 5.7 It is necessary to impose the Requirements on an urgent basis given the seriousness of the risks and the need to protect client money and assets.
- 5.8 The Authority considers that it is necessary for the Requirements to continue unless and until varied or cancelled by the Authority (either on the application of the Firm or of the Authority's own volition).
- 5.9 The regulatory provisions relevant to this First Supervisory Notice are set out in the Annex.

6. PROCEDURAL MATTERS

Decision-maker

- 6.1 The decision which gave rise to the obligation to give this First Supervisory Notice was made by an Authority staff member under executive procedures according to DEPP 2.5.7G and DEPP 4.1.7G.
- 6.2 This First Supervisory Notice is given under section 55Y(4) and in accordance with section 55Y(5) of the Act.
- 6.3 The following statutory rights are important.

Representations

- 6.4 The Firm has the right to make written representations to the Authority (whether or not it refers this matter to the Tribunal). The Firm may also request to make oral representations but the Authority will only consider this in exceptional circumstances according to DEPP 2.3.1AG. The deadline for providing written representations and notifying the Authority that the Firm wishes to make oral representations is 14 days by 30 March 2023 or such later date as may be permitted by the Authority. Any notification or representations should be sent to:

Supervision, Policy and Competition Decision Making Secretariat
The Financial Conduct Authority
12 Endeavour Square
London
E20 1JN
Email: SPCDecisionMakingSecretariat@fca.org.uk and lynn.duffy@fca.org.uk

The Tribunal

- 6.5 The Firm has the right to refer the matter to which this First Supervisory Notice relates to the Tribunal. The Tax and Chancery Chamber is part of the Tribunal which, amongst other things, hears references arising from decisions of the Authority. Under paragraph 2(2) of Schedule 3 of the Tribunal Procedure (Upper Tribunal) Rules 2008, the Firm has 28 days from the date on which this First Supervisory Notice is given to it to refer the matter to the Tribunal.
- 6.6 A reference to the Tribunal can be made by way of a reference notice (Form FTC3) signed by or on behalf of the Firm and filed with a copy of this First Supervisory Notice. The Tribunal's contact details are: The Upper Tribunal, Tax and Chancery Chamber, 5th Floor, Rolls Building, Fetter Lane, London EC4A 1NL (telephone: 020 7612 9730; email: uttc@hmcts.gsi.gov.uk).
- 6.7 Further information on the Tribunal, including guidance and the relevant forms to complete, can be found on the HM Courts and Tribunal Service website: <http://www.justice.gov.uk/forms/hmcts/tax-and-chancery-upper-tribunal>

- 6.8 The Firm should note that a copy of the reference notice (Form FTC3) must also be sent to the Authority at the same time as a reference is filed with the Tribunal. A copy of the reference notice should be sent to [Supervision Manager] (insert email address) and the SPC Decision Making Secretariat (SPCDecisionMakingSecretariat@fca.org.uk).

Confidentiality and publicity

- 6.9 The Firm should note that this First Supervisory Notice may contain confidential information and should not be disclosed to a third party (except for the purpose of obtaining legal advice on its contents).
- 6.10 The Firm should note that section 391(5) of the Act requires the Authority, when the First Supervisory Notice takes effect, to publish such information about the matter to which the notice relates as it considers appropriate.

Authority contacts

- 6.11 Any questions regarding the executive procedures decision-making process should be directed to the SPC Decision Making Secretariat (SPCDecisionMakingSecretariat@fca.org.uk).

Annex

RELEVANT STATUTORY PROVISIONS

1. The Authority's operational objectives established in section 1B of the Act include securing an appropriate degree of protection for consumers, and protecting and enhancing the integrity of the UK financial system.
2. Section 55L of the Act allows the Authority to impose a new requirement on an authorised person if it appears to the Authority that the authorised person is failing, or likely to fail to satisfy the Threshold Conditions (section 55L(2)(a)), or it is desirable to exercise the power in order to advance one or more of the Authority's operational objectives (section 55L(2)(c)).
3. Section 55N of the Act allows a requirement to be imposed under section 55L of the Act so as to require the person concerned to take specified action (section 55N(1)(a)), or to refrain from taking specified action (section 55N(1)(b)).
4. Section 55P of the Act allows a requirement to be imposed under section 55L of the Act prohibiting the disposal of, or other dealing with, any of an authorised person's assets (whether in the UK or elsewhere), or restricting such disposals or dealings.
5. Section 55Y(3) of the Act allows a requirement to take effect immediately (or on a specified date) if the Authority, having regard to the ground on which it is exercising its own-initiative power, reasonably considers that it is necessary for the requirement to take effect immediately (or on that date).
6. Section 391 of the Act provides that:

"[...]

- (5) When a supervisory notice takes effect, the Authority must publish such information about the matter to which the notice relates as it considers appropriate.
- (6) But the Authority may not publish information under this section if in its opinion, publication of the information would, be unfair to the person with respect to whom the action was taken or proposed to be taken [or] prejudicial to the interests of consumers or detrimental to the stability of the UK financial system.
- (7) Information is to be published under this section in such manner as the Authority considers appropriate."

RELEVANT REGULATORY PROVISIONS

The Enforcement Guide

7. The Authority's approach in relation to its enforcement powers is set out in Chapter 8 of the Enforcement Guide (EG), certain provisions of which are summarised below.
8. EG 8.1.1 reflects the provisions of section 55L of the Act by stating that the Authority may use its own-initiative power to impose requirements on an authorised person where, amongst other factors, the person is failing or is likely to fail to satisfy the threshold conditions for which the Authority is responsible (EG 8.1.1(1)), or it is desirable to exercise the power in order to advance one or more of its operational objectives (EG 8.1.1(3)).
9. EG 8.2.1 states that when the Authority considers how it should deal with a concern about a firm, it will have regard to its statutory objectives and the range of regulatory tools that are available to it. It will also have regard to the principle that a restriction imposed on a firm should be proportionate to the objectives the Authority is seeking to achieve (EG 8.2.1(2)).
10. EG 8.2.3 states that in the course of its supervision and monitoring of a firm or as part of an enforcement action, the Authority may make it clear that it expects the firm to take certain steps to meet regulatory requirements. In the vast majority of cases the Authority will seek to agree with a firm those steps the firm must take to address the Authority's concerns. However, where the Authority considers it appropriate to do so, it will exercise its formal powers under section 55L of the Act to impose a requirement to ensure such requirements are met. This may include where, amongst other factors, the Authority has serious concerns about a firm, or about the way its business is being or has been conducted (EG 8.2.3(1)), or is concerned that the consequences of a firm not taking the desired steps may be serious (EG 8.2.3(2)).
11. EG 8.3.1 states that the Authority may impose a requirement so that it takes effect immediately or on a specified date if it reasonably considers it necessary for the requirement to take effect immediately (or on the date specified), having regard to the ground on which it is exercising its own-initiative powers.
12. EG 8.3.2 states that the Authority will consider exercising its own-initiative power as a matter of urgency where: 1) the information available to it indicates serious concerns

about the firm or its business that need to be addressed immediately; and 2) circumstances indicate that it is appropriate to use statutory powers immediately to require and/or prohibit certain actions by the firm in order to ensure the firm addresses these concerns.

13. EG 8.3.3 states that it is not possible to provide an exhaustive list of the situations that will give rise to such serious concerns, but they are likely to include one or more of four listed characteristics, these include: 1) information indicating significant loss, risk of loss or other adverse effects for consumers, where action is necessary to protect their interests; 2) information indicating that a firm's conduct has put it at risk of being used for the purposes of financial crime, or of being otherwise involved in crime; 3) evidence that the firm has submitted to the Authority inaccurate or misleading information so that the Authority becomes seriously concerned about the firm's ability to meet its regulatory obligations; 4) circumstances suggesting a serious problem within a firm or with a firm's controllers that calls into question the firm's ability to continue to meet the threshold conditions.
14. EG 8.3.4 states that the Authority will consider the full circumstances of each case when it decides whether an imposition of a requirement is appropriate and sets out a non-exhaustive list of factors the Authority may consider, these include:
15. The extent of any loss, or risk of loss, or other adverse effect on consumers (EG 8.3.4(1));
16. Under EG 8.3.4, factors that may be considered by the Authority include:
 - (1) The extent of any loss, or risk of loss, or other adverse effect on consumers*
 - (2) The extent to which customer assets appear to be at risk*
 - (4) The seriousness of any suspected breach of the requirements of the legislation or the rules and the steps that need to be taken to correct that breach*
 - (7) The risk that the firm's conduct or business presents to the financial system and confidence in the financial system*
17. EG 8.3.4(9) includes the impact that use of the Authority's own-initiative powers will have on the firm's business and on its customers. The Authority will need to be satisfied that the impact of any use of the own-initiative power is likely to be proportionate to the concerns being addressed, in the context of the overall aim of achieving its statutory objectives.

PRIN

18. The purpose of the Principles for Businesses is set out at PRIN 1.1.2. PRIN is a general statement of the fundamental obligations of firms and the other persons to whom they apply under the regulatory system.
19. Principle 3 of PRIN requires a firm to take reasonable care to organise and control its affairs responsibly and effectively and ensure that it has adequate risk management systems to effectively manage risks with its business.

20. Principle 10 of PRIN, requires a firm to arrange adequate protection for clients' assets when it is responsible for them.

CASS

21. CASS 7 – client money rules; in particular:
22. CASS 7.13 - the segregation of client moneys for protection;
23. CASS 7.15 - the requirements on a firm to record, accounts for and provide reconciliations in order to ensure adequate protection of clients moneys;
24. CASS 7.18 - the requirement to have acknowledgment letters to ensure parties are on notice that moneys held are client moneys.